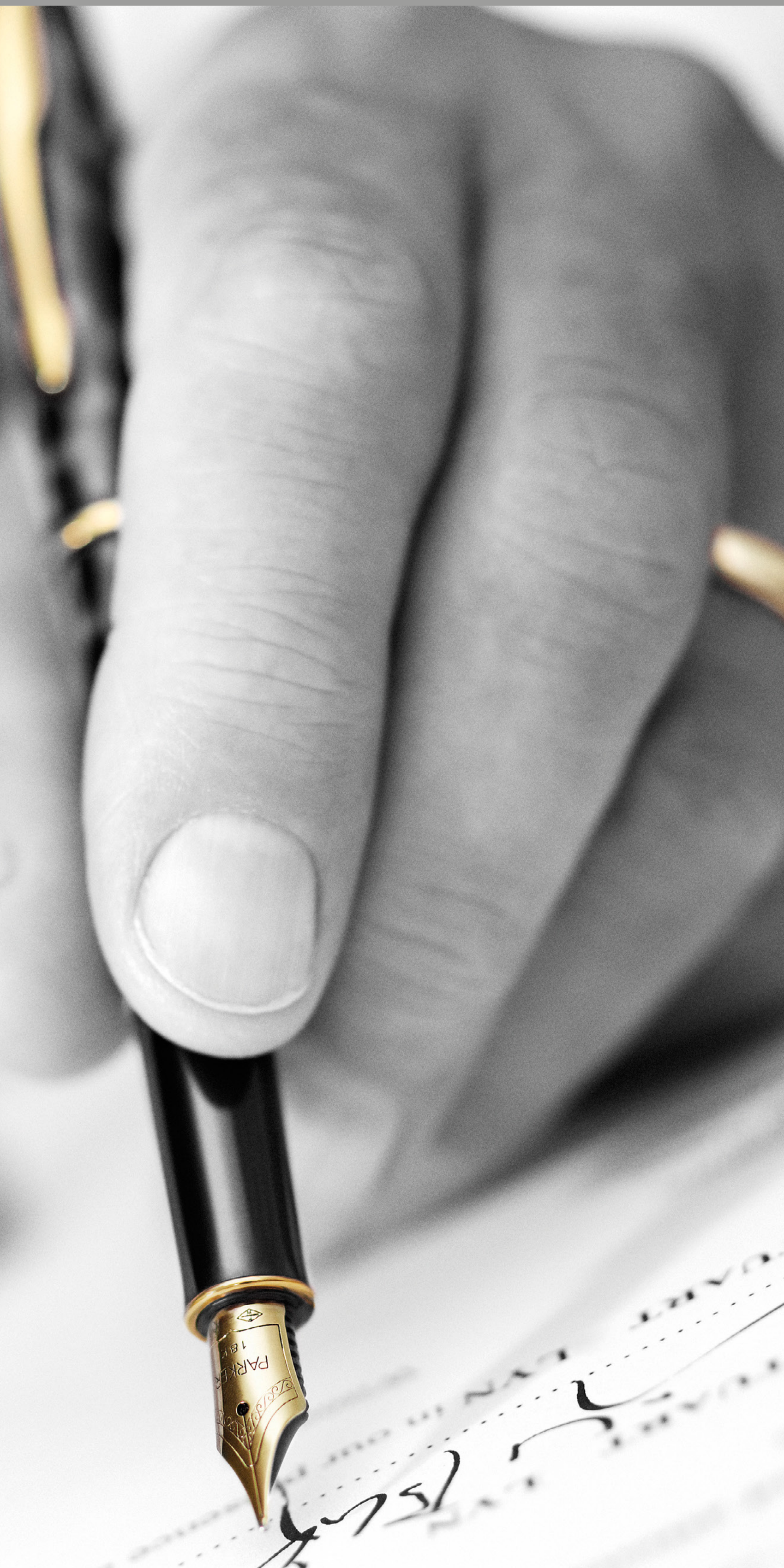
Corporate NEWSLETTER

Winter 2017/2018



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CORPORATE & COMMERCIAL LAW

Watson v Watchfinder.co.uk Ltd - Contractual Discretions: Arbitrary Board and Capricious Directors

