Neutral Citation Number: [2023] EWHC 588 (Ch)

Case No: BL-2020-0016121

IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
COMPANIES COURT

Royal Courts of Justice, Rolls Building
Fetter Lane, London, EC4A 1NL

Date: 16 March 2023

Before :

MR SIMON GLEESON
Sitting as a Deputy High Court Judge

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Between :

(1) Decision Inc Holdings Proprietary Limited **(2) Decision Inc Shareco (RF) Proprietary Limited**	**Claimants**
- and -	
(1) Stephen Garbett **(2) Anis El Mariesh**	**Defendants**

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- -

Mark Warwick K.C. (instructed by **Ince Gordon Dadds**) for the **Claimants**
David Lowe (instructed by **Wallace LLP**) for the **Defendants**

Hearing dates: 17-20, 23-25 and 27 January 2022

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Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

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MR SIMON GLEESON
Sitting as a Deputy High Court Judge

Mr Simon Gleeson :

1. This case involves the cramming of a factually square peg into a legally round hole. The issue between the parties is relatively straightforward – the Defendants sold a company to the Claimants, the company performed very substantially worse than expected in the months after the acquisition, and the Claimants feel that they were misled. Ordinarily this would give rise to a straightforward case in misrepresentation, in which the court would examine who had actually said what to whom when and consider whether the statements made were sufficiently incorrect to merit an award of damages.

2. However that is not the approach to be adopted in this case. The reason for this is that the parties entered into an agreement in respect of the sale (conventionally tautologously described as a "sale and purchase agreement", or SPA) in relatively usual form for a transaction of this kind. One of the aims of an SPA in a corporate transaction is to severely limit the scope for subsequent litigation between the parties to the transaction. This is achieved by a variety of techniques – limiting the period in which litigation can be commenced, requiring formal notification of any such litigation in prescribed form, and, most importantly, limiting the types of actions which can be brought. As a result of this, the action which the Claimants have brought is based on allegations of breach of specific contractual warranties.

3. These contractual warranties are two – one being the warranty that there had been no material adverse change in the turnover or prospects of the company at the time the contract became effective, the other being that the records of the company were accurate.

4. The fact that the Claimants are obliged to proceed in this way has consequences for the conduct of this action, and for the issues considered in this judgement. During the hearing it proved hard at times for all those involve to avoid lapsing into what I might call a "misrepresentation mindset", in which the debate turned on who said what when, and whether what was said was justifiable in the circumstances. However, that issue was not before me. The issue that is before me is simply as to whether either or both of the alleged warranties had been breached, and in neither case was the truth or otherwise of what was said during the negotiations for the sale of the company in issue. It was necessary to consider the content of some of the negotiations in the course of deciding whether or not there had been a breach of warranty, but the only relevance of that consideration was evidential.

5. The Claimants' pleadings state that the First Claimant has assigned the benefit of its claims in this litigation to the Second Claimant, who therefore also appears as a party. However, at all material times the entity engaged in the transaction was the First Claimant. Clause 16 of the Agreement explicitly permits such an assignment. and its validity was not challenged during the hearing. Consequently I proceed on the basis that the claim has been validly assigned to the Second Claimant.

Background

6. On the 8th October 2018 the First Claimant ("Decision"), and the First and Second Defendants, executed an SPA (the "Agreement") under which Decision agreed to acquire from the Defendants all the shares in Copperman Consulting Limited ("the Company"). The Agreement took effect on the 12th October (the "Effective Date").

7. Decision is established in South Africa, the Company in the UK. Both are I.T. consultancies specialising in the design of enterprise performance management ("EPM") software. EPM software helps the finance departments of very large businesses manage and control financial flows across the business, and facilitates planning, modelling, consolidation and reporting of data across multiple systems within an organisation. In general a business will come to an EPM specialist when they want a new system designed and built for them. This means that the revenues of that specialist arise in what I would describe as "large lumps" – at any given time, such a business will have a relatively small number of relatively large projects ongoing, and there is relatively little "flow" work. In summary, the continual winning of a few large mandates is essential to the business.

8. The conventional industry approach to assessing the future of a business of this kind is to compile what is known as a "pipeline" – a list of new business prospects which may, over time, mature into mandates. A pipeline document can include everything from a remote prospect to a concluded agreement – it simply lists all of the identified possibilities. It is conventional to analyse pipelines by allocating percentage probabilities to each possibility, and thereby arriving at a probable future revenue calculation. However, on the basis of the evidence before me here I do not think that it could be said that a pipeline document which was not prepared in this way could be described as inaccurate or defective on that ground alone.

9. I should also mention at this point that the nature of the EPM consultancy business is such that its operational gearing is very high. The design and implementation of EPM systems is difficult and complex work, and in order to be successful a firm needs a strong bench of full-time employed specialist consultants. The vast majority of such a firm's costs are therefore fixed. This means that when the firm is fully employed the profits may be very high, but a relatively small downturn in turnover may have a significant negative impact on profits.

10. Because of this, it is common ground between the parties that in assessing the value of the Company, the focus of both sides in the sale negotiations was on the Company's ability to consistently generate future revenues. It is common ground that the Claimants were not buying a particular set of existing or future contracts. What they wanted to buy was twofold – the ability to execute mandates of this kind, and the ability to generate such mandates. It should be emphasised that Decision, at the time of the contract, had no business in Europe, and the business of the Company was more or less exclusively in the UK and Ireland. Decision therefore had no ability to generate business for the Company, or to refer business to it – the future profitability of the Company was entirely dependent on the Company's own ability to generate new business.

11. The discussions between Decision and the Defendants in the course of negotiating the deal therefore turned significantly on the future business that the Company might be expected to win. In order to provide comfort to Decision as to the future potential the Company, information was provided at various points as to the future "Pipeline" of work. This was a list of potential assignments which the Defendants believed that the Company might win. The most significant elements of this pipeline in terms of their size were potential mandates for four clients; The BBC, TfL, Kerry and Nidec (the "Four Contracts").

The Terms of the Sale and Purchase Agreement

12. The relevant provisions of the Agreement are set out below:-

> 10 WARRANTIES
>
> 10.1 The Sellers acknowledge that the Buyer is entering into this Agreement on the basis of, and in reliance on, the Warranties.
>
> 10.2 The Sellers warrant to the Buyer that except as Disclosed, each Warranty is true, accurate and not misleading on the date of this Agreement and the First Completion Date if this date is later than the date of this Agreement.
>
> 10.3 Except where otherwise specifically provided for in this agreement and without prejudice to the Buyer's right to claim on any other basis, or to take advantage of any other remedies available to it, if any Warranty is breached or proves to be untrue, inaccurate or misleading, the Sellers shall pay to the Buyer on demand:
>
> 10.3.1 the amount necessary to put the Company into the position they would have been in if the Warranty had not been breached or had not been untrue, inaccurate or misleading;
>
> 10.3.2 all costs and expenses (including, without limitation, damages, legal and other professional fees and costs, penalties, expenses and consequential losses whether arising directly or indirectly) reasonably incurred by the Buyer, the Company as a result of such breach, or of the Warranty being untrue, inaccurate or misleading; and
>
> ....
>
> 10.5 Each of the Warranties is separate and, unless otherwise specifically provided, is not limited by reference to any other Warranty or any other provision in this Agreement.
>
> 10.6 Except for the matters Disclosed, no information of which the Buyer (or any of its agents or its advisers) has knowledge (in each case whether actual, constructive or imputed), or which could have been discovered (whether by

investigation made by the Buyer or on its behalf), shall prejudice or prevent any Claim or reduce the amount recoverable under any Claim.

10.7 The Buyer warrants that it has no actual knowledge at the date of this Agreement of any fact, matter or circumstances constituting a breach of Warranty save as Disclosed.

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11. LIMITATIONS ON CLAIMS

11.1 Save as provided in clause 11.19, this clause 11 limits the liability of the Sellers in relation to any Claim.

11.2 The aggregate liability of the Sellers for all Claims shall not exceed an amount equal to the aggregate Purchase Price (being the amounts payable to the Sellers for the First Tranche Shares and the Second Tranche Shares calculated in accordance with clauses 4 and 6) actually received by the Sellers (and which has not otherwise been the subject of any recovery by the Buyer from the Retention Amount). Should the aggregate Purchase Price not have yet been finally determined as at the date of any Claim, the aggregate liability of the Sellers will be finally determined once the aggregate Purchase Price has been finally determined and paid to the Sellers subject to any rights of set off set out in this Agreement.

11.3 The Sellers shall not be liable for a Claim unless:

11.3.1 the Sellers' liability in respect of such Claim (together with any connected Claims) exceeds £10,000; and

11.3.2 the amount of the Sellers' liability in respect of such Claim, either individually or when aggregated with the Sellers' liability for all other Claims (other than those excluded under clause 11.3.1 and all claims under the Tax Covenant), exceeds £100,000, in which case the Sellers shall be liable for the whole amount claimed (and not just the amount above the threshold specified in this clause 11.3.2.)

For the purposes of this clause 11.3, a Claim is connected with another Claim if the Claims arise from the same facts, events or circumstances.

11.4 The Sellers shall not be liable for a Claim unless notice in writing summarising the nature of the Claim (in so far as it is known to the Buyer) and, as far as is reasonably practicable, the amount claimed, has been given by or on behalf of the Buyer to the Sellers:

11.4.1 in the case of a Claim for breach of the Tax Warranties, on or before the seventh anniversary of First Completion; or

11.4.2 in any other case, on or before the expiry of the period of 24 months commencing on the First Completion Date.

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SCHEDULE 4 - Warranties

....

19 CHANGES SINCE THE ACCOUNTS DATE

Since the Accounts Date:

19.1.1 the Company has conducted the Business in the normal course and as a going concern;

19.1.2 there has been no material adverse change in the turnover, financial position or prospects of the Company;

....

20 FINANCIAL AND OTHER RECORDS

20.1 All financial and other records of the Company (“Records”):

20.1.1 have been properly prepared and maintained;

20.1.2 constitute an accurate record of all matters required by law to appear in them, and in the case of the accounting records, comply with the requirements of section 386 and section 388 of the CA 2006;

20.1.3 do not contain any material inaccuracies or discrepancies; and

20.1.4 are in the possession of the Company.”

The Claim

13. The Claimants say that the Defendants were in breach of Warranty 19.1.2 (“Since the Accounts Date .... there has been no material adverse change in the turnover, financial position or prospects of the Company”) and of Warranty 20 (“All financial and other

records of the company ("Records") .... do not contain any material inaccuracies or discrepancies"). The Defendants, in reply, say not only that this is not the case, but also that the facts on which the Claimants seek to rely were in fact known at the time of entry into the SPA, and as a result the Claimants are either prevented from suing by Warranty 10.7, or the Defendants have a countervailing claim in damages for breach of that warranty which should be set off against any award. The Defendants further say that the Claimants have already lost their cause of action at the end of the notice period, because the notice given, although within the time, was invalid.

The Facts

14. At the time when negotiations between Decision and the Defendants commenced, Decision had recently acquired an EPM consultancy business in Australia. That acquisition had gone well, and it was looking for a similar acquisition in the UK.

15. Decision's founder and CEO is Nicholas Bell, who owns 40% of the issued share capital. The other major shareholder is South African Enterprise Development (Pty) Limited ("SAED"), a private equity fund which owns 48% of the issued share capital. Its representatives on the board of Decision are David Pimstein and Louis Geeringh. Mr Pimstein is the CEO of SAED.

16. The Company was founded by Mr El-Mariesh in 2007, and Mr Garbett joined as a director in 2009. By the time of the transaction it had approximately 40 staff. Management appears to have been almost entirely informal, with relatively little formal reporting or record-keeping. Commercially the Company had been relatively successful, and by 2017 it was (in Mr Bell's words) "the UK's leading SAP BPC (systems, applications and products business planning and consolidation) focused consultancy and it also had an impressive list of clients".

17. The Defendants were concerned that market developments meant that the Company's small size counted against it when pitching for new work, and believed that in order to develop its business it needed to become part of a larger group. Consequently, in October 2017 the Defendants approached a corporate finance firm, Equiteq, with a view to selling the Company. Equiteq's representative as regards the transaction was Gabriela Silvestris ("Ms Silvestris"). Ms Silvestris was aware of Mr Bell's interest in acquiring a UK firm active in this area, and sent him an e-mail on 18th October 2017 proposing the transaction. She provided a one page overview of the Company's business.

18. Mr Bell was interested in knowing more about the proposal, and on 20th October Decision signed a non-disclosure agreement. Ms Silvestris then provided an information memorandum on the Company. This information memorandum contained positive statements about the pipeline of new work that the Company had in place.

19. On about 14th November 2017 Mr Bell came to London, where he met the Defendants and Ms Silvestris. He sought more information about the Company, including information as to existing sales, and as to the sales pipeline. A conditional "Term Sheet" was signed on 22 December 2017.

20. On 25th January 2018 Mr El-Mariesh sent to Mr Bell by email a sales pipeline for January 2018 and a sales breakdown. The sales pipeline showed a grand total of

£13,360,000 of possible work. Two of the biggest new projects in the pipeline were BBC and Kerry Group – two of the Four Contracts.

21. As the negotiations proceeded, discussion within Decision revolved largely around the price to be paid for the acquisition. The Defendants had produced a very ambitious set of financial forecasts, indicating that the Company's gross profit for 2018 would be 60% up on the 2017 figure. Mr Bell and the other directors of Decision were sceptical about the deliverability of this projection. However, the question of what the likely profits of the Company would be was critical for Decision in deciding what price they would be prepared to offer for it. The key piece of evidence for them as regards this likelihood was therefore the state of the pipeline of new business of the Company. Decision made a series of requests during the negotiation period for updates on the state of the pipeline, and these updates were provided. It was clear to the Defendants that the better the pipeline looked, the more Decision was likely to be prepared to pay for the Company.

22. I note in this regard that Mr Lowe, for the Defendants, submitted that profitability was not the sole determinant of the price to be paid by, or the attractiveness of the deal for, Decision. Decision was acquiring a significant "footprint" in a new market, along with the skills of an established base of consultants and a set of client relationships, and all of these had a value to them. This is clearly true. However, the attractiveness of all of these attributes of the Company depended upon their being at least self-financing, and that required a minimum level of profitability. Mr Garbett said in evidence that there was considerable value in the Company in the form of its "installed base", in the form of its assembled team of BPC experts and senior consultants. However, Mr Pimstein and Mr Bell were adamant that this had very little value to them unless accompanied by a sufficient flow of new business. Hence, expected future profitability seems to have occupied the majority of the attention of both sides during the negotiation.

