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International fraud and asset tracing litigation - Spring: A windfall opportunity

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CATEGORY:
ARTICLE

4 Eng v. Roger Harper and Another [2008]EWHC 915 (Ch)

Facts of the case

The Court gave judgment on 29 April 2008 following the trial on the assessment of damages of 4 Eng Limited ('4 Eng') which had been defrauded in its purchase of the entire issued share capital of Ironfirm Limited trading as Excel Engineering ('Excel').

By a contract dated 29 June 2001 4 Eng were to pay £1.2million of which £550,000 was payable on completion and the balance over three years. The balance was not paid as the owners of 4 Eng – David Shepherd and Ian Tapping – discovered that there were significant problems which the Court held 'as a result of their painstaking investigations over a period of at least four years' … established that the defendants, Roger Harper and Barry Simpson had engaged in systematic bribery of employees of Excel's principal customer, Mars UK Limited ('Mars'). 4 Eng was established by David Shepherd and Ian Tapping as a vehicle for acquiring companies in the engineering sector, of which Excel was the first. Due to the problems encountered, Excel was the only acquisition of 4 Eng. Roger Harper and Barry Simpson were convicted at Reading Crown Court on 8 December 2005 of conspiracy to corrupt and conspiracy to defraud – convictions, which established the liability of Excel to account to Mars. Excel was found to be insolvent and went into creditors' voluntary liquidation on 13 July 2006.

4 Eng sued and obtained judgment in deceit against both defendants on 3 May 2007. In this trial for damages it claimed five separate heads of loss: (1) the purchase price paid to the Defendants amounting to £550,000, (2) the costs and expenses of the acquisition amounting to £72,371.50, (3) the liabilities incurred by 4 Eng after acquisition for salaries, pension payments and national insurance contributions amounting to £384,651.08, (4) the liability for cost of investigation into the fraud amounting to £711,200 and (5) the loss of opportunity to purchase and profit from another company Tarvail Limited amounting to £10,218,320.

The first and last of these claims for damages merit further consideration.

The purchase price paid to the Defendants of £550,000

Mr Shepherd and Mr Tapping subscribed £50,000 in total for shares in 4 Eng. Save for this sum 4 Eng obtained the funds for its purchase of Excel by Excel lending to it (4 Eng) £500,000.

(This provision by Excel of financial assistance for the purchase of its own shares would have been, at the date of completion on 29 June 2001, a breach of s 151 Companies Act 1985 save for the fact that the procedure set out in s 155 Companies Act was followed).

4 Eng did not repay its debt of £500,000 to Excel directly. An agreement for Excel to pay 4 Eng £29,000 per month management charges was entered into following 4 Eng's acquisition, and when Excel couldn't pay, the amount of £29,000 per month was set off against 4 Eng's liability to Excel on its inter-company loan. By February 2003 Excel's loan to 4 Eng was thus repaid.

One of the arguments put forward by the Defendants was to deny the claim for the loss of the £550,000 paid on completion on 29 June 2001 on the grounds that 4 Eng did not fund the purchase of Excel (or only did so to the extent of its share capital of £50,000) and incurred no losses or liabilities as a consequence.

Loss of opportunity to purchase and profit from another company, Tarvail Limited claimed at £10,218,320 (less certain deductions).

Mr Shepherd's and Mr Tapping's detailed business plan for the acquisition of both Excel and Tarvail revealed their interest in acquiring Tarvail. The subsequent meetings and offers, (subject to contract) and due diligence confirmed this. In October 2000 4 Eng had approached Lloyds for funding for their intended acquisition of Excel and Tarvail. Evidence was called from both Lloyds TSB Bank and Lloyds TSB Commercial Finance Limited to substantiate that there was no reason why finance should not have been provided for the acquisition of Tarvail on similar terms to that provided for the acquisition of Excel.

The Court considered whether Mr Shepherd and Mr Tapping would in fact have been able to finance the balance (£253,000) required over and above bank finance for 4 Eng to complete its (hypothetical) acquisition of Tarvail at £950,000 of which £650,000 was payable on completion.

And if the Court found that Mr Shepherd and Mr Tapping could have acquired Tarvail it then had to consider how it would quantify this loss of opportunity.

The Decision

1. The Court held that 4 Eng had in fact paid £550,000 to the Defendants and incurred a liability on its loan from Excel. The Defendants had not suggested that the agreement for management charges was either a sham or involved artificially inflated charges – and in those circumstances 4 Eng had fully repaid the loan and suffered the loss of £550,000.
1. The Court held that on the balance of probability 4 Eng would have been able and willing to purchase Tarvail and that Mr Tapping's assets in particular were sufficient to fund the balance required to complete over and above bank facilities from Lloyds (which on the same basis as those provided for the Excel acquisition would leave £253,000 to be provided from other resources). More to the point Mr Justice Richards held that there was an 80% chance that Mr Tapp and Mr Rogers, (the owners of Tarvail) would have sold their shares to Mr Tapping and Mr Shepherd.

Points of interest

There was sufficient evidence to enable the court to quantify the financial advantages 4 Eng would have enjoyed had it completed its proposed purchase of Tarvail instead of Excel. To the adjusted net profits of Tarvail for the period 2001-2008 of £5,835,061 there was deducted Lloyds' interest charges of £70,000 for the presumed term loan, overdraft facility and revolving debt facility; management charges at £24,000 per month; and the same payments to Mr Dalton and Mr Ede the two key director employees who ran the business as they in fact received.

As to the capital loss due to 4 Eng not owning Tarvail shares, the capital value of Tarvail was valued by Mr Djanogly the joint expert account at £4,383,259 from which the (hypothetical) acquisition price of £950,000 and acquisition costs of £72,000 were deducted. Both the loss of this profit for the period 2001-2008 and the loss of capital value were reduced by 20% to reflect the risk of a decline in turnover following the acquisition, and the risk that Mr Dalton and Mr Ede the two key directors employees could have left Tarvail to form their own business or work for a competitor.

These losses were in addition to the losses caused by 4 Eng's purchase of Excel, the payment of the £550,000 for the acquisition and the expenses incurred in completion. In all a remarkable result for David Shepherd's and Ian Tapping's original £150,000 investment in 4 Eng.