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2024 Half-year in review M&A legal and market developments

In this issue…

Authors: Philip Broke, Savi Hebbur, David Lewis, Tom Matthews, Guy Potel, Allan Taylor, Sonica Tolani, Alex Woodfield, Di Yu, Veronica Carson, Darius Lewington, Peter Wilson

We set out below a number of interesting English court decisions and market developments which have taken place and their impact on M&A transactions. This review looks at these developments and gives practical guidance on their implications. Summaries feature below, and you can click where indicated to access more detailed analysis.

Contractual provisions

A number of cases have looked at common contractual provisions in M&A deals.

Novation of SHA by conduct despite "no dealings" clause

The High Court decided on the facts that a clause in a shareholders' agreement (SHA) prohibiting a party from assigning or dealing in any way with its rights or obligations under the SHA without the other party's prior written consent did not prevent a novation by conduct of the SHA from an outgoing to an incoming shareholder.

The shareholders in company C were individual D (who was also a director) and trustee company N, holding 50% each. Trustees (T) of a separate family discretionary trust alleged that N had validly transferred to them its shares in C and its rights and obligations under the related SHA. This had been organised by the settlor of their family trust (S), who was also D's co-director of C. Clause 18.1 of the SHA stated that a party may not *"assign or grant any Encumbrance over or sub-contract or deal in any way with any of its rights or obligations"* under the SHA without the prior written consent of all parties. Clause 13.1(a) further provided that the SHA would terminate when one party ceased to hold any shares. The SHA also contained no oral variation or waiver provisions. It was alleged that D had orally consented to these arrangements, following which N had purportedly transferred it rights and obligations under the SHA under a so-called deed of "assignment". D argued the transfer was void because S had obtained his consent by fraudulently misrepresenting that it was a permitted transfer under the SHA on the basis the trust behind N was another family trust of S. D also alleged that the SHA had terminated under clause 13 for one party ceasing to hold shares. The High Court found in T's favour that the share transfer was valid, an effective novation by conduct had occurred and T could enforce the SHA. The court decided that S had not made any fraudulent misrepresentations, noting that, as it happened, it was relatives of S that stood to benefit under both trusts. D had consented to the transfer by signing the new share certificates and acquiescing in T's registration as shareholder. The test for whether a novation had occurred was an objective one and would only be inferred from conduct if that was necessary to give business efficacy to what the parties had done. The court would be more cautious in finding a novation by conduct where the primary contract contained a prohibition on dealings without consent as well as no oral variation or waiver clauses. However, it was key here that novation involves terminating and replacing a contract by substituting a new contract in place of an existing one. Under it a new party assumes rights and obligations equivalent to those of the original contracting party that it replaces. By contrast, assignment is merely the transfer of contractual rights from one party to another. The court held that a novation must have been the effect of what the parties had agreed when discussing that T would step into N's shoes regarding the SHA if its shares were transferred. Their conduct over subsequent years supported that. Even though they had labelled the transfer a deed of "assignment" you had to characterise it as novation to give business efficacy to it. The prohibition on dealings in clause 18.1 did not apply because the words *"or deal in any way with any of its rights or obligations"* in it followed the references to prohibition on assignment and granting any encumbrance, which pointed to a bilateral disposition of rights rather than the tripartite termination and substitution of a new contract that had happened. In any event, the effect of the parties' conduct was that D was estopped from requiring consent or had waived his right to rely on that or on termination under clause 13.1(a). (*Magee and Ors v Crocker and Anor* [2024] EWHC 1723 (Ch))

Key lessons

- **Another example of the court finding an effective novation by conduct:** This is another example of the court finding an effective novation by conduct, as in *Musst Holdings Ltd v Astra Asset Management UK Ltd* [1]. Interestingly, the Court of Appeal in *Musst* had stated it was arguable that a prohibition on dealings could in principle catch an informal novation. However, the High Court here decided that was not the effect in this case, distinguishing *Musst* because: (i) the counterparty there had waived (in writing) the requirement for prior consent and instead consented after the dealing occurred; (ii) the novation there was only of some obligations under the contract.
- **Broaden express contractual prohibitions on dealings:** As a drafting matter, consider extending prohibitions on dealings expressly to prohibit any form of novation, including oral or by conduct. However, depending on the facts, as with "no oral variation" clauses, a novation taken to have been agreed to orally or by conduct may nonetheless still give rise to an estoppel against the party seeking to rely on the requirement for writing and consequently be upheld in any event.

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Effect of repudiatory breach on termination rights under SHA

The High Court decided that a compulsory transfer notice was not deemed served under an SHA for the buyout at issue price of the shares of a party which was in repudiatory breach of the SHA, and that the breaches had been remedied now anyway, although curing a repudiatory breach could not deprive the innocent party of the right to elect whether to affirm or terminate the contract under the general law.

Company H owned a hospital at which claimant C was a senior consultant and heavily involved in management. Under the SHA in relation to H, defendant D had originally subscribed for 51% of the A shares in H and C was to take 49% of them. In practice, C had only subscribed and paid for one share. After disputes arose, D admitted various repudiatory breaches of the SHA, including: (i) wrongfully registering itself as owner of the A shares to which C was entitled; (ii) breaching statutory pre-emption rules by allotting to itself 2,000 B shares without offering a proportionate entitlement to C; and (iii) wrongfully purporting to terminate the SHA by letter dated 28 August 2020 allegedly on the basis of an incorrect recital in the SHA that C held 1,652 A shares. It was also alleged that D had wrongfully failed to recognise C's appointment of individual S as his nominated director in accordance with C's nomination rights under the SHA. C alleged that D's breaches had triggered a compulsory transfer provision in the SHA entitling him to buy out D's shares at the lower of issue price and fair value.

Key lessons

- **Repudiatory breach:** Interesting guidance on the interaction between repudiatory breach under the general law and repudiatory breach triggering a contractual compulsory buyout event on a material or persistent breach of an SHA.
- **Express duties of good faith:** The comments on express duties of trust and confidence are another reminder that inclusion of an express generic duty of good faith can raise the bar on compliance with other provisions in an agreement.

