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Court of Appeal Rejects "Empty Formalism" in Allowing a Challenge to the Form of a "Notice of Claim" Clause under an SPA

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Last month, the Court of Appeal handed down judgment in *Dodika Ltd and Others v United Luck Group Holdings* [2021] EWCA Civ 638 and allowed the Defendant's appeal against an order for summary judgment that had been granted to the Claimant by the High Court in *Dodika Ltd and Others v United Luck Group Holdings Ltd* [2020] EWHC 2101 (Comms) (about which we have written here).

In overturning the High Court's judgment, the Court of Appeal found that a notice of claim given by the buyer under a share purchase agreement did not lack "*reasonable detail*" in circumstances where the recipient already had knowledge of the underlying facts, events and circumstances giving rise to the buyer's claim. The Court held that what constitutes "*reasonable detail*" depends on the specific circumstances and, in this case, to require the buyer to provide details of which the recipient was already aware, amounted to little more than "*empty formalism*".

Background

The appeal concerned the question of whether a notice of claim given by the buyer, United Luck Group Holdings (the "**Buyer**"), complied with certain contractual notification requirements set out in a share purchase agreement entered into with various sellers (the "**Sellers**") dated 21 December 2016 (the "**SPA**"). The SPA concerned the purchase of the entire issued share capital in Outfit7 Investments Ltd, a holding company of various businesses specialising in the development of apps for mobile phones, for the sum of US$1 billion.

The SPA included a tax covenant that was given by some of the Sellers, pursuant to which they agreed to reimburse the Buyer for any tax liabilities of the target group arising from certain pre-completion matters. Pursuant to the terms of the SPA: (i) US$100 million of the consideration was placed in an escrow account to meet any claims by the Buyer, including under the tax covenant; and (ii) in order to claim under the tax covenant, the Buyer was required to give written notice to the Sellers by 1 July 2019 setting out various matters in "*reasonable detail*", including "*the matter which gives rise to such Claim*".

In July 2018, the Slovenian tax authority commenced an investigation into the transfer pricing policies of one of the companies within the target group, Ekipa2 d.o.o. ("**Ekipa2**"). From an early stage in the investigation, the Sellers were kept informed of the progress of the investigation by the Buyers.

On 24 June 2019, the Buyer sent a letter to each of the relevant Sellers stating "*[W]e hereby give you notice … of Claims under the Tax Covenant of the SPA. Such claims relate to an investigation by*

the Slovene Tax Authority … into the transfer pricing practices of Ekipa2". Other than stating that the period under investigation for Ekipa2's transfer pricing practices was 2013–2017, the letter only set out the chronology of the engagement with the Slovenian tax authority and confirmed that the investigation was ongoing (the "**24 June Notice**").

High Court decision

In December 2019, the Sellers issued a Part 8 claim form seeking a declaration from the Court that the 24 June Notice failed to comply with the requirements set out in the SPA, because it did not give "*reasonable detail*" of the "*matter*" giving rise to the Buyer's claim, and later applied for summary judgment in February 2020.

The judge at first instance agreed that the 24 June Notice had not provided "*reasonable detail*" of the "*matter*" giving rise to the claim, as he concluded that the "*matter*" for this purpose was not the tax investigation itself, but rather the underlying facts, events or circumstances on which the Buyer's claim was based. The judge noted that the mere existence of the tax investigation, without providing more detail as to the facts underpinning it, did not serve the purpose of informing the Sellers of the "*matter*" giving rise to the claim. The Court also noted that, while the existence of the tax investigation might reveal that a claim under the tax covenant would arise, it did not identify or explain the basis of the claim—it should have set out the reasons why a tax liability had accrued or might accrue. Accordingly, notwithstanding that the Sellers were aware of the investigation, the Court found that the 24 June Notice failed to identify and set out the facts which were being relied upon for the purposes of bringing a claim for breach of the tax covenant.

Court of Appeal decision

The Buyer appealed on the basis of the following four grounds: (i) first, that a reasonable recipient, with knowledge of the tax investigation, would have known what the 24 June Notice referred to; (ii) second, that the 24 June Notice fulfilled the purpose of notification under the SPA; (iii) third, that there was no failure to identify facts unearthed during the tax investigation; and (iv) fourth, that adequate details of the "*matter*" giving rise to the claim had been given as the "*matter*" was the tax investigation itself.

