Neutral Citation Number: [2019] EWHC 2996 (QB)

Case No: QB/2019/001942

IN THE HIGH COURT OF JUSTICE
QUEENS BENCH DIVISION

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 4th November 2019

Before :

His Honour Judge Simpkiss
(sitting as a Deputy Judge of the High Court)

- -

Between :

(1) PAUL WELLS **(2) ROBERTO SOLARI**	**Claimants**
- and -	
(1) CATHAY INVESTMENTS 2 LIMITED **(2) PNC GLOBAL LOGISTICS LIMITED**	**Defendants**

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Chris Quinn (instructed by **Simons Muirhead and Burton LLP**) for the **Claimants**
Edward Levey and Nick Daly
(instructed by **Dentons UK and Middle East LLP**) for the **Defendants**

Hearing dates: 22nd to 26th, 29th and 30th July 2019

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Approved Judgment

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

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HIS HONOUR JUDGE SIMPKISS

His Honour Judge Simpkiss:

Introduction

1. The Claimants bring this claim for damages for wrongful dismissal and for declarations that they did not act in material breach of their Employment Agreements with the Second Defendant and are entitled to be paid a fair value for their shares in the Second Defendant. They allege that the sole reason for their dismissal was to enable the First Defendant to avoid paying them the fair value of their shares in the Second Defendant under option agreements. There are also issues about the enforceability of restrictive covenants in the Claimants' employment and shareholder agreements with the Second Defendant.

Introductory Background

2. The Second Defendant is a transport and logistics business. Its chairman was until the transactions referred to below, Mr. Paul Solari, the father of the Second Claimant. He and Mr. Geoffrey Osgood were the directors, resigning on 18th January 2017.

3. In 2007 the First and Second Claimants commenced employment with the Second Defendant, then called Unitas. It was incorporated in 2011. Mr. Daniel Stokes was the Financial Controller of the Second Defendant.

4. In 2016 the First Defendant approached the Second Defendant with a view to purchasing it. On 20th January 2017 the transaction went ahead with various agreements being entered into:

    a) The Share Purchase Agreement ("SPA");
    b) The Employment Agreements ("EA")
    c) The Put and Call Option Agreements ("OA")
    d) The Shareholders' Agreement ("SHA").

5. Mr. Kevin Johnson and Mr. Ben Chaing were and are directors of the First Defendant. On 18th January 2017 they were appointed the sole directors of the Second Defendant and this remains the position.

6. At the time of these transactions the shares in the Second Defendant were held as follows:

    a) Mr. Solari Snr: 41%;

    b) Mr. Geoffrey Osgood: 48%;

    c) Mr. Dan Stokes, the financial controller of the Second Defendant: 1% given to him by Mr. Solari Snr shortly before the transaction;

    d) The Claimants: 5% each.

7. In the transactions Mr. Solari Snr, Mr. Osgood and Mr. Stokes agreed to sell their shares to the First Defendant. The Claimants retained their shares, but entered into the OAs. They continued their employment with the Second Defendant and entered into the EAs. Mr. Osgood continued with the Second Defendant on a part time consultancy basis.

8. The Claimants were employed by the Second Defendant throughout 2017 and 2018. On 2nd January 2019 they exercised their put options, requiring the First Defendant to purchase their shareholdings for a Fair Value. Under the terms of the EAs once a notice had been served in exercise of the Put Options, that Claimant's employment by the Second Defendant was automatically terminated 3 months after notice.

9. The parties were unable to agree the value of the shares and the Second Defendant instigated disciplinary proceedings against the Claimants. These resulted in the termination of their respective employments on the grounds of gross misconduct on 22nd March 2019. On 28th March 2019 the Second Defendant's solicitors gave notice to the Claimants that they were in Material Breach of the terms of the OAs and that they were required to transfer their respective shareholdings to the First Defendant at nominal value. The Claimants appealed under the disciplinary process, but the appeals were dismissed.

The Agreements

The Share Purchase Agreement ("SPA")

10. This agreement was made between Dan Stokes, Geoffrey Osgood, Paul Solari Senior (the "Sellers"); the First Defendant (the "Buyer") and the PNC Global Logistics (UK) Limited ("the Subsidiary").

11. By Clause 2 of the SPA each seller agreed to sell to the buyer the shares that they owned. The consideration was set out in Clause 3 and divided into Initial Consideration and Deferred Consideration. The Initial Consideration was agreed at £3,194,066. Clause 3.3 provided that the amount to be paid on completion was the balance after deducting from this sum various other sums. These included:

    a) The Suggero Indebtedness (£438,416 owed by Suggero369UK Ltd to the Second Defendant);

    b) A director's loan of £88,584 owed by Geoffrey Osgood to the Second Defendant;

    c) The loan of £522,000 owed by Ticco Foods to the Second Defendant;

    d) The Retained Consideration;

    e) All other deductible amounts set out in the Completion Statement.

12. The Deferred Consideration was provided for in Schedule 6 of the SPA and was limited to a maximum of £2,100,000. There were two periods during which Deferred Consideration might arise. Each could give rise to a liability for the Second Defendant to make further payments to the Sellers if Group EBITDA during each period exceeded the EBITDA target for that period. If the Group EBITDA during each period fell below £1,000,000, then the Sellers were liable to make payments to the First Defendant of a Shortfall Payment. Group EBITDA was defined as the aggregate of EBITDA for the Group during the relevant period, and Group was defined as the Second Defendant and the Subsidiary.

13. The EBITDA target for the First Deferred Consideration Period was £1,050,000 and for the Second Deferred Consideration Period was the higher of the First EBITDA target and the actual group EBITDA during the First Deferred Consideration Period provided it was no higher than £1,400,000.

14. Schedule 8 makes provision for calculating the Retained Consideration. For example, if there is a Shortfall payment due, this can be set off against the sum retained or if there is a Leakage Payment due from them as defined in Clause 8. It is not necessary for me to go into any further detail at this stage.

15. Clause 6 sets out the warranties that the Sellers gave to the Buyer. These are set out in more detail in in Schedule 3 and in the Tax Warranties.

16. Clause 6.7 provides an express warranty that the Sellers have made due, diligent and careful enquiries of each other and of the First Claimant before giving each warranty or making the statement made in the Disclosure Letter.

17. Finally, Clause 11 sets out various restrictive covenants entered into by the Sellers.

18. Schedule 3 sets out the warranties, which included at 5.1.3 a warranty that the Locked Box Accounts gave a true and fair view of the state of the Second Defendant at the Locked Box Date and of the results for the period ended with that date or the Accounts Date as appropriate. The Locked Box Date was agreed as 30th June 2016 and the Accounts Date 30th March 2016.

The Employment Agreements ("EA")

19. The Claimants were retaining their shareholdings in the Second Defendant as they believed that following the take-over, the Second Defendant would prosper and they would therefore increase the value of their shares. Mr. Kevin Johnson, a Director of the First Defendant, said that although the First Claimant's name appears in the SPA and that he may initially have intended to sell his shares, this would not have been agreed by the First Defendant, as they wanted some continuity in the senior management.

20. For statutory purposes the date of their employment by the Second Defendant was agreed as having started on 2nd July and 3rd December 2007 respectively. Their respective salaries were £82,700 and £81,100 respectively. They were based at the Second Defendant's premises in Egham.

21. It was expressly provided that the Second Defendant was required to give three months notice of termination of their employment in writing. Similarly, the Claimants could terminate their employment on three months notice. If either party exercised the put or call option under the OA, then they were deemed to have given three months notice of termination of employment on that date, unless notice had already been served for an earlier period.

22. It was expressly provided that the disciplinary rules regarding any disciplinary action that might be taken against the Claimants were set out in the employee handbook. The appeal process was also set out in the employee handbook.

23. There was dispute about whether the Claimants saw any handbook at the time of entering into the EAs and, if so, which version – the 2015 or 2016 version? The

Defendants also contended at the start of the trial that the version of the handbook produced by the Claimants had been "*doctored*". This allegation was withdrawn following the evidence. It was potentially relevant to the allegation that the Second Claimant was in serious breach of his EA because there is an express term in the 2016 version that (a) the email or internet system should not be used for on-line gambling or accessing or transmitting pornography; and (b) the transmission of confidential information (grounds B, C and D). Gross misconduct is defined as including: Serious misuse of the Second Defendant's email/internet. There is a warning that a breach could lead to dismissal. This was a change from previous versions of the handbook.

24. I am satisfied that the March 2016 version was the subsisting version at the time of the EAs. Whether the Claimants read it is unclear, and unlikely. There is no evidence that it was actually seen by them when they signed. Nevertheless, the EA must be construed as obliging the Claimants to abide by the version of the handbook current from time to time and therefore they are bound by the March 2016 version.

25. This does not in fact matter because the Second Claimant accepted in cross-examination that accessing a pornographic and gambling site on a work computer by a senior manager would be a serious misconduct and similarly with disclosure of confidential information. I should point out that this does not necessarily mean that it is either gross misconduct amounting to a repudiatory breach of the EA nor that it is a Material Breach under the SHA.

26. There was the following express term:

"Confidential Information

During your employment with the Company and after its termination (however this occurs) you must not (other than in the proper course of your employment with the Company):

a) *use for your own purposes or those of any other person, firm, company, association or other organisation whatsoever;*

b) *disclose to any person, firm, company, association or other organisation whatsoever*

any Confidential Information of or belonging to the Company or to any third party (which includes customers, suppliers, employees and officers of the Company or any Group Company) which was learnt or disclosed to you in confidence in the course of your employment.

The above clause does not prevent you from using or disclosing Confidential Information if you are ordered to do so by a court of competent jurisdiction, or if authorised by the Company in writing to do so if such information has become public otherwise than by default of yourself, the employee or if you are making a protected disclosure with the meaning of section 43A of the Employment Rights Act 1996."

27. Confidential Information is not defined.

28. Clause 1.2 of the EAs makes provision for restrictive covenants which I will deal with in detail later in this judgment.

The Put and Call Option Agreements ("OA")

29. The Claimants also entered into a put and call option agreement with the First Defendant, each in similar terms.

30. Clause 3.1 provided that the Put Option could only be exercised on or after 1st January 2019 and that it would lapse if not exercised by 6th January 2019. Provision for its exercise by notice is set out in Clause 4, and the Seller must give a date for completion not earlier than 5 nor more than 10 business days after the date of the notice. It cannot be revoked once exercised.

31. Clause 6 makes provision for the consideration – which is the Fair Value, defined by reference to Schedule 1 and is the amount agreed by the Seller and the Buyer, or in the absence of agreement within 30 days of the exercise notice, as calculated by an expert appointed under the Schedule. In the first place the auditors, but if they won't act, then an independent chartered accountant. There is specific provision for the basis of determining the Fair Value, in particular that there is to be no discount on account of the size of the shareholding or class of share. This was a significant concession by the First Defendant in the original negotiations as the Claimants' shareholding represented 10% of the Second Defendant's share capital and was further restricted by the class of shares.

The Shareholders Agreement ("SHA")

32. Finally, the Claimants and the Defendants entered into the SHA. The scheme of the SHA was that new articles of association of the Second Defendant was annexed to it. The shareholdings were divided into A ordinary shares (all owned by the First Defendant) and B ordinary shares (all owned by the Claimants). At completion the parties agreed to procure that the new Articles were adopted and that the new share capital structure would take effect – with the Second Defendant entering into the EAs with the Claimants.