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1 [2023] EWCA Civ 128.

This stated that a transfer notice was deemed served if a shareholder committed a material or persistent breach of the SHA which, if capable of remedy, was not remedied within ten business days of the board serving notice to remedy the breach (with shareholder consent). D argued that the compulsory transfer provision had not been triggered because its breaches were capable of remedy and the board had failed to issue a notice to remedy the breach. Whilst C's consent was needed for the board to issue the notice, C had no means under the SHA to compel it to do so. By contrast, C argued that repudiatory breaches were by their nature irremediable for all purposes and that no remediation notice was needed because any repudiatory breach was therefore irremediable for the purpose of this compulsory transfer clause. The High Court decided that all four breaches were repudiatory but rejected C's assertions that repudiatory breaches were by their nature irremediable for the purpose of the clause and that the board did not need to serve the notice. A remediation notice was a necessary step for the deemed transfer process, taking into account the severe impact of compulsory transfer on share valuation. The effect was that the contractual compulsory transfer clause had not been triggered. On the facts, all four breaches had now been remedied anyway. Having said that, a party's attempt to remedy a repudiatory breach could still not deprive the innocent party of their right under the general law to elect whether to affirm or terminate the contract. D's own purported termination could not deprive C of that right. However: there had been no valid compulsory transfer event; C had not accepted D's alleged termination; and the SHA remained in force. The court also discussed the meaning of "material or persistent breach". "Persistent" meant not just a breach that was continuing, but could also catch a breach that the wrongdoer did not desist from at the earliest opportunity. By contrast, materiality went to the seriousness of the breach. The court said the analysis might have been different if the SHA had contained an express duty of trust and confidence. In such cases deliberate and cynical conduct can itself form a breach and a pattern of such breaches may render that breach irremediable, even if a single instance does not. Permission has been granted to appeal the decision. (*Dr Rohit Kulkarni v Gwent Holdings Limited and Anor* [2024] EWHC 1357 (Ch))

Penalty implications of default rate clause considered

The Court of Appeal decided that the High Court had incorrectly applied the test for determining whether a sum payable on a contractual breach amounted to an unenforceable penalty under English law. It discussed the correct test, which focuses on whether or not the amount is proportionate for the purpose of protecting a legitimate interest.

Lender L had agreed to loan £1.881 million to company C in July 2020. Under the facility letter interest was payable at 1% per month with a default rate of 4% per month, and interest being compounded monthly in each case. The facility was secured by a debenture over C's assets, as well as personal guarantees from C's husband and wife directors, and mortgages over their family home (the Property) and five buy-to-let properties which they owned. In September 2020 L alleged that a non-occupation covenant in the facility letter had been breached through residential occupation of the Property. It claimed default interest on the outstanding sum until such time as the breach was remedied. The occupation breach continued and the sums demanded were not paid. In November 2020 L demanded immediate repayment of the full amount of the loan plus interest at the default rate, and appointed joint receivers in respect of the properties. The High Court had held that the default interest rate of 4% was

Key lessons

- **Old "commercial justification" test no longer applies:** Prior to the Supreme Court decision in *Cavendish Square* a trend had developed in some cases of considering whether a clause was commercially justifiable in the circumstances of the transaction when determining whether its primary purpose was to deter a breach. The *Houssein* case is helpful in demonstrating that the former commercial justification test no longer applies and that in *Cavendish Square* the Supreme Court set what is arguably a higher bar for what amounts to an unenforceable penalty of whether the clause is penal by virtue of being extravagant, exorbitant or unconscionable.
- **Three-stage test for whether a provision amounts to a penalty:** The *Houssein* case is also helpful in highlighting, in line with other case law[2], a three-stage test for determining whether a sum is a penalty when applying *Cavendish Square*, being whether it is: a secondary obligation engaged on breach of a primary contractual obligation; protecting a legitimate interest; and nonetheless extravagant, exorbitant or unconscionable.

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2 *Vivienne Westwood Ltd v Conduit Street Development Ltd* [2017] EWHC 350 (Ch).

an unenforceable penalty on the basis that it did not protect a legitimate interest of L. The Court of Appeal decided that the High Court judge had failed to apply the correct test for what amounts to an unenforceable penalty because he had not applied the test set by the Supreme Court in *Cavendish Square v Talal El Makdessi; ParkingEye Limited v Beavis*[3]. It remitted the case back to the judge at first instance to apply the correct test. The initial consideration should be whether the provision is a secondary obligation which imposes a detriment on the contract-breaker on breach of a primary contractual obligation. You had to then consider whether any (and if so what) legitimate business interest is served and protected by the clause and then, assuming there is one, whether the provision is nonetheless extravagant, exorbitant or unconscionable. The trial judge had not approached the issue of protectable legitimate interest correctly and had wrongly concluded that there was none here. First, he had failed to take into account past case law that there is a good commercial justification for charging a higher rate of interest on a loan after default in repayment because a person in default is a greater credit risk[4] . Second, he had incorrectly decided that L was not subjectively seeking to protect an enhanced credit risk on the basis there was one flat default rate (not limited to payment breaches) and that the only purpose of the "no residency" covenant had been to structure the loan to qualify as regulated under the Financial Services and Markets Act 2000. The Court of Appeal stated that the judge appeared to be looking for a justification for the default rate rather than considering whether it was extravagant, exorbitant or unconscionable. Whether a clause is penal depends on its purpose determined as a matter of construction, which does not depend on evidence of subjective intention. Occupation of the property was a breach of the no-residency covenant which entitled L to call in the loan and demand repayment at the higher rate of interest. L had a legitimate interest in principle in enforcing the primary obligation to effect such repayment, and the higher interest rate protected the increased credit risk from this. (*Houssein & Ors v London Credit Ltd & Ors* [2024] EWCA Civ 721)

Valuation of leaver shares under articles of association

The High Court considered the effect of leaver provisions in a company's articles of association. It decided that a deemed transfer notice had been served for the transfer of a member's shares when he retired from his position as a director of the company, but not on an earlier date when he had been dismissed as an employee of a different group company. This meant that the member was entitled to be paid a higher "fair value" for his shares, rather than lower "market value".

