Neutral Citation Number: [2020] EWHC 32 (QB)

Case No: HQ18X01039

IN THE HIGH COURT OF JUSTICE
QUEEN'S BENCH DIVISION

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 13/01/2020

Before :

MR GAVIN MANSFIELD QC
(Sitting as a Deputy Judge of the High Court)

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Between :

DEMAND MEDIA LIMITED	**Claimant**
- and –	
KOCH MEDIA LIMITED	**Defendant**

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- -

MS SARAH BAYLISS (instructed by **Keystone Law**) for the Claimant
MR LLOYD MAYNARD (instructed by **Shoosmiths LLP**) for the Defendant

Hearing dates: 22-26 July 2019

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Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

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THE DEPUTY JUDGE:

INTRODUCTION

1. This is a dispute about the termination of a distribution agreement between the Claimant ("Demand") and the Defendant ("Koch"). The agreement concerned distribution of DVDs, DVD/gift sets, and "gifting products" such as construction sets.

2. Demand is a company which carries on business designing and distributing DVDs and gifting products. Demand is owned by Mr Jason Fenwick, who is also a director of the company.

3. Koch is an English subsidiary of a German-Austrian media enterprise. In the UK it manufactures and distributes digital entertainment products and accessories. It distributes the products of others, and it also develops and sells its own products.

4. Demand entered into two agreements with Koch for the distribution of its products. The first agreement, made in 2014, ran until April 2015 when it was replaced by a second agreement ("the Distribution Agreement") which is the subject of these proceedings.

5. Products distributed by Koch under the Distribution Agreement were sold to a range of retailers, both online (such as Amazon) and traditional "bricks and mortar" retailers. Products were commonly sold to retailers on consignment, meaning that the retailers did not themselves have to pay for products until they sold them.

6. Over the lifetime of the Distribution Agreement (and the first agreement that preceded it) Demand did not, on the whole, supply products to Koch to sell on its behalf. Instead, Demand supplied product ideas and licensing rights. Koch was responsible for manufacturing products and for their distribution and sale. Koch financed the manufacture of products and recouped its manufacturing costs from the proceeds of sale.

7. Mr Fenwick describes the commercial arrangement at the commencement of the relationship between the parties in his second statement at paragraph 5: "Koch offered us a full production, manufacturing, finance, sales and distribution facility. This meant that Demand could focus on releasing lots of own brand and licensed products with this support. Koch suggested they had supply chains in place for manufacturing and customers to supply to."

8. Demand terminated the Distribution Agreement by notice given on 19 January 2018, as it was entitled to do. The agreement ended on 31 March 2018.

THE ISSUES

9. There is no agreed List of Issues; each party produced its own. In broad summary the issues I need to determine are as follows. The terms used in this summary are defined elsewhere in the body of this Judgment or are terms defined by the parties and used at trial.

   i) **The Book People Sale**. After Demand served notice to terminate it requested 50,000 items of stock to be returned to it, and in due course made an application to the Court for delivery up of its stock. Koch gave an undertaking, scheduled to a Consent Order, to return all stock that was unsold as at 29 March 2018. After service of the application, Koch sold a large amount of premium stock to The Book People (a retailer) at what Demand claims to be a drastically reduced price. Demand's case is that Koch acted in breach of contract by (a) selling the stock rather than returning it; and/or (b) selling the stock at a reduced price not approved by Demand. Demand puts the claim alternatively in conversion. Demand claims damages, including damages for consequential losses.

   ii) **Unpaid Monthly Sums**. Demand claims that Koch acted in breach of contract by failing to make monthly payments required under the Distribution Agreement in respect of December 2017 and January 2018 sales.

   iii) **The Missing Stock and the Further Missing Stock**. Demand claims that even after termination (and after the undertaking to return stock) there remains stock that was not returned for which Koch is liable.

   iv) **The Final Account**. After termination Koch delivered a draft final account. That has been revised, resulting in version dated 13 February 2019. That shows a balance owing to Koch. Demand argues the final account is wrong, and that in fact sums are owed to Demand. The principle areas of difference are:

      a) Manufacturing costs in respect of stock sold on consignment to WH Smith which was subsequently destroyed by WH Smith when unsold ("the WH Smith Debited Sum").

      b) A figure in respect of a retrospective credit credited by Koch to WH Smith ("the Further Debited Sum").

   v) **The Flying Scotsman Indemnity**. This is linked closely to The Book People Sale. Demand claims that one product forming part of The Book People Stock was sold in breach of a minimum price agreement between Demand and the licensor of the product.

   vi) **The Copycat Product Claim**. In 2017 Koch launched some construction kits through its own "Smart Fox" brand. Demand claims that in doing so Koch acted either (a) in breach of an implied term not

to compete; and/or (b) in breach of a contractual, equitable or tortious duty of confidence.

10. The Re-Amended Particulars of Claim ("RAPoC") include a claim for breach of a registered design right in a Spitfire construction set. The Re-Amended Defence challenges the validity of the registered design right. The Defendant applied to have that claim, and its challenge to the registered design right, transferred to the Intellectual Property and Enterprise Court ("IPEC"). I heard that application at the beginning of the trial. I made an order transferring that claim to IPEC, and it formed no further part of this trial.

THE WITNESSES

11. I heard evidence from the following witnesses:

    i) On behalf of Demand:

        a) Jason Fenwick, owner and a director of Demand.

        b) Melissa Barclay, Demand's financial manager.

    ii) On behalf of Koch:

        a) Craig McNicol, Managing Director (Northern Europe) of Koch.

        b) John Cronin, Sales Director of Home Entertainment and Boxed Gifting employed by Koch.

        c) Carl Edwards, Senior Merchandiser employed by WH Smith.

        d) Karl Penhaligon, Head of Vendor Management employed by Koch.

        e) Ben Jones, Senior Business Development Manager employed by Koch.

THE DISTRIBUTION AGREEMENT, ITS CONSTRUCTION AND IMPLIED TERMS

The first agreement

12. Before coming to the Distribution Agreement it is useful to consider briefly its predecessor. This agreement, and its terms, forms part of the factual matrix against which the Distribution Agreement falls to be construed. On 1 March 2014 Demand and Koch entered into an agreement for Koch to distribute DVDs, on Demand's behalf, to retail outlets in the United Kingdom and Channel Islands. That agreement comprised a "Commercial Terms Summary" setting out terms negotiated between the parties, and it expressly incorporated Koch's "General Distribution Terms and Conditions".

13. I note the following terms of the first agreement:

i) Demand granted to Koch exclusive distribution rights in the UK and Channel Islands for a list of accounts (i.e. customers) and further accounts that may from time to time be agreed between the parties. Demand was to continue to service and sell to its existing customer base and to customers not listed in the agreement. New customers were to be discussed and agreed between the parties.

ii) The products to which the agreement applied were described as "DVD and DVD Plus Gift Sets".

iii) A Price Protection clause provided "In certain instances it may be necessary to drop the SRP of the Products. Either temporarily, for such things as post-Christmas sales promotions (this is known as "sales out allowance" or permanently due to slow demand. In such cases the proportional % price change from old to new SRP shall result in the same drop in buy price. However, since such promotions take place from existing purchased stock [Koch] may debit the differential multiplied in the case of sales out allowances by the amount of products sold during the period. E.g. SRP drops from 29.99 to 19.99 for one week and the customer sells 100 units within that week at the lower price. Then we shall debit 100x([Koch] normal buy price less [Koch] normal buy price lowered by 33.3%)."

iv) The "Distribution buy Price" clause provided "Koch's margin comprises two elements, one for sales service and the other for logistics service." Where Koch sells the product it earns a margin 7% or 10% depending on the product. Where Demand sells the product, Koch earns only a logistics fee. The logistics fee is a price per unit shipped, as set out in detail in the clause.

v) Koch also earned a "Stock Holding Fee" charged per unit on stock held in Koch's warehouse.

vi) A Supplier Returns clause provided: "Should you require stock to be returned to you, then these are chargeable at a rate of £0.20 (twenty pence) per unit. Any stock transferred on Termination then these are chargeable at a rate of £0.05 (five pence) per unit plus the cost of freight."

The Express Terms of the Distribution Agreement

14. The first agreement was replaced by a subsequent agreement between the parties, made on 1 April 2015. This agreement ("the Distribution Agreement") is the relevant agreement for the purpose of these proceedings. The Distribution Agreement comprised a document entitled "Commercial Terms Summary" ("the Commercial Terms"), and it expressly incorporated by reference the General Distribution Terms and Conditions.

15. The main changes to the Commercial Terms between the first agreement and the Distribution Agreement were as follows:

i) The Territory was extended to include "Southern Ireland".

ii) The definition of Product was changed, to become "Suppliers entire existing physical product catalogue together with all new releases made available during the Term".

iii) Koch's distribution rights were made exclusive to all retail outlets, rather than those listed or agreed.

iv) Provisions were included for replication of stock by Koch, and for transfer of stock at commencement to Koch; this included a passage upon which Demand relies "Stock to the value of the outstanding amount due will be reserved to Koch until such time as the resultant invoice has been paid by [Demand]".

v) The Price Protection clause was rewritten.

vi) In place of the two-component margin provision referred to above, the Commercial Terms provided for Koch to be paid a sales commission as follows "Koch shall earn 20% of the invoice value on all sales. Likewise Koch shall lose 20% on all credit notes raised where the Product was sold by Koch for such things as Trade co-op, Price Protection and Returns."

vii) Payment terms provided that payment was to be within 45 days from the date of a self-billing invoice. Any debit value transaction (Demand owes Koch) shall be debited from the next available payment.

viii) The term of the agreement was until 31 March 2018, and thereafter a subsequent period of one year.

16. The parties agree that the General Distribution Terms and Conditions applying to the Distribution Agreement were the same as those which applied to the first agreement ("the General Terms"). They provide (insofar as material):

i) By clause 1.1 Koch is nominated as distribution partner for the duration of the Agreement in the Territory and Demand assigns the Distribution Rights covered by the Agreement. Distribution Rights, Territory and duration are all defined by the Commercial Terms.

ii) Clause 1.2 provides that if Demand grants Koch full or limited exclusivity it guarantees at the same time "within the framework of the exclusivity granted" not to offer any third party the aforementioned Products for sale, distribution or on any other commercial basis that would infringe on the Distribution Rights conferred on Koch and/or could lessen the sales potential of the Products.

iii) Also at clause 2.6 Demand agreed not to supply itself or through any affiliated companies any customer that Koch has supplied Demand's products to.

iv) There is no express term limiting Koch's right to supply similar or competing products to those it distributes for Demand. I will turn to the question of an implied term below.

v) By clause 2.1 (under the heading "Suppliers Obligations") Demand agrees to "inform Koch fully and without delay regarding new releases, new versions, price changes, sell offs, deletions and provide all product data that is necessary to keep Koch's product database up to date."

vi) By clause 4.1 "Koch takes the Product(s) on a consignment basis. If Koch has advanced any form of monies against the Products for manufacture or similar, then the Product(s) title passes to Koch upon payment of said amount. Otherwise the Product(s) remain the property of [Demand] until Koch has sold the Product(s) and invoiced its customers."

vii) Clause 4.5 provides for discrepancies in warehouse stock. I will address this clause under the heading of the Missing Stock below.

viii) Clauses 4.7 and 4.8 ("Mint Returns") provide that Koch is responsible for warehouse management. Should there be an excess of stock, Koch can send it back to Demand at Demand's cost, or Demand may have the stock destroyed.

ix) 4.10 (under the heading "Deleted Products") provides "If [Demand] deletes certain products or demands that Koch return them from the Market, Koch shall take steps to do so immediately. In normal circumstances, a complete recall shall take six months. Products that are being allowed to run out according to [Demand's] notification will not be rendered resaleable when prepared for return, but will be booked to [Demand's] warehouse stock irrespective of their condition." 4.11 provides "Stock held in the Koch warehouse of Products deleted by [Demand] shall be actioned for return immediately, the resulting freight cost shall be payable by [Demand]."

x) Clause 4.12, headed "Price Protection" provides "if reducing the official retail price either temporarily or permanently can increase the overall revenues of a Product, then either party with advance notice to the other may reduce the retail price."

xi) Clause 6 deals with expiry and termination. Clause 6.1 provides for either party to terminate by giving 60 days or more notice before the expiry of the Agreement.

xii) Clause 6.4 provides "In the event of Termination of the Agreement, the Parties shall reckon up their accounts with one another. After final settlement of the accounts Koch will make [Demand's] remaining Product(s) available for collection. [Demand] shall take back the Product(s) at its own expense."

xiii) Clause 8 deals with confidentiality. I will deal with that clause when dealing with the Copycat Products claim.

