De Sena v Notaro [2020] EWHC 1031 (Ch): The family, the demerger and the expert who wasn't an expert

The parties

The case arose out of a corporate demerger which took place in relation to a family owned company, S Notaro Holdings ('Holdings'), on 28 April 2011. The First Claimant (C1), and the First Defendant (D1) were siblings. Prior to the demerger, they were both shareholders in and directors of Holdings. Neither were majority shareholders. D1 held 43.75% of the shares in Holdings, and C1 held 31.25%. In the demerger, C1 gave up her shares in Holdings in exchange for some assets of Holdings or its subsidiaries being transferred to the Second Claimant (C2), a company formed for that purpose, owned and controlled by C1.

The Second Defendant (D2), was the company which, following the demerger, would retain the remaining assets of Holdings. In essence, the claim against D1 and D2 was that the demerger was procured as a result of undue influence by D1, that D1 acted in breach of fiduciary duty to C1, and that D2 had been unjustly enriched at C1 or possibly C2's expense.

The Third Defendant (D3) was a firm of accountants who had been retained to act on the demerger. The Fourth Defendant (D4), was a firm of solicitors who had been similarly retained. It was alleged that D3 and D4 had acted in breach of their duty of care to C1 and C2, were in breach of fiduciary duty, and that (D4 only) was in breach of contract. Both Defendants' position, broadly, was that they had been retained by Holdings rather than C1 or C2, and consequently did not owe a duty to either in tort or contract and that no fiduciary duty had arisen.

C1 alleged that, following their father's death in 1993, D1 had become increasingly controlling towards other family members and in 2003 had commenced a campaign to expel her from the business, and that this had continued up until the demerger.

It was a central tenet of the Claimants' case (against all Defendants) that, because C1 had held 31.25% of the shares in Holdings, she was accordingly entitled to 31.25% of the group's assets following the demerger.

Findings

In relation to the claims against D1, HHJ Paul Matthews held that C1 had found it difficult to adjust when D1 had taken over from their father as managing director: '*she did not like the fact that it was now her younger brother (whom she had helped to look after) and not her father making business decisions and giving the instructions*' (paragraph 91). The court took into account the fact that D1 was a minority shareholder, and could have been removed by the others, had they so wished.

It was also material that, once or twice every year, D1 and C1 would sit down together to revalue the company's assets. At these meetings, they would go over the land and buildings

owned by the group and consider whether the value of these properties ought to be altered to reflect their current view of what they were worth. These were never the subject of any third-party valuation.

Moreover, after hearing evidence from both C1 and D1, the judge rejected the notion that a deal more beneficial to C1 could have been negotiated. He found that, just as C1 had some reservations about the assets she was receiving for her shares, D1 had '*been pushed as far as he would go'* (paragraph 137).

Ultimately, the court found that there had been no undue influence by D1 towards C1. This was not a case in which they had a relationship giving rise to a presumption of undue influence, so actual undue influence had to be proven. The Claimants had failed to do so. This was not to say D1 did not put *any* pressure on C1. He was a businessman who was not averse to looking after his own interests. However, C1 had failed to prove any conduct by D1 that amounted to improper or illegitimate pressure, or coercion.

Furthermore, the court held that the assertion that C1 '*was entitled to a pound for pound equivalence between her share in the company and the assets she received [was] entirely without foundation'* (paragraph 220). This would suggest that she owned a proportion of the company's assets. This was an '*elementary error'* which had been '*exploded long ago'* by the House of Lords in *Macaura v Northern Assurance Co Ltd* [1925] AC 619 (paragraph 220). No shareholder had the right to any property owned by the company. Rather, a shareholder was entitled to a share in the company's profits whilst it carried on business, and a share in the distribution of surplus assets when the company was wound up. As a demerger was a consensual transaction, she did not have an entitlement to any particular share of assets, but only to what she could obtain by negotiation. There was no basis for saying that her shares were disposed of at an undervalue.

In relation to the claims against D3, it was found that, at no point had D3 been advising C1 personally as a shareholder as against the interests of the other shareholders or the company. At every instance, it was found, D3 had been acting for the company. Furthermore, the court accepted the evidence of David Savill, an employee of D3, that at a meeting in March 2011 he had advised C1 to obtain independent valuation advice. Therefore, no duty of care or fiduciary duty had arisen.

As to the claims against D4, it was found that the partner at D4 dealing with the transaction had made it clear to C1 and D1 at a meeting on 10 March 2011 that D4 was acting only for the company and not the shareholders. Furthermore, though D4 had received the list of properties to be transferred to C2 in the demerger, D4 had had no role in selecting or negotiating those properties. It was also found that each step of the demerger had been explained to C1 and the other shareholders by D4. The court rejected the submission that the fact that D4 had acted for C1 personally in the past, and was at the time of the demerger acting jointly for D1 and C1 personally in relation to a family dispute against another sibling, was a sufficient basis to found a personal duty to C1 in relation to the demerger. As regards the demerger its role was limited to preparing the legal documents for a pre-agreed deal: '*a kind of "execution only" role'* (paragraph 261).