C was the holding company of SP Limited, which was an engineering company. Mr T held 24% of the shares in C, with the remainder held by another company (SC). SC was controlled by Mr R, who was T's co-director of C. T was both an employee and director of SP and was also a director of C. T was dismissed as an employee of SP in October 2022 and brought proceedings before the Employment Tribunal in respect of that dismissal. The following month he was also removed as director of SP. T subsequently resigned as a director of C in May 2023 when he retired at the age of 65. Article 11.3 of C's articles of association provided that: *"If any Employee Member shall cease for any reason… to be employed as an employee, director or consultant of a Group Company (and does not continue in that capacity in relation to any Group Company), then a Transfer Notice shall be deemed to have been served … on the date of such cessation",* whereupon they would be obliged to offer their shares for sale to the other shareholder(s). The transfer price would

Key lessons

- **Clear and express drafting needed:** Clear and express drafting is required for leaver provisions in articles over how compulsory transfer provisions operate where a dismissed employee has, or over whether or not they should continue to have, continuing roles with other companies in the same group.
- **Interpretation of articles of association:** The court will interpret the articles in the round, taking into account reasonably ascertainable surrounding circumstances when they were adopted, such as public filings at Companies House. It was a relevant factor that the leaver provisions were aimed at T alone, to the exclusion of R, and consequently the court decided that they should not be interpreted to impose a lower transfer price where T was a continuing director in the group.
- **High test for implication of terms:** The judgment demonstrates the high test under English law for implication of contractual terms, where the court commented that it would not imply a term that the original dismissal had to be lawful because the reference in the article to ceasing to be employed "*for any reason*" suggested that the lawfulness of the reason was not relevant.

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3 [2015] UKSC 67.
4 *Cargill International Trading PTE Ltd v Uttam Galva Steels Ltd* [2019] EWHC 476 (Comm).

be *"market value"* (which applied a minority discount) with limited exceptions. One of these was where a transfer notice was deemed served on an employee member's *"retirement at 65 years of age"*, when the transfer price would instead be *"fair value"* (which would be higher because it valued shares on a proportionate basis). R was expressly excluded from the definition of *"Employee Member"*, with the effect that these deemed transfer provisions only applied to T. The question was whether T was entitled to fair or market value for his shares. This hinged on whether article 11.3 had been engaged in October 2022 or May 2023. The High Court decided that T was not deemed to have served a transfer notice until he retired in May 2023, meaning that he was entitled to receive fair value for his shares. It decided that the word "employed" in article 11.3 caught being engaged as a director or consultant and was not used in the strict sense of being an employee under a contract of employment. Significantly, the reference to not continuing "in that capacity" related back to all three capacities, not only the particular capacity that the Employee Member previously held. This was the more natural meaning of the wording and made commercial common sense. The purpose of article 11.3 was to set a way to buy out a shareholder who had stopped contributing to the day-to-day running of the business. However if, say, a senior employee retired from full-time employment while staying on as a consultant it was not commercial good sense for them to have to sell their shares at the lower price. Any other interpretation would mean someone could be dismissed for no good reason in order to trigger a forced sale of their shares at the lower valuation. It was significant that R was expressly excluded from the scope of article 11.3, which in practice applied solely to T. This exposed T to the risk of a forced sale of his shares at the lower price if he was dismissed from a company controlled by R while remaining a director of C. You should interpret article 11.3 to protect T from this. Permission has been granted to appeal the decision. (*Syspal Capital Ltd v Truman & Anor* [2024] EWHC 1561 (Ch))

No interim injunction where restrictive covenants in investment agreement void and unenforceable

The High Court declined to grant an interim injunction to give effect to restrictive covenants in an investment agreement to prohibit a former director, employee and shareholder from competing with the business of the company and all other subsidiaries in the buyer's group. The common law rules on restraint of trade applied and the restrictive covenants were void and unenforceable under them because they were too wide in scope and too long in duration.

Defendant W was a doctor who had acquired company C with her business partner in 2014. W had run and developed C into providing certain medical healthcare services in England, focused in Norfolk and Suffolk. In 2018 claimant investment company L acquired W's 25% shareholding in C for a purchase price payable partly in cash but mainly by way of loan note. Three years later W resigned from C and all other directorships connected with L and the parties renegotiated the sale of her shares. Under restrictive covenants in the new investment agreement (IA), W was prohibited from competing not just with C's business but also with the businesses of all of L's subsidiaries in the UK and Channel Islands within: (i) 12 months of ceasing to be director or employee of a company in C's group; and (ii) the period commencing when she became a loan note holder and ending 12 months after the loan was fully repaid (which potentially could amount to ten years). W and her business partner subsequently formed a new company which started offering comparable medical care services in Wales in 2024.

Key lessons

- **Restraint of trade law:** The case demonstrates that, to be enforceable under English law, restrictive covenants must not be in restraint of trade, meaning that they must be reasonable and go no further than is necessary to protect the legitimate business interests of the party seeking to rely on them.
- **Scope of restrictive covenants:** In assessing the reasonableness or otherwise of the geographical extent and business scope of restrictive covenants the court will take into account the geographies in which the subject business operates and the services and operations it covers. With this in mind, in a joint venture or other ongoing or long-term relationship it can be prudent to include an acknowledgement in the agreement between the parties that the company's business may develop over time.