33. Clause 9 makes provision for compulsory transfer of B shares and, so far as is relevant, is as follows:

> ***"9.2.1 Definitions***
> *Departing Shareholder means a B Shareholder in relation to whom an event specified in Clause 9.2.2 has occurred.*
> *Termination Date means the date upon which any of the events specified in clause 9.2.2 has occurred.*
>
> ***9.2.2 Events leading to compulsory transfers of B Shares***
> *Clause 9.2.3 shall apply if any of the following conditions are met in relation to a B Shareholder:*
>
> > *(k) he commits a material breach of any provision of this Agreement; or*
> > *(l) he commits a material breach of any provision of his Employment Agreement.*

9.2.3 Consequences of events leading to compulsory transfers of B Shares
If any of the events or circumstances listed in Clause 9.2.2 shall occur:

a) ……

b) *the Departing Shareholder shall forthwith cease to be entitled to exercise any rights to vote his B shares;*

c) *the A shareholder may within 30 Business Days of becoming aware of the event or circumstance constituting the B Shareholder a Departing Shareholder by notice in writing deem the Departing Shareholder to have given a Transfer Notice pursuant to Clause 9.3 in respect of all of the B Shares held by him as at the Termination Date (or such later date as determined by the A Shareholder) at the Prescribed Price, in which case all of the provisions of Clause 9.3 (Voluntary Transfers) shall apply to the deemed Transfer Notice save that: the Offered Shares shall comprise all the Departing Shareholder's Shares; and no intended Transferee shall be specified in the Transfer Notice and none of the provisions in relation to intended Transferees shall apply.*

9.2.4 Prescribed Price means:

a) *……*
b) *If the date of the deemed Transfer Notice is at any time before the second anniversary of the date of this Agreement the nominal value of the B Shares which are the subject of the Transfer Notice unless….."*

34. It was common ground between the parties at the trial that if the Claimants were Departing Shareholders, then the First Defendant could acquire their shareholdings at nominal value and not Fair Value.

35. Clause 12.1 provided further restrictive covenants on the part of the Sellers which I will refer to later.

The issues

36. In the Particulars of Claim, the case is pleaded as a "*contrived attempt*" by the First Defendant to avoid paying the Claimants a Fair Value under the OAs.

37. In paragraph 8 it is pleaded that it was an implied term of the EAs that the Second Defendant was under a duty of good faith and a duty not, without reasonable and proper cause, to conduct itself/himself in a manner calculated or likely to destroy or seriously damage the relationship of trust and confidence between employer and employee. The purpose of this pleading appears to be to enable the Claimants to argue that it was a breach of these duties for the Second Defendant (a) to investigate alleged gross misconduct on the part of the Claimants; and (b) to act upon any findings of gross misconduct if they came to light "*if its sole and principal motivation was to seek to avoid payments which would otherwise be due from the First Defendant under the SHA or the OAs*".

38. The Claimants contend that the restrictive covenants contained in the SHA are not enforceable (i) because they extend further than reasonably necessary; (ii) were not reasonable as between the parties; and (iii) the First Defendant is in repudiatory breach of the SHA. No particulars of repudiatory breach are pleaded in the Particulars of Claim and although the Defendants made an extensive request for particulars, this was not one of them.

39. The Claimants' pleaded case is that prior to their exercising the Put Options there were no disciplinary concerns raised about them by the Second Defendant. When the price was not agreed, they say that the Defendants "*engaged in a scheme to find any conceivable reason to dismiss them for gross misconduct and to support a finding that they had acted in Material Breach*". The ground shifted during the course of the disciplinary process and other grounds have been added subsequent to their dismissal. The Claimants say that they were wrongfully dismissed and that they are not in material breach of their EAs.

40. An issue appeared to arise between counsel as to the relevance of breaches of the EAs which came to light after their dismissals. It was not conceded by Mr. Quinn that these matters could be relied upon by the Defendants, and I will deal with what is, essentially, a point of law before I move on to the main issues.

41. The Defendants' case is very straightforward. They say that at the time the Put Options were exercised, the Claimants were Defaulting Shareholders because they were each in Material Breach of their EAs. It is also contended that they were each guilty of Gross Misconduct justifying their dismissal – although this is not relied upon as justification for treating them as Departing Shareholders.

42. The checks carried out on the Claimants were "*routine checks of the Claimants' respective email accounts to ensure that there had been no irregularities during the course of their employment*" and that in any event there were already concerns that one of the Claimants had been leaking confidential information to Solari Senior.

43. The Material Breaches and Gross Misconduct relied upon are divided into 3 categories as follows:

    a) Disclosing confidential information to Mr. Solari Senior, namely, board minutes, and improper preparation of the 2017 budget for the Second Defendant by Reverse Engineering;

    b) As against the Second Claimant, that he sent confidential information belonging to the Second Defendant to his personal email account without permission;

    c) As against the Second Claimant, that he accessed gambling and pornographic websites on his work laptop.

    d) As against both Claimants, that they used the Second Defendant's equipment or internet to send and receive sexist and pornographic messages via WhatsApp.

    e) The Cumulative effect of the breaches gives rise to a material breach or a repudiatory breach, even if the individual breaches do not themselves qualify on their own.

44. At the start of the trial an application was made to amend the Defence and Counterclaim. This possibility had been presaged by Mrs. Justice Yip when she ordered a speedy trial, and, having heard the arguments, I ruled that the amendment should be allowed. The amendments were not opposed save in so far as they related to the addition of allegations relating to a WhatsApp group (Breach D above). This group comprised male employees of the Second Defendant and the major complaint against the Claimants is that their participation as senior managers with younger and junior employees was a material breach and gross misconduct.

45. The Defendants counterclaim for a declaration that the restrictive covenants in the SHA and the EAs are valid and enforceable and a declaration that the OAs have been validly rescinded. Damages are claimed in the alternative.

The implied term point

46. Before I move on to consider the main issues in this case, I will deal with two matters:

    a. Are the Defendants under the alleged duty not to investigate the alleged misconduct of the Claimants and, if misconduct comes to their attention, prevented from acting on it. In short, even if the sole motivation of the Defendants was to avoid paying a Fair Value, does this prevent them from operating the Defaulting Shareholder provision? and
    b. Can the Defendants rely upon matters which were discovered after the purported dismissals of the Claimants to justify the dismissals and as Material Breaches even if they were not part of the case against them during the disciplinary process?

47. In his opening skeleton, Mr. Quinn said that it was common ground that there was an implied duty of trust and confidence between the Second Defendant and the Claimants. He identified the point of dispute as being: whether or not it was an incident of this duty that the Second Defendant was prohibited from both investigating and also acting upon any subsequent discovery of gross misconduct if its sole motivation was to avoid payments that would otherwise be payable? No authority was cited by Mr. Quinn for this proposition. The point was not developed in final submissions.

48. The point can be dealt with shortly. The ability of the Claimants to dispose of their shareholdings in the Second Defendant is governed contractually by the SHA which provides:

    "9.2.6 Save as set out in this Clause 9 or as provided in Clauses 10 or 11, a Departing Shareholder may not sell or dispose of his B Shares or any interest in them."

49. If the Claimants are Departing Shareholders, they have no right to dispose of their shares. They are either Departing Shareholders or they are not. In my judgment the motives of the Second Defendant or First Defendant cannot have any relevance to the issue of their being Defaulting Shareholders. Mr. Quinn's answer to this in paragraph 89 of his closing submissions isn't addressing the same point. Mr. Levey is not saying that Clause 9.2.6 prevents the implication of the terms, he says that there is an express term that the shares cannot be sold in these circumstances and you don't get as far as the implication of terms. I agree with this.

50. Furthermore, I cannot see any justification for there being an implied term (whether free standing, or as part of a duty of good faith, trust and confidence) which prevents the employer from investigating whether there has been gross misconduct or acting upon any findings that there has been. The Second Defendant's contractual entitlement is to acquire the shares at nominal value if the shareholders are Departing Shareholders having committed Material Breaches. It would be odd indeed if they could only rely on this clause once the Put Option had been exercised if evidence of gross misconduct fell into its lap and not if they took active steps to investigate. Even odder if, having established that there was gross misconduct they had to ignore it and override the express contractual provision of the SHA. The implication of the term would also negate the express term. A term is implied where it is necessary in order to make the contract work. There is no such necessity here where the contractual terms are clear.

51. This point doesn't therefore help the Claimants. Nor was any separate argument advanced alleging conspiracy.

Subsequently discovered breaches of the EAs

52. Mr. Levey submits that the second point is disposed of by the principle in **Boston Deep Sea Fishing and Ice Co v Ansell** (1888) 39 Ch D 339. This is that there is no requirement that grounds relied on to treat a contract as repudiated are not restricted to those that have come to the attention of the party at the time the contract is treated as repudiated. It can rely on matters which subsequently come to light. The principle is set out in Chitty on Contracts 24-014:

"The general rule is well established that, if a party refuses to perform a contract, giving a wrong or inadequate reason or no reason at all, he may yet justify his refusal if there were at the time facts in existence which would have provided a good reason, even if he did not know of them at the time of his refusal".

53. This applies to dismissals for gross misconduct. There are some exceptions, but no-one has suggested that they have any application in the present case, and they clearly don't. In **Reinwood Ltd v L. Brown & Sons Ltd** [2008] EWCA Civ 1090 the Court of Appeal approved the passage in Chitty and said that there was no reason why the principle should not be used in relation to facts known to the party at the time it refused to perform the contract, unless an estoppel could be established. Estoppel is not alleged in the present case.

54. In his closing submissions Mr. Quinn took a point based on Clause 9.2.3(c) of the SHA. This provides for the A shareholders to give written notice deeming the B shareholders to be Departing Shareholders. This must be done within 30 days of the A shareholders becoming aware of "*the event or circumstance constituting the B shareholder a Departing Shareholder*".

55. The only notices that have been sent are those dated 28th March 2019 to the Second Claimant and another to the First Claimant. The former identifies one Material Breach, namely: that on 27th January 2017 he shared the agenda for a board meeting of the Second Defendant with a third party. The only breach alleged against the latter was that he shared a board minute with a third party on 7th March 2017.

56. Mr. Quinn submits that, apart from these alleged breaches, it is not open to the Defendants to rely on any other breaches because no notice has been sent in relation to them.

57. Mr. Levey makes two points: Firstly, that this argument was only raised in final submissions and has not been pleaded; secondly, that the only requirement on the Defendants' part is to serve a notice and to establish that at that date there were Material Breaches. There is no requirement to serve a new notice every time a further Material Breach comes to light.

58. In my judgment, the point is squarely within the principles of **Boston Deep Sea Fishing**. Absent any express provision in the SHA, or any other agreement between the parties, restricting the Defendants to reliance only on those breaches expressly identified in a written notice, the Defendants, having served the notice, are entitled to rely on any other Material Breaches subsisting at the time of the notice, even if they are not referred to in the notice but known to them at the time the notice was served. None of the breaches now relied on by the Defendants could have been put right by the Claimants if they had been given notice as the damage (if it was sufficient to amount to a Material Breach or Gross Misconduct) had been done.

59. All that Clause 9.2.3(c) requires the Defendants to do is to serve notice "*if any of the events or circumstances listed in Clause 9.2.2 shall occur*". The subsequent reference to "*the event or circumstance constituting the B Shareholder a Departing Shareholder*" is any event which triggers the right to serve the notice. I do not read this as requiring the Defendants to list all such events – even if they are aware of others which they continue to investigate.