The Court of Appeal distilled these into the following two questions: (i) what was the "*matter*" which gave rise to the claim; and (ii) whether the 24 June Notice provided "*reasonable detail*" of that "*matter*".

The leading judgment was given by Nugee LJ (with whom Popplewell LJ and Underhill LJ agreed).

What was the "matter" giving rise to the claim?

The Court of Appeal agreed with the High Court that the "*matter*" giving rise to the claim constituted more than the mere fact of the tax investigation. The Court found that, while the fact that there had been an investigation was relevant, the "*matter*" giving rise to the claim also included the underlying events, facts, and circumstances which took place before completion and, in particular, those relating to the transfer pricing practices which had been adopted by Ekipa2.

In this regard, the Court followed the High Court's interpretation of the words "*giving rise to*". Nugee LJ observed that such words indicate that the relevant "*matter*" is one on which the claim is based and formulated and that the Buyer's claim was not itself based on the existence of the tax investigation, but rather the factual reasons for why a tax liability accruing before completion had accrued or might accrue post-completion.

Was the matter stated in "reasonable detail"?

The Court noted at the outset that this was not a straightforward question and that the 24 June Notice did not say very much about the underlying facts giving rise to the potential tax liability.

The Court accepted that a notification clause, in principle, must be complied with strictly. In the present case, the SPA did not specify precisely what information the notice was required to contain in order for it to provide "*reasonable detail*" and the Court observed that what is reasonable depends on all of the circumstances. In the Court's view, such circumstances must include what is already known to the recipient. In this regard, it relied on the decision of the House of Lords in *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd*[1], which showed that the information conveyed by a unilateral notice to the reasonable recipient was capable of being affected by the background context, including the knowledge of the recipient.

The Court noted that the Sellers had been kept informed of the tax investigation and knew all the details about the course of the investigation, including the fact that Ekipa2 had been provided with very little information about the specific suspicions that the tax authority had about its transfer pricing. On the issue of whether the 24 June Notice needed to provide more information than it did, Nugee LJ was guided by the additional reasoning of Popplewell LJ who held that no specific details were required, as: (i) the tax authority's investigation was, in fact, based on a high level of generality; (ii) the inclusion of further detail (which was already known) would have served no commercial purpose; and (iii) the inclusion of further information would not have advanced the purpose of giving notice of a claim. In this case, the Court held that it was unnecessary for the 24 June Notice to say more than it did in order to provide "*reasonable detail*" and that requiring the Buyer to include details which the Seller already knew would "*elevate the requirement to state matters in reasonable detail into empty formalism*". Accordingly, the notice was not invalid.

What does this mean in practice?

In determining whether a notice is valid, the fundamental question is what a "reasonable recipient", with knowledge of the underlying context, would understand by the notice. Where a notice is required to give "reasonable detail", subject to any express terms setting out precisely what information the notice is required to contain, what is reasonable will depend on all of the circumstances. This recent decision of the Court of Appeal confirms that one of the factors that will be taken into account is the recipient's actual knowledge of the matters which are relevant to the underlying claim. It shows that contractual interpretation may bend to commercial realities so that, unless specifically required, a notice may not have to restate information already known to the recipient.

That being said, while the decision will be welcomed as endorsing a more common-sense approach by which the provision of detail may be deemed unnecessary if it serves no commercial purpose, it must be considered in its context. In this case, the Sellers were very aware of the tax investigation and had been kept informed on a rolling basis by the Buyer. However, it will not always be the case that a recipient will have as much knowledge about all of the matters which form the basis of a claim, and knowledge should certainly not be assumed. In addition, notice requirements invariably differ, and provisions which specify precisely what information is required to be given leave far less room for manoeuvre, and any failure to comply with the prescribed requirements may render the notice invalid.

Notwithstanding that the decision of the Court of Appeal is welcome, having to go to the Court of Appeal to ascertain the validity of a notice is a most unwelcome distraction. Accordingly:

- when drafting notice provisions in agreements, it is important to ensure that, as a practical matter the provision is reasonably straightforward to deal with and that it does not impose unduly onerous obligations on the claimant at too early a stage in the claim process; and

- it remains key to comply with the particular requirements of a notice provision. A buyer would be wise to include as much detail as it reasonably can; however, it should also be wary of: (i) avoiding giving information on which it is unsure and may need to row back on later, as this could itself affect the validity of the notice; and (ii) providing so much information that it is effectively prevented from developing the claim any further in the future.

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1 [1997] AC 749.