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L alleged that this breached the second limb of the restrictive covenants, which would have entitled it to cease paying W £500,000 a year in interest on the loan. Exceptionally, the High Court decided at interlocutory stage here that the restrictive covenants were clearly void and unenforceable and that there was no arguable case otherwise. The rules on restraint of trade clearly applied, given that the covenants arose from W's expertise in starting and developing the relevant healthcare business. That is what L had acquired. The ten-year duration was far longer than was allowed in a business sale context. The nationwide geographical scope was also unjustified and unnecessary. The scope of businesses covered by the covenants was also far too wide. The core of L's legitimate protectable interest was C's business. It did not extend to L's other subsidiaries as W had no expertise in their fields, their businesses were wholly unrelated to C's and they did not need to be protected. For a restraint of trade to be reasonable it had to be no more than was reasonably required by the party in whose favour it was imposed to protect their legitimate interests. The onus of establishing that was on the person seeking to rely on it. When determining what is reasonable, the court will consider, among other things, whether a narrower covenant would have sufficed. The High Court decided that the covenants here could not be severed in any simple and clean way and were therefore wholly unenforceable. (*Literacy Capital Plc v Webb* [2024] EWHC 2026 (KB))

Implied terms on discontinuance of Libor

In a test case under the Financial Markets Test Case Scheme, the High Court considered the effect of the discontinuance of London interbank offered rate (Libor) on perpetual preference shares whose terms of issue provided for dividends to be paid by reference to "Three Month LIBOR". It decided to imply a term to allow dividends to be paid using a "reasonable alternative rate".

International bank SC had issued US$750 million preference shares in 2006 in accordance with its articles of association to raise what at the time was classified as Tier 1 capital. The preference shares were perpetual, having no maturity date, and broadly were redeemable at ten-year intervals. Dividends were payable on the preference shares at the discretion of the board at a floating rate of 1.51% plus Three Month Libor. Three Month Libor was defined by reference to the Three Month London interbank offered rate for deposits in US dollars. As well as containing a primary means of ascertaining Libor, the definition set out three alternatives where that could not be operated. For some time after the end of December 2021, when banks were no longer compelled to submit rates to enable Libor to be calculated, synthetic US$ Libor was published. However, this ceased at the end of September 2024. The effect was that the primary and alternative definitions of Three Month Libor could not be operated. The High Court decided to imply a term to allow dividends to be paid using a "reasonable alternative rate". Noting that this was a very long-term contract, the High Court stated that a flexible approach was most appropriate and would best match the reasonable expectation of the parties. The role of Libor essentially had been to provide a measure to link the amount of the dividend to the changing costs of borrowing over time and, accordingly, the court would imply a reasonable term to allow the contract to be carried out when the dividend falls to be calculated. Relevant factors were: the use of the fallback alternatives for ascertaining Libor, which suggested that discontinuance of Libor should not affect continued performance; the original driver to raise Tier 1 capital, which demonstrated the importance that the dividend calculation continue to operate; and this approach reflected that the alternative reference rates might change with time over the life of the preference shares. At the current time the court found that the reasonable alternative rate was the term Secured Overnight Financing Rate (SOFR) published by Chicago Mercantile Exchange Group Benchmark Administration (CME term SOFR) plus the spread adjustment recommended by the International Swaps and Derivatives Association. (*Standard Chartered plc v Guarantee Nominees Ltd & Ors* [2024] EWHC 2605 (Comm))

Key lessons

- **Guidance on contractual interpretation and implication of terms:** Interesting guidance on contractual interpretation and the analysis for implying a term requiring the use of a reasonable alternative rate where an index used to measure payments under a contract ceases to be published. This is based on the premise that, without implying a term into the contract "to fill the gap", the contract would lack business efficacy.
- **Alternative of automatic redemption:** The High Court noted that the only suggested alternative to such an implied term here, involving automatic redemption of the preference shares (albeit with fallbacks if redemption could not be carried out lawfully at the relevant time), was untenable as it was not necessary to give business efficacy to the contract and was inconsistent with the express terms of the contract and the mandatory requirements for Tier 1 capital. The arguments against an implied term for automatic redemption would be similarly persuasive in the case of debt instruments, where it would operate without statutory limitations controlling the redemption of share capital.

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Expert determination clause could be separable from underlying agreement

The High Court stayed proceedings arising from the purported termination of a contract for the sale of land to enable the parties to comply with an expert determination provision in the contract, raising interesting issues on the interaction between the expert determination clause and the jurisdiction clause in the contract.

The first defendant (D1) agreed to sell land to claimant C and the second defendant was named as contractor in the contract. Clause 8 of the contract allowed C to terminate the contract if certain conditions were not met. Whilst clause 28 provided that any dispute under the contract would be submitted for expert determination (ED), clause 31 gave the courts of England and Wales exclusive jurisdiction to settle any dispute arising out of the contract or its subject matter or formation. C brought court proceedings over whether it had validly terminated the contract by written notice under clause 8 and could recoup its deposit. The defendants challenged the court's jurisdiction, arguing that the dispute should have been referred to mandatory ED. They argued that the principle of separability, which applies to arbitration agreements, also applies to ED clauses, with the effect that the ED clause was separable from the contract and continued after the contract was terminated. The High Court decided that the ED clause was separable from the underlying contract after the contract came to an end in the same way as an arbitration clause where, as here, the parties had not agreed otherwise. The court granted the defendants' application for a stay of proceedings so that the matter could be referred to ED. The court noted the wide language in clause 28 that *"any dispute"* under the contract would be submitted to ED. The natural reading was that it was an all-embracing provision. It was irrelevant that ED clauses are usually narrower and used for specific identified specialist matters. The parties were business people operating in property development. They were objectively taken to know that the scope of the clause was apt to cover all disputes arising in relation to the agreement, like an arbitration clause. It was significant that the ED clause was not carved out of the jurisdiction clause, which suggested an all-embracing "one-stop" construction of the clause. It was also relevant the ED clause came before the jurisdiction clause in the contract, which did not position the latter as the primary dispute resolution provision. The jurisdiction clause still had purpose under the contract, for example, for enforcing an ED if a party failed to comply or in the agreed circumstances where the ED was not binding (being manifest error or fraud). Here, however, where the parties had created a "one-stop shop" in the form of the ED clause, there was a presumption of separability as with arbitration clauses. It depended on the parties' objective intentions and the burden of proving otherwise was on the party arguing against separability. That had not been met here. (*Dandara South East Ltd v Medway Preservation Ltd and Anor* [2024] EWHC 2318 (Ch))

Key lessons

- **Expert determination clauses on M&A transactions:** On M&A transactions standard practice is to restrict expert determination provisions to specific identified specialist matters under the agreement. Those particular provisions should be expressly carved out from the general disputes resolution clauses, to ensure that the two sets of clauses do not conflict.
- **One stop shop for separability:** The judgment demonstrates that an expert determination clause may be separable where the agreement fails to carve out from the jurisdiction clause specific matters to be determined by expert determination. Prior to this case there was no authority on separability in the context of expert determination clauses.