Russel Shear, Head of Corporate & Commercial

In a recent case of *Watson v Watchfinder.co.uk Ltd* the High Court has criticised a company's board of directors for unreasonably exercising their veto powers in a share option agreement, finding that there was an implied duty upon the directors not to use their right under the agreement in a manner that was *'unreasonable, capricious or arbitrary'*.

Editor's Note

Welcome to the Winter 2017/18 edition of our Corporate Newsletter which contains a variety of articles covering property, intellectual property, employment, corporate & commercial and property litigation law.

I am delighted to announce that the firm has been ranked as the 104th law firm in *The Lawyer 'UK 200' 2017*, up by seven places from last year. **Full press release available to read here.**

The General Data Protection Regulation (GDPR) will come into force on 25 May 2018 and it represents the biggest change in the European data protection law and practice for 20 years – every business or organisation needs to know about it and plan for it. Join us on Thursday, 29 November 2017 when we will be hosting a seminar on *'Getting to know the GDPR'*. **Find out more information here.**

If you have any legal issues or concerns that you would like to discuss, please do not hesitate to contact me.

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The case acts as a warning to directors of the obligations typically placed upon them when exercising contractual discretions and emphasises the importance of detailed record keeping when undertaking their duties.

The case involved three individuals (the Claimants) who were directors and shareholders of Adoreum Partners, a company engaged by Watchfinder.co.uk Limited (the Defendant) to provide business consultancy services. The Defendant, a retailer of pre-owned luxury watches, sought to utilise Adoreum's extensive network of businesses and high-net-worth individuals within the luxury goods sector in an attempt to secure significant investment in its business.

As part of the contractual package agreed between the parties, the Claimants and the Defendant entered into a share option agreement (the Agreement) which granted the Claimants the right to subscribe for shares in the Defendant at a pre-determined price. The Agreement, however, stipulated that the *"Option may only be exercised with the consent of a majority of the board of directors of the Company"*, purporting to give the directors of the Defendant an unfettered right of veto over the Claimants' use of their subscription rights.

Despite successfully introducing a number of investors to the Defendant, when the Claimants attempted to exercise their option, following a considerable increase in the option's value, the Defendant refused to issue the shares on the grounds that the necessary consent, which had not been forthcoming from the board, had not been obtained. The Claimants, therefore, brought a claim against the Defendant seeking specific performance of the Agreement.

The court was asked to determine whether the contractual provision requiring board approval amounted to an unconditional right of veto or a discretionary power and, if the latter, whether the directors were under a duty to exercise their discretion in good faith.

In its judgment, the High Court held that the proper construction of the clause did not grant the directors an absolute veto over the exercise of the option, stating that to do so would render the Agreement meaningless as the grant of shares would be entirely within the gift of the Defendant. As the option had been granted in a self-contained agreement, the court considered that rendering that part of the deal worthless would be contrary to commercial common sense, which could not have been the parties' intention when entering the Agreement.

The court nonetheless found that the clause did operate so as to restrict the exercise of the option and the directors had a degree of discretion over its use. This discretion, however, was subject to the directors exercising their powers in a manner which was not arbitrary, capricious or irrational, the so called 'Braganza Duty'. In order to discharge this duty, the board were under an obligation to ensure that a proper decision-making process was followed, which included the taking into account material points whilst disregarding those that were irrelevant and in doing so reaching a decision that was not unreasonable.

"The court's finding demonstrates the importance of the proper administration of a company's affairs, particularly when exercising a contractual discretion."

