

## ***VC Company to pay over £2 million in damages for breach of Confidentiality Agreement***

The English High Court recently ordered a venture capital company to pay more than £2 million in damages for exploiting a business opportunity identified and disclosed to it in confidence by the Claimants, in breach of Confidentiality Agreements.

The facts of *Vercoe, Pratt and Anr v Rutland Fund Management Ltd and Others* are complex; stated simply the case concerned the exploitation of a business opportunity identified by two young businessmen, Mr Vercoe and Mr Pratt (the 'Claimants'), disclosed in confidence to the venture capital company, Rutland Fund Management Ltd (RFML), with a view to raising finance for a management buy in of a target business. During the course of negotiations which began in September 2003 with the execution of a confidentiality agreement and continued for the best part of a year, the Claimants disclosed in detail the business opportunity they had identified and provided RFML with copies of the business plan that they had developed for the acquisition and their financial model for developing the target business to increasing its efficiency and profitability. The management team proposed by the Claimants, although not identified by name in the Confidentiality Agreement, included themselves as CEO and Commercial Director and a named Chairman who they had already approached and briefed for the position.

Despite having decided at an early stage that neither of the Claimants were suitable for the positions they were seeking as they lacked commercial experience, RFML encouraged the Claimants to continue to work to promote and develop the acquisition and strengthen their business plan. In March 2004 Mr Pratt was dropped from the negotiations following RFML's disclosure that it regarded him as lacking commercial experience to be part of the management team post acquisition. In July 2004 Mr Vercoe fell out with RFML because the latter refused to appointment the former as CEO of the target company following the acquisition preferring instead to leave the existing CEO in post.

In spite of correspondence from the lawyers for the Claimants in August 2004 warning that the acquisitions would be in breach of Confidentiality Agreements RFML had entered into with the Claimants, RFML proceeded with the acquisitions in September 2004 without involving either of the Claimants. Although RFML did not adhere to the business plan prepared by the Claimants, it did appoint the Chairman they had proposed. Following completion of the acquisition, RFML paid an introductory fee of £490,000 (representing 1% of the purchase price) to the accountants who had originally introduced RFML to the Claimants and sent a cheque for £25,000 to Mr Pratt, but this was returned.

Despite the actions of RFML, the Claimants chose not to issue legal proceedings immediately but instead waited until 2008 before starting proceedings. Their decision to initiate proceedings was ultimately triggered

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by publication of the financial results of RFML in 2007 which revealed that it had realised a profit of over £30 million on its investment following the flotation of the target company in May 2006.

Although such a delay in issuing legal proceedings for this type of action is unusual, the judge hearing the case indicated that he did not find it surprising or objectionable given the considerable cost and risks associated with litigating, in the circumstances it was entirely understandable that the Claimants should wait to see if the business was a success.

However understandable the delay, one consequence was that recollections of the events at issue were not as clear as they might have been, resulting in a greater reliance being placed by the judge on the limited number of contemporaneous notes made by the parties rather than on their subsequent statements. This was to the Claimants advantage as they had more contemporaneous notes than the Defendants.

The judge held that the effect of the confidentiality agreements that the parties had signed at the outset was to restrict RFML's use of the information disclosed to the acquisition of the target company with a specific management team. RFML sought to argue that the contracts were too vague to be binding or to commit them to a specified management team, but the judge disagreed. He went on to find that there had been a breach of the Confidentiality Agreement in that the information disclosed had been used for a purpose other than that permitted because the management team ultimately appointed was not that originally proposed.

The judge acknowledged that the standard approach to the assessment of compensation was to determine the compensation necessary to put the innocent party back into the position it would have been in but for the breach, however, where there were several possible outcomes (e.g. the del might not have proceeded at all) the court would ordinarily have to analyse and assess each one and the chances of it occurring. However to limit these complexities (and the associated cost) the parties agreed instead that damages should be assessed on the basis that the Defendants had agreed to pay the Claimants for their consent to use the information for a different purpose (or rather, a different management team). The judge dismissed as inappropriate the Claimants' demands for an account of all the profits made by the Defendants. Instead, taking into account expert evidence, he awarded £860,000 calculated on the basis of a notional payment of a 3% equity stake to Mr Pratt for his consent to use the information for a different specified purpose and 5% or £1.72 million to Mr Vercoe.

### ***Impact***

We often hear clients questioning the merits of entering into confidentiality agreements believing them to be difficult to enforce. This case should reassure clients that such documents are not only worthwhile but can provide a sound basis for challenging in court commercial Goliaths who might otherwise pay them little regard. Confidentiality Agreements are not however a panacea. Accurate contemporaneous notes of discussions can also play an important role in determining the merits of a case as can the behaviour of the parties.

*This case summary has been prepared for information purposes only and does not constitute legal advice.*

*For more information about this and other recent intellectual property decisions and how they might affect your business please contact me, **Belinda Isaac, on 01865 516449** or email me: [Belinda.isaac@isaacandco.com](mailto:Belinda.isaac@isaacandco.com).*