LITIGATION - UNITED KINGDOM

# *Caveat emptor*: buyer's inadequate notice precludes £3.5 million warranty claim

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## Introduction

In *Teoco UK Limited v Aircom Jersey 4 Limited*(1) the High Court held that a buyer gave inadequate notice of certain breach of warranty claims, thereby preventing it from pursuing those claims (worth around £3.5 million). The court held that the buyer did not specify the warranties in respect of which it was claiming, and that it was too "tentative and contingent" in the description of its claims.

The court's approach stands in stark contrast to the recent decision in *The Hut Group Limited v Oliver Nobahar-Cookson*.(2) It highlights the importance of complying strictly with applicable notice provisions.

## Facts

Claimant Teoco UK Limited was purchaser under a sale and purchase agreement. Teoco acquired two companies and their subsidiaries from defendants Aircom Jersey 4 Limited and Aircom Global Operations Limited.

The relevant clauses of the sale and purchase agreement were as follows:

- Clause 9.2 and Schedule 3 – the sellers gave certain general warranties to Teoco and tax warranties in relation to the tax affairs of the companies.
- Schedule 8 – under a tax covenant, the sellers covenanted with Teoco that they would be jointly and severally liable to Teoco in respect of the tax liability of the companies in six prescribed circumstances.
- Schedule 4 – the notice provisions stated that no seller would be liable for breach of warranty unless:
    - Teoco gave notice of the claim to the seller, setting out reasonable details of the claim (including grounds and an estimate of the amount of the claim); and
    - notice was given as soon as reasonably practicable after becoming aware of such a claim, and in any event on or before July 31 2015.

On February 19 2015 Teoco's solicitors wrote to the sellers regarding two potential tax claims. The letter contained the following key passages:

- "[W]e refer to the Tax Covenant, the Tax Warranties and the General Warranties."
- "[T]his letter constitutes notification in accordance with clause 24 and schedule 4."

These tax warranty claims were referred to as claims that "may exist" and "potential claims" with an "initial estimate of their possible quantum".

Teoco's solicitors wrote again to the sellers on June 2 2015. The sellers' solicitors responded on June 4 2015 stating that the letter contained only "high-level summaries of each purported claim" and that it was an inadequate notice of the claims. This prompted a further letter from Teoco's solicitors dated June 29 2015, which contained a detailed breakdown of the claims and their quantum.

On August 14 2015 Teoco commenced proceedings in relation to the tax warranty claims.(3) On December 18 2015 the sellers applied to strike out the tax warranty claims.

**Decision**

The court granted the sellers' application to strike out the tax warranty claims. It held that notice of the claims had not been given as stipulated by the sale and purchase agreement. It concluded that the letters of February 19 and June 29 2015 had failed to comply with the specific requirements of Schedule 4.

In reaching this decision, the court held that the following principles applied to the construction of warranty claim notice provisions:

- Every notification clause turns on its own wording; the court will construe the clause by focusing on the meaning of the relevant words in their documentary, factual and legal context (*Arnold v Britton*(4)).
- The underlying commercial purpose of contractual notices in this area is that of commercial certainty – sellers should know in sufficiently formal terms that a claim for breach of warranty is to be made, so that financial provision can be made for it and/or in order to allow the seller to remedy the breach or satisfy or settle the liability.
- There is a significant difference between notifying a party of a claim and notifying a party that a claim may be made.
- Where, as a condition of the seller's liability for breach of warranty, the purchaser is required to give some level of detail of the claim – a compliant notice should identify the particular warranty that is alleged to have been breached and state why.
- Proper compliance with contractual notice requirements is not a technical or trivial matter.

On the facts, Teoco had failed in both letters to identify the particular warranties that had been breached, save in the most general terms. Such failure was fatal. Further, in the first letter no claim was actually being notified; rather, what was being notified was a possible claim. The court held that a reasonable recipient of the first letter would not understand that it comprised the making of claims, as opposed to Teoco's notification that it had, or may have, claims.

As to the second letter, although the sums were specified, that letter still used language that referred to "possible or potential", rather than actual, claims.

As well as providing useful guidance on the rules regarding notice provisions and a helpful analysis of the case law surrounding it, the court started its judgment confirming that clauses cutting down a purchaser's rights should be construed *contra proferentem* (here, in favour of Teoco), or at least narrowly. Despite this, the court still found that Teoco had not complied with the notice provisions. As such, the claims were struck out.

**Comment**

The decision appears draconian, especially in circumstances where a second – clarificatory – letter was sent to the sellers that set out further details of the claims. The court placed great weight on the commercial purpose of the notice provisions, which appeared to be the principal driver behind its decision.

Further, the decision stands in stark contrast to the first-instance and Court of Appeal decisions in *The Hut Group Limited v Oliver Nobahar-Cookson*, neither of which were referred to by the judge in *Teoco*. In that case, both the High Court and the Court of Appeal applied the same rules of contractual construction, in particular *Arnold*. In *Hut* the defendants had alleged that the notice of breach of warranty claims was similarly deficient (in that the notice had not provided sufficient detail within the prescribed time limit). However, the notice in *Hut* did specify an actual claim in respect of

specific warranties, albeit that the judge at first instance held that "not much was contractually required" in the notice and that "details [of breaches of warranty claims] would likely follow [the notice]". In those circumstances, both at first instance and on appeal, Hut held that the notice had complied with the applicable notice provisions.(5)

Finally, the decision serves as a reminder that contractual construction cases turn on their own facts, and can be interpreted differently by different judges. While this is by no means a new lesson, it again highlights the importance not only of clear drafting of commercial documents, but also of strict compliance with seemingly 'formalistic' notice requirements.

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**Endnotes**

(1) [2015] EWHC (Ch) (unreported).

(2) [2014] EWHC 3842 (QB); [2016] EWCA Civ 128.

(3) Teoco also made certain other warranty claims against the sellers, which were not the subject of the strike-out application and this decision.

(4) [2015] AC 1619, per Lord Neuberger at 1627G.

(5) The Court of Appeal, applying *Arnold*, stated:

> "*the natural meaning of the language is by no means so clear as to preclude serious consideration of the commerciality or otherwise of rival interpretations or, for that matter, to preclude recourse to the principle that ambiguous exclusion clauses should be construed narrowly*."

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