When assessing whether the Defendant had complied with its duties, the court found that there had been no meaningful exercise of any discretion. The matter had been dealt with fleetingly at a board meeting with many of the directors operating under the mistaken belief that the board held an absolute right of veto under the Agreement. The court took the view that, where any consideration had been given as to whether consent should be granted, the directors had been overly focussed on the loss of potential investment from a luxury goods group rather than considering the value that the Claimants had added to the Defendant's business by introducing new investors. Having failed to comply with its *Braganza Duty*, the court found in favour of the Claimants and granted their request for specific performance of the Agreement.

The court's finding demonstrates the importance of the proper administration of a company's affairs, particularly when exercising a contractual discretion. The current case could well have been decided differently had the Defendant been able to produce evidence that a measured decision making process had been followed. When deciding whether to use discretionary powers companies should ensure that comprehensive records are kept detailing the factors considered in the decision making process together with the ultimate reason for granting or refusing consent.

The decision also illustrates the court's willingness to imply terms into agreements to give effect to what it considers are the parties' intentions and provides a warning to companies of the risks of relying too heavily on contractual veto powers. If it is a company's intention for an option to be exercisable only in specific circumstances, it is far better for such requirements to be clearly and explicitly incorporated as conditions of the option agreement rather than relying on overarching powers of veto, whose validity may be subject to judicial scrutiny.

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PROPERTY LITIGATION LAW

All change in the Court system: New Business and Property Courts

Joanna Osborne, Head of Property Litigation

The Business and Property Courts is a new umbrella Court system created to replace the Commercial Court, the Chancery Division and the Technology and Construction Court. In London this Court will continue to operate in the Rolls Building on Fetter Lane. It will form the largest specialist centre for financial, business and property litigation in the world.

"One of the main reasons for reorganising the Court system in this way is to ensure that cases which have specific links to a region can be tried in that region and by a specialist Judge."

Similar Courts have also been established in the five main regional centres to cover the specialist business which used to be conducted by the previous Courts namely in Birmingham, Bristol, Cardiff, Leeds and Manchester.

County Court cases are being given a similar re-organisation under what is now described as the Business and Property Courts List.

Within these new Courts there is now a sub-list covering specific areas of dispute as follows:

(1) Admiralty Court (QBD)

(2) Business List (ChD)

- **(a) Business**
- **(b) Financial services and regulatory**
- **(c) Pensions**

(3) Commercial Court (QBD)

- **(a) Commercial Court**
- **(b) Circuit Commercial Court (QBD) (formerly the Mercantile Court)**

(4) Competition List (Ch)

(5) Financial List (financial disputes worth over £50million) (ChD/QBD)

(6) Insolvency and Companies List (ChD)

(7) Intellectual Property List (ChD)

- **(a) Intellectual property**
- **(b) Intellectual Property and Enterprise Court (IPEC)**
- **(c) Patents Court**

(8) Property, Trusts and Probate List (ChD)

(9) Revenue List

(10) Technology and Construction Court (QBD).

One of the main reasons for reorganising the Court system in this way is to ensure that cases which have specific links to a region can be tried in that region and by a specialist Judge. Clearly also the purpose is to present the Court system in England and Wales as the global Court system of choice.

Cases involving Property disputes will now be dealt with by the Property, Trusts and Probate List, cases involving insolvency will be dealt with by the Insolvency and Companies List and cases involving disputes about buildings, engineering and surveying, building construction and engineering contract disputes will be dealt with by the Technology and Construction Court, which has now been specifically identified as the appropriate Court to deal with dilapidations claims in landlord and tenant disputes.

All existing Court proceedings will have to have the title to the proceedings amended to specify the Court in which the claim should now be brought.

It remains to be seen whether this will improve the running of the Courts, but if it means at least that there is a better chance of securing a Judge with specialist knowledge, then this has to be a good thing.

