SCHEDULE OF IMPUGNED VAR TRANSACTIONS

Structure of this Schedule

1. In this five-part Schedule to the main body of this judgment I address each of the impugned VAR transactions. Although more conveniently set out in a Schedule, the findings I make should be treated as if in the main body of the judgment. The discussion is intended to complement the more general analysis in the main body of the judgment and my conclusions there, and to provide detailed exemplars of the 'pattern' which the Claimants alleged and which I have concluded was demonstrated.

2. Although some repetition of the more general points made in my general analysis of the impugned VAR transactions in the main body of this judgment is inevitable, my intended focus is on any significant evidence or features which have not emerged from, or which provide a particularly significant illustration of some feature identified in, my overview of the impugned VAR transactions in the main body of the judgment.

3. There is a general point on the issue of knowledge, and in particular, Dr Lynch's knowledge of improper accounting of the individual impugned VAR transactions, which I should clarify. Although I do address this issue in respect of the individual impugned VAR transactions, the Claimants' position was that, in particular as regards the bulk of the impugned transactions which were with 'friendly' VARs, they did not need to establish that Dr Lynch knew about every one of them; and that it was sufficient that he knew of and authorised the practice of calling upon a friendly VAR, as and when required by a shortfall in aggregate revenue, to recognise revenue improperly. Accordingly, in some cases, they did not put forward transaction-specific evidence of his "guilty knowledge". I confirm that I have concluded, in line with this submission, that Dr Lynch knew of and authorised the practice, which became a pattern of which all the impugned VAR transactions were exemplars, of improperly recognising revenue from sales to VARs which lacked any real substance in order to make good (to the extent possible) shortfalls in properly recognised revenue from software sales. Subject to the proviso that if in any instance there was positive evidence to show that the relevant Defendant (in effect, Dr Lynch) did not have any knowledge the burden would be on the Claimants to provide additional positive evidence the other way, I have broadly (and except as otherwise appears in the context) accepted the Claimants' approach.

4. Most of the VAR transactions addressed were impugned by reference to some form of side agreement or understanding; but some (the *"pure collectability VARs"*) were impugned only on the basis that none satisfied the requirements of IAS 18.14(d). This Schedule is structured as follows:

   (1) Part I addresses VT1 (with MicroLink), VT2, VT3, VT4 and VT10 (all with Capax Discovery), VT5, VT6, VT7, VT8, VT13, VT25, VT32, VT33 and VT37 (all with MicroTech), VT11, VT12, VT30, VT31, VT35 and VT36 (all with DiscoverTech) and VT18 (with FileTek).

   (2) Part II addresses four further impugned VAR sales to Capax Discovery which followed VT10. These were VT20 (in Q4 2010, for end-user DKO), VT27 (in Q1 2011, for end-user McAfee), VT28 (in Q1 2011, for end-user UBS), and VT34 (in Q2 2011 also for end-user UBS).

(3) Part III addresses VAR transactions comprising the parts into which a very large composite deal with BofA (or subsidiaries of BofA) was split in circumstances described below. Two (VT16 and VT21) were with Capax Discovery and two (VT23/24) were with DiscoverTech.

(4) Part IV addresses three impugned VAR transactions (VT14, 15 and 26) with counterparties other than those I have called "the friendly VARs" (that is to say, Capax Discovery, FileTek and the Truitt companies).

(5) Part V addresses the remaining five impugned VAR transactions (VT9, 17, 19, 22 and 29), all with counterparties which were not "friendly VARs, and in respect of which no side-agreement or the like was alleged (the *"pure Collectability VAR transactions"*).

5. I adopt the same definitions in this Schedule as in the main body of the judgment.

PART I OF SCHEDULE OF IMPUGNED VAR TRANSACTIONS

Various exemplars of the impugned VAR transactions with 'friendly' VARs

6. In this Part of this Schedule, I have grouped various exemplars of the impugned VAR transactions with 'friendly' VARs. They are grouped according to the identity of the VAR involved, rather than chronologically: this reflects the way they were addressed in the written closing submissions.

VT1: comprising the 11 impugned MicroLink VAR deals

7. I have already noted some basic details about MicroLink in paragraph 1963 of the judgment. As there stated, MicroLink was the VAR in a series of reseller transactions in 2008 and 2009, of which the Claimants have impugned 11, all entered into in 2009. The Claimants referred to this series of transactions as "VT1".

8. MicroLink was one of a growing stable of 'friendly' VARs. It was headed by Mr David Truitt (who subsequently headed DiscoverTech, another 'friendly' VAR, and who co-founded MicroTech, a third 'friendly' VAR of which Mr David Truitt's brother, Mr Steve Truitt, was made Chief Operating Officer at Mr David Truitt's instigation). Without thereby pre-judging their activities with Autonomy, it is to be noted that Mr Stephan gave the following evidence at the US criminal trial:

> *"From my - what I saw at MicroLink, I was concerned that was the modus operandi of all these resellers, that the head of the company would sign whatever we wanted them to sign for the auditors but they had no intention of paying."*

9. The MicroLink transactions were the first of the *"at risk deals"* or *"acceleration deals"*[1] which Autonomy embarked on using 'friendly' VARs as vehicles through which Autonomy could recognise revenue in the quarter in which the transactions occurred to cover shortfalls identified in revenue from other sources identified by Mr Hussain. Impetus was given to the use of this expedient when EMC withdrew from its close association with Autonomy and the use of the favoured alternative programme of hardware sales for the same purpose became more difficult.

10. Autonomy had undertaken various transactions with MicroLink before the impugned VT1. None of the transactions with MicroLink prior to the Relevant Period was impugned, though (as explained above) no details were provided of their number or nature, except for a brief reference by Mr Egan, when he was cross-examined, to some of them being *"at risk deals"* (see footnote 283 in the main body of the judgment). The Defendants also referred to deals with MicroLink in 2009 which were not impugned: but again, no details were supplied.

11. The prospective end-users in the 11 impugned VAR sales referred to under the rubric 'VT1' were Allstate, JICPAC, United States Postal Service, United States Federal Government, Public Works & Government Services Canada, CIPM, VA VACO, IBM-Ameriprise, Navy Commander Sub Forces and DiscoverTech (though in respect of the last no side agreement was alleged to have been made and the transaction is impugned by

[1] See footnote 283 in the main body of the judgment.

reference to the alleged use of funds from Autonomy's later acquisition of MicroLink). The Claimants did not suggest that anything turns on the individual details of the various VT1 transactions: their claims apply across them all.

12. All of the purchase orders in respect of the VT1 transactions were made under the *'Autonomy Government Reseller Agreement'* made between Autonomy and MicroLink on 20 November 2003 ("the Q4 2003 MicroLink VAR agreement"). Under the terms of that agreement:

    (1) MicroLink was obliged to pay Autonomy irrespective of whether it closed a deal with an end-user. Clause 5.5 provided:

    > *"Government Reseller shall not be relieved of its obligations to pay fees owed to Autonomy hereunder by the nonpayment of such fees by an End-User."*

    (2) Clause 5.1 provided that once Autonomy's products on a purchase order had been shipped (which happened electronically), MicroLink could not cancel or amend the purchase order without prior written consent from Autonomy. Clause 5.1 also provided that the agreement superseded any pre-printed terms and conditions that could appear on any purchase order.

    (3) Clause 14.4 provided that no amendment to, change, waiver or discharge of any provision of the agreement was valid unless in writing and signed by an authorised representative of each party.

    (4) Clause 14.10 was an entire agreement clause which confirmed there were no other representations, understandings or agreements.

13. In aggregate, the total licence fees invoiced by Autonomy for the VT1 transactions amounted to $15,317,488 (all of which Autonomy recognised as revenue at the date of the transactions). It is not disputed that only $2,098,772 of this was ever paid by MicroLink to Autonomy; but it is alleged by the Claimants that even this payment was only generated as a result of a purchase by Autonomy from MicroLink of software produced by MicroLink known as Search Analysis Tool ("SAT") for $4,100,000.

14. Mr Egan provided a general review of Autonomy's transactions with MicroLink as follows:

    > "*In around 2008 and 2009, Autonomy did a series of what I called "at risk" VAR deals with Microlink.*[2] *They followed the pattern I have described in the section above headed "Value Added Resellers". In my discussions with Mr. Truitt I followed the guidance that Mr. Hussain gave me as described in paragraphs 28 and 29 above. In many instances, Microlink was not involved in the pursuit of the sale with the end-users*[3]*. In some situations, where the end-user deal could not be completed by the end of a particular quarter, Autonomy asked Microlink to submit a purchase order to Autonomy. The purchase order identified the software that we were attempting to license to the end-user*

[2] See footnote 283 in the main body of the judgment.
[3] And it was not involved in any of the impugned VAR transactions.

customer and stated that the software was to be licensed to Microlink for sublicense to the end-user. Autonomy would invoice Microlink for the software, deliver the identified software to Microlink, and recognize revenue on this paper transaction in the quarter that was ending.

I then continued to attempt to sell a license to use the same software to the true customer. On many occasions, either Autonomy or Microlink succeeded in making the sale to the end-user; on others, the end-user sale was delayed for a long period of time, but eventually was made. In yet other situations, no sale to the end-user was ever made. I believe that in one way or another, including, ultimately, Autonomy's purchase of Microlink, we made sure that Microlink never suffered a loss on these deals, in accordance with the understanding between Mr. Truitt and me in respect of these deals."

15. The basis on which the Claimants impugned the 11 VT1 sales can be summarised as follows:

(1) In each, Autonomy's sole purpose of resorting to a VAR was to enable it to recognise revenue in the quarter of the sale to the VAR notwithstanding delay or difficulties in closing a transaction with what Mr Egan described as its *"true customer"*, that is a prospective end-user.

(2) In none of the VT1 transactions was there any evidence of MicroLink making any effort to sell to the end-user: rather, the evidence available is that Autonomy continued its efforts to sell a licence for the same software to the *"true customer"*.

(3) In none of the VT1 transactions did MicroLink contract with an end-user. The end-user deals were between Autonomy and the end-user.

(4) Even though in various cases no end-user deal eventuated, there is no evidence that MicroLink was ever required to post a loss, and Mr Egan's unchallenged and uncontradicted evidence was that he believed that:

> *"in one way or another, including, ultimately, Autonomy's purchase of Microlink, we made sure that Microlink never suffered a loss on these deals, in accordance with the understanding between Mr Truitt and me in respect of these deals."*

(5) Furthermore, there was no evidence that the VT1 transactions were ever accounted for in MicroLink's accounts. The only money ever paid by MicroLink to Autonomy in respect of the 11 transactions was money that Autonomy had channelled to MicroLink for that purpose.

(6) I address in greater detail below (see paragraphs 25*ff*) the basis on which the Claimants contended that the SAT purchase and a further purchase of Autonomy / SharePoint Integration Suite for MOSS ("AIS") software (in Q3 2009) were contrived to fund MicroLink to enable it to appear to discharge its indebtedness to Autonomy, and that the purpose of Autonomy's subsequent acquisition in Q1 2010 of the entire issued share capital of MicroLink was to enable Autonomy to release MicroLink's very substantial remaining deficit in its deals with Autonomy on an intra-group basis.

16. Against this, the Defendants' case was based on the following:

(1) Both Mr Egan and Mr David Truitt were clear that they understood MicroLink to be *"on risk"*; they meant this in the sense that the legal liability to pay was clear, unequivocal and unconditional, as is apparent from the account of their evidence already given in my overview above.

(2) When cross-examined in the US criminal proceedings, Mr David Truitt confirmed (albeit in the context of DiscoverTech transactions) that the VAR acquired the licensed software, and full ownership and control of it, which it would be left with and have to realise value from if an end-user contract did not eventuate:

> *"Q. And is what you meant is that once you made the agreement, you, be it Discover Tech, MicroTech, whoever made the agreement, owned the software? It was your software?*
>
> *A. Yes.*
>
> *Q. And was -- if it didn't close, it's still your software and you owed money; right?*
>
> *A. Yes.*
>
> *Q. If you sold it to the end-user, the terms were already set. It was there in the agreement; right?*
>
> *A. Correct.*
>
> *Q. So you had control of the software, you owed the money, and you were fully the owner; right?*
>
> *A. Yes."*

(3) In the same proceedings, Mr David Truitt also said that there was never an understanding that he could cancel the deals with no further obligation if the end-user did not purchase the software.

(4) In addition to the plain contractual terms, MicroLink signed the usual confirmation letter acknowledging the indebtedness and confirming that:

> *"…there are no side letters or other agreements in respect of the subject matter of this request…"*

(5) According to Deloitte's working notes, and contrary to the Claimants' case, at least one of the impugned transactions was originated not by Autonomy but by the VAR: thus, Mr Egan had given information to Deloitte in respect of one of the impugned deals (for end-user US Federal Government[4] in Q2 2009). This was a deal for the National Security Agency ("NSA"). Mr Egan had informed Deloitte as follows:

> *"We discussed this deal with Stouffer Egan (CEO of Autonomy US) and noted that MicroLink won this contract with the NSA off the back of another project with a major US*

[4] National Security Agency.

> *intelligence agency. The NSA are upgrading their entire national network with IDOL search. In the past, it used to take about 1 day to search the entire network to gather the information they required. MicroLink has the relevant security clearance to go and integrate this software into the NSA network. It will be a year- long project for MicroLink to do this, and they charge the NSA based on a day rate. None of the professional services work comes back to Autonomy, it is only the perpetual licence that they contribute."*

(6) Deloitte's conclusion as regards this transaction was that the risk and rewards of ownership had passed to MicroLink, and that the other revenue recognition criteria were satisfied. In cross-examination, Mr Egan was asked whether he had any reason to disagree with Deloitte's conclusion; he said he did not, though he did also make clear that this was really because he did not *"have much memory of this deal"*.

(7) Dr Lynch accepted that Mr Stephan's evidence that MicroLink had made no provision for any liability to Autonomy in its accounts was *"the literal truth"*, but suggested (contrary to the Claimants' contention) that this did not reveal anything untoward. According to Dr Lynch he had discovered no more than that *"MicroLink did its accounting net, not gross, so it accounts on a basis where it doesn't take the licences through its books. That doesn't mean to say that in any way those liabilities are not there."*

(8) As to Mr Stephan's failure to clarify this, Dr Lynch emphasised that Mr Stephan had not attended trial and he characterised his evidence admitted under a hearsay notice as not only vague and untested (since the Defendants had no opportunity to cross-examine him), but also as given under significant pressure from the US DoJ. According to Dr Lynch, Mr Stephan was intercepted by them when on holiday in the USA and told that he would be prosecuted if he did not cooperate. Dr Lynch submitted that no reliance should be placed on the evidence thus procured (though I note that Dr Lynch himself relied on other parts of Mr Stephan's testimony in the context of the hardware allegations in the US criminal trial, where he said that he saw nothing wrong in a software company selling hardware *"to bring in revenue, to meet a target"* as it was put to him in his cross-examination).

17. As to these arguments:

(1) The Defendants' reliance on the contractual terms and the audit confirmation letters as confirming contractual indebtedness and legal control is a reflection of their main general point, which they maintained in respect of all the VAR claims, that even if the contractual position is not conclusive, it is of preponderant weight. I have concluded, however, that whether the purchase price should be regarded as recognised revenue for the purposes of the seller's accounts depends on the real economic substance of the transaction; that the substance of the transaction is to be determined according to the true intentions of the parties, as opposed to their strict legal rights and obligations, and according to the economic intent and substance of the transaction as thus revealed.

(2) The Defendants never satisfactorily addressed any of the matters referred to in paragraph 15 above.

(3) I was not persuaded by Mr David Truitt's evidence, admitted as hearsay, that there was never an understanding that he could cancel the deals with no further obligation if the end-user did not purchase the software. His evidence in this regard was given to try to overcome contemporaneous documentary evidence in the form of an email headed *"Cancellation of VAR agreements"* sent by him to Mr Joel Scott and dated 23 September 2011. That email, though it in fact refers to DiscoverTech transactions[5], provides a revealing insight which certainly does not assist the Defendants' case:

> *"Hello Mr. Scott, I am writing to formally request that VAR agreements signed on June 30th, 2011 between Discover Technologies and Autonomy, regarding Abbott Laboratories and Dell/Hyatt be cancelled. Per my discussions with Stouffer Egan, <u>under the condition that the end customer did not ultimately license the proposed Autonomy software, the agreements would be cancelled with no further obligation on the part of Discover Technologies</u>. Thank you for your attention and prompt response."* [Emphasis as supplied by the Claimants]

(4) Indeed, it seems to me that this rather let the proverbial cat out of the bag, requiring the explanation offered by Mr David Truitt that it was a mistake. Mr Scott's reply on 26 September 2011 corrected the "mistake" but not the actual economic result of DiscoverTech being *"let off the hook"* by the 'liability' being erased:

> "*Having checked internally and spoken with Stouffer, I think you misunderstood; however, given that you haven't closed the deals and there is no prospect of us getting paid, we are prepared to write these off."*[6]

(5) The Claimants' closing submissions did not address Dr Lynch's main point in relation to Mr Stephan's evidence that his inspection of MicroLink's accounts, after Autonomy's acquisition of MicroLink, when Autonomy's finance team were provided with MicroLink's books and accounting records, showed that the VT1 transactions were never accounted for in MicroLink's accounts, which was that MicroLink accounted on a net rather than gross basis. I was not shown accounts which would have (presumably) revealed the basis of MicroLink's accounting. In the circumstances, I do not feel able to make a finding on this intriguing point. However, it remained the case that notwithstanding the shortfall between the amounts charged by Autonomy and the payments apparently generated by MicroLink, there was no accounting evidence which

[5] Mr MacGregor, who referred to Mr David Truitt's denial of any understanding that if an end-user deal did not occur, the deals would be cancelled, suggested that this was referrable to MicroLink transactions just as much as DiscoverTech transactions because Mr Truitt referred to *"deals going back to 2006"* (when DiscoverTech did not exist).

[6] The upshot was that on 29 December 2011, Autonomy Inc issued DiscoverTech with credit notes covering the entire ostensible indebtedness. The Claimants submitted that *"There could hardly be a clearer indication that these transactions lacked economic substance in the first place."*

reflected the fact that MicroLink had suffered a loss. (Dr Lynch told me in cross-examination on Day 50 that he suspected that there must be some such evidence but none was ever identified.) Further, I would accept Mr Stephan's evidence in the US criminal proceedings of his own impression, which seems to me to be consistent with the other oral evidence, that:

> *"From my – what I saw at MicroLink, I was concerned that the modus operandi of all these resellers, that the head of the company would sign whatever we wanted them to sign for the auditors, but they had no intention of paying."*

(6) In all the circumstances I accept the Claimants' arguments that the intention of the parties was in truth that (a) MicroLink would never be required to pay, that any legal obligation to do so would be cancelled, forgiven, or somehow funded by some other apparently but not actually separate transaction with Autonomy to put money in the hands of MicroLink which would then be 'paid' to Autonomy; and (b) Autonomy retained managerial involvement and effective control in the sense that only Autonomy would negotiate its sale, and any end-user contract which eventuated would be a sale by Autonomy to the end-user. In Mr Egan's words, the *"true customer"* would throughout be the end-user, and it was only from the *"true customer"* that Autonomy had any real expectation of receiving revenue at the end of the day.

(7) That undermines the accounting treatment of VT1. Revenue recognition in respect of the VAR sale was wrong. That is so notwithstanding the approval of that accounting by Deloitte and the Audit Committee. Their view could only have been based on what they saw (and in particular, the signed documentation). Deloitte were not, of course, told of what I have held to have been the true intentions and expectations of the parties; and the Audit Committee were substantially reliant on Deloitte's reports. Whether or not Deloitte or the Audit Committee should have detected signs of the untoward is beside the point in a claim to which they are not a party. In my judgment, on this simple basis, the Defendants' reliance on the approval of Deloitte and the Audit Committee for the VT1 transactions must fail.[7]

Did the Defendants know that the MicroLink transactions were improperly accounted for?

18. The Claimants did not rely on any evidence specific or particular to the VT1 transactions themselves in respect of their allegation that the Defendants knew that their accounting treatment was improper. As the Defendants pointed out, neither the RRAPoC nor the Claimants' Further Information of 30 January 2018 identified any material facts specific to VT1 in that regard. The basis of the Claimants' claim that both Defendants had "guilty knowledge" was the evidence given, especially by Mr Egan, of the way the *"at-risk*

[7] Deloitte's working papers for the VT1 transactions, so far as made available, demonstrate a careful and methodical, but essentially process-driven, approach based on the apparent contractual arrangements. The criteria stipulated by IAS 18.14 were ticked off against the contractual provisions and buttressed by the audit confirmation letters: but the economic reality was not sceptically examined. (As Mr MacGregor noted, Deloitte's working papers for 7 of the 11 VT1 transactions were available but not for the remaining four.)

deals" were implemented. The Claimants also relied on the Defendants' knowledge of the subsequent transactions to put MicroLink in funds (and ultimately Autonomy's acquisition of MicroLink) to ensure that it was not left *"holding the bag"*: see below.

19. Dr Lynch, in particular, denied any involvement in or knowledge of the MicroLink transactions comprising VT1. His written closing made the point that there was no cross-examination of him with regard to his involvement and/or knowledge of those transactions. This culminated in the submission that the Claimants had *"not even put any case to Dr Lynch"*.

20. However, the Claimants did cross-examine Dr Lynch about the subsequent purchases made by Autonomy which put MicroLink in funds to pay amounts outstanding under VT1, and also about MicroLink's subsequent acquisition by Autonomy. Further, as recorded in paragraph 3 above, I have accepted the Claimants' position that they did not need to prove knowledge of every individual transaction and that proof that Dr Lynch knew of and authorised the practice of calling upon a 'friendly' VAR as and when required to generate revenue to cover a shortfall sufficed. If and insofar as Dr Lynch sought the dismissal of this part of the claim against him on the basis of the case not having been put, I do not think that was warranted: there is no proper basis for dismissing the claim on that ground.

21. Notwithstanding the absence of transaction-specific evidence of knowledge in relation to VT1, I have concluded (as always, on the balance of probabilities) that both Defendants knew that its accounting treatment was improper.

22. I have been especially influenced in reaching that conclusion by:

    (1) The fact that the VT1 transactions were the first of the *"at-risk deals"* marking the commencement of what became, in effect, a programme of vital importance to the Defendants and key to Autonomy meeting its revenue and earnings per share targets in every quarter. Having concluded that Mr Hussain conceived and directed the strategy and that Dr Lynch (though not usually involved in implementation) presided over and encouraged it, it seems to me that both would have known and kept themselves well informed about the fact and progress of the first of the impugned VAR transactions.

    (2) The amounts involved in the licence sales were such as would undoubtedly have come to the attention of Mr Hussain, who would have closely monitored their implementation and progress, and would in all likelihood have kept Dr Lynch informed in any event, even if he had not been involved in the overall strategy. The total fees invoiced by Autonomy for the 11 transactions comprised in VT1 amounted to $15,317,488, of which only $2,098,772 was ever paid by MicroLink to Autonomy, and even then, the payment was funded by a reciprocal purchase by Autonomy.

    (3) In those circumstances, it is more likely than not that Mr Hussain would also have known about, and kept himself well informed about, Mr Egan's continuing attempts to conclude a deal with the end-user, and that Mr Hussain would have reported those attempts to Dr Lynch.

(4) More generally, it seems to me clear that Mr Hussain was well aware of the transactions and that they were contrived; Mr Hussain habitually reported to Dr Lynch on any matters of significance, value or importance; and I cannot accept that Mr Hussain was on a frolic of his own. In general terms it seems to me more likely than not that Dr Lynch knew what Mr Hussain knew.

(5) Both Defendants were involved in the subsequent purchases from MicroLink by Autonomy, and I have concluded (for reasons I have set out below) that each was aware that their true or driving purpose was to put MicroLink in funds to pay down some of its debt to Autonomy to fulfil the assurances given to MicroLink that it would not be left *"holding the bag"*.

23. It is to those purchases and then the acquisition by Autonomy of MicroLink that I next turn.

Autonomy's purchases from MicroLink

24. As mentioned above, the only money ever paid by MicroLink in respect of the transactions comprising VT1 was money that Autonomy had channelled to MicroLink for that purpose. The way Autonomy did this was to contrive purchases of software though it had no need or use for it, and in the end, to acquire MicroLink itself (which eliminated the debt on consolidation).

The SAT purchase

25. In Q1 2009, Autonomy purchased a one-year licence to use MicroLink's SAT software (defined in paragraph 13). The agreed purchase price for the one-year licence was $4.1 million. Mr Kalbag explained in his witness statement that his understanding was that the SAT was:

> *"a tool to monitor and visualise statistics such as search performance and search behaviour of users to allow administrators to better tune the search results."*

26. The Claimants described the SAT purchase in considerable detail; but I think the purchase and the basis on which the Claimants portrayed it as contrived to fund MicroLink rather, or more, than to benefit Autonomy can briefly be summarised as follows:

(1) At the time of the purchase, Autonomy already had a comparable product called Statistical Server ("Stat Server"). This was a feature of IDOL which Mr Kalbag believed was included for free as part of the IDOL package rather than being sold to customers as a separate product. According to Mr Kalbag, the SAT and Stat Server had very similar functionality and could achieve predominantly the same results.

(2) It was Autonomy's stated policy to develop and grow its own software products rather than buying in, if at all possible: it would only usually buy in if the functionality of its own product proved deficient in some material way or its performance proved unsatisfactory. The purchase of a licence was an aberration from that policy; and yet there was no evidence to suggest that prompting the

purchase was any perception of deficiency in Stat Server or some specific need to buy in a product which seems so similar to one of Autonomy's own.

(3) There is no evidence that before the SAT purchase any technical evaluation was made by anyone within Autonomy of the SAT software. The purchase was driven by Mr Hussain, Mr Kanter and Mr Egan, none of whom could or would have been involved in such an evaluation. The only technical input was comprised of an urgent review by Dr Menell three days before completion of the purchase, and two days after Mr Hussain had asked for his approval urgently. Dr Menell's report was *"ok – tech pieces look fine"*. No document has been produced recording any prior interest in buying SAT before the purchase was driven forward.

(4) No-one on the technical side, other than, at the last minute, Dr Menell, was consulted or involved. Dr Blanchflower would have expected to be so; but his unchallenged evidence was that he was *"not aware of this transaction at the time"*. He added that had there been a perceived need to extend the functionality of Autonomy's own product (Stat Server) to include a user interface like the SAT's, that could easily have been done, but no one had ever suggested it was needed.

(5) The purchase was ascribed considerable urgency within Autonomy. No reason was suggested in evidence. Dr Lynch speculated that perhaps the product was needed urgently for a customer: but he accepted this was no more than speculation.

(6) The rationale developed thereafter, with the assistance of Dr Menell, was that (according to Deloitte's working note after discussions with him) the SAT allowed Autonomy *"access to the portals to surface IDOL functions directly into a federally certified SharePoint Environment. This creates IDOL function capabilities in SP Portals within the Fed."* SharePoint was presented as *"a product which is actively used by US Federal Government departments"*.

(7) However, according to the Claimants, the reason thus recorded in Deloitte's working paper would not have been a good reason for purchasing the SAT, because SAT had nothing to do with SharePoint.

(8) Dr Lynch's attempt to explain this in cross-examination tended to confirm the impression that those explaining the matter to Deloitte (and, in particular, Dr Menell) did not really know what the rationale was, and reinforced the conclusion that no one within Autonomy conducted any technical evaluation of the SAT in advance of the purchase. Dr Lynch told me that he thought there had been *"confusion between two different products"* namely SAT and AIS, and explained that whilst SAT was a *"tool that analyses the searches done on IDOL…AIS is a web part for SharePoint"*. He added that he did not know how the confusion had happened. But the metadata showed that Deloitte's working paper was dated 29 April 2009, some four months prior to Autonomy's purchase of AIS on 2 September 2009. The Claimants suggested that it was *"hard to see how on 29 April 2009 Deloitte could have confused SAT with a different product that Autonomy only decided to buy four months later"* and that the inaccurate description was likely to have come from Dr Menell. They supported the suggestion by pointing out that when later on, in October 2009, Deloitte

prepared a further interim review summary memorandum to consider both the purchase of the SAT and AIS, they recorded that Dr Menell had *"noted that both items of software related to the Microsoft Sharepoint software"*. The Claimants summarised the position as being that:

> *"there is no contemporaneous document which records a commercial rationale for the purchase of SAT which reflects SAT's true functionality."*

(9) There is no evidence either of anyone within Autonomy making any use of the SAT after the SAT purchase. Dr Lynch said that Dr Blanchflower's evidence that it was never used either internally within Autonomy or by customers was wrong, but when pressed for examples could provide none. No witnesses were called by Dr Lynch to assert that they had used SAT at any time or sold it to customers.

(10) The payment flows of the purchase moneys show, and Mr David Truitt in his deposition in the MicroTech litigation confirmed, that MicroLink did indeed immediately use all the money it received from the SAT purchase to pay down some of its debt to Autonomy. At that time, MicroLink had no available resources of its own from which to do so.

27. Against this, the Defendants submitted that the transaction had in fact a sound commercial rationale: the SAT was useful software developed by MicroLink on the basis of their specialist expertise in working with customers on Autonomy products. They relied on the following:

(1) SAT was said to enable *"clients to capture and analyse metrics regarding their utilisation of IDOL server and IDOL-based applications."*

(2) Dr Blanchflower accepted in cross-examination that the SAT had more differences from Autonomy's own Stat Server software than he had identified in his witness statement. He had suggested that the only real difference was that Stat Server did not have an interface to display results diagrammatically, and that this did not justify paying anywhere close to $4.1 million. His evidence was based on a review of the SAT licence and a proposal document by MicroLink *"to determine what it was trying to do"*: he had not analysed the actual SAT software, because he did not have a copy of it.

(3) The SAT had core features and additional and useful capabilities and functionality of real utility which IDOL's Stat Server did not have, as email exchanges in August 2009 revealed had been noted within Autonomy.

(4) Further, and as Dr Lynch emphasised particularly in cross-examination, SAT could export to systems like 'Cognos' providing business intelligence reporting capabilities, which again Stat Server could not, as then configured.

(5) Although Dr Blanchflower talked of writing additional functionality within an hour, that was likely to have been greatly exaggerated.

(6) Even where there was an overlap in functionality between Stat Server and SAT, there was evidence that the Stat Server was poorly regarded within Autonomy.

(7) Further, the Defendants submitted that SAT was acquired at fair value, and indeed that the Claimants did not suggest otherwise at trial.

28. The Defendants did not, however, have evidence to contradict the other two points relied on by the Claimants in relation to the SAT: they acknowledged that the evidence of the use after its purchase was *"not clear"*, and they did not dispute the flow of funds, instead submitting that it was irrelevant if the transaction (which was endorsed by Autonomy's board of directors) was a sound one for fair value.

29. In my judgment, the preponderance of the evidence is such as to cast real doubt on the reasons relied on by the Defendants for the purchase of the SAT at such a price. As so often, the Defendants could muster ostensibly coherent points of justification (as, for example, for the 'pure' hardware sales); but the weight of evidence against those points having really driven the decision is considerable and, in my assessment, clearly preponderant. I cannot accept that the Claimants did not suggest that the price paid was excessive: that was the inevitable consequence of their arguments, and Dr Blanchflower expressly stated that the SAT was not worth nearly as much.

The AIS purchase

30. The second transaction which the Claimants relied on in this context was Autonomy's purchase in Q3 2009 of resale and distribution rights in respect of AIS software from MicroLink at a cost of $5.2 million.

31. MicroLink's presentational material explained that AIS, which had two principal components (AIS webparts and AIS Fetch) had been developed by MicroLink, leveraging its long experience of both Autonomy's products and Microsoft SharePoint, to enable its customers to enhance their use of Autonomy's products by allowing them to utilise IDOL 7 and Microsoft SharePoint in a unified platform. It was designed to have encryption levels up to US federal standards so that it could successfully be deployed to the US Government and Fortune 500 companies.

32. The Claimants made very similar points in relation to the AIS purchase as in relation to the SAT purchase, contending that:

(1) No proper evaluation was undertaken by Autonomy prior to purchase;

(2) Autonomy already had its own SharePoint connector prior to the purchase;

(3) The creation of such a connector is not particularly complex, and Mr Greenwood (who was Autonomy's Head of Connectors) was not challenged on his evidence that it would probably not have taken more than 3-4 weeks of a developer's time; but Mr Greenwood was not consulted or even told about the AIS purchase;

(4) There was sparse, if any, evidence of its use within Autonomy after its purchase; and

(5) The payment flows between Autonomy and MicroLink, showing the moneys received by MicroLink being paid on to Autonomy almost at the same time, constituted further strong evidence that the true reason for the purchase was to

put MicroLink in funds with which to pay its debt in respect of its VAR transactions with Autonomy.

33. Likewise, the Defendants rejected the Claimants' contentions in relation to AIS on much the same basis as they had sought to reject the SAT allegations, contending that:

(1) Contrary to the Claimants' case (and evidence on their behalf from Mr Greenwood) there had been a proper evaluation including by Mr Lucini, which had also satisfied Deloitte which reviewed it with the assistance of its in-house technical expert, Mr Ben Johnstone, who consulted both Mr Lucini and Dr Menell;

(2) The AIS product did not overlap with Autonomy's connector product. The Claimants' suggestion to the contrary was based on a narrow review of only one element of the product, known as the AIS Fetch (as the connector was called), whereas the product's other element, the "webparts" constituted the real *"heart of the product"* which was both different and of great utility to customers (offering, for example, enhanced search and encryption levels), as illustrated by its deployment in Government and Fortune 500 companies (including the US Joint Forces Command and NASA) for use with their IDOL and SharePoint products;

(3) There was no suggestion that the purchase was not at fair value: and Deloitte had been satisfied in that regard also.

34. Again, as in relation to the SAT, the evidence of subsequent use within Autonomy was sparse; but the Defendants pointed to the fact that there is no reason to suppose that the product was not used, given the evidence of its use in the market, and also to the fact that although the Claimants had originally pleaded that Autonomy never used the product, they had amended to delete and abandon that plea. As to the money flows, the Defendants made the same point as in the context of SAT: that if the transaction was a commercially fair one, what was done with the proceeds was irrelevant.

35. I consider the assessment whether the AIS purchase was predominantly an expedient to rescue MicroLink from the *"hook"* to be more finely balanced than the similar question relating to the SAT. On balance, however, even if there was a coincidence of benefit to Autonomy and an imperative to release MicroLink, the episode is consistent with, and mildly supportive of, it having always been the intention and shared understanding that MicroLink should not be left *"on the hook"*.

Acquisition of MicroLink by Autonomy

36. The third of the transactions relied on by the Claimants as further evidence of the side agreement or understanding they alleged in the context of VT1 was the MicroLink acquisition, which closed in January 2010 for $55,000,000.

37. The Defendants contended that the MicroLink acquisition was made for solid and sound commercial reasons: being to ensure that Autonomy could continue sales to the US Federal Government after the US regulatory clearance which it had through a US subsidiary called Verity Inc expired. This happened when the US Federal Government changed the rules and prohibited foreign companies (such as Autonomy) conducting such

business through a US subsidiary unless that subsidiary was ring-fenced or segregated in management terms from its foreign parent. Dr Lynch gave the following explanation in his witness statement:

> *"285. MicroLink was a longstanding partner of Autonomy based in the US. It had federal security clearances and thus could sell to and work with the US Federal Government, like the National Reconnaissance Office, which typically only purchased through companies with security clearances. MicroLink were very familiar with Autonomy technology and its marketability in the federal space. They had been a partner of Autonomy's since 2004.*
>
> *286. As a UK company, it was difficult for Autonomy to get federal security clearance. Prior to the MicroLink acquisition, as a workaround solution, Autonomy's US federal business was run by Verity, a US subsidiary that did have these clearances. In Autumn 2009, the US Federal Government changed the rules on how foreign companies could conduct US federal business. Using a US subsidiary was no longer sufficient; the subsidiary had to be ring-fenced from the parent. This was not practical with Verity because the majority of its business was commercial, and its commercial and federal businesses were integrated. Autonomy therefore needed to acquire a company that would be solely federal, that could be ring-fenced from the commercial business. MicroLink was a good choice for Autonomy- it had contacts in the federal space, had the requisite security clearances and was already a strong Autonomy partner. We thought the acquisition would keep our federal business alive and strengthen it. Autonomy approached Mr Dave Truitt, then CEO of MicroLink, about the idea. He was receptive and saw that it was a good business opportunity.*
>
> *287. The negotiations were led by Messrs Kanter and Hussain. I agreed with the strategy to acquire MicroLink and was kept abreast of developments by other members of management. Autonomy valued MicroLink at $55M and that was the price ultimately agreed. It was also agreed that Mr Dave Truitt could spin out certain business from MicroLink to form DiscoverTech. Mr Dave Truitt negotiated a deal whereby DiscoverTech would own the IP to certain MicroLink products that were in their infancy, including DiscoverEngine, which DiscoverTech could then further develop and sell.*
>
> *288. It was further agreed that Mr Dave Truitt would stay at MicroLink for one year after the acquisition, to facilitate the transition, and then be allowed to move to DiscoverTech full-time as the CEO. I understand HP has suggested that something nefarious can be inferred from the fact that Mr Dave Truitt was involved with a number of the resellers implicated in their claims. As explained, Mr Dave Truitt was the prior CEO of MicroLink who then became the CEO of DiscoverTech, a business he spun out of MicroLink. I now know that he was also a silent investor in MicroTech, where his brother Mr Steve Truitt worked, but had no role in the management of the MicroTech business. I do not recall being aware of this at the time. However, from my perspective, nothing improper can be inferred from the above and Mr Dave Truitt's role in both MicroLink and DiscoverTech did not raise any concerns for me at the time.*

> *289. From my perspective, $55M was a fair price for the acquisition of MicroLink. The federal business was a reasonable slice of Autonomy's business but we felt we were underrepresented. In acquiring MicroLink we acquired the necessary clearances and cleared personnel to be able to operate in the US federal sphere. Security clearances can take years to come through, making MicroLink much more valuable than an ordinary services company. It turned out to be a very successful acquisition and led to considerable business for Autonomy.*
>
> *290. Autonomy's Board of Directors approved the acquisition after reviewing information regarding the strategy behind the deal and the valuation. I also understand that Deloitte handled the acquisition accounting and assessed the value of MicroLink, how it should be valued on our books and what to do with the inter-company debt. To my knowledge, Deloitte did not raise any concerns about our accounting for the acquisition."*

38. In those circumstances, the Defendants contended that Autonomy had limited options, which Dr Lynch presented as having been as follows:

    (1) It could seek to restore Verity's clearance by imposing the strict segregation required. However, this was considered to be commercially unrealistic given the substantial size of Verity and the level of integration of Verity's business, products and staff with the wider group.