17. On 26 May 2016 the Distribution Agreement was extended to include Demand's gifting products. This was done by an addendum to the 1 April 2015 agreement which was headed "Non-DVD physical boxed product manufacturing and far east sourcing" ("the Non-DVD Addendum"). That agreement covered the provision of services by Koch in sourcing and manufacturing gifting products on behalf of Demand. I will return to the Non-DVD Addendum below, but at this stage I note that it is not referred to by either party in the pleadings, and barely featured in the course of evidence or argument.

18. A number of issues arise as to the proper construction of the Distribution Agreement, and Demand alleges five implied terms, all of which are in dispute.

Legal Principles as to Construction of the Distribution Agreement and Implied Terms

19. There is no disagreement between the parties as to the relevant legal principles, which are well established.

20. As to the construction of the Distribution Agreement, both parties rely on ***Arnold v Britton*** [2015] AC 1619 per Lord Neuberger at paragraph 15

> "15 When interpreting a written contract, the court is concerned to identify the intention of the parties by reference to "what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean", to quote Lord Hoffmann in *Chartbrook Ltd v Persimmon Homes Ltd* [2009] AC 1101, para 14. And it does so by focusing on the meaning of the relevant words, in this case clause 3(2) of each of the 25 leases, in their documentary, factual and commercial context. That meaning has to be assessed in the light of (i) the natural and ordinary meaning of the clause, (ii) any other relevant provisions of the lease, (iii) the overall purpose of the clause and the lease, (iv) the facts and circumstances known or assumed by the parties at the time that the document was executed, and (v) commercial common sense, but (vi) disregarding subjective evidence of any party's intentions."

21. Koch also draw my attention to paragraph 19 of the same judgment:

> "commercial common sense is not to be invoked retrospectively. The mere fact that a contractual arrangement, if interpreted according to its natural language, has worked out badly, or even disastrously, for one of the parties is not a reason for departing from the natural language. Commercial common sense is only relevant to the extent of how matters would or could have been perceived by the parties, or by reasonable people in the position of the parties, as at the date that the contract was made. "

22. Paragraph 19 forms the third of seven factors emphasised by Lord Neuberger at paragraphs 16-23. I have regard to all of those factors in analysing the Distribution Agreement.

23. As to the implication of terms, both parties rely on ***Marks and Spencer plc v BNP Paribas Security Services*** [2015] UKSC 72**.** At paragraph 23 Lord Neuberger said:

> "23 First, the notion that a term will be implied if a reasonable reader of the contract, knowing all its provisions and the surrounding circumstances, would understand it to be implied is quite acceptable, provided that (i) the reasonable reader is treated as reading the contract at the time it was made and (ii) he would consider the term to be so obvious as to go without saying or to be necessary for business efficacy. (The difference between what the reasonable reader would understand and what the parties, acting reasonably, would agree, appears to me to be a notional distinction without a practical difference.) The first proviso emphasises that the question whether a term is implied is to be judged at the date the contract is made. The second proviso is important because otherwise Lord Hoffmann's formulation may be interpreted as suggesting that reasonableness is a sufficient ground for implying a term. (For the same reason, it would be wrong to treat Lord Steyn's statement in *Equitable Life Assurance Society v Hyman [*2002] 1 AC 408, 459 that a term will be implied if it is "essential to give effect to the reasonable expectations of the parties" as diluting the test of necessity. That is clear from what Lord Steyn said earlier on the same page, namely that "The legal test for the implication of … a term is … strict necessity", which he described as a "stringent test".)"

24. Further, per ***Chitty on Contract*** (33rd edition):

    i) No term can be implied into a contract if it contradicts an express term (14-018);

    ii) The term sought to be implied must be capable of being formulated with sufficient clarity and precision (14-017).

25. Demand relies on the judgment of Leggat J (as he then was) in ***Yam Seng Pte Ltd. v International Trade Corporation Ltd.*** [2013] EWHC 111 at 119 and 142 in support of the proposition that in a relational contract such as a distribution agreement it may be necessary to imply a term to ensure business efficacy or to give effect to the obvious intentions of a reasonable person in the position of the parties.

    i) I accept the general proposition that a relational contract is more likely to give rise to events for which the parties have not expressly provided and may therefore more commonly give rise to questions of construction and implication of terms. As Leggatt J put it (paragraph 139):

> "To apply a contract to circumstances not specifically provided for, the language must accordingly be given a reasonable construction which promotes the values expressed or implicit in the contract. That principle is well established in the modern English case law on the interpretation of contracts. It also underlies and explains, for example, the body of cases in which terms requiring cooperation in the performance of the contract have been implied".

    ii) Legatt J's judgment predates both ***Arnold*** and ***Marks and Spencer***. There is nothing in the cases to indicate that the approach in those Supreme Court judgments should be in any way modified in relational contract cases. Ms Bayliss, for Demand, quite rightly confirmed in her oral closing that she did not submit that there was a different test for implication of terms in relational contracts.

    iii) The specific issues addressed by Leggatt J were the circumstances in which terms as to good faith, cooperation and mutual trust and confidence fall to be implied. The decision in ***Yam Seng*** is by no means the last word on that issue. However, no such implied terms are alleged in this case, so I need not consider the point further.

The Alleged Implied Terms

26. Demand alleges the following implied terms (RAPoC paragraph 5):

i) (a) Save as permitted by way of express terms of the Distribution Agreement, stock sold to third parties by Koch on behalf of Demand would be sold at a price determined by Demand (the "Set Price").

ii) (b) During the term of the Distribution Agreement, Koch would not produce and offer for sale to customers of Demand products that were copies of and/or were substantially similar to those that Koch had agreed to sell on behalf of Demand.

iii) (c) In the alternative to the same being permitted by reason of the Supplier Return provision of the Commercial Terms, that Demand would be entitled, within a reasonable period following such a request being made (being no more than 7 days) to regain possession of stock to which it held title.

iv) (d) Upon receipt of the notice set out in sub-paragraph (c) above, Koch would not take any further steps to dispose of or otherwise deal with that stock save as required to bring about its return to Demand.

v) (e) Save as already provided for in the Distribution Agreement, the terms on which Koch would manage the replication needs of Demand would be agreed between the parties on an order by order basis and such terms would be incorporated into the Distribution Agreement.

27. Demand alleges that each of these terms is to be implied as obvious and/or to give business efficacy to the agreement. Koch denies all of the implied terms.

28. There does not appear to be an allegation of breach of implied term (e); accordingly I say no more about it. Implied term (b) is relevant only to the Copycat Products claim and I will deal with it below in the section dealing with that claim. I deal in the immediately following sections with implied term (a) (price) and implied terms (c) and (d) (right to return of stock). These implied terms are central to The Book People claim.

Terms as to Returns

29. A central issue in The Book People claim is whether Demand was entitled to call for the return of products during the lifetime of the agreement.

30. A related question arises as to ownership of stock. Demand's alleged implied term (c) relates to return of stock to which it held title.

31. Demand alleges that the proper construction of the Supplier Returns clause is that it gives a right to return of stock, or at least that it assumes such a right. In the alternative, it alleges that, as a matter of obvious implication, implied terms (c) and (d) arise. Mr Fenwick says in his second statement (paragraph 14):

"it was obvious to both parties at the time of entering into the Distribution Agreement (and necessary for the proper functioning of the agreement) that

Demand could request for its stock to be returned at any time, given that, quite simply, it was Demand's stock which at the time of the request Demand had paid for in full for the manufacturing of."

32. Koch argues that the Supplier Returns clause does not give a right to return of stock, but simply provides for the cost of returns in the circumstances where such rights are provided elsewhere in the agreement. It points to a number of circumstances in which Demand may be entitled to returns: 4.6, 4.7 and 4.11.

33. The Distribution Agreement makes limited express reference to return of stock to Demand. There is no express provision giving a general right to require stock to be returned. Such a right is a significant one: Koch argues, and I accept, that such a right would interfere with its right to earn commission by selling the Products. That would be an interference with a distributor's earning ability in any distribution agreement, but is of particular impact in this case, where the cost of manufacturing the products is being met, in the first instance, by Koch. I am cautious to draw such a wide-ranging conclusion from the words "Should you require stock to be returned to you" at the beginning of the Supplier Returns clause. In my judgment, that language does not create a right to require return, nor does it necessarily assume a general right to return. It is, as Koch argues, consistent with a provision that applies in those circumstances where there is a right of return provided elsewhere in the agreement.

34. Clause 4.10 of the General Terms provides the most wide-ranging express right to require return, but that applies to a situation where a product is deleted or withdrawn from the market. It does not give rise to a general right to return.

35. It is clear that clause 6.4 of the General Terms permits Koch to retain stock on termination until the final account is settled. That is inconsistent with a general right to require return of stock. Demand argue that the right under clause 6.4 only arises on termination, and that prior to termination it has a right to require return.

36. It is true that clause 6.4 applies on termination, but the question is what does that clause tell us about the parties' rights prior to termination. In my judgment, there would be no commercial justification for an arrangement where Demand's right to require return of stock was more extensive during the period that Koch had an exclusive right to sell the stock than it would be after termination. Demand's construction, and its alleged implied term, would allow Demand to defeat the purpose of clause 6.4 by serving sixty days' notice and then calling for return of stock shortly prior to termination taking effect. That cannot have been the parties' commercial intention: in effect it would give Demand the right to terminate Koch's right to sell the stock on less than 60 days' notice, and before expiry of the term, simply by requiring return of all its stock. Implied term (d) highlights this: the effect of that term is that once Demand gives notice, which can be at any time as long as it is at least 60 days before expiry of the fixed term, Koch would no longer be able to deal with stock save as to return it to Demand. Demand would therefore be able to require Koch to stop distributing its stock with immediate effect, and with no

warning. This cannot have been the commercial intention of the parties, as it would defeat the purpose of a notice period.

37. Mr Fenwick's evidence was that if Koch can keep stock until the final account has been completed Demand would not survive as it would not have stock to sell to maintain its cash flow (paragraphs 14-16, first statement). However, that is the effect of clause 6.4. The alleged implied terms are at odds with that clause. While I recognise the financial position that Demand found itself in, the task of the court is to ascertain the meaning of the agreement, not to protect Demand from what, in hindsight, may appear to have been a bad bargain.

38. In my judgment, a clause permitting Demand to require return of any stock it wishes during the lifetime of the Distribution Agreement is neither obvious nor necessary to give business efficacy to the agreement. Accordingly, I reject Demand's argument on construction, and reject the alleged implied terms (c) and (d).

39. In its submissions, Demand focussed on the question of ownership of stock. Paragraph 29 of the closing submissions say, in respect of The Book People Stock, that by the time Demand called for return of stock on 19 February 2018 it had paid for and owned the stock, and accordingly had a right to call for it. I will consider briefly below the position in relation to ownership of stock. However, in my judgment Demand's argument rests on a flawed assumption. Its submission that if it owned the stock "accordingly" it had the right to call for it assumes that it has an unfettered right to return of its property. As I have set out above, that is not right. Even if all the stock was owned by Demand, the effect of the Distribution Agreement is that Demand granted Koch rights to sell its property during the lifetime of the agreement, and the unfettered right to return that Demand alleges is an interference with Koch's rights.