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Party could not rely on failed condition precedent caused by its own breach

The Court of Appeal decided that buyers could not rely on their own non-fulfilment of a condition precedent (CP) to their contractual obligation to pay a deposit. The sellers of three ships successfully appealed against the earlier High Court decision that they had no claim in debt in respect of the buyers' failure to pay the deposit even where the buyers had caused the CP to fail by their own breach.

The dispute arose in relation to deposits payable under three memoranda of agreement (MOA) for the sale of three ships. Under clause 2 buyers B had to provide an escrow holder without delay with various documents so that it could open an escrow account. B was also required to pay a 10% non-refundable, forfeitable deposit into that account within three days of the MOAs being signed and the escrow holder confirming that the account was fully open. Under clause 13 sellers S could cancel the MOAs if the deposit was not paid and claim compensation. After the MOAs were signed B failed to provide the designated documents to the escrow holder. This meant the escrow account could not be opened nor the deposits paid. S served notice to terminate under clause 13 and claimed aggregate deposits totalling US$4.94 million as a debt. The issue was whether, where the accrual of a party's obligation to pay a debt is subject to a condition precedent (CP) which that party wrongly prevents from being fulfilled, you can treat the condition as dispensed with so that the debt still accrues. Overturning the High Court decision, the Court of Appeal decided that, under English law, a party could not renege on its obligation to pay a debt by relying on the failure of a CP to that debt obligation caused by its own breach of contract. B had contractually agreed to pay forfeitable deposits irrespective of any damages claim or loss quantified by reference to market movement.

Key lessons

- **Presumption that a person may not take advantage of their own wrong:** The judgment highlights the English law presumption that parties do not intend to allow a party to benefit from their own breach of contract.
- **Deposits on M&A transactions:** The issue in this case would be less likely to arise in an M&A context, where deposits are relatively rare outside particular industry contexts. In the rare circumstances that deposits are payable on M&A transactions, this is more commonly on signing the sale and purchase agreement (SPA) and likely the SPA would be terminable for material beach if the funds were not transferred. The obligation to pay would be more in the nature of a CP to the SPA coming into force in the first place.

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This reflected the general position that a person should not be allowed to take advantage of their own wrong. For this principle to apply you need an agreement: giving rise to a debt rather than damages; that the debt will accrue or be payable subject to satisfaction of a CP; and (crucially), express or implied, that the party obliged to pay the debt will not act in a way to prevent the CP being satisfied so as to prevent the debt accruing or becoming payable. This was a principle which gave effect to the parties' contractual intention, not one which frustrated it. The parties were free to contract out of it. Here, a remedy in non-compensatory debt, rather than compensatory damages, reflected the loss of bargain. Permission has been granted to appeal the decision. (*King Crude Carriers SA and Ors v Ridgebury November LLC and Ors* [2024] EWCA Civ 719)

Monetary cap limiting liability imposed single cap applying to all claims and not multiple separate caps

The High Court decided that a monetary cap on liability under a digital transformation contract operated as a single aggregate cap on liability applying to all claims and not as multiple separate caps.

Claimant C entered into a contract with non-departmental public body D to take over D's manually intensive processes and build a new system to digitise its processes (the R software). There were huge project delays, contract milestones were adjusted and D removed part of the intended

Key lesson

- **Clear and consistent drafting needed:** The judgment demonstrates that clear and consistent drafting is needed in relation to limitation clauses imposing monetary caps on liability to ensure that there is no ambiguity in the drafting and that the interaction between different limbs of cap on liability under an agreement, or alternatives within a clause imposing a liability cap, are expressly articulated.

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project from the scope of the contract. Among other disputes, each party brought a financial claim against the other arising out of the delays and D also alleged quality defects in the R software. The limitation on C's liability in clause 52.2 of the agreement capped C's liability as contractor for different types of claim under clause 52.2.6, stating that its *"aggregate liability": "in respect of all other claims, losses or damages, shall in no event exceed £10,000,000 (subject to indexation) or, if greater, an amount equivalent to 100% of the Charges paid under this Agreement during the 12 month period immediately preceding the date of the event giving rise to the claim under consideration less in all circumstances any amounts previously paid (as at the date of satisfaction of such liability) by the Contractor to [D] in satisfaction of any liability under this Agreement"*. Clause 52.4 also excluded liability of either party for loss of profits, turnover, business opportunities or damage to goodwill (whether direct or indirect). One issue was whether the limitation clause created a total aggregate cap on liability of £10 million for all claims covered by the clause or multiple separate caps of that amount for each claim. The High Court decided that it created one total aggregate liability cap. It was significant that the words the *"aggregate liability… in respect of all other claims, losses or damages shall in no event exceed"* clearly indicated that the clause delineated C's total liability, however many claims, losses or damages might exist. It was notable that the simple words *"per claim"* were absent and the expression *"all… claims"* was present. Although the words the *"claim under consideration"* within the alternative charges-based cap which would apply if greater than £10 million suggested that more than one claim could occur, the clause then netted off sums previously paid. That indicated that the parties did not intend the calculated capped sums to be additive where the alternative applied. A later claim under the charges-based alternative might give rise to a greater overall cap than that previously calculated by reference to an earlier claim. If so, it was that later claim which should be the reference point for calculating the cap, meaning that the alternative cap would be the charges in the 12 months before any claim was brought giving rise to the greatest cap. Separately, C had claimed for loss of revenue, arguing that anticipated cost savings never materialised due to delays by D. This related to costs per transaction that C was incurring for processing D's transactions, which should have reduced over time but allegedly had not due to project delays. The High Court rejected this and found in D's favour on this aspect, on the basis this claim was in fact a disguised claim for loss of profits by another name and, as such, was excluded by clause 52.4. Permission has been granted to appeal the decision. (*Tata Consultancy Services Ltd v Disclosure and Barring Service* [2024] EWHC 1185 (TCC))

Company law

There have been particular cases of interest on a number of company law issues.

