[2008] All ER (D) 209 (Nov)

Rayden and another v Edwardo Ltd (in members voluntary liquidation) and another

[2008] EWHC 2689 (Comm)

Queen's Bench Division, Commercial Court

Gloster J

5 November 2008

Contract – Construction – Warranty – Share purchase – Claimant selling share to first defendant – Second defendant guaranteeing first defendant's obligation – Whether payment claimed by claimants accruing – Whether guarantee could be maintained in light of statutory set-off scheme – Whether defendant entitled to claim rescission of contract.

Abstract

Contract – Construction. Queen's Bench Division, Commercial Court: Summary judgment was granted to the claimants in respect of its claim for £3.2m less a credit of £20,000 per calendar month for any payment earlier than 31 December 2008, arising out of a share sale and purchase agreement.

Digest

A share sale and purchase agreement (SPA) dated 5 March 2008 contained a guarantee given by the second defendant of the obligations of the first defendant. Under the terms of the SPA, the claimants agreed to sell and the first defendant agreed to purchase the claimant's remained 50% shareholding interest (the shares) in S, the claimants having sold their first 50% shareholding to the interests of the second defendant in December 2005. The sale also comprised the sale to the first defendant of debt in the sum of £1,044,530 (the shareholder debt) owed to the claimants by S (as to £814,983 to the second claimant and £229,547 to the first claimant). The consideration for the shareholder debt was £1,044.530. By cl 3.1 of the SPA, the consideration for the shares was defined as the 'first share consideration' and the 'second share consideration'. The first share consideration comprised the sum of £453,000. The second was to take the form of certain shares (the consideration shares) or the sum of £3.2m, less the sum of £20,000 for every calendar month earlier than 31 December 2008 by which such amount was paid (the cash alternative). The claimants sought summary judgment under Pt 24 of the Civil Procedure Rules, SI 1998/3132 against the second defendant in the sum of £3.2m (less a credit of £20,000 per calendar month for any payment earlier than 31 December 2008). The claimant also claimed the outstanding purchase consideration against the second defendant.

The issues which arose for determination on the claimant's application for summary judgment were (i) whether, on the true construction of the SPA, the second defendant had a reasonable prospect of successfully arguing that the time for payment of the £3.2m claimed by the claimants had not yet accrued and would

only accrue on 31 December 2008; (ii) whether, on the true construction of the SPA, the second defendant had a reasonable prospect of successfully arguing that the claim under the guarantee could not be maintained against him in the light of the mandatory statutory set-off scheme; and (iii) whether the second defendant had a reasonable prospect of successfully arguing that the defendants could claim rescission of the SPA such that summary judgment should not be awarded against the second defendant under CPR 24.

The court ruled:

The clear intention of the payment provisions was that the second completion date was to take place within a specified number of days after the relevant event, namely, deemed election. It followed that the defendants would not have a realistic prospect of success at trial on that short point of construction. The relevant provisions of the SPA were clearly broad enough to preserve the claimant's right to sue the second defendant, notwithstanding the operation of the mandatory insolvency set-off in relation to the principal debtor, the first defendant. As guarantor, the second defendant had a primary obligation to ensure that the first defendant complied with its contractual obligations to pay the cash alternative on the second completion date without set-off warranty claims, and to perform the relevant guaranteed obligations if it failed to do so. The fact that, if and when the warranty claims came to be established, the result would be that the first defendant's debt would be deemed to have been retrospectively pro tanto discharged as from the date of the winding-up resolution could make no different to the second defendant's continuing and separate obligation as principal debtor to honour the payment of cash consideration without any set-off in respect of the warranty claims. Accordingly, on the construction of the guarantee, the second defendant had no reasonable prospect of success of succeeding in that defence at trial. Further, there could be no realistic prospect of either the defendants successfully being able to rescind the SPA (see [19]-[37] of the judgment).

Richard Millett QC and Charles Hollander QC (instructed by Teacher Stern) for the claimants.

Christopher Parker QC (instructed by Osborne Clarke) for the defendants.

Vanessa Higgins Barrister.

Judgment

[2008] EWHC 2689 (Comm)

QUEEN'S BENCH DIVISION (COMMERCIAL COURT)

5 November 2008

JUSTICE GLOSTER, DBE

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.

MRS JUSTICE GLOSTER:

Introduction

1. These are my reasons for the order which I made on 27 October 2008 giving summary judgment for the claimants, Clive Rayden ("CR") and Paul Rayden ("PR") (together "the Claimants") under CPR 24 against the second defendant, Vincent Tchenguiz ("the Second Defendant") in the sum of £3.2 million (less a credit of £20,000 per calendar month for any payment earlier than 31 December 2008). I also made a declaration that the Second Defendant was liable to pay equal monthly instalments of £18,875 to the Claimants (in the proportion 75% to CR and 25% to PR) from the date of the order to 31 March 2010, with liberty to the Claimants, or each of them, to apply to restore this action for further relief should the Second Defendant default on any future instalment.

