UNJUST ENRICHMENT: WINDFALL OR SHORTFALL?

HOW NOT TO GET WHAT YOU PAID FOR WHEN BUYING AND SELLING ASSETS

DARGAMO HOLDINGS LTD AND ANOTHER V AVONWICK HOLDINGS LTD AND OTHERS [2021] EWCA CIV 1149

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Introduction

Shareholder Disputes have been on the rise during the past year. Often this is due to the inadequate or misunderstood documents drawn up at the time of relationships being formed to demarcate the value and risks being shared. So this case is a timely reminder of the pitfalls of allocating risk and reward in an SPA whilst failing to grasp the commercial rationale in the way the valuation, consideration and asset portfolio are being redistributed.

Further, parties have purchased companies/businesses and been disappointed with the results, leading to an increase in breach of warranty claims which (often) must be notified within 1 year of completion.

Commercial parties buying and selling shares tend to have in mind differing approaches to valuation. When one party appears to have obtained a windfall or shortfall without the ancillary comparable consideration being paid, then that can lead to disputes. Nobody likes to think they have either overpaid or underpaid.

Asset valuation and assessment of portfolios is further complicated when considering cross border investments and deals that have imported English Law into a shareholder agreement which deals with a variety of complex group shareholdings.

This case shows that it is possible for clients to over pay and under receive when the asset portfolio exchange fails to live up to the aspirations and objectives of the paying parties.

Background

The Court of Appeal had to review a claim for unjust enrichment arising from a complex shareholder transaction which produced outcomes beyond what one party thought was fair.

In order to get a claim for unjust enrichment off the ground, a claimant needs to have evidence of the following:

- There has been a financial improvement enjoyed by the intended defendant which amounts to an enrichment;
- Such improvement was at the expense of the intended claimant;
- It is unjust for the intended defendant to keep the benefits of such enrichment.

Unjust enrichment can be a useful tool to correct the imbalance in unfair rewards received by one party at the expense of another.

In shareholder disputes for example one party may by mistake have received property or value that is above that which was intended compared to the allocation of risks taken by that party. However, where there is a contract, many of the unjust points of concern which a party may raise, may have been dealt with in the contract and terms may have been included on the basis of a mistaken assumption or representation which the contract excludes as a possible breach.

Separation of mutually owned interests in connected companies in Ukraine

The Court considered an agreement referred to as the Castlerose SPA which had been concluded by the parties as part of the division of assets in the “divorce” of dealings between three Ukrainian businessmen who had fallen out. These three men had a number of shared business enterprises in the metallurgical sector in Ukraine involving a company called Industrial Union of Donbass (“IUD”) and used a variety of special purpose companies to invest in with each other, namely Dargamo Holdings Limited (Dargamo), Avonwick Holdings Limited (Avonwick) and Azitio Holdings Limited (Azitio).

Avonwick was the Claimant and First Respondent in the Appeal. Avonwick had issued a claim against Dargamo and Azitio alleging deceit which in turn led to various cross claims and/or Part 20 claims being asserted.

Put briefly, the SPA included express terms dealing with the payment of USD 950 million for transfer of shares in IUD, (the holding company) but did not include express terms dealing with the transfer of other assets which had been alluded to in an unsigned memorandum of understanding and side letter which had been prepared at the same time as the SPA.

Judge’s comments at First Instance

Avonwick had agreed to sell its interest in a company called IUD but asserted in its claim that such sale had been induced by fraudulent misrepresentations. Put briefly, the various asset transfers and splits were supposedly to be conducted in such a way that would enable the “same price per share” to be paid to and received by each party. The Judge at first instance held that this had not happened.

In addition to various contractual claims that were raised, the Judge considered a claim for unjust enrichment, which he ultimately dismissed. He considered whether Avonwick had not done what it had agreed to do. The Judge found that Avonwick had only agreed under the SPA to transfer shares in a company called Castlerose.

Court of Appeal

The issue considered by the Court of Appeal was whether a claim for unjust enrichment could be made where the SPA had expressly provided the basis of the payment as being consideration for the transfer of shares in Castlerose and such transfer had already completed.

The Appeal was argued on the basis that it was a matter of agreement that the Avonwick shares represented only USD 750 million of the total USD 950 million,000 which had been paid. The Appellants argued that the remaining USD 200 million was contingent on other things being transferred which did not happen.

Ultimately the Court of Appeal decided that the parties had taken a risk when entering in to the Castlerose SPA in the agreed terms by not being clear as to how consideration was allocated under the calculation of the price of USD 950 million. Of this sum USD 200 million was agreed as being assets other than the Castlerose shares but there was not an actual agreement for transfer of any additional assets as had been suggested.

Comments

This case highlights that a claim for unjust enrichment will face significant difficulties if used to seek to “override” contractual agreements and thus goes against the express intentions of the parties.

It is a reminder that unjust enrichment is not a licence to overwrite the black letter of any related written agreement which has been made by the parties.

The case is a timely reminder of the utility of having litigation input on corporate transactions which are managing expectations and redistributing assets following longstanding animosity between shareholders, in particular when the deal involves a variety of international companies and assets with differing approaches to asset valuation.