Terms as to ownership of stock

40. As I have explained above, Koch were responsible for sourcing and manufacturing products, and they financed manufacture, recouping the manufacturing costs from sales proceeds.

41. Clause 4.1 of the General Terms provides that if Koch has advanced any form of monies against the Products for manufacture or similar then the Products' title passes to Koch upon payment of the said amount. Otherwise the Product(s) remain the property of the Supplier until Koch has sold the Product(s) and invoiced its customers.

42. In practice, almost all, if not all, stock was covered by clause 4.1, as Koch paid the manufacturing costs and is therefore to be taken as having "advanced monies" for manufacture. The starting point therefore is that at point of manufacture products belong to Koch.

43. Demand's case is that once manufacturing costs have been paid, Demand has title in the stock. Koch submits that there is no express provision for Demand

to own the stock on repayment. As a matter of construction, it is less than clear from the Distribution Agreement if and in what circumstances title transfers to Demand once manufacturing costs are paid. However, Mr McNicol accepted that if all outstanding liabilities to Koch had been paid Demand would own the stock that Koch had manufactured. I am prepared to accept that the Distribution Agreement is to be construed as making Koch the owner of stock if it advances monies but only while such monies are outstanding. In the light of my findings above as to the right of return of stock, Demand's right to return does not turn on ownership of the stock.

Terms as to Price setting

44. It is a curious feature of the Distribution Agreement that almost nothing is said about the right to set prices for the products to which the agreement applies. Recognising this, Demand argues for an implied term that it was entitled to set the prices: implied term (a). Koch, on the contrary, argues that it was entitled to set the price.

45. The express terms relating to price are as follows:

i) The Commercial Terms "Price Protection" clause provides that if the parties jointly agree to reduce "the selling price of Products already sold to customers" the parties shall share the impact of the reduction. This clause replaced a Price Protection clause in the first agreement under which the parties also shared the effect of a drop in price. That clause had referred specifically to dropping the "SRP" which I understand to be synonymous with RRP.

ii) General Terms clause 2.1 places Demand under an obligation to inform Koch of "price changes". That does not amount to the reservation of a right on Demand's part to set the price; it is an obligation imposed on Demand to provide up to date information about a range of matters relating to products, price being only one of them. The most that can be argued is that the obligation to provide information as to price changes assumes that Demand has the right to change prices.

iii) As I set out above, General Terms clause 4.12 ("Price Protection") provides that, in defined circumstances, either party can reduce "the official retail price" on advance notice to the other party.

iv) Demand's written opening and closing submissions point to the Non-DVD Addendum, which provides that Demand's agreement is required to "unit pricing and terms and item level specification confirmation." Little was made of this provision during the course of the trial. Had it amounted to an express right on Demand's part to agree to sales prices I would have expected it to be pleaded, and to be a key feature of Demand's case. In its context, this language relates to matters to be agreed before purchase orders are raised by Koch for the manufacture of products. I heard no argument as to the proper interpretation of the clause, but it is likely that "unit price" refers to the manufacturing or

production cost of the products: hence its appearance alongside "item level specification".

46. These terms give only limited clues, if any, as to which party had the general right to set prices at which products were sold to customers.

47. As part of the factual matrix against which the agreement is to be construed, each party led evidence as to the nature of pricing in this business, and as to the way in which the agreement was operated in practice, and their understanding of the right to set prices.

48. As to the nature of pricing, the parties agreed that there were different prices to be considered.

i) Mr Fenwick drew a distinction between the RRP (recommended retail price) and the trade price. His evidence (third statement paragraph 17) is that the trade price is derived from the RRP by a simple formula: RRP, less VAT, x 50%. In his second statement (paragraph 36) he said that in all the dealings Demand had with Koch they did not once set a price without reference to him, save where they made minor reductions in the price in exchange for a large order. However, he accepted that trade discounts were offered to customers, making the price at which products were sold to customers less than the trade price. His evidence was that he would not have objected to Koch unilaterally offering a trade discount of no more than 20% against large orders. Any discount more than this required Demand's prior approval. When cross examined, he said that Koch could sell at a reasonable discount, but anything over 20% would require a conversation. I found his evidence as to Koch's scope to agree prices to be less than clear.

ii) Mr Maynard, Koch's counsel, identified in his opening submissions four different types of price:

a) The RRP, which is the recommended price to consumers;

b) The cost price, which is the cost of manufacturing the product;

c) The dealer or trade price, a price which for DVD products in particular can be worked out as a percentage of the RRP minus VAT;

d) The actual price sold to a customer, which is likely to be a matter of negotiation, and for which the trade price is a starting point.

iii) Mr Cronin's evidence was that Koch set the price at which products were sold to customers. Koch was incentivised to sell at the best possible price as it earned a commission of 20%. Although for DVDs there was a formulaic "industry standard" way of reaching a trade price, there was not such a standard for gifting products; Koch was free to negotiate pricing on volume sales. He said that Koch would set the

pricing of products throughout, and Demand was aware of this. As a matter of practice he would agree pricing with Demand before making any deal which would be loss-making for Demand if Koch applied its normal commission rate. He said (first statement paragraph 28) that Koch would set the pricing 95% of the time without any discussion with Demand. In cross-examination, he said that if the price reduction was more than 20% he would discuss with Demand eight out of ten times. I accept Mr Cronin's evidence on these matters.

49. Each side took me to documents which, on their account, supported their respective cases that Demand was involved in setting the price or that Koch was setting the prices unilaterally. I did not find these references helpful.

    i) First, the Court has to determine the meaning of the contract (and any terms to be implied) as matter of objective consideration of the contractual documents in the light of the factual matrix as at the time the contract was agreed. Evidence of the parties' subsequent operation of their relationship is of limited value to understanding the meaning of the contract at the time it was agreed.

    ii) Second, the parties conducted a trading relationship pursuant to the Distribution Agreement for three years; the selective handful of documents referred to by each side is unlikely to be a reliable indicator of the totality of the trading relationship throughout the period.

50. Demand's case is that implied term (a) falls to be implied because it is obvious, or because it is necessary to give business efficacy to the Distribution Agreement. In my judgment the alleged implied term is neither obvious nor necessary.

    i) The express terms of the agreement give no clear indication that the obvious assumption of the parties must have been that Demand would set the price. I accept Koch's argument that such express references as there are in the Commercial Terms and General Terms are references to the RRP, and that the price at which products are sold to customers is neither the RRP, nor a trade price that is a mere mathematical function of the RRP.

    ii) In terms of business efficacy, the agreement can function either if Demand set the price, or if Koch set the price. It is not necessary for the proper functioning of the contract for Demand to set the price.

    iii) I accept that there is a potential disadvantage to Demand if Koch is at liberty to set the price, as it is at risk of Koch selling at a low price in order to earn commission, leaving Demand to make a loss.

    iv) On the other hand, Koch is paid a percentage commission on the sale price; it is incentivised to maximise the sales price, or at least to maximise sales revenue (i.e. price multiplied by volume).

v) Further, an important part of Koch's role under the Distribution Agreement is to sell Products. Part of the armoury of a sales person is their ability to negotiate on price. If Koch can only sell at Demand's "Set Price" then its sales staff are deprived of a significant element of their ability to make sales. It would mean that either a customer accepts the price pre-set by Demand, or in any case where there is negotiation on price Koch would need Demand's input and agreement. That, in my judgment, is impractical, if not unworkable.

vi) Implied term (a) for which Demand argues is that Koch can only sell at the Set Price determined by Demand. It is perhaps a recognition of the unworkable rigidity of this clause that at trial Demand put its case on the basis that Koch could in practice make volume sales at a discount of up to 20%, but anything over that would need to be agreed. However, that is not the implied term alleged. A power on Koch's part to unilaterally set discounted prices, even in limited circumstances, is inconsistent with implied term (a). If in practice Koch was permitted to set discounts at up to 20% that suggests that implied term (a), that Koch could only sell at Demand's Set Price is not a necessary term to be implied for the business efficacy of the contract.

vii) Although the implied term is that Koch could only sell at Demand's "Set Price", by the end of the trial there is no clear evidence that Demand established such "Set Prices" for any particular products, and it is perhaps telling that the claim in relation to The Book People Stock is not based on the difference between actual sale price and "Set Price", but rather the difference between actual sale price and the average price that had been achieved by Koch. That indicates an absence of "Set Prices".

51. Accordingly, in my judgment I reject Demand's case that the Distribution Agreement falls to be construed so that Koch could only sell Products at prices set by Demand, and I reject the case that implied term (a) forms part of the Distribution Agreement.

WH Smith Terms

52. Both parties rely on special arrangements made in 2016 in relation to stock sold to WH Smith. They disagree as to what those arrangements were. The dispute on this issue is relevant as when Demand served notice to terminate the Distribution Agreement Koch says a substantial sum was owed by Demand in relation to the manufacturing cost of stock sold to WH Smith. Demand denies that the sum was owing and alleges that stock which had been sold to WH Smith on consignment forms part of the "Missing Stock" that should have been returned to Demand.

53. Demand say that the final account shows £64,580.71 for the cost of manufacture of goods provided for sale by WH Smith ("the WH Smith Debited Sum"). RAPoC paragraph 23B pleads that the goods were neither sold by WH Smith nor returned, therefore should not have been debited.

54. There is no dispute that these goods were neither sold nor returned. They represent stock held in store by WH Smith that WH Smith destroyed after an agreed minimum sale period of 36 weeks. The terms upon which WH Smith bought the stock from Koch allowed WH Smith to do so. The issue is whether Koch or Demand must bear the cost of manufacture of the destroyed stock.

55. The normal position under the Distribution Agreement is that Demand is obliged to pay the manufacturing costs incurred by Koch. Those costs can be treated as a debit transaction by Koch and debited from the next available payment due to Demand.

56. Demand's case is that there was a variation in these terms in relation to stock sold to WH Smith. RAPoC paragraph 23B.1 pleads that on 15 April 2016 Mr Fenwick and Mr Penhaligon (of Koch) reached terms, referred to as "the WH Smith Terms" which were "agreed orally by a teleconference of that day and/or in writing by exchange of emails also dated 15 April 2016". The WH Smith Terms alleged are that:

    i) Koch would manufacture stock to be supplied to WH Smith on consignment;

    ii) Demand would only be liable for the cost of manufacture of stock actually sold by WH Smith;

    iii) In relation to unsold stock, Demand would only become liable for the cost of such stock as was not sold if and upon that stock being returned to Koch in a saleable condition.

57. Koch's case (Re-Amended Defence paragraph 26B) is that it was agreed that unsold stock in WH Smith stores would be destroyed and stock in its distribution centre would be returned. It was agreed that Demand would pay the manufacturing cost when stock was sold, or when it was destroyed or returned upon the expiry of the sale period.