2. The Second Defendant's liability arises under the terms of a guarantee given by him of the obligations of the first defendant, Edwardo Limited ("Edwardo") contained in a share sale and purchase agreement dated 5 March 2008 ("the SPA"). Under the terms of the SPA, the Claimants agreed to sell and Edwardo agreed to purchase the Claimants' remaining 50% shareholding interest ("the Shares") in the Sonata Group Limited ("Sonata"), the Claimants having sold their first 50% shareholding to interests of the Second Defendant in December 2005. The sale also comprised the sale to Edwardo of debt in the sum of £1,044,530 ("the Shareholder Debt") owed to the Claimants by Sonata (as to £814,983 to PR and as to £229,547 to CR). The consideration for the Shareholder Debt was £1,044,530, which has all been paid.

3. In the action commenced on 30 June 2008, the Claimants also claim the outstanding purchase consideration against Edwardo, but, for reasons which I explain later, the Claimants do not proceed with their summary judgment application as against it.

The facts

4. By clause 3.1 of the SPA, the consideration for the shares was defined as the "First Share Consideration" and the "Second Share Consideration". The First Share Consideration comprised the sum of £453,000 payable in 24 monthly instalments of £18,875. These Edwardo has paid up to 30 September 2008, although the Claimants have what I regard as a genuine concern that the Defendants are likely to default on such payments in the future, given not only the circumstances of this litigation, but also the fact that the Defendants failed to make payment in May and June 2008, only bringing their payments up to date at the end of July 2008, when these proceedings were instituted against them.

5. The Second Share Consideration was to take the form of certain shares ("the Consideration Shares") or "the sum of £3,200,000 less the sum of £20,000 for every calendar month earlier than the 31st December 2008 by which such amount is paid", which was defined in the SPA as "the Cash Alternative".

6. The Defendants' defence to the claim for payment is twofold. Originally, they contended that the Claimants were liable to Edwardo for damages for breach of warranties contained in the SPA and thus that the Defendants had a counterclaim in respect of such breaches in the sum of £1.8 million odd, which they sought to set off against the £3.2 million outstanding balance of the purchase price.

7. By letter dated 9 September 2008 (i.e. some time after the issue of proceedings) those counterclaims were formally notified as a “Notice of Claims” for the purpose of clause 1(a) of Schedule 4 to the SPA. That letter of claim expressly stated that investigations were on-going and that fresh claims might be discovered.

8. It was common ground that, under the terms of the SPA, Edwardo was not entitled to set off any claim for breach of warranty against its liability to pay the purchase consideration to the Claimants pending final determination of a warranty claim; see clauses 8.6 to 8.8 of the SPA. Thus, as a matter of contract, the entire purchase consideration was due and payable to the Claimants notwithstanding any cross-claim for breach of warranty.

9. However, on 11 July 2008, Edwardo went into members' voluntary liquidation, and Jeremy Willmont and Philip Sykes of Moore Stephens were appointed liquidators (“the Liquidators”). Immediately prior to the commencement of the liquidation, Edwardo's directors made a statutory declaration of solvency. That embodied a statement of assets and liabilities that showed that Edward had an estimated deficit at the time of £8,305,529 a proportion of which related to amounts due to the Claimants. The declaration of solvency referred to the fact that an indemnity had been provided by Euro Investments Overseas Inc, BV to pay all the debits of Edwardo and its liquidation expenses, on the basis of which Edwardo was able to pay all its debts as they fell due. Apparently, Euro Investments Overseas Inc is a company connected with the Second Defendant.

10. Notwithstanding that the liquidation is a members' voluntary liquidation, it was common ground that the statutory insolvency mutual credit and set-off rules, contained in Rule 4.90 of the Insolvency Rules 1986 SI 1986/1925 (as amended by the Insolvency Amendment Rules 2005 SI 2005/527), apply, and that it is not possible validly to contract out of those rules: see *National Westminster Bank Ltd v Halesowen Presswork* [1972] AC 785. It was also common ground that the court has a discretion to stay proceedings brought against a company in members' voluntary liquidation. Thus, the Claimants accepted that they could not rely on the no set-off provision of the SPA as against Edwardo, notwithstanding that it can be inferred from the evidence (which gives no explanation for Edwardo's liquidation) and from certain comments made by leading counsel on behalf of the Defendants during the course of argument, that Edwardo had deliberately gone into members' voluntary liquidation for the express purpose of avoiding the no set-off provisions contained in the SPA. No attempt was made by the Claimants to argue that, in such circumstances, the principle expounded in *National Westminster Bank v Halesown Presswork* did not apply. For that reason, no application for summary judgment under CPR 24 was pursued by the Claimants against Edwardo.

11. I was told by Mr. Christopher Parker QC, who appeared on behalf of the Defendants, that, pursuant to section 91 of the Insolvency Act 1986, the Liquidators had sanctioned the continuance of the powers of the directors of Edwardo in relation to the investigation and prosecution of warranty claims, and other claims against the Claimants.