    (2) It could exit the federally cleared business, transacting only such deals as it could achieve with cleared resellers who dealt with those federal customers. This would be to cede a substantial potential business stream to middlemen, leaving Autonomy with far less control of the business and forced to pay margin to the reseller on any sale. Dr Lynch explained (in fact, in connection with the ATIC transaction) that Autonomy had striven over the years to get itself out of the position of being beholden to the margins extracted by large resellers such as Lockheed Martin. The prospect of operating in this arena without a federally cleared subsidiary was not attractive.

    (3) Autonomy could alternatively acquire a federally cleared reseller which was able to maintain as a sufficiently segregated entity that it complied with the clearance requirements, but without impeding the integration of important members of the group (as would happen if Autonomy attempted to restore Verity's clearance). This, according to Dr Lynch, was precisely what the MicroLink acquisition offered.

39. The evidence of full board of directors' approval of the acquisition after careful explanation was clear. Deloitte, which was fully aware of MicroLink's indebtedness, also prepared a detailed analysis paper, addressing primarily whether after acquisition MicroLink would have to be treated as a separate segment for accounting purposes but dealing also with the structure and rationale of the acquisition including the prior spin-off of the DiscoverPoint business which formed a prong of the Claimants' attack as described below.

40. The Defendants pointed out that the Claimants' own witnesses, and in particular Mr Egan and Mr Kalbag, supported the rationale and the decision. Mr Egan said he was *"100% for this, absolutely, yes"* though he also made clear that his memory of the transaction was very limited. He added that his belief at the time was that it *"was a nice benefit of it"* that the debt *"would be effectively forgiven because MicroLink would be a part of Autonomy"*. When cross-examined on the broader statement in his witness statement that he believed that to have been also the perspective of Dr Lynch, Mr Hussain and Mr Kanter, he accepted that he did not have evidence of their belief or outlook: *"It was just a belief that I had…"*

41. Against this, the Claimants' case was that it was that benefit which was an operative, and probably the primary, rationale of the acquisition. They accepted that the rationale offered by the Defendants was also part of it, but they asserted that it was not the whole or even the largest part of it. They relied in summary on the following matters:

(1) By September 2009, MicroLink owed Autonomy some $22.7 million, which would cause problems also for any future deals when Deloitte assessed collectability, as Dr Lynch accepted in cross-examination he knew.

(2) Although Dr Lynch added that it *"wasn't due…"*[8] and there was an email from Mr Hussain supporting that, the Claimants suggested that the effort to downplay the position was *"carefully-crafted"* and that there was real concern about the debt and MicroLink's deteriorated position, including the concern that Deloitte would be against further sales to MicroLink on collectability grounds.

(3) Mr Egan's evidence in his witness statement was that from his perspective and (again as he perceived it) also that of both Defendants and Mr Kanter forgiveness of debt which it would enable was *"one reason for Autonomy to purchase Microlink"*.

(4) Even though there was a likely benefit to Autonomy in acquiring a federally-cleared reseller such as MicroLink, that was not an imperative. The acquisition was not necessary in order for Autonomy to continue selling to US government customers: they pointed out that Autonomy could instead have sold through federally-cleared resellers, and they cited in that context an email to Dr Lynch dated 14 September 2009 where Mr Kanter had said just that.

(5) The process (between Mr Hussain and Mr David Truitt) which then started to negotiate terms was far from arms' length. Various proposals were discussed; but a hallmark of each was the focus of both parties on ways of structuring the deal so that (a) Mr Truitt would pay for certain proprietary products/rights from MicroLink to enable him to carry on business using them in a new vehicle of his own (which was the basis of DiscoverTech) (b) the acquisition price for MicroLink would be calibrated to cover the purchases and (c) in that way Autonomy would be able to recognise revenue from the sales of assets taken out.

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[8] An email dated 14 September 2009 from Mr Hussain to Mr Egan cc Dr Lynch stated that the indebtedness was not such a concern because *"June 09 deals not owed is $10.9m leaving $11.8m; $9.6m is owed from the EDD deal in December 08 which had long payment terms; so as long as we receive about $1.5m we should be up to date"*.

(6) MicroLink's financial position by December 2009 was difficult (if its indebtedness to Autonomy was real). It had paper assets of just under $24.5 million; only some $362,069.17 of these assets were in cash, and by far the largest asset, in the sum of $13,711,426.50, which was classified as *"Inventory Asset"*, was stated to be *"Licences purchased from Autonomy not yet resold"*. Its total liabilities were stated at $26.9 million, of which the vast majority, $23,961,729.22, consisted of *"Accounts Payable"* explained as being sums *"Due to Autonomy"*. There was little or no prospect of MicroLink paying Autonomy out of its own resources. If some or all of the Autonomy software held in in MicroLink's inventory could not be onsold then MicroLink's liabilities would very substantially exceed its assets.

(7) In the event, MicroLink's outstanding indebtedness was duly forgiven or written off after the acquisition in October 2011.

42. The Claimants added to this that the purchase price of the acquisition was, in effect, enhanced by $10,000,000 so that, in return, Mr David Truitt's new company, DiscoverTech, would have the funds to purchase a software licence of the same sum from Autonomy so that Autonomy could recognise $10,000,000 of revenue in respect of the impugned VAR transaction between Autonomy and MicroTech for end-user DiscoverTech referred to as VT5. I shall deal later with that last point relating to VT5: see paragraphs *255ff*.

43. In concluding my assessment of the issue as to the rationale of the MicroLink acquisition it is fair to acknowledge the following points of importance:

(1) There was considerable dispute as to the exact net position in MicroLink given that (a) Dr Lynch was correct in saying that not all the indebtedness to Autonomy was yet due and (b) some of the *"inventory"* of Autonomy software licences that MicroLink had not yet onsold was capable of being realised, though it does appear that its value was written down shortly after the acquisition by $10.66 million;

(2) Dr Lynch was adamant in cross-examination that *"the company was not struggling, it was very successful and growing rapidly and had blue chip customers"*;

(3) Autonomy's board of directors unanimously approved the acquisition on the express basis that it was *"critical to accelerate the adoption of Autonomy solutions in the Federal space, where our growth prospects are limited by the lack of direct selling ability due to security requirements"*;

(4) The Claimants acknowledged that this was an important factor in the decision to acquire MicroLink;

(5) Mr Egan's evidence was that he did think at the time that the acquisition proved successful and there was evidence suggesting, for example, that some six or seven months after the acquisition, MicroLink was awarded a very large contract (the largest, it was said, in its history) by a major US Federal agency.

44. Nevertheless, the coincidence and urgency of the timing, the nature of the negotiations between Mr Hussain and Mr David Truitt, and the basic fact that the effect was to enable

MicroLink's indebtedness to Autonomy to be dissolved, have persuaded me that the latter was a substantial part of the rationale for the acquisition, and that it is supportive of the Claimants' case that one way or another, Autonomy did what was necessary to ensure that its 'friendly' VARs were not left *"on the hook"*.

Summary of conclusions in respect of VT1 and associated purchases

45. In summary, the three purchase transactions addressed above reinforce my conclusion that the VAR transactions comprising VT1 were not true sales, and the obligations assumed in law were never intended or expected to be enforced.

46. I accept the Claimants' case in relation to the VT1 transactions that:

(1) Notwithstanding the legal enforceability of the provisions of the contracts governing them, in reality it was never intended or expected that the VAR would have any role in respect of the negotiation and sale to an end-user of the software licenced to it: that was intended to be and in the event was exclusively a matter for Autonomy. The VAR was in terms of what was actually intended or expected of it, no more than a placeholder.

(2) It was not expected or intended that the VAR should ever be required to pay, or in fact pay, any sums due under the VAR sale out of its own resources. The three purchase transactions provide confirmatory evidence of this.

(3) The Defendants knew this; and that recognition of revenue from the VAR sale was improper.

The Capax Discovery VAR deals in Part I: VT2, VT3, VT4 and VT10

47. I turn to address the following impugned VAR transactions with Capax Discovery: VT2 (for proposed end-user TXU), VT3 (for proposed end-user Kraft), VT4 (for proposed end-user Eli Lilly) and VT10 (for proposed end-user the UK FSA). I have selected those four transactions with Capax Discovery as providing examples from the formative stages of Autonomy's engagement with Capax Discovery and thereafter a reasonable chronological spread, and also because they appear to me to illustrate particularly clearly, but representatively, certain important aspects of that engagement.

Various antecedent points

48. Before turning to the specific transactions, however, it is convenient to record certain details of the antecedents to the VAR sales to Capax Discovery, which provide some insight into the pattern of those sales, and a few key points relevant or common to all the impugned VAR sales to Capax Discovery.

A relevant antecedent arrangement?

49. The first of these key points relates to the background to Autonomy's use of Capax Discovery as a VAR. Autonomy's first engagement with Capax Discovery was not a VAR sale. It was a licence and distribution agreement made between Autonomy Inc and Capax Discovery on 31 March 2009 (the last day of Q1 2009), signed by Mr Egan on behalf of Autonomy Inc and Mr Baiocco on behalf of Capax Discovery ("the first Capax

Discovery/EDD sale"), which forms part of the Capax reciprocal transaction, which I address in detail in the chapter of this judgment that deals with the "Reciprocal" transactions. The term of the agreement was five years from the effective date of 31 March 2009.

50. The licence and distribution agreement provided for Autonomy Inc to grant Capax Discovery a licence to use software whilst providing services or installing Autonomy software (which included Autonomy's e-Discovery software, Introspect and EAS) for the benefit of Autonomy customers. The consideration for the licence grant was (i) an initial licence fee of $7,500,000, (ii) a royalty fee equal to 20% of the net revenues earned by Capax Discovery, which was payable once Capax Discovery's net revenues from distributing Autonomy's services and/or providing its own Software-as-a-Service ("SaaS") offering exceeded $25 million, and (iii) an annual support fee equal to 5% of the licence fee, i.e. $375,000, the first two years of which was payable with the initial licence fee. The initial licence fee and the support fee for the first two years of support services, totalling $8,250,000, were payable in accordance with a schedule set out in the first Capax Discovery/EDD sale. The first instalment of $500,000 was due on 30 April 2009. There were then eight instalments of $968,750, which were due at three-month intervals thereafter until 31 March 2011. Autonomy recognised the $7,500,000 licence fee as revenue in Q1 2009.

51. The first Capax Discovery/EDD sale was clearly important to Autonomy's quarterly revenue targets, as the emails demonstrate. On 31 March 2009, Mr Robert Sass ("Mr Sass") sent Mr Hussain and Mr Egan (among others) an email marked with 'high importance' saying: "*CAPAX IS IN (SIGNED COPY IN HAND)*". A few hours later, Mr Hussain replied, copying Dr Lynch, saying "*Very well done to the both of you – I like $7.5m deals!*".

52. The problem was that, at the time, Capax Discovery was a newly-formed entity, established by Mr Baiocco to set up an e-Discovery business. It had no substantial assets, no revenue stream and no trading record, as documentary evidence makes clear Mr Hussain and Autonomy's finance department were well aware. According to the Claimants, this was no real impediment from the point of view of Mr Baiocco and Mr Egan because they had reached an agreement that Autonomy would channel sufficient funds to Capax Discovery to allow it to pay instalments due under the first Capax Discovery/EDD sale, and to provide what Mr Baiocco referred to as a *"champagne smacking"* profit. But it was a problem from the point of view of establishing a paper trail of financial information sufficient to justify a deal of such magnitude with such a fledgling counterparty.

53. When Mr Chamberlain outlined the financial information he would want to see from the new entity, including "*at least the first years['] worth of payments as funding*" and a budget to demonstrate that it was expected to be a profitable business that would be able to generate cash to meet the longer term obligations, on 31 March 2009, Mr Baiocco provided Mr Sass with financial statements for Capax Global. But this was accompanied by a letter stating that:

> *"Capax Discovery LLC is looking forward to a successful business relationship with Autonomy. The specific contract terms are being finalized and the contract should be ready for signature shortly.*

> *In the meantime, Autonomy has requested financial information for Capax Global LLC. We are here providing that information but with the express understanding that Capax Global LLC is a separate and distinct entity from Capax Discovery LLC. All contractual obligations will be between Capax Discovery LLC and Autonomy only."*

54. The message was clear: it should <u>not</u> be assumed that Capax Global would stand behind the financial obligations of Capax Discovery. As Dr Lynch was keen to point out in his first witness statement and in his oral evidence, in the real world, parent companies will often be expected to stand behind their subsidiaries, for reputational and other reasons. Mr Baiocco's letter negated any such expectation. If it was not already apparent to Autonomy that a reason for Mr Baiocco forming the new entity was to insulate Capax Global, that point was driven home by this letter.

55. According to Mr Welham, that clear message was not, however, shared with Deloitte: it was Mr Welham's unchallenged evidence that Deloitte was <u>not</u> provided with a copy of this letter, either during its review or at any time thereafter. As the Claimants submitted, it is not easy to think of an innocent explanation for why Autonomy withheld the letter from Deloitte; even Dr Lynch was stumped: he resorted to a generality about a parent always wanting to avoid reputational risk, not able to come up with an explanation. Mr Hussain could not be asked: but the Claimants submitted, as must be right and I accept, that with the finance department so exercised about the issue it is most unlikely he did not know about the difficulty or that any of this happened without his knowledge.

56. If a paper trail to justify the position could not be developed, the importance of showing that Capax Discovery was in fact paying its debts became all the more important. Consistently with what according to the Claimants' case had been agreed between Mr Egan and Mr Baiocco (as they each confirmed it had been), the process adopted to give the appearance of a fast-developing revenue stream from which Capax Discovery could (and in the event, did) pay the instalments due under the first Capax Discovery/EDD sale was for Autonomy to invoice and pay Capax Discovery for "*outsourcing*" what were described as 'specialised EDD services' to Capax Discovery.

57. According to the Claimants, the supposed *"outsourcing"* was a fiction. It was Mr Egan's clear evidence that, just a week or so after the licence, Capax Discovery was not then in a position to perform e-Discovery services for Autonomy's customers; in other words, Autonomy could not outsource its own e-Discovery work to Capax Discovery. Mr Egan accepted in cross-examination that he did not *"proactively tell"* anyone in Autonomy's finance department; but he was firm in his belief that Mr Hussain and Dr Menell would certainly have known this from the fact that the work could not possibly have been done so little time after the licence.

58. To return to the 'handshake' agreement between Mr Egan and Mr Baiocco, it is to be noted that the existence of an arrangement between Mr Baiocco and Mr Egan was not challenged. Rather, the challenges came in the form of: (i) the timing of the arrangement, (ii) its terms, and (iii) who else knew about it. There was considerable dispute about all three issues, and especially the question of the terms of the agreement in light of conflicting evidence that a note of an interview with Morgan Lewis in February 2013 suggested Mr Baiocco had given, to the effect that the only agreement was that Autonomy was going to send Capax Discovery enough business to cover the instalments due under

the first Capax Discovery/EDD sale, rather than that Autonomy would initially fund such instalments.

59. For reasons more elaborately explained elsewhere (see paragraphs 2497 to 2502 in the main body of the judgment) I have concluded that the 'handshake' agreement was before the written agreement, as Mr Baiocco told me it was; and that the agreement was a means of getting the funds to Capax Discovery to enable it to pay instalments due under the first Capax Discovery/EDD sale. But for present purposes, the more immediately relevant points are, as it seems to me, that these arrangements (a) do suggest a previous track record of arrangements between Mr Baiocco and Mr Egan that sat outside a contract, and quite radically altered its economic substance from that apparent from the legal terms and (b) provide a foretaste of the arrangements which on the Claimants' case underpinned all the impugned VAR sales.

Standard terms of the Capax Discovery VAR sales

60. The second of the 'key points' is that each of the Autonomy/Capax Discovery VAR sales transactions took place under a VAR agreement between Autonomy and Capax Discovery dated 30 June 2009 ("the June 2009 Capax Discovery VAR Agreement"). This provided for the following, amongst other things:

    (1) Clause 5.1 stipulated that there was required to be a purchase order for each sale transaction, and in the event of any conflict between the terms of a purchase order and the agreement, the terms of the VAR agreement would prevail.

    (2) Clause 23 stated:

    > *"**ENTIRE AGREEMENT: AMENDMENT**. This Agreement sets forth the complete and exclusive agreement between the parties with respect to its subject matter and supersedes any and all other written or oral agreements previously existing between the parties with respect to such subject matter. No alterations, modifications or additions to this Agreement shall be valid unless made in writing and signed by a Director or Officer of each party. The terms of any purchase orders or the like submitted by the VAR which conflict with any terms in this Agreement whether or not countersigned as accepted by Autonomy shall not be binding on Autonomy, regardless of Autonomy's failure to object to such terms."*

    This provision was drawn so as to invalidate the legal effect of even written variations drawn up in purchase orders between Capax Discovery and Autonomy. Any variation necessarily needed to be in writing and signed by a director or officer of Autonomy. The clause similarly negated any prior arrangement reached between Capax Discovery and Autonomy (or more pertinently, any Autonomy salesman).

    (3) Clause 7(c) made it clear that Capax Discovery was unequivocally on risk for any purchase, irrespective of whether or not Capax Discovery could obtain payment from an on-sale to an end-user:

> *"VAR shall not be relieved of its obligations to pay fees owed to Autonomy hereunder by the non payment of fees by an end-user."*

61. These provisions made crystal clear the legal position that no side or collateral agreements would be effective in law to modify in any way the legal obligations assumed, and that the VAR's obligation to pay was not in any way conditional on itself receiving funds from an end-user.

Audit confirmation letters in every case

62. The third of the 'key points' is that this position in law was further buttressed by the requirement of the auditors that the VAR (here, Capax Discovery) must sign 'debtor confirmation letters' in respect of the debt arising under the impugned VAR deals. The debtor confirmations are identified further below by reference to the individual transactions. For example, in VT16 (which *inter alia* related to the Amgen deal) the debtor confirmation stated:

> *"The items listed above were properly charged to our account and were unpaid as of 30th September 2010 and there are no side letters or other agreements in respect of the subject matter of this request, except as noted below:*
> *[Nothing was noted.]*
>
> *We acknowledge that Autonomy Corporation plc retains no continuing managerial involvement in the delivery of this product or service, other than stipulated in the licence agreement."*

63. Fourth of the 'key points' was that Mr Baiocco, who invariably represented Capax Discovery in each of the sales, confirmed in his evidence that he *"absolutely believed"* the debtor confirmations he signed to be true. Mr Egan also believed them to be true. In Mr Baiocco's witness statement, in language smacking of considerable lawyering, Mr Baiocco set out his view of the nature of the Capax Discovery transactions in general terms as follows:

> *"A value-added reseller ("VAR"), as that term is usually used, is a company that purchases a product from a manufacturer or supplier to which it adds features or services and then resells the package (usually to an end-user) as an integrated or completed solution. However, that was not the nature of the relationship we had with Autonomy. Instead, Mr Egan told me that Autonomy often faced the situation where it was very close to completing a sale to an end-user, which it was not able to conclude by the end of the quarter. Rather than Autonomy lowering the price to get the end-user to sign a contract before quarter end, Autonomy wished instead (a) to enter into an agreement with us at quarter end supposedly for on-sale by us of the software in question to the end-user, and then (b) to continue to negotiate with the end-user and to close the deal with the end-user in the following quarter. In return, Capax Discovery would receive a 10% fee."*

VT2: Capax/TXU in Q2 2009 and Q3 2009

64. The Capax Discovery/TXU VAR transaction (VT2) was the first VAR sale by Autonomy to Capax Discovery. Mr Baiocco's evidence was that he was approached in around May or June 2009 by Mr Egan, asking whether Capax Discovery would become a reseller for Autonomy.

65. VT2 was in two parts. Both sales were on the terms of purchase orders issued under the June 2009 Capax Discovery VAR Agreement (see paragraph 60 above) for prospective end-user TXU. The first purchase order was dated 30 June 2009 and was in an amount of $783,086 for the licence fee plus $78,309 for support and maintenance to be paid in three instalments within 90, 180 and 270 days respectively of 30 June 2009. The second purchase order was dated 30 September 2009 and was in an amount of $462,840 for license ($61,652), support and maintenance ($6,165) and hardware ($395,023).

66. The Claimants relied especially on the following features of VT2:

(1) At the time, Capax Discovery had only very recently been incorporated. At least if looked at as an entity legally separate from its parent (Capax Global), the risk in taking on a liability of $1.3 million was very considerable.

(2) Although Mr Baiocco accepted in cross-examination that part of the incentive for doing the TXU deal was that Capax could try to build a relationship with TXU, and Capax did then obtain some business from TXU, the Claimants contended that the risk was so disproportionate to the reward for a recently incorporated entity that it lacked any *"sensible business justification"* absent some other explanation of its acceptability to Capax.

(3) The Claimants submitted that the obvious explanation of this basic mismatch between legal exposure and the rationality of taking the risk was that there was a side agreement or understanding that Autonomy would relieve it of the risk.

(4) They contended further that that explanation is supported by the fact that there is no evidence of any price negotiation between Capax Discovery and either Autonomy or TXU, nor of any assessment by Capax Discovery of the inherent risk by reference to the then state of negotiations for an end-user deal and the reliability of the end-user and its covenant.

(5) There is no evidence that Capax Discovery was ever intended to, or did in fact, have any involvement in Autonomy's ongoing attempts before and after the purchase orders to negotiate an end-user deal with TXU. Only Autonomy negotiated with TXU.

(6) After its exclusive negotiations with TXU, Autonomy entered into a direct Master Services Agreement with TXU and a Product Purchase Agreement exhibited to it on 18 September 2009 for the sale and purchase of both software and hardware for a total fee of $1,693,404 with an additional fee for consulting and training of $112,500.

(7) The 'direct' sale differed in substance from the VAR sale: and the fees payable were more than double those payable under the first Capax Discovery purchase

order. In an email dated 15 September 2009 from Mr Livius Guiao ("Mr Guiao") to Mr Hussain, Dr Menell, Mr Kanter, Mr Chamberlain and others Mr Guiao expressed the need to check that given that *"the terms of this deal were not contemplated at the outset, and largely defined in response to customer demands in the context of the negotiation"* and "*Given the one-off nature of where we ended up",* all concerned were *"Ok with moving forward"*. Of course, Autonomy had it in its power to deliver software whether or not the subject of the VAR sale, and to make an agreement without regard to any restrictions that might apply to a VAR.

(8) Although the contract was "direct" between Autonomy and TXU, the direct sale agreements provided that TXU was to pay Autonomy or Autonomy's designated payee. On 30 September 2009 Autonomy notified TXU that all fees due under the Product Purchase Agreement were to be paid to Capax Discovery.

(9) The sums thus to be paid to Capax Discovery exceeded the sums payable under the first purchase order by almost double; it was (so the Claimants alleged) because of this that Autonomy arranged for Capax Discovery to issue the second purchase order for the purchase of software and hardware.

(10) Mr Baiocco gave unchallenged evidence that:

> *"TXU paid Capax Discovery $47,000 per month over the next 36 months. Between December 31,2009 and September 6, 2011, Capax Discovery paid Autonomy the full amount of the two TXU purchase orders and retained the balance of $370,000."*

(11) Although Capax Discovery thus pocketed some $370,000 despite having no role in bringing about any sale of the software licence to TXU, unusually the payments from TXU came in 36 relatively modest tranches: and, significantly according to the Claimants, this coincided with (or the Claimants would say, resulted in) an exactly corresponding delay in Capax Discovery paying on to Autonomy what was owed. That, the Claimants suggested, evidenced a side agreement or understanding that Capax Discovery would only pay if and when paid.

67. The Claimants' case was that the vice of the arrangements was further demonstrated by the fact that Autonomy never told Deloitte about the direct Autonomy/TXU agreement; and in (allegedly) unchallenged evidence Mr Welham stated in his witness statement that this was would have been relevant for Deloitte:

> *"…because evidence of revenue reversals on sales to Capax Discovery would have been relevant to our assessment of the timing of revenue recognition in relation to further Capax Discovery sales. As I will explain further below, Deloitte became aware in the first two quarters of 2010 of a handful of VAR transactions being replaced by direct deals between Autonomy and the end-user, and these caused Deloitte concern."*

68. Mr Welham added that he would have expected any direct deal with TXU in Q3 2009 to have been included in a list of all revenue deals of $100,000 or more provided by

Autonomy to Deloitte for the purpose of its Q3 2009 review: but it was not. The Claimants contended that by not including the direct TXU deal in Autonomy's list of Q3 2009 transactions with revenues exceeding $100,000 Autonomy deliberately concealed from Deloitte the fact of the direct dealing because (it was stated in the Claimants' closing submissions):

> *"the existence of the direct sale would have given rise to a concern that the agreement with Capax Discovery had, in effect, been reversed and would later be seen by Deloitte as part of a pattern of such reversals."* [9]

69. The Defendants disputed all these contentions, and submitted that:

(1) The terms of the June 2009 Capax Discovery VAR Agreement made it clear that the VAR was obliged to pay (and was not relieved by any non-payment by the end-user) and that the agreement comprised the entire agreement between the parties. The terms of the contractual arrangement also made it clear that the risk of ownership had passed, and that managerial control was not retained.

(2) None of this was said to be a sham. The June 2009 Capax Discovery VAR Agreement represented the intentions of the parties, and they had promised they had no other.

(3) Further, there was no 'direct' evidence of any side agreement or understanding. On the contrary, Mr Baiocco had accepted that on all the Capax Discovery VAR deals, including this one, Capax Discovery was well aware of the terms of the arrangement and the nature and legal fact of the risk; he accepted the risk because he was confident that an end-user deal would be closed and in the hope and expectation of immediate profit and then longer term reward by way of a direct and valuable relationship with the end-user. Mr Egan did not specifically address the TXU deal in his witness statement, and did not suggest there was anything unusual or improper about it.

(4) The second purchase order was not occasioned to *"remedy the disparity between Capax Discovery's 30 June 2009 purchase order and the Autonomy/TXU agreement"* (as the Claimants alleged) but to cover additional licences, newly agreed managed services and support and hardware, as recorded in an internal Autonomy email dated 15 September 2009 from Mr Livius Guiao to Mr Hussain, Dr Menell, Mr Kanter, Mr Chamberlain and others requesting confirmation of the deal, which stated (*inter alia*) as follows:

> *"Background: We sold licence and support through our reseller CapAx last Q, and they submitted a PO for $783k licence + 10% maintenance. It has since evolved into a managed services engagement for which TXU will pay CapAx $47k per month for 36 months. This fee is payment for Qfiniti licences, hardware and managed services (including support). It's my understanding that we are waiting for a second PO for CapAx to cover the managed services and hardware."*

[9] Being precisely the concern later expressed by Deloitte in 2010.

(5) As mentioned above, Capax Discovery did indeed subsequently enter into a sub-contracted service agreement with TXU; and Mr Baiocco confirmed in his testimony in the US criminal proceedings that the deal worked *"in the way we hoped it was going to work"* (though it is fair to add that he said this to contrast the position with later deals).

(6) The statements in the Goldberg Segalla letter (see paragraph 2024 in the main body of the judgment) were true: and see paragraphs 2020 to 2028 in the main body of the judgment. The most that was said between Mr Egan and Mr Baiocco was that Autonomy would try to assist Capax Discovery if the end-user did not close by slotting Capax Discovery into another deal (*"backfilling"*, which did not deprive the original VAR deal of substance and did not undermine revenue recognition in respect of it). Mr Baiocco did not regard this as a side agreement at the time, or consider that he was involved in anything fraudulent.

(7) Capax Discovery had the ability to pay, if it had to. Deloitte expressly noted in their Q2 2009 review that it had a profitable business model, and drew comfort from the fact that the prospective end-user (TXU) was a Texas power company serving around 2 million homes, with latest accounts showing revenue of some $15 billion. Further, Capax Discovery's parent company, Capax Global, had adequate resources; business with Autonomy was potentially very profitable and a source also of valuable service work, all of which default would have squandered.

(8) Criticism of the second purchase order was misplaced: there was nothing improper in completing the overall transaction via the reseller, the reseller having already assumed the risk in relation to the first (major) portion.

(9) Likewise, criticism that Capax Discovery made a *"tidy profit"* was misplaced and did not suggest any side agreement or impropriety: risk deserved reward.

(10) The provision for Capax Discovery to be paid by TXU as designated payee was unobjectionable likewise: the fact that Capax Discovery paid Autonomy only as and when paid by TXU might show reluctance or forbearance in the exercise of contractual obligations, but not that there was no real sale, nor that risk or reward or managerial control had been retained.

(11) Deloitte had reviewed the revenue recognition on the deal as part of their Q2 2009 review (in July 2009) and, with an expressly recorded recognition in their "method statement" that particular care was required since *"given the nature of Autonomy's business…revenue is seen as a driver for market assessment of the performance of the business",* were satisfied that revenue was correctly recognised.

70. As to the allegations that Deloitte was misled, the Defendants submitted that:

(1) It was only later, in 2010, that Deloitte became interested in being told about deals that had gone direct and where the VAR was relieved of liability as a result. After Deloitte had expressed that concern, Autonomy's finance department made a point of informing Deloitte of any such deals where the reseller was relieved of its liability as a result. The TXU deal occurred at an earlier stage.

(2) In any event this was not a deal where the VAR was relieved from liability (rather, it was paid by TXU as its designated payee). Dr Lynch was asked about this in cross-examination. He told me he was not involved and did not know whether Deloitte was told of the direct deal; but he added that (a) in the case of a *"designated payee deal"*, *"the original deal isn't cancelled, it stays"* (b) Deloitte *"were given free run of all deals"* and (c) it was quite *"incorrect"* to suggest that Deloitte were intentionally not informed lest it might cause Deloitte to question the propriety of recognising revenue on VT2.

(3) There was no reason to include the direct deal in the list of Q3 2009 deals in excess of $100,000 provided to Deloitte because that list was for revenue deals, whereas the direct deal raised no revenue additional to the Q2 2009 and Q3 2009 sales to Capax Discovery which had already been included in the revenue sheets, and it would have been wrong to double-count.

(4) In reality, such complaint as the Claimants might have does not impact on the recognition of revenue from VT2: the most Mr Welham was prepared to say was that its disclosure *"would have been relevant to our assessment of the timing of revenue recognition in relation to further Capax Discovery sales."* It did not, in other words, affect their assessment of VT2.

My assessment of VT2

71. In my judgment, VT2 is not sensibly explicable except on the basis that the shared intention and expectations of the parties to it were that Autonomy's *"real customer"* (to use Mr Egan's phrase) was the end-user, and Capax Discovery was in substance what the Claimants labelled a *"placeholder"* for the real transaction, expected to do nothing and pay nothing out of its funds.

72. It is not realistically conceivable that a newly incorporated VAR which was genuinely at risk would have played such a minimal role after no due diligence and left Autonomy to carry on negotiations without participation of any kind or any process of keeping it updated and informed.

73. Nor is it really conceivable that Autonomy would have expected to be paid by the newly incorporated entity set up (according to Mr Baiocco) to provide a further layer of insulation from any risk, or accepted payment in dribs and drabs from the VAR once the end-user sale was closed, unless the real deal was of a different nature and substance than the contractual one, and ascribed to the VAR in effect a nominal role.

74. Any notion, sometimes suggested by the Defendants, that Autonomy was acting as agent for Capax Discovery and not on its own behalf is, in my view, almost impossible to square with the 15 September 2009 email from Mr Guiao referred to in paragraph 66(7) above, which demonstrates the extent to which Autonomy was negotiating for itself and without regard for the VAR, and the substantive economic irrelevance of the VAR sale save to trigger revenue recognition. It is a vivid illustration, to my mind, that Autonomy's customer was the end-user.

75. I cannot regard the contractual terms as precluding an accountancy treatment consistent with the true substance of the transaction. The legal position would have held sway in any legal proceedings; but the accounts were intended to reflect its economic substance, and

to include as recognised revenue only the revenue from a true sale where any onward sale to the end-user would truly be the adventure and responsibility of the VAR.

76. I do not accept the argument that such a conclusion is based on hindsight, which is impermissible. The events which occurred did not alter the substance of the transaction: they reveal its true substance and what it always was intended to be. In my judgment, these considerations, which of course do relate in part to facts occurring after the date of the VAR sale, are relevant in determining the real intentions of the parties and the economic substance of the transaction.

77. My conclusions as above summarised are fortified by the failure to notify Deloitte of the fact of the "direct deal". I do not accept the distinction sought to be made by Dr Lynch for these purposes between a "cancelled" deal and a "designated payee" deal: the effect that the VAR was provided with the funds whereby to pay off the amounts due under the VAR sale and that the VAR sale otherwise became an irrelevance (so that the VAR apparently retained no rights under the licence notionally granted) appears to have been the same in both. I do not think any good reason was provided or suggested for the failure to disclose. In my judgment, the most likely explanation is, and I find, that Deloitte were not told because it would have upset Deloitte's understanding of the nature of the transaction and led to questions about the role of Capax Discovery.

Particular points on the Defendants' involvement and knowledge of VT2

78. The Claimants contended that both Defendants were aware of facts demonstrating the impropriety of the decision to recognise revenue from VT2 and that both are culpable accordingly.

Mr Hussain's knowledge

79. As regards Mr Hussain in particular, the Claimants contended in summary that:

(1) The idea of involving Capax Discovery was, at least in part, his; and he took the credit for it: when Mr Egan reported to Mr Hussain and Dr Lynch by email dated 1 July 2009 that some large deals (*"Big ones"* with VMS, JPMC, Morgan and Intel) had successfully closed and also that *"…MM [Mr Mooney] got a $700k+ in from CAPAX that was not in Sush's planning"* Mr Hussain quickly responded that *"Unfortunately TXU (Capax) was in my planning but it came in a bit bigger!"*

(2) Mr Hussain (as well as Dr Menell, Mr Kanter, Mr Chamberlain and others) was responsible for the allegedly inappropriate issue by Capax Discovery of a second purchase order to cover the unanticipated difference between the licence fees payable under the Autonomy/TXU direct agreement and those payable by Capax Discovery under the first purchase order (and see paragraph 66(7) above);

(3) Mr Hussain was well aware, and kept a careful track, of the correlation between the staggered (36 in all) (i) receipts by Capax Discovery from TXU and (ii) payments by Capax Discovery to Autonomy, and was thus aware of the matters alleged by the Claimants to reflect and demonstrate the "pay only if and when paid" side agreement or understanding;

(4) Mr Hussain was also aware of the direct deal between Autonomy and TXU: the Claimants appear to imply (there is no direct allegation) that Mr Hussain would have known that this should have been reported to Deloitte and that he should have ensured that it was so; likewise, they contended, he should have ensured the inclusion of the TXU direct deal in the list of revenue deals for the purposes of Deloitte's Q3 2009 review (see paragraph 68 above). The Claimants went on to assert that Mr Hussain probably authorised both omissions with a view to ensuring that the direct deal did not prompt a concern on the part of Deloitte about deal "reversals".

80. Except for emphasising his position as regards (4) in the preceding paragraph that *"it was right not to include the TXU deal in the revenue list and indeed it would have been wrong at that point to recognise revenue from the direct deal"* Mr Hussain did not respond in detail to these allegations, but he denied that there was any impropriety in anything that was done in respect of VT2.

81. In my judgment, Mr Hussain was closely involved in the salient elements of VT2 and knew that the VAR sale was simply intended to provide the basis for revenue recognition prior to the "real deal" with TXU. He was aware and indeed party to the fact that there was never any intention of requiring Capax Discovery to do or pay anything; and he knew and was involved in the arrangements which resulted in the "designated payee" way of enabling Capax Discovery to discharge its obligations under and make a profit on the VAR transaction which then became in law the irrelevance which in substance it had always been.

82. I also find that Mr Hussain knew and approved of the decision not to include the Q3 2009 direct deal between Autonomy and TXU in the list of revenue deals over $100,000 compiled for the purposes of Deloitte's Q3 2009 review, because to attribute revenue to direct deals which followed impugned VAR transactions (in respect of which revenue had already been recognised) would have been double-counting. I do not consider that decision to have been improper in the case of VT2, given that both the Q2 2009 and the Q3 2009 sales to Capax were included in the revenue sheets.