60. Mr. Levey referred to the judgment of Sales J in **F & C Alternative Investment (Holdings) Ltd v Barthelemy and Anr** [2011] EWHC 1731(Ch) which concerned put options. There was a provision in the relevant agreement entitling the defendants to a right to exercise a put option within the period of 3 months following discovery by either of them that the corporate member was in breach of any provision of the agreement in a manner that amounted to gross negligence or gross misconduct and which has a materially adverse effect. In paragraph 728 Sales J said:

> *"728 In ordinary circumstances, an innocent party who purports to accept a repudiatory breach and rescinds the contract is entitled thereafter to justify his conduct by reference to matters amounting to serious breach of the contract which were not referred to him at the time he rescinded the contract ……. I do not consider that there is any language in paragraph 7 of the Fourth Schedule sufficient to displace this ordinary rule. Although the paragraph refers to the right to exercise the Put Option within a period of three months "following a discovery …. That the Corporate Member is in breach of any provision", the object of that is to lay down a time limit within which matters have to be brought to a head by service of a notice in respect of any discovered breach of the Agreement, not to displace the usual rule that once matters are brought to a head by notice to terminate an agreement it is open to the terminating party to seek to justify the termination by reference to any breaches of the agreement that may have occurred up to that point and which have the requisite character (as repudiatory breaches or, in this case, as breaches which satisfy the criteria of seriousness set out in paragraph 1.7)".*

61. There is therefore nothing in Mr. Quinn's point, but even if there had been, I would have rejected it on the ground that it wasn't pleaded. The knowledge of the Defendants and whether it was sufficient to enable them to give notice was not an issue that was raised in the pleadings and they were not cross-examined on it. No application was made to amend the pleadings.

62. Apart from the restrictive covenant dispute, the main issue in this case is, in my judgment, whether the Claimants were in Material Breach of their EAs at the time the notices were served, and whether they committed Gross Misconduct in the course of their employment.

The witnesses

63. From the Claimants' side, I heard oral evidence from the Claimants themselves and Mr. Solari Senior. For the Defendants I heard from Mr. Johnson and David Nicholas, the financial controller of the Cathay Group and a director of the First Defendant. A witness statement had been served by the Defendants for Carl Baker, an employee of the Second Defendant. He did not give oral evidence and his statement covers his involvement in the WhatsApp group until January 2019. Whilst he describes the material which was distributed on this group, he does not state exactly which period he is referring to, nor say that it continued until he left the group. I was not told why he did not attend for cross-examination and although there were thinly veiled suggestions from the Claimants that he had given his statement under pressure, there was no evidence of this. Nevertheless, the only potential relevance of his evidence is to prove that the WhatsApp group continued to disseminate the same type of material after Mr. Stokes left the group on 25th January 2017. This is a potentially important issue. In these circumstances I am unable to give any weight to it.

64. I found the Claimants and Mr. Solari Senior very unconvincing witnesses.

65. The First Claimant described the management of the Second Defendant prior to the acquisition by the First Defendant. Mr. Solari Senior was not involved in the day to day running of the business, his office was in Colnbrook at his company, Ticco. Day to day control of the Second Defendant was with Mr. Osgood, who was based in Egham. The Claimants and Mr. Osgood had email addresses belonging to the Second Defendant and Mr. Solari Senior did not and only visited Egham every few months, being heavily involved in his other businesses. The First Claimant's evidence, which I accept on this point, was that he was not directly involved in the accounting and financial side. He managed the operations side of the business while the Second Claimant managed the distributions side.

66. Mr. Solari Senior and his son, the Second Claimant, were very prone to arguing what they perceived to be the Claimants' case and did not focus their answers as responses to the question asked. This itself weakens the reliability of their evidence. Both of them, particularly Mr. Solari Senior, persistently avoided answering the question by shifting their responses from the point.

67. In the course of cross-examination Mr. Solari Senior was taken through a number of emails which had been sent to him by Dan Stokes prior to the acquisition, but after discussions had commenced with the First Defendant. An email of 22nd September 2016 complains about the increase in his workload to carry out due diligence, but includes the following: "*In addition, I also feel extremely vulnerable as all the "additional uploads" and backdating of invoices which I get TOLD to do due to poor*

cash flow, no one else is putting their names to. If shit hits the fan I have already accepted in my own mind, I will be jobless as I fully expect to be the scapegoat". Mr. Solari Senior's response was to dismiss that there were any concerns being expressed: "*The document says to me that he had a full time job*" and that the letter caused him no concern. I will explain in more detail later what this email was really complaining about, but I simply don't believe that Mr. Solari Senior had no idea that Mr. Stokes was complaining about his involvement in irregular accounting practices.

68. In another email to Mr. Solari Senior dated 26th September 2016 Mr. Stokes refers to Mr. Solari Senior having told him that he would "*cover off*" the various items with an email. These were listed and it is clear from the email that Mr. Stokes was unhappy with these practices. When it was put to Mr Solari Senior that Mr. Stokes was asking to be "*covered off"* because he thought he was doing something wrong, Mr. Solari Senior's response was that he was just asking for an explanation that it was ok.

69. I am satisfied that Mr. Solari Senior has lied to the court in these answers and is trying to brush aside and downplay what he knew were Mr. Stokes' very real concerns. I am also satisfied that he was well aware at this time that various things that were being done at the Second Defendant at this time were improper and that he has come to court to try to avoid such a finding as he knows that it would be potentially damaging to the Claimants' case, and probably also to his own disputes with the First Defendant.

70. The Second Claimant has also lied to the court. An example of his reluctance to answer straight questions relates to an email Mr. Stokes send to the Claimants and Mr. Solari Senior on 21st March 2019, at a time that the Defendants say they were involved in Reverse Engineering the 2017 budget. Mr. Stokes says: "*See attached after discussions. Paul S and I have adjusted the numbers to show EBITDA as per highlighted in yellow, but can only get to 1,041,000 (not 1.2m)*". Instead of waiting for the question he started making a submission as to why, if they were trying to give a false picture of the budget, they would choose the higher figure. I found his attempts to deny that he attended a meeting earlier that day to discuss the figures wholly unconvincing and at odds with the email traffic.

71. The Second Claimant was also asked extensively about the way in which they reached the 2017 budget but his answers were totally unconvincing and he appeared unable to accept the obvious proposition, that the EBITDA figure would risk being objectively less accurate if one started with that figure and then worked backwards.

72. Finally, the First Claimant. He said that he was not involved in the accounting side, only providing an operating cost estimate for the purpose of the preparation of the budget. He also denied attending the meetings that the Defendants say that they all attended in order to work out the 2017 budget. Unfortunately, he was drawn into the Reverse Engineering and other matters.

73. The First Claimant was cross-examined about his knowledge of the alleged accounting irregularities and the Second Defendant's cash flow problems in the run up to completion of the sale. He was asked to look at a number of emails to him, during which Mr. Stokes confided in him about his concerns and the stress that he was feeling as a result. Over a lengthy period of cross-examination he was asked whether Mr. Stokes had confided in him that he was unhappy about having to backdate customer invoices and uploading other invoices in order to ameliorate the Second

Defendant's cash flow problems. As I will explain later, this was to enable the Second Defendant to draw down funds from the Royal Bank of Scotland (RBS) by creating invoices that were never sent to customers before those moneys were payable. Furthermore, the payment of receipts from customers into a separate account (the Second Accounting Irregularity), led to a significant "*gap*" between what the Bank was being told was being invoiced to customers and what was being received at the Bank.

74. Over this lengthy period, the First Claimant gradually conceded ground to Mr. Levey. He agreed that Mr. Stokes was under pressure and that there were cash flow problems but said he was not aware of the scale. Gradually he was forced to agree that he knew more than he originally admitted. On 23rd November 2016 Mr. Stokes forwarded to the First Claimant an email that he had sent to Mr. Solari Senior. This, in clear terms, shows that the Second Defendant had drawn down from the RBS £677,000 more from the invoice credit scheme than the actual invoices it received. The lack of explanation strongly suggests that the First Claimant well understood what Mr. Stokes was talking about. The tone of Mr. Stokes' emails to the First Claimant, and the way in which the latter shifted his ground during this cross-examination, lead me to conclude that he knew much more of what was going on than he is prepared to admit to the court. It is impossible to accept the First Claimant's explanation that Mr. Stokes was a worrier and a flapper and therefore his concerns could be discounted. It is quite clear that Mr. Stokes was seriously unhappy and, as I will explain later, for good reason.

The Law

Material Breach

75. In Dalkia Utilities Services plc v Celtech International Ltd [2006] EWHC 63 (Comm), Christopher Clarke J summarised the authorities and applicable principles in relation to material breach as follows:

a) A material breach is not the same thing as a repudiatory breach;

b) The breach must, however, be serious enough to justify the consequences provided for under the contract;

c) He cited with approval the judgment of Neuberger J in **Glodite v Jaspar Conran Ltd** (28 January 1998, The Times), who held that "*whether a breach of an agreement is "material" must depend upon all the facts of the particular case, including the terms and duration of the agreement in question, the nature of the breach and the consequences of the breach*".

d) He also cited **Fortman Holdings Ltd v Modem Holdings** [2001] EWCA Civ 1235, where the Court of Appeal emphasised the importance of "*the commercial context*" and the seriousness of the breach.

76. In **Phoenix Media Ltd v Cobweb Information Ltd** (unreported 16 May 2000) Neuberger J held that in considering whether a breach is "*material*" (in the context of a termination provision), a court should take into account (i) the actual breaches, (ii) the consequences of the breaches to the innocent party, (iii) the explanation for the breaches, (iv) the breaches in the context of the agreements, (v) the consequences of holding that the contract was terminated, and (vi) the consequences of holding that the contract continued.

Gross Misconduct

77. Gross misconduct is eponymous with repudiatory breach of contact (**Ardron v Sussex Partnership NHS Foundation Trust** [2018] EWHC 3157(QB) where Jacob J said:

"*The concept of "gross misconduct" in the employment law context connotes misconduct which justifies summary dismissal, and which therefore amounts to repudiatory breach of contract. There is no fixed rule of law defining the degree of misconduct that will justify dismissal. Gross misconduct may include, but is not limited to, dishonesty or intentional wrongdoing, for example: conduct which is seriously inconsistent with the employees' duties to his employer; or conduct which is of such a grave and weighty character as to amount to a breach of the confidential relationship between employer and employee, such as would render the employee unfit for continuance in the employer's employment, and give the employer the right to discharge him. The focus is on the damage to the relationship between the parties. Dishonesty and other deliberate actions which poison the relationship will obviously fall into the gross misconduct category, but so in an appropriate case can gross negligence".*

78. Mr. Quinn referred me to the decision of May J in **Richards and Purves v IP Solutions Group Ltd** [2016] EWHC 1835(QB) where he summarises the test to be applied in determining gross misconduct and also the meaning of "*material breach*". At paragraphs 34 and 35 she says:

"What constitutes gross misconduct by an employee will vary according to the nature of the employment and the circumstances under which the particular behaviour is said to have occurred. The test is unhelpfully, but necessarily, circular: gross misconduct is behaviour which is such as to so wholly undermine the relationship of trust and confidence between employer and employee that it justifies the employer in treating the contract as repudiated.

In **Williams v Leeds United FC** [2015] IRLR Lewis J summarised the approach as follows:

> *"In general terms in assessing the seriousness of any breach, it is necessary to consider all the relevant circumstances including the nature of the contract and the relationship it creates, the nature of the contractual term that has been breached, the nature and degree of the breach and consequences of the breach…in the context of contracts of employment, relevant circumstances include "the nature of the business and position held by the employee": see Jupiter General Insurance Co Ltd v Shroff [1937] 3 All ER 67 per Lord Maugham. The opinion of the Privy Council in that case recognises that immediate dismissal is, as Lord Maugham expressed it, a "strong measure" and there needs to be careful consideration of the evidence to determine whether the conduct is such as to amount to a repudiatory breach entitling the employer to dismiss the employee without notice".*

79. In relation to a contractual clause that permitted the employer summarily to terminate an employment if he committed a material breach, May J held that this had to be "*significant*".

80. I now turn to the individual breaches which the Defendants now rely upon as material breaches and gross misconduct.

Breach A: Discosure of confidential information and reverse-engineering the 2017 budget

81. The Defendant's case is that between January and March 2017, after completion of the acquisition of the Second Defendant by the First Defendant, the Claimants were parties to communications and discussions which involved the unauthorised disclosure of confidential information belonging to the Second Defendant to Mr. Solari Senior and that the 2017 budget was prepared by them improperly.