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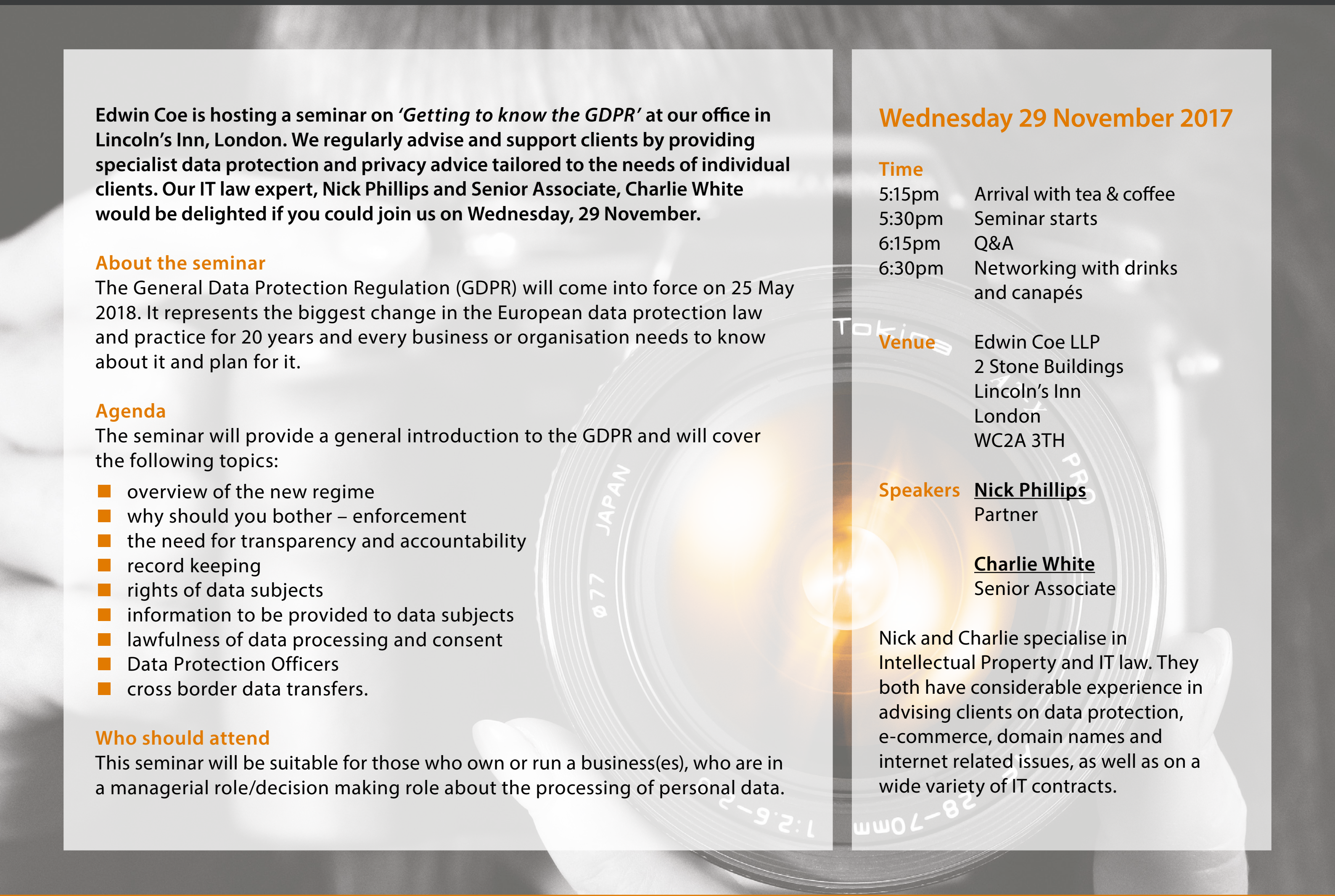
Getting to know the GDPR

Seminar



Edwin Coe is hosting a seminar on *'Getting to know the GDPR'* at our office in Lincoln's Inn, London. We regularly advise and support clients by providing specialist data protection and privacy advice tailored to the needs of individual clients. Our IT law expert, Nick Phillips and Senior Associate, Charlie White would be delighted if you could join us on Wednesday, 29 November.