23. One result of this is that as negotiations progressed, the enquiries by Decision as to the pipeline, and its presentation by the Defendants, became more granular and more sophisticated. However, it was understood on both sides that the pipeline was no more than a series of best guesses as to the future.

24. Mr Garbett's evidence was that the Company did not have any sort of formal pipeline monitoring system in place for the majority of its life. Mr Garbett explained in evidence that this was because he and Mr El-Mariesh spoke regularly to all of the senior consultants involved in the business, and therefore had this information in their heads. It therefore seems that it was only at the suggestion of Equiteq that they built a spreadsheet for the purposes of monitoring and reporting the Company's pipeline.

25. The first pipeline document created by the Defendants (the January Pipeline) contained no information as to the likelihood of a mandate being won. The Defendants subsequently created a risk-sensitive pipeline document for the purpose of informing and reassuring Decision as to their future. The risk sensitivity element was provided by the use of a RAG (Red/Amber/Green) colour-coding system, referred to in this hearing as the "traffic-light" system. It seems that the Defendants regarded this as at least in part a marketing document – Mr El-Mariesh produced a draft which he sent to Mr Garbett for comment, and Mr Garbett, according to his cover e-mail, "tweaked" it so it now has more colour, is a little simpler and has positive sales wording (WIN) included". This document (the "March Pipeline") was sent to Mr Bell on 29th March 2018 by Ms

Silvestris, with a cover e-mail describing it as "pretty strong". It totalled £15,210,000. RAG coding was used in the March Pipeline to classify the items it listed according to the likelihood of their turning into paid work

26. The sales director of the Company, a Mr Chris Smith, maintained a Customer Relationship Management system ("CRM") which was intended to capture information as to business opportunities, and applied percentage weightings to estimate possible success. Mr Smith sent a copy of the output of this system to Mr El-Mariesh on the 27th May. It showed a total pipeline of £11,351,000, with a weighted value of £1,542,300. This was intended to form the basis of an update of the pipeline document. However, the final document as sent to Decision (the "May Pipeline") was a heavily edited version of this document created by Mr Garbett and Mr El-Mariesh. The edits involved increasing the value of some items, removing the percentages, and applying the "traffic light" format. The total was now £15,128,000.

27. The question of the significance of the traffic light system was a matter of some dispute before me. The Defendants say that it was intended as no more than an indication of low, medium or high risk, so that even items coloured green were not thought to be certain. Both Mr Bell and Mr Pimstein say that what was said to them was that items coloured green were certain subject to process and/or timing constraints – thus, although there might be uncertainty as to when revenue would be received in respect of a project, there should be no doubt that the Company was (or would be) retained for the project.

28. The May Pipeline was produced at the same time as, and was intended to accompany, a detailed profit forecast produced by the Company (the "May Forecast"), which showed forecast EBITDA for the full year of £1,628,393. This forecast assumed that the Four Contracts would begin generating revenue in the current year, in June, September, June and June respectively.

29. Some emphasis was placed in argument upon the email that Mr El-Mariesh sent internally in the course of the preparation of the May Pipeline to the effect that "Have put TfL as "won" as I think we need to go out on a limb on this ....". I think that all that was intended by this communication was that the Defendants needed to take a view on the likelihood of this mandate being won, and decided that it should be treated as virtually certain. I think that this confirms that in the minds of the Defendants the fact that a contract was regarded as "won" meant something very much less than that the client had formally legally committed to the mandate.

30. Drafts of May Pipeline and the May Forecast were sent to Mr Bell. Having reviewed them, he sent an e-mail that included the comment "With regards to the Revenue and the Conversion what is the impact if the projects are delayed by 2 month – where does that leave the business. There is great reliance on Nidec, TFL and Kerry starting to bill in June. If that is deferred or delayed what does that mean. What proof is there that those 3 will commence billing in June[?]"

31. Mr Bell came to London to meet the Defendants on 11th June 2018. The pipeline document was discussed, including the Four Contracts. His evidence is that he was told that (a) Kerry was almost certain, (b) Nidec was secure and was starting soon, (c) TFL was also "won" and billing would commence shortly, and (d) the BBC was yellow, to signify a delay, but the Company was almost certain to secure the BBC business.

32. After the meeting of 11th June, Decision entered into a share purchase agreement ("The First SPA") with the Defendants. This document was subject to significant conditions precedent, and seems to have been regarded by both parties as a declaration of intent whose major function was to set out a pricing framework.

33. This pricing framework in the First SPA is significant. The basic proposal was that Decision would buy 100% of the shares of the Company. An initial payment was to be made of £8m. If EBITDA was £2m for both years, there was to be a second payment of £1.75m, along with the issue to the sellers of a stake in Decision worth £3.25m. The purchase price declined with EBITDA. It was floored at a cumulative EBITDA for the two years of a little over £3m (say £1.5m p.a.) in which case the sellers would receive the aggregate cash amount of £9.75m and nothing further.

34. On 11th July 2018 Ms Silvestris provided Mr Bell with the Company's draft June 2018 management accounts. At this point Mr Bell was becoming increasingly dubious as to how likely it was that the Company would hit even the £1.5m p.a. EBITDA target. He therefore sought more information as to the state of the projects in the pipeline.

35. There is a series of emails in the last week in July 2018 that shows the steps that the Defendants took to produce information to be provided to Decision, and what information was actually provided to them.

36. On 23rd July Mr Bell sent an email to the Defendants as follows:

> "We are preparing for the Shareholder meeting this week and we need to provide an update on this forecast document that we went through on my last visit.
>
> Please can you update it to show the performance for June as well as at the project level given where the work plans are. Please also provide an updated pipeline should this be different.
>
> Many of the conversations have been about the radical difference between the first 6 month and the second 6 months. I have taken them through the pipeline and the importance of the Nidec, TFL, BAE Applied Intelligence, BBC and Kerry projects that are starting thereby meaning that the forecast is effectively closed out and anything above would be further upside.
>
> With Nidec, BAE App Int, Kerry and TFL having commenced and the June start being critical I was confused to see that those client names haven't come up on the debtors report from June (BAE Applied was very small). This was picked up and in order to assure the board that the work plans are well on track and valid we require some supplementary proof.
>
> Please can you send through the signed proposals and proposals and project plans for these 3 projects along with any other documents that build the case to show we are well under way."

37. On the same day Mr El-Mariesh responded saying *"*Will get back to you asap."

38. On 24th July Mr Bell emailed the Defendants saying:

> "We need to get the documentation out before the meeting so if we can get it today please. Are all of those projects that are referred to on track with a revenue plan? Were they all started in June with the teams growing in July".

39. Mr Garbett responded a little later that day:

> "Anis [Mr El-Mariesh] is now camping with limited connectivity so I will be responding to you. Yes we are getting all the SOWs, proposals and extra information together for you and it will be with you later today.
>
> Yes as previously discussed these projects have started and are progressing".

40. This last sentence was untrue to Mr Garbett's knowledge, since on the previous day, the 23rd July, he had been informed that the BBC had rejected the tender for the work concerned, and was proceeding with two other possible suppliers.

41. Shortly afterwards, Mr Garbett sent a longer e-mail to Mr Bell with a large number of attachments and a series of observations about the Four Contracts. The observations were as follows

> "BBC (via HCL) £2m to £3m
>
> A large project proposal in conjunction with HCL is currently under assessment by the BBC. The ROM is attached.
>
> Nidec — Led by Rick Newbould £900k to £1.1m
>
> Starting off with a scoping project, to ensure the various senior stakeholders (mainly US & Japan) are comfortable with our proposal.
>
> TfL (Transport for London) — led by Phil Jong with additional Principal Support on each of the workstreams £1.5m to £2.2m
>
> We have engaged working with TfL. This will likely be one of the larger clients in our portfolio. The project scope is still to be defined in detail, and it is larger than we initially thought. It is clear that TfL need our support and insight to enable them to generate and develop a roadmap, and to then fulfil that longer term plan. Contractual/Procurement hurdles do exist in an organisation of this size and nature, with their desire to exclusively contract with Copperman at odds with their defined OJEU process. TfL have engaged SAP's help to act as an intermediary that we can invoice/bill through as an interim measure. Copperman have tendered for and succeeded in listing as an official government G-CLOUD supplier which not only provides the mechanism TfL needs to contract with Copperman, but has opened the door to further government contracts.

> Kerry — Led by Anis/Rick Newbould £1.5m to £2.5m
>
> A large consolidation proposal is currently under assessment by Kerry. The ROM is attached. Due to the size and magnitude of the project, Kerry feel that they need to ensure they are fully resourced internally with enough backfill and spare capacity before fully engaging on the project. We continue to be very positive and patient with this large Irish client."

42. Later that day Mr Garbett sent an e-mail to Mr Bell saying "Yes we are happy with the plan we worked on with you and I have attached the updated pipeline plan". The attached document (the "July Pipeline") listed TFL and Nidec in green and BBC and Kerry in amber. The BBC was specifically described as "ongoing". The total value given for the BBC was £3 million. This sum was included in the grand total on the Pipeline of £21,554,000.

43. On 25th July Mr Bell met with the shareholders of Decision. He was asking them to commit substantial capital to the transaction, and it appears that there was significant pushback from them. As a result, he sent an e-mail the following day to the Defendants reporting on the meeting. He explained that the shareholders were not prepared to commit to the purchase, as yet, although they were fully supportive. Mr Bell said:

> "Despite the positive signs there remains a high degree of scepticism with the first half performance to June, and whilst June was really positive, it is only one month and the previous five have been very poor by comparison."

44. Mr Bell therefore proposed a meeting to discuss a new structure for the purchase of the Company. This meeting was held in London on 1st and 2nd August 2018. Mr Garbett was not present at this meeting, explaining his absence as due to illness, so only Mr El-Mariesh attended the meeting.

45. At the August meeting there was a detailed discussion about TFL, Nidec, Kerry and BBC. Mr Bell and Mr Pimstein say that they were told that TFL and Nidec were projects that had been won, Kerry was delayed, but would be won soon, and that BBC was also delayed but was progressing. This is why Kerry and BBC had both been coloured amber on the pipeline document.

46. It is clear that Mr Bell remained in some doubt as to the true financial position of the Company. On 28th August he sent an email to Ms Silvestris and the Defendants saying "What is enormously frustrating is your refusal to provide me despite three emails with the July accounts for the business. I do not understand why this is the case and what the issue is?". Ms Silvestris apologised for the delay.

47. The explanation proffered to Mr Bell - that the Company's accountants were on holiday - seems to have appeased him only somewhat. He therefore asked for – and was provided with – a list of the July invoices.

48. His motivation here is reasonably clear. A business like that of the Company invoices on a monthly basis. The monthly list of invoices will not correspond exactly to the monthly revenue, as there will be accruals and prepayments to take into account.

However, for a business operating in a relatively steady state, the monthly invoice schedule should provide an indication as to the overall level of business in any particular month. The July invoice schedule was sent by Ms Silvestris to Mr Bell.

49. It is notable that the Defendants were clearly aware by this time of the fact that Mr Bell scrutinised these sorts of document closely, and was likely to remark on the fact that there were no invoices for projects which he had been informed had commenced. The e-mail therefore also contained the observation “Please note that there are some other invoices for TFL and Nidec which are not included in this list”.

50. No more information about the Company was supplied for some time.

51. On 5th October 2018 Mr Bell was sent the Company’s June and July management accounts. He responded *“Are you able to provide a view of the August performance please”.* He went on to say “needing September as well”. These documents were not received. Nonetheless on 8th October 2018 the Agreement was signed.

52. On the same day that the Agreement was entered into there were exchanges between Mr Bell and the Defendant’s solicitor at Wallace (John Woodhouse). Mr Bell was seeking information as to the performance of the Company in August. Mr Woodhouse responded by saying that the Company's external accountants (Barrow) had been asked “to send over some financial information for August”, and shortly afterwards that day sent a further e-mail to the effect that “I am forwarding on financial information for August which arrived this afternoon from Barrow”. The document supplied was headed *“August 2018 relevant invoices/revenue”,* and is referred to as “the August Invoice Schedule”.

53. Mr Bell continued to press for sight of the August accounts; hence on 10th October Mr Bell asked Mr Woodhouse “When Barrow will be able to have the final accounts for August closed out?” and Mr Woodhouse responded at the end of the day “No definite ETA on the August accounts. Barrow has been instructed to prepare them, but I have no update I’m afraid”.

54. The 12th October 2018 (the Effective Date) was the First Completion Date under the Agreement. This is the day when payments were made, and shares transferred. The Defendants were paid £5 million, a further £1.75 million was placed in escrow, and 70% of the shares in the Company were transferred to Decision.

55. Strictly speaking this is the end of the factual matrix within which the decision before me is to be made. The questions of breach of warranty arise at the date at which the Contract became effective, and it would be wrong to apply hindsight to that determination by looking at subsequent facts. However, it may be helpful to record subsequent events, since they help to understand and interpret the evidence of the parties.

56. Once the transaction had completed, Mr Bell paid another visit to the Company’s offices. He sent an email in advance informing the Defendants that he wanted to focus on the pipeline. Mr Garbett therefore produced a revised draft pipeline for this meeting, and sent it to Mr Smith. Mr Smith responded on 24th October as follows:

> "Let's talk at 09.30, but I'm really struggling with this. It does not present the reality of the situation and I'll take a couple of examples;
>
> TFL is not worth £1.5M as I stated in my latest forecast the real figure is £850K
>
> Nidec is definitely not going to close in November for the big project. We'll pick up a number of smaller pieces of work during the next few months, but the big prize won't happen until the new year
>
> Kerry is not going to happen in October, I'm not meeting with them until w/c 5th November to understand where they are and their timetable. I had it down to close in April.
>
> I would have thought now that we are past the sales of Copperman, we need to present a realistic picture of where we are.
>
> If we don't I'll be asked some very difficult questions at the end of November why these deals didn't close. Shouldn't we face the difficult questions now rather than putting them off?"

57. Mr Garbett dismissed Mr Smith's concerns, and presented a Pipeline document which, as regards three of the Four Contracts, was the same as the May Pipeline. The BBC was however deleted. The October Pipeline, unlike the earlier Pipelines, did not include "BAU" business. The unweighted total of £13,130,000 for this Pipeline therefore compares with a like-for-like figure of £13,744,000 in the July Pipeline.

58. It was only on the 31 October that Mr Bell was provided with the monthly accounts for the Company for August and September. They showed a net loss after tax for August of £40,746 and an equivalent figure for September of £2,382. Mr Bell was clearly astonished by these figures – he responded almost immediately "I think there is a mistake as this cannot possibly be right that the revenue is a quarter of the budget. Please recheck and get back to me ASAP. If this is the case it would be quite disastrous". Again, the significance of this is that it makes clear that Mr Bell was not expecting anything like the figures which he in fact received.