82. Since the Deferred Consideration under the SHA was calculated by reference to actual EBITDA figures, the Defendants have to put forward a reason for these actions. They put forward several reasons why Mr. Solari Senior and Mr. Osgood might want to be involved in the preparation of the 2017 budget:

    a. During the negotiations for the sale of the Second Defendant, Mr. Solari Senior had represented to the First Defendant that the EBITDA for the financial year following the acquisition was expected to be between £1m and £1.2m and that it operated at a margin of 24%. Therefore, when the EBITDA figure first put forward by Mr. Stokes in 2017 came to £678,783 steps were taken to produce a budget to be presented to the Second Defendant's board which matched, or was at least much closer to, the sum represented;
    b. The Claimants were aware that Mr. Solari Senior's interests were, potentially, adverse to those of the Defendants. This was because there were already concerns about financial information about the Second Defendant which had not been disclosed before the acquisition, for example: an undisclosed director's loan to Mr. Solari Senior of £183,066 which led to the First Defendant bringing a breach of warranty claim against him in respect of that director's loan and other matters, and obtained a default judgment in respect of the full amount of the claim.
    c. It was also in Mr. Solari Senior's interests and contrary to the Second Defendant's interests, that the First Defendant should not be encouraged to start investigating in greater detail the information provided to them before the acquisition and the way in which the Second Defendant had been run beforehand. The Defendants say that prior to the acquisition, Mr. Solari Senior had been involved in accounting irregularities and improper practices ("the Accounting Irregularities").

83. The basic facts relating to the allegation that confidential information had been forwarded to Mr. Solari Senior were not really disputed – they are clearly shown in the emails. The Claimants' case is firstly, that they were not involved in any Reverse Engineering of the 2017 budget (even if it was engineered which is denied) – it is for the Defendant to prove that any involvement was a Material Breach; secondly, that the Claimants were not involved in any of the alleged Accounting Irregularities; thirdly, any confidential information that was disclosed by the Claimants to Mr. Solari Senior was done in a context that does not amount to a Material Breach. The principal point that they made was that this was their first involvement in drawing up a budget, they wanted to impress the new owners and therefore involved Mr. Solari Senior because of his great experience in the preparation of budgets. They said that they saw nothing wrong in what they did. In his opening, Mr. Quinn stated that "*indeed there is*

actually an abundance of evidence that there were no information barriers in place" between the Second Defendant and Mr. Solari Senior post acquisition.

The disclosure of confidential information

84. In their oral evidence, both Claimants and Mr. Solari Senior accepted that the information disclosed to Mr. Solari Senior between January and March 2019 was confidential to the Second Defendant and should not have been disclosed without the Board's authorisation.

85. On 27th January 2017 David Nicholas, of the First Defendant, sent the Claimants the agenda for a Board Meeting of the Second Defendant on 3rd February 2017. The agenda listed "*invited attendees*" as including the Claimants and Mr. Osgood. Two of the items on the agenda were the 2016 performance and the 2017 Budget, which had not at that stage been prepared.

86. On 27th January 2017 the Second Claimant sent an email to Mr. Solari Senior, Mr. Osgood and the First Claimant, copying in Mr. Stokes. He pointed out the above items on the agenda and said: "*given the deal that has been done and started on 1st Jan 2017, do the budgets need to be amended to match that period*?". "*Have they seen any budget apart from 2016/17 budget which we are using at the moment*". "*I really want to make sure we impress at this meeting and get all our ducks in a row to get off to a good start*".

87. The First Claimant responded: "*I agree Roberto. We need to be on the same page going into the meeting*". Mr. Solari Senior responded that he was happy to help with the budget and a meeting was then suggested and set up by the Second Claimant for 31st January 2017 to discuss the budget. The attendees notified were the Claimants, Mr. Solari Senior and Mr. Stokes. The invitation described the meeting as the "*Cathay Board Meeting Agenda Review*" and it was to take place at Mr. Solari's office at Ticco in Colnbrook. The Second Claimant asked Mr. Stokes to bring any financial data for the 2016 budget and any budgeting that had been done since to the meeting. In fact no budget documentation had been prepared since the 2016 budget at this time. It is common ground that Mr. Johnson was shown a budget up to 30th June 2016 during the negotiations, but Mr. Solari Senior said that he had prepared one up to 30th June 2017 which he showed to Mr. Johnson. If he did, then no-one has produced it and Mr. Johnson denies seeing one. I am satisfied that only the budget to 30th June 2016 existed. The projected EBITDA of 1 to 1.2m given to Mr. Johnson by Mr. Solari Senior was not the result of any formal budget work.

88. The Claimants and Mr. Solari Senior deny that any meeting took place on 31st January 2017. When questioned about this, the First Claimant said that there had been discussions, but could not recall how they occurred – he said they might have been by phone. He also accepted that at the Board Meeting on 3rd February 2017 he had been the one reporting the figures to the Board and that these must have been given to him by Mr. Solari Senior, or someone else, what to say at this meeting. In the Reply, it is pleaded that the First Claimant was not sure whether it was he or Mr. Osgood who reported the figures to the Board, but that he does recall Mr. Johnson responding: "*Great, that matches the figures we have already given to the bank*". Another email from the First Claimant says that he could not make this date, and a new date of 24th February 2017 was set at All Bar One in Windsor. He volunteered that this had nothing to do with the meeting, but was a social meeting to celebrate the transaction.

89. The Second Claimant's oral evidence about this meeting was hardly a categoric denial that it took place: "*I have to agree with Paul [the First Claimant] these meetings – I tried to push for them often….. but he [Mr. Solari Senior] was so busy these meetings didn't happen*". He also accepted that whether or not there had been a meeting, there had been dialogue between them at this time. He then went on to suggest that Mr. Solari Senior was intended to attend the Board Meeting on 3rd February 2017. No-one else has suggested this, and there is no evidence to suggest that he was invited.

90. Mr. Solari Senior's evidence was that the meeting had not gone ahead at the time arranged, but that Mr. Stokes and Mr. Osgood had come over later that evening. He was questioned about how the meeting could have taken place without the Claimants present, since the purpose of the meeting was to ensure that at the Board Meeting "*everyone was on the same page*" and that the Claimants had approached him because they wanted to impress the new owners. He also said that he had looked at his diary and "*Cancd*" had been written against the meeting. He had been present in court throughout the trial and while the Claimants were cross-examined on this point. He has not produced the diary entry.

91. The evidence from these three witnesses is not consistent and not convincing. There was further unsatisfactory evidence that other meetings that the emails clearly show were arranged and imminent, did not take place. This meeting was set up with the specific intention that both Claimants would be present. Mr. Solari Senior was particularly unconvincing and was clearly lying. I find that the meeting did take place, although it is possible that some of the participants attended by phone, and that both Claimants and Mr. Solari Senior were present one way or another.

92. The Board Meeting went ahead on 3rd February 2017 and the Claimants, Mr. Osgood, Mr. Johnson and Mr. Chaing, amongst others, attended. One of the routine items agreed was to switch the Second Defendant's bank account from RBS to HSBC. Under "*2017 Forecast*" it was recorded: "*PNC have generated 2017 projections. £9.1m turnover and £1.2m EBITDA stand alone for PNC*". PNC is the Second Defendant. It was then agreed that a budget was needed for the 2017 calendar year and that Mr. Johnson would review this with Mr. Stokes. It was disputed who gave this figure at the meeting, the First Claimant denying that it was him.

93. Following this meeting, Mr. Stokes prepared a draft budget ("the First Draft"). This showed an EBITDA of £678,789.51. It was not shown to Mr. Johnson nor produced prior to or at the next Board Meeting.

94. On 7th March 2017 the First Claimant forwarded the minutes of the Board Meeting of 3rd February 2017 to Mr. Solari Senior, Mr. Stokes, Mr. Osgood and the Second Claimant, with a note saying: "*Budget Forecasts – We gave Cathay figures however need to put this into 12 month budget so visible to all parties (Dan Stokes can you review as discussed)*". He also pointed out that a second Board Meeting was due on 9th March 2017.

95. The agenda for the 9th March 2017 Board Meeting identified the Claimants and Mr. Osgood as invited attendees, and added Mr. Stokes. The minutes recorded that Mr. Stokes had completed the draft budget for Mr. Johnson to review. It was noted that they would review the draft budget and present it to the Board later.

96. On 13th March 2017 Mr. Stokes sent Mr. Solari Senior a copy of the draft budget, saying "*I have attached a budget that was discussed at the board meeting, and also the original numbers that we discussed with you and put together. Sales 9.1, EBITDA with 24% of Dist 1.2M*".

97. There followed an exchange of emails and on 15th March 2017 Mr. Stokes sent a second version of the budget ("the Second Draft") to the Claimants and Mr. Solari Senior saying: "*All, Amended budget with Temps adjusted. Maybe discuss tomorrow/Fri with a view to submit Fri COB*". Next, on 15th March 2017 Mr. Stokes emails the Claimants and Mr. Solari Senior and says he has spoken to the latter who suggest they all go over to see him the following week "*to finalise*". Mr. Stokes then set up a meeting for 21st March 2017 between 10.30 and 12.00 at Mr Solari Senior's office in Colnbrook. All 4 of them were to attend, but not Mr. Osgood. The next email is from Mr. Stokes to his father on 21st March 2017 at 11.00am. He states that he is meeting "*Geoff and Solari*" at 1.30 that day. This must be a reference to Mr. Osgood and Mr. Solari Senior. A second meeting notification was sent by Mr. Stokes to the Claimants, Mr. Osgood and Mr. Solari Senior for 1.30 that day and it was noted that no-one had responded. At 16.48 Mr. Stokes sent an email to the Claimants, Mr. Osgood and Mr. Solari Senior with an attached amended version of the budget ("the Third Draft"). He said: "*see the attached after discussions. Paul S, I have adjusted the numbers to show EBITDA as per highlighted in yellow, but I can only get EBITDA to £1,04100 (not 1.2m). Give me a call when you get a chance just to run through*".

98. The Claimants and Mr. Solari Senior deny that this meeting took place. The First Claimant said that it had been suggested that they meet but this never happened, but on 15th March 2017 he clearly anticipated that it would, because he asked Mr. Stokes to send him an "*invite if all OK for next Tuesday*". At 8.18 am on 21st March 2017 Mr. Stokes sent everyone an email attaching the draft budget "*for discussion later*".

99. The Second Claimant's explanation for not attending the meeting was that his father didn't want everyone to turn up "*mob handed*" and therefore the Claimants' presence was not needed. He was unable to explain at what stage he and the First Claimant had been told by his father that they need not or should not attend, notwithstanding that they had been notified on the day of the meeting that they should attend. Mr. Solari Senior's evidence was again particularly unconvincing. Firstly, he said that the meeting had been shifted again to 4.00pm and that only Mr. Osgood and Mr. Stokes had come over to his office. He later tried to retreat by suggesting that it was sometime after 1.00. If it was 4.00 then it did not give Mr. Stokes enough time to get to the Second Defendant's office in Egham and make the adjustment to the budget which he sent everyone at 16.48. He said the meeting had lasted 30 minutes or so and that it would take 5 minutes to get back to Egham. This was later changed to 15 minutes. I found all this very unconvincing.

100. The emails show that a meeting was set up that day – albeit that the timing was changed. Both Claimants expected to attend and the First Claimant had said that he would. They were included that morning in the circulation of the budget and no emails have been produced showing that there was any change of plan. One document referred to above refers only to "*Geoff and Solari*" but I am satisfied that there is overwhelming evidence that the meeting went ahead as scheduled and that all were present.

101. The final version of the budget ("the 2017 Budget") was sent by Mr. Stokes to the Claimants, Mr. Solari Senior and Mr. Osgood on 29th March 2017. This showed EBITDA of £1.18m. The First Claimant sent this version to Mr. Johnson on 5th April 2017 and this was the first version of the 2017 budget that Mr. Johnson had seen.