About the seminar

The General Data Protection Regulation (GDPR) will come into force on 25 May 2018. It represents the biggest change in the European data protection law and practice for 20 years and every business or organisation needs to know about it and plan for it.

Agenda

The seminar will provide a general introduction to the GDPR and will cover the following topics:

- overview of the new regime
- why should you bother – enforcement
- the need for transparency and accountability
- record keeping
- rights of data subjects
- information to be provided to data subjects
- lawfulness of data processing and consent
- Data Protection Officers
- cross border data transfers.

Who should attend

This seminar will be suitable for those who own or run a business(es), who are in a managerial role/decision making role about the processing of personal data.

Wednesday 29 November 2017

Time

5:15pm	Arrival with tea & coffee
5:30pm	Seminar starts
6:15pm	Q&A
6:30pm	Networking with drinks and canapés

Venue
Edwin Coe LLP
2 Stone Buildings
Lincoln's Inn
London
WC2A 3TH

Speakers
[Nick Phillips]
Partner

[Charlie White]
Senior Associate

Nick and Charlie specialise in Intellectual Property and IT law. They both have considerable experience in advising clients on data protection, e-commerce, domain names and internet related issues, as well as on a wide variety of IT contracts.

If you have any questions about this topic please contact info@edwincoe.com.
To register your interest to attend please contact events@edwincoe.com.

EdwinCoe LLP

INTELLECTUAL PROPERTY LAW

Clarity in Unjustified Threats Actions

Simon Miles, Head of Intellectual Property

The Intellectual Property (Unjustified Threats) Act 2017 (the Act) came into force on 1 October 2017 reforming the UK's law on unjustified threats concerning intellectual property rights (IP) infringement.

One of the aims of the Act is to encourage parties in IP infringement disputes to negotiate fairly with a view to settling disputes rather than resorting to costly and timely litigation. The Act is also designed to protect parties likely to be harmed by unjustified threats over allegations of infringement.

Remedies

Under UK law there is a statutory right of redress against unjustified (or groundless) threats to sue for infringement of a patent, trade mark or registered/unregistered design. Threats to sue for infringement of IP rights can be a powerful weapon and if made against retailers for example, fear of the costs involved in litigation may result in them capitulating and their business being damaged, even if the IP right is invalid. Therefore, anyone so threatened can seek a declaration that the threats are unjustified, damages, and an injunction to prevent further such threats in the future.

"Threats to sue for infringement of IP rights can be a powerful weapon and if made against retailers for example, fear of the costs involved in litigation may result in them capitulating and their business being damaged, even if the IP right is invalid."

Need of reform

There is a consensus that the pre-Act threats provisions were in need of reform. Criticisms included:

- different rules related to different IP rights and so were confusing for those wishing to assert their rights;
- it was too easy to fall within the groundless threats provisions with the result that smaller businesses felt disinclined to assert their IP rights; and
- parties were less inclined to try and settle disputes at the outset for fear of leaving oneself open to a threats action.

The difficulty was that the threat could be oral, implicit or indirect so there did not need to be any express mention of the right albeit that mere notification of the existence of the right would not amount to a threat. However, mere notification of a right is often considered to be a communication without teeth. A good example of what amounts to a threat is contained in *Grimme Landmaschinenfabrik GmbH & Co KG v Scott*, a case on design rights. The Court held that even though the claimant's solicitor's letters expressly stated that the claimant did not intend to take proceedings, the combination of a reservation of rights together with a reference to contacting the customer again if it was successful in its action against the defendant, amounted to a threat.

The Act encompasses the recommendations the Law Commission made in its 2014 and 2015 reports and harmonises the previous provisions on patents, European patents (including under the Unified Patents Court), trade marks, EU trade marks, registered designs, design rights and Community designs. As with the previous law copyright and passing off are excluded from the threats provisions.