59. A completion statement showing the position of the Company at the completion date was required under the SPA. This was produced and signed both by Decision and the Defendants. It showed a balance sheet of £571,949, and a cumulative profit for the year of £315,073 (note that this is not an EBITDA figure).

60. Revenues continued to be low, with the Company making a loss of £16,197 EBITDA in October and a profit of £1,078 EBITDA in November. However, these figures paled into insignificance in the face of the December figures, which showed an EBITDA loss of £97,387. The position did not noticeably improve in 2019, when the January EBITDA loss was £95,708.

61. As a result of this on the 28th February 2019 the Claimants made a proposal to the Defendants to restrike the deal between them. This proposal started from the position that on the basis of the agreed multiple of 6.43 and the actual EBITDA of the Company for calendar 2018 of £314,000, the value of the Company was just over £2m. What the Claimants proposed was that the Defendants should return £2m of the £5m purchase price that they had received, and that the arrangement be rejigged so that if the Company could achieve its forecast EBITDA level by 2020, it would effectively be paid back. The Defendants rejected this offer.

62. On 6th March 2019 the Claimants sent a formal letter to the Defendants, alleging breach of warranties within the Agreement, including 19.1.2 and 20.1.3.

63. On 27th March 2019 the First Claimant assigned the benefit of rights, claims etc to the Second Claimant, and notice of that assignment was given to the Defendants on about 3rd April 2019.

64. On 31st January 2020 the 2019 figures for the Company were agreed between Decision and the Defendants. They showed a loss of £615,620.

65. On 4th September 2020, the Claimants gave formal notice of a claim pursuant to clause 11.4 of the Agreement.

The Evidence

66. The witnesses before me were Mr Bell and Mr Pimstein for the Claimants, and both of the Defendants. Each side put forward an expert – Mr Dearman for the Claimants, and Mr Thompson for the Defendants. The experts produced a joint report which I found of great assistance.

Mr Bell

67. Mr Bell was a very focussed man of business. He did not seem overly emotional about what had happened, and gave the impression that his focus at all times had been to work out what the true position was and how to make the best of it. He was adamant that he would never have entered in to the transaction to buy the Company if he had known what was going to happen – and in particular if he had known that he would subsequently be called upon to recapitalise it – but he did not appear to be motivated by any sort of rancour. My impression was that he believed that the acquisition of the Company was a mistake which he regretted, but that he was resigned to the fact that all business careers involve some mistakes, and this one was his.

68. Mr Lowe sought to construct a theory that Mr Bell's evidence was deliberately falsified in order to exculpate him from criticism of his part in the transaction, and that this was demonstrated by the existence of dissension between the shareholders of Decision as regards the transaction. This was an odd suggestion, given that Mr Bell is not only the founder, CEO and 40% shareholder of Decision, but also very clearly its guiding mind. It is impossible to see where Mr Lowe's proposed censure might come from, or why Mr Bell should be so concerned about it that he would be prepared to lie in evidence.

69. It was clear from the evidence that the transaction was a substantial step for Decision, and as with any such transaction there was considerable shareholder discussion. It is

also the case that Mr Bell was not able to recall perfectly in the witness box every aspect of the corporate equity-raising which was necessary to effect the transaction. Again Mr Lowe asked me to conclude from this that he was deliberately hiding something from the court. I can see no basis for doing any such thing.

70. The majority of Mr Bell's cross-examination – unsurprisingly - related to what he knew of the prospects of the Four Contracts. His evidence was that the projects (at least whilst they were colour-coded green on the pipeline documents) "had been won, or had started and that there was a binding commitment in respect of them". Mr Lowe repeatedly put to him the point that he had never been told that formal legal documentation had been signed in respect of these projects, or formal PO numbers confirmed by the clients. His evidence – which I accept – is that (a) he had been assured by the Defendants that that was not how business worked in the UK, and (b) that his primary focus was not on the specific projects, but on the EBITDA figure. He was not at any point concerned with the specific legal status of any project – his questions to the Defendants about the contracts were simply seeking confirmation that the expected levels of EBITDA for the current financial year remained achievable. To that extent, what he was looking for was not formal commitments, but evidence to support the judgement of the Defendants as to which contracts would start when – i.e. that they had been "won" or were "ongoing". Mr Lowe suggests that the fact that Mr Bell was not able to define with precision what exactly he believed the terms "won" or "ongoing" to mean in this context indicates that he must be exaggerating the extent to which he had been told that these contracts had that status. I do not agree.

71. Mr Lowe placed considerable emphasis on the difference between the account of Mr Bell and the account of Mr El-Mariesh as to the sequence of events at the meeting on the 1-2 August. It is quite clear that the two accounts differ significantly as to the sequencing of the discussions over the two days of the meeting. However, I have tried hard to see the significance of these differences, and I cannot. The meeting was convened for two purposes; to persuade the Defendants to accept the revised offer, and to enable Mr Bell and Mr Pimstein to discuss the pipeline (including the Four Contracts). Mr Garbett's absence from that meeting must have seriously inhibited the discussion of the pipeline, since Mr Garbett seems to have been primarily responsible for producing it. It is therefore no surprise that the majority of the time seems to have been taken up with discussing pricing. However the question of whether the pipeline was discussed before, after or (as seems most likely) simultaneously with the revised pricing structure is – I think – a matter of no consequence, and I am not at all surprised that recollections differ in respect of it.

72. Finally, Mr Lowe argues that Mr Bell was dishonest in his answers in respect of the TfL contract. He says that Mr Bell knew at the time of the August meeting that the only TfL contract that had been won was a small scoping project, whereas his evidence was that at that time he believed that a £750,000 contract had been won. Mr Lowe argues that this is evidence of Mr Bell's untruthfulness as to what he was in fact told by the Defendants. Mr Lowe is probably correct that the only TfL document which Mr Bell could have been shown at the August meeting was a statement of works document relating to a £28,750 scoping project. However, the July Pipeline document that Mr Bell had been provided with in advance of that meeting read "TfL - £1,500,000 – ongoing – closed in June – scoping started" (this replaced the May pipeline, from which the £750,000 figure had been derived, which read "£750,000 – NEW – close in June –

Won"). It seems extraordinarily unlikely that Mr El-Mariesh would have rowed back so spectacularly from the pipeline produced by Mr Garbett only a few days earlier at that meeting, and I therefore have no difficulty in concluding that Mr Bell came away from the meeting honestly believing what he thought he had been told in the July Pipeline document. I do not regard Mr Bell's evidence in this regard as indicating any dishonesty or attempt to mislead the court.

Mr Pimstein

73. Mr Pimstein is the CEO of SAED, which owns 48% of Decision. He is also a non-executive director of Decision. His evidence largely supported that of Mr Bell, differing on a number of matters of detail. Mr Pimstein's recollection on some matters was defective – for example, he said that he was focussing on the Four Contracts as early as the March Pipeline, whereas one of them (Nidec) does not appear in that pipeline at all. However, I think that this is accounted for by the fact that whereas Mr Bell was deeply engaged in the detail of the transaction, Mr Pimstein's role was directorial rather than managerial. Again, Mr Pimstein's evidence made clear that the focus of the analysis being conducted by both SAED and Decision focussed on the expected EBITDA, and the formal legal position with respect to the contracts was not his primary concern.

74. Mr Pimstein was clearly aggrieved, even at this distance in time, by what he perceived to be the dishonesty of the Defendants, and I felt that that emotion may well have coloured some of his testimony. However I do not believe that that emotion went so far as to cause him to give evidence which he did not believe to be true.

Mr Garbett

75. Mr Garbett's evidence was at times surprising. Although he and Mr El-Mariesh worked closely together, there seems to have been a division of labour between them such that Mr Garbett focussed on new business and Mr El-Mariesh on existing business. As regards his performance of that function, Mr Garbett aggressively asserted that he had no time for systems of any form, and that even though he knew that Chris Smith, the sales director, maintained a CRM system, he declined either to look at it or to use its output. His evidence was that the content of the various pipelines was the result solely of the application of his personal judgement.

76. Mr Garbett's disregard of formality appears to have extended to documents produced on his behalf – when examined on the information memorandum prepared in respect of the sale by Equiteq, he said "we had no knowledge, and it literally just got chucked in the bin".

77. The most important aspect of Mr Garbett's testimony was his evidence as to the process by which the sales projections which he produced were converted into the financial forecasts used to support the EBITDA targets. This was to the effect that this was Mr El-Mariesh's responsibility and not his – his job was merely to produce the aggregate estimates along with potential commencement and completion dates.

78. It was difficult to avoid the impression that Mr Garbett was seeking mentally to distance himself as far as possible from the events surrounding the transaction, and this at times gave the impression of evasiveness. However, on balance I think that the evidence that he did give was truthful.

Mr El-Mariesh

79. Mr El-Mariesh was a credible witness. He clearly enjoys spreadsheets, and the production of the forecasts and other financial information supplied to Decision was his own work. He also seems to have been pleased to demonstrate these skills to Messrs Bell and Pimstein at the August meeting – in particular his ability to produce scenario analyses identifying the consequences of different delays in different contracts.

80. The surprising thing about Mr El-Mariesh's evidence is that he claims that the translation of pipeline information into financial models was not his responsibility. Given that it had been Mr Garbett's evidence (which Mr El-Mariesh had heard) that it was not his responsibility either, this did raise the question of whether one of them was not telling the truth. I formed the view that in fact both were truthful. The fact thus revealed – that there seems to have been almost no connection within the Company between the numbers set out in the pipeline and the EBITDA forecasts provided to Decision – may go some way towards explaining the circumstances of the transaction. However, I do not think that it casts any doubt on the honesty of Mr El-Mariesh as a witness.

The Experts

81. I considered Mr Thompson, the expert for the Defendants, to be an able and admirably impartial witness.

82. Mr Dearman was the expert for the Claimants. Mr Lowe mounted a sustained attack on Mr Dearman's credibility as an expert on the basis that he had advised the Claimants in the course of the preparation of their claim, and was not therefore fully independent. He also pointed out – correctly – that some of the material contained in Mr Dearman's report set out his views on the facts, and in particular the states of knowledge of the Claimants and Defendants as regards the facts in relation to the Four Contracts. These were of course issues for the court to decide, and not matters which were the concern of expert witnesses.

83. In different circumstances these criticisms might have significantly undermined Mr Dearman's testimony. However, in this case they had no great significance. I of course disregarded those parts of Mr Dearman's report which set out his assumptions or opinions as to the facts to be determined, but I did not feel that any of the assumptions which he made were egregious or exaggerated. The joint experts report which he prepared with Mr Thompson demonstrated that the experts were agreed as to the approach to be taken to the quantitative aspects of the matters before the court, and – importantly – on the calculation mechanic which was to be applied to determine prospects and loss. The experts – understandably - differed as to the values to be employed in that calculation, and arrived at very different estimates of loss suffered. However, the fact that they agreed on approach meant that there was no significant issue on which I found myself having to decide between the professional opinion of one versus the other.

Issues

84. The issues before me are relatively straightforward. The primary question is as to whether the Defendants were, on the Effective Date, in breach of their warranties as to

19.1.2 (Material adverse change since the Accounts Date) and/or 20.1.3 (material inaccuracies or discrepancies in the Company's records). If they were not, then the case is at an end. If they were, two further questions arise. One is as to whether the Claimants were in breach of the warranty which they gave in clause 10.7 of the Agreement that they were not aware of any facts, matters or circumstances giving rise to a breach of warranty (and if so what consequences that breach should have for the liability of the Defendants), the other is as to whether the Defendants have a defence to some or all of these claims based on deficiencies in the notice of claim which the Claimants were required to give under clause 11.4.

The Records Warranty

85. The warranty itself reads

> All financial and other records of the Company ("Records"):
>
> 20.1.1 have been properly prepared and maintained;
>
> 20.1.2 constitute an accurate record of all matters required by law to appear in them, and in the case of the accounting records, comply with the requirements of section 386 and section 388 of the CA 2006;
>
> 20.1.3 do not contain any material inaccuracies or discrepancies;
>
> and
>
> 20.1.4 are in the possession of the Company."

86. The documents relied upon as "records" under this claim are identified in the Statement of Claim as:

(a) a document titled "Analysis reports 20180216" which sets out, on nine tabs, an analysis of the management accounts for FY2016 and FY2017;

(b) the forecast profit and loss account for FY2018 prepared as at 31 May 2018 ("The May Forecast"), which incorporated actual results up to 31 May 2018 and forecast revenue and expenses from 1 June 2018 to 31 December 2018;

(c) a schedule setting out the sales pipeline for FY2018, (the "May Pipeline");

(d) a schedule setting out the sales pipeline for FY2018 prepared in July 2018 (the "July Pipeline");

(e) a schedule of invoices purportedly raised in July 2018 (the "July Invoice Schedule");

(f) a schedule of invoices purportedly raised in August 2018 (the "August Invoice Schedule").

87. The question here is simply as to the meaning of the term "financial and other records" as used in the Agreement, given that the term is not therein defined. More importantly, the term is not a term of art in either legal or accounting science.

88. Mr Warwick K.C., for the Claimants, argues that that term "records" as used in this warranty is deliberately much wider than "the statutory records required to be kept by Section 386 of the Companies Act 2006". It is clear to me that the documents concerned here would not fall within the scope of s.386, and I agree that this clause does have the effect of widening the potential scope of the term "records" beyond that scope.

89. Mr Lowe proposes that the correct place to start in interpreting this term in this context is the Agreement itself. Although not defined, the term "records" is used in a number of other places in the Agreement. In particular:

    i) Clause 9.5 obliged the Defendants, as soon as possible after the First Completion Date, to "send to the Buyer all records, correspondence, documents, files, memoranda and other papers relating to the Company which are not kept at the Property and which are not required to be delivered at First Completion".

    ii) Schedule 3, para 1 provides for various documents to be to be delivered to Decision on First Completion, including (at 1.1.6) "the registers, minute books and other records required to be kept by the Company under the CA 2006". Section 1134 of the Companies Act 2006 defines "company records" as "any register, index, accounting records, agreement, memorandum, minutes or other document required by the Companies Acts to be kept by a company, and (b) any register kept by a company of its debenture holders".

    iii) Various other clauses reflect the Company's obligations to maintain or keep "records" for the purposes of tax and employment matters: see schedule 4, part 1, para 25.27.3, schedule 4, part 2, para 1.3, para 1.8; para 10.2.