Personal claim of shareholder where directors allot shares for an improper purpose

The Privy Council decided that in principle a shareholder could have a personal claim against the company if the company's directors allotted shares for an improper purpose and the share allotment had the effect of altering the balance of voting power between shareholders within the company and the relative economic stakes they held in it.

Company C was a Cayman Islands exempted company that was registered in Hong Kong and whose shares were traded on the Hong Kong Stock Exchange (HKSE). C had operating subsidiaries in Hong Kong and China and the group's principal business was supply of cement and related construction products in China. C's principal shareholders included: BVI claimant company T (with a 28.16% shareholding); Taiwanese company ACC (with a 26.72% shareholding); Chinese company CNBM (with a 16.67 % shareholding); and Hong Kong company CSI (with a 25.09% shareholding). Each of C, T, ACC and CNBM competed in the cement production industry in China. C's shares were suspended from trading on the HKSE from April 2015. On 23 October 2017 the HKSE gave notice that C would be delisted unless by 31 October 2018, among other things, C restored its public float above the 25% minimum threshold required by a rule of the HKSE Main Board Listing Rules. In May 2018 C passed a resolution, at a general meeting requisitioned by votes of ACC, CNBM and CSI, to reconstitute its board of directors to comprise one director of each of CNBM and ACC and three independent non-executive directors. C subsequently issued two tranches of convertible bonds in August and September 2018, for a total value of over US$530 million. C then accelerated conversion of US$456.6 million in principal amount of the bond issues into shares at a reduced price. It passed a resolution mandating the directors to allot 1,067,830,759 shares, partly to bondholders in exchange for some of the bonds and partly representing shares relating to bonds held by persons who had not already agreed to the share conversion. Once issued on 30 October 2018, the new shares restored C's public float to 25% and trading in C's shares on the HKSE resumed the following day. C alleged the proceeds of the bond issues were used primarily to repay

US$500 million loan notes that were repaid in November 2018. T alleged that the bondholders were connected with ACC and CNBM by an undisclosed agreement or concert party to take over control of C and that the share issue was an improper exercise of the board's power to allot and issue securities, concluded in secret and not arms' length transactions. It alleged that the purpose had been to allow ACC and CNBM to control C and dilute T's holding to below 25% so that T could no longer block special resolutions. T sought declarations that the bond issue and conversion and the share issue were invalid.

The Privy Council allowed T's appeal and decided that, on the assumed facts, T's claim should not have been struck out by the Court of Appeal of the Cayman Islands for lack of a personal right to bring a claim. As in the lower courts, the Privy Council decided this strike-out appeal on the basis that the assumed, pleaded facts were true whilst acknowledging that they might not be established at trial. The Privy Council held that, if the assumed facts proved to be true, this was a strong case for a personal shareholder's action notwithstanding that the claim involved allegations of breaches of fiduciary duties by the reconstituted board that were owed to C rather than individual shareholders. Key factors were that: the disputed share issue allegedly was allotted to outsiders acting in concert with the majority and the directors to consolidate control over C; the allotment was ratified by the same majority in general meeting; and dilution of T's shareholding deprived T of negative control of C and interfered with T's rights as shareholder to have a say in the collective control of C's affairs. It was critical to finding a personal shareholder right here that a shareholding of 25% or more such as T's conferred negative control and was consequently highly sensitive to dilution, because dilution here could critically affect the balance of power between shareholders. It did not matter whether the claimant was a minority shareholder nor whether the breach could in theory be ratified in general meeting (noting that a majority may not do so by way of oppression of a dissenting minority). The analysis did not affect the power of directors to effect a share allotment for proper purposes (such as to raise new capital) that had the incidental effect of diluting a pre-existing shareholding. However, no part of such proper purposes included deliberately altering the balance of power between shareholders. Such impropriety would breach the constitutional contract between shareholder and company. The company's power under the articles to issue shares brought with it an implied term that the directors would exercise the power in accordance with their fiduciary duties. (*Tianrui (International) Holding Company Ltd v China Shanshui Cement Group Ltd* [2024] UKPC 36).

Key lessons

- **Personal right of shareholder to bring a claim:** The Privy Council's judgment clarifies that a shareholder may have a personal right against the company where it suffers share dilution due to an allotment of shares by the directors for an improper purpose which has the effect of altering the balance of power between shareholders. The Privy Council found an implied term of the constitutional contract between company and shareholder in the articles that the directors would exercise the company's power under the articles to issue shares in accordance with their fiduciary duties.
- **Dilution where shares allotted for a proper purpose:** The Privy Council commented that a share allotment which has the incidental effect of diluting a pre-existing shareholding will be valid where the directors exercise the power to allot shares in good faith for the benefit of the company as a whole and for the purposes for which the power was conferred. This excludes a share allotment deliberately aimed at altering the balance of power between shareholders.

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Register of members presumptive evidence as to who the company's members were

The Court of Appeal decided that the general principle that a company's register of members was evidence of who the company's members were applied, in the absence of express provision to the contrary, when determining the validity of members' resolutions to appoint voluntary liquidators. It did not matter that a member's name had been removed from the register wrongly on the basis of a forged or unauthorised stock transfer form.