Key changes

A few of the notable changes contained in the Act are as follows:

- A threats action may not be brought for threats made to a primary actor, that is, someone who is usually the source of the infringement and is responsible for carrying out one or more of the most commercially damaging acts such as importation or manufacture. This is already part of the current law for patents but will now apply to the other rights. The question of whom or what is a primary actor was heavily debated at all stages of the development of the Act. A late attempt at the Public Bill Committee stage in the House of Commons, to extend the extent of protection to those who contact parties who hold themselves out to be primary actors when they are not, was rejected. It was said that the change was justified because of the increasing complexity of supply chains, but the rejection means that someone who holds themselves out as a primary actor when they are not can bring a claim for groundless threats if such a threat is made.
- However, if you are unsure whether someone is a primary actor you will be able to contact them if your communication amounts to a *"permitted communication"* – essentially safe harbour provisions. The communication must be for a *"permitted purpose"* for example: simply giving notice that the rights exists or discovering if the right is being infringed and by whom. There is also guidance on what is not a permitted purpose, for example, requesting an undertaking relating to a product or process.
- The Act provides justification defences permitting communications with a secondary actor (if a primary actor cannot be found). One must demonstrate that *"all reasonable steps"* were taken to identify the source of the infringement but have been unable to identify anyone. The communication must cover what those steps were and that notification was served either before or at the time the threat was made.
- A regulated professional adviser acting in their professional capacity and on instructions from their client will not face personal liability for making threats as the new rules provides protection to advisors allowing freer communication with clients.
- The Act makes it clear that threats do not just have to be made to an individual but can also be made in public and in mass communications such as in press releases.

However, some of the existing principles derived from the case law, such as the test for whether a communication contains a threat, remain good law. The test has two elements:

(1) whether the communication would be understood by a reasonable recipient to mean that a right exists, and

(2) that someone intends to bring infringement proceedings for an act done in the UK.

A recent re-stating of the law was set out in *Nvidia v Hardware Labs* in which the writer acted for the successful Defendant. It adds useful guidance to the circumstances in which a threat is deemed to be a threat in the UK.

Legal representatives

Whilst it may appear that the rules have been relaxed, the legal framework is anything but straightforward and if you are going to threaten someone with infringement of IP rights in the UK a great deal of care still needs to be taken otherwise you could find yourself on the receiving end of a claim for damages, an injunction to prevent the threat from recurring, a declaration that the threat is unjustified as well as legal costs.

If you wish to issue a letter before action to a potential infringer in the UK, or if you think you may have a potential claim, we recommend that you first consult with a UK regulated advisor for infringement advice. We can of course advise on IP infringement and can carry out a risk-based assessment. If a claim has merit then we can ensure that the letter is drafted correctly so as to eliminate the risk of triggering litigation.

"If you are going to threaten someone with infringement of IP rights in the UK a great deal of care still needs to be taken otherwise you could find yourself on the receiving end of a claim for damages, an injunction to prevent the threat from recurring, a declaration that the threat is unjustified as well as legal costs."

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EMPLOYMENT LAW

Labouring the point - Brexit uncertainty and Employment Law

Rachel Harrap, Partner

An essential part of the exit of the United Kingdom from the European Union will be the repeal of the European Communities Act 1972. That Act is the primary legislation that incorporates European Law into the UK's domestic law. This is very significant for industrial relations as a significant proportion of the UK's labour law derives from the EU. The Government has already committed to converting all employment legislation into domestic law, so at least in the short-term the effect should be negligible. However, much uncertainty still remains.

"Although in theory following Brexit all employment law could be repealed, it is clear that this will not occur and the EU will continue to exercise a significant influence."