12. The second defence asserted by the Defendants in the action to the claim against them is rescission. On the afternoon of 7 October 2008, the day before the hearing of the Claimants' part 24 application, Edwardo gave notice, by letter of the same date from its solicitors, purporting to rescind the SPA “in the light of further investigations”. According to the second witness statement of Mr. Willmont, served on the same date, the basis upon which the Liquidators contended that Edwardo was entitled to rescind was:

> i) the matters set out in the Notice of Claim dated 19 September 2008; and
>
> ii) the further matters set out in Mr Willmont's second witness statement.

As described in that statement:

> "The liquidators have concluded that the extent and magnitude of the misrepresentations made by [PR] entitle [Edwardo] to rescind the agreement."

13. In his second witness statement, also dated 7 October 2008, the Second Defendant said:

> "I make this second witness statement for the purposes of notifying the Claimants of my rescission of my guarantee of the Agreement dated 5 March 2008. I gave my guarantee of Edwardo Limited's obligations on the basis of my understanding of the financial position of the Sonata Group as set out in the companies' 2006 Year end Accounts and Management Accounts. Had Paul Rayden not been prepared to warrant that these Accounts were not materially inaccurate, that the Management Accounts fairly reflected the trading position of the Sonata Group and that there had been no material adverse change since the date of such accounts I would not have been prepared to give my guarantee. Indeed, Edwardo Limited would never have entered into the Agreement. Equally had such information been accurate I would have appreciated that the Sonata Group's financial position was worse than I believed it to be. I would not have given my guarantee and Edwardo Limited would never have entered into the Agreement.
>
> The contents of Osborne Clarke's letter to Teacher Stern of 19 September 2008 and of Jeremy Willmont's Second Witness Statement herein have been brought to my attention. In light of that information I wish to rescind the Agreement and my guarantee and hereby do so."

14. Mr. Richard Millett QC, appearing for the Claimants at the hearing on 8 October 2008, described the notice of rescission as "a last-minute stunt". However, although the service of the two notices of rescission at such a late stage appeared, to say the least, opportunistic, nonetheless, if there were a sufficient basis for rescission to satisfy the requirements of CPR 24, that would provide a defence to the Claimants' application for summary judgment against the Second Defendant.

Issues

15. The issues that arise for determination on the Part 24 application against the Second Defendant can be stated as follows:

> i) On the construction of the SPA, does the Second Defendant have a reasonable prospect of successfully arguing that the time for payment of the £3.2 million claimed by the Claimants has not yet accrued and will only accrue on 31 December 2008?
>
> ii) On the construction of the SPA, does the Second Defendant have a reasonable prospect of successfully arguing that the claim under the guarantee cannot be maintained against him in the light of the mandatory statutory set-off scheme applied by rule 4.90?
>
> iii) Does the Second Defendant have a reasonable prospect of successfully arguing that the Defendants can claim rescission of the SPA such that summary judgment should not be awarded against the Second Defendant under CPR Part 24?

Issue 1: has the date for payment accrued?

16. The provisions of the SPA relevant to this issue are the following:

> "1.1
>
> …

'Second Completion Date' means the date upon which completion of the sale and purchase of the Shares takes place pursuant to clause 4.6(f) or clause 4.11 as the case may be.

…

3.1 The Purchase shall, in consideration of the sale to it of the Shares, pay to the Vendors (as to 75% to PR and 25% to CR) the First Share Consideration and the Second Consideration. The 'First Share Consideration' means the sum of £453,000 paid in 24 monthly instalments (each in the sum of £18,875) on the last day of each month (or if not a Business Day, the next following Business Day) the first of which payments shall be made on 31 March 2008. The 'Second Share Consideration' means, at the option of the Purchaser either:

(a) issue and allot to the Vendors the Consideration Shares; or

(b) pay to the Vendors the sum of £3,200,000 less the sum of £20,000 for every calendar month earlier than 31st December 2008 by which such amount is paid (the 'Cash Alternative').

…

4.1 The Purchaser shall use all reasonable endeavours to procure that approval from the Financial Services Authority to the change in control of County Estate Management Limited, which will result from the sale of the Shares ('FSA Approval') is obtained as soon as possible and, in any event, not later than 31 December 2008 (or such later date as the parties may agree). The Vendors shall, as and when requested by the Purchaser, as soon as reasonably practicable provide to the Purchaser such assistance as the Purchase may reasonably require in connection with obtaining the FSA Approval.

…

4.5 The Purchaser or the Purchaser's Solicitors shall notify the Vendors' Solicitors of the obtaining of the FSA Approval within two Business Days of receipt of notification of the same from the Financial Services Authority.