58. The relevant documents show the following:

    i) On 13 February 2016 [1/286] Mr Cronin emailed Ms Natalie Simpson of WH Smith, cc Mr Fenwick, with proposals for the sale of a range of products, following up on a conversation that had taken place at a Spring Fair earlier that week.

    ii) On 8 March [1/285] Ms Simpson replied, expressing interest but asking some questions, not least on price.

    iii) On 8 March 2016 [1/284] Mr Fenwick emailed Mr Cronin and Mr Penhaligon. He said before the parties embarked on these projects with WH Smith he would like to agree financials with Koch on the account. He said as discussed in the past consignment did not work as Demand could not afford to "cash flow" this, meaning carry the manufacturing cost. He said he needed to set up a deal where Demand was only charged for the manufacturing cost at the time of sale.

iv) Mr Cronin made a proposal to Mr Fenwick on 24 March 2016 [1/283]. The proposal was that Koch would require a 25% fee to finance the stock, but that it would only deduct COGs (i.e. manufacturing costs) for actual units sold; when the product has run its lifecycle in store and is removed Koch would claim back the total COGs amount outstanding.

v) On 12 April [3/1522] Ms Simpson emailed Mr Cronin, cc Mr Fenwick, regarding an order. The terms she proposed were that at the end of the agreed minimum on sale period (then put at 20 weeks) stock at WH Smith's distribution centre would be available for collection but "Stock remaining in store will be destroyed".

vi) On 13 April [3/1522] Mr Fenwick forwarded Ms Simpson's email to Mr Cronin with comments. Mr Fenwick said "we need a destruction certificate from them for all stock destroyed".

vii) On 14 April [3/1581] Mr Cronin replied to Ms Simpson, cc Mr Fenwick. He repeated the point made to him by Mr Fenwick. He said: "Stock remaining in store will be destroyed (we need a destruction certificate from you for all stock destroyed, we need this for royalty reporting)".

viii) On the same day [3/1581] Ms Simpson queried what was meant by a destruction certificate. Mr Fenwick replied directly to her (also on the same day) [3/1581] explaining the destruction certificate is for him "we just need something to say you have destroyed x amount of stock".

ix) Also on 14 April, Mr Penhaligon [1/283] forwarded Mr Cronin's 24 March email to Mr Fenwick. On 13 April Mr Penhaligon had emailed Mr Fenwick asking for a response regarding the WH Smith consignment now that there was an order. It appears that Mr Fenwick could not find the 24 March email, so Mr Penhaligon resent it.

x) Mr Fenwick replied the same day to Mr Penhaligon (cc Mr Cronin) [1/283] and made a counterproposal; he proposed a different percentage (22.5%); he said "we need to agree that you will only invoice for this stock once all the stock is back at Koch/K&N in a saleable condition".

xi) On 15 April [1/280] Mr Fenwick emailed Mr Penhaligon, stating that his email was further to a telcon earlier and Mr Penhaligon's 13 April email. Under the heading WH Smith Consignment he said this: "as previously emailed we needed to agree 22.5% as we have royalties to pay on these products, but from an email forwarded by John this has been knocked back and you require 25% to do this. John called this morning asking about this, but as I said to him we cannot move forward now until we know the COGs. Once we have this and assuming we can achieve the margin required we can move forward, but if we can't we will walk away from these orders. But happy to agree COGs on sales so this is fine, but can you also confirm in writing

re-stock left after the sale period, we need to agree that you will only invoice for this stock once all the stock is back at Koch/K&N in a saleable condition so we can sell it straight away and recoup the monies paid to Koch for the remaining stock".

xii) There was no confirmation in writing as sought.

xiii) On 18 May [1/290] Mr Fenwick emailed Mr Cronin, Mr Jones and Mr Penhaligon setting out the terms of purchase: "As just discussed with John I just want to get all the WH Smiths potential business onto one email so we are all clear on when we need to deliver component parts, customer's expectations and our terms of trade". He sets out Terms of Purchase which were in summary:

a) 25% S&D fee to Koch;

b) Koch would only deduct COGs on actual units sold;

c) "When the product has run its life cycle in store and is removed at this point we would claim back the total COGs outstanding only, once all stock has been returned to Koch/K&N and is in a saleable condition".

xiv) Mr Fenwick concluded that email by saying "Can you please confirm by return email all points". There does not appear to have been a reply from Koch.

xv) There followed some emails between Ms Simpson and Mr Cronin (with Fenwick cc) about costs and the pricing model. On 6 June [3/1526] Ms Simpson emailed summarising the proposed terms. In her email she again included the wording "Stock remaining in store will be destroyed". Mr Cronin replied to that email on 14 June [3/1525], again cc Mr Fenwick, commenting on various elements of Ms Simpson's proposal. Following the passage which concluded "Stock remaining in store will be destroyed" Mr Cronin wrote "YES".

59. Demand pleads an agreement that Demand would only pay manufacturing costs on stock returned in saleable condition; the pleaded case is that the agreement was made either orally on the telephone, or in emails on 15 April 2016. However:

i) Mr Fenwick gave no evidence as to any oral agreement, and no such oral agreement was put to Koch's witnesses. Indeed, the focus of cross-examination of Koch's witnesses was that there was no oral agreement of the kind that Koch argued occurred.

ii) There was no concluded agreement in an exchange of emails on 15 April. Mr Fenwick set out his proposed terms on 15 April and asked for written confirmation from Koch, but there was no response from Koch.

60. Mr Cronin (paragraphs 64-69) says that there was an agreement by Demand that WH Smith would destroy unsold stock in store. He relies on the 13 April email above. Mr McNicol pointed to the 14 April emails [3/1581].

    i) It was put to Mr McNicol that [3/1581] does not show a concluded agreement. He was cross examined on the basis that there was no oral agreement as to the destruction proposal.

    ii) Mr Cronin, when he was cross-examined, could not remember a specific call with Mr Fenwick after Mr Fenwick's 15 April email, but said there was such a call and he took Mr Fenwick at his word.

61. Mr Fenwick (second statement paragraph 37) said it was untrue that Demand agreed with WH Smith that WH Smith could destroy some out of date stock. He said he didn't know when the agreement is alleged to have been made. If Koch did it, he said, it did it without reference to Demand.

62. In the email exchanges, set out above, between Ms Simpson, Mr Cronin and Mr Fenwick, destruction of stock in store was repeatedly referred to by WH Smith and Mr Cronin agreed to that. Mr Fenwick was cross examined about [3/1581], a document which he did not refer to in any of his three statements. It was put to him that he knew that stock in store was going to be destroyed. His answer was that he said that stock would need a certificate if it was destroyed, the email didn't say that he agreed to it. He said that the certificate related to a separate point regarding royalty reporting and was nothing to do with an obligation to pay Koch's manufacturing charges. His evidence was that if Koch wanted to permit WH Smith to destroy stock that was Koch's business, but it did not follow from this that Demand must now pay Koch's manufacturing charges for the destroyed stock. He said he would not have agreed to it if there was a risk Demand would have to pay manufacturing costs on units it didn't sell or get back. In my judgment his answers were unpersuasive, and not a fair reading of the email exchange. It is implicit in the request for a certificate that Mr Fenwick accepted the position that the stock would be destroyed.

63. While it is true to say that was an arrangement between Koch and WH Smith, it is clear that Mr Fenwick knew these were the terms upon which WH Smith prepared to buy and agreed on that basis. He was included in the email from Mr Cronin to Ms Simpson on 14 June in which Mr Cronin agreed to Ms Simpson's proposal to destroy stock remaining in store.

64. Koch also relied on emails between the parties and WH Smith in the Autumn of 2017 when WH Smith indicated that it intended to write off unsold items in store. There was an exchange of emails between Mr Cronin, Mr Fenwick and WH Smith in which Mr Fenwick sought to persuade WH Smith not to write off the stock, but to keep it on sale at a lower price. In summary:

    i) An email dated 25 September 2017 [3/1545] shows that Mr Fenwick was aware that WH Smith were going to write off unsold DVDs. Mr

Fenwick wrote an email to Mr Cronin which was fairly characterised by Koch's counsel in cross-examination as an attempt to convince him not to write off the stock because Demand wanted to be able to sell to recoup manufacturing costs. Mr Fenwick's suggested draft email proposed that Mr Cronin tell WH Smith "I have spoken to Jason and this would be detrimental to his business writing this stock off".

ii) Mr Fenwick's view in an email dated 28 September 2017 was that Demand was looking at a £40,000 loss on the unsold WH Smith stock [3/1562].

iii) On 2 October 2017 Mr Fenwick emailed Mr Edwards at WH Smith saying "If we are going to have a lot of stock left then I would rather set up a heavily discounted price now so that I at least get my money back on this stock, can you please liaise with John on this and get back to me with your comments". Further on in the same email he says, regarding the 2016 stock in store, "We cannot and will not allow a write off of this size, it is too damaging to our business." He again refers to a potential £40,000 loss.

65. Mr Fenwick was cross examined on these exchanges: it was put to him that Demand was only concerned not to write off stock because it had to pay the manufacturing cost of stock that was to be destroyed. It was put that if the stock had to be returned in a saleable condition for Demand to have to pay the manufacturing cost, then destruction would be of no concern to him. Mr Fenwick had no satisfactory explanation for this, beyond repeating that he wanted the stock back to sell on. He could not, when asked, give a reason to have sent a number of emails to persuade WH Smith not to write stock off because he would incur a cost of £40,000.

66. Those emails indicate that Mr Fenwick understood that a write off/destruction of stock in store by WH Smith would be to Demand's financial disadvantage, as it would still have to meet the manufacturing cost of that stock.

67. In my judgment, on the basis of the exchanges of emails (and to a lesser extent the oral evidence of the witnesses) the terms as to WH Smith stock were as Koch alleges, and not as Demand alleges. That is to say manufacturing costs would be payable on sold stock when sold, and then after the minimum period manufacturing costs would be payable on unsold stock, whether that stock was returned from the WH Smith distribution centre, or destroyed in store:

i) Demand's case relies on there being specific WH Smith Terms which were a departure from the terms of the Distribution Agreement. If it cannot establish such a term, then under the terms of the Distribution Agreement it has no entitlement to postpone payment of manufacturing costs until sale.

ii) There is no clear evidence of an oral agreement either as alleged by Demand or as alleged by Koch. Demand offered no evidence at all as to its own alleged oral agreement.

iii) The email record does not show a concluded agreement on Demand's proposed terms on 15 April (which is Demand's pleaded case). Mr Fenwick's email of that day, and his email of 18 May both ask for confirmation from Koch that was not forthcoming.

iv) As at 15 April Mr Fenwick was aware, and in my judgment had consented to, the terms offered by WH Smith that unsold stock in store would be destroyed. This term was subsequently reiterated by WH Smith on 6 June before placing its first order. Mr Cronin, with Mr Fenwick's knowledge, agreed to the term.

v) Mr Fenwick's evidence seeking to explain his request for a destruction certificate was unpersuasive. It is clear that at the time of his 15 April and 18 April emails he was aware of WH Smith's offered terms. His emails to Koch fail to address that which he knew would be the case: that WH Smith would destroy stock held in store. Despite that knowledge he did not seek agreement to a term that Koch, not Demand, would have to pay the manufacturing cost of such stock. Absent such an agreement, I can find no reason why Koch would have to bear the risk of carrying the manufacturing cost of stock which was not sold by W H Smith.

TERMINATION OF THE AGREEMENT AND THE BOOK PEOPLE SALE

68. Mr Fenwick's evidence was that by the end of 2017 he had decided that he did not wish to renew the Distribution Agreement when it came to an end on 31 March 2018. On 19 January 2018 he served notice that the Distribution Agreement would terminate on 31 March 2018. The parties agree that notice was properly given pursuant to clause 6.1 of the Distribution Agreement and that the agreement did in fact terminate on 31 March 2018.

69. On 22 January 2018 Mr McNicol wrote to Mr Fenwick [1/124] acknowledging receipt of the notice to terminate, and drawing attention to clauses 4.1, 6.4 and 6.5 of the General Terms.

70. On or by 23 January 2018 Mr Fenwick proposed terms for a new agreement between the parties. In an email dated 26 January 2018 Mr McNicol responded to Mr Fenwick outlining the termination process and reacting to Mr Fenwick's proposal. He stated that the contract requires the parties to settle accounts and for Koch to make Demand's stock available for collection thereafter. He included a schedule which showed £92,600.45 as due to Koch. This figure comprised £44,142.99 due to Demand, less £136,743.44 said to be owed in respect of WH Smith deductions. He went on to explain that return of stock would be charged at £0.05 per unit, and that there was a "WH Smith" retro of £21,000. 68,000 units of stock were held in Koch's warehouse. Therefore, he stated, a total of £117,680 was owed by Demand, against which would be offset sales of January, February and March, which he estimated between £60,000 and £81,600.