Dilution of Rights

A key concern raised by workers' representatives is that when EU Law is transferred into domestic legislation, it will be implemented by way of Regulations rather than Acts of Parliament. This means that it will bypass the parliamentary debate phase and thus run the risk of being watered down into reduced employee rights or legislation that employers (and their legal advisers) find easier to exploit. Notably, the Trade Union Congress has expressed concerns in this regard, particularly as it perceives a general failure on the part of the Government to keep pace with the changing nature of the economy and preserve the rights of workers on the fringes of the mainstream workplace, such as agency workers or those working in the *"gig"* economy.

Areas considered particularly right for dilution of rights include those that arise on the transfer of a business or change of service provider and under discrimination law. The Transfer of Undertaking (Protection of Employment) Regulations 2006, which are the Regulations that preserve employment protection on the sale or transfer of a business or change of service provider, are perennially unpopular with businesses. Although these Regulations are unlikely to be repealed, there is a suggestion that harmonisation of terms (something currently very difficult to achieve) may be made much more straightforward, allowing a new employer to impose less favourable terms on its workforce in line with the terms and conditions of its existing workforce. There would be some rationale to such an adjustment as it would bring a sale of business assets in line with a share sale.

Protection from discrimination is far too deeply enshrined (much of the UK legislation predates that of the EU) to be repealed, but there is real concern from worker representatives that a cap on compensation might be applied such as currently exists for unfair dismissal claims. This would of course be advantageous to employers because of the lack of a cost regime in Employment Tribunal claims. In vanilla unfair dismissal claims, compensation is capped at the lower of one year's pay, or about £80,000. Currently compensation where the dismissal is for a discriminatory reason or for whistleblowing is currently unlimited. The costs of running an even straightforward Employment Tribunal claim for unfair dismissal can be upwards of £50,000 and the general rule in such proceedings is that win or lose both sides bear their own legal costs. It can be seen therefore that for an employee to litigate an unfair dismissal claim alone is seldom cost effective. However, in discrimination claims and whistleblowing claims where compensation can run to seven figures, the landscape is currently very different. Impose a cap on discrimination and whistleblowing compensation and the outlook is dramatically changed.

Holiday and working time rights are equally enshrined, but there are some various anomalies arising under EU law, which are perceived by employers as unattractive. For example, workers on sick leave are able to continue to accrue holiday, so this means a worker who is absent on sick leave for a year can still *"take holiday"* during which time they are entitled to receive their normal full pay. Understandably this sits awkwardly with many businesses.

Role of the CJEU

Post Brexit the UK will fall outside the direct jurisdiction of the Court of Justice of the European Union (CJEU). This must be absolute as no nation can cede jurisdiction into another nation, as this would entirely contradict the principle of respect and recognition for a sovereign state. The Government's *"Future Partnership Paper"* published on 23 August 2017 states that following the withdrawal from the EU, all CJEU decisions that predate Brexit will have the same precedential value as if they were decisions to the UK Supreme Court. This is important as currently the UK Courts must interpret law derived from the EU in accordance with judgments of the CJEU and following established precedents is necessary to preserve legal certainty. However, it does mean that arguments based on the supremacy of the CJEU will no longer be valid. UK Courts will continue to use CJEU decisions for guidance, but they will not be legally binding and the removal of the CJEU as the final arbitrator will remove a layer in the litigation process and UK Supreme Court will become the Court of last resort.

> "UK Courts will continue to use CJEU decisions for guidance, but they will not be legally binding and the removal of the CJEU as the final arbitrator will remove a layer in the litigation process and UK Supreme Court will become the Court of last resort."

The draft of the European Union Withdrawal Bill 2017 provides that no references can be made to the CJEU after the *"Exit Day"* and although Courts and Tribunals may have regard to EU case law, in making determinations they are not bound to do so. There is also a power under the Bill to rectify any *"failure of retained EU law to operate effectively"*. There are certain restrictions on when this power may be exercised (for example in relation to tax and criminal law), but there is currently no fetters regarding removing or amending employment law.