4.6 The Purchaser shall on the earlier of:

(i) 40 Business Days after the notice relating to FSA Approval is served pursuant to clause 4.5; or

(ii) 31 December 2008;

(the 'Compliance Date')

serve written notice on the Vendors specifying whether it has elected to satisfy the Second Share Consideration in accordance with clause 3.1(a) or 3.1(b) (the 'Purchaser's Notice') and the following provisions shall then apply:

(a) if the Purchaser does not give the Purchaser's Notice, together with the Purchaser's [Fair Market Value – “FMV”] pursuant to sub-clause (b) by the Compliance Date then the Purchaser shall be deemed to have elected to satisfy the Consideration in accordance with Clause 3.1(b); or

(b) the Purchaser shall provide to the Vendors with the Purchaser's Notice the Purchaser FMV together with a copy of the Purchaser's FMV;

(c) the Vendors shall (within 15 Business Days of the Purchaser's Notice) give written notice to the Purchaser stating whether or not they dispute the Purchaser's FMV and stating their reasons for the same (a 'Dispute Notice'). If the Vendors do not give a Dispute Notice within such period then the Vendors shall be deemed to have accepted the calculation and be bound by the same;

(d) if the Vendors give a Dispute Notice then the dispute shall be referred to an Independent Accountant and the relevant provisions of clause 3.3 in respect of such Independent Account shall apply;

(e) if the Vendors give a Dispute Notice, the Purchase may change its election for the purposes of clause 3.1, by electing to satisfy the Consideration by way of payment of the Cash Alternative as opposed to the issue of the Consideration Shares, provided it does not by written notice to the Vendors within 5 Business Days of the date of the Independent Accountant determining the Fair Market Value;

(f) Subject to the other provisions of this Agreement, Completion of the sale and purchase of the Shares shall take place:

(i) if the Vendors do not give a Dispute Notice, 6 Business Days after the Purchaser's Notice; or

(ii) if the Vendors give a Dispute Notice and the Purchaser does not change its election pursuant to sub-clause 4.6(e), 6 Business Days after Fair Market Value has been determined; or

(iii) if the Vendors give a Dispute Notice and the Purchaser changes its election to the Cash Alternative pursuant to sub-clause 4.6(e), 3 Business Days after the Purchaser has given notice of its change of election;

and the date referred to in sub-clauses (1), (ii) or (iii) as applicable, shall be the Second Completion Date.

4.7 If the consideration is to be satisfied by payment of the Cash Alternative then, on the second Completion Date:

(a) the Vendors shall deliver to the Purchaser stock transfer forms, duly completed and executed by them as the registered holders, in favour of the Purchaser (or as it may direct) in respect of the Shares, and the relevant share certificates (or an indemnity in the agreed form in respect of any lost share certificates); and

(b) The Purchaser shall pay the Cash Alternative to the Vendors (or as the Vendors shall direct).”

17. The FSA gave its approval to the transfer of control in County Estates Management Limited (“CEM”) (a subsidiary of Sonata) on 9 April 2008. Edwardo did not give a Purchaser's Notice (as defined) and therefore, as was common ground, it was deemed to have elected to have satisfied the consideration in cash. The Defendants' case is that, in the circumstances, the time for payment has not accrued, and that they have an option, pursuant to clause 3.1(b), to pay the Cash Consideration at any time up to 31 December 2008. The Claimants' case is that the time for payment of the Cash Consideration was in June 2008, in accordance with clause 4.6(f)(i) and clause 4.7(b).

18. Mr. Parker submitted that the SPA did not state a date on which the Cash Alternative was to be paid and that accordingly, one had to infer the date of payment from the other provisions of the SPA. He further submitted that the wording of clause 4.6 did not cover payment of the Cash Alternative, and that (in the absence of a claim for rectification) there was no sensible basis for reading words into clause 4.6 to make it cover

completion by means of payment of the Cash Alternative. Therefore, he submitted, one had to look at the wording of clause 3.1(b) to identify the Second Completion Date in the event that the Cash Alternative was the relevant method of payment. He submitted that the language of that clause was not consistent with the £20,000 monthly instalments operating as a penalty for late payment. He submitted that the reference in the definition of "Second Completion Date" to clause 4.11 was an error and should have been a reference to clause 4.7, which was the clause referring to payment by means of the Cash Alternative, but that that clause did not identify the Second Completion Date.

19. I disagree with Mr. Parker's analysis. The drafting of the relevant provisions is sloppy, but I accept the submissions made by Mr. Millett, and subsequently amplified by Mr. Charles Hollander QC (who appeared for the Claimants at the hearing on 27 October 2008), that, on a commercial and purposive construction of the relevant clauses, the Second Completion Date (in circumstances where the Purchaser does not give a Purchaser's Notice, and therefore is deemed to have elected to pay the Cash Alternative) is six Business Days after the day of the Purchaser's deemed election. Clause 4.7 makes clear that payment of the Cash Alternative must be made on the Second Completion Date, that being the date when the Claimants are also to deliver stock transfer forms. The definition of Second Completion Date refers to Clause 4.6(f). It also refers (wrongly) to clause 4.11 which may have been intended to be a reference to either clause 4.7 or 4.12, but neither assists the Defendants. Contrary to Mr. Parker's submission, Clause 4.6 (including Clause 4.6(f)) addresses completion by means of payment of the Cash Alternative: see sub-clause 4.6(f)(iii). Clause 4.6(f) itself explains how the Second Completion Date is identified. The Second Completion Date must be calculated from the terms of Clause 4.6(f). Once that is recognised, then the position is straightforward. The scheme of Clause 4.6(f) is that the Second Completion Date will take place six Business Days after the last stage in the process has been completed: see (f)(i) and (ii), or in the case of a change of election under (f)(iii) only three Business Days thereafter. What the draftsman has forgotten is that where there is a deemed election under Clause 4.6(a), there will be no service of a Dispute Notice, and thus the six business days will run from the deemed election.