71. He went on in the same email to make a counter-proposal for the future trading relationship.

72. Mr Fenwick replied on 26 January 2018 saying "Your counter proposal is wholly unrealistic so we will proceed with the termination. You need to make our stock ready for collection w/c 2 April 2018." In his email he went on to query the "WHS COGS" figures (sums relating to the cost of manufacturing stock supplied to WH Smith). He also agreed that Demand would need to pay 5p per unit for returns and the WHS Smith retro less a 25% deduction. He said "Sales in January, February and March must be accounted for in the usual way under our agreement, though can be partially offset by the pick pay and ship costs and the net WHS retro if you want".

73. On 16 February 2018, Mr McNicol reiterated his position regarding WH Smith manufacturing costs, and his position that stock would not be returned until the account had been settled.

74. On 19 February 2018 Demand wrote to Koch to request the return of 50,000 units of stock held by Koch [1/132]. He did so purportedly pursuant to the "Supplier Returns" provision of the Commercial Terms. That amounted to around 40% of the stock held by Koch at that time.

75. Mr Fenwick's purpose in making the request (Second Witness Statement paragraph 14) was so that Demand would have stock to fulfil orders that it would receive from 2 April 2018 onwards. He was mindful of potential delays while the parties' final account was reconciled. It appears from his statement that customers were already, in March, placing orders with Demand for the period after 31 March. Mr Fenwick says that the amount of stock subject to the delivery up application would allow Demand to fulfil orders, while allowing Koch to recoup sums due to it on reconciliation of accounts.

76. Koch did not return the requested stock.

77. On 2 March 2018 Demand's solicitors, Keystone Law, wrote to Mr McNicol [1/134]:

    i) They said that clause 6.4 (return of stock after settlement of account) only applied on termination and did not permit Koch to refuse to return stock prior to its termination.

    ii) Demand disputed the sum Koch estimated to be owing on termination. The letter raises a series of allegations of breach of contract (some, but not all of which form part of these proceedings). As a result of those alleged breaches, Keystone stated that substantial sums would in fact be owed by Koch to Demand. Keystone disputed Koch's entitlement to withhold stock, accusing it of holding Demand to ransom. It proposed an arrangement for security to be held in respect of the stock, failing which it threatened an application for "interim delivery up" of stock.

78. On 4 March 2018 Demand became unable to access Koch's online stock tool, KM Hub. There is some dispute on the evidence about this. During pre-action

correspondence Koch (and in all probability Mr McNicol) had instructed its solicitors to attribute this to a technical error. On the evidence at trial it is clear to me that access had been deliberately cut off in order to prevent Demand learning of Koch's sale of stock prior to termination on 31 March 2018. That behaviour does Koch no credit.

79. On 19 March 2018 [1/223] Koch's solicitors, Shoosmiths, replied to Keystone's letter of 2 March 2018. They disputed Keystone's interpretation of the effect of clause 6.4, and stated that Koch was exercising an equitable right to set off the liquidated sums owed to Demand pursuant to recent invoices against the total sums owed to Koch pursuant to the Agreement, including sums that are in relation to the cost of manufacturing goods held on consignment by WH Smith as well as the normal trading account.

80. On 20 March 2018 Demand issued an application for interim delivery up of the 50,000 units of stock. The application papers were emailed to Shoosmiths at 16.42 on 20 March and were served at Koch's registered office at 19.34 the same day. The application was listed for hearing on 26 March 2018.

81. The stock at that time held by Koch was the entirety of Demand's trading stock, apart from a small amount of stock that Koch had not taken at the beginning of the Distribution Agreement. Mr Fenwick's evidence (second statement para 19) was that the stock held by Koch (or on consignment to retailers) cost £228,000 to manufacture and had a retail value of £495,000.

82. On 23 March the parties agreed terms of a consent order ("the Consent Order") to settle the delivery up application.

    i) The application was withdrawn, and the claim stayed generally with liberty to restore on 7 days' notice.

    ii) Koch gave undertakings set out in Schedule 1 to the Order.

83. Schedule 1 was signed by Sharon Mew, Finance Manager of Koch. She dated, and timed, her signature as "23 March 2018 16:32". The key provisions of the undertaking were as follows:

    Paragraph 1 "[Koch] shall by 4pm on 29 March 2018 deliver up to the Claimant all products in its custody or power produced by or for [Demand] that are unsold at 29 March 2018 ("the Stock") by making those items available for collection by Demand …" The undertaking expressly excluded products in the possession of customers (whether on consignment or otherwise), or products recently returned by customers and not processed. Such items "shall remain subject to the agreement dated 1 April 2015".

    Paragraph 4 "[Koch] will not dispose of, damage, modify, move or otherwise deal with the any [sic] unsold products in its possession custody or power produced by or for [Demand] save for the purpose of carrying out the terms of this Order".

84. My understanding of the undertaking is that it would have permitted Koch to sell stock until 29 March 2018: the Stock which is to be delivered up comprises those products which are unsold as at that date. Paragraph 4 is to be read subject to Paragraph 1.

85. In the meantime, and unbeknown to Demand until 28 March 2018, Koch sold approximately 19,000 units of stock to The Book People.

i) Mr Cronin contacted Sarah Walden of The Book People on the evening of 20 March. At 05.59 on 21 March he emailed her, referring to their discussion the previous night and set out a range of items, quantities available and prices. All items were gifting products, including five different construction sets (one of which was the Flying Scotsman). The subject line of the email was "Last Chance to Order".

ii) At 08.39 on the same morning Ms Walden replied, proposing to take 19,000 units. She could not take all of the lines, for a range of stated reasons, one of which was that "you want a little too much on the construction sets".

iii) At 14.06 on 21 March Ms Walden wrote "Happy to confirm we have deal at £3.20 per unit on the construction kits and the prices in the presentation for Dinosaur and Fairy Nightlight". She asked Mr Cronin to provide relevant data to a colleague, so a purchase order could be raised. She said "To confirm – we will take delivery next week …. For payment in August".

iv) Mr Cronin provided a spreadsheet of the relevant information at 15.59 on 21 March. In his email he said (in bold) "Lisa can you please confirm that when these POs are sent over to us and when we get confirmation of delivery that under no circumstances should emails also be sent to anyone at Demand Media – or anyone with a Demand Media email address." In the same email Mr Cronin instructed a colleague to ring fence the stock for The Book People on a dummy order, anticipating that purchase orders would be received the following day.

v) Invoices from Koch showing the sale of stock to The Book People are dated 23 March 2018.

vi) An email from Kuehne & Nagel on 23 March 2018 at 14.43 to Koch, subject line "Book People" states "Just to confirm this order is now off the system, no shortages". [3/1475A]

vii) Kuehne & Nagel's delivery notes show The Book People accepting delivery on 26 March 2018.

viii) Mr Fenwick discovered The Book People sale on 28 March. On that day:

a) Mr Peter Rowlandson of Koch sent Demand a stock report which was said to contain all the stock that Demand was due to collect the following week. Compared to a stock report of 21 March 2018 it appeared that there were 18,699 units missing of which 14,894 were construction sets.

b) Mr Fenwick regained access to KM Hub. He learned that Koch had sold stock to The Book People.

ix) On 28 March Mr Fenwick wrote to Ms Walden asking to speak to her (or a colleague) as soon as possible regarding the stock The Book People had purchased which, Mr Fenwick stated, Koch was not allowed to sell.

x) Ms Walden forwarded the email to Mr Cronin asking "I do not want to be caught in the middle of this – can you advise?". Mr Cronin replied on the same day saying that the sale of stock in question was conducted with the help of Koch's lawyer. He said "Obviously it is important to recall that you took possession of the stock on Friday afternoon (23 March 2018) when the sale was completed and you organised and provided the collection of the goods via a third-party logistics company." Mr Cronin accepted, when it was put to him in cross-examination, that Koch wanted to emphasise that the sale was on 23 March because after that it would not have the right to sell stock.

86. Mr McNicol's evidence (statement paragraph 43) was that The Book People sale allowed Koch to recover its manufacturing costs and limited the scope for Demand to go into insolvency and escape its obligation to account for manufacturing costs.

87. Mr Cronin's evidence (first statement paragraph 26-27) is that he was asked by Mr McNicol to conclude any sales he could to minimise the loss to Koch/Demand arising from the unpaid manufacturing costs that Koch had advanced.

88. In cross examination he said that The Book People and Koch shared the same Kuehne & Nagel warehouse. Stock was moved from Koch's area to The Book People's area.

89. Mr Cronin said that he was aware that there were legal exchanges but did not know exactly what. He was reluctant to accept that The Book People Sale was put through urgently, but in my judgment it is clear that it was. Mr Cronin said that he was asked to sell stock to recoup the money Koch was owed in respect of the manufacturing costs of the WH Smith stock, and I accept that. It seems clear to me that Mr McNicol's desire was to recoup as much as possible before Koch became bound to stop selling and deliver up unsold stock to Demand.

90. It is clear that, faced with the prospect of a court application for delivery up of stock, Koch acted as quickly as it could to make a sale of stock, and that it deliberately tried to keep that from Demand by excluding Demand from KMHub, and by asking The Book People not to communicate with Demand.

91. Selling stock when there was a live issue as to whether it was entitled to retain or sell stock, and when there was a pending application for delivery up, was a risky strategy. Koch may be regarded as sailing very close to the wind. It was put to Mr McNicol variously that Koch's actions were "sharp" or "dishonest". But the real question is whether, as a matter of contract, the terms of the Distribution Agreement permitted Koch to carry on selling products until expiry of the agreement, or until the undertaking in the Consent Order came into effect.

92. Demand's case is that the stock sold to The Book People was sold at drastically reduced prices, well below the prices set by Demand, and well below the prices previously obtained by Koch for the same stock. The prices, according to Demand, represented a reduction of some 70% of the trade price.

93. Demand does not identify prices that were set for the stock sold to The Book People. Paragraph 29 of the Particulars of Claim originally claimed the difference between the prices at which Koch sold the stock and "the Set Price" (defined as the price set by Demand pursuant to its implied term as to price – paragraph 5(a)). However, in the Re-Amended Particulars of Claim reference to "Set Price" is deleted from paragraph 29(a) and replaced with the "average selling price achieved by the Defendant" for the stock.

94. Mr Cronin (first statement paragraphs 31-33) disputed that The Book People, or any other customer would have paid more for the volume of stock sold. The sale was of 18,699 units, compared to 15,000 of the same gift sets sold in the previous seven months. Mr Cronin pointed to volume sales to The Book People at lower prices than £3.20 per unit: £2.80 for 6,000 camper van units in September 2016 and £2.80 for 20,000 campervan units in February 2017. Mr Fenwick was aware of the pricing in October 2016.

95. My conclusions on The Book People Sale are as follows:

    i) As Koch had originally paid the manufacturing costs of this stock (as with all stock) it had advanced monies within the meaning of clause 4.1 of the General Terms, and therefore it had title to the stock.

    ii) Demand argues that at the time the sale of The Book People Stock occurred it had paid all sums owing to Koch, and therefore title to the stock transferred to Demand. It follows from my findings in relation to the WH Smith Terms that Demand is wrong about this: a substantial sum was owing to Koch in respect of manufacturing costs for WH Smith stock.

    iii) Whatever the position as to title (i.e. even if Demand owned The Book People Stock) it follows from my findings on the terms of the Distribution Agreement that Koch was entitled to sell the stock, up to the date of expiry of the Distribution Agreement. Demand did not have the right to require return of stock before that date, and during the notice period there was no limit imposed on Koch's freedom to sell stock.

iv) By the Consent Order Koch voluntarily agreed to a restriction on what otherwise would have been its right to sell stock. It is not alleged that The Book People Sale was a breach of the terms of the Consent Order.

v) I have rejected Demand's case as to price setting, and therefore Koch was entitled to sell The Book People Stock at the prices obtained.