Dr Lynch's knowledge

83. As regards Dr Lynch, the Claimants did not in their pleadings identify any involvement or participation in VT2 on his part; and the Claimants' Further Information in respect of the allegations of knowledge against Dr Lynch did not identify any particulars in relation to VT2. The only specifically transaction-related evidence of his involvement that the Claimants advanced was his receipt of the email exchange on 1 July 2009 between Mr Egan and Mr Hussain which I have quoted above (of which he was an addressee).

84. Nevertheless, he was cross-examined as if he must have known about the transaction and understood that Capax Discovery was to be a "placeholder", required to do nothing and required to pay nothing in return for a large fee for (in effect) facilitating the improper recognition of revenue by Autonomy.

85. Dr Lynch rejected every aspect of this, emphasising that:

(1) He had no knowledge of or involvement in the TXU deal beyond what he had been told in the email exchange of 1 July 2009 referred to above;

(2) He had no reason to think that either the direct deal or the payment of a MAF was in the least improper (and nor was it ever suggested to him on what basis he should have known there was anything improper about the transaction);

(3) He was not involved in determining how the deal should be reported to Deloitte, but he had no reason to believe that Deloitte had not been told of the direct deal because of a concern that it might cause Deloitte to question its propriety;

(4) In any case, Deloitte had been *"given free run of all deals"*, with open access to Autonomy's books and accounting records, to see whatever they wanted to see about any of them;

(5) Furthermore, this was not, in his view, an example of a cancelled deal: it was *"a designated payee deal…in which case the original deal isn't cancelled; it stays"*;

(6) He also rejected the description used by the Claimants of Capax Discovery being a mere *"placeholder to facilitate the improper recognition of revenue"* as being a self-minted term or tag which, notwithstanding the VAR's unquestioned liability, assumes some inherent impropriety in a VAR deal where there was none.

86. I cannot accept this, or its implicit suggestion that Mr Hussain was on a frolic of his own or prepared to proceed in such a matter and in such a way without keeping Dr Lynch informed. Furthermore, this was the first VAR deal with a new 'friendly' VAR, Capax Discovery. It seems to me very unlikely that Dr Lynch would neither himself have kept an eye nor been informed as to its features and progress.

87. Further:

(1) Autonomy was a tight-run company, managed in effect by a small 'gang' of which Dr Lynch and Mr Hussain were at the apex, and who corresponded regularly with each other;

(2) Dr Lynch and Mr Hussain often shared an office, and always worked closely together;

(3) I had not the opportunity to observe Mr Hussain; but the documentary record, especially of his emails to Dr Lynch before Earnings Calls and other pressure points, suggests to me that Mr Hussain is a highly strung and anxious person, who was apt to share his concerns with, and seek assistance and reassurance from, Dr Lynch;

(4) There was no reason for Mr Hussain to bear alone the burden of what I have held he knew about the impugned VAR deals: a natural inclination, stronger for someone in need of reassurance, would have been to discuss what was on any view an area of some risk and sensitivity (and exposure);

(5) Dr Lynch was, or at least after 2008 had become, fixated on meeting revenue forecasts, and followed revenue targets and shortfalls closely and continuously in close conjunction with Mr Hussain: it is not disputed the VAR deals were an

obvious integral part of this, being (it was common ground) resorted to frequently for revenue recognition purposes;

(6) It is, to my mind, much more likely than not that Mr Hussain kept Dr Lynch informed, and Dr Lynch (who was controlling and interventionist) would have wished to and did discuss the position with him in some detail.

88. I have concluded, on a balance of probabilities, that Dr Lynch would have been kept informed by Mr Hussain and made well aware of the importance of the deal in the context of Mr Hussain's need to cover a revenue shortfall, and would have recognised the transaction as fitting the format that Mr Hussain had conceived and which he and Mr Hussain needed and encouraged as I have previously described. In short, I consider it more likely than not (and I find) that in accordance with the strategy the sale to Capax Discovery VT2 was in commercial terms illusory, despite its ornate legal clothing.

89. In other words, in my judgment, the only real sale was the direct one by Autonomy to TXU; no revenue should have been recognised from the VAR sale; and both Defendants knew that.

VT3: Capax/Kraft

90. VT3 was a VAR transaction between Autonomy Inc (referred to in the agreement and below as Autonomy) and Capax Discovery in Q3 2009. It was established by a purchase order in September 2009 for a licence fee of $4,000,000 and a maintenance fee of $200,000 in which the prospective end-user was Kraft (a well-known American grocery manufacturing and processing conglomerate, and, by Q3 2009, already a long-standing customer of Autonomy).

91. The Kraft deal, which was to convert Kraft's then-existing data hosting relationship from a pure fee-for-service arrangement into a licence plus hosting arrangement, was a large (originally some $4,300,000) and important one for Autonomy, and negotiations to close it were a matter of keen interest to both Mr Hussain and Dr Lynch.

92. Although as early as 31 August 2009 Mr Hussain reported by email to Dr Lynch that *"Kraft is won at $4.3m",* that proved over-optimistic, and negotiations continued in September, so that by 23 September 2009 Mr Patrick Ryan, one of the Autonomy salespeople involved, was *"not sure they can pull it off"*. When Mr Hussain forwarded this gloomy report to Dr Lynch, he replied in his blunt and dictatorial style, *"Ryan is as always useless someone else must close"*.

93. When cross-examined on whether he could recall that deal at around this time, Dr Lynch described the Kraft deal as "key to the quarter" he replied:

> *"I don't, but it's a $4.3 million deal a week off the end of the quarter, so, yes, it's going to be an important one."*

Its importance, and the pattern of Mr Hussain keeping Dr Lynch closely and regularly informed, was emphasised again in an email from Mr Hussain to Dr Lynch and others on the next day (24 September 2009) noting:

> *"...Key are eli, ameriprise, kraft"*

94. On 25 September 2009, Mr Hussain sent a series of emails including one in the morning to Mr Egan starting *"so the wild card is kraft (stouff – good luck!) – we really need this deal"*, and one a little later to Dr Lynch reporting on an *"Overall miserable day"* because expected deals had not materialised (including Kraft). Later that day, however, Mr Hussain emailed Dr Lynch saying,

> *"I have an idea on kraft".*

95. There is no written evidence as to the nature of that idea, so the Claimants contend it must have been elaborated and discussed orally between Mr Hussain and Dr Lynch. Again, there is no record of that discussion, but Dr Lynch (though he explained he had no specific recollection) said in cross-examination that he *"suspect[ed]"* that it was to use a VAR to take over the Kraft deal and to enable revenue to be recognised in Q3 2009 notwithstanding delays in concluding the end-user deal. Plainly that was the reason and purpose: Dr Lynch's equivocation on this, and also his refusal to concede that by then Autonomy no longer expected to conclude a deal with Kraft in that quarter (though he accepted that it was *"certainly looking less likely"*) seemed to me to be designed to suggest detachment and was unconvincing.

96. Mr Hussain, in an email shortly before midnight on 25 September 2009 sent to Mr Egan (which was not sent to Dr Lynch), stated that *"we may have to use capax for the K[raft] deal??".* The Claimants suggested that the implicit hesitation in using Capax Discovery was caused by Mr Hussain's concern that there were still outstanding amounts due from Capax Discovery in respect of the prior Capax Discovery EDD (RT1) and TXU transactions (VT2), which could prevent Deloitte from agreeing to the recognition of revenue on a further Capax Discovery transaction in view of IAS 18 §14(d) (lack of collectability). Mr Hussain therefore told Mr Egan he needed "*paperwork for capax - suggest $750k or so?*"

97. The Claimants alleged that what this signified was that Autonomy was to channel further funds to Capax Discovery (in the event, $1 million rather than $750,000) to enable Capax Discovery to pay down its outstanding debt: the *"paperwork"* required was for this purpose. Such a payment would enable Autonomy to present Capax Discovery to Deloitte as a counterparty that was complying with the payment schedule in its prior deal.

98. Mr Egan then approached Capax Discovery with a proposal that Capax Discovery should submit a purchase order to Autonomy for a Digital Safe licence for onward licencing to Kraft for $4,000,000. In his witness statement he said:

> *"At Mr. Hussain's direction, I approached Mr. Baiocco (Capax Discovery) with a proposal. I told him about the status of the Kraft deal, including the fact that I expected it to close shortly after the end of the quarter. I asked Capax Discovery to act as a VAR, to submit a purchase order for a Digital Safe license for onward licensing to Kraft, and to agree to pay $4 million for that software -- the same price I had been discussing with Kraft. I followed the guidance that Mr Hussain gave me as described in paragraphs 28 and 29 above. I told Mr Baiocco that Autonomy would continue its efforts to close a deal with Kraft and, when we were successful, we would get Kraft to pay its license fee to Capax so that Capax, in turn, could pay Autonomy. I also told him that, if for some reason we could not get Kraft to pay Capax, we would find another way to make sure*

that Capax did not have to reach into its own pocket to make a payment to Autonomy. I agreed that Autonomy would pay Capax 10% of the purchase price for assisting us by submitting a purchase order that said that Capax Discovery was obligated to pay for the software under the terms of its VAR agreement with Autonomy. I told Mr. Baiocco that the 10% fee arrangement was the normal margin for resold deals."

99. On 30 September 2009, the last day of the quarter, Capax Discovery issued a purchase order for a licence of Digital Safe archiving software for on-sale to end-user Kraft. Dr Lynch accepted in cross-examination that he would *"probably have known shortly after quarter end"*. Mr Baiocco's evidence, which Dr Lynch said he had no basis to dispute, was that *"Capax's purchase order was drafted for us by Autonomy"*. The inference (which I accept) is that Autonomy had to draft the purchase order because it was only Autonomy (rather than Capax Discovery) that knew what software was being offered to Kraft and at what price.

100. The Claimants relied on the following features of the purchase order itself:

(1) The amount was almost the same as the original proposed deal between Autonomy and Kraft.

(2) Kraft was the only authorised end-user under the terms of the purchase order: Capax Discovery could not sell to anyone else. Thus, if a deal with Kraft could not be closed, then, according to the contract, Capax Discovery would still have to pay Autonomy, but be unable to recoup its payment by a sale to another third party.

(3) The licenced software was Digital Safe and related products, and a hosted arrangement was envisaged: the Claimants submitted that Capax Discovery *"could have no conceivable role to play in that commercial context"*.

101. The Claimants submitted that, having regard to these features, the VT3 deal made no commercial sense at all, unless accepted to be an expedient to enable Autonomy to accelerate into Q3 2009, revenue that would be likely to be earned in Q4 2009 by the mechanism of introducing Capax Discovery as a placeholder, which would sign up to an agreement on the basis of an assurance that it would not have to do anything for its reward and, whatever the agreement might provide in law, would in reality not have to pay Autonomy if the end-user deal failed.

102. The Claimants further submitted that the conclusion that this indeed was the key to what they presented as the otherwise commercially incoherent, was supported by the further evidence that:

(1) When, on 30 November 2009, the $3.8 million balance payable by Capax Discovery in respect of the Kraft purchase order fell due, it was not paid. This non-payment was entirely consistent with the handshake agreement between Mr Egan and Mr Baiocco: as at 30 November 2009, no end-user deal with Kraft had been concluded, and so Capax Discovery was not expected to pay Autonomy.

(2) The end-user deal eventually struck was another direct deal between Autonomy and its established customer Kraft for the identical software as was detailed in

the purchase order from Capax Discovery: just as, according to the Claimants, had always been expected by the "placeholder" (Capax Discovery).

(3) Although Autonomy requested Kraft to pay Capax Discovery, which would have enabled Capax Discovery to pay Autonomy, Kraft declined and insisted on its arrangements being exclusively with Autonomy; again consistently with the alleged assurances, Autonomy took steps to relieve Capax Discovery, and on 29 December 2009, they entered between them a letter agreement cancelling the licence fees due from Capax Discovery in recognition of the direct receipts by Autonomy from Kraft.

(4) The same letter agreement also provided for Capax Discovery to be paid a *"one-time fee"* of $400,000, which the Claimants contended was:

> *"to reward Capax Discovery for having acted as a placeholder in order to enable Autonomy to recognise revenue improperly and as an incentive to do additional, similar deals with Autonomy."*

103. Finally, the Claimants contended that both the fact of the impropriety of these arrangements and the knowledge that they were so on the part of the Defendants is shown by the steps that the Claimants claimed were taken to mislead both Deloitte and Autonomy's regulators.

104. Before addressing that latter question whether Autonomy misled its auditors and regulators about VT3, it is convenient to record the basis on which the Defendants sought to rebut the Claimants' contentions as to its features and their alleged conformity with the Claimants' case that, in accordance with the side agreement or understanding they alleged, Capax Discovery was only ever a *"placeholder"*.

105. As to the Defendants' rebuttal:

(1) They again stressed (a) the unequivocal nature of the June 2009 Capax Discovery VAR Agreement's provisions as to (i) the unconditional transfer of risk and reward (ii) the unconditional obligation to pay (iii) the absence of any provision for Autonomy to retain any managerial control and (iv) the entire and exclusive nature of the contractual agreement, and (v) the stipulation that to be valid any modifications would have to be in writing signed by a director or officer; and (b) Mr Baiocco's evidence, written and oral, that (i) Capax Discovery was genuinely on risk (ii) Capax Discovery perceived there to be a good commercial rationale sufficient to warrant the risk; and (iii) there was no side arrangement or understanding such as might impact on revenue recognition. In this context, the Defendants again pointed out that Mr Baiocco has expressly vouched on oath for the accuracy of the Goldberg Segalla letter which confirmed the above, and for the confirmation letters to Deloitte.

(2) They rejected the Claimants' contention that there was anything wrong or improper in the admitted circumstance that the Kraft VAR transaction (VT3) was (a) entered into right at the end of the quarter, because (b) delays with Kraft meant that the deal with Kraft could not be signed until October 2009 and (c)

the VAR deal enabled Autonomy, by securing the deal with Capax Discovery, to recognise revenue in Q3 2009.

(3) They referred to and adopted Mr Baiocco's evidence in the US criminal trial, which he reiterated in cross-examination in these proceedings, that Capax Discovery had its own line of credit, and that even if that *"would have been painful",* it could have drawn down on it and would have been able to pay what it owed.

(4) They rejected any suggestion that the software was not delivered to Capax Discovery, citing Mr Baiocco's express confirmation that it had been delivered in the usual way, on execution, through Autonomy's electronic portal (Automater).

(5) They made the point that the fact that Capax Discovery could legally only sell on to Kraft only impacted against it if the end-user sale was in doubt: but the Kraft deal, though delayed, was secure.

(6) Further, they stated that the Claimants' suggestion that because (a) Kraft was Autonomy's customer and Autonomy would probably handle negotiations for closing the end-user deal to it and (b) the Digital Safe element was to be hosted there was no realistic prospect of Capax Discovery forging a relationship with Kraft (so that a primary perceived commercial benefit to Capax Discovery would never in fact eventuate) was factually incorrect. Digital Safe was the biggest but not the only element of the software package sold. The package included also Autonomy Legal Hold. In the event, Capax Discovery did in fact provide services to Kraft, including in connection with Autonomy Legal Hold.

(7) They also emphasised that the original intention was that the end-user (Kraft) should purchase from the reseller (Capax Discovery). There was nothing abnormal, still less improper, for a reseller to be interposed to complete a deal even where the manufacturer had been involved in the negotiations. Nor, in any logic, so they argued, would revenue recognition be affected by who was at meetings and carried on negotiations with Kraft, the end goal being a shared one, to achieve an end-user sale.

(8) They denied that the provisions for cancellation of Capax Discovery's obligations when Kraft insisted on a direct deal with and direct payment to Autonomy demonstrate any impropriety. There was no anterior agreement; and the cancellation was a proper way of dealing with the events that happened. It also ensured that revenue would not be recognised twice in respect of a sale of the identical software. Dr Lynch explained in cross-examination:

> *"…the problem is that we've now got a reseller who has gone on risk in good faith that when the Kraft opportunity, if it appears, they will be the one that's in the queue to supply it. Kraft, for whatever reason, have decided that they don't want to work with these people. We don't want Kraft to be unhappy because they're an important, big customer, and we don't want one of our resellers to get turned over by events which are beyond their control and so we have come up with a solution and the solution here…looks like a sensible outcome to us in that there's $4 million worth of real deal – remember, the software goes on and is used by Kraft and*

> *thousands of employees so it's a perfectly real thing – and there's $4 million of cash coming in and we end up with Kraft being happy and we end up with Capax being happy.*
>
> *Another way of looking at this is, what would be the situation if we supplied Kraft and then we left Capax unable to sell to Kraft, then we'd be looking like we were behaving with our partners in very bad faith in that situation. And that would be very damaging to the business and the ecosystem with partners. Why would anyone work with us? Why would anyone trust us in that situation?*
>
> *It's a commercial decision ultimately about how you handle a difficult situation…"*

(9) Likewise, they contended that the payment of a fee to Capax Discovery did not connote that anything improper had happened, or that Capax Discovery had not been on risk, or that the revenue was not properly recognised. It was (as Dr Lynch said in cross-examination) *"eminently reasonable"* to pay Capax Discovery a fee in circumstances where Capax Discovery had gone on risk, but Autonomy had taken the Kraft sale opportunity (and any upside from it) for itself.

(10) They relied on Deloitte's assessment of VT3 and their conclusion that each of the criteria of IAS 18.14 was satisfied.

(11) They rejected the allegation that they had misled Deloitte, and also the FRRP, about VT3 and in doing so further demonstrated its lack of commercial sense and real substance.

Approval by Deloitte

106. As the Defendants emphasised, Deloitte reviewed VT3 and were satisfied with the revenue recognition. It is clear from Deloitte's working papers for the transaction that their approval was in the full knowledge that (a) Autonomy had been negotiating directly with Kraft throughout Q3 2009 but the deal could not be struck directly before quarter-end due to time constraints; (b) Autonomy continued to be in negotiation with Kraft after the date of the VAR transaction (as recorded in the working papers); (c) during Q4 2009, Kraft made clear that it wished to deal directly with Autonomy, rather than through Capax Discovery, and ultimately, the deal went direct with Kraft; (d) the VAR deal was cancelled to make sure (as Mr Welham explained in his cross-examination) that *"revenue wasn't, as it were, recognised twice"*; and (e) a MAF was paid to Capax Discovery so that (to quote from Deloitte's working paper)*"the VAR retained the margin they would have got, had the end-user actually signed with them"*.

107. Deloitte did not apparently consider that any of these features were an issue for revenue recognition, whether as regards the *"genuine commerciality"* of the VAR agreement or otherwise. (They have more recently confirmed that this remains their position in their own defence in the Formal Complaint against them brought by the Financial Reporting Council ("the FRC")).

108. The Claimants sought to answer this on the basis that Deloitte was fundamentally misled as to vital aspects of the true transaction. In particular, the Claimants claimed that:

(1) Deloitte was misled into treating Capax Discovery as a creditworthy counterparty because it was able to and did pay a deposit of $400,000 for the VT3 transaction: Deloitte was not told, and did not know, that the funds used by Capax Discovery to pay the deposit were principally derived from payments by Autonomy for allegedly non-existent EDD services;

(2) Deloitte was misled into believing that behind Capax Discovery stood the resources of Capax Global and the group, and that it had always kept up to date on payments for previous large deals: Deloitte was not told, and did not know, that Mr Baiocco had set up Capax Discovery as a separate entity in part to bolster the alleged assurance that it would not be at real risk by making it unprofitable to sue, and had written (on 31 March 2009) to Autonomy expressly disavowing any suggestion that Capax Global could be expected to stand behind Capax Discovery's obligations;

(3) Deloitte was misled by Autonomy's management into an understanding that it was intended that Capax Discovery would on-sell to Kraft and that Capax Discovery would at least participate with Autonomy in negotiations with Kraft: whereas in truth (so they contended) Autonomy never expected Capax Discovery to have any dealings at all with Kraft, still less to complete a deal with Kraft;

(4) Deloitte was misled into concluding that Capax Discovery was genuinely taking the risk that no end-user deal might eventuate: they were not told and knew nothing of assurances given by Mr Egan which (so the Claimants alleged):

> *"meant that, in commercial reality, Capax Discovery was not intended to be left out of pocket if no end-user deal eventuated"*.

(5) Deloitte was misled into concluding that the cancellation of the VAR transaction was simply a necessary way out of a most unusual eventuality, and that the payment of a MAF was a suitable recompense for depriving Capax Discovery of its expectation of an end-user deal and future service fees, for which it had taken on substantial risk: whereas in truth, some method of reversing or cancelling the VAR transaction was always going to be required, Capax Discovery had never in truth had any such expectation and the MAF was a gratuitous payment for its role as a *"placeholder"*.

109. As to (1) in the preceding paragraph 108, it does appear that Messrs Hussain, Chamberlain and Egan did have concerns that Deloitte might have an issue about Capax Discovery taking on such a large debt whilst there remained outstanding amounts due from Capax Discovery on the TXU (VT2) deal, and did press for this to be resolved. E-mails exchanged between Messrs Chamberlain, Hussain and Egan in October 2009 demonstrated their concern in this regard:

(1) On 1 October 2009 at 12.06 a.m., Mr Chamberlain sent an email to Messrs Hussain and Egan saying:

> "*It would be a big help on rev rec if Capax pay the amount due on TXU. 1/3rd ($287,131,66) of the Q2 deal was due on 28 Sept 2009. Taking*

such a large deal through someone not up to date on payment presents issues. Can you get the cash?"

(2) Mr Hussain then wrote to Mr Egan:

"*Important that we try to get something – auditors will be an issue, I didn't know this one was o/s*" (i.e. that the Capax Discovery/TXU debt was outstanding)

(3) Mr Egan replied:

"*me neither, does it have to be today or can we get it asap. Remember they have sent 400k against the 4M Fedex today*"

(4) Mr Hussain replied:

"*Find out if they got the cash on the first txu deal – I assume they did*"

110. This concern regarding collectability continued into October 2009 as Deloitte considered revenue recognition on the Capax Discovery/Kraft deal:

(1) On 9 October 2009, Mr Stephan sent an email to Mr Hussain (copied to Messrs Egan and Chamberlain) saying:

"*On the Capax/Kraft deal, the auditors want to understand the status of the deal between the reseller and the end-user (is the deal closed and if not, when is it expected?). This is necessary because Capax is not a big company and it would probably be difficult for Capax to prove that they could pay us if they did not get paid by Kraft*".

(2) Mr Hussain replied:

"*I'll let stouff handle but obviously capax have given us an unconditional PO and are upto [sic] date with all payments. PLUS and most importantly they have paid 10% on signing so the risk is lower than most other deals!*"

111. Mr Miles took Mr Welham, in the course of his cross-examination, to invoices and confirmation letters in relation to the TXU deal, which were sent to Deloitte in October 2009, and also to a "Debtor testing spreadsheet" e-mailed to Mr Tom Murray of Deloitte on 15 December 2009 making clear to Deloitte that Capax Discovery's debt remained outstanding. Furthermore, Deloitte's working paper schedule recorded that indebtedness as outstanding. Thus, it seems clear that Deloitte actually knew that the VT2 amounts remained outstanding, as Mr Welham had eventually agreed. Mr Welham also agreed that

(a) he had in effect been misled by it being framed as an assumption in his instructions that there were amounts outstanding and that Deloitte did not know this (when in fact it did) and (b) as a matter of fact, this was not an issue which impacted their assessment of revenue recognition anyway.

112. As to (2) in paragraph 108 above, it is true that Deloitte were not specifically shown the letter from Mr Baiocco (dated 31 March 2009) making clear, when providing financial information for Capax Global at the request of Autonomy in the general context of discussions about VAR deals with Capax Discovery, that Capax Discovery was a separate and distinct entity from Capax Global. However, when cross-examined as to his evidence in his witness statement that the letter *"may have been of some relevance to the exercise we undertook of assessing the collectability of revenue from Capax Discovery"* he accepted that Deloitte were well aware that Capax Discovery was a new company, legally separate from Capax Global, and emphasised the next following phrase in his witness statement that:

> *"…it is fair to say that we were not proceeding on the basis that other companies within the group would be guaranteeing Capax Discovery's payment obligations."*

113. As to (3) in paragraph 108 above, and as stated previously, it seems that Deloitte were aware that Autonomy had handled all the negotiations with Kraft prior to the VAR transaction and were also well aware that it would continue such negotiations directly with Kraft after it. In the course of his cross-examination, Mr Welham confirmed as accurate the following paragraph in Deloitte's Defence to the FRC's Formal Complaint:

> *"…it is admitted that Deloitte and Mr Knights were aware (a) that Capax's principal role was to allow Autonomy to complete a sale and for revenue to be recognised in the quarter in which the Kraft deal was negotiated because it could not be formally completed with Kraft in that quarter, and (b) that Autonomy were negotiating directly with Kraft."*

114. It was clear also from Deloitte's working papers that Deloitte did not consider that either the fact that Autonomy had brought Capax Discovery in when the direct deal could not be closed, or the fact that Autonomy was negotiating with Kraft after the sale, affected the genuine commerciality of the agreement, or whether revenue should be recognised. Indeed, it appears that Deloitte took some comfort from Autonomy's continuing involvement in the negotiations with the end-user, in that it reassured them on the collectability issue; the Deloitte spreadsheet records:

> *"Note that we have also seen an email from Joel Scott ... that contained draft professional service contracts between Autonomy and Kraft, thus evidencing that the two parties continue [to] negotiate in good faith and that the deal is progressing.*
> *Given that we have seen evidence that directly links Autonomy and Kraft, both pre and post the deal with Capax, we conclude that there is satisfactory evidence to support the fact that Kraft are the end-user. As such, we conclude that this amount is recoverable, on the basis that*

> *Kraft are a multi-national blue chip company, who will be able to pay Capax for the purchased licence."*

115. Mr Welham's reservation appears to have been that if Autonomy were under what he called a *"performance obligation"* to close the deal, that might suggest that perhaps risk had not passed. This was a matter taken up in my own questions after his cross-examination, and Mr Welham explained that if the VAR:

> *"…habitually had an agreement, albeit not written down but verbally, where Autonomy would sell to the VAR but the VAR would be under the understanding that Autonomy close the deal, that would be different to our understanding at the time and that would suggest to me that perhaps risk hadn't passed"*

But he then continued:

> *"But the trouble with accounting is that, perhaps unlike law, it's never really black and white. There's a lot of judgment involved."*

116. In supplemental questions after mine, Mr Miles asked Mr Welham to elaborate as to what he meant, in the context, by the notion of a *"performance obligation"*. After some rather vague answers appearing to suggest that it would depend on the level of involvement required of the VAR and the seller, he reiterated that ultimately it was a matter of accounting judgement, and would depend on the extent and nature of the seller's involvement. As to that, he said that although *"some involvement may well be OK",*

> *"…I think extensive would be more problematic."*

117. Mr Miles pressed him on this, given that Deloitte had actually seen evidence of extensive continuing involvement but had not expressed concern. Mr Welham answered:

> *"You can have isolated cases. Clearly, <u>if you take Kraft as an example, the deal with the end-user was very, very close to completion, so I'm not sure you would need extensive involvement because it's so close.</u> I can't remember the specifics of the Eli Lilly deal[10], but <u>I think if it were always the case that there was extensive involvement in closing a deal, then that would be a problem, yes."</u>* [My underlining]

118. Mr Miles pressed again:

> *"Q. Going back to my point about whether Autonomy was* [under] *some sort of obligation, leave aside for a minute the question whether that's a legal obligation or not, so I'm not assuming that it's a legal obligation. But as between the parties, the VAR is, as it were, saying that it's for Autonomy to do, to close a deal.*
>
> *That's one case, but take a case where it's something Autonomy may well choose to do because it's got a good relationship with the end-user, the end-user wants to speak to Autonomy about the technology and so on, so there are*

[10] See paragraphs 133ff below.

good commercial reasons, if you like, for Autonomy continuing to deal with the end-user, again, in that case, it's all a matter of judgment, isn't it, on the particular facts and a matter of nuance?

A. Yes, so I think what you've described there is a little bit different to what we were talking about before. If there's continuation of involvement because of commercial reasons, and it's more assisting the sales process and the close process that the VAR is doing, then I think that's where it's more nuanced and there's judgement involved, but that's a little bit different to what we're suggesting where it's the obligation or sole responsibility of Autonomy to close. That's quite different.

Q. Yes, and that's a different case?

A, Yes, agreed."

119. I have dwelt on these answers because they seem to me to demonstrate that the Defendants' point – well made, as far as it goes – that Deloitte knew of Autonomy's involvement in discussions with Kraft after the VAR sale does not, on analysis, go very far. In particular:

(1) It seems clear from Mr Welham's approach that Deloitte did not know that the negotiations were proceeding solely between Autonomy and Kraft, to the exclusion of the VAR: and there was no evidence to suggest that they did;

(2) Nor is there anything to suggest that they were aware that Autonomy was negotiating in reality on its own account with a view to a direct contract; and

(3) The points above have additional power given Mr Welham's singling out of Kraft as a deal where the deal was so close that extensive further involvement would be difficult to justify.

(4) Furthermore, Deloitte assumed that the object of Autonomy's involvement was to conclude a sale by the VAR: but (as I find) the objective throughout was a direct deal, and the fiction that at the last moment Autonomy's old customer suddenly determined it wished to deal with Autonomy rather than the VAR is just that – fictional. Although in an email dated 28 December 2009 to Mr Scott and Mr Egan, Mr Hussain (in response to a question whether Mr Hussain was aware of repayment arrangements with Capax Discovery in respect of the Kraft deal after conclusion of the contract between Autonomy and Kraft) wrote that *"Kraft decided to reissue the order direct to us for the same amount as Capax – strange but I guess they decided it was too strategic a project for them to buy the software from a partner"* it was not in the circumstances *"strange"* at all.

120. As to (4) in paragraph 108 above, the issue as to whether Deloitte knew of the side agreement or understanding pleaded by the Claimants is of course premised on there having been one in the first place; but I have concluded that there was, whether described as understanding, agreement or shared intentions and expectations. Plainly, Deloitte knew nothing of that and was never told of any such thing.

121. As to (5) in paragraph 108 above, it appears that Deloitte reviewed the VT3 deal and were in fact aware of, and saw no problem in, the cancellation of the VAR sale, repayment to

Capax Discovery of its deposit, and the payment to it of a MAF. Various internal Deloitte documents confirm this, including a Memorandum dated 22 January 2010, the stated objective of which was *"To summarise the facts surrounding the sale to Kraft (using Capax Discovery) in Q3 2009 and the subsequent deal signed directly between Autonomy and Kraft in Q4 2009"*. An extract from the Memorandum, which also records as being Deloitte's main concern the need to ensure *"that only one amount of revenue has been recognised over this deal in the year…",* reads:

> *"This was a deal where Autonomy had been negotiating directly with Kraft throughout Q3 2009 but due to time constraints the deal could not be signed directly before quarter end….. During Q4 2009 Kraft expressed a willingness to sign the deal directly with Autonomy rather than through Capax. As such, Autonomy negotiated a fee with Capax to purchase the contract off them so that a deal could be signed directly between Autonomy and Kraft. In exchange for this right, Autonomy agreed to pay Capax $0.4M and waive Capax's contractual obligations to Autonomy under the original contract.*
>
> . . .
>
> *We conclude that as no additional revenue has been recognised in Q4 2009, the year-end debtor position has been corrected and the full year revenue position is correct that this accounting treatment is satisfactory."*

My assessment of VT3

122. Some of my conclusions with respect to VT3 will by now be apparent. However, in summary:

(1) The Kraft deal/VT3 provides, in my judgment, a very clear example of the use of a VAR as a placeholder, the VAR being intended and expected to do nothing and pay nothing from its own resources (as is the most arresting characteristic of all the impugned VAR deals).

(2) That use is clear from the oral evidence, from the way VT3 proceeded (with the VAR entirely excluded from the process and eventually entirely by-passed except when it came to arrangements to compensate it for its nominal role), and from what Deloitte were not told.

(3) Although the Defendants emphasised and relied on the apparently informed approval given by Deloitte after obviously careful and fully documented consideration of the transaction, Deloitte were not told and did not know any of the matters referred to in (1), which, in my judgment, cast a fundamentally different light on the nature and substance of the transaction.

(4) Had Deloitte appreciated those matters, I have no real doubt that they would have determined (a) that in economic substance there was no sale, (b) that notwithstanding the position in law, in reality Autonomy was in full control of the software to be sold to Kraft, that if no sale eventuated Autonomy would have somehow to reverse the VAR transaction or in some other way rescue the VAR from the legal *"hook",* and that the risk of a sale not eventuating was its risk, so that (c) the criteria of IAS 18.14 might apparently be, but were not actually,

satisfied so that no revenue should be recognised from VT3 at the stage of the impugned VAR sale. Mr Welham was clear in his oral evidence that:

> *"….the standard requires you to consider the substance of what the transaction is. So although you might have a legal document, if there is persuasive evidence that any arrangement exists then that would be relevant."*

In my judgment, on the facts, it was both relevant and determinative.

(5) Even taking into account a generous margin of appreciation, it does not seem to me that revenue recognition of the VAR sale in VT3 can be justified.

Particular points on the Defendants' involvement and knowledge of VT3

123. The question then, as ever, is whether the Defendants or either of them had "guilty knowledge". For the present, I note only the following factual matters specific to the VT3 transaction which may be of relevance in my assessment of the allegation that the Defendants knew the VAR sale was not in reality a sale at all and/or that its accounting treatment was improper.

Mr Hussain

124. As regards Mr Hussain, the Claimants relied especially on the following:

(1) As may be seen from paragraph 95 above, the introduction of a VAR to enable revenue recognition in Q3 2009 notwithstanding the delay in closing the end-user deal with Kraft was Mr Hussain's *"idea"*.

(2) It was Mr Egan's evidence that:

> "*At Mr Hussain's direction I approached Mr Baiocco…with a proposal..[for] Capax Discovery to act as a VAR, to submit a purchase order for a Digital Safe licence for onward licencing to Kraft, and to agree to pay $4 million for that software…I followed the guidance that Mr Hussain gave me…"*

(3) Mr Hussain was clearly conscious of the need to persuade Deloitte that the $4.2 million debt was collectable from Capax Discovery in light of Capax Discovery's other payment obligations to Autonomy, including its outstanding indebtedness under the TXU sale, and its continuing commitments in respect of the first Capax Discovery/EDD sale; and he was closely involved in the process of persuading them. That involved very selective disclosure: for example, Mr Hussain was aware that Capax Discovery was up to date on the Capax Discovery/EDD transaction only because Autonomy had sent it cash for non-existent EDD services; and that Autonomy had in effect funded Capax Discovery to pay the deposit on the Kraft sale which was intended to present a picture of independent credit-worthiness.

(4) Indeed, the Claimants contended that it was again Mr Hussain who master-minded and oversaw the alleged channelling of funds (amounting in all to $1,000,000) to Capax Discovery to enable it to pay down its existing debt before undertaking VT3 and (to quote from the Claimants' closing submissions) to:

> *"enable Autonomy to present Capax Discovery to Deloitte as a counterparty that was complying with the payment schedule in its prior deal."*

(5) Mr Hussain was well aware that Autonomy was negotiating with Kraft, to the exclusion of Capax Discovery and with the objective of completing the sale which had been nearing completion before the end of the quarter. Mr Egan also said in an unchallenged part of his witness statement that it was only <u>after</u> Autonomy's deal with Kraft was complete that he asked Kraft's representatives if Kraft would be willing to take its licence from Capax Discovery or to pay Capax Discovery as Autonomy's designated payee. His evidence was that *"Kraft was unwilling to involve Capax Discovery in any capacity"* so that *"…we had to find another way to make Capax Discovery whole, consistent with the intent of the deal we had agreed with Mr Baiocco."* Mr Egan added that (a) Mr Hussain approved all the ensuing arrangements to return Capax Discovery its $400,000 deposit and to pay it its 10% ($400,000) "profit"; and (b) though Mr Hussain stated in an email of 28 December 2009 that *"the referral fee should be paid to capax…as it was contracted"* the truth was that Capax Discovery did not refer Kraft to Autonomy and the $400,000 was not a referral fee: as Mr Hussain well knew, it was a fee for signing a purchase order "at risk" to enable Autonomy to recognise $4 million revenue in Q3 2009 in accordance with Mr Hussain's *"idea"*.

125. I have concluded that Mr Hussain must have been aware of the true nature of VT3, that Capax Discovery was a compliant placeholder, that Autonomy's true customer was Kraft, and that the only true sale ever envisaged was a sale direct to Kraft. He was a trained accountant. He must have known this was wrong. I find that he did.