102. In cross-examination, the Claimants admitted that the documents that they had sent to Mr. Solari Senior between 20th January and the end of March 2017 were confidential and should not have been sent without authority. These comprised the agenda and minutes of the Board Meetings on 3rd February and 9th March 2017 and the financial information relating to the 2017 Budget. The First Claimant did not believe that he was doing anything wrong and the Second Claimant believed that he had a discretion to share confidential information with third parties. This is not usually the case with senior employees, unless specifically authorised, and no authority or discretion was given in this case. In my judgment, the Claimants continued to believe that they owed their loyalties to Mr. Solari Senior and the team that controlled the Second Defendant prior to the acquisition by the First Defendant, and had not taken on board that there was a new regime and that their duties now differed. They repeatedly referred to the Second Defendant as Cathay, failing to appreciate that Cathay owned the majority of the shares but that their duties were towards the Second Defendant and not the previous owners.

103. Nor was there any credible evidence that "*there were no information barriers in place*". In his witness statement, the First Claimant set out the documents that he relied on as demonstrating his point. When cross-examined he had to accept that not one of them provided that evidence.

104. It was suggested by the Claimants that the Second Defendant had withheld emails which supported their case on this point, but I am satisfied that Mr. Johnson understood the importance and need for a proper search on disclosure and carried out that obligation properly. There is no reason why Mr. Solari Senior could not have produced emails on his Ticco address supporting this case if any existed. He sat in court for most, if not the whole of the trial, and there is no reason to suppose that they would not have been produced if they had been helpful to the Claimants.

105. It was also contended by the Claimants that Mr. Solari Senior was allowed access to confidential information because of his ongoing involvement with the Defendants after completion of the acquisition. The First Claimant's evidence of this was set out in paragraph 47 of his witness statement, in which he refers to a number of emails. None of these emails establishes his point. One matter related to Mr. Solari Senior's involvement in a dilapidations claim in respect of the Second Defendant's warehouse in Kings Norton. This was because the sellers under the SPA were liable for these dilapidations and, naturally, had to be consulted. This simply doesn't get off the ground as justifying the receipt of the confidential information passed over.

106. I find that the confidential information was passed to Mr. Solari Senior without any authority (express or implied) from the directors or the Second Defendant. Apart from certain specific issues relating to the acquisition and the dilapidations, Mr. Solari Senior had no role with the Second Defendant. It was also suggested that Naresh Patel was aware that the Second Claimant was consulting his father about the budget, but there is no reliable evidence of this and I accept Mr. Johnson's evidence that Mr. Patel had no involvement in the budget beyond providing some information relating to the Amethyst business.

107. The Reverse Engineering and Accounting Irregularities issues are relevant to the issue of the seriousness of the disclosure of confidential information, which I will now turn to.

108. Mr. Quinn submitted that the Defendants' case rested "*to an unsustainable extent*" on the hearsay evidence of what Mr. Johnson says he was told by Mr. Stokes after the acquisition. When Mr. Stokes resigned from employment by the Second Defendant on 14th February 2019 he spoke to both Mr. Johnson and Mr. Nicholas, explaining in detail what the Second Defendant had been doing prior to the acquisition in order to deal with the cash flow difficulties. In particular at meetings on 14th March 2019 and 17th April 2019 (the latter at Dentons' offices when a note was taken by a solicitor at Dentons).

109. Mr. Stokes has not been called by either side to give evidence in this case and no formal statement has been filed. There has been no evidence to explain his absence. Mr. Quinn says that there are two important consequences of this: Firstly, he has not been able to cross-examine Mr. Stokes about the various budget drafts and the original EBITDA figure of £678,000 which he says is worthless and contained many mistakes. Secondly, there is no evidence of the Accounting Irregularities save from what Mr. Stokes told Mr. Johnson and Mr. Nicholas. Nor has he been able to put the case that Mr. Stokes was a worrier, who was out of his depth and not, as the Defendants say, stressed out by having to act improperly under pressure from Mr. Solari Senior. Mr. Wells described him as "*a bit of a flapper and worrier*". This begs the question, however, why?

110. I agree with Mr. Quinn, that great care needs to be taken before placing any reliance on hearsay statements of what Mr. Stokes told Mr. Johnson and Mr. Nicholas. The reason for his complaints in the emails was, if the Defendants' case is accepted on this, that he was being asked to do something improper. He therefore has a motive for apportioning the blame elsewhere. It is difficult, however, to see how if that was the case he would send such explicit contemporary emails to Mr. Solari Senior blaming him if he was the person solely in the wrong.

111. As I will explain later, the contemporary emails are both frank and clear in many respects and where there is little or no room for doubt about the conclusions to be drawn from them I will place weight on them.

The Reverse Engineering of the 2017 Budget

112. Mr. Solari Senior told the First Defendant in June 2016 that EBITDA for 2017 was predicted to between £1 – 1.2m and that the Second Defendant's distribution business operated at a profit margin of 24%. At the meeting on 31st January 2017 to discuss the budget for 2017, Mr. Solari Senior told the Claimants what he had told the First Defendant. This is to be inferred from the emails between the Claimants on 27th January 2017, the minute of 3rd February 2017 which records projected EBITDA for 2017 at £1.2m and Mr. Stokes' email to Mr. Solari Senior of 13th March 2017 (copied to the Claimants) in which he refers to the figures of 24% and 1.2m "*which we discussed*". This figure could only have come from Mr. Solari Senior as no budget had yet been prepared the Claimants had not been involved in the earlier negotiations, weren't aware of what the First Defendant had seen in the negotiations and there was no draft budget yet in existence. The first draft budget showed a much lower figure. Mr. Solari Senior suggested that he had prepared a draft budget for the period to June

2017 at the time of the negotiations, I reject this evidence. No copy has been produced and he did not show it to Mr. Johnson. The only budget he was shown before the acquisition was the budget to 30th June 2016.

113. Following the board meeting on 3rd February 2017 Mr. Stokes started to prepare the First Draft, which he circulated to the Claimants, Mr. Solari Senior and Mr. Osgood on 13th March 2017. This showed EBITDA of £678,000 odd and showed a profit margin of 8.2%. Mr. Solari Senior accepted that as Mr. Stokes would have used the previous year's figures as his starting point.

114. The draft budget then progressed as follows:

a) On 7th March 2017 the First Claimant sent the Second Claimant, Mr. Osgood and Mr. Stokes a copy of the Board Minutes for 3rd February 2017 and highlighted a number of matters arising. He copied it to Mr. Solari Senior. He did not copy it to Mr. Johnson (whom the minutes record as going to review the budget with Mr. Stokes). Under "*Budget Forecasts*" he says: "*We gave Cathay figures however needs to put this into 12 month budget so visible to all parties (Dan Stokes can you review as discussed)*". At that stage there was no draft budget in existence.

b) On 9th March 2017 Mr. Stokes produced the First Draft, which showed EBITDA of £678,789. This was sent to the others on 13th March 2017 as stated above.

c) Another Board meeting took place on 9th March 2017 at Dentons (after Mr. Stokes had produced the First Draft). This was not shown to the meeting as the First Claimant accepted in cross-examination. It was agreed that Mr. Johnson and Mr. Stokes would review the draft budget and present it to the Board in due course. The minutes of this meeting were not forwarded to Mr. Solari Senior. Shortly before the Board Meeting, there was a meeting between the Claimants and Mr. Stokes to discuss the budget.

d) The First Draft was sent to Mr. Solari Senior on 13th March 2017 attached to an email (copied to the Claimants) asking for his thoughts on it and the original numbers "*we discussed with you and put together: Sales 9.1, EBITDA with 24% of Dist 1.2M*". The First Claimant denies that he was involved in any discussions about these figures, other than providing the revenue figures for distribution. I reject that evidence as the emails show that he was closely involved throughout. He was at the very least a witness to discussions about these figures.

e) At the foot of the First Draft is a section headed "*ADJ'd EBITDA*". All the other figures in the spreadsheet remain the same, but the profit margin for distributions is increased to 24% showing an adjusted EBITDA of £1.211m. To get there, the profit from distribution sales had been increased

from £297,988 to £871,200 without the sales revenue increasing.

f) On 15th March 2017 Mr. Stokes emails Mr. Solari Senior and the Claimants the Second Draft stating "*Amended budget with Temps adjusted*" and suggested a discussion in the next 2 days. In fact, following further emails, the First Claimant emailed to suggest a meeting the following Tuesday (21st March). The only difference between this and the First Draft is that against Temp & Agency staff the figure has been reduced from £203,128 to £130,865. This gets the EBITDA to £751,045. The First Claimant could not think of a reason why it would be possible to make this reduction.

g) On 21st March 2017 there was another meeting with Mr. Solari Senior at his office, which I find was attended by the Claimants and Mr. Stokes. Earlier that day Mr. Stokes had emailed the Claimants, Mr. Solari Senior and Mr. Osgood with a budget template for the Second Draft "*for discussion later*".

h) At 16.48 on 21st March 2017 Mr. Stokes sent the Claimants, Mr. Solari Senior and Mr. Osgood an email attaching the Third Draft. In it he says: "*Paul S I have adjusted the numbers to show EBITDA as per highlighted in yellow but can only get EBITDA to 1,041,000 (not 1.2M)*". The first figure for EBITDA was £1,014 but there is a further adjustment of £27,000 for rent. The original ADJ'd table has gone and the £1.041m is described as the adjusted EBITDA.

i) On 27th March 2017 the First Claimant emails Mr. Stokes saying "*we need to button this up to submit. Then every month we need to have a meeting (internal) to discuss this month and numbers we are going to give to Cathay*". This was how the Claimants saw matters. That Mr. Johnson and Mr. Chaing were not to be regarded as directors of the Second Defendant, to whom all of them owed a duty, but as the other side in the acquisition.

j) Mr. Stokes then emails Mr. Solari Senior and the Claimants and Mr. Osgood reminding them that he can only get EBITDA to 1.04M "*and not the 1.2 that you previously expected as was talked about at the board meeting*". He attaches the Third Draft and asks him to tell him if any change was required.

k) On 29th March 2017 Mr. Stokes sends another email to everyone stating that he has "*tinkered with the sales slightly, so that we now show (near enough) 1.2M EBITDA as reported at the first Board Meeting.*". He attaches the Final Draft, which is the version given to Mr. Johnson by the First Claimant on 5th April 2017. The EBITDA is now £1,187,254. It has therefore increased by 75% as a result of this exercise in 3 weeks. The movement between the Third Draft and the Final Draft is achieved by increasing the distribution revenue by £70,000, reducing distribution costs by £75,000 and thereby increasing gross profits by £145,000. The First Claimant initially accepted that he could not recall any significant changes in the business or his understanding of it during those 3 weeks, although he then suggested that further business may not have been taken into account in the earlier drafts as a result of the business that was expected to come from a subsidiary of the First Defendant. This explanation doesn't fit with the figures for freight staying the same.

115. There cannot be any doubt that the 2017 Budget was approached from a starting point that Mr. Solari Senior had told Mr. Johnson before the acquisition that EBITDA would be £1.2m and that this was the figure that should be in the budget. Apart from Mr. Stokes' First Draft, all the subsequent adjustments were made in order to try to reach this figure. The email chain makes this quite clear. Although Mr. Solari Senior said that Mr. Stokes had made some basic errors when he produced the First Draft, this simply doesn't stand up to scrutiny. In the first place, he said that the profit margin for distributions was always 24%. If that was the case, then there was no need to adjust the other figures. Nor is it likely that the Financial Director of the Second Defendant, who had prepared the 2016 budget, would make such a basic error. If there were obvious errors then Mr. Solari Senior would have pointed them out at the start of this process and the Final Budget would not have been arrived at by the circuitous route that it was.