96. It follows therefore that Koch did not act in breach of the Distribution Agreement in making The Book People Sale.

97. Nor did the sale amount to a conversion. I accept Ms Bayliss' statement of the law at paragraph 21 of her Closing Submissions. Conversion, as she says, consists of dealing with property inconsistent with another's right. Failure to return on demand may constitute an act of conversion. A person who consigns goods has a right to give directions as to how the goods should be disposed of. The application of these general principles to this case depends on the scope of Koch's rights in respect of the goods consigned under the Distribution Agreement. Koch dealt with The Book People Stock in a manner consistent with its contractual rights and there was therefore no conversion.

MONTHLY PAYMENTS

98. Demand also claims that Koch did not make the monthly payments that it was obliged to make in the period between notice and termination:

i) On 15 February 2018 payment for December sales was due, put by Demand at £2,714.62;

ii) On 15 March 2018 payment for January sales was due, put by Demand at £15,820.02.

99. Koch accepts that under the Commercial Terms it was obliged to pay Demand sales revenue generated within 45 days of the end of the calendar month when sales were reported. However, Koch argues that it was entitled to debit manufacturing costs from sales invoices 75 days after they had been incurred. I do not understand Demand to dispute that. The dispute is whether there were in fact manufacturing costs outstanding at the time of the February and March monthly payments.

100. Koch's case is that no payments were due between December 2017 and March 2018 as the WH Smith manufacturing sums were due and owing, and those sums exceeded the amount that would otherwise be due. Demand argues that WH Smith costs were not owing because of the WH Smith Terms, which meant that manufacturing costs were not payable unless and until stock was sold or returned in saleable condition by WH Smith to Koch. I have rejected Demand's case on the WH Smith Terms. It follows that the manufacturing costs in respect of WH Smith stock were owing. The amount owed exceeded the monthly payments that would otherwise have been due.

101. In my judgment there is no breach of contract on Koch's part in not making monthly payments in February and March 2018 and the claim in respect of those monthly payments fails.

MISSING STOCK

102. After the Consent Order had been made Koch delivered up stock to Demand. Demand's pleaded position (RAPoC paragraph 21) is that 2,147 units are missing, even after accounting for 989 subsequently recovered units. These units "the Missing Stock" are set out in a schedule to Ms Barclay's statement [1/578], which shows 2147. The Missing Stock was calculated by Ms Barclay by comparing the list of stock delivered up with the stock report sent by Mr Penhaligon on 21 March 2018.

103. In her oral evidence in chief Ms Barclay changed her evidence from paragraph 5 of her first witness statement, explaining that the correct figure for the Missing Stock was 2147, not 1,743 as referred to there. 2147 is what the document ([1/578] exhibited to her first statement shows. I accept Ms Barclay's evidence on that, and she was not challenged on it in any event.

104. Koch does not dispute that these units were not returned. It gives no explanation as to the whereabouts of the units, or as to why they were not delivered up. It does not say that the units were in fact sold. Accordingly, in the absence of evidence from Koch, I take the documents at face value. I find that the Missing Stock units were in Koch's possession as at 21 March 2018 and have not been returned.

105. Ms Barclay's schedule of the Missing Stock shows Mr Fenwick calculated the value of the Missing Stock to be £10,930.64. That is based on an estimated value that could have been achieved by selling the stock taking into account its age and sales potential. The manufacturing value of the Missing Stock is £3,371.48 (Ms Barclay's Schedule [1/578]).

106. Koch's defence to this claim is to rely on clause 4.5 of the General Terms. This provides:

> "Discrepancies of the warehouse stock (calculated once a year on all adjustments made up to 31 December) of up to +/-3% shall be allowed and will not be charged by one party to the other. Larger discrepancies shall be charged at the Supplier's manufacturing costs of the relevant Product(s)(not including author royalties, licences etc). The foregoing must be documented by the Supplier by means of invoices from its suppliers (manufacturer, printer etc). Koch shall only have liability for accounting for greater discrepancies than +/-3% so long as Supplier has supplied to Koch within 7 days of every month end, a report showing by product, quantities that have been sent to Koch for storage in that month. This used as the basis for agreeing the stock and sales report that is issued by Koch to Supplier (see clause 5.1)."

107. Koch argues that clause 4.5 applies to the Missing Stock. It submitted that on a natural reading of clause 4.5 it applies to discrepancies of warehouse stock at

any time in either party's favour. Warehouse stock included all stock whether in its warehouse or on consignment. It accords with the commercial purpose and reality of the Distribution Agreement in that in managing large quantities of stock in its own warehouses and on consignment at customer's stores stock may go missing. Koch argues that the Missing Stock is within the 3% tolerance.

108. I am not satisfied that 4.5 provides a defence to Koch in these circumstances.

i) For clause 4.5 to apply it would be necessary to show that the Missing Stock is "warehouse stock". That is the term used in the General Terms – not "stock" or "any stock". Koch has offered no explanation as to the reason the stock is missing, nor as to its whereabouts before it was realised to be missing. In those circumstances, in my judgment clause 4.5 cannot be used as a catch all to excuse liability for any missing stock for whatever reason or in whatever circumstances it is missing.

ii) The Missing Stock appears from a comparison of what was delivered up to Koch after 29 March with a stock report prepared by Mr Penhaligon on 21 March 2018, at which point the application for delivery up had been served. Given the stock was accounted for by Koch as late as 21 March I do not accept that its loss is attributable to a warehouse discrepancy.

iii) It is difficult to see how clause 4.5 of the General Terms functions in the circumstances of the trading relationship between the parties. The information provision part of the clause depends on Demand providing information from which discrepancies can be determined. Given that all manufacturing was in fact undertaken by Koch, who then distributed the manufactured goods to sellers, it is difficult to see how Demand could ever be in a position to know of any discrepancies, other than as and when stock was returned at the end of the agreement.

109. I also accept Demand's argument that if clause 4.5 were to apply, Mr McNicol's calculation of the 3% tolerance is wrong. The discrepancies are to be calculated on an annual basis, not over the lifetime of the Distribution Agreement. In my judgment only 2018 discrepancies would be relevant, and the discrepancies for the year must be taken as actual discrepancies in the part of the year concluded by the time the Distribution Agreement terminated.

110. In my judgment, Koch is liable to account for the Missing Stock, and that should be taken into account in the final account. However:

i) Given that I have rejected Demand's claim that Koch was obliged to return stock under the Distribution Agreement prior to termination, and after termination Koch is entitled to retain stock pending final account, I find that Koch was not in breach of contract by failing to deliver up the Missing Stock, nor is it liable for conversion; but it must now account for the Missing Stock in the final account.

ii) I am not persuaded that Koch was in breach of the Consent Order in failing to return the Missing Stock. Paragraph 1 of the undertaking to the Consent Order applies to products which are in Koch's possession, custody or power. Further, the paragraph does not apply to products which are in the possession of customers or have recently been returned. As paragraph 1 makes clear, those products remain subject to the Distribution Agreement, but fall outside the undertaking. The onus falls on Demand to show a breach of the undertaking. For the undertaking to be breached it would be necessary to show that Koch were in possession, custody or control of the Missing Stock at the time that it should have been delivered up, and the evidence in relation to that is inconclusive.

111. In accounting for the Missing Stock I accept Demand's case that it is entitled to the market value of the stock and is not limited to manufacturing cost (which Koch argued was the effect of clause 4.5). As to that value, Koch offered no evidence, and Mr McNicol's evidence in cross-examination was that clause 4.5 meant that Koch was not liable for the Missing Stock and therefore its value was not material to Koch's case. Having failed in that argument, Koch offers no good basis to depart from Demand's valuation, which I accept, in the sum of £10,930.64.

FURTHER MISSING STOCK

112. The "Further Missing Stock" is 35,484 units that Demand alleges have not been returned. Demand says that the failure to return these units became clear when Koch produced the draft final account in October 2018. The failure to return is alleged to be a breach of contract and/or a conversion, but not (in contrast to the Missing Stock) a breach of the Consent Order. Demand claims the total sales value, which it puts at £105,124.87.

113. Koch's case is that part of this stock was stock destroyed by WH Smith. I accept Koch's case that this is in fact what happened, and I have also accepted Koch's case that Demand had agreed WH Smith's terms in this regard. There can be no claim in respect of the WH Smith portion of the Further Missing Stock. I will invite the parties to agree on the WH Smith portion of the Missing Stock before making a final order following judgment and will hear further submissions if necessary.

114. Koch say that some of the Further Missing Stock is held by Amazon on Demand's behalf, and Koch presumed that Demand would take over this stock at the end of the Distribution Agreement. Mr Fenwick's evidence (third statement paragraph 40, confirmed in cross-examination) is that Amazon have said that it does not have this stock. Mr Fenwick points out that the stock is showing as in Koch's warehouse in an October 2018 stock report. Koch has produced no evidence to substantiate Mr McNicol's assertion. In any event, the suggestion that it is Demand's obligation to retrieve the stock from Amazon at the end of the agreement, rather than Koch's obligation to return it, is at odds with the terms of the Distribution Agreement.

115. As to the remaining units, Koch has led no affirmative case as to what has happened to the stock. Mr McNicol deals very briefly with stock consigned to Wowudu, Amazon, Gardners, HMV and The Hut at paragraph 134-135. Beyond saying The Hut stock is available for collection, he offers little explanation as to the stock discrepancies and relies on clause 4.5 of the General Terms.

116. I have rejected Koch's argument as to clause 4.5 of the General Terms. In my judgment Koch are liable to account for the Further Missing Stock (save for the WH Smith stock) and either to deliver it up or account for it. Having rejected Koch's argument as to the application of clause 4.5 I accept Demand's case as to the applicability of the market value of the stock, and as to the quantum of that value. Koch offered no real evidence as to an alternative value.

117. However, as with the Missing Stock, in my judgment the proper analysis is that Koch are not obliged to return the Further Missing Stock pending the final account. In preparing that account they will have to give credit for the Further Missing Stock, less that part of the Further Missing Stock which is attributable to the WH Smith issue.

FLYING SCOTSMAN INDEMNITY

118. One of the construction sets distributed by Koch was a "Flying Scotsman" set. Demand was able to produce and sell the Flying Scotsman set as it had entered into a licensing agreement with SCMG Enterprises Ltd (the SCMG Licence Agreement).

119. The Flying Scotsman sets formed part of The Book People Sale. I have dealt with The Book People Sale above. I have rejected Demand's claim that Koch sold The Book People Stock at a price less than that at which it was entitled to sell that stock. Demand make a further specific claim in relation to the Flying Scotsman set. It says that it had agreed with SCMG Ltd. that the retail price permitted for the sets would not be less than £12.99, and that RRP should have generated a trade price of £10.83. The sets were sold to The Book People at £3.20.

120. I am not satisfied that Koch was obliged to sell the Flying Scotsman at no less than a minimum price set by reference to the SCMG Licence Agreement.

    i) I have already rejected Demand's case that Koch could only sell products at prices set by Demand.

    ii) There is no evidence that Demand either agreed a minimum price with Koch for the Flying Scotsman sets, nor notified Koch that it was subject to a particular minimum price. Demand points to an email from Mr Fenwick of 4 May 2017 as informing Koch of the RRP of the Flying Scotsman sets. That email attaches to it a list of construction sets and other gift products, each with an RRP. The RRP for the Flying Scotsman set is £24.99.

iii) There is nothing in that email that suggests that there was a particular minimum sale price for the Flying Scotsman set; it was treated no differently to the other sets: the list does no more than give an RRP for each product.

iv) As I have found in relation to The Book People Stock, the RRP is neither the price at which gift products were sold to customers, nor a figure from which such a price can be worked out by application of a mathematical formula. Accordingly, notifying Koch of the RRP did not limit Koch's freedom to negotiate on price in selling the products.

v) Koch was not party to the SCMG Licence Agreement, and there is no suggestion that it was aware of its terms.