Dr Lynch

126. As regards Dr Lynch's knowledge in relation to Kraft:

(1) Overall, his position was that he *"didn't know anything about what happened on the ground in Kraft."*

(2) His position emerged more elaborately from a sequence of answers to questions in cross-examination, as follows:

> *"Q. You knew that Capax Discovery had been given the assurance described by Mr Egan in order to get it to agree to enter into a contract to buy from Autonomy the software for Kraft, didn't you?*
>
> *A. I did not know that. Mr Baiocco confirmed that he thought he was on risk, so he obviously didn't consider that to be the case. And thirdly, he was capable of reading the contract.*
>
> *Q. And you knew in particular that Capax Discovery had been told that Autonomy would do everything it could to avoid Capax having to dip into its own pocket to pay for the software if an end-user deal failed to eventuate?*
>
> *A. No, I didn't.*
>
> *Q. You also knew that Capax Discovery had been told that*

> *Autonomy would continue its efforts to close the deal with the end-user?*
>
> *A. I didn't know that, no.*
>
> *Q. And you knew that Capax Discovery would not be making any efforts to close a deal with the end-user?*
>
> *A. No, I didn't know that.*
>
> *Q. You knew that the VAR was not in reality taking the significant risk of ownership of the goods?*
>
> *A. No. The VAR -- you know, I wouldn't have gone away and looked at the purchase order, but all our purchase orders were the same and they were absolutely clear: they owned the goods and they were on risk.*
>
> *Q. You also knew, following the VAR deal, that Autonomy retained continuing managerial involvement or control of the goods?*
>
> *A. No, I didn't.*
>
> *Q. And you knew it wasn't probable that Capax Discovery, a new company, would pay from its own resources for those goods?*
>
> *A. No, I would have expected and I understand my finance department did do that test and that was checked by Deloitte and the judgment was correct.*
>
> *Q. You well understood that it was wrong for Autonomy to recognise the revenue on this Capax Discovery transaction, correct?*
>
> *A. No.*
>
> *Q. And you knew that the same was true of all the subsequent VAR deals with Capax Discovery that are at issue in these proceedings?*
>
> *A. No."*

(3) He was made aware by Mr Hussain by email dated 25 September 2009 that the Kraft deal was unlikely to close that quarter, and he understood that this *"increased [the] risk"* of Autonomy having a shortfall on its revenue target for Q3 2009. He did not recall seeing Mr Hussain's email about his *"idea on Kraft"* but accepted that *"there would have been some communication, I assume, yes"*. He said that he would have regarded it as perfectly normal to use a VAR in such circumstances. He would have expected Capax Discovery to be getting involved because *"by getting a reseller involved in a deal, it gave them the ability (a) to introduce themselves to the end-user, if they weren't already, and (b) it meant that they could then do services"*. He referred in that context to "Capax Discovery" as *"our largest services partner in terms of number of engagements"*.

(4) He had no basis for disputing Mr Baiocco's evidence that the purchase order was drafted entirely by Autonomy. He did not see the Capax Discovery purchase order at the time, nor any of the other paperwork, and so it was unlikely he would have known of the restriction on any onward sale by Capax Discovery except to

Kraft: but he expressed his view that if despite Autonomy dealing directly with Kraft, Capax Discovery had been required to fulfil its payment obligations under the purchase order, Autonomy would no doubt have taken a commercial decision to allow Capax Discovery to sell to other end-users.

(5) He would *"probably have known shortly after quarter end"* of the VAR deal (VT3) and *"quite possibly"* proceeded on the basis that the VAR deal was for essentially the same amount as the Kraft deal.

(6) When questioned as to the ability of Capax Discovery, as a newly-formed entity, to have any means of paying, and how Deloitte were to be persuaded of collectability, he stated that he thought *"the reason they would have been reassured was the 400,000 that was paid on signing"* but when asked whether he knew that was using Autonomy's money, he said he did not know where the money would have come from.

(7) He told me he did not know whether Mr Egan had said to Mr Baiocco that Autonomy would deal with and close a direct deal with Kraft and would then get Kraft to pay Capax Discovery so that in turn Capax Discovery could pay Autonomy; but in any event, that did not strike him as *"problematic"*.

(8) He said he had no *"first-hand knowledge"* that Autonomy was negotiating directly with Kraft to conclude a deal after the VAR sale and was not able to say whether Capax Discovery had been involved at all in those negotiations; but he seemed to me to accept (albeit remonstrating that he could not police every meeting, and it was the reseller's choice if it did not participate) that the impression he gave in his witness statement, and which was given to Deloitte, was that Autonomy was only seeking to help Capax Discovery to close a deal. He saw no difficulty either way: *"…if I'm wrong, then fine"*.

(9) He said he did not know that Kraft had refused to agree to pay Capax Discovery and was not consulted about the cancellation of VT3 after Autonomy's direct deal with Kraft: he said that he assumed *"it would have gone to the level of Mr Hussain and perhaps Mr Kanter."*

(10) He defended the payment of a MAF for going on risk, even if in the event the reseller did no more and was never called upon, saying *"You've got to at least give them some compensation for that situation"*; but he did not recall whether he had been specifically consulted about the $400,000 payment to Capax Discovery.

127. Dr Lynch also made the following, for the most part more general, observations in the course of cross-examination:

(1) He told me he did not know what Mr Egan and Mr Baiocco had discussed before striking the deal, nor what guidance Mr Hussain had given Mr Egan, but said:

> *"I think Mr Hussain would have been happy with the normal industry general warm comments that are given. I don't think Mr Hussain would have said anything more than that."*

(2) He added:

> *"…as the CEO of the company sitting in London, what I rely on is the fact that no matter what the sales guy says that I can't control in a meeting on the other side of the world in a closed room with someone, the paperwork is absolutely clear, which is: you're on risk, you're going to have to pay us, and this piece of paper contains all the terms of the deal. If ever there was a dispute, they would lose, they would have to pay us.*
>
> *If Mr Egan said more than warm words, then he wasn't authorised to do that. But also Mr Baiocco is not an idiot. He knows perfectly well that that's worthless."*

(3) Equally memorably, he observed:

> *"I think you can't legislate against hope. For good commercial reasons the reseller would hope that in the case of something going wrong, that the vendor would try and help them, but the vendor is under no obligation to do that, other than the reputational damage of being seen to leave a reseller in the lurch."*

128. These two passages seem to me to encapsulate Dr Lynch's position in these proceedings as to how he perceived this transaction and, more generally, Autonomy's use of VARs and what he would have understood the understandings of the parties to be. Dr Lynch consistently maintained that whilst Mr Egan may have given assurances that fostered and encouraged the hope and belief in the VAR that the risk was worth taking and that if the worst eventuated, Autonomy would do all it could as a business partner to assist, he knew of nothing that had been said to indicate, and would have regarded it as unauthorised to indicate or invite the understanding, that the VAR would be taking anything less than the significant risks and responsibilities of ownership and managerial control over the goods. He was clear that he would have expected Mr Baiocco, and all VARs, to have understood they were bound, and whilst they might hope for assistance, they could not depend on release: none of them was *"an idiot"*.

129. Dr Lynch expressed himself with cogency and conviction. He seemed to me to have persuaded himself by the time of trial of the truth of what he said, and in particular, that VT3 was in the general run of VAR deals not impugned in these proceedings which Autonomy had been undertaking for many years. His reference to not legislating against hope carried real force in general terms; I do not, however, accept his evidence.

130. VT3, like the other impugned VAR sales, was not in the general run of deals. The impugned sales were marked out by features which inexorably and fundamentally distinguished them, as the Claimants' case identified. Capax Discovery was not proceeding on the basis of hope; it was proceeding on the basis of a settled understanding which was a basic feature of all the impugned VAR transactions, which would have been far too rich a commercial risk without it. Dr Lynch had no real answer to these special features and the sales' lack of substance which they revealed: the probability is, and I find, that he did know of them, as I have found Mr Hussain plainly did.

131. I accept that in the context of VT3 and more generally, there is little direct evidence of any direct and express conversations between Mr Hussain and Dr Lynch relating to the terms of the sales or how matters proceeded after an impugned VAR sale. Again,

however, it seems to me much more likely than not that they shared the same understanding of a strategy which was becoming so essential to them. The same considerations and factors as I have set out in relation to VT2 apply in the context of VT3 (and indeed all the impugned VAR transactions).

132. Put shortly, I have concluded that Mr Hussain knew, and that it is more likely than not that from him, Dr Lynch would have known if he could not see for himself (which I suspect he could), that in VT3 and those other sales the VAR was (a) a 'best friend' (b) resorted to (as it well knew) as an urgent expedient (c) to whom a considerable *"champagne smacking"* fee would be paid (d) to take on a legal obligation on paper which each was assured would not be enforced but which (e) could not have sensibly taken on such an existential risk without more than usually warm comfort and in any event, (f) had not the resources itself to pay and which (g) where necessary to persuade Deloitte of collectability, had been put in funds by Autonomy through purchases with that as at least part of their aim, and which (h) was never expected, or intended, or itself expected or intended to, or ever did, pay (out of its own resources) or do anything.

VT4: Capax/Eli Lilly (Q4 2009)

133. I turn to the next impugned VAR transaction to which Autonomy Inc and Capax Discovery were the parties, in respect of which the prospective end-user was the pharmaceutical company Eli Lilly, another large existing customer of Autonomy. The VAR transaction was entered into on the last day of Q4 2009.

134. VT4 was another big transaction: the licence fee for the purchase order was $5,986,827, plus a support and maintenance fee of $299,342. The software sold was a *Licensor Archiving Solution*, which included Digital Safe, Digital Safe Retention-Deletion and Digital Safe Audit Center Software, as well as Aungate Legal Hold and Aungate Real-Time Policy Management.

135. As in the case of VT2 and VT3, the sale was under the June 2009 Capax Discovery VAR Agreement. I have set out the most relevant terms of that agreement in paragraph 60 above; but in summary the agreement made clear that the reseller was obliged to pay (and was not relieved by any non-payment by the end-user), that the agreement comprised the entire agreement between the parties and that there could be no valid modifications without following the stipulated formalities. According to the terms of the contractual arrangements, therefore, the legal risk of ownership had passed, and managerial control was not retained.

136. In terms set out in Exhibit "B" to the purchase order, the *"End-User"* was defined as Eli Lilly. As in VT3 (Kraft), the *"Authorised Use"* was restricted (to use by that end-user; so Capax Discovery had no contractual right to sell the software to any other end-user if no deal with Eli Lilly eventuated. The purchase order stated that payment in full was to be made within 90 days (so, by 31 March 2010). Capax Discovery did pay a deposit of $400,000; but it did not make any other payment by 31 March 2010.

137. This was another impugned VAR transaction which was not followed by an onward sale by the VAR. Ultimately, on 15 June 2010, Autonomy entered into a direct deal with the end-user, under the terms of an agreement which provided for Eli Lilly to pay Capax Discovery as Autonomy's designated payee. The direct sale to Eli Lilly was for the same

software, but at the lower licence fee of $5,303,431 plus support and maintenance fee of $265,172.

138. Again, the Claimants alleged non-compliance with IAS 18.14(a) (they submitted that there was in substance no transfer of risk of ownership); with IAS 18.14(b) (they contended that Autonomy in substance retained managerial control of the goods); and IAS 18.14(d) (they alleged there were grounds for doubting collectability).

139. The Claimants submitted that:

(1) Capax Discovery was introduced as a VAR on the very last day of the quarter as a response to Autonomy's urgent financial response to a delay in closing a direct deal between itself and Eli Lilly, and with no time for Capax Discovery to assess the prospect of an end-user deal eventuating, or to negotiate on price or other terms.

(2) The large amounts involved made it especially important for Autonomy to establish a transaction from which revenue could be recognised. Failure to secure the revenue from it in Q4 2009 would have materially reduced quarterly earnings and imperilled the achievement of the market expectations for that quarter.

(3) The evidence of Mr Baiocco that the purchase order *"was drafted for us by Autonomy"* and that Capax Discovery *"had no dealings with Eli Lilly before it issued its purchase order and did nothing to try to sell software to Eli Lilly after it issued its purchase order"* was not contradicted, except to the extent of a bare (though four-times repeated) assertion by Dr Lynch that he had *"seen information"* that *"Capax were actually working inside Eli Lilly at this point anyway"*. Nor was the evidence of both Mr Egan and Mr Baiocco that Capax Discovery would not be required to participate in the continuing negotiations for a sale to Eli Lilly and played no role in discussing the terms of the direct sale eventually agreed, contradicted either.

(4) Capax Discovery acted simply as a *"placeholder"* for a fee (10% of the total contract price, and so in excess of $600,000), having been assured (so it was alleged) that Autonomy would require nothing from it, and (apart from a $400,000 deposit for which Autonomy would indirectly provide the funding) would require payment only if and when the end-user deal was closed, again consistently with the assurance alleged.

(5) The Claimants referred also to email exchanges when Autonomy's accounts department pressed for payment. Mr Baiocco is reported as having said that Capax Discovery was *"waiting for payment from Eli Lilly and once they get the payment Capax will issue a payment to Autonomy".* When Mr Baiocco complained to Mr Egan about being chased Mr Egan responded *"Got your message. The calling will stop."* Mr Baiocco forwarded that response to one of his business partners, with the comment, *"Fyi this is autonomy CEO telling me not to worry about the collection calls!!!",* which the Claimants also relied on as signifying that Mr Baiocco relied on Mr Egan having the authority of a CEO.

(6) As it was, Capax Discovery did not pay until after the direct deal was closed; but it did pay as soon as it received Eli Lilly's payment to it as Autonomy's *"expressly designated payee"*.

140. Against all this the Defendants again relied on (a) the evidence of Mr Egan and Mr Baiocco, both generally as regards the Capax Discovery VAR transactions and with particular reference to VT4, that they well appreciated that Capax Discovery was genuinely at risk, and nothing that Mr Egan did could alter this, and that there was no side agreement or understanding that impacted on revenue recognition; (b) the contractual terms including the entire agreement clauses, as well as the strict instructions to sales employees prohibiting side agreements and understandings; (c) Mr Baiocco's evidence specifically confirming that he saw the reseller deal with Autonomy as a way of becoming an approved vendor of professional services to Eli Lilly, even though in the event his objective was not achieved; (d) the fact that Deloitte carefully reviewed the accounting for the transaction at the time and were satisfied with the revenue recognition; and (e) the fact that Deloitte reviewed the accounting treatment afresh in the light of Mr Hogenson's allegations (as to which see paragraphs 2232 to 2289 in the main body of the judgment) and continued to be satisfied that the revenue was correctly recognised.

141. Further as to (d) and (e) in paragraph 140 above, the Defendants emphasised that:

(1) Deloitte had considered shortly after the reseller deal had been entered into that there was a real prospect that this deal would end up going direct. They concluded that this did not bar the revenue recognition. Mr Welham told me in cross-examination that his perception was that a direct deal was a risk but not his expectation: and went on to suggest that had it been his expectation then that might have precluded revenue recognition. However, in his almost contemporaneous email (dated 16 January 2010) to Mr Knights he stated that he *"would expect that both Eli Lilly and Morgan Stanley will go direct to Autonomy during the course of Q1 2010"* and in the next paragraph recorded that he understood from Mr Chamberlain that *"what I have described above may well happen"*.

(2) Mr Welham confirmed that Deloitte knew that the Autonomy/Eli Lilly agreement allowed Autonomy to designate a payee to which Eli Lilly should submit a purchase order and pay fees. They knew that Autonomy had directed that Eli Lilly should submit its POs and pay its fees to Capax Discovery, and that Capax Discovery would in turn pay Autonomy in fulfilment of its obligations under the June 2009 Capax Discovery VAR Agreement.

(3) Mr Welham also (in cross-examination) confirmed as correct the following extract from Deloitte's Defence to the FRC Formal Complaint:

> *"…Mr Hogenson raised queries in respect of transactions, including Eli Lilly, and these were treated with appropriate scepticism by the audit team. It was because of Deloitte's earlier work which had already been carried out with heightened scepticism and enhanced procedures that Mr Hogenson's queries were not alarming: these issues had already been the subject of careful consideration."*

(4) This was one of the transactions specifically queried by Mr Hogenson (see paragraph 2264(1) in the main body of the judgment). His queries in relation to the Eli Lilly transaction were not seen by Deloitte as alarming, because the issues raised had already been the subject of careful consideration by Deloitte.

(5) Deloitte's summary of their views on this transaction after seeing and investigating Mr Hogenson's complaints about it included the following:[11]

> *"We have discussed and reviewed management's views on the matter as summarised above and concur with the accounting policy in place. The determination of the revenue recognition of the Capax sale as at 31 December 2009 is consistent with our understanding of this transaction at that time."*

142. As they did in the context of VT3, the Claimants contended that Deloitte were knowingly misled by the Defendants about the true nature of VT4. They relied especially on draft responses to Deloitte's request to Autonomy management to justify the recognition of revenue on VT4, which Deloitte sent after receiving Mr Hogenson's letter dated 26 June 2010 raising concerns about possible false accounting in respect of the Eli Lilly transaction (see paragraphs 2232 to 2289 in the main body of the judgment). These draft responses were prepared by Mr Hussain, and sent in draft to Dr Lynch, Mr Kanter and Mr Chamberlain, before Mr Hussain sent them on (in substantially the same form) to Deloitte attached to an email dated 5 July 2010.

143. I set out below the assertions in the draft response to Deloitte on which the Claimants particularly relied, the Claimants' submission in respect of them, followed in each case by the Defendants' response:

(1) The Claimants first criticised the assertion that:

> *"Additionally management were aware that an ultimate end-user was identified - Eli Lily ["Eli"] who are a major multi-national business that had a track record of purchasing Autonomy software ($22m). Indeed Autonomy had spent some time seeking to sell this product direct to Eli before ultimately selling it to Capax. The key feature that Capax was able to offer to Eli was an ongoing partner/servicing arrangement."*

As to this:

(a) The Claimants submitted that this assertion was false for two reasons: (i) that it gave the impression that it was the introduction of Capax Discovery that assisted the end-user sale, whereas there is no evidence that Capax Discovery's willingness to offer services to Eli Lilly had anything to do with the matter; and (ii) that in fact, since the licensed software was Digital Safe which was to be hosted, along with Eli Lilly's data, in Autonomy's data centre, Capax was not in any position to offer any services.

[11] Mr Welham suggested in his witness statement that he did not see Mr Hogenson's complaint as amounting to an allegation of improper conduct by management.

(b) The Defendants sought to counter this submission on the basis that the assertion was fair: Capax Discovery was able to offer Eli Lilly an ongoing partner/service arrangement, especially in respect of the elements of the package sold other than Digital Safe; and Mr Baiocco himself confirmed in cross-examination that he had entered into the reseller deal with the aim of providing professional services to Eli Lilly and becoming one of its approved vendors. Although this objective was not realised, Mr Baiocco firmly believed in the opportunity, certainly did not believe that Capax Discovery had nothing to offer, and continued to pursue it even after the direct deal, as shown by his email to Eli Lilly dated 23 August 2010 (which I interpolate should be noted to be some time after the direct sale) asking for a meeting and stating:

> *"The biggest reason I have been calling you, is to get connected as a vendor to Lilly. I can promise you, that if you get us in front of your folks, we will blow them away with our capabilities in both the MS [Microsoft] and Discovery/Autonomy lines."*

(2) The Claimants criticised also the assertion that:

> *"There were ongoing conversations between Eli and Autonomy as Eli remains a significant customer although it was expected that Capax and Eli would be in contract as at 31 December 2009. These conversations resulted in a revised agreement with Eli and Autonomy in June 2010, though the agreement provides for Capax to invoice Eli directly and, importantly, Capax remain fully liable to Autonomy for the obligation established under the original PO."*

As to this:

(a) This too, the Claimants submitted, *"included lies"*, in that Autonomy management had no expectation that Capax Discovery and Eli Lilly "*would enter into a contract*" by 31 December 2009. They had entered into the Capax Discovery transaction precisely because Autonomy could not reach agreement with its long-time customer, Eli Lilly by the end of Q4 2009. Capax Discovery was not even approached by Autonomy until 31 December 2009; and Capax Discovery never even tried to sell a licence to Eli Lilly. The transaction with Capax Discovery had been concluded solely as a means of enabling Autonomy to meet its revenue target for Q4 2009.

(b) The Defendants accepted that this assertion (which was made some time later in similar form in a letter to the FRRP)[12] was *"not precisely phrased"* but submitted that *"Everyone knew that the deal between Capax and Eli Lilly had not been done by that stage"*, and the assertion should be interpreted sensibly as signifying an

[12] See Autonomy's letter to the FRRP dated 3 March 2011 in relation to investigations made by the FRRP after Mr Hogenson had raised concerns: and see paragraph 2304 in the main body of the judgment.

expectation that there would in the future be a contract between Capax Discovery and Eli Lilly, not that one had already been made.

(3) Thirdly, the Claimants criticised the assertion that:

> *"We have discussed and reviewed management's views on the matter as summarised above. Their determination of the revenue recognition on the Capax sale as at 31 December 2009 is consistent with our understanding of the original transaction at that time.*
>
> *As a result of unforeseen circumstances arising in Q2 2010 we understand that additional work was involved on this transaction as summarised in the information from Brent [Hogenson] and as explained above. As these events took place in 2010 this information was not known as at the time of completing the 2009 group accounts and accordingly adjustments, if any, would fall to be treated in 2010."*

As to this:

(a) The Claimants submitted that this too was false: it proceeded on the basis that something unforeseen had happened in 2010 that was not known about as at 31 December 2009, whereas in fact, what happened was always foreseen (including especially that Autonomy would continue negotiating directly with Eli Lilly, regardless of the VAR transaction).

(b) The Defendants did not address this specifically in their written closing submissions; but they asserted generally, and both experts accepted, the need to assess revenue recognition as at the date of the VAR agreement, and not by reference to events afterwards; and they rejected the notion of there being anything improper in Autonomy continuing to negotiate with the end-user.

144. The Claimants also relied on Autonomy's responses to the FRRP in March and June 2011, when it too asked Autonomy's management for their response to Mr Hogenson's allegations about VT4. I set out below the assertions relied on by the Claimants as being false, and again I summarise, in respect of each of the Claimants' arguments, the Defendants' counter-arguments:

(1) The Claimants referred to Autonomy's response dated 3 March 2011 to the FRRP's letter dated 2 February 2011 as follows:

> *"It was expected that the VAR and end-user would be in contract as at 31 December 2009. However due to evolving regulatory requirements, conversations between Eli Lilly and Autonomy resumed in 2010, resulting in an agreement between Eli Lilly and Autonomy in June 2010. This was accommodated because of the relationship between the companies with Autonomy as a key supplier."*

As to this:

(a) The Claimants submitted that these *"were further, deliberate falsehoods"* on the basis that, in reality, the Defendants never expected Capax Discovery to contract with Eli Lilly, whether by 31 December 2009 or at all. They invited me to reject Dr Lynch's evidence in cross-examination in this regard as unconvincing. Further, they submitted that it was not some unforeseen *"regulatory"* issue which resulted in direct contact being *"resumed"*: rather, it had been the intention all along that Autonomy would deal directly with Eli Lilly.

(b) The Defendants offered the same explanation for the *"not precisely phrased"* language as they had in relation to the draft response to Deloitte; and although they accepted that Autonomy had always intended to carry on negotiating with Eli Lilly (as they considered, as did Deloitte, to be both proper and commercially of obvious sense and advantage), they again rejected the suggestion that a direct deal had been intended all along.

(2) The Claimants then also criticised Autonomy's response (by letter dated 8 June 2011) to the FRRP's follow-up letter dated 5 April 2011 asking for an explanation as to *"why Eli Lilly decided to contract direct with Autonomy rather than seeking to revise its contract with Capax."*

In that regard:

(a) The Claimants criticised Autonomy's reply that it was *"unable to comment further on the reasons that Eli Lilly decided to ultimately contract with Autonomy"* on the basis that *"No attempt was made to correct the FRRP's evident misapprehension."* Further, the Claimants criticised what Autonomy went on to say, which was:

> *"Under the terms of the subsequent direct agreement between Autonomy and Eli Lilly, Capax are a party to the contract and are invoicing Eli Lilly for the software."*

The Claimants submitted that this was untrue, since Capax Discovery was not a party to the direct agreement but was *"merely Autonomy's designated payee."*

(b) The Defendants rejected both criticisms, denying any need to say anything further about Eli Lilly's preference to deal direct (since they regarded that as ultimately Eli Lilly's choice even if it was always on the cards), and depicting that and (given that in effect the arrangement was tri-partite in that Capax Discovery became a *"designated payee"*) the following criticism as *"nit-picking"* and *"unfair"*.

(3) In conclusion, the Defendants rejected the Claimants' final salvo in this context that:

> *"the Defendants displayed no compunction about dissembling to the regulatory authorities"*.

145. The Claimants further relied on two other explanations or arrangements that they alleged were *"demonstrably untrue",* or fraudulent pretexts advanced by the Defendants to mislead Deloitte and the regulator. Both relate to the arrangements made after the direct deal for reimbursement of Capax Discovery and payment of a MAF:

(1) The first was a letter dated 30 September 2010 which Mr Kanter sent to Capax Discovery which described Capax Discovery as a *"Referral Partner"* and set out terms and conditions that purported to *"formalize our prior discussions."* These included:

> *"Referral Partner will: (1) introduce Autonomy into the deals with Eli Lily [sic] ("End-User"); (2) obtain quotes from Autonomy on behalf of the End-User; and (3) work with the End-User to assist in executing purchase orders and contracts with Autonomy.*
>
> *Autonomy will (1) pay Referral Partner commissions in the amount of $629,000 as a result of Referral Partner's direct and proximate participation in the account …".*

(a) The Claimants submitted that this was *"another work of fiction".* Capax Discovery had not, and was not expected to, introduce Autonomy into deals with Eli Lilly, or to obtain quotes from Autonomy on Eli Lilly's behalf, or to work with Eli Lilly to assist in executing contracts. Capax Discovery had nothing to do with the transaction between Autonomy and Eli Lilly. The natural interpretation, the Claimants submitted, was that this was a contrivance made necessary by the perceived need to avoid putting in to writing or in any way leading to the supposition that the real reason for the payment was that:

> *"Capax Discovery was being paid for providing documentation that enabled Autonomy to recognise revenue prematurely."*

(b) The Claimants also made the point that in opening they had made clear that Mr Kanter would have to explain what they regarded as this fabrication: but he had been subsequently withdrawn as a witness. They contended that the subterfuge was further compounded when, on 30 September 2010, Mr Hussain approved payment *"on the basis that we have a signed MAF".*

(c) Dr Lynch, under cross-examination, said he did not know whether he had approved this letter. He appeared to me to be somewhat flummoxed, stressing when asked what it was referring to that he was not a lawyer and was *"just reading this cold here".* He suggested that the letter (and the payment for which it provided) appeared to him to be dealing, at least in part, with the future and the need to ensure that Capax Discovery did not use their introduction to Eli Lilly to compete with Autonomy; but although the letter did also contain what was in effect a non-compete stipulation, that explanation was not convincing in relation to the express wording that:

> *"Autonomy will pay Referral Partner commissions in the amount of $629,000* [equating to 10% of the deal already done] *as a result of Referral Partner's direct and proximate participation in the account…"*

(d) When it was put to him that *"Mr Kanter's letter is simply laying a false paper trail",* he disagreed and said that *"all that he's done is taken a standard MAF agreement"* and the letter appeared to him to look *"like a perfectly standard MAF paperwork…the normal paperwork we would use, something like that"*; but that did not explain its reference to Capax Discovery's *"direct and proximate participation".* Dr Lynch appeared discomfited; and his responses were not convincing.

(e) As it seems to me, Mr Kanter's perception of the need for such a letter does support the Claimants' case that at least he felt uncomfortable paying a MAF without (a) some written agreement and (b) the reseller having actively participated in the transaction in some way.

(2) Secondly, the Claimants relied on the steps taken to reimburse or protect Capax Discovery from liability to pay for the shortfall of some $700,000 between the VAR transaction licence fee (for which Capax Discovery remained legally liable) and the lower amount eventually charged by Autonomy to Eli Lilly in the direct deal. Again, the Claimants contended, it was Mr Kanter who devised a solution, which I have already dealt with in some detail above (see the section in the main body of the judgment where I deal with the Capax Discovery/EDD reciprocal transaction (RT1)), and again it involved pretence.

In summary:

(a) By email to Mr Hussain and Mr Egan dated 6 October 2010 Mr Kanter referred to *"experiencing bandwidth constraints on EDD processing"* as the basis for recommending (so as to *"ensure availability of service for customers"*) an *"increase in European EDD processing availability for Capax of 500GB per month for the next seven months"* at a price of approximately $100k per month.

(b) There is thus an exact coincidence with the amount of shortfall; and the coincidence in timing is notable also.

(c) Mr Egan stated in his witness statement that Mr Kanter had *"generated emails that created the appearance that Capax was actually providing overflow EDD services for Autonomy"* though he (Mr Kanter) knew that was not the case, and the emails were pre-textual. Mr Egan also referred to the fact that he *"knew that Mr Kanter and Mr Hussain had made similar pre-textual statements."*

(d) Mr Baiocco's evidence in his witness statement was that these payments were made following a proposal from Mr Egan and Mr Kanter that the shortfall be covered by Autonomy, though in cross-examination he clarified that he did not discuss the matter with Mr Kanter, at least until much later. Mr Baiocco further confirmed that:

> *"…Capax Discovery did not work on any 'European projects'. I believe that this documentation was simply designed to paper the payments by Autonomy to Capax Discovery to cover the shortfall on the Eli Lilly transaction."*

(e) This evidence was not really contradicted. Indeed, it will be recalled that at the commencement of his cross-examination when asked whether there were any matters that on reflection he felt were untoward, Dr Lynch singled out the issue as to the purchase orders and payments made to Capax Discovery for EDD services as his one area of concern that there might have been wrongdoing, although he insisted that he had no knowledge of this at the time, and did not accept that Mr Kanter and Mr Hussain had either. Dr Lynch told me that he did not think that Mr Kanter knew, or had any reason to know, that money was being sent to Capax Discovery for doing nothing because he sat:

> *"in a legal office in Cambridge, he doesn't go to the US, he doesn't stand in data centres and he's getting approvals from Mr Egan saying that the work has been done."*

(f) However, there is no doubt that Mr Kanter was involved in the process under which Autonomy contracted for Capax Discovery to provide the EDD services; and, for example, there was a statement on the face of the purchase order in question, *"REQUESTED BY: Andrew Kanter"*.

(g) When it was suggested to Dr Lynch that surely Mr Baiocco would not have failed to tell Mr Kanter that Capax Discovery was not doing any work, he denied this tersely, reasoning that if Mr Baiocco had told Mr Kanter that (in effect) he was defrauding Autonomy, Mr Baiocco would have been sued. When the riposte from Mr Rabinowitz was that this might be so unless, of course, there was agreement on a contrivance, including by Dr Lynch, Dr Lynch dismissed that completely.

(h) It would certainly have been helpful to hear from Mr Kanter on these points; but I did not, in circumstances I have previously explained. In his absence, and for reasons I have already given, I have concluded that the likelihood is that these arrangements were a contrivance orchestrated by Mr Kanter, and implemented by Mr Egan and Mr Baiocco, each of whom knew that at the time Capax Discovery was not able to provide the overflow EDD services it was purportedly issuing a purchase order in respect of, and being paid for.

(i) The Claimants submitted that whether or not Mr Baiocco, Mr Egan or Mr Kanter actually told Dr Lynch about the specifics (as to which see below) the contrivance was:

> *"entirely in keeping with the arrangement – which the Court should find Dr Lynch had authorised (or at the very least knew about and supported) – of ensuring that Capax Discovery was not left out of pocket, thus enabling Autonomy to call upon Capax Discovery as and when required to enable revenue to be recognised improperly."*

(j) I address the issue as to what the Defendants knew of this below.

146. The final episode of VT4 relates to the process by which, in the end, the $299,342 support and maintenance fee was dealt with, which the Claimants also relied on as the final implementation in the context of the transaction of the side agreement or understanding they allege, and improper accordingly. As to this:

(1) Capax Discovery never paid that sum, and Autonomy never threatened any recovery process.

(2) Rather, on 28 July 2011, Ms Helen Ku of Autonomy's finance department informed Mr Baiocco, copying Mr Chamberlain, that the outstanding balance on the Eli Lilly purchase order was $299,680. Mr Chamberlain forwarded this to Mr Hussain the same day, and said, "*Down to $300k which is the maintenance credit that I need to sort*". Mr Hussain responded, and did not dissent from, the notion that a credit should be given.

(3) Accordingly, on 8 August 2011, Autonomy issued a credit note to Capax Discovery in the amount of $299,342, effectively cancelling Capax Discovery's remaining payment obligation relating to the Eli Lilly deal. Mr Chamberlain approved the issue of the credit note.

(4) The Defendants dismissed the suggestion that this was improper as *"unreal"*. As with the Kraft transaction, after Autonomy had closed a direct deal with Eli Lilly, it was commercially sensible, and avoided counting the same revenue[13] twice, to issue a credit note in respect of the outstanding support and maintenance component, which Autonomy had instead committed to undertake for a commensurate fee.

(5) In the circumstances as they then were, plainly, the Defendants are correct that the revenue could not be counted twice, and the loose end of the VAR sale had to be tied up. But the Defendants' dismissal of any complaint about this last part of the process as *"unreal"* does not answer the overall picture painted by the Claimants, and which I accept as encapsulating the economic result, which was

[13] Is it the same revenue or is (1) revenue for software delivered via Automater to VAR, the other is revenue from sale of software presumably delivered by Autonomy directly to Lilly.

that as regards Capax Discovery's total debt of $6,286,169 under the Eli Lilly purchase order:

(a) Capax Discovery paid about $5.3 million using money which Autonomy was entitled to receive from Eli Lilly, but which Autonomy directed Eli Lilly to pay to Capax Discovery, so that Capax Discovery could, in turn, hand it over to Autonomy;

(b) Capax Discovery paid $700,000 using money which Autonomy channelled to Capax Discovery for fictitious services, so that Capax Discovery could then pay it back to Autonomy; and

(c) Autonomy cancelled Capax Discovery's obligation to pay the remaining $299,342.

147. In effect, the difference between the Claimants and the Defendants as to this was that the Claimants contended that outcome further justifies the inference that, at the time of the purchase order, Capax Discovery did not genuinely take the risk of having to pay $6,286,169 (or any amount) to Autonomy from its own resources; whereas the Defendants presented it as illustrating how far Mr Egan, Mr Baiocco, and Mr Kanter were prepared to go to preserve the goodwill of Capax Discovery and the VARs, and what Dr Lynch was fond of referring to as the *"ecosystem of resellers"* on which *"a company like Autonomy stands or falls…"* Dr Lynch put up an energetic case for the latter:

> *"So one of the crucial things is to make this ecosystem of resellers strong because not only do they bring you business, not only do they keep the competitors out, not only do they do the marketing for you, but they're also the ones that are there supporting the customers and doing the installations, so – and of course if they don't get the revenue through their books, they have to go and do it with competitors.*
>
> …
>
> *And you know, yes, I guess theoretically Autonomy could turn round and say, well, even though we sold it to you, we're going to sell it again, but in that case, as soon as the ecosystem heard about that, no one would trust you anymore, so there's a sort of mutually assured destruction in that situation."*

148. This was energetically put and well thought out: but I am not persuaded that it has anything much to do with the present case. Of course, a company in the position of Autonomy would not wish to let a reseller down; of course, it would not seek to extract a double revenue; of course, if a direct sale resulted, Autonomy would need to pay the VAR what, or substantially what, it would legitimately have expected had it re-sold, Autonomy having destroyed the prospect of an onward sale. But the result was the real purpose of the arrangements, and not an unexpected one, and I am persuaded that it conformed with the intentions of Autonomy and Capax Discovery all along.

149. In my judgment, therefore, the explanation offered by the Claimants is plainly the most likely.

150. In the round, I have concluded that VT4 lacked economic substance; the only real substantive sale was direct by Autonomy to Eli Lilly. In my judgment, no revenue should have been recognised from impugned VAR sale VT4; and the repetition of its features in subsequent sales is of general relevance and requires the like conclusion in respect of subsequent Capax Discovery sales accordingly.

Defendants' alleged knowledge of false accounting in respect of VT4

151. As to the second limb of their case, that the Defendants both knew that the inclusion in Autonomy's accounts and published information of recognised revenue from VT4 was misleading, the Claimants relied on the following:

(1) Their general or overriding case to the effect that the introduction of a VAR so late in the day, and only because of a delay in closing the intended end-user deal with Eli Lilly, and the fact that after the VAR transaction, Autonomy continued to conduct the negotiations which led to a direct sale by it to Eli Lilly (rather than an onward sale by Capax Discovery as the VAR to Eli Lilly as end-user) were ultimately directed by Mr Hussain and must have been known by Dr Lynch;

(2) The specific arrangements made for (a) Eli Lilly to make a payment, at Autonomy's direction, to Capax Discovery (rather than) Autonomy to enable Capax Discovery to discharge its indebtedness to Autonomy under its VAR transaction and (b) the payment of a MAF to Capax Discovery, though (as the Claimants saw it) it was not expected or intended to participate at all (so that it was merely a *"placeholder"*) were similarly known to, and known to be improper by, Mr Hussain, and it is to be inferred, also by Dr Lynch;

(3) The further arrangements to ensure that Capax Discovery was either held harmless in respect of, or given funds to discharge, any remaining indebtedness under the VAR transaction to which legally Capax Discovery remained subject by reason of the lower sums achieved in the direct sale were known by Mr Egan, Mr Baiocco, Mr Kanter, Mr Hussain, and by inference, Dr Lynch to be contrivances or (as the Claimants put it) *"works of fiction"*;

(4) The guilty knowledge of both Defendants being confirmed by the fact that they did, and perceived the necessity to, (a) neutralise Mr Hogenson and (b) mislead both (i) Deloitte and (ii) the FRRP and the FRC about the true nature of the VAR transaction and the ultimate direct deal.