Conclusion

Although in theory following Brexit all employment law could be repealed, it is clear that this will not occur and the EU will continue to exercise a significant influence. The reason for this is twofold. Firstly, the fact that many laws perceived as European actually predated the European legislation and secondly, there is an overwhelming business reason to have an ongoing relationship with the EU, so that the UK is clearly going to have to have *"equivalence"* with the EU Regulations to maintain access to EU markets.

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PROPERTY LAW

When is a Deed of Variation not a Deed of Variation?

Susan Johnson, Senior Associate

It is not unusual for a landlord and a tenant to vary the terms of a lease by a Deed of Variation. However, the legal effect of such a deed can in fact end the lease and create a new one, known as *"a surrender and re-grant"*, with unexpected far reaching consequences for both the landlord and the tenant.

When does a surrender and re-grant occur?

A surrender and re-grant occurs when variations to a lease are so inconsistent with the continuation of the existing relationship of landlord and tenant, that the law deems the existing lease to have been surrendered, and a completely new lease brought into existence in its place. This surrender and re-grant occurs without the parties intending it, or even realising that this is the effect of their purported variation of the lease.

"The surrender and re-grant occurs without the parties intending it, or even realising that this is the effect of their purported variation of the lease."

What variations can trigger a surrender and re-grant?

A surrender and re-grant usually only happens where the variation that the landlord and the tenant require changes the legal estate, namely:

- the term of the lease is extended, or
- land is added to the demise.

The other terms of the new lease will be the same as those of the old lease.

How does this impact on a landlord?

A surrender and re-grant has the following consequences for a landlord:

- If the original lease was excluded from the security of tenure provisions of the Landlord and Tenant Act 1954, the exclusion will not be carried over to the new lease, and the tenant will accordingly benefit from security of tenure under the new lease.
- The surrender will release the liability of former tenants and guarantors, and a guarantor under the old lease will not be liable under the new lease.
- If the existing lease pre-dates the Landlord and Tenant (Covenants) Act 1995, the landlord may find that an *"old tenancy"* with full original tenant liability is lost, and is replaced with a *"new tenancy"* under that

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Act with the new privity of contract regime under that Act. The *"new"* lease will also not include provisions relating to assignments and authorised guarantee agreements that are typically included in a *"new tenancy"*.

How does this impact upon a tenant?

Any new lease created could trigger a new Stamp Duty Land Tax (SDLT) payment, and could also trigger a requirement for registration of the new lease at the Land Registry.

How can I avoid a surrender and re-grant?

If the landlord and the tenant wish to extend the term of a lease without triggering a surrender and re-grant situation, they can enter into a reversionary lease that only commences on the expiry of the existing lease. The new lease can incorporate the relevant terms of the existing lease by reference, and can also include any updating that is necessary.

If the landlord and tenant wish to extend the physical extent of the land in the lease, a separate supplemental lease of the additional area can be granted by the landlord to the tenant.

> "Any new lease created could trigger a new Stamp Duty Land Tax (SDLT) payment..."

Again, the new lease can incorporate the relevant terms of the existing lease by reference, and can also include any updating that is necessary.

International capabilities

An international member of

Ally Law

Ally Law's 2018 Annual Client Seminar is now confirmed and will take place in London, UK on Thursday 31 May 2018. Further details will follow shortly.

Increasingly we find that clients' needs have an international dimension and we are able to offer access to Ally Law, of which we are a member. Ally Law is a group of independent law firms that provide comprehensive legal services worldwide.

If you have questions about how Edwin Coe and Ally Law can address your global business and legal needs, please contact Russel Shear, Head of Corporate & Commercial at Edwin Coe. Alternatively, please email team@ally-law.com.

We hope you find this newsletter useful and interesting, and we would welcome your comments. For further information and additional copies please contact the editor: Russel Shear on t: +44 (0)20 7691 4082 e: russel.shear@edwincoe.com

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