116. It is clearly wrong in principle when preparing a budget to start with the EBITDA figure and then adjust the other figures in order to justify it. The EBITDA has to be the product of the input of the other figures arrived at independently. In this case the other figures were changed arbitrarily – as with the 35% cutting of temp and agency costs and the increase of distribution sales. Although Mr. Solari Senior and the Claimants attempted to provide explanations for these changes, they were totally unsubstantiated and unconvincing. The best that they could do was to say that the actual figures were higher at the end of the day. That itself was disputed by the Defendants, but the relevance of the Reverse Engineering to this case is not affected since the issue is the seriousness of the disclosure of confidential information (judged at the time of the disclosure).

The Accounting Irregularities.

117. The relevance of this issue is that the Defendants say that it provides a motive to Mr. Solari Senior to Reverse Engineer the 2017 Budget EBITDA figure. Therefore, it is submitted, the Claimants, Mr. Stokes and Mr. Osgood were parties to produce the figure he had represented to Mr. Johnson before the acquisition in order to prevent the Defendants from finding out about the Accounting Irregularities.

118. The Defendants say that the Accounting Irregularities were the way that the cash flow difficulties that the Second Defendant had prior to the acquisition were dealt with.

119. There are 4 questions that arise:

> a) Were there cash flow problems at the Second Defendant in late 2016 and early 2017?
>
> b) Were false invoices and credit notes raised in order to enable the Second Defendant to draw down on its RBS invoice discounting facility?
>
> c) Were invoices backdated in order to cover up the diversion of funds from the RBS scheme to the Second Defendant's current account?
>
> d) What, if anything, did the Claimants know about this?

120. On the evidence, there can be no doubt that the Second Defendant had significant cash flow difficulties in late 2016 and early 2017. The First Claimant accepted that he was aware of this in cross-examination. The difficulties are very clearly borne out by the emails between Mr. Stokes, Mr. Solari Senior and the First Claimant. In an email from Mr. Stokes to his father on 4th January 2017 he graphically describes the situation: "*I'll call tonight … But bank on lock down as over-drawn, people screaming for dosh, and deal still waiting to be signed*".

121. Mr. Solari Senior said that he had the cash available to keep the business afloat, but it is clear that he was relying on the deal going ahead in order to solve the cash flow. Whether this was the case or not was not fully tested, but not of any great significance. The emails make it very clear that the Second Defendant was struggling to pay its bills as they came due. One particularly poignant example was an email sent by Mr. Stokes to Mr. Solari Senior and copied to the First Claimant in which he says that a driver is heading to the airport for a pick-up of goods and that they haven't yet cleared the import duty payment required to release the goods from bond *"…this is the most desperate we have ever got and this close to the deal do we want any customers walking*". The First Claimant firstly said this was exaggeration and downplayed it as Mr. Stokes panicking, but then drew back from that and recognised that there was "*clearly an issue*" and "*it's not even like we had £1 in the bank – he probably would have some money but not enough…*". He accepted that he knew that suppliers and people who were trying to get paid were "*screaming for money*" and in answer to my point to him that the company was "*at the cliff edge*" he replied: "*it was difficult, yeah*".

122. The Second Defendant had a discount facility with RBS to enable it to draw funds against invoices to customers ahead of payment. Under the arrangement, funds could be drawn from an account at RBS based on unpaid invoices. At the end of each month there was a reconciliation based on actual receipts and any invoice payments from customers were to be paid into a designated trust account.

123. What the Second Defendant did in order to cover the cash flow difficulties, was to issue invoices mid-month, but not send them to the customer. At the end of the month that invoice would be cancelled and another invoice for the same sum sent out to the customer. In this way the Second Defendant was able to draw funds under the discount facility earlier than it would otherwise have been able to do. Mr. Stokes explained this to Mr. Johnson and Mr. Nicholas and his evidence is therefore hearsay, but the documents show that this was what actually happened, as confirmed by Mr. Johnson in his first witness statement. Invoices were raised mid-month for particular customers at an estimated amount, and a credit note followed by a new invoice to the same customer at the month end. A number of customers were involved, with the most for Rapha Racing Ltd, the Second Defendant's biggest customer.

124. Mr. Johnson's evidence is that Mr. Stokes had told him that the Claimants had full knowledge of this, but the weight to be attached to this must be judged against all the other evidence and circumstances with care, even if I accept, as I do, that this is what Mr. Stokes said. In particular, the Claimants have not been able to cross-examine him on the statement attributed to him in the note of the meeting on 17th April 2019 that the First Claimant was not involved.

125. I am satisfied from other evidence that the Claimants were well aware of this practice. The First Claimant at first downplayed his knowledge of the seriousness of the cash flow difficulties, but I do not accept this and find that he was aware of it. The email evidence that he was is overwhelming. He accepted that he was aware that invoices were being sent out mid-month based on estimates and he also knew that fresh invoices were being sent out at the end of the month. He said that he didn't think this was improper. The emails sent to him by Mr. Stokes which I have referred to above, if he read them which I am sure that he did, made it quite clear to him that this was improper and that it was an internal matter. The Second Claimant was also aware of this practice but said that he did what Mr. Stokes or the Bank or customer told him to do and didn't think it improper. He suggested that some customers "*wanted a foresight of what their invoices were going to be*". This is not credible as it would be sufficient to produce a figure of projected costs without issuing an invoice and later give a credit note. I also reject this evidence and find that he knew that it was improper and done in order to get round the cash flow problems. It is simply not credible that he could think this proper or that the RBS knew and agreed it.

126. Mr. Solari Senior gave a long and elaborate, and wholly incredible, account of how Rapha had requested this system and how it was for its benefit. He then accepted the following: (1) only invoices that were due and payable were acceptable to RBS under the discount facility; (2) the invoices issued mid-month and then re-credited were not due and payable; (3) these invoices were not the ones that the customer was being asked to pay. These answers made a nonsense of his long explanation.

127. I find that the Second Claimant knew perfectly well that it was improper, why it was being done and that even if the customer didn't suffer any loss, it enabled the Second Defendant to benefit under the RBS discount facility without the latter knowing.

128. The second Accounting Irregularity involved making payments from customers directly into the Second Defendant's current account, circumventing the RBS designated trust account required to be used under the discounting facility. This meant that RBS was not aware of these payments because they were not used in the monthly reconciliations, and it would appear that the debts remained outstanding. It could therefore draw on the facility but when it received the money from the customer it did not have to account back for the receipt, improving cash flow.

129. Mr. Johnson says that Mr. Stokes told him that in order to conceal this from RBS he created false accounting records for RBS so that the figures matched by backdating subsequent invoices. This had the effect of falsely inflating the amount of the aged debt at the month end. The correct figures were restored in the Second Defendant's internal accounting records. Although I cannot give full weight to this hearsay evidence for reasons already given, Mr. Johnson refers to spreadsheets which Mr. Stokes gave him, which evidence I accept. There is also clear evidence in the emails in late 2016 that Mr. Solari Senior, Mr. Osgood and the First Claimant were well aware of this practice and that at each month end it became increasingly difficult to reconcile the figures to RBS. For example:

a) 22nd September 2016 – Stokes to Solari Snr and Osgood: "*In addition I feel extremely vulnerable as all the "additional uploads" and backdating of invoices which I get TOLD to do due to poor cash flow, no-one is putting their name to. If shit hits the fan I have already accepted in my own mind, I will be jobless as I fully expect to be the scapegoat*".

b) 26th September 2016 – Stokes forwards to the First Claimant an email he had sent to Solari Snr and Osgood in which he refers to "*various uploads to RBS Facflow, over and above the invoiced amounts to cover payroll and ease cash flow wher I came to you for advice etc*"; "*back date invoices in Sage in order to balance the books for MER reports for last 4 reporting months; Raise 2 invoices to Allianz Shipping … in order to receive funds into RBS account to clear off Part of Tuvia Invoices; Upload addition funds again in order to rtf funds to the same value as Allianz Shipping receipt, and pay to Polar Foods Limited £126,383.40*".

c) 1st December 2016 – Stokes to First Claimant, Solari Snr and Osgood: "*AS expected, Facflow reserves due to target have swung. This month's target is 1.9m! we don't even have 1.9m worth of debtors!! So we will have this issue next month, potentially bigger! Just to keep you update more than anything. So we will need to bill out 250K before we can start to draw down again. I expect a call from RBS today regarding this, and all the contras on the MER, so (w)ill fend them off for the time being. I won't know until 15th but hoping to claw a few grand back of the diff this month, but if this deal happens I guess it goes away?!*".

130. The answers to the first 3 questions in paragraph 117 above are therefore: Yes, yes and yes. This leads to whether the Claimants were aware of these practices and their impropriety.

131. Although I have not heard from Mr. Stokes, unless the contents of his emails are pure invention (and I can think of no conceivable reason why this would be the case in 2016 and 2017) he quite clearly felt that he was being asked to do things that he thought were improper and that when "*the shit hit the fan*" he would be the one in the firing line.

132. The Claimants argue that they didn't know that there was anything wrong with these practices. I find that each was well aware that the RBS was being misled about the amount of money coming in from customers and that the second Accounting Irregularity was designed to mislead it so that cash flow could be protected during this very difficult period.

133. Mr. Solari Senior was well aware of this practice having received Mr. Stokes' numerous emails. His suggestion that these were merely an expression by Mr. Stokes of complaint at being overworked and that he didn't understand invoice discounting cuts no ice. Although he gave another lengthy explanation why the practice was legitimate, this was also totally unconvincing and failed to explain how the gap (between actual receipts and what RBS were told were the receipts) would be closed legitimately.

134. I am satisfied that both Claimants were well aware of the second Accounting Irregularity, even if they had not been directly involved in creating it in the first place. In a sustained period of cross-examination about this area of the case the First Claimant moved his position significantly. He started by stating that he was only generally aware of cash flow difficulties and denied that Mr. Stokes was sending him emails because he was concerned about propriety. He then accepted that he was aware of cash flow problems and was being asked to bill as much as possible. He then accepted that he was aware of the gap (between invoiced bills and actual receipts) but not the amount. He never accepted the amount but that is not a sustainable position on the documentation. He also started by denying that he was aware of the RBS facility but this is also unsustainable on the documents that he received and his answers later when he accepted that he was aware that the RBS facility could no longer be drawn down.

135. The Second Claimant acknowledged that he was aware of the first Accounting Irregularity and his suggestion that he didn't think it was improper is untenable. It is not necessary to be an accountant to understand the impropriety – the creation of a false impression to a third party (the RBS) to cover the cash flow problems. It is improbable that his father, the First Claimant, Mr. Stokes and Mr. Osgood were all aware of the second Accounting Irregularity and that the Second Claimant was not. During the trial Mr. Nicholas produced an email which Mr. Johnson had sent him on 14th March 2019 following a meeting with Mr. Stokes. In it Mr. Johnson records that Mr. Stokes told him at the meeting that both Claimants would have been aware of the second Accounting Irregularity. Mr. Stokes' account of the irregularities is backed up by the documentation, showing that it is true. This statement therefore provides additional evidence that the Second Claimant knew.

136. In his final submissions Mr. Quinn made much of the fact that the Defendants had not contacted RBS to ask it to confirm that it did not know about the alleged deception. These proceedings have been prepared in something of a rush (issue on 30th May 2019 with speedy trial directed on 10th June 2019 and commencing on 23rd July 2019). The

RBS was no longer interested as it had been paid off and, in the context, this criticism is not of any significance.