20. The drafting is clearly infelicitous. But I agree with Mr. Hollander that the Defendants' case cannot possibly be right. First, it requires the Second Completion Date to be determined solely by reference to Clause 3.1(b). But Clause 3.1(b) merely defines the Cash Alternative and specifies the amount of the consideration. It does not purport to deal with the Second Completion Date. The definition of Second Completion Date does not refer to Clause 3.1(b) either. Secondly, the Defendants' construction would have the effect that determination of the Second Completion Date is entirely at the option of the Defendants. There is nothing in the SPA which supports that conclusion, although it would be a highly material provision to be agreed between the parties. Thirdly, the submission put forward by the Defendants is that the last date on which the Defendants could elect to have the Second Completion Date is 31 December 2008, as a result of Clause 3.1.(b). But there is no support for that either in Clause 3.1(b). All Clause 3.1(b) does is to provide a discount for payment prior to 31 December-it does not state that payment is required to happen by or on 31 December. Indeed, completion could not happen by that date if FSA Approval had not been obtained by then.

21. Such a construction (i.e. no end date by which the Purchaser was obliged to pay the Cash Alternative) would be commercially absurd. In my judgment, the clear intention of the payment provisions (and support for this is also to be derived from clause 4.3 which provides for what is to happen in the event that no FSA Approval is obtained prior to 31 December 2008) is that the Second Completion Date is to take place within a specified number of days after the relevant event – here deemed election. If necessary, I would imply a term to that effect.

22. Accordingly, it follows that in my judgment, the Defendants would not have a realistic prospect of success at trial on this short point of construction. Following the guidance in the Notes to CPR 24.2.3 at page 559, it is appropriate for me to decide the point of construction as a preliminary issue, which I do pursuant to my case management powers under CPR 3.1.

Issue 2: the liability of the Second Defendant in light of Rule 4.90

23. It was common ground before me that Rule 4.90 applies in members voluntary liquidation: see Rule 4.1(1)(c). The effect of Rule 4.90 is that a valid set-off is (retrospectively) treated as payment at the date of the liquidation. Where the set-off is disputed, as in the present case, the notional payment can only be intermediate, or provisional, in nature. It was also common ground between the parties that the terms of a guarantee can require payment by the guarantor to the creditor, notwithstanding the statutory set-off scheme under Rule 4.90 and the decision in *National Westminster Bank v Halesown Press (supra)*, and there is no rule of law which precludes this. Accordingly, the issue becomes one of the construction of the guarantee. From a practical perspective, the issue is one of timing. The "deemed payment" may subsequently be found not to have been a payment at all, if the purported set-off subsequently turns out to be ill-founded. The question is whether the guarantor is obliged to pay in the meantime, pending the determination of the warranty claim and whether or not it was in fact a deemed payment by way of set-off.

24. Mr. Parker submitted that the terms of the Second Defendant's guarantee were not sufficiently broad to allow the Claimants to recover from the Second Defendant, as surety, the sums that, because of Rule 4.90, the Claimants had already been deemed to have received from the principal debtor by virtue of insolvency set-off. He referred to paragraph 18.35 in *The Law of Set-Off*, Derham, 3rd Edition where it is stated:

> "If the principal debtor has become bankrupt or gone into liquidation, so that the insolvency set-off section applied automatically on the occurrence of the bankruptcy or the liquidation so as to extinguish the debt owing to the creditor to the extent of the debtor's cross-claim, it is suggested that the clearest words would be required to preserve the guarantor's liability to the creditor."

25. I attach, as Appendix 1 to this judgment, clause 12 of the SPA which is the relevant guarantee clause. In my judgment, these provisions, taken together (or, for example, in the case of clause 12.7 and clause 12.10, individually) are clearly broad enough to preserve the Claimants' right to sue the Second Defendant, notwithstanding the operation of the mandatory insolvency set-off in relation to the principal debtor, Edwardo. As guarantor, the Second Defendant had a primary obligation to ensure that Edwardo complied with its contractual obligation to pay the Cash Alternative on the Second Completion Date without set-off of warranty claims, and to perform the relevant Guaranteed Obligations if Edwardo failed to do so. The fact that, if and when the warranty claims come to be established, the result will be that under Rule 4.90 Edwardo's debt will be deemed to have been retrospectively pro tanto discharged as from the date of the winding-up resolution, can, in my judgment, make no difference to the Second Defendant's continuing and separate obligation as principal debtor to honour the payment of the Cash Consideration without any set-off in respect of the Warranty Claims.

26. Accordingly, in my judgment, on the construction of the Guarantee, the Second Defendant has no reasonable prospect of succeeding in this defence at trial. I decide this point, too, as a preliminary point of construction.