S had held 50% of the shares in company C, with the other 50% being held by J. Both S and J were the directors. J executed a stock transfer form in S's name and, purportedly, C's register of members was then written up to show J as the holder of all the shares in C. J proceeded to pass a written resolution to wind up C and appoint liquidators L. S alleged that J had forged her signature on the stock transfer form and that the share transfer, purported entry on the register and resolution for winding up and appointment of L were all void and of no effect. The Court of Appeal considered the issue on the assumption S's signature had been forged, whilst stating that the analysis would be the same if the stock transfer form had been signed without her authority. The key issue was whether S was an eligible member of C for the purposes of the statutory rules on members' voting rights when J signed the written resolution. The Court of Appeal was guided by statements in *Farstad Supply A/S v Enviroco Ltd*[5] that *"except where express provision is made to the contrary, the person on the register of members is the member to the exclusion of any other person, unless and until the register is rectified"*. One example given of an express contrary provision was section 112(1) of the UK Companies Act 2006 (the CA 2006), which establishes that a subscriber is a member irrespective of whether their name is subsequently entered on the register of members. Another was section 112(2), which states that a non-subscriber must agree to become a member, in addition to having their name entered on the register, without which registration alone is insufficient. These examples explained why section 127 of the CA 2006 describes the register as presumptive, not conclusive, evidence of the identity of the members. However, neither example concerned the scenario where a person whose name had been properly entered on the register of members was removed from the register without her consent. No authority had been identified to suggest that this was a further exception to the general principle. For the purpose of voting on the written resolution here, the Court of Appeal decided that the members were those shown on the register at the time, unless and until the register was rectified by the court. Accordingly, the written resolution was effective and L had been validly appointed. The law did not just disregard the entries on the register of members. This was not an "open … door to fraudsters and forgers". Indeed, the court could make an order for retrospective rectification of the register, or undo the effects of misconduct, or make an order for compensation. It could also limit a retrospective rectification to preserve the validity of meetings or resolutions, so as to prevent prejudice to third parties. (*Re JDK Construction Ltd, Bland & Anor v Keegan* [2024] EWCA Civ 934)

Key lessons

- **Eligibility to vote on shareholder resolution:** The judgment demonstrates that, for eligibility to vote on a shareholder resolution, the members of the company generally are those entered on the register of members unless and until a court order is obtained to rectify the register.
- **Action required in cases of forgery or fraud:** This case highlights the importance of applying to court for rectification of the register of members as a priority where forgery, fraud or unauthorised execution of a share transfer form have been identified.

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5 [2011] UKSC 16.

Enforceability of interim dividends and variation of articles by unanimous consent

The Upper Tribunal (Tax and Chancery Chamber) decided that, where a company with Table A articles of association pays an interim dividend to one shareholder, another shareholder of the same class has an enforceable debt against the company subject to any agreement to the contrary.

PG and his brother NG were principal shareholders in company C. In March 2016 the board of directors resolved to pay an interim dividend, to which PG and NG were entitled as to £20 million each. NG's interim dividend of £20 million was paid to him on 5 April 2016. However, PG's interim dividend of £20 million was not paid to him until 16 December 2016 at a time when he was not resident in the UK. C had Table A articles of association, which provided in article 104 that all dividends should be apportioned and paid proportionately to the amounts paid up on the shares. The First Tier Tribunal (Tax Chambers) (FTT) had held that the interim dividend to PG was treated as "paid" for income tax purposes in the tax year 2016-2017 (when he was non-resident), even though the interim dividend to NG, who held the same class of shares, had been paid in the previous tax year. The effect was that no income tax was payable by PG on the dividend. The analysis hinged on when a shareholder has an enforceable debt against the company to enforce the dividend payment. His Majesty's Revenue and Customs (HMRC) appealed various grounds of the decision to the Upper Tribunal, including the suggestion that where a company with Table A articles pays an interim dividend to one shareholder but not to another of the same class, no debt is owed to the second shareholder at that time. The Upper Tribunal only found in favour of HMRC on this one ground. On this issue it drew by analogy on the analysis for final dividends, where it is established that a company's declaration of a final dividend in general meeting gives rise to a debt payable by the company to its shareholders. This reflects the principle that shareholders of the same class must be treated equally and that the shares confer the same rights on all holders. By contrast, in the case of an interim dividend an enforceable debt only arises once the interim dividend is paid to some shareholder(s) of the class. This has the same effect as a company's declaration of a final dividend in general meeting. However, the Upper Tribunal upheld the FTT's other findings, with the effect that the interim dividend was not treated as "paid" to PG for income tax purposes in the earlier tax year anyway. It decided that there had been shareholders' unanimous consent under *Re Duomatic*[6] to amend C's articles before the dividend was paid to allow the directors to pay the interim dividend to NG without creating an enforceable debt to PG for his share. This was partly for PG's tax planning and also due to logistical issues he faced receiving payment of such a large sum while abroad. It did not matter that the shareholders did not have the articles in mind when agreeing the terms on which the interim dividend would be paid. In any event, the Upper Tribunal decided that there had also been a contractually binding waiver by PG of any right to enforce payment of the interim dividend before 6 April 2016 made *before* the dividend was declared, in consideration of C's agreement to pay the dividend. (*HMRC v Gould* [2024] UKUT 00285 (TCC))

Key lessons

- **When interim dividend is paid:** The judgment confirms that there is an enforceable debt against a company in relation to an interim dividend once it is paid to some shareholder(s) of the same class and the use of the principle of shareholders' unanimous consent to vary the articles of association to delay the time for payment.
- **Contractually binding waiver:** The case is a reminder that a promise by a creditor to waive an *existing* entitlement to be paid all or part of a debt is unenforceable for lack of consideration. It was significant here that the waiver had been agreed *before* an enforceable debt was created by payment of the interim dividend to the other shareholder(s) of the same class.

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6 [1969] 2 Ch 365.

Listed companies

The following decisions are of particular interest to listed companies.

Tracker funds prevented from claiming regarding information published by an issuer

The High Court has dismissed claims brought by tracker funds against an issuer under section 90A and Schedule 10A of FSMA in respect of published information.

