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Insights

COVID-19: HIGH COURT ISSUES PRELIMINARY RULING ON INTERPRETATION OF MATERIAL ADVERSE EFFECT CLAUSE

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In a dispute between WEX (Inc.) ("**WEX**") and the shareholders (the "**Sellers**") of eNett International (Jersey) Limited ("**eNett**") and Optal Limited ("**Optal**"), following an expedited trial on a number of preliminary issues, the High Court's judgment (*Travelport Limited & Others v WEX INC* [2020] EWHC 2670 (Comm)) provides helpful guidance on the interpretation of material adverse effect ("**MAE**") clauses which are not commonly used in English law acquisition documents.

The judgment is also notable for the proactive and efficient approach of the Commercial Court to resolving time critical issues in the most proportionate manner against the background of the COVID 19 pandemic.

Background

On 24 January 2020, WEX entered into an SPA with the Sellers to purchase eNett and Optal for approximately $1.7 billion. Following signing but before the transaction completed, the Covid 19 pandemic adversely impacted (how adversely to be determined in the main trial) eNett's and Optal's businesses due to the collapse of the worldwide travel market. On 4 May 2020, WEX sent a letter providing notice that there had been a MAE under the SPA due to Covid 19. As a result WEX argued that under the SPA it was not obliged to complete the transaction. The Sellers sought declarations from the Court that there had been no MAE and for specific performance under the SPA.

"Material Adverse Effect" was defined in the SPA. As is usual in such agreements, it had a number of "carve-outs". Certain of these carve-outs then had their own "exception". Conditions resulting from pandemics was one of the carve-outs, however, this pandemic carve-out was then covered by the exception. The effect of the exception was that if the pandemic and its effects had a disproportionate effect on eNett or Optal (or their subsidiaries) as compared to other participants in the "*industries*" (a key word) in which they operated, there would be a MAE.

The Decision

Whilst there were a number of preliminary issues which the Court was asked to decide, a key consideration for the Court was the definition of "industry" in the MAE clause. This would determine the comparator against which eNett / Optal would be measured in order to determine whether they were disproportionately affected by other participants in the industry. The Sellers' position was essentially that industry referred to the "travel payments industry" while WEX's position was that there was no such thing as a travel payments industry and that the appropriate industry was the "business to business" (B2B) payments industry or the payments industry.

On the key issue of the definition of industry the Court considered that the relevant industry was the B2B payments industry. The Court also found that there was insufficient evidence to establish the existence of a "travel payments industry" (either in the limited sense the Sellers suggested or even in a wider sense).

In approaching the construction and interpretation of the MAE clause, the Court was focussed not simply on the literal meaning of the words but on the balance between the words used and the contract as a whole. This meant giving more or less weight to elements of the wider context "*depending on the nature, formality and quality of drafting of the contract*".

The Court chose to give considerable weight to the choice of the parties, given the SPA was a "*complex heavily lawyered*" document. It deemed the use of "industries", as opposed to possible alternative words such as "markets" or "sectors" or "competitors", significant. Use of one of the narrower set of words might have suggested the comparison set out in the MAE clause should be triggered by firm specific issues only. By comparison, "industry" was a broader word that connoted scale and a high level of generality. This was also supported by other references to industry in the SPA and elements of the expert evidence before the Court.

The Court also considered the changes of regulatory or political conditions or law carve-out. The exception did not apply to this carve-out and the question was: if the collapse in travel was connected to conditions resulting from the pandemic as well as changes in the regulatory or political conditions or law, could this still come within the exception to the carve-out. The Court decided in the Sellers' favour. If an event was excluded from being an MAE by a carve-out to which the exception did not apply, that conclusion could not be negated simply because those changes in law were also essentially caused by a pandemic (a carve-out to which the exception did apply).

Conclusion and take away points

It is never possible to cover every eventuality in a commercial contract, however, this decision may cause transactional lawyers to reconsider whether any ambiguous or undefined terms in their MAE clauses (particularly comparator terms used in the way "industry" was in this case) require addressing.

That being said, a running theme throughout the judgment was the possibility that ambiguity in MAE clauses may have a separate purpose that could drive the parties in such a dispute to renegotiate a transaction rather than simply pull out of it altogether or resort to litigation. The Court's judgment, which has elements both sides could regard as decided in their favour, may well result in renegotiation and settlement. On the other hand, it currently appears both sides intend to appeal the decision and given the value of the transaction it may be that the parties are simply too far apart. Only time will tell.

Stepping back, this judgment is a strong advert for the benefits of having English law and jurisdiction governing transactions, and particularly for complex commercial transactions which can be considered by the Commercial Court. This is a highly complex dispute which was obviously hard fought on both sides. Despite this, the Court's decision arrived only five months after proceedings were first issued. There will undoubtedly be a considerable amount of litigation brought as a result of Covid and judgments like this demonstrate the English courts are well equipped to handle it, both in terms of the trials themselves (in this case heard as a "hybrid" hearing) and in the timing of any decision.

Finally, this case is notable as being one of the few English cases to consider an MAE clause in the context of an SPA. Due to the lack of relevant English authority, the Court reviewed US authorities which, although not binding or formally persuasive, were helpful to the Court. It is notable that Delaware, the leading forum for such cases, is well known as reluctant to uphold a finding that there has been a MAE. It will be interesting to see whether the English Courts display the same reluctance, both in this case and in the others that will surely arise.

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