The expert evidence

It is perhaps the section of the judgment which deals with the parties' expert evidence which is of greatest general interest. Indeed, it serves as a stark warning of the mistakes which litigators should avoid when instructing experts and putting questions to them.

Expert evidence was adduced by the parties on 3 issues: (i) property valuation (with Mr Gladwin giving evidence for the Claimants, and Mr Jones giving evidence for the Defendants); (ii) share valuation (Mr Mesher for the Claimants and Mr Butterworth for the Defendants); and (iii) aspects of accountants' liability (Mr Mesher for the Claimants and Mr Plaha for D3).

In summary, the court was unimpressed with the expert evidence before it on issue (iii). 2 problems are identified in the judgment:

1. Whether Mr Mesher or Mr Plaha in fact had the appropriate expertise to give evidence on demergers; and

2. The questions posed to the parties' respective experts; namely the fact that they were asked to advise on issues of law and fact that were a matter for the tribunal.

On the first point, the court expressed reservations regarding the '*assumption made by the parties that, no doubt because accountants regularly advise clients on demergers such as to acquire the relevant expertise therefore* any *accountant, whether he has the experience of advising clients on demergers or not, is qualified as an expert witness in this field*' (paragraph 154). The judge observed that, on scrutinising Mr Mesher's CV, there was no reference to any experience in demerger transactions in his list of professional specialisms; neither did Mr Plaha's CV state that he had any experience in demergers. After this was raised with counsel, a supplementary document dealing with Mr Mesher's expertise in more detail was provided. However, this stated frankly that Mr Mesher did not '*claim to be an expert in "demergers" per* se' (paragraph 156), but that from 1993 to 2010 he had worked at KPMG and had been exposed to various M&A transactions, had worked at Grant Thornton where he had dealt with the drafting of sale and purchase agreements, and that from 2012 he had been practising at his present firm where he had dealt with many post-transaction disputes. However, the judge found that, whilst he may have had the opportunity to see one or more demerger transactions and may even have participated in them, this did not make him an expert in demergers, and '*it is for the expert witness tendered to demonstrate the expertise, not for the court to assume it'* (paragraph 156).

In the circumstances, the court found that neither Mr Mesher nor Mr Plaha had acquired sufficient experience in carrying out demergers to be able to claim expertise in the area. The judge stated the general principle as follows:

Those firms that provide expert witness services really ought to have learned by now that expertise is acquired by doing the thing in question, usually over many years, and that merely being an accountant (or anything else) for a long time does not mean that you thereby become an expert in everything *that accountants (or whatever it may be) commonly do* (paragraph 157).

Given that the court had disregarded both the Claimants' and D3's evidence on accountants' liability, it was strictly unnecessary to examine the substance of that evidence. Nonetheless, the court took the opportunity to raise grave concerns about the questions that had been put to the respective experts.

For the Claimants, Mr Mesher had been asked to consider a number of questions, including:

> *(i) What were the terms of the contractual retainer which BF [of D3] had with SNHL group of companies (the 'Group')?*
>
> *(ii) Was the Group's retainer limited to BF's function as auditor?*
>
> *(iii) If so, should BF have entered into a further contractual retainer to advise the Group of a demerger?*
>
> *(iv) In order to advise the Group on a demerger would it have been necessary to have the assets of the Group independently valued?*
>
> *(v) What are the circumstances in which BF could act for the Group and also advise the shareholders on a demerger?*
>
> *(vi) In particular, would BF need clear written instructions from each of the shareholders that there was no conflict of interest inter se and that the terms of the demerger had been agreed?*
>
> *(vii) BF's case is that it was acting for the Group and not the shareholders. If it became apparent to BF (or if BF ought reasonably to have concluded) that there was no agreement between all the shareholders as to the terms of the demerger, should BF have:*
>
> > *(a) advised [C1] that it could not continue to act for her and that she should be independently advised; and, or*
> >
> > *(b) ceased to act for any party on the demerger?*
>
> *(viii) would a reasonably competent chartered accountant in the position of DS or AB have considered it necessary to record in writing any suggestion given orally to [C1] (none being admitted) firstly as to the conflict of interests and secondly that she should obtain separate accountancy of valuation advice?*
>
> *(ix) do you consider that BF came under a duty of care to [C1] or [C2] having regard to the principles set out in the case of BCCI (Overseas) Ltd (in Liquidation) v Price Waterhouse…*
>
> *(x) What was the scope of BF's duty, if so, when did arise?*

On these questions, the judge stated, in rather uncompromising terms:

> *I have to say that I have never before seen such an extraordinary set of questions put to a witness being asked to give expert evidence. Questions (i), (ii) and (iv) are mixed questions of law and fact, both of which are for the court and not this witness. Question (iii) is not relevant, given that the third defendant obviously did advise on a demerger. Questions (v) and (vii) are questions of law for the court. Questions (vi) and (viii) are, to the extent that they are relevant at all, questions of law for the court. Question (ix) is one of the most egregious and naked usurpation of the functions of the court that I have ever seen. Moreover, since it refers only to one authority (and that more than 20 years old, when there have been many relevant decisions since), even if it were admissible, it would be of no use to the court. Question (x) is almost as egregious and objectionable. I am unable to regard the answers to any of these questions as admissible evidence in this case. I am astonished that these questions were asked at all, and almost as astonished that they were answered* (paragraph 159).

The court did consider that question (xi) was better than the others, as it did concentrate on important aspects of the *Bolam* test; however, this question still failed to ask whether or not the particular Defendant's actions fell below the standard required of a reasonably competent firm of accountants.

The judgment is almost as critical of the questions put to Mr Plaha, specifically:

> *(a) whether BF had a duty to advise [C2] and/or [C1] personally, and specifically:*
>
> *(i) in circumstances where BF were engaged by SNHL and/or the Notaro Group from whom were BF entitled to take instructions?*
>
> *(ii) Were BF engaged formally to act for [C1] personally?*
>
> *(iii) Did BF assume responsibility to advise [C1] personally?*
>
> *(iv) Were BF formally engaged to act for [C2]?*
>
> *(v) Did BF assume responsibility to advise [C2]?*
>
> *(b) Comment upon the following issues that would only be relevant if the Court were to determine that BF owed a personal duty to [C1] and/or a duty to [C2] (which BF denies):*
>
> *(i) The advice which [C1] should have received in relation to the alleged duty to advise her to obtain an independent valuation of assets. In particular, what with the duty of a reasonably competent firm of accountants have been and, in the circumstances of this case, did the actions of BF fall short of that standard?*
>
> *(ii) BF's duty to advise [C1] on the impact of the bulk transfer discount on her and/or [C2]*
>
> *(c) Explain the reasons for the second capital reduction and comment on:*
>
> *(i) What was the reason for the second capital reduction; and*
>
> *(ii) The effect of the second capital reduction on the value of [C1] shareholding in [C2].*

(d) Comment on the allegations in relation to the Clearance Letters.

In commenting on these, the judgment concludes:

> *Question (a) is just as objectionable as questions (ix) and (x) were in Mr Mesher's report. They are questions of law for the court. The first sentence of question (b) (i), the first 15 words of the second sentence and the whole of question (b)(ii) are also questions of law, and likewise objectionable. The remainder of question (b)(i) is acceptable. Question (c)(i) is a question of fact, which is also for the court (and on which the witness has none but hearsay evidence to give). Question (c)(ii) is partly a matter of law, but partly a matter of share valuation expertise, which I do not understand Mr Plaha (or Mr Pooler) to claim to possess. Question (d) is hardly a proper question at all* (paragraph 162).

In short, both parties' expert evidence in respect of accountants' liability was rejected wholesale, due to both the lack appropriate expertise of the experts, and the nature of the questions put. Clearly, this was a stark result. It provides a cautionary tale for litigators, and serves as a reminder that:

1. When instructing experts who are to give evidence in a specific field of a discipline, be sure to enquire whether that expert has the appropriate experience and expertise in that field. Do not assume, because they are an expert in that discipline, and may have had some exposure to the field in question, that a court will accept that they have the appropriate expertise. As stated in the judgment, it is for the party tendering the expert to demonstrate that that expert has the appropriate expertise.

2. When putting questions to an expert, the *Bolam* test is central. Any gloss on that test is undesirable. Questions which are nakedly questions of law, fact, or mixed questions of both, should be avoided at all costs. For example, when asking about the appropriate construction of D3's retainer, it may have been more prudent to ask: On reviewing D3's retainer, would a responsible body of accountants consider the that that retainer limited D3's function to that of an auditor? Depending on the answer that was given, this may have provided strong evidence as to the scope of D3's duty, without usurping the role of the court.

In relation to the expert evidence tendered by the parties on property and share valuation, the court held that there were no such problems. However, the court observed that D1 and D2 had mounted an argument that such evidence was not relevant on the basis that a shareholder was not entitled to the proportion of company assets correlating to her proportion of the shares.

Conclusion

The judgment is interesting primarily due to the treatment the expert evidence received by the court. However, the case also provides a useful illustration that, when professional advisers are clearly retained by a family company, it can be very difficult for a shareholder of that company to establish that any duty was owed concurrently to them personally. This was

even true in D4's case, despite the fact the firm had acted for C1 personally in the past and was continuing to act for both C1 and D1 in an ongoing family dispute against their other sibling.

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