Issue 3: Rescission

27. The claim to rescission was based on: (i) what was said to be the discovery of the receipt of £86,180 by the Claimants; and (ii) the discovery of 19 allegedly "rogue accounts", as described in the latest evidence served by the Defendants. It is worthy of note that no claim for misrepresentation had ever previously been made by the Defendants. In my judgment, there is no realistic prospect that the Defendants will succeed in their defence of rescission, for the reasons adumbrated by Mr. Hollander.

Issues arising in relation to the rescission claim

28. The issues arising in the context of this Part 24 application against the Second Defendant in relation to the Defendants' claim for rescission can be summarised as follows:

Do the Defendants have a realistic prospect of successfully claiming rescission of the SPA in the light of:

i) the Claimants' contention that the Defendants have affirmed the SPA by their conduct;

ii) the Claimants' contention that little or no damage has been suffered by Sonata or the Defendants;

iii) the Claimants' contention that rescission would not be awarded as a remedy by the court because restitutio in integrum is impossible.

29. On 19 September 2008, the Liquidators formally put forward the warranty claims relied on by the Defendants. By so doing, the Defendants, in my judgment, elected to place reliance on the warranty provisions contained in the SPA and affirmed the contract. There was no reference in that (or any previous) letter to those claims being treated as misrepresentation claims. The Notice of Claims refers to further claims being investigated, which is likely to have been a reference to the new claims, given the timing of events referred to in the written statement of Ms Charalambous, the head of Estate Accounts at CEM. On 29 September, payment was made to the Claimants of further sums due to them from the Defendants pursuant to clause 3.1 of the SPA. Those payments treat the SPA as continuing in force and in my view constitute a further affirmation of it as a contract.

30. In such circumstances, there is, in my judgment, no realistic prospect of either of the Defendants successfully being able to rescind the SPA based on the claims which were the subject matter of the Notice of Claims on the grounds of breach of warranty. At best they can only rely on the new claims to base their claim for rescission. But, in my judgment, they also have no realistic prospect of successfully showing that they are entitled to rescind on the grounds of the new claims.

31. Insofar as the Defendants sought to suggest that the evidence relating to the new claims showed possible grounds for rescission based on fraudulent misrepresentation, I reject such suggestion. The evidence served by the Second Defendant, when viewed in the light of the explanations given in PR's witness statement, did not show any solid grounds for avoiding the SPA on grounds of fraudulent misrepresentation.

32. Nor, in my judgment, did the evidence show any solid grounds for avoiding the SPA on grounds of non-fraudulent misrepresentation.

33. So far as the “discovery” of the receipt of £86,180 is concerned the first time (apart from an oblique reference at a without prejudice meeting on 3 October 2008 to a misdirected receipt which was not in sufficient detail to enable PR to make any inquiries) any detailed reference was made to this receipt was on 7 October 2008, the day before the first hearing. PR explained in his witness statement: (a) that the payment was made into the account in error, presumably by the managing agents, the Edge, or Gross Fine; and (b) that he knew nothing about it until it was raised by the Defendants. After the hearing on 8 October, the Claimants' solicitors sent a cheque for that sum to the Defendants' solicitors, inviting the Defendants' solicitors to come back with an interest calculation for payment. Initially, the cheque was not accepted by the Defendants, on the grounds that this was a matter between the Claimants and those who made the mistaken payment. However, during the course of the hearing on 27 October 2008, I was informed that, if the cheque was delivered to Osborne Clarke as CEM's solicitors, rather than the Defendants' solicitors, it would be accepted.

34. In regard to the 19 alleged “rogue” accounts, the evidence showed that these were client accounts operated for the benefit of third parties. According to the evidence, they never contained monies belonging to Sonata. Some of them were “pub” accounts, which related to business never transferred to Sonata. Others

had been closed long before the SPA. Still others were in the names of clients themselves, rather than Sonata or CEM.

35. In his email dated 21 October 2008, Mr Gray, on behalf of the Defendants (who continue to ask PR for information pursuant to his obligations under Clause 6.3 of the SPA, notwithstanding the purported rescission) asked PR:

> "… were the funds held in the HSBC accounts part of the monies referred to in note 8(c) of the accounts of [CEM]."

The Claimants stated that they believed this to be the case. Thus there appears to have been a reference to these monies in the disclosed accounts in any event.

36. The complaint now seems to be that in certain respects these accounts were overdrawn by the clients and thus, to the extent that the accounts were in the name of CEM, there was a potential liability on Sonata which should have been disclosed. It is not suggested that any such liability in fact ever arose, or that there was any reason to believe that such liability would ever arise. Indeed, it appears that PR had personally guaranteed these accounts in any event. I agree with Mr. Hollander that, at best, there might have been a technical breach of the warranties in this respect, but the likelihood of any successful rescission claim succeeding on this basis is remote.