121. Accordingly, I do not accept that Koch acted in breach of contract in selling the Flying Scotsman sets, as part of The Book People Stock, at the sale price of £3.20. Nor did it commit the tort of conversion. I find no basis upon which Koch is liable to indemnify Demand in respect of sums Demand may have had to pay to SCMG. Demand's claim, for £634.27, is rejected.

FINAL ACCOUNT

122. Subsequently Koch produced no further monthly account for the period after January 2018 until 4 October 2018 when it produced a final account. That final account was revised on 13 February 2019. In it, Koch shows an amount of £14,820.02 as owing from Demand to Koch. Demand dispute this figure and claim that in fact Koch owe Demand £55,299.72 (leaving aside matters of damages for the claims in these proceedings). The difference is due to two items:

i) Koch has debited outstanding manufacturing costs of the WH Smith Stock in the sum of £64,580.71 (referred to by Demand as "the WH Smith Debited Sum")

ii) £5,539.03 has been debited attributable to credit notes issued to WH Smith (referred to by Demand as the Further Debited Sum).

123. Demand's claim that it is not obliged to pay the WH Smith Debited Sum depends upon the WH Smith Terms. It claims that it was not obliged to pay for the manufacture of stock which was neither sold by WH Smith, nor returned in a saleable condition. I have rejected Demand's case that the WH Smith Terms applied and found that Demand knew and agreed that WH Smith would destroy unsold stock in store. In the absence of special terms such as the WH Smith Terms Demand is obliged to pay manufacturing costs of products manufactured under the Distribution Agreement. Koch was entitled to deduct the manufacturing cost from the account, and I find that the WH Smith Debited Sum was properly debited.

124. The Further Debited sum is said by Koch to have been debited in respect of credits to WH Smith.

125. Demand accept that WH Smith were entitled to a 5% retro commission on sales but claim that all such retro commission had been paid by the end of the agreement.

126. The only witness on behalf of Koch to deal with the Further Debited Sum is Mr Cronin. In his second statement paragraphs 7.5 and 30-31 he speaks to the existence of the arrangement for a 5% retrospective credit as a discount to WH Smith on stock sold to them. He does not say anything about the specifics of the particular credit to which the Further Debited Sum relates.

127. However, when he gave evidence in chief Mr Cronin changed this evidence. He said that the agreed retrospective discount was 10%. That change in his evidence is at odds with Koch's pleaded case (Amended Defence paragraph 26B(d)) which refers to a 5% discount. It is also at odds with the contemporaneous documents: Mr Cronin's 19 May 2016 email to Ms Simpson refers to invoicing WH Smith at 45% and allowing a 5% retro. The reference to 45% is, I understand from Mr Cronin's evidence, a reference to 45% of RRP.

128. Mr Cronin in his oral evidence said that the arrangement was that Koch would invoice at 50% and the retro would be 10%. On his evidence, the net result would be the same: i.e. the end result would be WH Smith would pay 40%. That may be right, but the late change in evidence to a position that is not supported by the documents leads me to conclude that Mr Cronin does not have a clear recollection or understanding of the arrangements in relation to the retro credit agreement. In addition, he does not give any evidence as to the circumstances of the particular credit said to give rise to the Further Debited Sum. No other witness deals with this on Koch's behalf.

129. In the circumstances, I find that no proper basis has been shown for the Further Debited Sum, and Koch is not entitled to debit that amount in the Final Account.

COPYCAT PRODUCTS

130. In or around the summer of 2017 Koch began to sell its own construction sets. Demand claims that they were "strikingly similar" to Demand's own construction sets. Demand refers to twelve construction sets which it labels "Copycat Products".

131. One of those sets, the Hawker Hurricane set is the subject of a separate registered design claim that I transferred to IPEC on Koch's application at the beginning of the trial. Demand claims that Koch's Hawker Hurricane infringes Demand's design right in relation to its Spitfire set. Having transferred that claim, I will say no more about it here.

132. Demand's claim about the Copycat Products raises two distinct grounds:

i) Breach of an implied term (implied term (b)) that Koch would not produce and offer for sale similar products to those it sold on behalf of Koch.

ii) Breach of a contractual or equitable/tortious duty of confidence.

Implied Term (b)

133. The RAPoC paragraph 5(b) alleges an implied term that during the term of the Distribution Agreement Koch would not produce and offer for sale to customers of Demand products that were substantially similar to those that Koch had agreed to sell on behalf of Demand.

134. Demand's claim did not focus on implied term (b); the thrust of the claim in relation to Copycat Products was breach of confidence:

i) RAPoC pleads implied term (b) and pleads at paragraph 28 that sale of the Copycat Products was in breach of the term.

ii) Demand's written opening submissions at paragraphs 81-86 and written closing submissions at paragraph 94-105 deal with breach of confidence and advances no case as to why an implied term not to compete arises. Similarly, oral argument focussed on the breach of confidence claim

iii) Mr Fenwick's evidence offers little, if any, basis for the implication of the alleged term. At paragraph 45 of his second statement he says that it is standard industry practice that a company's distributor does not sell its own competing products to the company it sells and distributes for. He goes on to say "That is not to say that they could not sell and distribute a competing product made by another customer they sell and distribute for, but that is a very different matter." At paragraph 46 he says that while it may have been the case that there may not have been anything to prevent any other party from making and selling construction sets similar to Demand's, he did not think that could apply to Koch. Koch was in a unique position to know which lines did or did not sell, and thereby produce a commercial advantage by only producing profitable lines. He returns to the Copycat Products in his third statement at paragraphs 44-45 but, again, the focus is on confidential information.

135. There is no express term in the Distribution Agreement limiting Koch's ability to sell products that compete with, or are similar to, those of Demand. It would have been open to the parties to negotiate such a term, but they did not do so.

136. Koch dispute the "standard practice" alleged by Demand, and there is no evidence as to whether there is such a practice or not, save for the say so of the parties. On the evidence, I cannot find that there was such a standard practice. I do not in any event understand the basis of Mr Fenwick's distinction between a distributor selling a third party's competing products (permissible) and a distributor selling its own competing products (impermissible).

137. I accept Koch's submission that there is no general implication as a matter of law that exclusive distributors must not compete with their suppliers. Neither party took me to any authority to that effect.

138. In my judgment such a term is neither obvious, nor implied as a matter of business efficacy.

i) The Distribution Agreement works without the implication of such a term. There may be good reasons why a distributor should not compete with its supplier. On the other hand, I accept Koch's argument that there may be sound business reasons for selling competing products, including an increased opportunity to penetrate a market (Mr McNicol's statement, paragraphs 7-9).

ii) As part of the factual matrix it is relevant that at the time of the first agreement, and at the time of the Distribution Agreement, Koch was a substantial enterprise in the business of manufacturing and distribution. Demand was aware of that. A restriction on selling products which competed with Demand may well have been a significant restriction on Koch's other business activities. I would expect a term with such potential impact to be expressly agreed between the parties. In my judgment Demand had no reason to believe that it was either obvious or a necessary implication that Koch would not sell similar or competing products.

Breach of Confidence

139. I turn then to the claim for breach of confidence. Clause 8 of the General Terms provides that the parties each undertake "to remain silent about all business and operational matters that become known to them within the framework of this Agreement, in particular stock or sales reports, statistics, customer lists etc."

140. Demand lists six categories of information it alleges to be confidential at RAPoC 12. Apart from (e), design and packaging specification, the other categories are all commercial data: such as customer lists, sale and manufacturing data.

141. The design and packaging information cannot be confidential once a particular product is on the market, but I accept that it may be confidential before the product is launched. Similarly, the identity of a licence partner will be public knowledge once a licensed product is on the market; it may be confidential before launch.

142. I accept that customer lists, sales data, manufacturing data and pricing may be confidential in nature and may be of use to a competitor. Koch's evidence, which I did not understand to be challenged, was that RRP and trade prices were published at spring and autumn trade fairs. Those prices may be confidential until such fairs. Discounted prices and manufacturing prices remained confidential.

143. There is however a fundamental difficulty as to whose information this is, and what is the scope of the duty in relation to this information.

144. The contractual duty in clause 8:

i) Is a duty to "remain silent". It is not clear what the extent of that obligation is and whether, and to what extent, it means that a party is restrained from using information for its own purposes obtained in performance of the Distribution Agreement. Most naturally, as Koch submits, it means that the parties must not disclose such information to third parties. Koch submits that the obligation to remain silent did not prevent either party from utilising any shared information gained under the Distribution Agreement. I accept that submission, principally because I do not see in practice how either party could be prevented from making use of this information (absent an express restriction on competition) and how it could be separated from the general skill and knowledge of the parties.

ii) The duty is mutual. Demand's case is that the information which it alleges to be confidential belongs to Demand. Koch is right in saying that much of the information in question was generated by Koch in the course of the operation of the Distribution Agreement. Koch sourced the manufacture of products, was responsible for placing orders, and for seeking and negotiating sales. In so doing, it is possible that a distributor acts as agent of the supplier, and therefore that information acquired as agent belongs to the supplier, but that is not necessarily the case. Although the case was put on this basis in cross-examination, it was not the way the case was pleaded, and the case was not advanced generally that Koch was an agent of Demand.

iii) The express terms of the Distribution Agreement do not provide that information generated during the course of performance of the Agreement belongs to Demand. The only express term, and the term on which Demand relies, is clause 8 of the General Terms.

iv) Clause 8 creates a mutual obligation to remain silent about all operational matters that become known to the parties within the framework of the agreement. The clause does not give a clear basis for finding that the commercial information about which Demand claims belonged to Demand, any more than it belonged to Koch.

145. Demand relies in the alternative on an equitable or tortious duty of confidence. Demand relies on the well-known principles for such a duty derived from ***Attorney General v Guardian Newspapers No. 2*** [1990] 1 AC 1091 at 281B.

i) The information must have the necessary degree of confidence;

ii) The information must have been communicated in circumstances importing an obligation of confidence to the recipient;

iii) There must be unauthorised use.

146. The alternative formulation of the claim does not assist Demand. I accept that in a suitable case a duty of confidence in equity may arise alongside a contractual duty of confidence and may differ in scope from a contractual duty. In this case, the question of the meaning and scope of the contractual duty is highly relevant to the questions (a) whether the information is Demand's confidential information; (b) whether it was imparted in circumstances imposing a duty of confidence; and (c) whether Koch's use of the information (if it was used) was outside the scope of authorised use. No specific case was advanced as to why any information (either individually or collectively) which may fall outside the scope of the contractual term may still be subject of an equitable or tortious duty.

147. Demand further relied on a passage from ***Gurry on Breach of Confidence*** (2nd ed) at 9.37-9.38. That passage, in a chapter entitled "Common Classes of Obligation", deals with distribution agreements. The passage is largely descriptive of common factual situations rather than a statement of law. I accept the proposition that, in the absence of an express contractual term as to confidentiality, the court may hold that confidential information disclosed by one party to the other was disclosed for the purpose of the agreement only. The case referred to, where technical drawings were disclosed to a distributor, is an illustration of that proposition. However, everything depends upon the circumstances. In contrast to the cases to which ***Gurry*** refers, (a) the significant information in this case (e.g. sales and manufacturing data) was not disclosed by Demand, but generated by both parties (and in most instances by Koch) in the performance of the agreement; (b) this is not a case where there were no terms as to use of information: the parties had expressly agreed to clause 8, which provides Demand with more limited rights in relation to that information.

148. I am not, in any event, persuaded that Koch has used any of this information in manufacturing and selling the Copycat Products.

149. Demand submits (relying on ***Snell's Equity*** 33rd edition at 9.18 and ***Wade v British Sky Broadcasting Ltd.*** [2014] EWHC 634 at para 59) that where there are significant similarities between the result of A's work and the confidential information there is a strong inference that the work done is a result of breach of confidence. The burden of proof then passes to A to establish independent derivation.