90. My starting point is the observations of Andrew Smith J in *Macquarie Internationale Investments Ltd v Glencore UK Ltd* [2009] EWHC 2267. In that case he observed that the books and records of a company are the records of everyday transactions which form the bedrock of that company's accounting and management systems – what might in a previous era have been called ledgers. They are the raw material from which the company's accounts are fashioned. There is a clear distinction between the records themselves and the analyses which are prepared by reference to them – thus Andrew Smith J observed that the term books and records "does not seem to me to cover management accounts, which are more naturally regarded as a product of the books and records of a business than the books and records themselves". This seems to me to be simply an articulation of the reference in s.386(2)(a) of the Companies Act 2006 to "records that are sufficient to show and explain the company's transactions". Thus, for example, if the cashbook of a business recorded a cash at bank balance which was different from the actual cash balance of the company at that bank, that would be a paradigmatic example of inaccurate books and records. The drafting of the warranty in this case seems to me to reflect this distinction, since the warranty is explicitly extended from "records" to "financial and other records", and this term is clearly intended to include the accounts of the company as well as the underlying records from which they are prepared.

91. Mr Warwick, for the Claimants, argues that the term "records" as used here is intended to be wider than simply those records caught by s.386. His suggestion is that the term "record" includes every document created by a business in the course of the conduct of its operations. I do not think that this can be right. If it were, the warranty would be – in effect – a warranty of the accuracy of every communication made pursuant to the negotiation of the Agreement, whether relating to the past, the future or hypothetical states which do not have any actual existence (such as "pro forma" accounts).

92. I think that it is clear that by no means all documents produced by a company in respect of its business are "records". Perhaps more importantly, the term itself implies a retrospective element – it is very hard to see how any statement about a future transaction into which a company intended to enter could be classed as a "record" in the ordinary sense of the word. This is consistent with the usages of the term elsewhere in the Agreement which I have noted above, which apply the term to documents recording what has already happened. A financial projection in relation to the expected future profitability of a company cannot, on this basis, constitute a "record" of the company.

93. In this regard, I should say that I entirely disagree with the argument that Mr Warwick put forward that these documents should be considered records because they were important to the recipients – in particular, that "In considering the scope of warranty 20.1 when valuing the Company's shares it was very important for the Buyer to know what sales were estimated to arise in the future." I think this is an attempt to turn the records warranty into a warranty of any projections contained in the warranted documents. I do not think that this would be a correct approach even if the document were covered by the warranty.

94. I think it follows from this that even if I am wrong that the documents concerned are not "records" for this purpose, there would still be no claim arising out of this warranty. The question of whether a record is accurate does not turn on what the record contains, but on whether it is an accurate record of the thing that it purports to record. If a director were to tell a series of lies to a board meeting, and the board minutes were to faithfully record what he said, the board minutes would not be an inaccurate record, even though the statements which they recorded would be inaccurate. Applying this principle to this case, in order to argue that the pipeline documents were inaccurate records, it would be necessary for the Claimants to show that they did not accurately record the beliefs of the Defendants. I think it is clear from the evidence that in practice this means the beliefs of Mr Garbett, since Mr El-Mariesh seems to have relied on Mr Garbett for this side of the business. I am strongly of the view that Mr Garbett was guilty of a degree of self-persuasion when he put the pipeline documents together. However he was extensively cross-examined on this point, and I can find nothing in his evidence which suggests that what was written was not an accurate record of what he believed the position to be. The same applies as regards the May Forecast – no matter how implausible the beliefs of the Defendants may have been at the time when this document was put together, I can find no evidence that it did not, at that time, accurately record their beliefs as to the likely course of the financial year.

95. On this basis, I find that the May Forecast, the May Pipeline, the July Pipeline were not "records" of the company in this sense, and, even if they were, they were not inaccurate.

96. I also find that the July and August Invoice Schedules were not records of the Company, in that – like management accounts - they were created from the records of the Company. Also, even if they were used in a way which was calculated to mislead, they are not themselves incorrect or misleading, since they are accurate statements of the position of the books of the Company

97. The first document ((a) in paragraph [86] above) was not identified or challenged in evidence.

98. I am therefore of the view that none of the documents identified in paragraph [86] above were records of the Company within the meaning of Warranty 20.1.3.

The Material Adverse Changes Warranty

99. This takes us to the most significant of the issues raised by the Claimants – the allegations of the breach of the material adverse change warranty. The Claimants put this claim on two bases – one being that there was a material adverse change in the turnover of the company, and the other being that there was a material adverse change in the prospects of the company.

100. Before addressing the facts, it is necessary to clarify how a breach of a warranty of this kind should be established. In essence, there are three stages to the process. The first is to determine what might be called a “baseline” figure – that is, what was the expected or forecast level of the relevant factor at the time of the contract. The second is to determine the “actual” figure – what was the actual position as at the date of the contract. The third is to consider the difference between the baseline and the actual figure, and determine whether that difference is so great as to be material.

101. The establishment of a baseline figure is not as easy as it seems. For a well-established business with predictable revenues, the baseline may simply be the historic level of that factor – thus, if turnover has been 100/month for the last five years, the baseline will be 100/month. However, for a business with highly variable turnover, such an exercise may make no sense. In this sort of case it is necessary to examine the process by which the agreement was reached, and to try and establish what a reasonable expectation would have been. Here again, the test is objective and not subjective – a wildly over-optimistic purchaser does not acquire a cause of action in this regard as a consequence of his over-optimism. The baseline is the level which reasonable buyers and sellers, had they been asked to do so, would have agreed to be the most likely estimate of the factor concerned over the period concerned.

102. The ease of establishment of the actual figure depends heavily on the factor forecast. For turnover, for example, the actual level of turnover as at the Effective Date can be established by simple inspection of the books of the Company at that date. However, for a warranty as to the future – in this case, of prospects – some analysis may be necessary in order to determine what the actual prospects of the Company were as at the Effective Date. This matter is addressed further below.

103. I note in passing that although this approach to the question of whether there has been a breach of a warranty, comparing expected and actual outcomes, is very similar to the process of calculating damages by comparing warranted and actual values, there is a very important difference. In deciding whether there has been a breach of a warranty,

the differences between the expected and the actual positions are both assessed objectively. The question of material breach is a question of fact, and is not determined by the state of mind of either party. The assessment of damages is very different. The essence of an award of damages is that it is not an assessment of the loss to a hypothetical purchaser – it is an assessment of the loss actually suffered by the specific purchaser. It would therefore be at least theoretically possible to find that a breach of a material adverse change has been established, but no liability for damages arose. The two are entirely distinct assessments, and must be kept separate.

The Meaning of "Material"

104. Material is an ordinary English word, and its application to a set of primary facts is itself a question of fact (*Fitzroy House, Epworth Street (No. 1) Limited v. Financial Times Limited* (2006) 1 WLR 2207 paragraph 36).

105. One way of testing whether a change is material is to ask whether it is so significant that the other party, had they known of the change, would not have entered into the transaction at all, or would have entered into it on significantly different terms (Per Blair J in *Grupo Hotelero Urvasco v Carey Value Added* [2013] EWHC 1039 (Comm) at [356]). I think that this is the correct test. However, the test is an objective test – evidence of the actual states of mind of the parties is not – and should not be – admissible in this regard. The question is as to whether a reasonable person who had entered into the transaction with the aims and objectives of the buyer would have sought to withdraw from or renegotiate the transaction had he known of the change. That is the true test of materiality.

106. There is a dearth of English authority on material adverse change, and those cases which have addressed the question have tended to be in the context of loan agreements (in which the occurrence of a material adverse change in the financial status of a borrower may constitute a default under the loan entitling the lender to call in the loan). Clauses of this kind have been considered in *BNP Paribas v Yukos Oil Company* [2005] EWHC 1321 (Ch) (Evans-Lombe J) and *Grupo Hotelero Urvasco v Carey Value Added* [2013] EWHC 1039 (Comm) (Blair J). In the latter of these, Blair J said at [364]

> "In summary, authority supports the following conclusions. The interpretation of a "material adverse change" clause depends on the terms of the clause construed according to well established principles. In the present case, the clause is in simple form, the borrower representing that there has been no material adverse change in its financial condition since the date of the loan agreement. Under such terms, the assessment of the financial condition of the borrower should normally begin with its financial information at the relevant times, and a lender seeking to demonstrate a MAC should show an adverse change over the period in question by reference to that information. However the enquiry is not necessarily limited to the financial information if there is other compelling evidence. The adverse change will be material if it significantly affects the borrower's ability to repay the loan in question. However, a lender cannot trigger such a clause on the basis of circumstances of which it was aware at the time of the agreement."

107. This passage was described by Cockerill J. in *Travelport Limited v Wex Inc.* [2020] EWHC 2670 (Comm) ("Travelport") as "the leading statement of principle in the English authorities".

108. In coming to his conclusion, Blair J cited with approval the decision of the Delaware Court of Chancery in *IPB Inc v Tyson Foods Inc* 789 A2d 14 (Del Ch 2001) as to the construction of a "material adverse effect" event in a corporate sale and purchase agreement, to the effect that such clauses "are best read as a backstop protecting the acquiror from the occurrence of unknown events that substantially threaten the overall earnings potential of the target in a durationally significant manner." There has been some debate in the English courts as the appropriateness of considering this and other Delaware authorities in this context. In my view, it is entirely appropriate for an English court to have regard to such cases, for the reasons set out by Cockerill J in *Travelport* at [176].

> "WEX resisted recourse to the US authorities. Ms Tolaney Q.C. argued that there was plenty of English authority and that, contrary to the Sellers' submissions, the cases were not admissible as factual matrix or under the Practice Direction. I have not been at all attracted by that submission. There is a dearth of relevant English authority. While I would agree that the cases are not admissible as factual matrix, this is just the kind of situation where a review of the authorities from a foreign court is called for. Those authorities will obviously not be binding or formally persuasive, but to ignore the thinking of the leading forum for the consideration of these clauses, a forum which is both sophisticated and a common law jurisdiction, would plainly be imprudent – as well as discourteous to that court. The same goes for the academic learning which is often cited in the Delaware Court."

With respect, I agree.

109. The observations made in *IBP* are of some relevance to the case before me. In particular, Vice Chancellor Strine said

> "These negotiating realities bear on the interpretation of § 5.10 and suggest that the contractual language must be read in the larger context in which the parties were transacting. To a short-term speculator, the failure of a company to meet analysts' projected earnings for a quarter could be highly material. Such a failure is less important to an acquiror who seeks to purchase the company as part of a long-term strategy. To such an acquiror, the important thing is whether the company has suffered a Material Adverse Effect in its business or results of operations that is consequential to the company's earnings power over a commercially reasonable period, which one would think would be measured in years rather than months. It is odd to think that a strategic buyer would view a short-term blip in earnings as material, so long as the target's earnings-generating potential is not materially affected by that blip or the blip's cause." (at p.67)

He summarised this as follows "A short-term hiccup in earnings should not suffice; rather the Material Adverse Effect should be material when viewed from the longer-term perspective of a reasonable acquiror." (at p. 68).

110. Although these views have no legal force in this jurisdiction, I regard them as setting out an entirely correct approach to the construction of clauses of this kind. In particular, I think that this is an entirely accurate description of the position in which Decision was when it acquired the Company. It is entirely clear from the evidence that it was not engaged in any form of financial speculation – its aim was to develop a UK business, and it regarded the acquisition of the Company as a step towards that aim. Viewed from that perspective, a shortfall in two months turnover cannot, of itself, constitute any sort of material change.

111. The point was raised before me that that the test of materiality for this purpose should be informed by the accounting definition of the term. This is set out in paragraph 2.6 of Financial Reporting Standard 102, which observes that

> "information is material, and therefore has relevance, if its omission or misstatement, individually or collectively, could influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances".

The accounting profession tends to use a ready reckoner of around 5% of profit before tax as its measure of materiality.

112. I do not think that there is any necessary read-across between the accounting concept of materiality and the use of the term in a contract. In fact the two perform entirely different functions. The challenge which faces the accountant is to guess what a hypothetical user of the accounts might consider significant, and to produce accounts which do not omit anything which might be considered significant by such a user. In the contractual context, by contrast, we know who the parties are, and can divine their interests by evidence. I think that the correct test of materiality in the context of a contractual term of this kind is that a breach is material if, had it been known to the other party in advance, the other party would either have declined to proceed with the transaction at all, or agreed to proceed only after a renegotiation of the financial terms. Determining whether this is the case is a matter of evidence, and cannot be reduced to a mathematical expression.

113. There is no presumption that a variation in any factor which exceeds the accounting definition of "material" in size is therefore "material" in the context of a contractual provision relating to "material adverse change".

114. Finally, there is the issue of delay. Mr Lowe argues that at the Effective Date the revenues due to arise from the Four Contracts should have been regarded as merely delayed, and that what the Company was suffering was, in the words of Vice Chancellor Strine, a "short-term hiccup". It is clear that this is not in fact what happened, but that is not a relevant factor – the question is as to what the position should have been perceived to be at the Effective Date.

115. The question of how big a disruption has to be before it is more than a "mere hiccup" is, unsurprisingly, entirely dependent on the business model of the Company concerned. The problem in this particular case was that the Company had a fixed cost base, in the form of its staff, and it had sized that cost base in the expectation of winning those contracts at the times projected. For a business of this kind, even a short delay in winning a large contract would result in significant losses being accumulated very quickly, and a delay of even a few months would have a massive impact on the business. That is, of course, exactly what happened here. I would also note that whereas for a large business a delay in some contracts might be of no significance, even a short delay in a substantial portion of the expected revenues could potentially be very material. In the case of the Company, a significant delay in winning even one of the contracts could potentially, given their size, have been material. The fact that (a) these contracts between them accounted for 35% of the total revenue of the Company for 2018, and (b) none of them produced revenue to anything like the levels set out in the May forecast, means that the issue of delay is not a minor point to be disregarded, but is the very root cause of the problem which subsequently arose. In short, it is absolutely not the case that an interruption to revenue streams which is expected to be corrected in the future is ipso facto not material. For certain business structures, even a short interruption in revenues can be material. Everything depends on the circumstances.

The Turnover Warranty

116. Here again, I can deal with the turnover point fairly shortly. I think that it is clear that what is meant by the term "a material adverse change in turnover" is that the turnover for the period concerned is significantly worse than a baseline. Unless the facts suggest otherwise, that baseline should be taken to be the historic level of turnover of the Company as set out in the financial information which has been provided by one side to the other.