The Claimants' knowledge

137. I am therefore satisfied that the Claimants were aware of the Accounting Irregularities and of the representation by Mr. Solari Senior as to EBITDA of £1-1.2m at the time they were starting to prepare the 2017 Budget and when they disclosed the confidential information. They were also aware that the 2017 Budget was being prepared without transparency and with a view to ensuring that it matched the figure given by Mr. Solari Senior before the purchase, the £1.2m reported to the board meeting on 3rd February 2017 and against a background of the severe cash flow problems and Accounting Irregularities prior to the acquisition of the Second Defendant. They were not actively involved in drawing up the final version, but they were full participants in the process and had initiated the involvement of Mr. Solari Senior. While I accept that neither Claimant had any experience of drawing up a draft budget, and did not actually produce the drafts, they attended meetings for the purpose of lifting EBITDA to £1.2m, were copied into important emails and were fully aware of what was going on. I am satisfied that they did this because they wanted to make sure that what had been represented to the First Defendant before the acquisition tied up with the Budget and reduce the risk that the First Defendant would look any more closely at the pre-acquisition position and discover the Accounting Irregularities and cash flow crisis.

138. It was suggested that prior to the acquisition due diligence was carried out and therefore there was nothing to hide. There was something to hide and the due diligence failed to unearth it.

139. Mr. Quinn made much of the fact that the representation of EBITDA had been "£1 – 1.2m" and therefore if the 2017 Budget was prepared improperly it is odd that those involved didn't stop at £1m. There is nothing in this point. They set the bar at £1.2m on 3rd February 2017 and stuck to it. The relevant matter is that the figure bore no resemblance to the right figure which Mr. Stokes produced in the first draft.

Breach B: Second Claimant sending Confidential information to his personal email

140. It is common ground that the Second Claimant sent information from his Second Defendant email account to his personal email account. This meant that the Second Defendant had no means of knowing thereafter what happened to that information. He did not ask anyone for consent to do this.

141. The transmission of information was as follows:

a) On 10th December 2018 he sent confidential information;

b) On 12th December 2018 he sent two separate emails attaching the Second Defendant's Actual v Earnout budget and other confidential information relating to the Second Defendant;

c) On 11th January 2019 he sent the Second Defendant's summary December Budget;

d) On 22nd February 2019 he re-sent the email dated 10th December 2019 attaching confidential information.

142. The Second Defendant's explanation for the above is that he needed the information in order to speak to his lawyers and accountants regarding the fair value of his shareholding in the Second Defendant. At this time discussions were taking place between the parties about the valuation of his shares. Mr. Johnson says that the information transferred goes beyond what was required for this purpose and that in any case, consent ought to have been obtained, and would probably have been given provided safeguards were attached to ensure that the information remained under the control of the Second Defendant.

143. The confidential information included information about some of the Second Defendant's most important customers and the profits being made on that business. The Second Claimant agreed in cross-examination that this information was "*highly confidential*". He also agreed that once it had been transferred the Second Defendant lost control over it and it could be transferred to 3rd parties without the Second Defendant knowing. The Second Claimant's explanation was that he believed this was "*ok*".

144. Although Mr. Johnson said in his witness statement that he is far from convinced that the information was needed for the share valuation, he stops short from saying that it was not. There is no evidence that it was intended for use for any other purpose.

145. I therefore conclude that highly confidential information was transferred to the Second Claimant's personal account without consent and in breach of the EA.

Breach C: Laptop pornography and gambling of Second Claimant

146. This allegation against the Second Claimant is that he accessed pornography and gambling sites on is work laptop on 20th December 2018. The print-out shows viewings of pornographic material between 1.39pm and 1.44pm and again for 4 minutes at 5.44pm plus one visit to an online betting site.

147. The Second Defendant explained this as an elaborate "*prank*" by other members of staff – it is an open plan office. The timings and length of viewing are inconsistent with his "*prank*" explanation and the viewing coincided with his viewing his emails. There was also evidence that the viewer had scrolled through several videos before selecting one. I therefore find that the Second Claimant did view pornography as alleged, in an open office.

148. In his oral evidence the Second Claimant conceded that this would amount to serious misconduct by a senior employee unless it was in the context of a prank. I agree.

Breach D: The WhatsApp Group

149. Following the dismissal of Mr. Stokes as an employee of the Second Defendant, a search was carried out of his mobile phone data. This revealed a WhatsApp group entitled "*Work*" of which he, the Claimants and several other more junior male employees were members. The group was set up on 23rd November 2016 and the latest evidence available about it is dated 25th January 2017, when Mr. Stokes left the group. There is no evidence of whether the group continued after this and, if so, what material was distributed.

150. I have no doubt that prior to Mr. Stokes leaving the group, various messages and photographs were put on it of a highly sexist, offensive, obscene and pornographic nature. There were also comments of a banterous nature of which no complaint is or could be made. I have not viewed the material, as it is adequately described in the evidence. Much of the material was sent during working hours using mobile phones belonging to the Second Defendant. The background context is that the members work in an open office, in which female employees also work. Some of the comments made on the group were not just of an offensive nature towards women in general, but made specific reference to 2 female employees working in the same office of an obscene and offensive nature.

151. On 3rd July 2019 there was a discussion between the Defendants' solicitor and the Claimants' solicitor about practical issues of disclosure in the case, in the course of which the WhatsApp group was mentioned. The group was closed that day. What led to this is not in evidence and a matter of speculation, which I will not enter into.

152. Mr. Levey submits that the court should infer that similar messages continued to be uploaded onto the group after Mr. Stokes left it and up to its closure. He says that by participating (actively or passively he says is irrelevant) as senior employees was a serious breach of duty by the Claimants (1) by undermining the positive and harmonious working environment and (2) creating, encouraging or contributing to a working environment which was intimidating, hostile, degrading, humiliating and offensive for other employees. The fact that the relevant "*other employees*" were unaware of this is neither here nor there. They might get to hear and the whole tenor of the WhatsApp created and encouraged a completely unhealthy office environment.

153. I would have no difficulty in finding that the above duties existed nor that the Claimants would be in breach by participating in a WhatsApp group distributing the material described. They were obviously embarrassed at the disclosure and agreed that it did not air well in a courtroom. If it had been proved that the WhatsApp group continued in the same vein after Mr. Stokes departure, then I would have found that there had been a serious breach of these duties amounting to gross misconduct and a Material Breach. In a modern office environment this is not banter but wholly unacceptable, particularly when commenting on female colleagues, and this is not something that a senior manager should be part of nor condone or permit.

154. However, the Defendants have not been able to prove that the group continued after 25th January 2017 as it had before. It is not enough to say that a leopard does not change its spots. Actual proof is required, or at least strong circumstantial evidence from which inferences can be drawn. If this had not been a speedy trial this evidence might well have been available, by examination of the other phones, but, pragmatically, the Defendants did not press for specific disclosure and did not request an adjournment. The only evidence therefore relates to a period of 4 days following the signing of the EAs and to the period prior to the EAs. The First Claimant put a pornographic clip on the WhatsApp group on 21st January 2017 and the Second Claimant on 25th January 2017. One of these was of a Buzz Lightyear toy holding a man's penis. That, in my judgment, was a breach of the duty but as there is no evidence that it was repeated thereafter, not sufficient to amount to gross misconduct or a Material Breach. In final submissions Mr. Levey accepted that unless I found that the WhatsApp group continued to post the material previously posted after 25th January 2017, then this would not be sufficient.

Conclusion on Material Breach and Gross Misconduct

155. Applying the principles set out in the authorities which I cited earlier I am not satisfied that the breaches under grounds B and C, although serious misconduct, are either Material Breaches nor Gross Misconduct. I am however satisfied that the breaches under A were both Material Breaches and Gross Misconduct amounting to repudiatory breach of the EAs.

156. In relation to ground A, I am satisfied that the Claimants shared confidential information with Mr. Solari Senior and did not do so unwittingly, or naively, but in order to give him oversight of the 2017 Budget so that the pre-acquisition representations were in line with the budget figures. If they had simply not acclimatised to the new ownership of the Second Defendant, but acted naively or in ignorance, then that might have been a different matter, but they went into it deliberately for a purpose that was totally inconsistent with their duties to the Second Defendant. This was a serious breach which went to the heart of the employer/employee relationship.

157. Both Claimants were aware that Mr. Solari Senior's interests were potentially adverse to the Second Defendant's. Even if they were not aware of the litigation between him and the Defendants, they were aware of the Accounting Irregularities and the significant discrepancy between Mr. Stokes' initial EBITDA figure and the sum represented in June 2016. They were aware that Mr. Solari Senior's interests conflicted with those of the Second Defendant – particularly in not rocking the boat with regard to the EBITDA representation and the Accounting Irregularities and cash flow difficulties. They participated in meetings with Mr. Solari Senior at his Ticco office, of which the directors of the Second Defendant were ignorant, in order to discuss how to arrive at the version of the 2017 Budget that could then be shown to Mr. Johnson. Mr. Johnson was unaware that Mr. Solari Senior was involved in the production of the 2017 Budget and why. The preparation of the 2017 Budget was undertaken in a way that prevented Mr. Johnson and Mr. Chang seeing it or having any knowledge of how it was being prepared until they were handed the final version.

158. This was a very serious breach of confidentiality, and a Material Breach – even when judged with regard to the consequences to the Claimants. Even if the actual EBITDA for 2017 exceeded the 2017 Budget figure, this is irrelevant and no-one knew whether this would be the case in early 2017. Budgets are important, and as Mr. Johnson explained, important documents to be shown to the Second Defendant's bankers. If there is no confidence in a budget then that can be significant.

159. The consequence of all this to the Defendants was that the Claimants could no longer be trusted at all with the Second Defendant's confidential information or with acting in the interests of the Second Defendant and, in particular, in providing financial information for the Second Defendant. Their loyalties were firmly with the "*old guard*" and not to their employer.

160. The consequence to the Claimants is severe, because they are Defaulting Shareholders. Set against this is the seriousness of the breach, and that they agreed to this term in the SHA and therefore the potential consequences. This was the price that was agreed for the shares in the event that they were Defaulting Shareholders.

Wrongful dismissal

161. The Claimants' conduct under Ground A was deliberate and a serious breach of the duty of confidentiality to the Defendants. They were not acting with regard to the Second Defendant. Their conduct undermined the whole basis of trust between employer and employee with the potential for undermining the trust and confidence of the Second Defendant's bank. In acting as such, the Claimants had no regard to their duties to the Second Defendant but were motivated by a misplaced loyalty to Mr. Solari Senior and a desire to put off the day when the previous improprieties in the running of the Second Defendant came to light, or perhaps avoiding it altogether if the trading figure improved as expected following the acquisition.

162. In my judgment, the Second Defendant was entitled to dismiss the Claimants summarily.

The restrictive covenants

163. The Claimants claim a declaration that the restrictive covenants in clause 1.2 of the EAs and clause 12 of the SHA are unenforceable. There is a counterclaim in which the Defendants seek a declaration that they are enforceable. The relevant EA clauses are as follow:

> *1.1 In order to protect the Confidential information and business connections of the Company and each Group Company to which you have access as a result of your employment with the Company (or any Group Company), you must not:*
>
> a) *for twelve months after the Termination solicit or endeavour to entice away from the Company or any Group Company the business or custom of a Restricted Customer with a view to providing goods or services to that Restricted Customer in competition with any Restricted Business;*
>
> b) *for twelve months after Termination, offer to employ or engage or otherwise endeavour to entice away from the Company or any Group Company any Restricted Person;*
>
> c) *for six months after Termination, be involved in any Capacity with any business concern which is (or intends to be) in competition with any Restricted Business;*
>
> d) *for twelve months after Termination be involved with the provision of goods or services to (or otherwise have any business dealings with) any Restricted Customer in the course of any business concern which is in competition with any Restricted Business;*
>
> e) *at any time after termination, represent yourself as connected with the Company or any Group Company in any Capacity, other than as a former employee, or use any registered business names or trading names associated with the Company or any Group Company.*
>
> *1.2 None of the restrictions in paragraph 1.1 shall prevent you from:*

a) holding an investment by way of shares or other securities of not more than 5% of the total issued share capital of any company, whether or not it is listed or dealt with on a recognised stock exchange;

b) being engaged or concerned in any business concern insofar as your duties or work shall relate solely to geographical areas where the business concern is not in competition with any Restricted Business; or

c) being engaged or concerned in any business concern, provided that your duties or work shall relate solely to services or activities of a kind with which you were not concerned to a material extent in the twelve months before Termination.