Investors brought claims against a listed company (B) under section 90A and paragraphs 3 and 5 of Schedule 10A of the Financial Services and Markets Act 2000 (FSMA). They alleged loss as a result of: (i) certain untrue and misleading statements and omissions of required matters regarding B's "dark pool" trading system in B's annual reports and announcements for 2011 to 2014; and (ii) B's allegedly dishonest delay in publishing certain information. The claimants included funds whose investment processes were wholly or partly passive (Tracker Funds) who did not read B's relevant published information or rely on others who had. The Tracker Funds alleged that they relied indirectly on B's published information because B was obliged to publish certain information, there was an efficient market for B's shares and accordingly B's share price reflected that information. B applied for strike out or summary judgment in respect of the Tracker Funds' claims under Schedule 10A of FSMA.

The test of reliance under paragraph 3 of Schedule 10A required determining whether the investors were induced to rely on the relevant published information and whether it caused them to acquire, hold or dispose of B's shares. The Tracker Funds could not satisfy this test unless their representatives read and considered the relevant information or third parties who directed or influenced their investment decisions read and considered it. For express representations, the test required the investors to prove that they read or heard the representation, that they understood it in the sense which they alleged was false and that it caused them to act in a way which caused them loss. A statement could only cause an individual to act, or operate on their decision-making process, if they heard or read the statement or if the statement (or the gist of it) was communicated to them by a third party. For omissions, investors did not need to prove that they had applied their mind to the absence of a particular statement, or relied on the omission itself. Investors were only required to prove that they relied on the published information itself. Paragraph 5 of Schedule 10A only imposed liability in relation to information which had been published. The investors did not allege that B had published any of the omitted information on which they relied. The Tracker Funds' claims under Schedule 10A had no realistic prospect of success at trial and would be summarily disposed of. (*Allianz Funds Multi-Strategy Trust and Ors v Barclays plc* [2024] EWHC 2710 (Ch))

Key lessons

- **Clarifies Schedule 10A of FSMA:** This decision clarifies the reliance requirement for claims for untrue or misleading statements or omissions from published information under paragraph 3 of Schedule 10A. It also clarifies that paragraph 5 of Schedule 10A only applies where information is disclosed late rather than not at all.
- **Prevents paragraph 3 claims by tracker funds:** The need to prove reliance essentially blocks claims under paragraph 3 of Schedule 10A of FSMA by passive or tracker funds, which comprise around a third of the UK investment market.
- **Reduces risk of paragraph 3 claims by other investors:** Many investors do not read every annual report, circular and announcement published by issuers they invest in. Only significant issuer disclosures are likely to be summarised in secondary sources read by investors (e.g. investor presentations, news or analysts' reports).
- **Investors will seek to appeal this decision:** The investors indicated that they are overwhelmingly likely to appeal this decision. If leave to appeal is granted, then the Court of Appeal will revisit these matters.

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Court enforces compensation rulings made by the Takeover Panel

The High Court has granted an order requiring certain former directors of MWB Group Holdings plc (MWB) to comply with compensation rulings made by the Takeover Panel (Panel)'s Hearings Committee.

The Hearings Committee had found in 2023 that Richard Balfour-Lynn (BL) and certain former directors of MWB Group Holdings plc (MWB) were part of an undisclosed concert party, which had gained control of MWB without making a mandatory offer to shareholders, as required by Rule 9 of the City Code on Takeovers and Mergers (Code). MWB had gone into voluntary liquidation in 2013 and had subsequently been dissolved and it was considered impractical to require a Rule 9 offer to be made. The Hearings Committee therefore exercised its powers under section 10(c) to the Introduction to the Code and section 954(1) of the Companies Act 2006 (CA 2006) to order the defendants to pay compensation of approximately £44 million to the former MWB shareholders. The Hearings Committee rulings were upheld by the Takeover Appeal Board in 2024 and, following the failure of the defendants to pay the compensation, the Panel sought an order from the court under CA 2006, s 955 to secure compliance with the rulings. CA 2006, s 955 provided the court with a discretion to make an order to secure compliance with a rule *"if, on the application of the Panel, the court is satisfied…that a person has contravened a rule-based requirement."* In *Panel on Takeovers and Mergers v King [2017] C.S.O.H 156* and *Panel on Takeovers and Mergers v King [2018] C.S.I.H. 30*, the Outer and Inner Houses of the Court of Session had observed that it would be a "rare" case and "only in exceptional circumstances" where a court would exercise its discretion not to make an order enforcing a Panel ruling. However, the High Court considered that it

Key lesson

- **Another weapon in the Panel's locker:** This is only the second time that the courts have enforced a Panel ruling and given the time and costs involved, it is not likely that the Panel will frequently seek to enforce its rulings in this way. However, the case illustrates the options available to the Panel where traditional enforcement methods such as private and public censuring and 'cold shouldering' are insufficient.

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was not helpful to add additional language to the statutory wording in this way and that the court should balance the relevant factors in the usual way, having regard to the policy of ensuring that offeree shareholders are treated fairly, are not denied an opportunity to decide on the merits of a takeover, and that offeree shareholders of the same class are afforded equivalent treatment by an offeror. BL's claim that he was unable to meet the liability was insufficient to justify not making a section 955 order. He had not produced a full disclosure of assets and liabilities and there were public interest reasons why inability to pay should weigh very lightly in the balance of discretion. In the case of the two other defendants, both of whom were adjudged bankrupt in 2022, the court noted that it had not been asked to decide on the issue of contingent liability. However, it could be argued that MWB's shareholders became contingent creditors at the time the defendants obtained more than 30% of MWB and failed to make an offer in breach of Rule 9, or alternatively that the shareholders became contingent creditors when the Hearings Committee determined that the date of compensation was the date MWB entered administration. (*Re MWB Group Holdings plc* [2024] EWHC 3044 (Ch))

White & Case LLP
5 Old Broad Street
London EC2N 1DW
United Kingdom
T +44 20 7532 1000