117. The question that needs to be addressed here is as to what time period needs to be used to assess the baseline. For a business (such as a construction firm) with a significantly fluctuating turnover, it may be that a very long period would be appropriate. For a business whose business involved a steady turnover (such as a petrol station), a significant deterioration week on week might, if sufficiently large, constitute a breach of this warranty if not disclosed. In effect, what the warranty is intended to do is to ensure that any sufficiently significant reduction in the level of business done by the company to be sold is to be notified to the buyer if it occurs before the contract date.

118. Here again, I think that the reference to "turnover" is retrospective. Prospective developments are covered by the warranty in respect of prospects. It is wrong to combine the two to create a sort of warranty of future performance – it seems to me to be clear that that is not what the clause is seeking to achieve.

119. The question is therefore the relatively simple one as to whether the deterioration in the turnover of the Company between 31 July (which is the last date from which the Claimants had financial information) and the 12 October 2018 (the Effective Date) was materially adverse.

120. The Company had historically maintained a fairly stable month-on-month revenue stream. In the year 2018 for which historical figures were available, monthly turnover had fluctuated between £314,998 and £515,372, and a similar, relatively steady rate of

month-on-month revenue was observed in the financial year 2017. The focus of this enquiry must therefore be on the two months of August and September. Turnover in August was £269,999 and in September £283,360. These numbers compared with the predicted amounts set out in the Forecast of £629,804 and £626,969 respectively.

121. This is prima facie a very significant change, whether the baseline for comparison is taken to be the historic average run-rate or the forecast level. However, this takes us back to the question of what is meant by materiality. Mr Lowe argued strenuously that even a change of this magnitude would not be material if the position were simply that revenues were being delayed for a few weeks – he argues that in a case like this materiality is not measured by a simple comparison of numbers one with another, but by reference to all the circumstances of the transaction. He is clearly correct in this regard – the assessment of materiality in a case like this is not – and cannot be reduced to - a merely mathematical exercise.

122. The very high level of operational gearing within the Company meant that relatively small changes in turnover could have a relatively large impact on profitability, and that is of course exactly what happened here. However, I think that the warranty in respect of turnover applies only to turnover, and should not be interpreted through the lens of impact on either current profits or future prospects.

123. The question is therefore simply as to whether the turnover figures for the months of August and September were so far away from the long-run average for the Company that a hypothetical reasonable seller would have concluded that there had been a fundamental change in the nature of the revenue flows into the Company. Although there was a significant drop in these figures – particularly considered on a month-by-month basis – I am by no means certain that it is large enough for such a seller to have concluded that there was such a fundamental change. It should also be emphasised that the turnover warranty, unlike the prospects warranty, is necessarily purely backward-looking. The question is simply one as to whether developments up to the Effective Date constitute a material change. I have some difficulty with this determination, but I think that on balance the Claimants have failed to make their case that these events, taken as a whole, show a change in turnover which was so significant as to be material.

The Prospects Warranty

124. This takes us to the real question which arises on these facts – was there a material adverse change in the prospects of the Company in the relevant period?

125. There was some debate between counsel before me as to the meaning of the term “prospects” in this context. Mr Lowe, for the Defendants, suggested in argument that “Prospects” refers not to any attempted mathematical assessment of future performance over an unspecified period (or to any “forecasts” or pipeline, which are transitory), but refers more generally to the Company’s chances of being successful in the future (by reference to company-specific, as opposed to market-based, factors affecting its trajectory, such as e.g. relationships with key third parties such as SAP, the quality of major ongoing client relationships, its reputation and goodwill, and the retention of key staff). Mr Warwick, by contrast, argued that all of these came down in the end to a single measure, that being the future profitability of the Company.

126. I think that there is some truth in both of these. However, as with much of this case, it is impossible to lay down any abstract definition, and it is necessary to approach the issue by interpreting the term in the context of the transaction. As noted above, the reason for the acquisition in the first place was to give Decision a platform from which to build a business in the UK. There is no doubt that there were a number of factors which made the Company attractive to them, and these include the factors that Mr Lowe identifies. However, the entire negotiation between the parties was based on EBITDA levels. It may well be the case that Decision would have been prepared to proceed with the transaction even if it had known that the earnings of the Company would drop significantly. However, it is entirely clear that it would not have been prepared to proceed at the price level which it had agreed. Thus, although other factors were of importance to Decision in its pursuit of the transaction, I think it is clear that the overriding primary factor was future gross profit. Specifically, it seems to me to be clear from the evidence that if anyone had asked Decision what it considered the "prospects" of the Company to be at any point prior to completion (or indeed thereafter), the resulting discussion would have been conducted entirely in terms of expected levels of EBITDA.

127. This brings us, by an admittedly circuitous route, to the core of the point at issue. The core of the issue before me is, as articulated in Issue 3 of the Outline Issues for Trial

> "As at the First Completion Date (viz 12 October 2018), since the Accounts Date (viz 31 December 2017) had there been a material adverse change in the … prospects of the Company on the basis that the … prospects of the Four Projects was not properly reflected in the FY2018 Forecast P&L, the May 2018 Sales Pipeline or the July 2018 Sale Pipeline, as alleged?"

128. I think that the way to approach this is to ask what the position would have been if, immediately prior to the first completion date, the Defendants had given an accurate account to Decision of the position as at that date. In subjective terms this question was partially answered by Mr Pimstein in cross-examination. The crucial observation is towards the end of his cross-examination, when asked about how he reacted to the discovery that expected revenues were well adrift. He said

> "At no point did either defendant, or their adviser, ever notify us to say, "Guys, we have hit a block. There had been a terrible thing happening here. Turnover has fallen off a cliff. Our guys are on the bench. We need to restructure this transaction. Things have not worked out how they were, and we need to sit down and work a way forward."

129. I accept that I must not approach this issue subjectively by reference to the position of Decision itself. However, I think that this is exactly how any other buyer in the position of Decision would have reacted. I am quite clear that such a buyer would not have abandoned the transaction completely – as Mr Lowe argues, they were acquiring the capability to execute mandates in the UK which they did not have, and that had a value to them. However, I think that the facts which would have been revealed by such a conversation – that the Company's ability to originate new work was failing – would have been of very great significance to any hypothetical reasonable buyer.

130. Consequently, I am of the view that if the Defendants had given full and frank disclosure to Decision as to the true position of the Company on the Effective Date, and of their true opinions of the likely profits of the Company at the year-end, Decision would have required a further renegotiation of the purchase price. The logic of this position is irresistible – Decision had negotiated a price based on an EBITDA for the year of no less than £900,000. I find it inconceivable that if they had thought that the Defendants expected the true figure to be around £300,000, they would have proceeded on the agreed basis.

131. The Defendants' position, in summary, is that this is not the case because, even in October 2018, a reasonable person in their position could not have expected that the year-end figure would be as bad as it in fact turned out to be.

132. There are two aspects to this. One is that at the Effective Date the Defendants knew, and Decision did not, the outcome of the months of August and September. I note that although the Defendants had probably not seen the formal management accounts at the Effective Date, everything that they told the court about the way that the Company was managed, and in particular their familiarity with the course of its business on a day-to-day basis, makes it impossible to believe that they would not as at 12 October have been fully aware of the course of business in August and September.

133. These months had been put down in the May forecast as producing EBITDA of £231,796 and £228,077 respectively. The Defendants knew that the actual figures were a loss of £40,746 in August and a profit for September of £2,382. This means that they knew that they were nearly half a million pounds adrift of the forecast which they had given Decision in May. This difference, although enormous, would not of itself have taken them out of the range of contemplated outcomes under the SPA. However, the only way that a reasonable person in their position could have concluded that there had not been a material change in the prospects of the Company would have been if they were very highly confident that the remaining months of the year would produce at the very least the £432,463 predicted for it in the May forecast.

134. I think this is relevant to the issue of the approach of the hypothetical reasonable seller. A hypothetical reasonable seller in this position would, I think have concluded that there had been a material adverse change in the prospects of the Company *unless* he had a very high degree of confidence that profits over the next few months would be sufficient to rebalance the ship. That question would depend almost entirely on the prospect of substantial revenue under the Four Contracts being received in that period. The question is therefore simply this – how confident of this were the Defendants at the time, and would that confidence have been shared by a hypothetical reasonable seller? I turn now to considering that issue.

The Four Contracts

BBC

135. The Company was in 2018 engaged as a subcontractor in a pitch to the BBC by another company, HCL. The BBC is listed in the July Pipeline with a value of £2,000,000, a status of “delayed” and a close month of August. Total revenue of £427,300 from this project was included in the May Forecast from September 2018 to December 2018.

136. On 23 July 2018, the Company were informed that the HCL bid had been rejected. This was never communicated to Decision prior to the Effective Date. The reason that the Defendants gave for this was that they were optimistic that they would be able to approach one of the other companies pitching for the contract and to become a subcontractor to them instead, thereby preserving the work.

137. The Claimants say that there was no justification for any belief that any revenue would be received under this contract at all. Mr Garbett in his evidence explained that because of the Company's good relations with the BBC, he believed that it would be possible to join the bid of another bidder and get the work that way. I am sure that he hoped that this would happen, but I absolutely do not think that a hypothetical reasonable seller would have had a high degree of confidence that this contract would produce any significant turnover in the medium-term future.

TFL

138. TFL is listed in the July Pipeline with a total value of £1,500,000, a status of "ongoing" and a close month of July. Revenue of £512,100 was included in the May Forecast, of which £251,550 was forecast to be earned between June 2018 and September 2018.

139. There is no doubt that the Company had at this point a mandate from TFL – the question is as to the nature of that mandate. The position seems to have been that the Company had been awarded a £28,750 mandate for a "scoping exercise". It was expected that this would in due course lead to a mandate for substantial work, but this further mandate had not yet been awarded. I think it was accepted by both sides that in this industry it would be unusual to mandate one firm to scope a project and a different firm to execute that project, so the expectations of the Company were not fanciful. However, the first defendant knew (as he said in his e-mail of the 24 July 2018) that TfL was required to go through a formal procurement process for the main contract due to its status as a public authority. The fact that the Company had been instructed on the scoping exercise did not therefore imply that it would certainly get the primary contract.

140. What does seem clear is that the Defendants' communications with Decision on this issue were – to put it at its mildest – open to misunderstanding. Mr Bell's evidence was that he took the pipeline documents at face value, as suggesting that there was a £1,500,000 mandate, work on which had commenced. There is nothing in the written documents which gives any clue that the true position was that a small scoping mandate had been won but the bulk of the work would have to go through a formal tender process.

141. The Claimants do not deny that there was a real prospect of this work being won as at the date of the warranty. However, what they do say is that the estimate in the May Forecast that £512,100 of revenue would be derived from this contract between June and December was absurdly overstated, and that a reasonable estimate would have been (a) no revenue for this project in June and July; (b) revenue of £1,500 in August to reflect the work that had been carried out; and (c) 50% of the estimated revenues for months 1 to 3 of the project (that is, £54,000, £94,650 and £92,400) for the months October to December. This would have resulted in a projected revenue for the year for this project of £122,025, as against the figure projected in the May Pipeline of £512,100.

142. I think that a hypothetical reasonable seller could well have concluded that it was certain that £28,500 would be received under this contract, and highly likely that £122,025 would have been received by the year end. This is not, however, anywhere close to the £512,100 which had been projected for the contract over 2018 as a whole.

Nidec

143. Nidec is listed in the July Pipeline with a value of £750,000 relating to "New client implementation". This is given a status of "Ongoing" and a close month of August. In the May Forecast, revenue of £358,288 was included for this project from June 2018 to December 2018. It seems clear that when the May Forecast was prepared, this project was still conjectural, and the narrative included in the July Pipeline indicates that at that point the project was still at the scoping phase.

144. The evidence suggests that the Company had good relations with the staff at Nidec, and were reasonably confident that a mandate would be won in due course. However, it is difficult to regard the projection that this work would commence in August as anything other than excessive over-optimism. The evidence suggests that when the June Pipeline was prepared, the Company did not have any grounds to believe that they had won the work or that it would commence at that date – indeed at that stage they had nothing but a sales lead. It is fair to note that the Company did eventually win a mandate from Nidec in 2019, but the mandate was worth less than £200,000. The Claimants argue that this mandate was so notional that it was wrong to include any revenue deriving from it in the FY2018 Forecast P&L in relation to this project.

145. Here again, I cannot accept that a hypothetical reasonable seller could have concluded that any forecast revenue should be attributed to this contract at all for the year 2018.

Kerry Group

146. Kerry Group is listed in the July Pipeline with a value of £1,500,000, a status of "Delayed" and a close month of October. Revenue of £669,456, to be generated between June and December 2018, was included in the May Forecast. As at 24 July 2018, the proposal was described as "currently under assessment by Kerry", on the basis that in order to undertake the project Kerry would have to commit resources of its own, and there was uncertainty as to whether it would be able to do so.

147. In fact, Kerry only sent out an RFP for this work on the 9th October. The Company tendered for it, but were notified that they had not made the shortlist on 14th December.

148. The Claimants say that it was wrong to include any revenue at all from Kerry Group in the 2018 forecast.

149. My conclusion on this contract is the same as for the Nidec contract – I do not believe that a hypothetical reasonable seller would have concluded that there was any reasonable prospect of any revenue being received under this contract in the course of calendar 2018.

The Prospects Warranty - Baseline

150. Part of the problem in determining the baseline for the prospects warranty is identifying what hypothetically reasonable parties would have agreed that the prospects of the Company actually were. The May Forecast suggested that EBITDA for the year might be £1.5m, but it does not seem to me that the Claimants ever regarded this as certain, or even probable. I think the best guide to the expectations of the parties can be derived from the agreed pricing structure for the transaction.

151. This structure was that Decision would pay £5m for the first 75% of the shares in the Company, with a further amount to be paid based on the EBITDA of the Company for 2018. This further amount would be zero if 2018 EBITDA were less than about £1.1m. The remaining 25% of the shares would be purchased for the issue of a number of shares in Decision plus a cash payment calculated by reference to the average EBITDA of the Company for the two years 2018 and 2019. This liability was floored at around £0.8m, which would be payable if the average EBITDA for these two years was less than £0.9m. It increased with earnings, such that if that average exceeded £1.5m, a further £2.9m cash would be payable. This is the pricing which was subsequently agreed between the parties.

152. Mr Bell explained in evidence that he thought of the effect of these arrangements as being tantamount to a "warranty" by the Defendants, in that if EBITDA was lower than the target of £1.5m, they would suffer financially from that underperformance, and the price that Decision would pay would be correspondingly reduced.

153. I think there are two propositions which can be derived from this. One is that Mr Bell had significant doubts that the business would produce an average of even £1.5m EBITDA for the two years, and had built significant protection against that outcome into his pricing proposal. The other is that Mr Bell clearly thought that the worst likely outcome was EBITDA of around £0.9m. Given that at the time that he made this proposal the actual EBITDA for the first half of the financial year was in excess of £0.4m, this must have seemed a reasonable worst case.