37. In the circumstances, the claim for rescission has no real prospect of success. It appears to be based on claims in relation to which, even if valid, no damage was suffered by Sonata. The conduct of the Defendants to date suggests that the rescission claim is opportunistic and a tactical move. As soon as the claim for the purchase price was made, Edwardo was put into members' voluntary liquidation. No commercial purpose for this has ever been suggested, other than in an attempt to enable Rule 4.90 to be used to avoid the no set-off provisions in the SPA. After a warranty claim had been made, on the afternoon before the hearing of the summary judgment application, notice of rescission was purportedly given, based on a possible claim for £86,180. A prompt offer to repay the amount in question was made by the Claimants once the position was understood. The Defendants' response appears to be that this was a matter between PR and The Edge. But it does not seem to be the case that Sonata has suffered any loss at all. Importantly, as the evidence of PR shows, the Second Defendant and his management team have been heavily involved in both the owning and the running of the Sonata business since 2004. I agree with Mr. Hollander that it is perhaps somewhat disingenuous of the Second Defendant to give the impression in his statement that he knew little of the business.

38. Secondly, even if a claim could be made, its value is likely to be insignificant in comparison to: (a) the consideration under the SPA; (b) the value of any warranty claims; and (c) the problems of restitutio in integrum.

39. Thirdly, even if it could be shown that there was some sort of misrepresentation, it is hard to see why such misrepresentation was, or could have been, material to the Defendants, particularly given that they already have the benefit and protection of warranties – which as the Second Defendant stated, was so important to him. The Defendants are not alleging any misrepresentation which was different from the representations which were covered by the warranties under the SPA. Moreover, even if, contrary to my conclusion, the Defendants were entitled to claim rescission, in my judgment the overwhelming probability is that the court would exercise its discretion under section 2(2) of the Misrepresentation Act to award damages in lieu of rescission.

40. These reasons are sufficient in themselves to justify my conclusion that the Defendants' claim for rescission has no realistic prospect of success. However, I should also say that, in my judgment, both Defendants' claim for rescission has no realistic prospect of success because of the unavailability of restitution or restitutio in integrum. Under the terms of the SPA, on signing the agreement, PR had to resign as director and as

Chief Executive Officer and employee of Sonata, and any other group company (clause 2.10). The SPA also acknowledged that, after the date of the SPA, Edwardo intended there to be a reorganisation of the Sonata Group and various related companies (clause 4.10). Neither PR or CR had any further involvement with the running of the business. Moreover, at the time of entry into the SPA, the Sonata business was in the process of being integrated with the Solitaire business, in anticipation that Sonata would exercise its option to acquire Solitaire. The option to acquire Solitaire has now lapsed, but the integration has continued because Sonata and Solitaire are currently under the same ultimate ownership. Since the SPA, the Sonata/Solitaire Group has also been integrated with the Peverel Group, that business also being in the same ultimate ownership.

41. While the Defendants contend that these changes could be reversed, and that restitution is possible, their evidence, on proper analysis, supports the opposite conclusion. Mr. Parker submitted that the Sonata shares were still the same shares, and indeed, had not yet been transferred, and that the Debt Consideration could be repaid, and the Shareholder Debt reassigned. He relied on dicta in *Armstrong v Jackson* [1917] 2 KB 822 at 828 and on *Newbigging v Adam* (1886) 34 Ch 582. Whilst I accept that restitution does not have to be precise, the reality here is that although the shares the subject of the SPA have remained the same shares, they are shares in a private company, not a publicly quoted company. Previously the Claimants were involved in running the company; after the SPA they ceased to do so. The result is that the underlying business has changed substantially in nature since the date of the SPA and Edwardo's agreement to purchase the Claimants' shares. All these features would, in my judgment, realistically be likely to make a court hold that the Defendants were precluded from claiming that they were entitled to rescission of the SPA. For this additional reason, in my judgment the Defendants have no realistic prospect of succeeding in their rescission claim.

42. For the foregoing reasons, I awarded summary judgment in favour of the Claimants.

Appendix 1

Guarantee

12.1 In consideration of the Vendors entering into this Agreement and payment by the Purchase of £1 to the Guarantor (receipt of which the Guarantor hereby acknowledges) the Guarantor, at the request of the Purchaser, irrevocably and unconditionally guarantees as a primary obligation to the Vendors and their permitted assigns:

> (a) the full, complete, due and punctual performance of all the obligations of the Purchaser (and its transferees, or assigns, and for the purpose of this clause 12, the term Purchaser shall includes its transferees and assigns) contained in this Agreement; and
>
> (b) shall pay to the Vendors on demand any sum of money which:
>
> (i) the Purchaser is at any time liable to pay to the Vendors under or pursuant to this Agreement; and
>
> (ii) which has not been paid at the time the demand is made.
>
> Together, the Guaranteed Obligations.

12.2 The obligations of the Guarantee in this clause 11 [sic] are as primary obligations and not as a mere surety and shall not be affected by:

> (a) any of the Guaranteed Obligations being or becoming void, voidable or unenforceable for any reason; or

(b) any of the Guaranteed Obligations not being recoverable by reason of illegality, incapacity, lack or exceeding of powers, ineffectiveness of execution or any other reason;

and in such event the Guarantor shall perform the Guaranteed Obligations as if it were primarily liable for the performance.

