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COURT OF APPEAL CONSTRUES A W&I POLICY

***Project Angel Bidco v Axis and others*[1] concerned a buyer-side warranty & indemnity policy, underwritten on behalf of Project Angel Bidco Ltd (PABL). A W&I policy allows a buyer of a company to insure the risk that the target is not in the state warranted by the sellers, and so worth less than the purchase price. The case is a useful illustration of how a policy will be construed, in a W&I context.**

Background

In November 2019, PABL entered into a share purchase agreement ("SPA") for a civil engineering and construction company (the "target company") and then negotiated a W&I policy.

This policy was unusual it that it would more commonly be negotiated in parallel with negotiations between the buyer and seller, but in this case placement took place after exchange of the SPA but before completion. The policy was heavily negotiated by insurers and the broker on behalf of the insured.

It was subsequently alleged that the sellers were in breach of certain warranties, although the details of this were confidential and under investigation by the police. As a result, it was said that a key client of the target company ceased or severely reduced its business with the company, the shares in the target company were worth less and PABL suffered a loss of £11 million. PABL sought to recover up to the maximum limit of indemnity of £5 million under the W&I policy, but insurers denied cover.

Issues

The key issue was PABL's argument that there was a contradiction between the extent of cover provided by the insuring clauses and the exclusions from cover.

The warranties in the SPA included a number of bribery and corruption related warranties (at clause 13.5). These are not set out in full here due to their length, but they included statements that amongst other things, neither the company nor the sellers were aware of any officers, directors, employees or others committing any bribery offences under the Bribery Act 2010 or under any legislation or common law anywhere in the world; that the company had procedures to prevent any person working for it from committing offences of bribery, corruption or facilitation of bribery or corruption; and that neither the company nor the sellers were aware of any officers, directors, or employees being the subject of any investigation or enforcement proceedings or of any threatened or pending investigations or proceedings.

The policy included cover for any breach by the seller of a list of obligations set out in a "Cover Spreadsheet". This contained a table which indicated that warranty 13.5 was "*covered*". However, the wording of the policy excluded cover for loss arising out of any "*ABC Liability*" which was defined as

"*any liability or actual or alleged non-compliance by any member of the Target Group or any agent, affiliate or other third party in respect of Anti-Bribery and Anti-Corruption Laws*."

PABL argued that if the exclusion was read literally then no loss arising out of a breach of warranty 13.5 could ever be covered. It was said that there had been a mistake in the drafting of the ABL Liability definition and it should have read as follows:

"*any liability **f**or actual or alleged non-compliance by any member of the Target Group or any agent, affiliate or other third party in respect of Anti-Bribery and Anti-Corruption Laws*." (ie or became for)

PABL argued that there was an obvious error in the policy and a clear means of curing it.

At first instance the judge found in favour of insurers, and PABL appealed.

[1] [2024] EWCA Civ 446

Judgment

The Court of Appeal dismissed the appeal by majority, with Phillips LJ dissenting.

Majority decision

Lewinson LJ gave the leading judgment.

Firstly it was noted that this was a specialist policy. Secondly, the loss insured by the policy was the difference in value of shares as warranted and their true value, and not the loss (if any) suffered by the target company itself. It was also relevant that PABL was able to claim under the policy without exercising any right of recovery against the sellers and the insurer's right of subrogation was excluded except in cases of seller fraud. The result of this was that, whilst PABL may have wanted the cover to be as wide as possible, insurers would have wished to limit their liability where they had no right of recourse against the seller and no opportunity to carry out due diligence on the target company.

PABL sought "rectification by construction" on the basis that there was an obvious error and a clear means of curing it.

Lewinson LJ noted the relevant rules to be applied in determination of this issue. Firstly, as a general proposition parties to a contract intend all of it should be effective, however there are sometimes different parts which are in conflict. The contract itself may provide for an order of preference (such as making one clause "subject to" another), or the nature of the apparently inconsistent clauses may lead to the answer. The location of the clauses may be relevant, as it may be obvious that one clause is intended to have higher contractual status than another. (This was the approach taken by the Supreme Court in *FCA v Arch* where an extension for business interruption cover for notifiable disease was not excluded by a general exclusion for pollution or contamination on page 93 of the policy). There was some dispute about the order in which a reasonable reader would read the parts of the policy, but Lewinson LJ found that this was an arid argument as the interpretation of the policy required consideration of it as a whole.

Lewinson LJ noted that there was on the face of it some inconsistency in the PABL policy, and it appeared that cover given with one hand was taken away with the other. If there was a mistake, then it would have to be a mistake common to both the parties and so it was necessary to consider the question from the point of view of the policyholder and underwriters.

PABL's proposed correction would confine the exclusion to cases of *"liability"* and so bring within the cover a diminution in share value attributable to an allegation of non-compliance with anti-bribery law even if the allegation was never proved or even investigated. For example, if the target's main customer became aware of an allegation of non-compliance and decided to cease business with the target that could impact the share value, and would then, on PABL's interpretation, be covered. However, it could not be forgotten in this context that warranty 13.5 extended to any legislation, common law, or regulation anywhere in the world. Therefore the wording of the exclusion as it was had a rational explanation from the point of view of insurers.

The Judge also found that although the definition of ABC liability was not a masterpiece of drafting, nor would it be if it was corrected as PABL proposed. Therefore, he was not persuaded that there was a clear drafting error.

Finally, in order to correct a drafting mistake by interpretation, the cure must also be clear (following *Arnold v Britton*). But it was not clear here whether the mistake would be in drafting the exclusion, or if it was in including warranty 13.5 among the obligations covered.

Therefore the appeal was dismissed.

Dissenting judgment

Phillips LJ gave a dissenting judgment. In his view the policy should be interpreted together with the SPA and the commercial purpose and intended effect of the policy must be understood in that context. The sellers were released from liability for the warranties listed in the policy, and their approval of its terms was a precondition of completion of the SPA.

Phillips LJ considered that there was a clear conflict in the wording here of the same type as a policy that has a specific term covering property damage caused by flood, that also has an exclusion for loss caused by flood. The inclusion of the exclusion rendered the use of the term "covered" in relation to warranty 13.5 wrong. Phillips LJ noted that the sellers, when approving the policy, would have considered that they were released from the warranties contained in the Cover Sheet, including warranty 13.5, and would not have appreciated the position was reversed by the exclusion. In conclusion, the wording of the ABC Liability exclusion was obviously wrong.

Phillips LJ considered that the cure proposed by PABL fixed all of the problems with the exclusion, removed awkwardness in the language, avoided rendering the concept of liability in the exclusion redundant and was consistent with the overall policy structure.

Conclusion

The judgment is a useful example of how the courts will interpret inconsistent aspects of policy wording, particularly in a W&I context. It is a reminder that whatever the position according to the warranty spreadsheets attached to the policy, coverage will still be subject to the full terms and conditions of the policy, including any exclusions.

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