154. Mr Lowe made detailed submissions on this point, accompanied by spreadsheets. His approach was to take the information which he said had been provided by the Company to Mr Bell in respect of each of the Four Contracts and to work out what the position would have been if the information given had been accurate. This was accomplished by reconstructing the May Forecast, inserting the historic figures for June and July (which Mr Bell had been given) and recalculating the forecast on the basis that the mandates concerned had commenced on the delayed dates on which Mr Bell had been told that they would commence (October in each case). This approach suffers from the defect that Mr Bell's evidence was that he had been told that TfL had in fact already commenced, and on a project which would bring in £447,600 by the year-end. To deal with this Mr Lowe produced a forecast which set out the position as it would have been if the other three projects had commenced in October but the TfL project had proceeded on the forecast time-line. This suggests that, on this basis, the reasonable expectation of Mr Bell should have been that EBITDA for the full year should have been £985,996.

155. This figure is not intended as a precise calculation but as an illustrative estimate. However, it does support my view that the baseline estimate from which the assessment of material adverse change must start is the expectation that the Company would

generate around £1m EBITDA in the year 2018, and possibly a little more in 2019. That is the expectation which a reasonable buyer would have had, and the baseline against which the question of whether there was a material adverse change must be assessed.

The Prospects Warranty - Actual

156. As regards the actual prospects as they would have been assessed by a hypothetical objective third party in the position of the sellers as at the Effective Date, I am assisted by a calculation contained in Mr Dearman's report and accepted in the joint experts' report. What Mr Dearman has done is to produce a forecast for the prospects of the Company for the financial year 2018 on the basis that it accurately reflects the true expectations under the Four Contracts as I have found them to be in paragraphs [135] to [149] above. That revised forecast is £325,897. Mr Lowe challenges this figure, but for the reasons set out in paragraph [210] below I reject that challenge. Consequently I am prepared to use this figure as an accurate estimate of what a reasonable hypothetical seller in the position of the Defendants would have known to be the true expected prospects of the Company for the year 2018. More simply, what that figure indicates is that the Company, in aggregate, would be lossmaking in the second half of the year.

157. If, on the Effective Date, the baseline figure for expected prospects for 2018 was £1m, whilst the actual expected profit was £0.3m, I think it is clear that this constitutes a material adverse change in the prospects of the Company as at that date. If the Company was now lossmaking, this would lead to cash-flow shortfalls and the need for recapitalisation – as indeed eventually proved to be the case.

158. I am therefore satisfied that at the Effective Date, the Defendants were in breach of their warranty that there had been no material adverse change in the prospects of the Company as at that date.

The Other Defences

159. I therefore turn to Mr Lowe's two other defences. The first of these it that there is a complete defence to action based on the fact that the Claimants had actual knowledge of the relevant facts at the relevant time. The second is that the notice given to the Defendants under the terms of the Agreement was ineffective, so their claim is invalidated by the terms of the Agreement.

Knowledge

160. The question of what the Claimants knew on the Effective Date is significant for three reasons. One is as to the question of what the reasonable expectations of the prospects of the Company might be for the purposes of Warranty 19. A second is as to the calculation of damages if Warranty 10.7 is engaged. A third relates to what might be called the *Urvasco* defence. In that case Blair J, in the passage cited above, observed that "a lender cannot trigger [a MAC] clause on the basis of circumstances of which it was aware at the time of the agreement.".

161. The starting point for this issue is the terms of the Agreement. As is usual with an SPA, the Agreement provided for the compiling of a disclosure letter setting out the matters which were formally disclosed to the purchaser. It then included clause 10.6, which provided that

> "Except for the matters Disclosed, no information of which the Buyer (or any of its agents or its advisers) has knowledge (in each case whether actual, constructive or imputed), or which could have been discovered (whether by investigation made by the Buyer or on its behalf), shall prejudice or prevent any Claim or reduce the amount recoverable under any Claim".

The term "Disclosed" is defined in the Agreement as meaning "disclosed in the Disclosure Letter". The Agreement also provides that

> "11.5 The Sellers shall not be liable for a Claim to the extent that the Claim:
>
> 11.5.1 arises from facts, matters or circumstances that have been Disclosed including Disclosed in the Disclosure Letter".

162. Mr Lowe very reasonably objected to this clause being given a meaning that meant that the Claimants could disregard actual knowledge of information which they had by reason of its having been provided to them by the Defendants or the Company. I agree with this – such a construction seems heavily at variance with any plausible intention of the parties. However, I think that the intention of these clauses is clearly to prevent the seller from raising defences of knowledge based on information which was not directly provided to the buyer, but which the buyer might or ought to have inferred. I therefore think that their effect is to give a seller a defence to a claim where he can show that information which he had provided to the buyer would have given that buyer actual knowledge of facts he relied upon, but to deny any defence based on allegations of any sort of constructive knowledge.

163. If actual knowledge based on information provided is required in order to defeat a claim on this basis under the Agreement, is the position different for the other heads identified in the paragraph above? I do not think it is. In particular, as regards what I have called the *Urvasco* defence, I do not think this defence arises in respect of circumstances of which the relevant party could in theory have made itself aware, but in fact did not do so – and in any event I think that in deciding how and whether the *Urvasco* defence does apply, the starting point must be the terms of the contract – and in this case clause 10.6. The enquiry is therefore in all cases as to the Claimant's actual knowledge, to the extent that that knowledge was derived from information provided by the sellers or the Company.

164. Mr Lowe placed great emphasis on the fact that it was made clear to Mr Bell and Mr Pimstein that the Four Contracts were possibilities which might come good in the future rather than legally binding commitments. He says that this information was provided to the Claimants, that they had actual knowledge of it, and that therefore they have no action.

165. I agree that neither Mr Bell nor Mr Pimstein were told, or believed, that the Four Contracts were formally legally committed. I do not, however, agree with Mr Lowe's binary presentation that a contract which is not firmly legally committed is so notional as to be disregarded. There is clearly a continuum of likelihood between a contract which is certain and one which is a mere ambition. I think the Claimants relied on the

Defendants to tell them where on that continuum each of the Four Contracts sat, and believed and relied on what they were told.

166. The fact that Mr Bell knew that there was a floating element to these contracts is confirmed by some of the e-mail traffic between him and the Defendants, in which he reacts with a degree of equanimity to the news that some of the possible mandates may be somewhat delayed. However, again, these e-mails are incompatible with the idea that he was told the truth – for example, in one e-mail he expressed disappointment with the fact that the TfL mandate had not in fact produced £54,000 of revenue in July – an expression which makes clear that he had no idea as to the true state of affairs with TfL.

167. The core of Mr Lowe's arguments in this regard is his position as to the meeting of 1-2 August. He says that at that meeting the Defendants delivered a complete and accurate account of the state of play as regards the Four Contracts, such that thereafter Decision had a complete picture of the position of the business. It thereafter was in as good a position as the Defendants to form as view as to the prospects of the business, and the fact that the actual outcome diverged from the expected path leaves them with no claim.

168. The difficulty with this argument is that there was no evidence from either side as to exactly what information as to the Four Contracts was provided or sought at that meeting. Unsurprisingly, the meeting was not minuted, and the recollections of those present are tainted by hindsight. What is clear is that Decision had two objectives for the meeting; one being to persuade the Defendants to accept their revised pricing structure, and the other being for them to verify that the fundamentals of the business were sufficiently robust to warrant the making of that offer. There was some largely unhelpful debate at trial as to what the precise sequence of events at that meeting was, but it is very unlikely that that point is in any way significant – the meeting was booked for two days, it took two days, and it seems unlikely that any of those involved would have paid any very great attention to the sequencing of the discussion of the issues.

169. I am therefore of the view that the only reliable way to ascertain what was in fact said at the meeting is, following the principle set out by Leggatt J in *Gestmin SGPS SA v Credit Suisse (UK) Ltd* [2013] EWHC 3560 (Comm) at [15]-[22], by reference to the contemporaneous correspondence entered into by the parties after it.

170. As I say, there is some conflict of evidence as to what Mr Bell was actually told at the August meeting. However, to my mind there is a single piece of evidence which dispenses with the idea that he was told the truth. If what he had in fact been told was that of the Four Contracts, one (the BBC) had been lost, one (Nidec) was for £30,000 rather than the £750,000 shown in the July Pipeline, one (TfL) was for £28,750 rather than the £1,500,000 shown in the pipeline, and the last (Kerry), far from starting in October as set out in the July Pipeline, would in fact not even commence until 2019 at the earliest, it is inconceivable that he would not have embarked on a major re-evaluation of the transaction. As he said in evidence, his perception was that "without [TfL and Nidec] there was nothing, nothing else".

171. I therefore think that the most telling piece of evidence as to what Mr Bell and Mr Pimstein were told in the August meeting is that Mr Bell did no such thing. Indeed he proceeded with the transaction as if he had been told nothing untoward. I regard this as strong evidence of the fact that he was in fact told nothing untoward.

172. In parallel with the August meeting, a proposal was being created and presented to the board of SAED to raise new equity to finance the acquisition of the Company by Decision. That proposal was based on a forecast EBITDA of £1,428,998 – slightly less than the £1,628,393 projected in the May Forecast, but clearly dependent on the revenues from the Four Contracts arising at roughly the times set out in that forecast. The idea that Mr Pimstein, having been told in clear terms that that would not in fact happen, would have taken no steps at all to inform his board of that fact is also not credible.

173. I turn now to the August Invoice schedule. I regard this as a significant document. Decision were becoming concerned by the lack of financial information from the Company, and required something which would provide some empirical evidence of what was going on. In the absence of management accounts, the next best option was a monthly schedule of invoices. In a business like that of the Company, where monthly billing was the norm, such a schedule should provide a rough and ready guide to the state of the Company's business. Mr Bell had previously requested and obtained a schedule of invoices for the month of July for this purpose. That schedule had totalled £515,860. This differed from the £456,422 actually recorded in the accounts, but a difference of that magnitude was unsurprising.

174. The August Schedule was very different. The month of August had been disastrous for the Company, and the provision of an accurate schedule to this effect would have put the Claimants on enquiry that projects were not coming on stream at the rate projected in the May Forecast, and that something was going wrong. I find it difficult to reach any conclusion other than that the August Schedule was prepared and sent with the aim of heading off any further investigation into the financial state of the Company. In this it succeeded.

175. The August Schedule purported to show revenue collected in August of £581,119. It was, however, a misleading document. It was prepared by aggregating all of the invoices which covered the month of August and calculating their gross amount – thus, a 12-month service contract with an annual value of £30,000 was included in the schedule as revenue of £30,000, rather than the £2,500 actually attributable to the month of August. Mr Lowe fairly points out that there are indications in the schedule itself that this might be the case. However, the point that Mr Bell made in evidence was that the schedule was presented to him as a rough summary of the August position, and he had in good faith treated it as such. He had therefore not subjected it to the sort of forensic examination which he might have applied in different circumstances.

176. I think that the best that Mr Lowe can say of this document is that its presentation affected Mr Bell with some sort of constructive knowledge of the true position of the Company in August. However, as I say at paragraph [163] above, I do not think that this sort of constructive knowledge is of any relevance to any of the determinations which I am required to make here.

177. The actual state of mind of Decision is clear from the correspondence before me. It is clear that Decision did not expect the Company to do much more than maintain its existing steady state as regards turnover and profit – in an internal e-mail of 22 June 2018 Mr Geeringh made clear his understanding that "Copperman is not growing, YTD performance is poor". However, Mr Bell set out his views very clearly in his e-mail of

the 23rd July to (inter alia) the Defendants. At that point he was preparing to explain the acquisition to the other shareholders of the Claimant. He wrote

> "With Nidec, BAE App Int, Kerry and TFL having commenced and the June start being critical I was confused to see that those client names haven't come up on the debtors report from June (BAE Applied was very small). This was picked up and in order to assure the board that the work plans are well on track and valid we require some supplementary proof."

178. I think it is clear that at this date Mr Bell believed that there was a common understanding between him and the Defendants that (a) the Company was still more or less on track to deliver the EBITDA set out in the May Forecast and (b) that the primary ground for believing this was that the contracts identified had been secured and would generate substantial revenue in the second half of the year.

179. I also note that Mr Lowe, in cross-examination, sought to construct a theory that Mr Bell and Mr Pimstein were deliberately misrepresenting what they had been told at the August Meeting in order to deflect blame for having entered into what turned out to be an extremely unfavourable deal. This, however, fails to account for the fact that if they had been given sufficient information at the August meeting to enable them to discern that the deal would be extremely unfavourable, they could have easily solved this problem for themselves by simply not doing the deal.

180. In this regard it is important to consider Mr El-Mariesh's evidence of the meeting. Given that Mr Garbett was not present, and it was Mr Garbett who had been responsible for the construction of the pipeline documents, Mr El-Mariesh says that the discussion went project-by-project through the forecast future work, looking in each case at both (a) the likelihood of getting the work, and (b) the volume of work involved. As regards the first of these, the discussion seems to have focussed primarily on Mr Garbett's e-mail of the 24th July. As regards the second, Mr El-Mariesh's evidence was that he had simply worked out how much work (in terms of man-days) the project concerned would require, multiplied it by the then prevalent charge-out rates, and used the result as an estimate of the revenue that the mandate would bring in. In particular, Mr El-Mariesh's evidence was that

> "It was categorically made clear to Mr Bell & Mr Pimstein that the timing of any project start dates were simply our best estimates, and in no way represented a guarantee that the projects would start exactly when we estimated they would. Mr Pimstein specifically asked the question about what the implication was (to the forecast) of any of these prospects being delayed, and I was able to demonstrate via "live" adjustments to the forecast model to show how the forecast for that project would "shift to the right", meaning it would move out, with the consequential delay in revenue generation." (paras 64-5 of his witness statement).

181. It is clear that the analysis described above was largely based on the July 24 e-mail. However, the question is as to how precise Mr El-Mariesh could have been as to the likelihood of the various projects being delayed. In his oral testimony, Mr El-Mariesh

was clear that the monthly numbers were produced by Mr Garbett. The 24 July e-mail provides no information as to the extent of any possible delay, and Mr El-Mariesh does not claim to have any insight into that part of the business – he described that process in his testimony as "a pure sales piece of work". Consequently, the only person who could have spoken to the issue of the probable length of the delay on these projects was not at the meeting. I am therefore quite sure that Mr El-Mariesh did not suggest to Mr Bell or Mr Pimstein that the delays on the Four Contracts might be so long as to destroy the EBITDA for the year, nor that they might be so long as to push the Company to the brink of failure.