1.3 The restrictions imposed on you by this agreement apply to you acting:

a) directly or indirectly; and

b) on your own behalf or on behalf of, or in conjunction with, any firm company or person.

1.4 The period for which the restrictions in paragraph 1.1 apply shall be reduced by any period of time you spend on gardening leave immediately before Termination.

1.5 …..

1.6 Each of the restrictions in this letter agreement is intended to be separate and severable. If any of the restrictions shall be held void but would be valid if part of their wording were deleted, such restriction shall apply with such deletion as may be necessary to make it valid or effective.

164. The Claimants' plead that these Restrictive Covenants are not enforceable on 3 grounds:| (i) because the Second Defendant cannot show that they extend no further than reasonably necessary to protect its legitimate business interests; (ii) they were not reasonable between covenantor and covenantee; and (iii) there has been a repudiatory breach of the EAs by the Second Defendant.

165. The relevant part of clause 12 of the SHA is phrased slightly differently:

12.2.1 Each covenantor covenants with each other Shareholder and the Company (….) that he shall not, and shall procure that no Restricted Person in relation to him shall, whether directly or indirectly, alone or jointly with or on behalf of any other person or as principal, partner, agent, shareholder, director, employee, consultant or otherwise howsoever:

a) *at any time during the Restricted Period or for a period of one year thereafter:*

a) carry on or assist with or provide advisory services in connection with or be interested in any Restricted Business within the Restricted Area; or

b) supply or procure or assist the supply of any Services to any Customer or Prospective Competitor within or for delivery or supply within the Restricted Area; or

c) solicit (or procure or assist the solicitation of) the custom of any Customer or Prospective Customer in respect of Services for delivery or supply within the Restricted Area; or

d) offer employment to, employ, or offer or conclude any contract for services with or solicit the employment or engagement of any Key Person or procure or assist any third party to do any of the foregoing; or

b) *at any time after the date of this Agreement, use any corporate or trading name, mark or style which may suggest a connection with any Group Company or which is similar to any corporate or trading name, mark or style used by any Group Company.*

166. Customer means any person who is or was a customer or client in any Group Company at any time during the Restricted Period. The Restricted Period is the period from the date of the SHA to the date the Claimant ceases to be a shareholder in the Second Defendant. Prospective Customer means any person who is or has been engaged in negotiations with any Group Company with a view to becoming a customer or client. Key Person means any director of any Group Company or any employee with a gross annual remuneration of more than £30,000 at any time during the Restricted Period. The Restricted Area is the UK. The Restricted Business is the supply of any Services or other business competing with the business of the Second Defendant or any Group Company. Services is defined as: third party logistics, e-fulfilment, warehousing and freight forwarding services and all other services of the nature of the type supplied by any Group Company.

167. The Claimants plead that these covenants are not enforceable for similar reasons as they advance for the EA covenants.

The Law

168. It is common ground that if the Defendants are in repudiatory breach of the EAs or the SHAs then they cannot enforce the Restrictive Covenants contained in the repudiated contract. This issue no longer arises in view of my decision that the Claimants were not wrongfully dismissed.

169. Mr. Quinn referred me to **Chitty on Contracts** (32nd edition) at para 16-085:

"All covenants in restraint of trade are prima facie unenforceable at common law and are enforceable only if they are reasonable with reference to the interests of the parties concerned and of the public. Unless the unreasonable part can be severed by the removal of either part or the whole of the covenant in question, its inclusion renders the covenant or the entire contract unenforceable … The doctrine of restraint of trade is probably one of the oldest applications of the doctrine of public policy; cases go back to the second half of the sixteenth century and as early as 1711 it was laid down in Mitchell v Reynolds that a bond to restrain oneself from trading in a particular place, if made upon a reasonable consideration, is good, though if it be upon no reasonable consideration or to restrain a man from trading at all, it is void.

The validity of a covenant in restraint of trade is assessed at the date the contract was entered into."

170. There are three stages in making the decision:

a) The court must decide what the covenant means when properly construed.
b) It must then decide whether the employers have shown, on the evidence, that they have legitimate business interests requiring protection in relation to the employee's employment.
c) The existence of legitimate protectable interests has been established, the covenant must be shown to be no wider than is reasonably necessary for the protection of those interests.

171. The relevant legal principles were summarised in **Cavendish Square Holdings BV v El Makdessi** [2012] EWHC (Comm), at 15:

a) The party seeking to enforce the covenants bears the burden of showing that they go no further than was reasonably necessary for the protection of the interest.

b) A covenant may be enforced when the covenantee has a legitimate interest, of whatever kind, to protect, and when the covenant is no wider that is necessary to protect that interest.

c) The two questions for the Court therefore are (i) what are the interests that it is legitimate for the covenantee to protect; and (ii) is the protection taken through the relevant provisions no more than is reasonably necessary to protect those interests?

d) The question of reasonableness is to be determined as at the date of the agreement in which the covenants are contained.

e) The law distinguishes between covenants in employment contracts and covenants in business sale agreements: the former are more difficult to enforce than the latter. The Court should be slow to strike down clauses freely negotiated between parties of equal bargaining power, recognising that parties are often the best judges of what is reasonable as between themselves.

172. In **Tillman v Egon Zehnder Ltd** [2019] UKSC 32 the Supreme Court clarified the test for when an unenforceable part of a covenant can be severed from the remainder. The two key questions are: (1) is the unenforceable provision capable of being removed without the necessity of adding to or modifying the wording of what remains ("the blue pencil test"); and (2) would the removal of the provisions generate any major changes in the overall effect of all the post-employment restraints in the contract? If the answers to those questions are respectively "yes" and "no", the covenant can be severed and the offending provisions/words deleted.

173. I will start with the SHA Restrictive Covenants, since the burden on the Defendants is less onerous. I will deal with the Claimants' points against their enforceability in turn:

Too wide

174. Mr. Levey conceded that the use of the words "*shareholder*" and "*or otherwise howsoever*" in clause 12.2.1 is too wide. The blue pencil test can clearly be applied to these words within the principles set out in **Tillman v Zehnder**.

No legitimate interest to protect identified

175. Mr. Quinn made a general point that the Defendants have not produced any evidence to justify the Restrictive Covenants by identifying and proving the business interest to be protected and the reasonableness of the provisions. Mr. Johnson's unchallenged evidence was that the Claimants were senior executives of the Second Defendant and key employees. They had central roles with a number of the Second Defendant's key clients and access to the confidential financial and operational information relating to its business. The Put Options had been agreed on the basis that a fair value would be paid for the shares without discount for their minority nature and therefore there was a legitimate interest in protecting the goodwill. In this context, it is established that the amount paid for the shares is a relevant consideration in assessing reasonableness.

176. Mr. Johnson also said that the nature of the Second Defendant's business of freight forwarding was that contracts were always on a one-off basis with no long term commitments from customers. I accept his evidence that the Claimants were in a position to do considerable damage to the Second Defendant's business if they chose to compete and to transfer the benefit of their contacts to a competing business and that there were therefore legitimate reasons for imposing restrictive covenants, both in the EAs and the SHAs in order to provide at least a buffer for a period. I therefore reject the suggestion that there is no evidence.

Post termination restrictions not reasonable unless "fair value" paid for shares

177. The covenant must be judged at the time of the contract. The Claimants were on an equal footing with the Defendants and agreed willingly to the restrictions and to the Defaulting Shareholder provisions.

178. This provision does not make the restrictions unreasonable. The three agreements were a package agreed between the parties and the Defaulting Shareholder provision is one of the terms that were agreed at the time as part of the overall consideration. The Claimants need not have acted so as to trigger this provision, in which case they would have received a Fair Value for their shares. Mr. Quinn is effectively saying (bar his other points) that if the SHA had been drafted so that the Restrictive Covenants did not bite if the Defaulting Shareholder provision was triggered then it would be ok. I cannot see how this would be reasonable. If the Put Option had permitted sale only at the discounted value, then I can see a strong argument that the Restrictive Covenants in the SHA might be unreasonable. Any protection would be provided by the EA Restrictive Covenants. That was not however the case here.

179. Although the case is pleaded specifically by reference to Clauses 12.2.1(a) (i) – (iv) of the SHA, the points are for the most part applicable to each of these.

180. Mr. Quinn submits that the twelve month duration is unreasonable. Much longer periods have been upheld by courts in share sale agreements. It is inevitably difficult to ascertain a minimum requirement to protect the business interest, but this period is in my judgment entirely reasonable in this context. This, and the other provisions referred to below, are all designed to stop the Claimants going to a competitor with

their "*know how*" and contacts, taking a significant part of the Second Defendant's business with them.

181. He says that the definition of "*Restricted Business*" and "*Services"* is too wide and should have a provision limiting the restriction to areas where the Claimants were directly involved. I reject the submission that these provisions are unclear and difficult to construe. The business of the Second Defendant was clear and specific and "*Restricted Business*" is expressly qualified by the words "*competing with*". The restrictions relate to this business. The reference to Group in the context of the SHA doesn't add anything significant. Services is clearly defined and having regard to the key role of the Claimants in the business, a narrower definition would be unworkable as they had access to so much material and contact information.

182. The UK is also submitted to be too wide a restricted area, but this is an international business operated by telephone and computer and therefore I cannot see that this is an unreasonable restriction.

183. The provision against employing a Key Person is clearly designed to prevent damage to the Second Defendant's business and is also reasonable.

184. I therefore reject the Claimants' case that the Restrictive Covenants in the SHAs are invalid and am satisfied that they are reasonable.

185. To the extent that the Restrictive Covenants in the EAs overlap those in the SHAs there are different considerations to be applied. Not only is the burden on the Defendant higher, but the legitimate interest to be protected is also different. Nevertheless, I am satisfied that they are reasonable. The precariousness of this business, as described by Mr. Johnson, with no long term contracts only contacts, means that the Second Defendant is vulnerable to losing key personnel who can then set up a competing business using their "*know how*" and contacts. I am satisfied that, even with the higher burden of proof, reasonableness is made out and that the restrictions are the minimum necessary to provide a buffer against the risks.

186. The definitions clause in the EA is not as comprehensive or as clear as in the SHA. Restricted Customer is limited to 12 months before Termination (of the EA) but covers prospective customers with no definition of the latter. Mr. Quinn said that "*with in the habit of dealing with*" was too vague. I don't agree as it clearly means that there is a course of dealing between the customer and the Second Defendant. The provision is further qualified to entities with whom the employee has had contact with or became aware of during his employment. This provision would also be construed against the first part of clause 1.2 – which sets out the reason for the restrictions as being to protect the confidential information and business connections of the Company and Group to which the employee has access as a result of his employment.

187. The anti-competition restriction is limited to 6 months. This is reasonable despite being a blanket restriction because of the inherent difficulty of proving that confidential information and business connections to which the employee had access during his employment has been used with the competing interest.

188. I therefore conclude that the EA Restrictive Covenants are also enforceable.

Summary of Conclusions

189. I conclude that the Claimants were in Material Breach and are therefore to be treated as Defaulting Shareholders under the SHA because of Ground A but not on the other grounds. This means that they are not entitled to be paid a Fair Value for their shares but must transfer them at nominal value.

190. I also conclude that for the same reason they were not wrongfully dismissed.

191. Save in respect of the matters conceded by Mr Levey (to which the blue pencil test should be applied) the restrictive covenants are enforceable under the EAs and the SHA.

192. I will list a further hearing as soon as possible to deal with the terms of the order and any other matters outstanding.