150. The passage from ***Snell*** is drawn from ***Wade***. In ***Wade*** Birss J at paragraph 59 summarised principles well established in copyright cases. He said the legal burden remained on the claimant throughout. The claimant may raise a strong inference that copying must have taken place by pointing to significant similarities between the claimant's work and the defendant's work and the existence of an opportunity for the defendant to copy. Such an inference may shift the evidential burden to a defendant to rebut the inference.

151. Birss J said "The logic is capable of applying in some breach of confidence cases". Having considered the facts of the particular case (which concerned a proposal for a new television programme) Birss J considered that the similarities in the parties' programmes meant that an inference of copying had

"some substance but it is not overwhelming". The inference was not strong enough to leave him in any doubt as to the defendant's evidence, which he accepted, of independent derivation.

152. ***Wade*** demonstrates that whether an inference arises, and whether such inference is rebutted, depends on the evidence. In ***Wade*** the claimants had shared a programme idea with the defendant; the defendant rejected it, but then went on to produce its own programme which the claimants claimed was strikingly similar in its elements. The information alleged to have been misused was a PowerPoint deck setting out a proposal for a television programme. The judge found the deck itself was confidential, but ultimately did not make a finding as to whether individual ideas within it were confidential. He found that the defendant's programme idea had been reached independently. The claimants' case was based on the similarity of the two "products": that is to say the two programme formats. In the circumstances where the claimants had given the defendant their ideas for their programme one can see the relevance of considering whether the two programmes were sufficiently similar to call for an explanation of whether the defendant's idea had been reached independently.

153. In my judgment, the present case is very different. Similarity between Demand's construction sets and those of Koch sheds no light on the question of whether Koch used Demand's confidential information.

154. Demand does not argue that the concept of the construction sets was confidential, nor (apart from in the transferred registered design claim) does it claim confidentiality in the particular design of the sets. Nor could it have made such arguments. There are other similar construction sets on the market, some made by well known brands. The evidence indicates that some of Demand's own sets were designed by reference to the sets of competitors publicly available in the market. Mr Fenwick's own evidence (second statement paragraph 43) is that he suggested the factory use a set previously sold by Meccano as a guide to what Demand wanted for its Spitfire Construction Set. There is also evidence that some of Demand's sets were "off the peg" designs chosen from a catalogue of existing sets offered by the manufacturers (McNicol paragraphs 143-146). The publicly available nature of such sets has two consequences. First, as I have indicated, it means that the product concept and design is not confidential information belonging to Demand. Second, no inference arises that Koch has used Demand's information in designing and launching its own set. While an inference may arise from similarity between a defendant's product and a product the concept for which is confidential, no such inference arises where the defendant's product is similar to a range of third-party products available on the market and available from manufacturers with which it works.

155. The confidential information upon which Demand relies is commercial information: customer lists, price lists, and sales data. In my judgment any similarity in product does not give rise to an inference that such data was used by Koch. Nothing in the evidence as to the nature of the products, nor as to the way in which they were sold and marketed, indicates that Koch had made use of customer, price or sales data.

i) Customer List. Demand relies on a customer list that was provided to Koch in March 2015 [2/1106-1111] (Demand closing submissions paragraph 102). Mr Fenwick's evidence was that the list showed the value of sales that Demand had achieved for each customer. I accept that evidence but:

   a) There is no evidence to indicate that Koch's sale of the Copycat Products had been targeted by use of this customer list.

   b) The customer list pre-dates the introduction of Demand's non-DVD gifting products (such as construction sets) by more than a year. There was no evidence to indicate how this list would be relevant to either party in formulating a plan to sell construction sets.

ii) Price Lists. There was no evidence to indicate that Koch's pricing of the Copycat Products was sufficiently similar to that of Demand to suggest that pricing information had been used by Koch, for instance to undercut Demand by a small margin.

iii) Sales data. At paragraph 102(3) of its closing submissions Demand deals with sales data about Demand's business, and also access to Demand's market projections, sales forecasts and schedules for new releases. In fact, the RAPoC paragraph 12 make no reference to projections, forecasts or schedules for new releases, but no objection was taken by Koch on a pleading ground, and I am prepared to consider that such documents could in principle be confidential. However, Mr Fenwick's evidence (second statement paragraphs 42-47, third statement paragraph 44-45) does not rely on any particular forecast, plan or projection. Rather his position is that historic data as to sales and manufacturing would help Koch to decide what products it should make and sell and what price and quantities it should make and sell. There is however no evidence that the product range, pricing, and quantities of Copycat Products was in any way informed by this information. Koch may well have obtained the idea of selling construction sets from Demand and may well have known that they were profitable as a result of the sales data from the Distribution Agreement, but that information is too generic to amount to protectable confidential information.

iv) Packaging – Mr Fenwick's evidence (second statement paragraph 45, third statement paragraph 43-46) falls some way short of establishing that there was any feature of the packaging that was confidential, either at all or once Demand's products were on the market. I accept Mr Fenwick's evidence that the email relied on by Mr McNicol at paragraph 162 of his statement (17 March 2017 [2/1103]) does not show that Demand copied Koch's packaging. However, the fact that Demand was considering looking at the same packaging as Koch demonstrates that, at that time, Koch's packaging was different to that used by Demand and not copied from Demand.

v) Licensing partners – Mr Fenwick complains that Koch has approached Demand's licensing partners (paragraph 45, second statement) the evidence he gives is in general terms. His complaint appears to be the fact of the approach, where he says, in some cases there was an agreement that Koch would not do so. There is no case brought on the basis that Koch was contractually bound not to approach licensing partners. I am not persuaded by Mr Fenwick's evidence that the identity of licensing partners was confidential, and he makes no specific allegation of misuse of confidential information in the approaches.

156. Koch argues that Demand's gifting business commenced in 2016, yet Koch indicated it intended to produce its own gifting products (including construction sets) in August 2016. In fact the email upon which it relies is dated 27 September 2016 [2/827], but the point remains valid: at the time Koch decided to produce construction sets, Demand's own construction sets were not yet well established and there would have been little sales data which Koch could have used in deciding on its own launch.

157. In conclusion on the Copycat Products breach of confidence issue:

i) I am not persuaded that the information about which Demand complains was confidential to Demand, either under the Distribution Agreement clause 8, or as a result of an equitable or tortious duty of confidence.

ii) If it was confidential to Demand, the obligation extended to "remaining silent" in relation to the information, and it is not clear that amounted to a restriction on either party using, as opposed to disclosing, the information.

iii) Whether or not the information relied on was confidential, it was not used by Koch to design or sell the Copycat Products.

CONCLUSIONS

158. In this section I set out a summary of my conclusions, by reference primarily to Demand's List of Issues.

159. *Did Koch breach the express or implied terms of the Distribution Agreement by failing to return The Book People Stock as requested by Demand?*

i) It did not.

ii) I have rejected Demand's case that the Distribution Agreement permitted Demand to require stock to be returned to it during the lifetime of the agreement. I have rejected Demand's case that there was an implied term to this effect. The limited express circumstances in which stock fell to be returned do not apply. Koch was not therefore obliged to comply with the request for return.

iii) Even if Demand had title to the stock, Demand was still entitled to retain the stock and to sell it up until the expiry of the Distribution Agreement.

160. *Did Koch breach the express or implied terms of the Distribution Agreement by selling The Book People Stock at a substantial discount without notice to Demand and without its agreement*?

i) It did not.

ii) I have rejected Demand's case that there was an implied term that Koch could only sell products at a price set by Demand, and I have rejected the contention that the agreement falls to be construed to that effect.

161. *Did Koch commit the tort of conversion by failing to return The Book People Stock and/or by selling the stock at a substantial discount*?

i) It did not.

ii) As I have found above, even if The Book People Stock belonged to Demand, Koch dealt with the stock in accordance with its contractual rights under the Distribution Agreement.

162. *Did Koch breach the express and/or implied terms of the Distribution Agreement and/or commit the tort of conversion and/or breach the terms of the Consent Order by failing to return the Missing Stock?*

i) For the reasons set out above under the heading "Missing Stock" I find that Koch was not in breach of contract, did not commit conversion and did not breach the Consent Order in failing to deliver up Missing Stock at an earlier time. It is, however, liable to account for the Missing Stock at is market sale value (as claimed by Demand) in the final account.

163. *Did Koch breach the express and/or implied terms of the Distribution Agreement and/or commit the tort of conversion by failing to return the Further Missing Stock*?

i) For the reasons set out above under the heading "Further Missing Stock" I find that Koch was not in breach of contract and did not commit conversion in failing to deliver up the Further Missing Stock at an earlier time. It is however liable to account for part of the Further Missing Stock at its market sale value (as claimed by Demand) in the final account.

ii) The part of the Further Missing Stock for which Koch is not obliged to account is the products consigned to WH Smith and Demand's claim fails in that regard.

164. *Did Koch breach the terms of the Distribution Agreement by failure to make the monthly payments required under the Distribution Agreement*?

i) It did not.

ii) It follows from my conclusions in relation to the WH Smith Terms that Koch was owed a substantial amount by way of manufacturing costs for the WH Smith stock. It was entitled to set those sums off against monthly payments that would otherwise have been due.

165. *What losses were caused to Demand by the above breaches and/or torts*?

i) It follows from my findings above that this question does not arise, as there were no such breaches or torts.

ii) The findings I have made in favour of Demand (as to Further Debited Sum, Missing Stock and Further Missing Stock) are matters to be taken into account in the final account. Demand has not been deprived of property at an earlier time, and no consequential loss arises.

166. *Did Koch breach the express and/or implied terms of the Distribution Agreement, and/or its duty of confidence to Demand in manufacturing and selling the Copycat Products*?

i) It did not.

ii) I have rejected Demand's case that there was an implied term that Koch would not sell competing products.

iii) Manufacture and sale of the "Copycat Products" was not a breach of confidence.

167. *Is Koch obliged to indemnify Demand for losses incurred by it in respect of the Flying Scotsman Stock including in respect of its obligations under the SCMG Licence Agreement?*

i) It is not.

168. *Did Koch breach the WH Smith Terms and/or the express and/or implied terms of the Distribution Agreement in respect of the WH Smith Stock?*

i) It did not.

ii) I have rejected Demand's claim as to the WH Smith Terms. In the absence of the WH Smith Terms, Demand was obliged to pay for manufacturing costs of the WH Smith Stock. Demand knew and agreed to WH Smith's required term that unsold stock in store would be destroyed. Demand was obliged to pay the manufacturing cost of such stock.

169. *Was the WH Smith Debited Sum lawfully debited by Koch in the final account?*

i) Yes it was, for the reasons set out in relation to the WH Smith Stock.

170. *Was the Further Debited Sum lawfully debited by Koch in the final account?*

i) I am not satisfied that Koch was entitled to debt the Further Debited Sum. Koch's case as to the terms of the retrospective credit arrangement with WH Smith was not clear, and I saw no clear evidence that Koch was entitled to this particular credit. Accordingly, in the Final Account Koch is not entitled to debit the Further Debited Sum of £5,539.03.

171. *What is the correct quantum of the Final Account sum?*

i) The correct figure is to be reached by starting with the February 2019 draft final account and making adjustments in Demand's favour in respect of:

a) The sale value, as claimed by Demand, of the Missing Stock;

b) The sale value, as claimed by Demand, of the Further Missing Stock (less the WH Smith consigned stock).

c) The Further Debited Sum.

ii) In circulating a draft of this judgment I invited the parties to agree the Final Account sum, so that a figure could be incorporated into the judgment. In the light of the draft judgment the parties have agreed the figures as follows.

a) The sale value of the Missing Stock, as claimed by Demand, is £10,930.64;

b) The sale value of the Further Missing Stock, as claimed by Demand, less the WH Smith consigned stock is £15,318.82.

c) The value of the Further Debited Sum is £5,539.03 (per paragraph 170 above).

d) When the February 2019 draft final account balance is adjusted to give Demand credit for the above three items, the final balance of the Final Account is £16,968.47 in favour of Demand. I shall give judgment for Demand in that amount.