182. A further piece of evidence as to Mr Bell's knowledge as at the Effective Date can be derived from his reaction to the receipt of the August and September management accounts. He received these on 31st October, several weeks after the Effective Date, from the Company's accountants, Barrow. Mr Bell responded almost immediately "I think there is a mistake as this cannot possibly be right that the revenue is a quarter of the budget. Please recheck and get back to me ASAP. If this is the case it would be quite disastrous". Mr Bell then sent Barrow the August Invoice Schedule which he had received, asking for an explanation as to why the August management accounts were so different from the invoice schedule. The response from Barrow was to confirm that they had prepared the August Invoice Schedule, but that they had prepared it in accordance with specific instructions from the Second defendant to provide a schedule of "all invoices where revenue fell within August 2018".

183. This interaction seems to me to make clear that not only did Mr Bell not have actual knowledge of the downturn in the Company's business as at the Effective Date, but that he was taken completely by surprise when he discovered it shortly thereafter.

184. I am therefore satisfied that Decision, in the persons of Mr Bell and Mr Pimstein, did not have actual knowledge of the fact that the prospects of the company had materially and adversely changed as at the Effective Date, and I find that any constructive knowledge which they might be found to have had would be of no relevance in this context.

The Notice

185. Mr Lowe also raised a point relating to the notice given by Decision under the Agreement. The Agreement, as is common with such agreements, provided that in order for any claim arising out of the transaction to be valid against the Sellers, notice of that claim, "summarising the nature of the claim (in so far as it is known to the Buyer) and, as far as reasonably practicable, the amount claimed", must be given within two years of the first completion date.

186. The clause itself (11.4) reads as follows

> "The Sellers shall not be liable for a Claim unless notice in writing summarising the nature of the Claim (in so far as it is known to the Buyer) and, as far as is reasonably practicable, the amount claimed, has been given by or on behalf of the Buyer to the Sellers … on or before the expiry of the period of 24 months commencing on the First Completion Date."

187. It is not disputed that the notice that was given was given within the prescribed period. However, Mr Lowe's challenge is as to whether the notice as given complied with these requirements. If it did not, he says, the claim is invalid per se.

188. The notice sets out a prospective claim under Warranties 19 and 20, and sets out the argument that an accurate forecast made at the Effective Date of the contract would have shown a material adverse change in the prospects of the Company.

189. It is common for SPAs (as in the present case) to contain a clause in this form. The effect of the clause is to extinguish a cause of action which might otherwise exist, and it is to that extent a limitation of liability clause. Such duties were considered by Cooke J in *Laminates Acquisition Co v BTR Australia Ltd* [2003] EWHC 2540 (Comm), from which, as Mr Lowe submits, the following general propositions can be derived:

i) Where a clause amounts to a condition precedent to liability (e.g. "no claim shall be brought unless", or indeed the language of the SPA in the present case) a compliant notice is "a matter of importance", and the burden of showing the condition precedent is met lies on the claimant: [30].

ii) While Courts may refer to other cases on notice provisions for guidance, the assistance to be derived may be "limited" since "each notice clause has to be construed for itself in the light of the commercial context in which it is found and the commercial purpose it is intended to serve": [29].

iii) "Notice" clauses of this kind are usually inserted for a purpose, to give some certainty to the party to be notified and a failure to observe their terms can rarely be dismissed on a technicality".

iv) More specifically, the purposes that can be served by a notice provision, in terms of enabling action to be taken, may include (as in that case they were agreed to include) enabling a party to (a) make informed enquiries; (b) make an informed assessment of a claim; (c) take precautionary steps (such as notifying insurers or preparing defence materials); (d) "obtain withdrawal of the claim or satisfy or settle it before legal proceedings are issued": [30].

v) A requirement to give notice as to the "nature of a claim" is likely to mean (as the parties agreed in that case) "notification of what is being claimed and the basis of it by reference to the SPA – namely the form and substance of the claim": [30].

vi) In construing a notice, the question is "how this notice would be understood by a reasonable recipient with knowledge of the context in which it was sent": [29].

190. The importance of the general purpose of notification clauses being to enable early settlement was emphasised in *Highwater Estates v Graybill* [2009] EWHC 1192 (QB). At [43], HHJ Waksman QC (as he then was) stated: "the commercial purpose of such clauses is to enable the vendor to know in sufficient detail what he is up against (not least because it might then enable the parties to settle without recourse to litigation)".

191. However, in *Triumph Controls – UK Ltd v Primus International Holding Company* [2019] EWHC 565 (TCC), O'Farrell J pointed out that the requirement is for clarity

rather than precision - she considered that this did not require "full details of particulars of the claims, such as required in a pleading", but did mean that "the description and quantification of the claims should be such as to give formal, unambiguous notice as to the basis of the allegations, so that Primus could investigate, respond to and make financial provision for the claims" (see at [115], also at [126]).

192. Mr Lowe argues that the pleadings plead six separate claims, two breaches of the turnover warranty, one breach of the prospects warranty and three breaches of the records warranty. He therefore says that the fact that the notice given did not specify, in respect of each of these breaches, the quantum of damages sought in respect of that breach means that the notice should be regarded as noncompliant and therefore disregarded. He also argues – correctly – that if this were found to be the case, the Claimants must fail completely. In support of this argument, he cites *Senate Electrical Wholesalers Ltd v Alcatel Submarine Networks Ltd* [1999] 2 Lloyds Rep 423. *Senate* is authority for the proposition that if a party pleads and advances its case in a way which leads to a particular damages calculation, and "does not offer the judge a more modest alternative", the court cannot adopt an alternative approach that was not pleaded. There is no element of any such consideration here – the claim pleaded by the Claimants did not lead to or require any particular outcome to the calculation of damages. The other is as to the form of contractual notices generally. On this topic, in *Senate* the Court of Appeal (Stuart-Smith LJ) had this to say about contractual notices

> "Certainty is a crucial foundation for commercial activity. Certainty is only achieved when the vendor is left in no reasonable doubt not only that a claim may be brought but of the particulars of the ground upon which the claim is to be based. The clause contemplates that the notice will be couched in terms which are sufficiently clear and unambiguous as to leave no such doubt and to leave no room for argument about the particulars of the complaint. Notice in writing is required in order to constitute the record which dispels the need for further argument and creates the certainty. Thus there is merit in certainty and accordingly, in our judgment the point taken by the appellants is not a matter of mere technicality and it is not without merit."

The court held that a letter which gave no specifics of a claim beyond references to communications made at earlier meetings did not constitute a valid notice for the purposes of a notice clause.

193. My starting point here is to consider the specific facts of the case. In particular, I cannot see how it would have been possible for the Claimants to proceed as Mr Lowe suggests and allocate different values to the different breaches. Mr Thompson attempted in his expert's report to calculate the loss relating to one particular breach – the breach of the turnover warranty – in order to demonstrate that this was theoretically possible. However, I agree with Mr Dearman that this exercise is in reality not possible, since, as Mr Dearman points out, the assumptions required to establish one breach necessarily imply other breaches which would fall to be valued in turn. In reality, the breaches here are so intertwined that it is impossible to say with any degree of plausibility that this breach caused £x of damage, whereas that breach caused £y. The reason that the Claimants gave only a single figure for the cumulative impact of the breaches was

because that was the best they could do, and that must mean that their estimate was "reasonable" – which is all that is required by clause 11.4.2.

194. I do not think that the facts of this case come anywhere near the principles established in *Senate*. There is no question that the Claimants' notice was such, or was pleaded in such a way, as to leave any doubt as to the allegations of breach being made or the calculation mechanism to be applied in arriving at the quantum of damages if the claim was successful. There is no question of the Defendants having been disadvantaged in any way by reason of the form of the notice or the way in which the case was pleaded.

195. I was also referred to *Teoco UK Ltd v Aircom Jersey 4 Ltd & O'rs* [2018] EWCA Civ 23, in which a notice which did not specify the warranties alleged to have been breached, and which it was suggested had been drafted in order to keep the claimants' options open, was held to be noncompliant with a notice provision. In that case the Court of Appeal approved the observations of Gloster J in *RWE Nukem Ltd v AEA Technology plc* [2005] EWHC 78 (Comm) to the effect that

> "I would expect that a compliant notice would identify the particular warranty that was alleged to have been breached; I would expect that, at least in general terms, the notice would explain why it had been breached, with at least some sort of particularisation of the facts upon which such an allegation was based, and would give at least some sort of indication of what loss had been suffered as a result of the breach of warranty, or, in other words … some sort of description of the "liability for breach of the Warranties" that it was alleged that AEAT had incurred".

196. All of these criteria seem to me to be met by this notice. Further, there is nothing about the notice which seeks to bind the court as to its findings in any way. The Claimants' case is that there was a breach, and damages should be assessed by the court. They put forward a calculation as to the damages which they would seek which was high, but by no means unarguable, and largely employed the methodology which was agreed between the experts at trial. I find that the notice delivered by the Claimants satisfied the requirements of the Agreement.

The Quantum of Damages

197. The next question is as to the measure of damages. Both parties accepted that the provisions of the SPA in this regard were somewhat mysterious. The SPA obliges the damages payer to pay to the Company (rather than the buyer) such amount as may be necessary to put the Company in the position which it would have been had the warranty been correct. The question as to how this might be approached in the event of a breach of a warranty as to prospects is deeply unclear – how would one go about compensating an entity for a lack of prospects? However both of the parties before me proceeded on the basis that the correct approach would be to ascertain the value of the company as it would have been if its prospects had been as mutually expected, to ascertain the value of the company as it was with its prospects impaired, to calculate the difference between the two, and to require that difference to be paid to the Company.

198. I should say that I think that this is the correct approach. Its practical outcome is that if the purchaser has paid 100 for a company, but because of a breach of warranty the company for which he has paid is only worth 80, he is appropriately and fully compensated by a payment of 20 to that company. Provided that he has purchased 100% of the company, it should make no difference to him whether that 20 is paid to him directly, or to the company of which he is the sole owner. If this line of reasoning is reversed, it demonstrates that the payment to the company concerned of the difference between its actual value and its warranted value satisfies the obligation to make the company good.

The approach

199. This is a claim for a breach of a contractual warranty, and damages in contract are intended to place a claimant in the same position as he would have been if the contract had been performed. As applied to share sales, the general rule is that "[t]he measure of loss for breach of warranty in a share sale agreement is the difference between the value of the shares as warranted and the true value of the shares": *Ageas (UK) Ltd v Kwik-Fit (GB) Ltd* [2014] EWHC 2178 (QB) at [14] (Popplewell J) citing the judgment of the Privy Council *Lion Nathan Ltd v C-C Bottlers Ltd* [1996] 1 WLR 1438 at 1441F-H (Lord Hoffmann), which describes this as the "prima facie" approach (by analogy with warranties of quality in sale of goods cases). The valuation exercise is to be carried out at the date of breach: see e.g. *MDW Holdings Ltd v Norvill* [2022] EWCA Civ 883 at [27] (Newey LJ).

200. The determination of "As Warranted" and "Actual" values should be conducted according to the following principles:

i) Valuation involves an assessment of "[t]he estimated amount for which an asset or liability should exchange on the valuation date between a willing buyer and a willing seller in [an] arm's length transaction, after proper marketing where the parties had each acted knowledgeably, prudently and without compulsion" (*The Hut Group Ltd v Nobahar-Cookson* [2014] EWHC 3842 (QB) at [180(2)] per Blair J),

ii) "There is no one methodology to be applied in a valuation". (*Hut Group* at [180(3)])

iii) Models used by valuation experts should be considered as a tool, with the output (and usefulness of the model) to be assessed in the light of all the circumstances and common sense: "you always have to stand back and say, does the answer give you a sensible result and not get too worked up in the model itself". (*Hut Group* [180(4)]).

iv) The valuation methodology actually used by the parties to the transaction is not determinative of how valuation ought to be carried out to determine either the As Warranted or Actual value. However, in principle it can be relied upon as evidence of the As Warranted value: see e.g. *116 Cardomon Ltd v Macalister* [2019] EWHC 1200 (Comm) at [130]-[134] (Cockerill J); or the Actual value (depending on the buyer's knowledge of the alleged breaches): see e.g. *Eurocopy v Teesdale* [1992] BCLC 1067. Further, it might give guidance as to an appropriate approach to assessing the Actual value: in *Senate Electrical*

Wholesalers Ltd v Alcatel Submarine Networks Ltd (1998, CA), Stuart-Smith LJ considered (obiter) that where applying a multiplier to maintainable earnings/profits was "how the original price is calculated, it is the obvious way to calculate damages by applying the same multiplier to the shortfall in maintainable profits/earnings"

v) It is, of course, "for the plaintiff to prove both the fact of the loss and the quantum of damage": see *Senate*. With regard to quantification, where a party fails to make out its case on damages, a Court will sometimes nevertheless do its best on the material available to make an assessment of the appropriate damages (though a claimant "cannot complain if, through opening his mouth too wide, he fails to prosecute a more modest claim and the judge does not deal with the matter as sympathetically as he might otherwise have done").

The Calculation Mechanic to be Applied

201. Very helpfully, the experts agree as to the calculation mechanic which should be applied in order to determine the quantum of damages. They differ as to the amounts to be inserted into the various legs of the calculation, but not as to its structure.

The "As Warranted" valuation

202. Ordinarily the "As Warranted" value in a transaction of this kind can be taken to be the purchase price. However, in this case the purchase price was a floating value dependent on the value of the EBITDA of the Company over the years 2018 and 2019. It is therefore necessary to begin by deciding what the warranted EBITDA should be taken to be.

203. It was suggested to me that the true value to be used for the As Warranted value was the forecast that the Company had put forward in May indicating EBITDA of £1.5m for the year. This was also the sum defined in the Agreement as the "Target EBITDA". However, it is quite clear to me on the facts that the Claimants were not proceeding on the basis of a belief that the outturn would be anything like that figure. Indeed, the Defendants' own case is that they fully informed the Claimants at the meeting on the 1st-2nd August that the mandates on which they were relying to produce that figure might not come through.

204. I am therefore of the view that the figure to be used in calculating the As Warranted value is the figure which I have found reflects the actual expectations that reasonable parties would have had. Another way of putting this is that the figure to be used should be the figure which, if it had been the outturn, would clearly <u>not</u> have constituted any sort of breach of warranty.

205. I found above that this figure was around £1m. On that basis the As Warranted value of the Company – that is, the value if the warranty had been correct – would have been £6.43m; a figure arrived at by simply plugging an estimated £1m EBITDA for 2018 (and 2019) into the pricing formula set out in the Agreement.