152. The points in (1) and (2) above substantially relate to the same 'pattern' and reflect points already addressed in relation to VT3. I do not propose to repeat my assessment of them. I turn to address, however, (a) various matters that the dispute in relation to VT4 highlighted, and which have a more general significance to this and the other Capax Discovery impugned VAR sales; then (b) the question whether either of the Defendants knew that the arrangements made to pay Capax Discovery for EDD processing were a contrivance (see in paragraph 145(2) above); and then (c) whether the way that Mr Hogenson was dealt with and/or the way VT4 was presented to Deloitte and the FRRP demonstrates "guilty knowledge".

Particular matters highlighted by VT4

153. The Claimants focused especially in the context of VT4 on a spreadsheet prepared by Mr Hussain, which he sent to Dr Lynch on 29 December 2009:

(1) The spreadsheet contained, between columns W and AB of the "*revenue*" worksheet, a table setting out the daily progress of the large deals on 15, 16, 17 and 18 December 2009 (cells X16 to AA16):

	15th dec	16th dec	17th dec	18th dec			
HOME OF	3	3	0	1			
MOD #1	2.5	2.5	2.5	2.4			
MOD #2	2	2	2		out		
MT	10	10	10	10	24th dec		
Dell oem	2	2	2		risk		
Dell MS	5	5	10	5	MS + BofA closed for $1m		
BNP	3.3	3.3	3.3		signed		
Eli	6.6	0	0		out		
D&T	2	0	0		out		
JPMC	5	10	10		disappeared		
Vat	19	19	19				
capax				6.5			
microtech				5			
Verdasys					collections		
integracion				2.5	collections		
HP OEM							
Filetech				8	recognition		
frank pao				1.5			
Imperva				1			
MS				12	risky		
Schwab	3.5	3.5	3.5		signed		
VT		2	2	1.9			
	63.9	62.3	64.3	56.8	0	0	

(2) Row 24 (marked with the first red arrow above) showed "*Eli*" (cell W24) with a value of $6.6 million on 15 December 2009 (cell X24), reduced to zero as at 16 and 17 December 2009 (cells Y24 and Z24) together with the comment "*out*" (cell AB24).

(3) Row 28 (marked with the second red arrow above) now had a new entry for "*capax*" (cell W28). This row was blank for 15, 16 and 17 December 2009 (cells X28 to Z28) but had a value of $6.5 million as at 18 December 2009 (cell AA28).

(4) It is easy to see that, as at 18 December 2009, the $6.6 million potential deal with Eli Lilly was to be replaced with a deal for approximately the same amount ($6.5 million) with Capax Discovery.

154. Dr Lynch said in cross-examination it was "*possible*" but "*unlikely*" he looked at this spreadsheet. But he was the primary addressee of Mr Hussain's email attaching it (Mr Stephan and Mr Chamberlain were copied, no doubt because they were working with Mr Hussain in the finance department). The Claimants submitted that Mr Hussain would not have sent it unless he expected that Dr Lynch would look at it. It is true that Dr Lynch (who said he disliked spreadsheets) considered that Mr Hussain was over-fond of them. But although Dr Lynch sought to portray his *"multi-page, multi-*

everything" spreadsheet as "*pretty incomprehensible*", that struck me as rather exaggerated in the particular instance: it contained a user-friendly table charting the day-by-day position on the major deals. Given his focus on revenue, and on the large deals which would make the difference between achieving forecast and falling short of it, I agree with the Claimants that that would have been of considerable interest to Dr Lynch, and the likelihood is that he read it.

155. The Claimants urged me to find that Dr Lynch knew that Mr Hussain's plan was to try to recognise revenue on the potential Eli Lilly deal in Q4 2009 by using Capax Discovery as a placeholder, on the basis of the same assurances as had been made in respect of the Kraft transaction. Although taken as a whole, I would have agreed with Dr Lynch that this rolled up set of assertions was *"going a bit further than the data on this spreadsheet".* I accept that he would have gleaned from it quickly that Mr Hussain planned to use Capax Discovery if Eli Lilly did not complete in time or fell out. Furthermore, whether he read it properly or not, the fact that it was sent to him demonstrates both Mr Hussain's perception that Dr Lynch was not aloof from everyday detail or concerned only with strategy as a CEO of a listed public company but rather wished and expected to be involved in such detail, and also Mr Hussain's wish and propensity to share information with Dr Lynch and seek his support or guidance. I find it inherently unlikely that Mr Hussain would have wished to share this sort of detail whilst keeping to himself the matters of which he was aware as to how in truth the impugned VAR deals were intended to operate.

156. A second point of detailed evidence relates to the fact that VT4 was only proposed to Capax Discovery on the very last day of Q4 2009, and had to be (as it was) completed by midnight. Capax Discovery (a fledgling entity which its parent had indicated it would not support in this regard) had no time, and made no attempt, to assess the potential for an end-user sale and thus the \$6 million risk which on the Defendants' case it was undertaking for an upside fee of 10% and the possibility of future servicing work for Eli Lilly if that proposed end-user deal eventuated. Dr Lynch sought to address the obvious point that such an indifference to risk might suggest that it was not a real one (or that some other reliable comfort was available to cover it) with a suggestion to the effect that Capax Discovery already had available the information:

> *"Q. Mr Baiocco's evidence is that Capax Discovery had not had any dealings with Eli Lilly about this potential transaction before Capax Discovery issued its purchase order. Again, that wasn't challenged. I don't understand you to dispute that either, do you?*
>
> *A. Well, other than I think I've seen information that says that <u>Capax were actually working inside Eli Lilly at this point anyway</u>."* [My emphasis]

157. Dr Lynch repeated this "understanding" three more times in the course of his cross-examination, but never gave any indication of its source or any other support for it. No evidence was provided to support it; and it was not suggested or put to Mr Baiocco that Capax Discovery was already working for Eli Lilly prior to 31 December 2009. It was suggested to Mr Baiocco that Capax Discovery subsequently became an approved vendor of professional services to Eli Lilly: but Mr Baiocco's evidence was that this did not end up happening.

158. A third point of focus in relation to VT4 was the arrangements made to pay Capax Discovery for the provision of EDD services, which as I have explained above the Claimants alleged were contrived to make good a liability to which Capax Discovery was contractually exposed because of a shortfall of some $700,000 representing the difference between the licence fee under the direct agreement between Autonomy and Eli Lilly (about $5.3 million) and the licence fee that had been agreed with Capax Discovery (about $6 million). I have described above how this was done and the Claimants' case that it was all a contrivance (which I have accepted): the question now is as to what the Defendants knew.

159. There are three facets to this question: (a) whether purchase orders issued by Autonomy supposedly in respect of *"EDD Services"* related to any actual EDD work done or to be done by Capax Discovery; (b) whether, if not, the Defendants knew that and (c) whether the Defendants were aware of the arrangements in the particular context of VT4 for which Capax Discovery's shortfall was to be paid off and their alleged contrivance.

160. As to (a), I have summarised in paragraphs 2507 to 2510 in the main body of the judgment and elaborated in the part of this judgment dealing with the allegations about 'Reciprocal Transactions', the question whether Capax Discovery had that capability at the time of the first Capax Discovery/EDD sale at the end of March 2009. I have concluded that it did not. The Claimants' case was that it did not develop a capability to provide EDD overflow services until late 2011. By way of summary:

(1) The device of using purchase orders for *"Specialist EDD processing"* on the purported basis that Autonomy had such a volume of EDD processing work that it could not do it itself and thus needed to secure from Capax Discovery *"overflow capacity"* had been devised in April 2009 to provide funds to Capax Discovery to enable it to make instalment payments under the first Capax Discovery/EDD sale and had become well-established: and see paragraphs 2507 to 2524 in the main body of the judgment.

(2) Use of such purchase orders was extended in May 2009 to cover hardware purchases from Autonomy to enable Capax Discovery to start an EDD processing facility and build capacity itself to do EDD processing work.

(3) It was then extended again to cover instalments due to Autonomy by Capax Discovery under a second Capax Discovery/EDD sale in early 2010.

(4) As at April 2009, and for a considerable time after that, probably until early 2011, Capax Discovery had not in fact the ability to do specialist EDD processing.

(5) The truth that Capax Discovery had no ability to deliver specialised EDD processing throughout this period was established by the evidence of Mr Baiocco, Mr Egan and Mr Sullivan, and by the absence of any proof of it ever being provided. Further, Mr Sullivan, who as CEO of Zantaz, had detailed insight of its e-Discovery business, stated in his witness statement that he

> *"knew of no instance of EDD work being outsourced to Capax or any other third party. Further, I do not believe that Autonomy needed standby EDD support services. When capacity constraints did arise, as in the case of our extremely large EDD contract with BP, Autonomy*

> *scaled up its operations by adding hardware and hiring additional staff to handle the additional workload."*

(6) The fact that the purchase orders, which were never followed by any contract to establish terms for the provision of services, were simply a means of generating funds for Capax Discovery was also discernible from the clear pattern which developed: Capax Discovery would never pay instalments unless and until it had received payment under the purchase orders. Indeed it was that pattern which Mr Hogenson discerned and expressed concern about in late June 2010 (see paragraphs 2239 to 2242 in the main body of the judgment), as (in July 2010) did Mr Tejeda as Autonomy Inc Director of Revenue in the Americas.

(7) Documentary evidence such as a spreadsheet sent by Mr Baiocco to Mr Kanter on 4 March 2010 under cover of an email explaining that it *"reflected the deal from q1 09"* and also drew attention to the fact that as regards the *"q4 deal"* it had not yet been populated *"because there has been no payments related to that deal as of yet"*, confirmed the expectation that funds would be provided for Capax Discovery to enable it to pay down its debt. Thus, the spreadsheet had a column for the "*Total Owed to Capax*", which listed the instalments due to Capax Discovery in order to fund Capax Discovery's payments under the first Capax Discovery/EDD sale, and then various columns showing when Capax Discovery paid Autonomy following receipt of funds from Autonomy pursuant to various e-Discovery purchase orders. The spreadsheet indicated that Capax Discovery was expecting Autonomy to pay it amounts equivalent to the instalments due under the first Capax Discovery/EDD sale and was using the funds it received from Autonomy under the guise of e-Discovery services to pay those instalments. The difference between the amounts in the Total Owed to Capax Discovery column and the amounts recorded in the column headed "Check Breakdown" was Capax Discovery's profit.

(8) If this was not clear enough from Mr Baiocco's spreadsheet, Mr Baiocco then sent Mr Kanter a follow up email, saying:

> *"…sorry to hit you again here. Just wanted to reiterate that we were promised more than a dollar for dollar on this. We were promised a profit as well. Trying not to sound ungrateful in any way, just that we were nowhere near ready to do a deal like this."*

(9) Dr Lynch himself acknowledged, when asked early in his cross-examination, whether having seen the material adduced and listened to the evidence up until then, he was still adamant that there was no wrongdoing, that he was concerned about impropriety in relation to the payments to Capax Discovery for EDD, in that he had seen evidence that:

> *"…we were paying for the provision of EDD outflow services and that Mr Baiocco was not in a position to actually provide that if that had been required and Mr Egan knew that."*

(10) As earlier noted, the invoices referred to *"Outsourced Specialist EDD Services…for European projects"*, but Mr Baiocco's evidence, which was on this point not challenged or contradicted, was that Capax Discovery never did work on any *"European projects."*

(11) Not only was the use of purchase orders purportedly for *"Specialist EDD processing"* an established device and pretence, but the propensity of those directly engaged in the deployment of the device, including especially Mr Egan, Mr Kanter and Mr Hussain, to co-operate in the creation of pre-textual correspondence with an eye to the auditors, which might otherwise not be likely, is apparent from an earlier email in the same email chain as culminated in Mr Kanter's *"bandwidth"* email of 6 October 2010 to Mr Hussain and Mr Egan dated 6 October 2010 (see paragraph 145(2) above). In that earlier email, Mr Kanter pretended to have been *"impressed with Capax's contribution to the FSA transaction"* so as to justify a MAF. He knew, and they all knew, that Capax Discovery had in fact done nothing.

161. As to who knew of the pretence:

(1) Mr Egan, Mr Kanter and Mr Hussain worked together in this area as a tight, close-knit team. They were all also part of what Dr Lynch considered to be his core management team. Of course, Mr Egan was on the ground in the US, whereas for the most part Mr Hussain and Mr Kanter were in the UK, sharing an open plan office when in London with Dr Lynch, and being in close proximity to each other when working in Cambridge; and they were able to and did keep in close contact with each other, both in writing, as the email chain itself illustrates, and in undocumented discussions. It seems to me much more probable than not that Mr Hussain would have come to know what Mr Egan and Mr Kanter knew.

(2) I consider it unlikely that Mr Kanter or Mr Egan would have contrived all this without the knowledge and approval of Mr Hussain; and all the more unlikely that either would have dared to do so alone and implicated the others by including them in emails seeking their approval. They were a tight team, all aware of the assurances given to Mr Baiocco, and the need to find a solution to fulfil them. It seems to me reasonably clear that Mr Kanter and both recipients of his "bandwidth" email were well aware of the device and its development and purpose.

(3) The documentary evidence lends further support by revealing a sharp difference in the way Mr Baiocco's frequent and increasingly urgent enquiries as to payment as instalment dates under the various EDD contracts became imminent were treated within Autonomy's finance department according to whether they did or did not know that no EDD work was in fact being done by Capax Discovery. By way of illustration of this:

(a) When Mr Crumbacher (who was not in the know) tried to find out in February 2010 who was dealing with Capax Discovery EDD purchase orders after Mr Phil Smolek had left (in December 2009), Mr Sullivan (who was not in the know either) responded that he did not know but assumed that Mr Chamberlain would be able to say, prompting Mr Crumbacher to ask:

> *"Doesn't your team have to tell finance how much processing work was done, and for what fee? Who are they giving that information to now? Or has no EDD work been done by Capax since Phil left?"*

(b) Those in the know, such as Mr Kanter (who had become by then responsible for the e-Discovery purchase process, which of itself is of interest), simply dealt with the enquiries for what they were: enquiries as to when Mr Baiocco would get the funds he needed. Thus, for example, after Mr Crumbacher had once more sought information about EDD sales after urgent enquiries from Mr Baiocco, Mr Kanter appears to have enquired of Mr Egan how much was required, and when told that an increased amount was outstanding, simply increased the payment by a total of some $350,000 without requiring or providing any explanation.

(c) Mr Egan, Mr Kanter and Mr Baiocco were in constant contact, and email evidence suggests that increasingly Mr Kanter kept a close eye on any purchase order from Capax Discovery relating to EDD Processing, without involvement on the part of others in the finance department.

(d) They kept a close eye on purchase orders with respect to EDD.

162. The third question, and the one of most specific relevance to VT4, is whether the Defendants knew that the purchase order which generated the funds used to cover Capax Discovery's shortfall of $700,000 was likewise a pretence. As to that:

(1) It seems to me clear that the purchase order was a pretence, just as the preceding purchase orders for *"Outsourced specialist EDD Services"* were pretences, to justify the payments that in effect Mr Baiocco had been promised would be made to enable Capax Discovery to make the instalment payments due by it, and in the case of VT4 the shortfall that had arisen;

(2) In the circumstances detailed above, I have concluded that Mr Hussain, Mr Kanter and Mr Egan were all aware of this and indeed involved in it;

(3) That leaves only the question of what Dr Lynch himself knew.

163. Dr Lynch was aware of the direct Autonomy/ Eli Lilly contract (not least, from Mr Hogenson's expressed concerns). However, he denied in cross-examination that either Mr Egan or Mr Kanter told him about this arrangement to cover Capax Discovery's shortfall. Dr Lynch's position was that, as far as he was concerned, the payments were for services which Autonomy needed to sub-contract; nothing suggested to him that the payments were for fictitious services.

164. The Claimants rejected this and submitted that "*given that the arrangement involved paying $700,000 to Capax Discovery in exchange for nothing, that is highly implausible.*" But that assumes against the Defendants the very point in issue, which is whether the payment was in fact for services. Nevertheless, having concluded that Mr Hussain was

involved (see paragraph 161 above), in addition to Mr Egan and Mr Kanter, I do not think it likely that they would all have kept from Dr Lynch the arrangement which lay behind the exchanges, which I have concluded they devised to fulfil the assurances given by Mr Egan and to ensure that Capax Discovery was not left out of pocket.

165. I consider that I am fortified in that conclusion by the following:

(1) On 9 December 2010 Dr Lynch was asked to approve the $700,000 purchase order by an Accounts Assistant, obviously on the instructions of Mr Hussain and/or Mr Kanter and/or Mr Egan (all of whom had previously given their approval), with a careful, but unusual, explanation that his (Dr Lynch's) approval was needed *"as the total exceed 30,000USD"*. Dr Lynch wrote *"ok"* from his iPhone. He asked no questions at all.

(2) This needs to be set in the context of the fact that in July 2010 Mr Percy Tejeda ("Mr Tejeda"), Director of Revenue at Autonomy Interwoven, had raised specific queries about various issues relating to VT4 and the Eli Lilly contract, including whether Autonomy were genuinely sub-contracting EDD services to Capax Discovery. He had also referred to the shortfall in question. Mr Tejeda's email had been forwarded by Mr Hogenson to Autonomy's Audit Committee on 8 July 2010, copying Mr Knights and Mr Knight of Deloitte and Mr Kanter. It was put to Dr Lynch in cross-examination that in light of these concerns, he would surely not *"have just said "okay" without asking any questions about these purchase orders?"*

(3) I accept this "dog that did not bark" point. In his oral evidence, Dr Lynch told me that he also sought to dismiss the concerns of Mr Tejeda and Mr Hogenson as *"nothing new"* and he had in fact drawn additional comfort that there was nothing amiss about the EDD purchase orders[14] from Deloitte's investigation finding nothing untoward. However, I cannot accept this justification for Dr Lynch having raised no questions in respect of an issue that had become such a focus of concern:

(a) It seems to me most unlikely that this request for approval came out of the blue: it is much more likely, in all the circumstances, that Dr Lynch had been told by Mr Hussain or Mr Kanter what to expect and why.

(b) That is especially so because it appears that the requirement for his approval of anything over $30,000 was new, and thus the request fairly new too. In that context, Dr Lynch disputed that there was any such rule at all: but in that case the request would surely have appeared all the more questionable unless pre-explained.

(c) Furthermore, in relation to EDD payments to Capax Discovery, he had no basis for supposing, let alone getting comfort as he suggested, from Deloitte's review: Deloitte never did consider EDD payments.

[14] He told me in cross-examination: *"The irony, which may be a slightly sad one, is that after Deloitte had looked at all this, I actually felt confident in these things."* The fact is, however, that Deloitte were not aware that Capax Discovery had no ability to provide the relevant EDD processing, and had never done so, as I have found to be the position; and if Dr Lynch knew this, the point rebounds on him.

166. In summary, therefore, I have concluded that all of the core management team of Dr Lynch, Mr Hussain, Mr Kanter and (for these purposes) Mr Egan were aware that the purchase order for $700,000 was a pretence, and was the mechanism whereby to appear to justify covering Capax Discovery's exposure in the VT4 transaction. That further substantially supports the Claimants' case for impugning VT4 and for liability on the part of the Defendants under FSMA.

167. In my judgment, the Claimants have established both limbs of their case in relation to VT4.

VT10: Capax/FSA (Q1 2010)

168. By mid-March 2010, Autonomy was close to concluding a substantial sale of software to the UK Financial Services Authority ("the FSA"). The sale was being negotiated by Mr Chris Hartley (a senior sales executive with ASL, based in Cambridge) directed and assisted by Mr Hussain. The FSA deal was one of the main targets for the quarter.

169. Mr Hussain told Dr Lynch by an email dated 15 March 2010, Autonomy at that stage needed *"5-8 more"* and though Mr Hussain still hoped to close the proposed FSA deal of about $4,500,000, which would have greatly assisted it to meet its revenue target for Q1 2010 of $195,500,000, by then the prospects were fading of doing so before the end of the quarter.

170. As at 29 March 2010, it was clear that no deal could be concluded with the FSA within Q1 2010. Dr Lynch sent Mr Hussain a document setting out the transactions that he understood needed to be concluded in order for Autonomy to achieve its total revenue target for Q1 2010. The attachment identified $4 million in revenue as coming from "*FSA PARTNER MT*". The use of the suffix "*PARTNER*" denoted the use of a VAR in order to recognise the revenue in Q1 2010, as Dr Lynch accepted.

171. Dr Lynch denied that he was thereby instructing, or at least, authorising Mr Hussain to enter into a VAR transaction to enable revenue to be recognised, but he accepted that he was content with Mr Hussain doing so. He went on to accept the following:

> *"Q. And so what Mr Hussain was proposing and you were going along with was for Autonomy to get this VAR to submit a purchase order that would enable Autonomy to recognise the revenue in Q1, correct?*
>
> *A. I assume that's what it would want to do, yes."*

172. On 30 March 2010, Dr Lynch sent Mr Hussain an attachment entitled "*115Done.docx*" and said in his covering email, "*Ok heres [sic] my list*". The attachment attributed $4 million of revenue to "*FSA PARTNER MT*". Dr Lynch accepted in cross-examination that MT "*could be*" MicroTech. No other meaning has been suggested.

173. The plan became to use as the VAR a company called Centennial, an affiliate of FileTek, which Mr Szukalski described to me, in the context of the FileTek/USDVA deal, as being *"very comfortable and familiar with these types of transactions"*:

   (1) On 30 March 2010, Mr Egan asked Mr Kanter to create a purchase order for Centennial "*to agree with the parameters you finalize on for FSA deal*".

(2) The same day, Mr Egan, Mr Kanter and Mr Hussain discussed what terms should be included in the purchase order. Mr Hussain said, "*the problem is rev rec on the reseller – are they financially strong?*"

(3) On 31 March 2010, Mr Crumbacher, at Mr Egan's request, set out in an email a list of "*big issues*" in the proposed FSA contract "*for your communication with Centennial tomorrow*". The list made apparent that the FSA deal was complex and there were a large number of potential issues for consideration by Centennial.

(4) That day (31 March 2010), Mr Hussain emailed Mr Egan saying, "*this doesn't look good to me*". Mr Egan agreed, "*I know I think I need to either do straight on the FS deal as financing or do FT deal*". Mr Hussain replied, "*With these guys I think you can only do a FT deal. PMI and citi thru DT. FSA?*". The Claimants submitted, and I accept, that this signified that they considered that a different VAR needed to be found.

174. Also on 31 March 2010, at 12:38 pm, Mr Hussain sent Dr Lynch (and Mr Egan) another revenue route-map document. The overall target was revenue of $200 million, equating to earnings per share of $0.25. A list of transactions was given to reach that target, including "*FSA 4.5*". No VAR was identified on this list.

175. Later that day (31 March 2010), at 7.19pm, Mr Hussain sent Dr Lynch a further version of the same document which stated at the foot of the page, under the heading "*ISSUES*", "*FSA??*". The VAR was still not identified on the list.

176. At 11.31pm on 31 March 2010, Dr Lynch sent Mr Hussain a further version of the document. He stated in the subject field of his covering email "*Important sheet ring if awake ... midnight italy*". Next to the reference to the $4.5 million FSA transaction, Dr Lynch wrote the letters "*cx*". Dr Lynch accepted in cross-examination that this was a reference to Capax Discovery. He explained how Capax Discovery had come to be chosen as the VAR for the FSA deal as follows:

> *"Q. On 31 March, you are identifying Capax as the VAR to use to recognise revenue on the potential transaction with the FSA?*
>
> *A. No, someone will have told me that that is who we are talking to about doing it.*
>
> *Q. Who?*
>
> *A. It could have been Mr Egan. It could have been Mr Hussain."*

177. There was still time to do a deal with Capax Discovery, because Capax Discovery was located on the US East Coast (five hours behind London time). Dr Lynch accepted in cross-examination that he had no reason to think that Capax Discovery (a New Jersey company) had had any dealings with the UK financial services regulator. It was the unchallenged evidence of Mr Baiocco that the first he heard of a possible transaction for end-user FSA was "*when Mr Egan called me right at the end of the quarter*".

178. On 31 March 2010, at 10.14pm, Mr Crumbacher emailed Mr Baiocco a draft purchase order for him to execute and return, which he did. The purchase order, drafted by Autonomy, stated a licence fee of $4,285,714 plus $214,286 for one year of support. Payment was required as follows: $450,000 by 30 April 2010, $1.05 million by 31 March 2011, $1.5 million by 31 March 2012 and $1.5 million by 31 March 2013. The software included Introspect (i.e. e-Discovery), Aungate Investigator and ECA. The payment order was issued under the June 2009 Capax Discovery VAR Agreement, summarised at paragraph 60 above, and which made clear that the reseller was unconditionally obliged to pay (and was not relieved by any non-payment by the end-user) and the agreement comprised the entire agreement between the parties. As the Defendants also emphasised, the terms of the contractual arrangements (which are not said to be a sham and must thus be given full effect in law) made it clear that the risk of ownership had passed, and that managerial control was not retained by the seller (Autonomy).

179. Notwithstanding the extreme hurry (necessitating the choice of a VAR in a different time zone) to enable recognition of revenue by the use of a VAR in anticipation of an end-user sale to the FSA, it appears that in the immediate aftermath there was some shilly-shallying as to whether or not to take the revenue in that quarter, or defer it. In particular:

(1) In the early hours of 1 April 2010, Dr Lynch (who was in California) emailed Mr Hussain to say, "*everything expected in IDOL US closed*" and attached an update. The update continued to show $4.5 million of revenue on an FSA deal, through Capax Discovery.

(2) Also on the morning of 1 April 2010, Mr Hussain emailed Mr Egan, subject "*update pls*". The body of his email identified the following transactions:

(a) *"Filetek 8m"*
(b) *"Discovertech – pmi & citi"*
(c) *"Capax – fsa"*

(3) But on 8 April 2010, Mr Chamberlain emailed Cynthia Watkins and Matt Stephan to say that "*Powers greater than me*" were making decisions which required adjustments to revenue, including "*Defer Capax (FSA) - $4,285k*".

(4) Then, on 12 April 2010, Mr Chamberlain emailed again, saying, "*We have had to make further changes to your numbers*", and identified "*Capax (FSA) back in*". The same day (12 April 2010), Mr Hussain sent Dr Lynch an "*audit update*" which stated, "*MT is ok (subject to some evidence) Capax ditto*".

180. In the event, Autonomy recognised the licence fee revenue immediately as at 31 March 2010, with the support and maintenance recognised over the course of the following year.

181. Subsequently, in August 2010 Autonomy entered into a direct agreement with the FSA which provided for three years of hosting and archiving services, together with software licences, for a total amount of $6,676,102 payable in stages subject to acceptance criteria not finally satisfied until August 2011. The last stage payment was not due or paid by the FSA until September 2011. In June 2011 Capax Discovery paid $1.5m due in respect of

its obligations.[15] After Autonomy had invoiced the FSA in respect of the sale, Autonomy credited Capax Discovery in respect of the balance of the debt due.

182. Some of the Claimants' submissions in respect of VT10 broadly mirrored those in respect of the other impugned VAR transactions between Autonomy and Capax Discovery (other than those relating to EDD). Thus:

(1) The VAR deal was offered to Mr Baiocco at literally the eleventh hour and Capax Discovery had no time or opportunity to assess the prospect of the proposed end-user deal, nor to negotiate price. Mr Baiocco said that he was told that *"the deal with the FSA was very close to closing, and that we would get a 10% commission once Autonomy had closed it"*; but Capax Discovery could and did make no enquiry of its own, and simply settled in to passively awaiting whatever Autonomy negotiated. It had not the time or the means, nor (if in reality it was taking none) any reason, to measure the risk.

(2) The Claimants relied on the unchallenged evidence of Mr Baiocco that Capax Discovery had no involvement in the negotiations, which continued after the VAR deal much as before, to conclude and close a deal with the FSA, so that Capax Discovery was entirely dependent on Autonomy for information about the progress of the negotiations;

(3) When on 30 April 2010 the first instalment (of $450,000) became due and payable by Capax Discovery under VT10, Capax did not pay, and yet Autonomy did nothing to enforce the debt pending a deal with the FSA;

(4) Although it had done nothing to assist the ultimate deal with the end-user, Capax Discovery was paid a MAF as if they had made a substantial contribution;

(5) After the direct deal had closed, Autonomy agreed with Mr Baiocco, in wording confirmed by Mr Kanter in a letter, that it would apply the payments it received (this time directly) from the FSA against Capax Discovery's account with Autonomy which, the Claimants submitted:

> *"in effect, involved waiving Autonomy's right to be paid $4.5 million by Capax Discovery, if that amount was paid to Autonomy by the FSA pursuant to a separate contract to which Capax Discovery was a stranger."*

183. The Claimants submitted that all this fitted the 'pattern' and was consistent with and confirmatory of the Claimants' overall case that Mr Egan had assured Mr Baiocco that Capax Discovery would not be required to pay for VAR deals like the FSA deal from its own resources. The Claimants submitted further that:

> *"Indeed, absent the handshake agreement, Mr Kanter's confirmation makes no sense: there is no other reason why Autonomy should be giving credit to Capax Discovery for a sale to the FSA which Capax Discovery had done nothing to bring about."*

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[15] The Claimants allege that this payment resulted from Autonomy's ramp up payment in respect of Capax Discovery's NearPoint services, dealt with at paragraphs 198 to 202 below.

Four particular matters relating to VT10 emphasised by the Claimants

184. Even though not with direct reference to VT10, I have addressed these matters in the context of my general analysis, and further in relation to VT3 and VT4. My comments there should be read in here *mutatis mutandis.* However, there were four matters particular to VT10 on which the Claimants placed considerable emphasis:

(1) One was the oddness and lateness of the sudden change to engaging Capax Discovery as a VAR, having originally contemplated engaging Centennial.

(2) The second was the Claimants' complaint that Deloitte was simply not informed of the direct FSA deal at all during their Q3 2010 review; and in cross-examination, Mr Bloomer told me that he did not recollect it being mentioned to the Audit Committee either.

(3) The third arose out of the provisions for deferment of payment under the direct deal, which meant that Capax Discovery remained legally *"on the hook"*. The Claimants highlighted two aspects of this: the first was that Autonomy never pressured Capax Discovery to pay out of its own resources until after the direct deal was closed in August 2010; and the second was that, when the position of Capax Discovery's outstanding indebtedness became a source of pressure and embarrassment for Capax Discovery, Autonomy allegedly contrived a transaction, the *"NearPoint"* transaction, as a means of passing funds to Capax Discovery to enable it to discharge part of that indebtedness. Capax Discovery was not pressed to pay for so long as the instalment payments due from FSA were deferred.

(4) The fourth matter related to the payment of a MAF, and more particularly, the rationale advanced for its payment, which (as previously noted) suggested some concern as to its true justification.

185. As regards the first of these particular matters, the hurried resort to Capax Discovery was certainly even more rushed than usual (such that Capax Discovery's time zone was of itself a necessary resort); and the Claimants' point that Capax Discovery was based in San Francisco and had had no contact with the FSA in the UK, so there was nothing to suggest that it had any ability to negotiate, or even materially assist in the negotiation of a transaction, seemed to me to be fairly made, even if of limited significance in the round (in light of my previous conclusions). The further suggestion floated by the Claimants, however, was that Capax Discovery had shown itself ready in the Kraft and Eli Lilly transactions to act *"obligingly"* (as the Claimants perceived and described it) in a *"placeholder role"* without any real interest in the end-user sale save if it brought a useful contact and a MAF.

186. Dr Lynch's response in cross-examination to these suggestions seems to me fairly to encapsulate his own outlook (even though he stressed he had very little involvement in either the VAR transaction or the direct deal):

> *"Q. I would suggest, just going back to this transaction with the FSA, that in proposing Capax you had very much in mind the placeholder role which I've suggested Capax performed on the*

Kraft and Eli Lily transactions.

A. *Well, first of all -- and it's getting repetitive, but I wasn't proposing anything. I'm just keeping a track of what's going on. Secondly, FSA, I now know, was a deal that required a very large amount of services. And, thirdly, we wanted one of our good partners to do those services. And then the outcome was that Capax actually did do services at FSA. So, to me, this is all a perfectly fine commercial decision which looks like a good one, getting a services partner in there. Secondly, I understand that the VARs all consider that they were on risk."*

187. Especially since it was not until much later that Capax Discovery did secure a service agreement with the FSA, there was obviously the use of hindsight in that response. But to my mind the greater objection is that it obscures the fact that Autonomy inserted a reseller minutes before midnight because it wished urgently to plug a shortfall in recognised revenue and trusted and paid Capax Discovery to take the legal risk but do no more. When Mr Baiocco agreed to Capax Discovery's use in this way, he would have known nothing about the potential for it to provide future services; and the emails he sent shout the message that he was in it first and foremost, for *"champagne-smacking"* commission. That may not of itself be improper; but the effort to disguise it tells against the Defendants' comfort with its propriety, and the fact of it fits the pattern relied on by the Claimants.

188. The second point of particular note is the FSA direct deal was not disclosed to Deloitte during Deloitte's Q3 2010 review, nor until long afterwards. The Claimants highlighted that (a) the direct deal was of a value many multiples of the $100,000 threshold for deals that were to be disclosed to Deloitte and (b) as Autonomy's finance department acknowledged and thus knew, Deloitte were expressing concern as to whether the reversal and replacement of VAR deals in two previous quarters (involving end-users Kraft (VT3), Morgan Stanley (VT8) and ManuLife (VT7)) called into question whether Autonomy had in fact retained managerial control and thus whether it had been appropriate to recognise revenue at the point of the original VAR transactions.

189. This was of some significance; for, as Mr Hussain knew, Deloitte was, at just this time, expressing concerns about the fact that some earlier VAR sales[16] had been replaced by direct end-user deals; and the importance attached by Deloitte to the issue was reflected in a note in that review:

> *"that no value added reseller deals have been reversed this quarter and resigned directly with the end-user and this supports management's policy of revenue recognition at the point of sale to the value added reseller".*

190. However, the Defendants pointed out (as to (a) in paragraph 188 above) that the disclosure required was of revenue-earning deals: and since Autonomy had already recognised the

[16] Deloitte expressly noted in their H1 2010 report that they had raised the concern, reminding that it would not be appropriate to recognise revenue if Autonomy was required to maintain ongoing managerial duties in respect of the product sold to the reseller or if the reseller could not show it could pay, and Autonomy's management had acknowledged it.

revenue from the VAR deal, it would have been wrong to include revenue from the direct deal in the list. That was especially so because (as Dr Lynch, with notable attention to detail) pointed out under cross-examination, there were acceptance criteria in the FSA direct deal which would not have permitted revenue recognition at that point.

191. Dr Lynch also made the point (especially with reference to (b) in paragraph 188 above) that Deloitte's concern related to reversals of previously booked revenue with resellers: and (until much later) there was no reversal of revenue, because Capax Discovery remained on the hook for the debt, as Mr Baiocco acknowledged[17]. There was a reversal only in September 2011, after the FSA had paid. The Defendants submitted that Deloitte were only interested to know about actual reversals of previously booked revenue and that in this case, there was no reversal of revenue as such until much later, in September 2011 when (it was common ground) the last instalment due was paid by the FSA and Capax Discovery's obligations were formally cancelled. Then, according to Mr Welham, when Deloitte subsequently learned, in Q1 2011, of a deal between Autonomy and the FSA, they did not associate it with the Capax Discovery/FSA VAR transaction.

192. Dr Lynch submitted that, for the same reason, the passage in the Q3 2010 report to the Audit Committee was accurate, and not misleading.

193. In my judgment, Dr Lynch's explanation did not grapple with the basic point underlying Deloitte's concern, which was whether there was developing a pattern of direct deals suggesting an intention that Autonomy should retain managerial control, and the signs that it in fact did so. Further, the suggestion that the note in the Q3 2010 report was accurate is a blinkered and self-serving one. It seems to me obvious that Deloitte would have wanted to know about a direct deal contemporaneous with their warning, especially such a large and important deal.

194. In relation to the third and double-faceted point summarised in paragraph 184(3) above, there is no doubt that Autonomy did not chase Capax Discovery to pay the instalment of \$450,000 due under VT10 in April 2010, and made clear efforts to cover its indebtedness. Then, on 27 September 2010, Mr Hussain emailed Mr Egan, Mr Scott and Mr Kanter, subject "*capax*", noting that Capax Discovery currently owed \$18 million and, having received the Eli Lilly cash, should pay \$5.5 million: "*That leaves \$12.5m of which \$5m is for FSA which is being sorted out as we went direct*". In a further email in the same chain, Mr Hussain said, "*Steve will sort out FSA*". The entirety of the chain was then copied to Dr Lynch.

195. The Claimants submitted that Dr Lynch must, therefore, have known that Autonomy had contracted directly with the FSA, and that Capax Discovery was not going to be made to

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[17] Dr Lynch stated:

> *"I think you're conflating two situations…The situation with Capax at this point is that Capax has not been lef off the hook, it's just that the payments from FSA are being allocated against their requirement, so no credit note is issued to Capax at this point. So it's a different situation to the one…where…the deals that have been sold to the VAR being undone and a credit note issued."*

pay from its own resources, and would instead be "*sorted out as we went direct*". Then on 30 September 2010, Mr Chamberlain sent Mr Hussain an email, subject "*FSA*", stating:

> *"Don't think we need to resolve this today but will keep going on this if you want me to. My recommendation would be that we enter into a one pager with Capax saying that they remain liable for this but that we will provide a credit as we receive amounts from FSA. To the extent we have a shortfall they have to make that good since they entered into an irrevocable PO."*

I consider this was a recitation of the legal position, but in reality all concerned knew that the direct deal released Capax Discovery.