12.3 The Guarantor shall, upon written demand by the Vendors or their permitted assigns, unconditionally perform the Guaranteed Obligations (or any one of them) in the manner prescribed in the relevant provision of this Agreement as if it were the purchaser.

12.4 The guarantee contained in this clause 11 [sic] (the “Guarantee”) is and shall at all times be a continuing security and shall cover the ultimate balance of all monies payable under this Agreement by the Purchasers to the Vendors irrespective of any intermediate payment or discharge in full or in part of the Guaranteed Obligations.

12.5 The Guarantor as principal obligor and as a separate and independent obligation and liability from its obligations and liabilities pursuant to the Guarantee, agrees to indemnify and keep indemnified the Vendors in full and on demand from and against all losses, actions, demands, liabilities, penalties, claims, fines, proceedings, contributions, compensation, remuneration, damages, costs and expenses suffered or incurred (including, without limitation reasonable legal expenses and other reasonable professional advisor's fees) arising out of, or in connection with:

(a) any failure by the Purchaser to perform or discharge any of the Guaranteed Obligations or discharge any of its liabilities thereunder;

(b) the enforcement of any rights under or in connection with the Guarantee by the Vendors.

12.6 The obligations of the Guarantor are continuing obligations and will not be satisfied, discharged or affected by any intermediate payment or settlement of account or any change in the constitution or control of, insolvency of, or any bankruptcy, winding-up or analogous proceedings relating to the Purchaser.

12.7 The liability of the Guarantor under the Guarantee will not be reduced, discharged, or otherwise adversely affected by any act, omission, arrangement, matter of thing (without limitation) which might operate to release, discharge or otherwise exonerate the Guarantor had it been a principal debtor instead of a guarantor or indemnifier, or by anything done or omitted to be done by any person which (but for this sub-clause) might operate to exonerate or discharge the Guarantor or otherwise reduce or extinguish the liability of the Guarantor or otherwise provide a defence to its liability, in respect of the Guaranteed Obligations (whether or not known to the Vendors) including, without limitation:

(a) any time or indulgence granted to or composition with the Purchaser;

(b) the taking, variation, compromise, renewal or release of or refusal or neglect to perfect or enforce any right or remedies against the Purchaser;

(c) any legal limitation, disability, incapacity or other circumstances relating to the Purchaser or any other person or any amendment to or variation of the terms of this Agreement or any other document or security; or

(d) any irregularity, unenforceability or invalidity of any obligations of the Purchaser under this Agreement with the intent that the Guarantor's obligations under the Guarantee shall remain in

full force and the Guarantee shall be construed accordingly as if there were no such irregularity, enforceability or invalidity.

12.8 The liability of the Guarantor under the Guarantee will not be affected by any arrangement which the Purchaser may make with the Vendors which (but for this sub-paragraph) might operate to diminish or discharge the liability of, or otherwise provide a defence to, the Guarantor. Without prejudice to the generality of the foregoing, the Vendors may at any time and without reference to the Guarantor:

(a) grant time for payment; or

(b) grant any other indulgence; or

(c) agree to any amendment, variation, waiver or release in respect of any of the obligations of the Purchase under this Agreement; or

(d) give up, deal with, vary, exchange or abstain from perfecting or enforcing any other securities or guarantees held by the Vendors at any time and:

(i) discharge any party to such guarantees;

(ii) realise such securities or guarantees or any of them as the Vendors thinks fit;

(iii) compound with, accept compositions from and make any other arrangements with the Purchaser;

without affecting the liability of the Guarantor under the Guarantee.

12.9 The Guarantor waives any right it may have to require the Vendors (or any trustee or agent on their behalf) to proceed against or enforce any other right or claim for payment against any person before claiming payment from the Guarantor under this clause 11 [sic].

12.10 If any payment by the Purchaser is avoided or reduced as a result of insolvency of the Purchaser or any similar event, the liability of the Purchaser and the Guarantor shall continue as if the payment, discharge, avoidance or reduction had not occurred and the Vendors shall be entitled to recover the value or amount of that payment.

12.11 The Guarantee is in addition to and shall not merge with or otherwise prejudice any other right or remedy of the Vendors in respect of the Guaranteed Obligations.

12.12 So long as the Purchaser remains under any actual or contingent obligation under this Agreement the Guarantor shall not:

(a) exercise any security or other rights which it may at any time have against the Purchase, howsoever such rights may occur;

(b) claim any contribution from any other surety of the obligations of the Purchaser; or

(c) take the benefit (in whole or in part and whether by way of subrogation or otherwise) of any of the rights of the Vendors under this Agreement or of any other security taken by the Vendors pursuant to or in connection with this Agreement.

12.13 The liability of the Guarantor under the Guarantee shall not be affected by the avoidance or any assurance, security or payment or any release, settlement or discharge which may have been given or made on the faith of any assurance, security or payment, in either case, under any enactment relating to bankruptcy or insolvency.