The “Actual” valuation

206. The Actual valuation is the valuation which a valuer would have arrived at if, on the Effective Date, he had conducted a valuation of the Company in the knowledge of its true position and prospects. Arriving at this involves four stages. First, the actual projected EBITDA (that is, the EBITDA figure which would have been arrived at if the projections had been correctly made) must be established. Second, a decision must be made as to the way in which such a valuer would have incorporated historic EBITDA figures into his valuation. Third, the adjustments to those historic EBITDA figures which would have been made by such a valuer must be made. Fourth, the resulting EBITDA figure must be multiplied by an appropriate multiplier to arrive at the valuation.

First stage – true estimated EBITDA on the completion date

207. Mr Dearman has attempted to calculate what a reasonable expectation for the performance of the Company would have been for the year 2018 if the true facts relating to the Four Contracts had been taken into account, and he concludes that the answer would have been an expected EBITDA figure of £325,897 (the final figure was in fact £314,219). Mr Thompson, the Defendants' expert, accepts this figure.

208. In cross-examination, Mr Lowe put to Mr Dearman – and he accepted – that he had not included in this figure two items relating to the Four Contracts – specifically work done for TfL in August of £32,700 and work done for Nidec in November and December totalling £15,000. However, his response was that in reaching the £325,897 figure he had incorporated an “adjustment” to catch entries of this kind. His point was that in assessing the likely profits of the Company for the year, it would be absurd to assume that, having suffered the loss and delay of the Four Contracts, the Company would not seek to deploy its resources in other areas. That deployment would produce revenue, and that revenue should be incorporated into the forecast. He had therefore made an upwards adjustment of £209,425 to the turnover forecast on which his EBITDA forecast was based in order to catch precisely this sort of activity. It is true that Mr Dearman characterises this adjustment as catching revenues arising after the Effective Date, whereas the TFL work referenced was apparently done in August 2018. However, this invoice was created on 1 February 2019 in unexplained circumstances, and does not appear to have been foreseen or accrued as at October 2018. I therefore think it belongs, along with the Nidec figures, in Mr Dearman's "adjustment".

209. I think the items identified above are exactly the sort of thing which this adjustment was incorporated into Mr Dearman’s forecast in order to reflect, and that no further adjustment needs to be incorporated into Mr Dearman’s year end revised forecast EBITDA because of them.

Second stage – calculation methodology

210. It is usual in valuing a company to have regard to its recent trading history. However there is no golden rule which tells us how much weight should be attached to historic performance. The experts in this case suggested different approaches. Mr Dearman, the Claimants' expert, suggested that there might be two possible approaches – one being to disregard prior years and use only the expected EBITDA for the immediate year. His basis for suggesting this was that for a valuer the expected performance for the current

year was so radically different from that of previous years that the valuer should disregard those years. He suggested in the alternative that, even if some consideration was to be given to previous years, those results should be weighted rather than simply averaged. He therefore suggested a 1:2:3 weighting, with the figures for 2016 weighted at 1x, the figures for 2017 at 2x and those for 2018 at 3x. Mr Thompson, the Defendants' expert, rejected the idea of looking only at the current year, agreed that the 1:2:3 approach was reasonable, but suggested that an unweighted 1:1:1 approach might be more appropriate, since it provided more historical perspective.

211. I reject both Mr Dearman's idea of using only the current year figures and Mr Thompson's idea of using a 1:1:1 weighting. I do not accept that the Company's position was so radically different in 2018 that it would be appropriate to completely disregard its performance in previous years in valuing it. However, equally I think that applying a simple 1:1:1 approach gives wholly insufficient weight to the significant variation between the current year and the previous years. Consequently, I think the correct approach to adopt is a valuation based on a 1:2:3 valuation. All that is therefore necessary is to identify the adjustments to be made to the EBITDA figures to be plugged into that calculation. It was on this point that the experts disagreed most significantly.

Third stage – adjustments

212. In order to determine what adjustments should be made to EBITDA in this calculation, it is necessary to say a few words about what the adjustments are intended to achieve. EBITDA is intended to be a measure of the revenue generation of an underlying business. The usefulness of this number is entirely forward-looking – identifying the revenue generating ability of the business today is, in theory, the best starting point for estimating its revenue generating ability tomorrow. However, historic financial information – necessarily – includes not only figures relating to the core business but also other costs or revenues arising during the period which are not integral to the core business, and may be one-offs. It is therefore usual, when using historic EBITDA figures to value a business, to create an adjusted, or "maintainable", EBITDA figure, by eliminating such one-off items, whether positive or negative. Also, when the acquisition will result in a specific identifiable change to the way in which the business is conducted, those figures may be adjusted to show the position as it would have been had that change been in place for the historic period concerned.

213. The primary debate between the experts in this area was as regards payments to the Defendants. Prior to the transaction the Defendants received revenue from the Company in the form of bonuses and payments to their personal service companies. The effect of the transaction was that, going forward, the Defendants would receive a salary of £150,000 each and a bonus of £25,000. This raised the question as to whether, in valuing the Company, the "maintainable EBITDA" figure to be used for prior years should reflect the actual EBITDA or the EBITDA figure that would have been arrived at had these payments been removed and replaced with the notional salary to be paid.

214. Mr Dearman says that the EBITDA figures for previous years should not be adjusted to remove the bonuses actually paid (£200,000 and £250,000 respectively). His explanation for adopting this approach was simply that since these bonuses had in fact been paid, they should be included in the actual costs of the Company and therefore reflected in the EBITDA figures for those years. Mr Thompson, by contrast, said that these were exceptional items which should be included in adjustments. His argument

was that since the purpose of an adjusted EBITDA figure is to form a basis of an estimate of how the Company will actually perform in the future, where the bonus structure to be used in the future is known, historic information should be adjusted to present the picture as it would have been had the new arrangements been in place over the historic period.

215. On this point I agree with Mr Thompson. I think that the principle that, where what it is sought to establish is future expected EBITDA, historic data should be adjusted in line with future expected practices is well-established. I also note this this is approach which the parties agreed between themselves at para 1.1.3 of Schedule 9 to the Agreement, so I do not think that the Claimants can argue that it is inappropriate.

216. Mr Thompson calculates that, on this basis, the EBITDA figure that would have been calculated on a 1:2:3 basis adjusted for directors payments would have been £599,000.

217. There is one minor issue here, in that Mr Thompson did not know when he prepared his report that it had been agreed that the Defendants would receive a bonus of up to 25% of salary, and that the common expectation seemed to be that they would receive a bonus of £25,000 each (this is why Mr Bell described the expected total remuneration of the Defendants as being £175,000 each). Consequently his figures need to be adjusted to take this into account for the years 2016 and 2017 (it can safely be assumed that no bonuses would have been paid in 2018 given the drop in EBITDA).

218. This is a merely arithmetical adjustment, which results in the maintainable weighted average EBITDA figure dropping slightly from £599,000 to £573,949.

219. Mr Lowe argued for a further adjustment to this figure, in that the cost of £175,000 incurred in the failed hire of a third managing director (a Mr Raj Thapar) should also be removed from the 2017 figures. However, Mr Dearman disputed this adjustment. As Mr Dearman pointed out in evidence, decisions of this kind are as much a matter of art as of science – on the one hand, this cost could be regarded as an unrepeatable one-off, but on the other it could be regarded as simply part of the normal "churn" of staff which is an integral part of a people business. In my view it is the latter, not the former, and no such adjustment should be made to the 2017 maintainable EBITDA.

Fourth stage – the multiplier

220. Finally, there is the question of the multiplier. Throughout the negotiations in relation to the SPA, a multiple of 6.43 was used by all sides as the appropriate tool for valuing the Company. Mr Dearman, however, in his report, proposes an alternative valuation approach based on a multiple of 4.5. His argument is that 6.43 would be an appropriate level to apply to a public company, but that when valuing a private company it is usual to apply a discount to the comparator figures for public listed companies, and this discount would be at the level of 20-30%. The application of a 30% discount gives a multiplier of 4.5.

221. Regardless of whether this is correct as a matter of corporate finance theory, I do not think that it has any relevance to this case. The Claimants operated throughout on the basis that the correct multiple to be applied to this particular company in this particular situation was 6.43. I do not think it lies in their mouths to challenge that approach to valuation as a means of increasing their damages claim. Even if their position is that no

other buyer would have paid that much for it, and they were paying a substantial premium to true value, the fact is that is what they were paying.

222. The issue here is that the Claimants' entitlement to damages is not an abstract calculation, it is the amount intended to redress the damage to them. The argument that the Company's worth to the Claimants should be assessed by applying a lower multiple flies in the face of the Company's own actions – as set out in paragraph [61] above, when, in the full knowledge of the actual state of the Company, the Claimants sought to settle this matter, they did so on the basis that the Company should be valued using a 6.43x multiple. I think that this demonstrates that this multiple accurately embodies the value of the Company to them.

223. The discount was also justified on the basis that the deteriorating position of the Company in October merited a reduction in the 6.43 multiple which had been arrived at before any notice of the deterioration had been received. I think this is double-counting. Where a consistent multiplier is applied to deteriorating EBITDA, the result is a corresponding reduction in valuation. The idea that a deterioration in EBITDA justifies a reduction in multiple would, I think, only be correct if the reduction were so significant as to suggest a fundamental shift in the whole nature of the business. No such thing happened here, and no such reduction is justified.

Valuation

224. If the adjusted EBITDA figure to be used is £573,949, and the appropriate multiplier is 6.43, the true value of the Company as at the date of completion was £3,690,493.

225. Although it is not directly relevant on the basis of the findings above, there is one other point which I should mention. As noted in paragraph [61] above, the Claimants attempted to settle their disagreement with the Defendants at a very early stage. At that time, in full knowledge of facts which were considerably worse even than those reasonably anticipated at the Effective Date, their proposal implied that the Company was worth £2m. Mr Lowe therefore says that the Claimants cannot legitimately take the view that at the Effective Date, before those facts were known, the value of the Company to them was any less than £2m. I agree with this point.

Damages

226. The prima facie damages flowing from the breach are therefore £6.43m less £3.69m – that is, £2.74m.

227. However, there is an important adjustment which needs to be made to this figure. If the EBITDA figure for the Company had in fact been £1m, the price that the Claimants would have had to pay to acquire 100% of the Company would have been £6.43m, composed of £5.43m in cash and £1m of shares in Decision. The Claimants have to date only paid £5m in cash. Thus, to put them in the position in which they would have been had the contract not been breached, they can claim £2.74m, but must account for £1.43m in unpaid consideration. This gives them a net claim for £1.31m.

228. The Claimants sought to add to their claim the sum of £311,633.50. This was on the basis that Clause 10.3.2 of the SPA provides that, in the event that there is a breach of any Warranty, the Sellers shall pay to the Buyer

> "all costs and expenses (including, without limitation, damages, legal and other professional fees and costs, penalties, expenses and consequential losses whether arising directly or indirectly) reasonably incurred by the Buyer, the Company as a result of such breach, or of the Warranty being untrue, inaccurate or misleading".

229. This claim was not pursued with any vigour at trial, and the only evidence that I was provided with in respect of it is a schedule of hours spent by Mr Bell dealing with solicitors. The schedule was unaccompanied by any indication of how this time might be valued, or what the justification of any such valuation might be. Mr Bell also referred in his witness statement to travel costs incurred in 2019, but I have no way of knowing what these costs relate to, or the extent to which they relate directly to the breach of warranty.

230. Given the lack of evidence on this issue, I am therefore unable to order any payment to be made in respect of this claim.

231. I therefore give judgement in favour of the Claimants for £1.31m.

232. For the reasons given above, I would address the issues identified for trial as follows.

Warranty 19.1.2 ("Since the Accounts Date .... there has been no material adverse change in the turnover, financial position or prospects of the Company".)

Issue 1 – Did the word "prospects" in Warranty 19.1.2 of the Agreement refer to the future financial performance (or forecasts) of the Company?

Yes

Issue 2 – As at the First Completion Date (viz. 12 October 2018), since the Accounts Date (viz. 31 December 2017) had there been a material adverse change in the turnover of the Company on the basis that the revenue for the full FY2018 based on annualising performance for January to May 2018 in the FY2018 forecast P&L was c.£4,377,071 which was less than FY2015 to FY2017?

No

Issue 3 - As at the First Completion Date (viz 12 October 2018), since the Accounts Date (viz 31 December 2017) had there been a material adverse change in the turnover and/or prospects of the Company on the basis that the turnover and/or prospects of the Four Projects was not properly reflected in the FY2018 Forecast P&L, the May 2018 Sales Pipeline or the July 2018 Sale Pipeline, as alleged?

No as regards turnover; yes as regards prospects.

Warranty 20 ("All financial and other records of the company ("Records") .... do not contain any material inaccuracies or discrepancies")

Issue 4 – For the purposes of Warranty 20, did the term "Records" include the FY2018 forecast P&L (and, insofar as alleged, the May 2018 Sales Pipeline or the July 2018 Sales Pipeline)?

No

Issue 5 – Did the FY2018 Forecast P&L (and, insofar as alleged, the May 2018 Sales Pipeline or the July 2018 Sales Pipeline) contain material inaccuracies or discrepancies as regards the Four Projects (or any of them) as alleged?

No

Issue 6 – For the purposes of Warranty 20 did the term "Records" include the July 2018 Invoice Schedule and the August 2018 Invoice Schedule ("the Invoice Schedules")?

No

Issue 7 – Did the Invoice Schedules contain material inaccuracies or discrepancies as alleged?

No

DEFENCES

Issue 8 – Did C1 have actual knowledge at the date of the Agreement of any of the alleged facts, matters and circumstances constituting breaches of warranty, and if so what was its knowledge?

No

Issue 9 – If the answer to Issue 8 is yes, then to the extent that C1 had actual knowledge, is this a defence to any part of the claim for breach of warranty?

N/A

Issue 10 – If the answer to Issue 8 is yes, then to the extent that C1 had actual knowledge, is this a breach of the Warranty in clause 10.7 of the Agreement, such that the Defendants are entitled to rely upon that breach as a set off?

N/A

Issue 11 – Did the Claimants fail to give adequate notice of their claims under clause 11.4 of the Agreement?

No

ASSIGNMENT

Issue 12 – Has C1 assigned all its rights, title, interest and benefit in and to the Agreement to C2, including its rights to bring this claim.

Yes

QUANTUM

Issue 13 – To the extent (if at all) that breaches of warranty on the part of the Defendants are established, then what is the quantum of the claim for such breaches (including in the light of any defence relating to knowledge)?

£1.31m