196. The Claimants relied also on a transaction referred to as the *"NearPoint ramp-up fee"* as further illustrating (especially by reference to its context and timing) how arrangements were always made to ensure that any legal obligations undertaken by the VAR should be covered by Autonomy in one way or another.

197. As regards the context, as the end of Q2 2011 approached, Capax Discovery's debt in respect of the FSA purchase order totalling $1.5 million was overdue. Mr Baiocco's evidence in his witness statement was that by then he had *"rising concern about the paper debt relating to [the FSA transaction], which was causing me issues with my fellow partners at Capax, all of whom wanted to know what was going on".* He had expressed this concern in an email to Mr Kanter dated 7 March 2011. He sent a number of chasing emails, all expressing rising concern and in effect calling upon Autonomy to do something to release Capax Discovery. After months of prevarication in response, by the end of Q2 2011 it was clear to Autonomy that something had to be done.

198. The *"NearPoint ramp-up fee"* was what Mr Hussain finally proposed (by email of 13 June 2011) as an answer. This was a fee Mr Hussain suggested might be paid to Capax Discovery, ostensibly at least to assist it to develop (*"ramp up"*) infrastructure to support legacy customers using the *"Nearpoint"* archiving product which Autonomy acquired as part of its acquisition of Iron Mountain software assets. Mr Hussain explained his proposal to Mr Baiocco in carefully orchestrated terms:

> *"Further to our meetings last week I would be grateful for a proposal from you to help us with our integration of the recently completed Iron Mountain Digital acquisition. As we discussed there are several areas which we believe you could immediately assist us:*
>
> - *The NearPoint asset is a direct competitor to EAS and we would want Capax to take over servicing the support and maintenance base*
> - *The Stratify asset and the DRCCM asset is a direct competitor to Introspect and Digital Safe. We would like to upgrade the data centres with additional products to enhance the offering.*
>
> *Can you come back to me with a quick high level proposal and we can then discuss further. Please feel free to call me. As i said at the meetings we are looking at a relatively small budget initially of between $5m and $6m and we are looking to engage quickly."*

199. When Mr Baiocco responded affirmatively, Mr Hussain wrote again on 24 June 2011 (copying Mr Kanter):

> *"John- further to our numerous discussions on Capax starting to engage on Nearpoint maintenance i'd like to propose the following: capax starts to build up the team and infrastructure and for that we pay you a fee of $2m to $2.5m. As we get all the information on Nearpoint customers consolidated from Iron Mountain we will provide the information to you and gradually get you to takeover the provision of maintenance. This should then follow the EAS structure whereby you take over the smaller contracts initially, leaving the very large strategic customers with us and then gradually we shift those customers to you.*
>
> *If this is ok with you then Andy can start the paperwork process."*

200. Unsurprisingly, Mr Baiocco, who had not in fact asked for $2-2.5 million, responded within hours, "*This sounds perfect*". This was not surprising in that it appears that Mr Hussain was volunteering the payment of an upfront fee of $2-2.5 million to Capax Discovery for taking on new business that would be profitable to Capax Discovery in any event. Mr Baiocco told me in cross-examination that:

> *"I would have done it for free with no ramp-up charge. It was good business for us, I would have done it for free."*

201. The Claimants claimed that in truth the fee was simply part of a circular funding process to enable Capax Discovery to appear to pay off its outstanding indebtedness to Autonomy in respect of instalment payments due under VT10, both for audit presentation purposes and to honour the side agreement/understandings they alleged. It is enough for present purposes to note that it is not disputed that:

    (1) Autonomy paid Capax the entirety of the $2,000,000 ramp-up fee, even before expiry of a 60-day grace period, and

    (2) The same day Capax made a payment of $1,500,000 in respect of VT10 as requested by Mr Hussain.

    (3) Mr Baiocco's concerns about outstandings under the FSA deal were not repeated, until a final instalment became due.

202. My impression that Mr Baiocco is something of a braggart, suggests to me that he may have exaggerated in saying he would have gone ahead with Mr Hussain's original proposal even without any ramp-up fee[18], even if he would in fact have been prepared to accept less, very possibly much less and thought he had done a good deal for his company. I also accept Dr Lynch's evidence under cross-examination that the immediate payment by Capax Discovery upon receipt was of advantage to both because of its positive effect on the "days sales outstanding" ("DSO") calculation in the books of account of each. Thirdly, I have taken into account that Deloitte reviewed the transaction, and noted that Autonomy had purchased support services from Capax Discovery, and the ramp-up fee was considered in substance to be prepaid support. Deloitte considered there to be nothing

[18] Especially given that his original view, expressed in 2013, was that some level of ramp-up fee was warranted.

to indicate that this was not a commercial arm's length transaction.[19] Nevertheless, it seems to me more likely than not that the NearPoint ramp up fee was at least in substantial part a means of funding Capax Discovery. Both its amount and timing seem to me to point strongly to that conclusion: and it fits a pattern. Furthermore, that Mr Baiocco saw a link between the NearPoint fee paid by Autonomy and Capax Discovery's payment of the debt under the FSA purchase order is apparent from his version of the Capax Discovery Aging Report, to which he referred during his examination-in-chief and to which he was taken again in re-examination, which included the $2 million NearPoint fee within the "*FSA*" worksheet (red arrows added for ease of reference):

Customer Name	Invoice #	Invoice Date	Due Date	Invoice Total	Received From AU	Paid to AU	Capax Commission	Commission Received	Notes
FSA	6815-ANA	03/31/09	04/30/10	$ 450,000.00					
			03/30/11	$ 1,050,000.00					
			03/30/12	$ 1,500,000.00					
			03/30/13	$ 1,500,000.00					
							$ 450,000.00	07/10/2010	
FSA 2				$ 4,500,000.00					
		30/06/2011				$ 1,050,000.00			
		30/06/2011				$ 450,000.00			
		30/06/2011			$ 2,000,000.00				NearPoint rampup

203. The fourth and last matter of special relevance relates to the payment of a MAF. In that regard:

(1) On 6 October 2010, Mr Kanter emailed Mr Hussain and Mr Egan, subject "*Capax*", to say:

> *"Having been impressed with Capax's contribution to the FSA transaction, I am comfortable that they have earned a marketing assistance fee in line with our standard terms. I have prepared the attached to document properly the transaction. Please can I have your views."*

(2) Mr Egan responded "*Agreed*" and Mr Hussain responded "*ok*" .

(3) There was no challenge to Mr Baiocco's evidence that Capax Discovery "*did not make any attempt to license Autonomy software to the FSA or participate in setting the terms of the license that I understand Autonomy sold to the FSA*".

(4) The Claimants' written opening specifically noted that this email would be explored with Mr Kanter in cross-examination. In particular, the Claimants would have challenged Mr Kanter to identify precisely what "*contribution*" to the FSA transaction on the part of Capax Discovery had so "*impressed*" him. The Claimants contended that the only truthful answer Mr Kanter could have given is that Capax Discovery made no contribution to the FSA transaction, and that Mr Kanter's email was, therefore, pretextual.

[19] [Deleted].

(5) Dr Lynch in cross-examination sought to justify Mr Kanter's email on the basis that Capax Discovery "*were doing a lot of the work to actually show the technology and use it for FSA*". However, it was not put to Mr Baiocco in cross-examination that Capax Discovery had started doing any work for the FSA by 6 October 2010, and there is no evidence to that effect.

(6) The same day, 6 October 2010, Mr Kanter sent a letter to Mr Baiocco, which was in essentially the same terms as the MAF letter for the Eli Lilly transaction. The letter again described Capax Discovery as Autonomy's "*Referral Partner*" and purported to record that Capax Discovery was to introduce Autonomy into deals with the FSA, obtain quotes from Autonomy on behalf of the FSA and assist in executing purchase orders and contracts.

(7) It was the unchallenged evidence of Mr Baiocco that Capax Discovery "*did none of these things; and I never discussed any of this with Autonomy*".

(8) After the necessary internal approvals, on 7 October 2010, Autonomy paid the $450,000 fee to Capax Discovery.

204. As in the Eli Lilly transaction, it is not the payment of a MAF which is objectionable; it is the confected basis for paying it which invites the conclusion that Mr Kanter, Mr Egan and also Mr Hussain were aware that Capax Discovery had done little or nothing to merit such a payment. I am not persuaded by the argument that Mr Kanter's letter of 6 October 2010 was simply an inapt deployment of a standard form: I consider its wording was chosen to present a justification to Deloitte because the truth that Capax Discovery had in substance done nothing would have invited a potentially difficult line of enquiry.

Summary as to propriety of recognition of revenue in respect of VT10

205. In my judgment, for all these reasons, some common to VT2 and VT3, others particular to VT10 itself, the recognition of revenue from the sale to the VAR in the context of VT10 was not proper.

Defendants' alleged knowledge of false accounting in respect of VT10

206. As to the necessary second limb of their case, that the Defendants both knew that the accounting treatment of VT10 was false, the Claimants relied on the following.

Mr Hussain

207. As regards Mr Hussain, and in addition to his alleged role in encouraging and giving guidance to Mr Egan in the use of VAR transactions to accelerate revenue when required to meet revenue targets or forecasts (which I have discussed above):

(1) Dr Lynch thought it was either Mr Egan or Mr Hussain who had identified Capax Discovery as the appropriate VAR to use in the emergency that developed.

(2) Mr Hussain knew at the time of the direct deal that Deloitte were concerned about the fact that some earlier VAR transactions had been replaced by direct deals: he was sent (and sent on to Dr Lynch) Deloitte's report to the Audit

Committee for Q3 2010 noting that *"no value added reseller deals have been reversed this quarter and re-signed directly with the end-user"*.

(3) It was also Mr Hussain who, with Mr Chamberlain, devised and put in place the process for Capax Discovery to remain legally liable unless and until the FSA paid Autonomy, whereupon the receipts from the FSA would be taken as a credit against Capax Discovery's indebtedness.

(4) Mr Hussain concurred in Mr Kanter's recommendation of payment of a MAF to Capax Discovery for its *"contribution to the FSA transaction"* though he must have known that Capax Discovery had made none in terms of assisting the end-user transaction.

(5) It was Mr Hussain who made the initial proposal for the NearPoint ramp-up fee, and it was Mr Hussain also who coordinated the payment of the fee to Capax Discovery and Capax Discovery's same day payment of the two VT10 outstanding instalments to Autonomy.

Dr Lynch

208. As regards Dr Lynch:

(1) It was he who, two days before the quarter end, sent Mr Hussain a document listing transactions that needed to be concluded in order for Autonomy to achieve its total revenue target for Q1 2020. The list identified [$]4 [million] as coming from *"FSA Partner"*, which Dr Lynch accepted referred to the use of a VAR.

(2) Dr Lynch denied thereby instructing Mr Hussain to do so, but he accepted that he was at least content that Mr Hussain should, introduce a VAR whereby to enable Autonomy to recognise revenue on the sale to that VAR: he told me that he did not *"have any issues about partners being involved in deals"*.

(3) On 30 March 2010, Dr Lynch sent the list referred to in sub-paragraph (1) above, apparently envisaging that MicroTech would be the VAR of choice.

(4) Mr Hussain kept Dr Lynch closely informed by email of the transactions needed to reach the target, sending a sequence of updated versions of a *"revenue route-map"* document.

(5) It was Dr Lynch who appears from one of such exchanges to have suggested the use of *"cx"* which he accepted was a reference to Capax Discovery, referring in the subject line of one email to *"midnight Italy"*, signifying close involvement going well beyond the overall strategic role which Dr Lynch sought to depict, and at least an awareness in the context of the importance of different time zones.

(6) Mr Chamberlain and Mr Hussain kept Dr Lynch closely involved as to what deals were ultimately included on the revenue recognition tally.

(7) Dr Lynch confirmed that an agreement with the UK financial regulator was an important win for Autonomy and that he would probably have been told about

it. However, he did not think he would have known anything about how the deal was negotiated.

(8) Although he told me that he was not normally sent Deloitte's reports to the Audit Committee that does not appear to have been wholly accurate. In any event, even if he was not on Deloitte's circulation list for these purposes there is documentary evidence of covering emails from Mr Hussain sending him such material fairly routinely; certainly, it appears that Mr Hussain sent him the report for Q3 2010 which included the note on page 6 that no VAR deals had been reversed in the quarter. I think it likely that the issue was topical: I think it likely that, having been sent it, Dr Lynch would have read it.

(9) Dr Lynch told me that he was not involved in and knew very little about the direct deal, and that included the payment of a MAF: although, in the latter context, he suggested reasons why the payment of a MAF could be justified. He emphasised the point that he was not on any of the emails relating to the agreement to pay a MAF for Capax Discovery's *"contribution"* nor was it suggested that he was responsible for approving it.

(10) Dr Lynch does not appear to have been sent any of the various emails relating to Mr Baiocco's concerns about his aging debt (see above) but he did approve the agreement for the NearPoint ramp-up fee and the early payment of that fee.

Summary as to whether the Defendants had "guilty knowledge"

209. I have concluded that both the Defendants knew that, in accordance with the 'pattern', Capax Discovery's role in the FSA VAR deal was nominal and that Capax Discovery was not intended to pay or do anything. I think it more likely than not, and I find, that they each knew that the VAR sale should not have triggered revenue recognition.

Conclusions on Capax Discovery transactions VT2, VT3, VT4 and VT10

210. The examples I have addressed at some length earlier seem to me to provide a representative sample, in the sense of illustrating features relied on by the Claimants as demonstrative of the 'pattern' on which they relied and the Defendants' answer.

MicroTech impugned VAR deals: VT5, VT6, VT7, VT8, VT13, VT25, VT32, VT33 and VT37

211. I turn next to identify particular features of the nine VAR deals between Autonomy and MicroTech which were impugned by the Claimants.

MicroTech itself and the MicroTech VAR agreement

212. MicroTech was described by the Claimants as *"a friendly VAR of choice"*. As will be recalled, it was one of the *"Truitt companies"*. Mr Steve Truitt was its COO, Mr Jimenez its owner (who had decision making power). I have described MicroTech itself and Mr Steve Truitt's perception of the various transactions in my overview of his evidence in paragraphs 2036 to 2048 in the main body of the judgment.

213. Autonomy's VAR transactions with MicroTech during the Relevant Period accounted for over $43 million of Autonomy's reported revenue. Each was for a sum exceeding $1,000,000.[20]

214. All the purchase orders for the impugned MicroTech VAR transactions were governed by the June 2006 MicroTech VAR agreement, entitled *"Autonomy Government Reseller Agreement"* ("the June 2006 MicroTech VAR agreement").

215. Like the agreement between Autonomy and Capax Discovery, the June 2006 MicroTech agreement, which was governed by the law of the State of California, made it clear that MicroTech was legally on risk and that the written contractual terms constituted the entire agreement between the parties and could not be modified except in writing signed by an authorised representative of each party.

216. More particularly:

(1) MicroTech was obliged to pay Autonomy unconditionally, irrespective of whether it closed a deal with an end-user. Clause 5.5 provided:

> *"Government Reseller shall not be relieved of its obligations to pay fees owed to Autonomy hereunder by the nonpayment of such fees by an End-User."*

(2) No amendment to, change, waiver or discharge of any provision of the agreement was valid unless in writing and signed by an authorised representative of each party (clause 14.4). The agreement also superseded any pre-printed terms and conditions that could appear on any purchase order (clause 5.1).

(3) Once Autonomy's products on a purchase order had been shipped, MicroTech could not cancel or amend the purchase order without prior written consent from Autonomy (clause 5.1).

(4) There was a comprehensive entire agreement clause which confirmed there were no other representations, understandings or agreements. Clause 14.10 provided:

> *"This Agreement and the Exhibits to this Agreement represent the entire agreement between the parties with respect to its subject matter, and there are no other representations, understandings or agreements between the parties relative to such subject matter."*

[20] 1. VT5 MicroTech/DiscoverTech is licence fee of $9,532,810 plus $476,190 support and maintenance.
2. VT8 MicroTech/Morgan Stanley is $4,656,000 licence fee plus $232,800 support maintenance.
3. VT6 MicroTech /Honeywell is licence fee of $1.8m and $90k support and maintenance.
4. VT7 MicroTech / ManuLife is licence fee of $1.08m and $104k support and maintenance.
5. VT13 MicroTech /Vatican Library is $11m licence and $550,000 support and maintenance.
6. VT25 MicroTech /US DoI is licence fee of $4m and support and maintenance of $200k.
7. VT32 MicroTech /Bank of Montreal is licence fee of $2,880,000 with maintenance and support of $144,000.
8. VT33 MicroTech / Xerox is license fee of $1,170,000 and maintenance and support of $58,500.
9. VT37 MicroTech /HP is licence fee of $7m with support and maintenance of $350,000.

217. In each of the impugned MicroTech VAR transactions MicroTech provided debtor confirmations directly to Deloitte, stating amongst other things that there were no side agreements or understandings with regard to the purchase orders and/or invoices referable to the transactions impugned. Mr Steve Truitt regarded them as accurate at the time, though it will be recalled that he came to be persuaded by the US prosecutors that the assurances he understood he had been given that somehow MicroTech would have the means to pay its debts effectively amounted to a side agreement.

218. The Defendants' case was that MicroTech was on risk in respect of each of the reseller transactions; and MicroTech acquired on transfer of the relevant software management control of it such as to comply with the accounting rules.

219. They relied on the contractual documentation which specifically stipulated the passing of risk and management control, and furthermore precluded any side-agreements which might affect those legal criteria. They added that there were no relevant discussions between Mr Egan and Mr Steve Truitt and that Mr Steve Truitt was clear about that in the evidence that he gave the US criminal court. Mr Steve Truitt also stated that he had never spoken to or met Mr Hussain, marked by Claimants as intended to be relied on.

220. The Defendants' case in summary was that given the documentation, there was nothing that could have been said which would have altered the fact that MicroTech was on risk, but nothing material was said in any event.

221. As in the context of the Capax Discovery sales, I turn to deal with examples of the impugned MicroTech VAR sales, starting with VT6, VT7 and VT8. (I address VT5 later, since it was an exception in that no side agreement was alleged).

VT6, VT7 and VT8: MicroTech/Honeywell, Morgan Stanley, ManuLife, all Q4 2009

222. Autonomy had tried to make sales to each of Honeywell, Morgan Stanley and ManuLife in Q4 2009, but was unable to close any of them prior to the end of the quarter. The failure to close the three deals left, in the Claimants' words, *"an unwanted gap in the revenue"* for Q4 2009.

223. The prospective deal with Morgan Stanley was substantially the largest of the three, and was described by Dr Lynch in an email of 26 December 2009 to Mr Hussain, Mr Egan, Mr Scott and Mr Mooney as being of *"criticality to the quarter"* .

224. Mr Hussain was personally involved in the proposed transaction, and according to an email dated 31 December 2009[21] from him to Mr Christian Lucas, Managing Director of Morgan Stanley Investment Banking who advised Autonomy from time to time, seeking urgent help on the last day of the quarter/year in trying to conclude it, it had *"suddenly been stopped by someone in [Morgan Stanley] legal"*. In the event, no part of the transaction, including the sale of hardware, was concluded by quarter end, leaving a considerable shortfall on revenue expectations.

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[21] The legal difficulty was not explained. The email was relied on by the Defendants in support of an argument that hardware sales at a loss fertilised (as it were) software deals, and in the email Mr Hussain stressed that *"the fact that we show value for the software and are selling hardware at a loss in our proposal is a commercial decision for us."* This might suggest that this may have been the origin of the legal query: but this was not explored and I can take it no further.

225. The other two deals failed to close also:

(1) On 24 December 2009, an internal Autonomy email sent to Mr Avila (among others) recorded that no deal had closed with Honeywell Aerospace.

(2) On 28 December 2009, an internal Autonomy email stated, as regards a proposed sale to ManuLife, that "*Unfortunately – this does not look like it will make the Dec 31 timeframe we all hope for*".

226. Mr Egan's evidence in his witness statement, which was not challenged in this respect, was that on 30 and 31 December 2009 he asked Mr David Truitt if MicroTech would agree to purchase a number of "at risk" deals, including these three deals. Mr Egan stated further that the purpose of these deals:

> *"…was to get the revenue associated with the corresponding prospective end-user deals into the fourth quarter of 2009."*

227. Following Mr Egan's conversation with Mr David Truitt, MicroTech submitted purchase orders to Autonomy:

(1) A purchase order for end-user Honeywell, with a licence fee of $1.8 million and $90,000 support and maintenance (VT6);

(2) A purchase order for end-user ManuLife, with a Digital Safe licence fee of $1.08 million and $104,000 support and maintenance (VT7); and

(3) A purchase order for end-user Morgan Stanley, with a licence fee for identified software of $4,656,000 plus $232,800 support and maintenance (VT8).

228. Autonomy recognised the licence fees on all three purchase orders as revenue as at 31 December 2009.

229. As with the other MicroTech reseller transactions, these deals were governed by the terms of the June 2006 MicroTech VAR agreement (see paragraph 214 above) which provided expressly that MicroTech was obliged to pay Autonomy for its orders unconditionally, irrespective of any sale to an end-user, that there was no other understanding or arrangement between the parties, and that modifications must be in writing.

230. Mr Steve Truitt gave evidence in respect of these deals that MicroTech knew it was on risk but wanted to do the deal because of the prospect of establishing a new customer relationship and providing services. His evidence was that MicroTech entered into three other at risk transactions at around the same time. The Claimants have not sought to impugn those transactions.[22]

231. MicroTech signed debtor confirmations in respect of these deals, each of which both Mr Steve Truitt and Mr Egan later confirmed was true and accurate. Thus:

[22] The transactions were for end-users KPMG, Assurion and CenturyLink. Steve Truitt referred to them in his testimony in the US trial against Mr Hussain.

(1) Honeywell: MicroTech provided written confirmation to Deloitte on 13 January, 8 July and 15 October 2010 that the invoices listed in the confirmations were proper and due, and that there were no "*side letters or other agreements*".[23]

(2) ManuLife: MicroTech provided written confirmation to Deloitte on 13 January 2010 that the invoices listed in that confirmation were proper and due, that there were no "*side letters or other agreements*", and that Autonomy retained no continuing managerial involvement.[24]

(3) Morgan Stanley: MicroTech provided written confirmation to Deloitte on 13 January 2010 that the invoices listed in that confirmation were proper and due, that there were no "*side letters or other agreements*", and that Autonomy retained no continuing managerial involvement.[25]

232. However, no-one at MicroTech had any relationship with any of the three proposed end-users, nor any knowledge of the state of negotiations thus far. Mr Steve Truitt confirmed in his deposition evidence in the MicroTech proceedings in the US (which was admitted in these proceeding as hearsay evidence) that he did not speak to any of them before (as it were, blindly) submitting MicroTech's purchase orders.

233. It was thus not intended by anyone that MicroTech should, following the submission of the purchase orders, make any effort to negotiate, or conclude, an onward sale to any of the three end-users; and MicroTech did not do so. At the US criminal trial, Mr Steve Truitt testified (and this testimony was likewise admitted as hearsay evidence) that:

> *"We didn't know anybody at these end-users, first of all. Secondly, the circumstances about why these opportunities were available was ostensibly that these were very late in the sales cycle with the Autonomy sales team. They were going to close imminently so there would be no need for our involvement to attempt to sell it. We would just, if all worked out well, service these accounts after they closed."*

234. In the event, MicroTech made no approach to any of the end-users to try to get follow-on business either, even though Mr Steve Truitt had given the prospect of doing so as a central part of the rationale for doing each VAR deal.

235. I cannot accept that the above is compatible with any genuine sale. I cannot accept either that it is consistent with any real expectation on Mr Steve Truitt's part that MicroTech could be left "on the hook" if the end-user deals did not eventuate. That would go a long way beyond commercial insouciance, especially given Mr Steve Truitt's acknowledgement (at the US criminal trial, in evidence also admitted in these proceedings as hearsay) that if MicroTech had really been left "on the hook" that *"would have been disastrous for MicroTech"*. Nor can I accept that Autonomy ever relinquished managerial control or involvement: it was always to be the supplier of the software to the end-user if a contract eventuated, and MicroTech had no say or input at any stage or in any way.

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[23] The signature on the first of these is dated '1/13/2009' – presumably a typographical error.
[24] See the footnote above in relation to the signature.
[25] *Ibid.*

236. That conclusion is fortified by what actually occurred:

(1) No deal was concluded with Honeywell by either MicroTech or Autonomy: MicroTech purported to pay Autonomy what it owed under the purchase order, but it is said by the Claimants that it was enabled to do so only by Autonomy's payment to MicroTech in respect of a transaction in Q4 2010 called "the ATIC transaction" which is discussed below.

(2) In March 2010, Autonomy entered into a larger, direct, deal with ManuLife. Shortly afterwards, Autonomy issued a credit note to MicroTech for $1,184,000. Later, in April 2010, Autonomy paid MicroTech a MAF of $118,400, followed by a further MAF of $101,908 in August 2010.

(3) In February 2010, Autonomy entered into a direct deal with Morgan Stanley for $5,288,800: however, this was for the sale of hardware, and not (nor anything like) the software (including DS Mail, Introspect and Autonomy Sharepoint Connector) which had been sold to MicroTech with a view to onward sale to Morgan Stanley. Nevertheless, in March 2010, a credit note was issued to MicroTech in the amount of $4,888,800. Autonomy thereafter (in April 2010) paid MicroTech a MAF of $488,880 (10% of the value of the original VAR deal).

237. In summary, therefore, in all three cases, Autonomy saw to it that one way or another MicroTech's ostensible liability was addressed, and MicroTech was rewarded by MAFs totalling $709,188.

238. In addition to the usual 'pattern' which these transactions further demonstrated, the Claimants relied on three specific matters in respect of them as showing that revenue ought not to have been recognised at the point of the VAR deals in respect of any of them:

(1) The automatic acceptance that a later direct deal of whatever nature would be treated as negating the VAR deal invoice and releasing MicroTech from continuing liability: the Claimants referred me in particular to an email dated 4 February 2010 from Mr John Cronin (an ex-employee of Autonomy who, though an independent contractor, effectively acted first as MicroLink's and then MicroTech's sales manager) to Mr David Truitt which seems to suggest an automatic assumption that a direct deal would be treated as negating the VAR deal invoice:

> *"The large trans, Morgan Stanley, is happening any moment. However, it will probably be going directly to Autonomy per customer request. A credit of some type will be issued to negate that invoice. MicroTech will still get the fee.*
>
> *Will have updates on the other trans shortly".*

(2) The fact that the reversals of the ManuLife and Morgan Stanley VAR deals (VT7 and VT8) troubled Deloitte and prompted them to give a warning in their report to the Audit Committee for Q1 2010 that:

> *"Management alerted us to the fact that two deals sold to Microtech in Q4 2009 have been credited in this quarter and resold directly to the two end-users. This was as a result of the end-users wanting to transact directly with Autonomy. This reduced the profit in the period by approximately $4 million. As there is no significant history of deals being reversed in this way, management has recognised the revenue at the point of sale to the reseller. Management has confirmed that these were isolated incidents which are not expected to be repeated in future periods.*
>
> *...*
>
> *...With regards to the reversal of revenue on two sales to the reseller Microtech in the quarter, we highlight to the Audit Committee that any further evidence of revenue reversals may jeopardise management's ability to recognise revenue at the point of sale to the reseller".*

(3) The fact that MicroTech was first released from its obligations under the Morgan Stanley VAR purchase order and was then paid a MAF, even though the ultimate end-user transaction between Autonomy and Morgan Stanley for the supply of hardware had nothing really to do with the VAR deal for the purchase of software, and the 10% fee paid cannot have represented compensation to Micro Tech for lost margin (a sale of hardware never being in its contemplation).

239. The Defendants emphasised that Deloitte carefully reviewed the deals and approved the revenue recognition; and it is necessary to consider how or on what basis it is that they came to a conclusion so different than seems to me to emerge from a consideration of the matters addressed above.

240. The starting point is to clarify Deloitte's basic approach. In summary, this was based on the only relevant sale being the sale to the VAR, and on the characteristics of that sale being determinative of the issue of compliance with IAS 18.14 for revenue recognition purposes. Deloitte then took from this that, provided that the VAR sale fulfilled the criteria in IAS 18.14, the VAR's arrangements with the specified or any other end-user were not of concern. In consequence, as Mr Welham put it in his witness statement, Deloitte

> "*did not therefore seek to interrogate either Autonomy or third parties as to the subsequent negotiations of the VAR's sale to the proposed end-users*".

241. This approach reflected, indeed implemented, Autonomy's insistence (which Deloitte well understood) that the position with the end-user was an irrelevance. When, for example, a senior associate at Deloitte queried with Mr Stephan the status of discussions with the end-user (called Sprint/Century Link) in the context of a VAR deal in January 2010 with MicroTech which has not been impugned, he received a dusty response. The associate had asked for supporting documentation in respect of the proposed end-user sale and *"...assuming this* [the sale to the VAR] *was put through Microtech late on, if we could see support of Autonomy's negotiation during the quarter direct with end-user that would be useful; or any discussion/agreement with Autonomy and end-user to go through a VAR."* Under cover of an email to the associate stating *"Steve sums it up pretty neatly I*

think", Mr Stephan forwarded in response a reply dated 12 January 2010 from Mr Chamberlain (to whom Mr Stephan had referred the query), which read as follows:

> *"I don't care if Microtech have closed their deal with Century Link. I have an order from Microtech not Century Link. I am providing maintenance to Microtech not Century Link.*
>
> *Microtech have an obligation to pay us irrespective of whether they get paid by Century Link or indeed close an order with Century Link. The issue is whether or not MT have capacity to pay. Nothing else."*

242. Mr Welham was asked in cross-examination whether he agreed also that the issue of credit notes, in effect releasing the VAR from liability under the purchase order where a direct deal had taken place, was a commercial decision which raised no issues of principle or caused any difficulty with the decision to recognise revenue from the VAR deal, so long as they remained exceptional items. Mr Welham (somewhat ruefully, it seemed to me) replied *"That was what was explained to us, yes",* though he did stress the caveat that it had to be exceptional and *"not something which happens regularly".*

243. He was also asked to confirm that, in light of Mr Hogenson's concerns, Deloitte had re-reviewed the three transactions presently under consideration. That prompted a more guarded response:

> *"Q…Again, Deloitte re-reviewed these and were content with the accounting treatment, weren't they?*
>
> *A. Yes. Albeit, as we've said before, we did then raise the point with regard to the fact that, if this was a pattern of events, then it would impact revenue recognition going forward.*
>
> *Q. Well, that's the point that we've discussed a number of times today. That's the point about probabilities and whether, as you explained it earlier on, there might need to be some sort of reduction to reflect the probability?*
>
> *A. Yes, <u>or change the whole policy if it's happening across all VAR transactions, yes."</u>* [My emphasis]

244. That caveat (as underlined) was an important one; but even that was later glossed by Deloitte to accord with their client. Deloitte's later memorandum dated 13 January 2011 on proposed changes to the VAR agreement to provide (in effect) for the VAR to be entitled to be paid out of any direct deal an amount to hold it harmless against its obligations under its purchase order also noted, in relation to the four deals from 2009 that had gone direct (including the above three deals), that:

> *"When compared to the number of deals done through VARs (c60 per annum) historical occurrences that would trigger this clause (hereafter "Direct Sales") have been rare.*

Four deals from 2009 were noted that subsequently became Direct Sales, three of which eventually being signed with Autonomy in 2010. Whilst large in the context of the average deal size, they were not material (total value c60% of materiality).

Since the Phillip Morris and Citigroup deals that were signed as Direct Sales in Q2 2010 there have been no further Direct Sales.

Based on this, management's assessment that the probability of current VAR deals becoming Direct Sales in the future is remote is considered reasonable.

Total license revenue recognised in the quarter on VAR PO's with the above clause present is $14.6m, over four deals. The largest of these deals accounted for $7m of the total figure.

Given the total value of these deals and the low number of VAR deals that actually became Direct Sales (based on a historical average for 2009/2010 of <1 deal per quarter, we would not expect there to be any Direct Sales in Q4), the likelihood of material misstatement of revenue based on the above is deemed low."

245. In all this, what, having in effect been warned off, Deloitte did not apparently know, and certainly what they did not factor in, was that the VAR sale was not intended or expected to result in the VAR doing anything at all, or paying anything out of its own resources. Even Mr Chamberlain's terse and vigorous response quoted above seems to me to be premised on there being an expectation of some real activity and exposure on the part of the VAR to signify a real change in the position of the parties to the VAR sale with respect to the control of the product and who would bear the risk of an end-user sale not eventuating. That is so even if, on Mr Chamberlain's approach, the nature of that activity was considered not relevant for accounting purposes. Put another way, Mr Chamberlain's approach assumes that the VAR sale has real economic substance; the question it overlooks is whether that is so, or whether the substantive reality is that the "true sale" was the envisaged sale to the end-user, and Autonomy's "true customer" was that end-user, and the VAR sale was all form and no substance. The assumption of legal risk is not determinative if it is never in reality intended or expected to be visited on the purchaser; and the delivery of the product is of no real consequence if it is never intended to be or in fact used or dealt with by the purchaser before its cancellation once the "true sale" has been either accomplished or abandoned.

246. The Defendants sought to downplay the caveats rather tamely introduced by Mr Welham, predominantly on the footing that in comparison to the universe of VAR deals done by Autonomy (though neither their number nor any detail was ever provided) the number of cancelled VAR deals was very small. But that is not, in my judgment, the right comparator to assist in the detection of a pattern. A proper comparator was the universe of VAR deals over $1 million with a 'friendly' VAR which had either been replaced by 'direct' deals or cancelled. The ratio revealed a pattern. The fact that the impugned VAR deals were egregious, in the sense of being different from the standard, does not alter this.

247. In my judgment, therefore, the fact that Deloitte went along with their client does not absolve the latter: the accounting treatment was wrong. This is not a case against Deloitte,

who settled the claim against them by HP. So I need not decide whether this was primarily because Deloitte were misled (as they were) or beholden to and leant on by their client (as also they were) or simply mistaken (as they were): the point is, as I have concluded, that their approval provides no escape from the conclusions I have expressed above, nor ultimately assistance to the Defendants.

Defendants' knowledge of and participation in VT6, VT7 and VT8

248. Mr Hussain was plainly involved in all three VAR deals and the subsequent direct sales.

249. Dr Lynch did not mention any of the three transactions in either of his two witness statements. In cross-examination, he maintained his position that he had had very little dealing or involvement in these deals; but he accepted that he probably knew that they were entered into at around the quarter-end:

> *"Q. Do you accept that you knew either at the time they were entered into or at any rate early in 2010 that Autonomy had entered into these transactions with MicroTech?*
>
> *A. I doubt if I knew when they were being entered into, but I would probably have seen a sheet listing deals for the quarter at the end."*

250. Mr Hussain sent a spreadsheet to Dr Lynch on 1 March 2010 (i.e. a couple of months later) which recorded that the "*Honeywell*" and "*ManuLife*" (VT6 and VT7 respectively) transactions had been entered into with MicroTech. It seems to me surprising that he was not aware of the three MicroTech deals before then. Certainly in the case of VT8 (Morgan Stanley), Dr Lynch's email dated 26 December 2009 emphasising the deal's *"criticality to the quarter"*, shows that he was aware of and abreast with the Morgan Stanley deal from its earliest stage. Further, Mr Hussain forwarded to Dr Lynch his 31 December 2009 email seeking to enlist the help of Morgan Stanley's Mr Lucas; on 5 January 2010 he sent Dr Lynch a reconciliation spreadsheet showing (in the *"IDOL summary worksheet"* and next to an entry *"dell – morgan stanley"*) a figure of $4,656,000 of revenue; and on 12 April 2010, he sent Dr Lynch an email subject-headed *"audit update"* stating that *"MT is okay (subject to some evidence)"*.

251. It was suggested to Dr Lynch in cross-examination that he *"knew that MicroTech was serving the same role as we've seen Capax Discovery serve in the Kraft and Eli Lily transaction, namely to act as a placeholder by submitting a purchase order which Autonomy could use to recognise revenue improperly*". In closing submissions, Dr Lynch objected to this question, on the basis that it invited him to subscribe to the Claimants' own dictionary, *"placeholder"* being their description of the role played by the VAR in the impugned VAR transactions. At the time, Dr Lynch simply reiterated that he had had very little involvement, but emphasised that what he did understand was MicroTech considered that *"it was on risk in all of these deals".* That was the case as far as the legal position went, and:

(1) Mr Steve Truitt's evidence was that he was genuinely purchasing the software and wanted to establish a relationship with the end-user and to *"service these accounts after they closed"* (in relation to the Kraft and Eli Lilly transactions Mr Baiocco's evidence was to the same effect).

(2) Neither Mr Egan nor Mr Steve Truitt (or Mr Baiocco in relation to the Kraft and Eli Lilly transactions) thought that there was anything improper, and Mr Egan thought that revenue was being properly recognised.

252. The Claimants did not cross-examine Dr Lynch on any specific documents. The Defendants dismissed the cross-examination of Dr Lynch as *"perfunctory"*. It was submitted for Dr Lynch that:

(1) There was no explanation or exploration in the cross-examination as to the basis on which Dr Lynch is supposed to have thought that these deals had been entered into in order to enable improper revenue recognition;

(2) The Claimants did not identify any information Dr Lynch had that was not also known to Deloitte whose job they said it was to check revenue recognition;

(3) The Claimants put to Dr Lynch that he *"knew it was improper to pay a fee to MicroTech for its involvement in the transactions"* but did not indicate or put to Dr Lynch any basis on which Dr Lynch was supposed to know that the payment of a MAF was improper.

253. As to these points:

(1) It is true that the Claimants did not put any specific documents to Dr Lynch to demonstrate knowledge of impropriety in the three transactions. They relied on Mr Hussain's knowledge of the facts, what the facts revealed as to the transaction's lack of real substance and what was kept from Deloitte.

(2) I have described what Deloitte were not told and did not know: they were warned off any enquiry as to the VAR's engagement with the end-user which might have revealed the facts that demonstrated that the VAR was to do nothing and pay nothing, which would have disqualified the transactions for revenue recognition purposes.

(3) I would accept that no specific additional reasons were put to Dr Lynch as to the impropriety of the payment of MAFs to compensate the VAR for going on risk in respect of an adventure ultimately not pursued: but that in my view comes back again to whether any real risk was assumed.

254. In summary: I have concluded that these three transactions demonstrate, and illustrate, the pattern which the Claimants identified and relied upon; they add little to the issue of knowledge; but for more general reasons explained above, I consider that both Defendants knew that the VAR sale lacked substance and was indeed a *"placeholder"* for the *"real sale"* to the *"true customer"*.

VT5: Autonomy/MicroTech sale of 'Control Point' licence in Q4 2009

255. VT5 was a transaction between Autonomy and MicroTech for the sale of a perpetual licence for the 'Control Point' module (which included some IDOL server software called "Retrieval Lite", though not full-blown IDOL capability). The licence fee was $9,523,810 and there was a first-year support fee of $476,190. The prospective end-user was

DiscoverTech. The sale to MicroTech was on the terms of the June 2006 MicroTech VAR agreement, summarised in paragraph 216 above.

256. The Claimants' claims in respect of this transaction, which arose in connection with the acquisition by Autonomy of MicroLink, (see paragraphs 36 to 44 above) were different from those made in relation to other impugned VAR transactions. It was, on the Claimants' case, another example of revenue generation through a series of transactions in a circle: it was not in reality a VAR transaction, as explained below. In particular, the Claimants did not allege that there was any side agreement or understanding in the context of VT5 such as to (on their case) alter the true substance of the arrangements; and there was no direct sale. However, the transaction throws light on the relationship between the Truitts and Mr Hussain and Mr Egan, and their willingness to devise or structure transactions for the sole substantial purpose of showing revenue in Autonomy's accounts.

257. According to the Claimants, the essence of VT5 was that when Autonomy acquired MicroLink for $55,000,000 it designedly overpaid Mr David Truitt and Mr Tim Wharton (Mr David Truitt's minority partner in both MicroLink and DiscoverTech) by $10,000,000 (see paragraph 42 above) with a view to their new company, DiscoverTech, then having the funds to pay MicroTech for DiscoverPoint and Control Point software, enabling MicroTech then to pay Autonomy under VT5.

258. The Claimants relied on Mr David Truitt's evidence in his deposition in the MicroTech trial, which was verified by reference to documents evidencing each of the payments and was adduced as hearsay evidence in these proceedings, as follows:

> *"Q. And the way the transaction worked was that Autonomy paid $55 million in the aggregate for the purchase of MicroLink; is that right?*
>
> *A. Yes.*
>
> *Q. Okay. 80 percent to you, 20 percent to Mr. Wharton; is that right?*
>
> *A. Yes.*
>
> *Q. Okay. And some of that money was put in an escrow for a period of time; is that right?*
>
> *A. Yes. That's correct.*
>
> *Q. And then you and Mr. Wharton deposited funds into Discover Tech's bank account, which together amounted to $10 million; is that right?*
>
> *A. Yes.*
>
> …
>
> *The way the software side of the equation worked was that Autonomy licensed the software to MicroTech as the reseller and MicroTech resold that software to Discover Tech?*
>
> *A. Yes, sir.*
>
> *Q. Okay. And then Discover Tech paid MicroTech $10 million for the software and MicroTech paid $10 million to Autonomy all on substantially the same day?*

A. Yes, sir.

Q. So you got paid on January 4th, 2010; is that right?

A. Yes.

Q. And you and Mr. Wharton put the money in Discover Tech on January 4th or 5th; is that right?

A. Yes.

Q. And then on January 4th or January 5th that money then was flowed by Discover Tech to MicroTech; is that right?

A. Yes.

Q. And on January 6th, MicroTech paid Autonomy the same $10 million?

A. I believe that's correct, yes."

259. In addition, the Claimants relied on the following as demonstrating the contrived and circular nature of the arrangements:

(1) An email dated 18 November 2009 from Mr David Truitt to Mr Hussain, in which Mr David Truitt suggested the transaction be structured so as to generate revenue:

> *"What I was thinking was that we would include the purchase of DiscoverPoint in with the Control Point OEM, <u>so Autonomy would show revenue on both products in the 10 million dollar order</u>. So total at closing for the MicroLink purchase would be 55 million with an immediate purchase of DP and Control Point OEM for 10 million from the New Company. I would take about 6 people from the development staff and one or two commercial sales reps (probably would not be needed by Autonomy anyway) and I would eventually transition out to run the new company when everything is running smoothly with MicroLink/Autonomy group. Autonomy would retain their rights to all of our other SW IP, including our AIS (Autonomy Integration Suite) and fetch framework. We can go through specifically what I would want to take with DP IP but that is the general concept…."* [My emphasis]

(2) The fact that the price of $10,000,000 originally proposed by Mr David Truitt for two pieces of software (DiscoverPoint and Control Point) remained the same even though, at Mr Hussain's suggestion according to Mr David Truitt[26], DiscoverPoint was spun out to DiscoverTech before the acquisition and Autonomy ended up selling only Control Point to DiscoverTech (through

[26] In his deposition evidence in the MicroTech proceedings in the US Mr David Truitt said: *"I thought it was going to work a bit differently where they were going to sell me the software, our software, that MicroLink had built. But in further conversations, it – you know, [Mr Hussain] preferred me to do the larger Control Point deal and allow me to take the software for free."*

MicroTech) but for the same $10,000,000 price, suggesting arbitrary pricing and/or contrived attribution of value;

(3) The fact that (as Mr David Truitt confirmed in his deposition in the MicroTech proceedings) DiscoverTech never managed to sell Control Point to anyone, suggesting that it was worth little and certainly less than the price attributed to it;

(4) The fact that DiscoverTech paid MicroTech on 5 January 2010 and MicroTech paid Autonomy on 6 January 2010, even though MicroTech had 30 days (i.e. until 29 January 2010) to pay, a suggested indication of a circular and contrived transaction;

(5) The fact that Mr Scott and Mr Kanter knew (and stated in an email) that the money would need to *"go through 3 wires"*, signifying transfers from Mr David Truitt (as part of the proceeds of the sale to MicroLink) to DiscoverTech, then to MicroTech and finally to Autonomy is again suggestive of contrivance and circularity;

(6) The fact that the original proposal from Autonomy was that 10% of the purchase price for the MicroLink acquisition should be placed in escrow, yet the escrow amount was only $4,500,000, suggesting a real purchase price of $45,000,000, and the contrivance of additional circular payments of $10,000,000 to give the appearance of revenue generation. This was confirmed by Mr David Truitt in his deposition evidence in the MicroTech civil proceedings:

> *"Q. ...And so it is correct that the escrow amount was $4.4 million, which was 10 percent of the $55 million that you got paid minus the $10 million that you paid back to Autonomy?*
>
> *A. Yes, that's true."*

260. The Defendants' answers were that:

(1) Mr David Truitt originally wanted $60,000,000 for MicroLink; Autonomy originally offered $45,000,000; after negotiation the agreed price was $55,000,000 but DiscoverPoint was spun out before the acquisition (to the newly-formed DiscoverTech).

(2) The MicroLink transaction for $55,000,000 was at a fair value, and reflected the value placed by Autonomy more on the services side than the product side of MicroLink's business: there is no basis (nor was there any evidence) for regarding the value of either the MicroLink shareholding or the Control Point software as inflated.

(3) There was no evidence that the amount of Control Point software ultimately licenced was not fairly valued at $10,000,000; further, the Claimants' submissions overlooked the fact that (a) as part of the arrangements MicroTech received from MicroLink the DiscoverPoint IP (b) the Control Point deal included "lite" IDOL technology (though not the full IDOL suite), permitted MicroTech to use that technology in its own products, and thereby enabled Mr David Truitt to start a new company with new technology.

(4) Mr David Truitt was adamant that, contrary to the Claimants' contentions, the $55,000,000 price for the acquisition was not related to the price of the software, and that the $10,000,000 order and purchase had no relationship with the $55,000,000 acquisition amount, other than that the acquisition gave Mr David Truitt (and through him, his new company DiscoverTech) the resources and commercial reasons to make the purchase.

(5) Mr David Truitt's reference in his email dated 18 November 2009 to including the purchase of DiscoverPoint in with the Control Point OEM *"so Autonomy could show revenue on both products in the 10 million dollar order"* could not in such circumstances bear the weight sought to be placed on it by the Claimants: the suggestion was in any event odd and misplaced since (as Dr Lynch pointed out in cross-examination) it was MicroLink, not Autonomy, which owned and could sell DiscoverPoint.

(6) The escrow arrangements did not suggest a true purchase price of $45,000,000: the $4,500,000 escrow amount was what Autonomy had offered as part of its original proposal to pay $45,000,000 and the simple explanation was that it was not changed when the price agreed eventually was higher.

(7) The Claimants' theory that the purchase price for the MicroLink shares was inflated by $10,000,000 so as to fund the $10,000,000 purchase of software was commercially unrealistic, not least because it failed to take into account tax payable on the acquisition consideration.

(8) DiscoverTech's success or otherwise with its business is immaterial given that it genuinely wanted the software at the time that it bought it, as Mr David Truitt confirmed. He explained that the reason why the product integrated with Control Point faced obstacles in penetrating the market was because of Microsoft's integration of FAST search which took over SharePoint search following Microsoft's acquisition of FAST:

> *"A. We immediately integrated that software into our platform. We demonstrated that software many times. In March of 2010, Microsoft integrated their billion dollar acquisition of FAST Search that took over for SharePoint Search. So when we would go and intro our DiscoverPoint product with Autonomy Control Point and IDOL on the back, we would get, Why would I put another search engine in here if FAST was their biggest competitor? It had lots of the same capabilities. Nobody wanted to introduce complexity into their Microsoft SharePoint environment. So over time, we phased out our investment of Autonomy software and went and integrated FAST into our product and continued on with a different search engine. So the answer to the question is, no. We weren't successful, but we tried really hard."*

(9) The overall deal was approved by Autonomy's Board of Directors and by Deloitte. Deloitte noted as regards the $10,000,000 Control Point acquisition:

> *"We understand the commercial rationale for the acquisition. We have reviewed the purchase agreement and have not noted any unusual terms…"*

261. The Claimants accepted none of this. They contended that both the Board and Deloitte were misled; and that, in particular, (a) they were not told of the links through the Truitt brothers (David, Steve and Dan) between MicroLink, MicroTech, and DiscoverTech (which would have been relevant as a factor in the consideration of whether the acquisition was at a fair and proper value) (b) they were not told that addressing MicroLink's mounting debt to Autonomy under VAR transactions was part of the rationale for the acquisition and were led to believe that only a relatively small amount of the acquisition price for MicroLink represented bad debts that would need to be written off, (c) they were misled as to how MicroTech was able to finance the payment of $10,000,000 and (d) they were given a misleading impression as to the arrangements between MicroTech and DiscoverTech.

262. As to (a) in the preceding paragraph, I do not accept the Claimants' contention that Deloitte was not told of the links between the Truitts and their companies; although he had given the impression in his witness statement that Deloitte was uncertain of these links, in cross-examination Mr Welham accepted that Deloitte did know about them[27] and Deloitte's working paper on the acquisition expressly noted this. As to (b) in the preceding paragraph, there was no dispute.

263. The last two matters ((c) and (d) in paragraph 261) related more specifically to VT5 and the payment of $10,000,000, and concern certain of the answers given by Mr Chamberlain in a draft document dated 11 January 2010 entitled *"ML auditor queries"* to queries raised by Deloitte about the transaction. Thus:

    (1) Question 2(2) asked what insight Autonomy had into how MicroTech had "*financed this $10m*". The answer given was, "*The $10m was financed from their operating cash.*" The Claimants submitted that this was untrue, since the only expected source was the exceptional receipt of sale proceeds remitted through DiscoverTech.

    (2) Question 3 sought information about Autonomy's trading history with DiscoverTech and DiscoverTech's ability to finance the $10 million payment. The answer was, "*No trading history with Autonomy. We have not done a deal with them, the deal is via a reseller*". The point about DiscoverTech having had no trading history with Autonomy was factually correct, but only because DiscoverTech had only recently been incorporated. Given the close nexus between the companies and the funding arrangements, these answers were plainly misleading. The Claimants submitted that this was an attempt to create the appearance of distance between the $10 million purchase, on the one hand, and the acquisition of MicroLink, on the other.

[27] It appears from an entry in a documented response to various questions that Deloitte had about the MicroLink acquisition, someone had written against the question about the nature of such links *"Not sure. These are independent companies with different groups of shareholders"*. That may be the origin of the misunderstanding clarified by Mr Welham in cross-examination.

264. In Dr Lynch's written closing submissions, it was suggested that:

> *"This was not Dr Lynch's document and the Claimants did not challenge his confirmation that he did not see the document at the time. The author (Mr Chamberlain) was unlikely to have known how MicroTech financed the purchase, and it was reasonable to suppose that he was addressing the issue from a collectability perspective."*

265. Although the collectability point was probably fair, the rest of this explanation was weak, especially since the draft responses that Mr Chamberlain prepared were circulated to Mr Hussain and Mr Kanter. The Claimants understandably made the point that if Autonomy senior management felt they lacked sufficient knowledge of the arrangement between MicroTech and DiscoverTech to give an accurate answer to Deloitte's question, they should have said precisely that, rather than provide a misleading answer.

266. The last point to note in respect of VT5 is that MicroTech was paid $100,000 for its role, and in particular, for acquiring $10 million worth of Autonomy software for immediate resale to DiscoverTech. In his 'direct' evidence (evidence in chief) in the MicroTech proceedings in the US, Mr Steve Truitt acknowledged that this was for *"doing practically nothing"*. He added that he had entered into the purchase arrangements at the direction of and to assist his brother (Mr David Truitt) who wanted to do the deal quickly. Put shortly, on the Claimants' case, this was an improper payment to recognise MicroTech's help in portraying a false impression; on the Defendants' case it was the price of, in effect, a guarantee to ensure satisfaction of collectability tests. In my judgment, both are probably true; but the first point demonstrates impropriety whether alone or in combination with the second.

267. In summary, I agree with the Claimants' depiction of the essence of VT5 as being a contrived and circular transaction involving:

(1) An artificial and unwarranted increase in the agreed purchase price for MicroLink from $45 million (which was correctly reflected in there having been a 10% deposit of $4.5 million) to $55 million: Autonomy designedly overpaid Mr David Truitt and Mr Tim Wharton (Mr David Truitt's minority partner in both MicroLink and DiscoverTech) by $10,000,000 (see paragraph 42 above) with a view to their new company, DiscoverTech, then having the funds to pay MicroTech for Control Point software, enabling MicroTech then to pay Autonomy under VT5;

(2) Incorrect responses to Deloitte's queries about (a) the rationale of the MicroLink acquisition (b) the financial position of MicroTech (c) various disguised efforts by Autonomy to create the appearance of distance between the $10 million purchase, on the one hand, and the acquisition of MicroLink, on the other, including (d) the true arrangements between MicroTech and DiscoverTech resulting in the purchase of software in order to provide recognised revenue for Autonomy before the end of the relevant quarter and (e) the source of the $10 million eventually paid by DiscoverTech;

(3) The payment of a MAF to MicroTech as a reward not for any properly rewardable contribution but for its participation in the contrivance.

268. Apart from the payment of a MAF, the contrivance is, to my mind, laid bare in the email dated 18 November 2009 from Mr David Truitt to Mr Hussain (which I refer to at paragraph 259(1) and 260(5) above). That email included the following:

> *"What I was thinking was that we would include the purchase of DiscoverPoint in with the Control Point OEM, so Autonomy could show revenue on both products in the 10 million dollar order. So total at closing for the MicroLink purchase would be 55 million with an immediate purchase of DP and Control Point OEM for 10 million from the new company…"*

269. In my judgment, the recognition of revenue of $10 million by Autonomy in its quarterly accounts which was enabled by the contrived and circular transactions comprising VT5 was improper.

Knowledge and involvement of the Defendants in VT5

270. Mr Hussain plainly knew about VT5; he was the recipient of Mr David Truitt's email of 18 November 2009; and there is nothing to contradict Mr David Truitt's evidence (see paragraph 259(1) and footnote 26 above) that it was Mr Hussain who suggested that DiscoverPoint should be spun out to DiscoverTech in advance of Autonomy's acquisition of MicroLink and it was he who also negotiated the $10 million price for DiscoverTech's purchase of software; he was (with Mr Kanter) copied into Mr Chamberlain's draft responses to Deloitte's questions (see paragraph 263 above); and he knew of the arrangements for the sequence of payments to *"go through 3 wires"*. I accept the Claimants' submission that Mr Hussain was involved first-hand in this transaction and knew the relevant facts.

271. There is no dispute that Mr Hussain kept Dr Lynch informed about the MicroLink acquisition. On 18 November 2009, Mr Hussain wrote to Dr Lynch regarding "*project DC*", which was the code word for the acquisition of MicroLink, as follows:

> *"I believe agreement in principle is possible on the following basis:*
>
> - *Valuation $55m*
> - *We would buy ML without the as yet not in production product "DiscoverPoint", 6 developers plus 2 sales reps*
> - *Dave would stay on for integration but eventually transition out*
>
> *Let me know if you are ok with this and I'll write up the Board Paper."*

272. The next day (19 November 2009), Dr Lynch replied "*ok*". Then, on 15 December 2009, Mr Chamberlain provided a memorandum entitled "*Financial Due Diligence*" to the board of directors of Autonomy regarding the MicroLink acquisition. Dr Lynch confirmed in cross-examination that he would have read this memorandum with care. It showed that MicroLink had total assets of just under $24.5 million. Only $362,069.17 of these assets were in cash. By far the largest asset, $13,711,426.50, classified as "*Inventory Asset*", was stated to be "*Licences purchased from Autonomy not yet resold*". For good measure, the memorandum went on to explain, "*The inventory assets relate to licences*

purchased from Autonomy that have not yet been resold to the end-users". Accordingly, there was little prospect that MicroLink could pay any substantial part of what it owed to Autonomy. The fact that this did not apparently cause him consternation suggests that it did not come as a surprise and that Dr Lynch, like Mr Hussain and the others involved, well understood that MicroTech was not expected to find the means of paying out of its own resources. But the memorandum did not explain either (a) how a valuation of $55 million for MicroLink could be justified or (b) the arrangements for DiscoverTech to purchase Control Point and acquire DiscoverPoint for (in aggregate) $10 million.

273. On 17 December 2009, Mr Kanter sent Autonomy's directors, including Dr Lynch, a number of documents, and in particular, a Memorandum about the acquisition of MicroLink prepared by himself and Mr Hussain, which (given its importance) I accept Dr Lynch must have read. That Memorandum referred to and discussed the proposed spinning-out of DiscoverPoint and expressed the view that they did *"not believe there is a material business in DiscoverPoint, and not materially different from technology Autonomy already has, and thus are happy for it not to be part of the transaction."* Again, little detail was given.

274. Dr Lynch accepted in cross-examination that he would have known about the $10,000,000 transaction before it was concluded. He was asked whether Mr Hussain had told him about it: he supposed that he would have seen it from the board papers when it went for board approval. In cross-examination he also accepted that he knew that $10 million of the purchase price for MicroLink was "coming back":

> *"Q. You knew about this transaction, both about the amount that was going to be paid out, the 55 million, and the 10 million that was coming back?*
>
> *A. I think I did, yes."*

275. Dr Lynch said in cross-examination that, at the time, he regarded VT5 as separate from the MicroLink acquisition and that Autonomy would have gone ahead with the acquisition whether or not DiscoverTech had proceeded with the acquisition of Control Point. When pressed he said:

> *"Well, they're linked in the normal sense that you wouldn't need to buy the software if you weren't spinning out the company. So if he wasn't selling his company, he doesn't need to buy the software, because he's buying the software for his new company which is spun out from the old one. So in that sense they're linked, but, as I said, Autonomy's board were happy to continue with the acquisition even if Mr Truitt had not decided he wanted to buy software. We viewed it round the other way, which is he was making it a condition of the deal that he would sell provided he could have a business to carry on with and that was the DiscoverPoint business. And in fact the software sale is heavily negotiated and he doesn't get what he wants."*

276. In arguing that there was no basis, nor had the Claimants put to Dr Lynch any basis apart from conclusory assertion with which he disagreed, on which Dr Lynch was supposed to have known that the purchase price was (allegedly) inflated, Dr Lynch relied on the following:

(1) Although he knew that $55 million was being paid to the shareholders, and $10 million would be being paid by DiscoverTech (ultimately) for the software, it was submitted that this did not suggest that the MicroLink acquisition price was inflated.

(2) David Truitt confirmed in his hearsay evidence that there was no relationship between the acquisition price and DiscoverTech's purchase of the software, and the material passing to Dr Lynch also showed that $55,000,000 was the negotiated price for MicroLink.

277. The Claimants referred Dr Lynch to Mr David Truitt's email of 18 November 2009 which I have also quoted from in paragraph 259 above. This email was not sent to him but to Mr Hussain. Dr Lynch's evidence was to the effect that his understanding was that the reason that the escrow was at that level was because that was the original proposal from Autonomy for the escrow amount (when their opening offer was at $45m), and that while the headline figure had been negotiated upwards no one bothered to move the escrow amount. In this regard he was later taken to an email from the lawyer for MicroLink to Mr Kanter on 30 December 2009 attaching a revised version of the draft escrow agreement (stated to be nearly ready for execution) changing the escrow amount from $5,500,000 to $4,500,000; but the email was not sent to Dr Lynch. When asked to agree that the email and its attachment showed that his supposition that the $4,500,000 was simply a hangover from a previous draft must be incorrect he answered:

> *"My understanding, and as I say I wasn't involved in this, was that the original price and escrow number that was agreed was 4.5 million, there was then a negotiation and it came to 55 and then this email seems to be a discussion about whether it should be 10% or it should still be the 4.5."*

278. What emerges from all this is that Dr Lynch was well aware of the overall picture, including (as well as the $55 million acquisition) of the broad detail of the arrangements for DiscoverTech to acquire DiscoverPoint and purchase Control Point for $10 million. I think it more probable than not, and I find, that he knew that the real purchase price for MicroLink was $45 million, that the escrow arrangements reflected this and that the additional $10 million was to enable MicroTech to pay back Autonomy. He may not have known how the $45 million was calculated: but that is of little moment.

279. In my judgment, both Defendants thus had "guilty knowledge" of accounting impropriety, which was part of the false presentation of Autonomy's financial position and performance in its published information.

VT13: MicroTech/Vatican Library Q1 2010

280. VT13, which was referred to at trial as "the Vatican Library deal", was prospectively by far the largest of the impugned VAR sales: and it illustrated in a variety of ways what the Claimants called "the pattern".

281. From early 2009, Autonomy had hoped to be involved in a project, which was initially secret, for the digitisation and saving in Digital Safe of the Vatican Library's collection of over 80,000 manuscripts and over 40,000,000 documents so as to make it widely available for scholars and the public for the first time. The overall project was huge (in

value terms in the region of Euro 75,000,000); it was likely to take years, and involve a programme of installation and sustained servicing; it was also prestigious, with huge potential marketing benefits for Autonomy. Dr Lynch perceived this as a flagship project for Autonomy, which Dr Lynch accepted in cross-examination, would *"certainly have been a contender for"* Autonomy's biggest ever single deal. Dr Lynch was clearly excited by the whole idea which he described as *"a wonderful thing for humanity"*.

282. It appears from email exchanges between Mr Goodfellow and Mr Lucini in October 2009 that Autonomy envisaged and proposed that Autonomy would provide *"the whole solution – hardware, software & services"* in conjunction with an Italian implementation partner. It also appears that the Vatican Library wanted, if possible, to fund the project through a foundation which would be funded, in whole or part, by public and corporate donations.

283. In February 2010, after the replacement of its original Italian partner, Selex (part of Finmeccanica), because of its involvement in an Italian corruption scandal (the replacement partner being Poste Italiane, the Italian postal service), Autonomy was sent confirmation by the Vatican Library that Autonomy could begin what was called a "*Test-BED*" of the digitisation project. An email from Mr Luciano Ammenti ("Mr Ammenti") on behalf of the Vatican Library stressed that Autonomy would have to pay for the hardware and labour and "*AUTONOMY won't have anything to claim to the Vatican Library in case the project of manuscripts digitalization won't take off*". In other words, Autonomy would be proceeding with the test bed entirely at its own economic risk.

284. This was followed by discussion of a Memorandum of Understanding to regulate the partnership between Autonomy and Poste Italiane and the Vatican Library in respect of the project. A draft of this was in circulation on 18 March 2010, although the terms were fairly broad, and did not constitute a contractual agreement. Some 8 days later, on 26 March 2010, a Letter of Intent was signed between the Vatican Library and Postecom SpA, providing for a 60-day period of negotiations with a view to the parties then discussing *"in good faith the terms of their possible collaboration."* However, Autonomy was not a party; the letter of intent was no more than that; and it was expressly agreed that its terms did *"not bind the parties in signing any collaboration contract."* This Letter of Intent was forwarded to Autonomy on 28 March 2010.

285. Although there is some suggestion that there was talk of a deal before the end of March, that was entirely unrealistic.

286. By 29 March 2010, it was clear that there could be no realistic expectation that the Vatican Library's proposed charitable foundation would be in a position to issue a purchase order to Autonomy by the end of the quarter; and indeed, that final closing of a deal was some way off.

287. It seems from the content of an email dated 29 March 2010 entitled *"BAV – the route to closing the deal tomorrow"* sent by Mr Hussain to Mr Broli (Autonomy's sales executive covering Italy), which Mr Hussain sent also to Dr Lynch, that Mr Broli suggested the involvement of an Italian partner. Mr Hussain appears to have welcomed that, on the basis of the partner acting as a VAR (in return for a suggested margin of 5%). Mr Hussain expressed his approach to Mr Broli, stating that *"having an Italian partner would be very useful to us"* but that:

> *"the partner that we would use would have to be sufficiently strong financially for us to be able to recognise the revenue and only if the [Purchase Order] and contract is signed this quarter."*

288. On 31 March 2010, the last day of the quarter, Monsignor Cesare Pasini (the Prefect of the Vatican Library) sent Mr Broli a new Letter of Intent between the Vatican Library and Postecom. Mr Hussain requested a translation from Mr Zanchini. This changed the exclusivity period to 50 days, extendable by a further 40 days subject to the agreement of the Vatican Library, but otherwise was essentially the same. Recital (f) to this Letter of Intent stated:

> *"It is understood that if by the terms as in d) of this preamble BAV finds the financial contributions to destine to the BAV Project and that the amount will be sufficient to cover at least the First Phase of the BAV Project, these contributions will be entirely used by BAV to pay Postecom the amounts due for such first Phase as defined at point a) of the Preamble."*

289. Evidently, therefore, the question of funding the digitisation project remained unresolved as at 31 March 2010. In the circumstances, it was plain that there was no prospect of the Vatican Library itself – or any newly established foundation – signing a contract in Q1 2010.

290. However, Autonomy needed recognised revenue from a sale prior to the end of the quarter. Without a Vatican Library transaction, Autonomy was at risk of missing the market consensus figures for revenue and earnings per share in Q1 2010: this was in the region of $193 million (revenue) and $0.25 (adjusted earnings per share). Accordingly:

    (1) On 28 March 2010, Mr Hussain sent Dr Lynch an email which made it clear that to achieve $195 million in revenue for the quarter "*we will need Vat and Stouffer's deal*".

    (2) On 29 March 2010, Dr Lynch sent Mr Hussain and Mr Egan a document setting out his suggestions or 'route-map' on which transactions were needed to achieve revenue of $196 million in the quarter. He identified $15 million of revenue from a "*VAT*" deal: this signified the Vatican Library transaction and what became VT13. This was larger than any of the other listed deals. Dr Lynch continued to work at ways of delivering results commensurate with revenue forecasts.

    (3) At 23:30 on 31 March 2010, Dr Lynch sent Mr Hussain a new iteration of his route-map document. This noted that: $22.5 million of revenue needed to be recognised from "*VAT*", the Vatican Library, in order to achieve revenue of $205 million in Q1 2010: a "*VAT contribution*" of $10 million was needed to achieve $193 million of revenue, which would involve Autonomy announcing earnings per share of less than $0.25; and a "*VAT contribution*" of $17 million was needed to achieve $195 million of revenue, which would enable Autonomy to announce earnings per share of $0.25. This document therefore picked up on the $193 million consensus revenue figure and the $0.25 market consensus earnings per share figure that had been identified in an email on the same day

(31 March 2010) from Mr Peter Goodman (who worked in Autonomy's Investor Relations team).

291. Only at the last moment did Autonomy resort to MicroTech. There is an issue whether in fact it was by then too late. It seems that it may be that the purchase order was not signed until 1 April (see paragraphs 323 to 327 below); but even on the basis of the Defendants' account, VT13 was not agreed until the dying hours of Q1 2010 (indeed, only then by the use of a VAR in a western time-zone). Mr Egan gave this evidence in his witness statement:

> *"Mr Hussain asked me to see if MicroTech would agree to take a part of the deal that Autonomy was trying to sell to the Vatican Library. He ultimately gave me the amount: $11.5m. I contacted David Truitt and asked him whether MicroTech would take an $11.55m Vatican Library deal on the usual terms. David Truitt said he would check with Steve Truitt, the MicroTech COO. At David Truitt's request, we then prepared a description of the deal terms for John Cronin who, in this context, was acting for MicroTech. MicroTech agreed to take the deal."*

292. Dr Lynch was asked about his "route-map" document referred to at paragraph 290(2) above which the Claimants relied on as showing calculations of the size of any VAR sales according to Autonomy's fluctuating requirement for recognised revenue. Dr Lynch dismissed this: he was adamant that the amounts were not calibrated by reference to revenue forecasts, but according to *"political"* considerations. His explanation, as I understood it, was that this signified simply consideration of the possibility of parts of the deal being sold off to different prime or sub-prime resellers, given the very considerable size of the deal, and given the likely political imperative of including an Italian partner[28], one of which might *"end up being the prime"*. This initially struck me as plausible: but an email dated 2 April 2010 from Dr Lynch to Mr Hussain stating *"I saw that MT is 11 so if we can get data more than that would be good"*, though not altogether clear (the reference to data appearing extraneous), suggested that Dr Lynch would have wanted to "sell" more to MicroTech (and see also paragraph 311(5) below). This seems to me to show that (a) Dr Lynch remained personally and directly involved and that (b) he knew full well that the size of the VAR deal was calibrated not by reference to any prospective and realistically anticipated end-user deal (there was none) but by reference to Autonomy's requirement for recognised revenue.

293. The VT13 purchase order for Autonomy software (IDOL Server and Autonomy Archive Solution with Digital Safe Core Appliance) for end-user Vatican Library was issued under the June 2006 MicroTech VAR agreement (see paragraph 214 above). This provided expressly that MicroTech was obliged to pay Autonomy for its orders irrespective of its sales to an end-user, and confirmed that there was no other understanding or arrangement between the parties.[29]

294. The licence fee for VT13 was $11,000,000, plus $550,000 for support and maintenance and was payable within 90 days (i.e. by 29 June 2010). The authorised use of the software was confined to use for the Vatican Library digitisation project and within the territory of

[28] A large Italian integrator called Selex (part of Finmeccanica) was originally identified, but the Vatican Library removed Selex because of a corruption scandal. Poste Italiane was then considered. See paragraph 283 above.
[29]And see paragraph 216(4) above.

the Vatican Library. VT13 related only to a part of what had always been envisaged as a larger Vatican Library deal.

295. In the event, no deal was concluded with the end-user (Vatican Library), either by MicroTech or by Autonomy. It appears from a letter dated 15 May 2014 from the Vatican Library to HP Autonomy, that some considerable time later, in March 2014, the Vatican Library selected and contracted with a different supplier of software, NTT Data, to undertake the digitalisation of its archives.

296. However, MicroTech remained under its legal liability pursuant to the terms of the agreement. The question which arose, in accordance with the usual pattern where no end-user deal had eventuated, was how it could be let *"off the hook"*.

297. The Claimants' case is that MicroTech was only rescued by a transaction between itself and Autonomy for the purchase by the latter of goods that Autonomy did not in fact need (the "ATIC" transaction, of which more later), which (exemplifying the 'pattern' asserted by the Claimants to be typical) got MicroTech *"off the hook"*.

298. More generally, the Vatican Library transaction was not only prospectively the largest of the VAR transactions: it was also a transaction which demonstrates many of the principal features of the Claimants' case on impugned VAR sales, and the Defendants' answers to their allegations. It also illustrated especially clearly the role expected of the VAR, in this case, MicroTech. It was dealt with at considerable length at the hearing, no doubt for that reason; and I deal with it at some length below.

Claimants' case on VT13

299. The Claimants highlighted the following particular features of VT13 and its context in support of their case that it made no commercial sense whatsoever to suppose that MicroTech perceived itself to be taking any more than a nominal risk for which it was to be handsomely rewarded for doing absolutely nothing. It was, in their language, no more than a *"placeholder"*.

300. First, the Claimants emphasised that MicroTech had no prior relationship with the Vatican Library, nor any knowledge of the Vatican Library project before agreeing to act as a VAR and signing up to the VT13 purchase order. MicroTech was based in Northern Virginia, USA. There is no evidence that it had Italian speakers working for it or any experience working for any customer located in Italy, let alone the Vatican Library. On the contrary, Mr David Truitt testified in the MicroTech proceedings in the US that MicroTech had not done any work outside the US, and had no employees located outside the US. The obvious choice of a VAR would have been one based in Italy, and indeed an "Italian partner" had been suggested (see above): but it seems likely, not least in light of the unlikelihood of any imminent end-user sale, that Autonomy needed a 'friendly' VAR and there was none there.

301. The Claimants submitted that Dr Lynch's justification under cross-examination that MicroTech *"had a couple of hundred people doing services and that's actually very difficult if that's done by people that are speaking Italian rather than English and it's much better done co-located nearer our own technical resources"* made no sense; and that Dr Lynch *"gave no evidence…to explain how a US reseller, with no insight into the Vatican Library, could ever hope to achieve such a sale"*. They quoted Mr Stephan's

statement in the US criminal trial that he was *"incredulous"* when he learned that the VAR for the Vatican Library deal would be in the Washington D.C. area. They noted and adopted his view that:

> *"It suggested that – to me it indicated that they were just a conduit for giving us paperwork to close – to book deals in the quarter end because there was no linkage in my mind between a U.S. federal government reseller and, you know, the Vatican in Italy."*

302. The Claimants also noted Mr Stephan's further evidence that he had telephoned Mr Chamberlain, who had shared Mr Stephan's surprise about the Vatican Library deal going to MicroTech; and that he had made clear to Mr Chamberlain that, as he considered:

> *"…these deals were, you know, garbage. They were not worth the paper they were written on, and I wasn't happy to front them up as good deals to our auditors"*.

His recollection was that Mr Chamberlain's response was that it was not his call: it was Mr Hussain's call, and that *"we just need to do our job and put it to the auditors"* but was resigned to the fact that it was *"Mr Hussain's call"*. Mr Stephan added the more general observation about Mr Chamberlain that:

> *"That was always his – his stance was like, troops in an Army. The general says what to do and we have to follow our orders."*

303. Dr Lynch submitted that Mr Stephan's hearsay evidence should be given no weight. His team had had no chance to cross-examine him and as previously noted, Dr Lynch gave evidence that Mr Stephan had, in effect been coerced (see paragraph 16(8) above). Plainly, it would be wrong to accept Mr Stephan's surprise and characterisation of the transaction as of itself demonstrative of the true nature of the transaction: but his recitation of his surprise and characterisation, though highly coloured, had the ring of truth, and was at least consistent with the inherent unsuitability of MicroTech for any more than a nominal role in the matter.

304. The Defendants' defence of the choice of MicroTech was that (a) *"much of the services work would not have required attendance in Italy"*, (b) it was *"common for software and service providers to provide services to international customers"* and (c) for example, according to the Defendants Capax Discovery had itself worked for Prisa, a Spanish company. This was not, to my mind, persuasive. In particular (a) Mr David Truitt's evidence was that MicroTech had no international experience nor even the service capability; (b) in any event, MicroTech's last ditch retention by Autonomy was notionally for the purpose of selling on the software: and its total lack of experience, lack of Italian speakers, lack of contacts, and unfamiliarity with the Vatican Library made it entirely unsuitable in that regard[30]; and (c) no details were provided of what "Capax Discovery"

[30] The Defendants made the point that Mr Steve Truitt had expressed enthusiasm for MicroTech providing services to the Vatican Library: but enthusiasm is obviously not enough.

did for Prisa[31], nor even of which "Capax Discovery" company it was or why it was chosen, and the example offered carried the matter no further.

305. The second feature highlighted by the Claimants was the clear and complete absence of any engagement on the part of MicroTech in any part of the negotiations with the Vatican Library: they were carried on exclusively by Autonomy. Mr Steve Truitt confirmed this in his deposition in the MicroTech proceedings as follows:

> *"Q. Did MicroTech at any time contact the Vatican Library in an effort to sell the identified software, the software identified in [the MicroTech purchase order], to the Vatican or to assist Autonomy in Autonomy's efforts to sell that software?*
>
> *A. No.*
>
> *Q. Did – did MicroTech, to your knowledge, have any involvement in the negotiation with the Vatican Library of the terms of a proposed transaction involving the software identified in [the purchase order]? [objection omitted]*
>
> *A. No."*

306. This was confirmed by a letter written considerably later (15 May 2014) by the Vatican Library to HP:

> *"As you well know, BAV [the Vatican Library] has never dealt with the company MicroTech and was not even aware of its involvement with Autonomy at the time of the latter's contacts with BAV to analyze the possibility of a possible collaboration on the digitisation project."*

307. MicroTech made no effort to even approach the end-user with a view to service work after any end-user sale, as Mr Steve Truitt confirmed in his deposition evidence in the MicroTech civil proceedings in the US:

> *"Q. Did you – did MicroTech at any time, to your knowledge, approach the Vatican Library in an effort to obtain service business from the Vatican Library?*
>
> *A. No."*

308. Indeed, in the same deposition evidence, Mr Steve Truitt made it clear that in his view, MicroTech did not have the capability of providing such services:

> *"Q. Mr. Truitt, in 2010/2011, did MicroTech have people on its staff who were familiar with Autonomy software?*
>
> A. *I'm going to say no. It's possible we had one or two, but also there -- there were people out working on contracts that knew stuff. I mean, you know,*

[31] As will be seen, one of the impugned VAR sales involved Prisa: but the VAR selected was DiscoverTech, and so cannot have been the same deal as in the example offered.

> *we didn't have on the -- we didn't have anybody on the bench, I don't think."*

309. A third feature pointed out by the Claimants was that, as Mr Lucini described it in his witness statement, Autonomy's proposal was for an "*end to end solution*". Although the Defendants contended in their written closing submissions that Mr Lucini's evidence had not stood up to cross-examination and he had accepted that numerous aspects of the overall project would naturally have had to be undertaken by professional services partners, the fact remained that Autonomy had stressed the advantage of a single point of supply in its own proposal to the Vatican Library:

> *"In order to minimise TCO Autonomy can provide a fully managed solution as part of its Digital Safe offering including Software, hardware, Support, Installation, Monitoring & Administration…A full Autonomy solution also provides the traditional advantages of single supplier sourcing."*

310. The Claimants acknowledged that, of course, Autonomy might have decided to subcontract some of its work or, as Mr Lucini said in cross-examination, it might have used a professional services firm for particular parts of the project. However, the Claimants made the point that the notion that Autonomy would outsource the <u>licensing of the Autonomy software itself</u>, i.e. that the Vatican Library would contract with Autonomy for the whole of the project, but with the specific exception of the Autonomy software, which the Vatican Library would instead purchase from a third party, made no sense. There is no evidence that anyone at Autonomy understood this to have been the plan at the time.

311. Fourthly, the Claimants pointed out that VT13 was even riskier than other deals from the point of view of a VAR, had it really been substantively on risk:

    (1) The progress of the project depended on attracting funding for the foundation which the Vatican Library wished to use for the digitisation project: see paragraphs 280*ff* above. By 31 March 2010 the funding issue remained unresolved, was (given the size of the project) an enormous undertaking, and was plainly some considerable way from being addressed.

    (2) It was thus apparent by then that delay in any end-user deal was almost inevitable: Dr Lynch's evidence in cross-examination that *"the feeling at the time was that it was very close to being signed"* and that *"it was considered to be a project that was very close to happening"* was based on emails containing vague expectations, and the terms of the Letter of Intent between the Vatican Library and Postecom (to which Autonomy was not even a party) confirm that any such expectations were entirely unrealistic, as was Dr Lynch's evidence accordingly.

    (3) Any onward sale was confined to the Vatican Library as end-user and was dependent, not only on the end-user wanting to purchase the goods purchased by the VAR, but also, since the software was only part of what was needed for the project, on the end-user proceeding with the larger project in a manner that made it still require the software.

(4) It made no sense to commit in March/April 2010 to pay $11,500,000 on the footing that the VAR would be able to on-sell the software licence to the Vatican Library within a reasonable time and at a profit, especially in circumstances where the VAR knew nothing of the end-user and was intended and expecting to have no participation in negotiations to bring about a resale.

(5) Dr Lynch's evidence in cross-examination when asked to explain what commercial benefit there could have been for MicroTech was to the effect that the advantages were (a) it would get *"an introduction into commercial business"*; (b) *"the services of doing all the gluing work"*; (c) *"the marketing effect of being able to say that they were part of this incredibly prestigious project"*; and (d) *"the revenue on the deal"*. Dr Lynch added that he would have signed off on a cost of $10 million *"just from a marketing point of view, just to be involved in it."* I did not find any of this persuasive. The *"introduction to commercial business"* struck me as somewhat condescending and unfocused generality; the *"services…gluing work"* was neither offered nor expected, or even within its capabilities; and though Mr Steve Truitt gave evidence in the US criminal trial (relied on by the Claimants themselves) that he was very excited by the project and *"the services add on here would be tremendous"* that was undermined by the fact that it was dependent on the risk in question (there never being an end-user deal) not eventuating, and upon MicroTech having a capability which (see above) Mr Steve Truitt had denied; and the marketing opportunity for MicroTech was very restricted in comparison to what Dr Lynch claimed for it, given MicroTech's low profile and minimal involvement. That leaves only the revenue on the deal.

312. The reality this confirms is that MicroTech could proceed only because it was never going to be *"left holding the bag"*. The VAR sale was a commercial proposition for it only because it was not required to take any real risk; it was required, as always, to do *"next to nothing"* in return for a substantial MAF.

313. Fifthly, the Claimants relied on Dr Lynch's replies to a question testing the aim of Autonomy's negotiations with Vatican Library and in particular, how the prospect of an onward sale by MicroTech would have been impacted, as follows:

> *"Q. Can you just explain this: what does Autonomy's considerable effort have to do with the fact that MicroTech was not able to close a deal with the Vatican?*
>
> *A. Because if Autonomy had closed a deal with the Vatican then that would have closed MicroTech's deal.*
>
> *Q. How so?*
>
> *A. Because it was a consortium deal. So if we'd closed the thing and the consortium had got going, then the software that MicroTech had would have been used as part of that consortium."*

314. The Claimants took this to mean that if Autonomy had closed a deal with the Vatican Library, that would have ensured that the software sold to MicroTech would be used. On that basis, they submitted that it could not be clearer that, in Dr Lynch's understanding,

Autonomy was going to retain managerial involvement and control over that software; and MicroTech had not assumed the significant risks or rewards of ownership, precluding revenue recognition.

315. Sixthly, the Claimants alleged that Deloitte were misled (as also they submitted, were the Audit Committee) about the true nature of VT13, and especially as to the role intended to be played by MicroTech. The Claimants contended that Deloitte were misled into thinking that MicroTech was intended to and did participate in the transaction, whereas in fact, it was not involved at all (other than on paper and in a passive, in reality nominal role) and the Vatican Library did not even know of its existence.

316. Deloitte's understanding of the position is shortly stated in a working paper dated 16 April 2010 which recorded the following:

> *"Per discussions with Sushovan Hussain, Microtech is still considered to be a key reseller of Autonomy licence and as a result has entered into one deal with Autonomy in Q 1 2010 with the end-user of the Vatican for $11.5 million. The end-user has been informed of the fact that the licence will be supplied through Microtech, therefore Autonomy management is confident that it is appropriate to recognise the revenue on the transfer of the risks and rewards to Microtech."*

317. The Claimants maintained that it was untrue that the Vatican Library had been "*informed of the fact that the licence will be supplied through MicroTech*"; and they relied on the Vatican Library's letter of 15 May 2014 to HP (see paragraph 306 above) making clear that the Vatican Library had never dealt with MicroTech and was not aware of its involvement with Autonomy at the time. This led on to the submission that if the Defendants had really thought that there was nothing wrong about their plan in relation to MicroTech and the Vatican Library transaction (that plan being that MicroTech would do nothing and that Autonomy would continue negotiating as before), they could and would have been open and honest with Deloitte about it. But they were not.

318. The Claimants submitted further that it was clearly an important point from Deloitte's point of view that (as was recorded in Deloitte's working paper dated 16 April 2010) the end-user had been *"informed of the fact that the licence will be supplied through MicroTech"*. But the Vatican Library's letter of 15 May 2014 (referred to above) made clear that the Vatican Library had never dealt with MicroTech and was not aware of its involvement with Autonomy at the time.

319. Moreover, and as also noted in the background section of the same working paper, Deloitte had recently found out that the Q4 2009 MicroTech deals for end-users Morgan Stanley and ManuLife (which have been addressed above) had gone direct. This had raised a question as to the recognition of revenue on deals with MicroTech. Deloitte had been told (it is to be inferred, by Mr Hussain) that the reason that these two deals went direct was because the end-users in question had not wanted to deal with a reseller; rather, they wanted to contract directly with Autonomy.

320. Accordingly, the fact (at least according to Mr Hussain) that the end-user had been informed of MicroTech's involvement was said ("*therefore*", see paragraph 316 above) to explain why Autonomy management was confident that it was appropriate to recognise the revenue on the transfer of the risks and rewards to MicroTech. That reflected Deloitte's expectation that, from April 2010 onwards, it would be MicroTech, rather than

Autonomy, that would be negotiating to supply the software licence to the Vatican Library.

321. Dr Lynch's efforts to answer this point by suggesting that he thought the Vatican Library's "*agents were"* informed were far from convincing. He mentioned what he thought might be the name of one of the *"agents"* (he named Mr Ammenti) but in a way which struck me as some possibility plucked out to provide some sort of footing which did not exist, and he could not name anyone who might have told Mr Ammenti beyond saying he thought that it would have been *"the technical people"*. When it was put to him that he was *"literally making this up"* he resorted (as became something of a pattern as his cross-examination drew out) to unidentified documents in the 'corpus'; which he assured me would back him up[32], but which were never identified or produced. He was more credible in saying later that he simply *"didn't know about many of the things you ask me about and I'm telling you the background of how these things work."*

322. In my view, Dr Lynch had no basis for supposing that the Vatican Library had been informed of MicroTech's involvement, and his evidence amounted to an acknowledgement that they should have been, in accordance with ordinary procedure. I find that as they later told HP (see their letter referred to in paragraph 306 above) they were not told, and that Deloitte were misled in being given to understand otherwise. (The Claimants claimed that one of the reasons why one of Dr Lynch's notified intended witnesses, Mr Marco Zanchini, a systems engineer in Autonomy's Milan office, who had been engaged in the transaction and would have been in a position to say whether anyone had been told about MicroTech's involvement, was withdrawn as a witness is that his evidence would have confirmed this.)

323. A more egregious element relied on by the Claimants (but not one which was unique, as will appear later) was that to achieve its only true purpose of enabling Autonomy to book the sale price as recognised revenue the VT13 purchase order had to be and was backdated.

324. As to this:

(1) Both documentary evidence and the evidence of Mr David Truitt appear to establish that the VT13 purchase order was not signed by Mr Steve Truitt until 1 April 2010 even though it bears the date 31 March 2010;

(2) Mr David Truitt's evidence was that prior to 1 April 2010 he had not even heard of any potential transaction with the Vatican Library; according to his deposition in the MicroTech proceedings he was telephoned that day by Mr Egan who asked him whether MicroTech would take a deal dated 31 March 2010, involving the Vatican Library end-user: and this appeared to be confirmed by an email chain dated 1 April 2010 between Mr Cronin and Mr Steve Truitt and in particular an email from Mr Cronin stating *"I just talked w/Dave re the most recent AU conversations. I'm available to help w/this…am awaiting details from AU…."* which was followed up when Mr Cronin sent Mr Steve Truitt the purchase order, stating *"It needs to be signed and emailed back to me, assuming it meets your expectations"*. (It was signed and returned that day.)

[32] Dr Lynch made a vague reference to documents and getting "*the names off of those documents I'm sure*".

(3) Mr Steve Truitt confirmed in his deposition in those proceedings that he had not signed until some time after 6pm on 1 April 2010.

325. Dr Lynch's response to all of this (in addition to emphasising that he was not sent any version of the purchase order and knew nothing of any backdating) was that the deal was agreed prior to the quarter end, even if it was only memorialised in writing the next day. He acknowledged that, if the document was intended to be effective from the date of the earlier oral agreement, that should have been stated; but that omission may have complicated matters and was not critical for revenue recognition. Mr Welham confirmed with regard to this transaction that there was no specific requirement under IAS 18.14 for a written contract, so long as there was a binding agreement on the relevant date. Dr Lynch relied also on the following:

(1) In cross-examination, Mr Egan said that his *"memory of this deal was that it was done inside of the quarter in which it was submitted"*, and seemed to think also that Autonomy and MicroTech had discussed the proposed deal at the end of March 2010; but Mr Egan cautioned that he didn't have *"specific knowledge of the dates"*.

(2) Mr Steve Truitt stated in his evidence to the Grand Jury which indicted Mr Hussain that his *"understanding"* was that he had actually agreed a deal before the end of the quarter; but his later evidence was to the contrary.

(3) A delivery confirmation appeared to show that the software was made available to MicroTech on 31 March 2010, signifying a transfer of risk on that date; but that did not necessarily assist Dr Lynch because (a) there was nothing to stop Autonomy sending MicroTech a delivery confirmation, even though MicroTech had yet to commit to buy and in any event (b) Mr Steve Truitt testified at the US criminal trial that this confirmation was *"false"*, both as to the delivery of the software and as to the date of delivery.

326. I consider it clear that the purchase order was not signed prior to the quarter-end. Accordingly, it was backdated. But I think it likely that a deal was struck in broad principle on or about 31st March. Whether the terms were sufficiently set out is debatable; the price was made clear and arguably the inference may be, and it might be sufficient that, there was already a definition of the terms in the draft agreement which had governed previous deals. However, I do not propose to make a finding in this regard, for (a) the relevance of VT13 in the broader context is primarily that it exemplifies the use of a VAR, whether at the very last minute or beyond it, to book recognised revenue without there being any intention or expectation of the VAR ever doing anything else, apart from assuming a liability from which it fully expected to be relieved, and on that basis (b) the transaction should not have been accounted for as having generated revenue to be recognised; so that (c) such a finding would be superfluous.

327. In addition, I do not think that there is sufficient evidence that Dr Lynch was, at the time, aware of the details to infer knowledge of the facts alleged to amount to backdating and thus forgery. I accept that:

(1) There is no evidence that Dr Lynch was sent any version of the purchase order.

(2) In the absence of specific proof of involvement it is unlikely that Dr Lynch would have been involved in this level of detail.

(3) Dr Lynch's denial of knowledge struck me as credible.

328. The last of the points particularly relied on by the Claimants was a familiar one in the pattern. The Claimants contended that the illusory nature of the transaction and their case that all the impugned VAR transactions were subject to side agreements or understandings intended to ensure that the VAR was not substantively at risk were confirmed in the context of VT13 by the extraordinary steps taken by Autonomy to ensure that MicroTech was, in effect, provided by Autonomy with the funds to meet its obligations.

329. The Claimants relied in this regard on (a) a contrived transaction involving the purchase by Autonomy of an exclusive three-year licence to use what was described as MicroTech's "*Advanced Technology Innovation Center*" ("ATIC") for $9,600,000; (b) the routing to MicroTech of further funds for the same purpose of enabling MicroTech to discharge its obligations to Autonomy under the VT13 purchase orders; and (c) the write-off of the remaining VT13 indebtedness in the "Dark Period" immediately after the announcement of the acquisition of Autonomy by HP.

ATIC

330. The ATIC was a facility built by MicroTech. It was often referred to in contemporaneous documents as the "I2C". It was essentially to be a mobile demonstration centre and a display facility which MicroTech was constructing to demonstrate MicroTech's own capabilities. The facts relating to Autonomy's purchase of a three-year non-exclusive licence to use ATIC for a fee of $9.6 million are complex and, in most instances, disputed.

331. Put in a nutshell, whereas the Defendants sought to justify the transaction and the ATIC facility as of great utility to Autonomy, especially in the context of its cleared federal contracts and projects, the Claimants' case is that ATIC was a facility which Autonomy did not in fact need, of which large parts were never even built. According to the Claimants, the purchase of a licence to use it was a transaction contrived to fund MicroTech when it was apparent by the end of Q4 2010 that Autonomy was no closer to securing an end-user deal with the Vatican Library: it was another example of Autonomy using its own funds to purchase or reimburse the costs of a purchase of its own revenue.

332. The Claimants contended that the purchase was also driven by the need urgently to assuage Deloitte's developing concerns and deflect further questions about the collection of the VT13 debt (which had become due in full on 29 June 2010). Deloitte noted these concerns in its Audit Committee report for Q3 2010, dated 17 October 2010, in which they warned that:

> *"We understand that Microtech has yet to receive the amounts due from its end-user and as such is delaying payment to Autonomy. As a result, this amount remains unprovided at this time. We highlight this as a significant balance which management will need to re-assess for the purposes of the 2010 year-end financial statements. Should a substantial proportion of this balance not be recovered by year end, provisioning will need to be considered."*

333. Mr Bloomer confirmed in cross-examination that the importance of getting some form of payment from MicroTech would have been apparent to those present at the related Audit Committee meeting (on 18 October 2010), when (he said) there had been considerable "*discussion about this topic and the deal with the Vatican"*. He was also asked about the reference to the presentation that MicroTech was awaiting *"amounts due from its end-user"* (see quotation above):

> *"Q. So you were told that the reason why MicroTech had not paid Autonomy was that MicroTech had not been paid by its end-user, the Vatican, yes?*
>
> *A. Yes.*
>
> *Q. And that's what you understood at the time, yes?*
>
> *A. Yes.*
>
> *Q. So you would have understood that MicroTech was looking to get paid by the Vatican in relation to the deal, yes?*
>
> *A. Yes.*
>
> *Q. If MicroTech had never had any dealings with the Vatican of any kind, that would have been contrary to your understanding at the time, yes?*
>
> *A. It would have been surprising."*

334. In fact, the Defendants well knew that MicroTech had not had, and it was never intended that it should have had, any dealings with the Vatican Library.

335. The Claimants also relied on the following as demonstrating the contrived nature of the ATIC transaction, and its true objective (being to fund MicroTech and enable it to pay back its liability under VT13):

(1) Autonomy showed no interest in ATIC when MicroTech first (and then repeatedly) pitched for business in November and December 2010. Dr Lynch acknowledged this in cross-examination. The Claimants suggested that the interest came first from Mr Hussain as a response to the need to find a way of paying down MicroTech's indebtedness.

(2) There is no evidence that Autonomy's technical department conducted any analysis of the ATIC beyond reading MicroTech's proposal.

(3) Email exchanges between Mr Hussain, Mr Scott and Mr Chamberlain appear to demonstrate that it became important to Autonomy to reach a deal on ATIC to justify a payment by Autonomy to MicroTech *"in 2010"*. An email from Mr Chamberlain to Mr Hussain and Mr Scott dated 17 December 2010 (subject "MT") illustrated the link and Autonomy's real concern:

> *"How close are we to agreeing? Need to collect their overdue balances"*

(4) The deal originally proposed was for a one-year licence for $3,747,500: Mr Scott testified at the US criminal trial that the impetus behind the increase in the size of the deal came from Mr Hussain. The development of the proposals was

haphazard, and the Claimants suggested that it appeared to be driven by some purpose other than by reference to what Autonomy needed of the ATIC. For example, the cost breakdown had little logic, and the price went within a fortnight from $3.4 million for a one-year deal to $9.6 million for a three-year deal, and it included an advance payment of the full salaries of five MicroTech employees to staff the ATIC for three years after its completion which Mr Kalbag told me was neither necessary nor justified. In other words, the size of the deal appeared to be calibrated according to the level of MicroTech's indebtedness.

(5) No written contract was ever drawn up to detail the respective rights of the parties in relation to the construction and operation of the ATIC: Mr Scott identified this as very unusual for such a large deal of such a type.

(6) Mr Steve Truitt gave evidence at the US criminal trial that a purpose of the ATIC was indeed to obtain funds with which to pay MicroTech's debt to Autonomy, and testified to the same effect in his deposition in the MicroTech proceedings. He added that the price for the ATIC was reverse-engineered: the price was arrived at by starting with a *"final number, and we would work backwards to provide goods and services that were worth about that much"*.

(7) The price paid by Autonomy exceeded the total construction costs for the display facility launched in July 2011: this made no sense where all Autonomy was getting was a three-year, non-exclusive licence to have its software displayed in the facility, potentially in competition with other companies.

(8) According to Mr Steve Truitt's deposition in the MicroTech proceedings, he was not aware of any other company paying MicroTech more than a million dollars to display their hardware or software at the ATIC. Yet when ATIC – the basic display facility - (by then renamed as the *"I2C"*) was launched in July 2011, (a) no mention was made of Autonomy in promotional videos and (b) none of the other companies show-cased had paid anything close to what Autonomy had paid; (c) the launch was labelled "Product Agnostic", and Mr Jimenez (CEO of MicroTech) sent an internal MicroTech email explaining the approach to be taken, which suggests no prominence was given to Autonomy:

> "*The intend [sic: intent] of doing a Grand Opening is to increase awareness (about our technical dominance) and to not only show our customers that we are ready for prime time but to show our partners that we are levels above the other partners they are leaning on.*
>
> …
>
> *Please be very sensitive to the "Product Agnostic" title we carry, but at the same time be sensitive to the fact that Microsoft, EMC, Dell, HP, VMware, Autonomy and Cisco account for more than half of our revenue and more than 90% of Product revenue and that even though we have received great support from Hitachi, Fujitsu, SGI, Christie Lucus, T-Mobile and others for our I2C they are not providing us with the Millions in revenue the big "7" provide and if they (Microsoft, EMC,*

Dell, HP, VMware, Autonomy, and Cisco) decide to take their ball and go home we will take a very hard hit!!!!

The bottom line is - We will try, even though we know we can't show love to everybody, but let's make sure we remember where MicroTech's bread is buttered and let's be respectful of that and show homage to the companies that have paid the dues over the years and have a seat at the BIGGER table!!!!"

(9) The manner in which payment was made and the way the funds were used was also relied on as reinforcing the conclusion that the true purpose of the ATIC was to route money to MicroTech so that it could pay down a significant part of its debt to Autonomy. As to this:

(a) As set out above, Autonomy paid the entire contract sum in full on 31 December 2010 and one day after it submitted its two-sentence purchase order. It paid in full, before the ATIC was constructed. There were no progress payments as the facility was constructed. Autonomy paid the salaries of the five most senior persons who were to work at the ATIC months before the need for the MicroTech employees to begin their work could have arisen, not as those salaries were incurred. The Claimants argued that, had this been a genuine commercial transaction, it is difficult to see why, commercially, this is something to which Autonomy would possibly have agreed. No credible explanation for this structure has been offered by the Defendants.

(b) An internal MicroTech email dated 30 December 2010 refers in its subject line to an "*Expected Incoming Payment and Associated Out-Going Wire Payment*". The body of the email notes that there was to be an "*incoming payment*" of $9.6 million from Autonomy Inc. and that there would then be a "*request for a wire transfer back to Autonomy as payee*" in the amount of $6.3 million. Mr Steve Truitt testified at the US criminal trial that this was "*Absolutely*" part of the purpose of the ATIC purchase.

(c) At his deposition in the MicroTech proceedings, Mr David Truitt agreed that it was his understanding that MicroTech was to use part of the $9.6 million paid by Autonomy for the ATIC in order to pay down MicroTech's debt to Autonomy. In fact, on the <u>same</u> day that ASL paid $9.6 million to MicroTech, MicroTech paid $6,305,140 to Autonomy Inc. Of that $6.3 million, $1.89 million was used to settle MicroTech's debt on VT6 (Honeywell) and $4.321 million was used as a partial payment on VT13 (Vatican Library).

(10) Lastly, the Claimants contended that *"large swathes of what were set out in MicroTech's $9.6 million proposal were never built"* including the following (i) the mobile data centre featured in the proposal (ii) the *"medical scientific research solution"* promised in the proposal (iii) the Department of Defence record management and archiving solution described in the proposal (iv) the

intelligence investigation solution set forth in the proposal and (v) a test evaluation laboratory using Autonomy applications. The Claimants noted further that Autonomy made no complaint (suggesting indifference); and that in respect of the part of what was described in the MicroTech proposal that the Claimants accepted MicroTech did build – the basic ATIC display facility – Mr Kalbag's evidence was that, so far as he was aware, the ATIC facility was not used by Autonomy or any of its customers (whether for demonstration purposes or otherwise). Autonomy's salesforce were not even told of the purchase: thus, for example, Mr Kalbag (Director of Federal Sales) was not aware of the purchase until he attended the *"I2C"* launch in July 2011.

336. Having paid Autonomy $4,321,000 after receipt of the ATIC monies, MicroTech still owed some $6,700,000 in respect of the VT13 purchase order. During Q2 and Q3 2011, MicroTech paid a further $4.4 million to Autonomy Inc:

(1) Of this, $2 million was paid on 21 April 2011.

(2) A further payment of $2.4 million was paid by cheque dated 1 July 2011 though it is recorded in Autonomy's accounting data as having been made on 30 June 2011. The $2.4 million was paid after receipt of funds received by MicroTech on 1 July 2011 from DiscoverTech, which, in turn, had been received from Autonomy. This is explained further in the context of VT30 below.

337. That still left $2.3 million of the original $11.55 million outstanding. That amount was never paid. Instead, Autonomy Inc wrote off this balance as at 30 September 2011 (three days before the HP acquisition completed). On 12 October 2011, Ms Lisa Harris sent an email stating, "*We need to write-off the attached list of debts on the AR modules as at 30th Sept*". The email was sent to Mr David Mobley and two others (all of whom I assume worked in Autonomy's finance department) and circulated to five others on Autonomy email addresses (who appear from the body of the email to have been working in the "collection teams"). Its attachment included the remaining debt of some $2.3 million due from MicroTech under VT13 as one of those to be written off as of 30 September 2011.

338. Ms Harris confirmed in her oral evidence that the write-offs included $2.3 million owed by MicroTech in respect of the Vatican Library transaction though she insisted that the write-offs were simply an accounting exercise to reflect accounting provisions already made. Dr Lynch, however, was adamant that the write-off *"was done by HP Finance after the acquisition"*. I return to this dispute later.

339. The Defendants rejected the suggestion that the ATIC transaction was contrived purely or predominantly to provide the means for Autonomy to fund MicroTech and enable it to discharge enough of its indebtedness under the VT13 purchase order to assuage Deloitte and the Audit Committee and give the appearance of substance to the transaction. On the contrary, Dr Lynch defended the transaction as having a sound commercial rationale, which was entered into at fair value, and which was approved by Deloitte. Mr Hussain endorsed and adopted his case. Further, the Defendants contended that when MicroTech did build the ATIC, it incorporated most of the features in MicroTech's initial proposal to Autonomy, and did employ the highly experienced staff who had been recruited for it.

340. Dr Lynch's answer to the Claimants' allegations, as adopted by Mr Hussain, can conveniently be dealt with under five headings: (a) what the ATIC comprised; (b) its

commercial rationale; (c) the Defendants' case on fair value; (d) Deloitte's review; and (e) construction and use of the ATIC.

341. As to (a) above, the ATIC was designed and subsequently run by Dr Roger Channing, then Chief Technology Officer and senior Vice President at MicroTech ("Dr Channing"). He was highly qualified and had current US secret clearance.

342. The ATIC was proposed to have a number of components. There were three main components which were costed. First, a "MicroData Center", a demonstration of private cloud technology solutions. Secondly, an "Emerging Technology Center", for MicroTech to highlight Autonomy software in a virtual store front. These were subsequently built. Although its footprint was not large (it was described by Mr Steve Truitt as something you could have (and MicroTech did in fact for a while have) in a *"trailer in the garage"*[33]), Dr Channing explained in the US MicroTech trial that the ATIC was usually in a building, and that "*that impressive room that you saw in the video*[34] *is where the Emerging Technology Center was*," and that that was where he demonstrated Autonomy software. Mr Kalbag explained that that was also demonstrated to him. Thirdly, a "Test, Evaluation and Integration Laboratory". (Dr Channing explained in the US that that was also built, and Autonomy software had been used there).

343. As to (b) in paragraph 340 above and the commercial rationale for the ATIC transaction, Dr Lynch told me that, after initial lack of interest, Autonomy then had a change of heart after Autonomy had installed a system for GCPD (which he explained referred to *"a number of UK intelligence community systems"* generating or storing classified items which Dr Lynch referred to as *"secret squirrel"*). The reason for this change of heart was that Autonomy had no cleared facility to demonstrate its capabilities to these customers. ATIC was identified within Autonomy (principally by the Defendants) as a vehicle which might assist in boosting Autonomy's federal business by showcasing functionalities of multiple products to a wide range of government and intelligence agencies in a purpose-designed security-cleared demonstration centre, staffed by cleared personnel with extensive experience with cleared customers.[35]

344. The federal business within Autonomy was an area that Autonomy was struggling to grow. Mr Kalbag,[36] a salesman in the federal business, accepted this. Mr Kalbag also accepted that this was an area of potential growth. He considered (which the Defendants' closing submissions did not mention) that what Autonomy really needed was wider exposure to more federal customers through *"a wider pool of integrators who are able to*

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[33] There was a dispute as to what he meant. The Claimants' presentation gave the impression that he was describing the whole ATIC facility. What he said (in his depiction in the MicroTech proceedings in the US) was that a part of the facility, the MicroData Center (MDC) which was to feature Autonomy-based MicroTech "Private Cloud Solutions", was *"not big. Like you could have it in a trailer in the garage like we did at MicroTech for a while".* The Defendants argued that he was not saying that the whole ATIC consisted of a large facility in a building. In the MicroTech proceedings, Dr Channing estimated its size as 3,000 sq feet. No evidence was provided to me otherwise.

[34] A video of the facility was shown to the Court in the MicroTech trial in the US, but neither that video nor any other, or any other photographs were provided to me in these proceedings. The Claimants' closing submissions mentioned that Dr Channing conceded when cross-examined that no video had been disclosed in the Microtech proceedings in which any mention was made of Autonomy.

[35] Dr Lynch was plainly intrigued by business with US and other Intelligence agencies and spoke almost conspiratorially of *"the Five Eyes"* services.

[36] Called by the Claimants.

sell your product rather than having to go through MicroLink"[37].[38] Mr Kalbag accepted that in theory having the ATIC was one route to giving Autonomy this increased exposure to federal customers.

345. Dr Menell described this (in an email dated 16 December 2010 to Mr Scott and Mr Hussain) as potentially providing *"a massive advantage if we can offer in the US a fully accredited storage capability for protectively marked content"*. Mr Hussain (so he wrote to Dr Lynch on 14 December 2010) considered *"the income potential could be huge but would require some investment from us…"*.

346. Mr Kalbag accepted that all the technology described above was likely to be a useful way of showing technology to customers. Mr Kalbag accepted further that the proposed staff were suitable for the work, the staffing structure was appropriate, and the costs were reasonable in terms of running the facility.

347. The personnel costs were a large proportion of the proposed cost to Autonomy of the ATIC: but Mr Kalbag confirmed that the staffing levels in terms of numbers and relevant accumulated expertise were reasonable. The other main cost of the ATIC was equipment related. Mr Kalbag accepted that this was reasonable also.

348. The Defendants relied on a combination of Dr Lynch's description (which omitted (2) and (3) below) and email evidence as demonstrating an orderly approval process for the project, as follows:

(1) On 5 November 2010 MicroTech had provided Mr Scott with an initial proposal. This costed the facility for only one year, at a cost of $3.745m.

(2) In the thread of emails is one from Mr David Truitt to Mr Scott dated 5 November 2010 explaining that he had been provided with the Proposal by MicroTech to pass along, and commending the proposal as offering Autonomy *"a unique and strategic advantage that will ultimately result in growing market share within the Federal Sector."*

(3) Mr Scott forwarded the email to Mr Hussain that same day (5 November), but nothing was done until 13 December 2010 after Mr Scott sent Mr Hussain a reminder, having himself *"Got another ping from MT"*.

(4) On 14 December 2010 Mr Hussain forwarded the proposal to Dr Lynch, stating:

> "*Given the success of GCPD and MicroLink in providing services in the federal space I think it may be a good idea to begin considering the need for a data centre and test bed for cleared federal data and projects. I believe the income potential could be huge but would require some investment from us. This is a proposal for Microtech who now owns our*

[37] It will be recalled that MicroLink was a small integrator favoured by Autonomy as a VAR, which had what was known as a "GSA Schedule" which meant that it was pre-approved for conducting business with US Federal Government departments and agencies.
[38] Mr Kalbag's theory was that Autonomy should have been making more use of the larger resellers and integrators such as Lockheed Martin. Dr Lynch explained the problem with this approach at paragraph 38(2) above, it would have made Autonomy beholden to the large Government suppliers, stripping out Autonomy's margin. Mr Kalbag accepted that his approach would have meant paying over margin.

GSA schedule I believe. If you think it appropriate, I can review with Pete and get some prices."

(5) Dr Lynch, who understood at the time that the opportunity had an intelligence focus, responded the next day: "*ok I assume this is secret squirrel so pls be careful who you talk to*". Mr Hussain responded that he would run it past Dr Menell (who was cleared) and that only cleared people would be involved. Dr Menell, when asked by Mr Scott whether he supported the purchase, replied:

> *"Yes, it's a massive advantage if we can offer in the US a fully accredited storage capability through protectively marked content"*

(6) Mr Scott negotiated with MicroTech over the price. On 22 December 2010 Mr Scott emailed Mr Hussain, Dr Menell and Mr Chamberlain with regard to negotiations that he had conducted on the one-year proposal, which he thought was "*the best we will do*". On 24 December 2010 Mr Scott explained to Mr Hussain, Dr Menell and Mr Chamberlain about the disadvantages of the one-year limitation in the proposal, and that he had negotiated pricing under which the best achievable discount involved a 3-year commitment for $9.6m. Again, there has been no suggestion that Mr Scott was acting improperly in this regard. Dr Menell confirmed that the pricing looked "*in the right ball park if not relatively reasonable*". He recommended some due diligence on comparative staff compensation to see if there was any "*wiggle room for further negotiation*". Mr Scott had done the negotiation and did not think there was.

Mr Hussain approved the purchase. Mr Scott then forwarded the approvals, with a deal summary, to Dr Lynch, and followed that up later in the day with a further email *"just to clarify this has already been run by Andy, and Sushovan and Pete have both signed off."*

(7) Dr Lynch approved it in terms which suggested that he had not read the deal summary but referring to an intelligence focus:

> *"Ok i assume this is the spooky stuff... God bless America"*

349. Dr Lynch emphasised the point that in the round this was all a matter of business judgement.

350. Turning to (c) in paragraph 340 above, Dr Lynch's position in his written closing submissions was that (i) the ATIC was purchased at fair value and (ii) the Claimants had not contended otherwise. As to (ii), however, the Claimants attacked the issue of fair value in their own written closing submissions, as has been referred to above. Further, Mr Welham had been instructed to assume for the purpose of his witness statement that *"what Autonomy paid for the right to use the ATIC licence substantially exceeded the value (if any) of the ATIC transaction to Autonomy".*

351. According to Dr Lynch:

(1) Contrary to the Claimants' case, the increase in the lifespan of the ATIC deal from one year to three years at an almost three-fold increase in the price was not motivated by a wish *"to put MicroTech in funds to pay more of its outstanding*

debt"; rather, Autonomy was interested in the arrangement continuing for more than one year because "*most government projects span more than 1 year from inception to award, with larger projects spanning 2 and 3+ years in many cases*". MicroTech offered terms for a multi-year arrangement including up to 5 years for $15.5m. In the event, Autonomy chose the option with the highest discount (16.77%), not the largest payment. This was $9.6m for 3 years.

(2) Mr Kalbag accepted in evidence that the component parts of the cost summary were reasonable.

(3) Dr Menell also thought at the time that the costs were reasonable given what was provided, but pushed Mr Scott to negotiate the best discount. Mr Scott, who had been handling the negotiation, considered the price offered to be "very compelling".

352. The Defendants placed reliance also on the review and approval of Deloitte (see (d) in paragraph 340 above). This was, in a sense, adventitious. In his witness statement, Mr Welham had stated that the ATIC purchase was not brought to Deloitte's attention by Autonomy, and it only became apparent to Deloitte when a member of the Deloitte team came across it when reviewing Autonomy's general ledgers as part of their 2010 audit work.[39]

353. Deloitte reviewed the ATIC purchase to satisfy themselves that it made commercial sense, was at fair value, and was not a reciprocal/barter transaction. In their workpaper they were content with the rationale and price (though they caveated this with the statement that given the uniqueness of the purchase they had no "conclusive evidence"), and were satisfied that it was not a *"barter transaction"*.

354. In relation to the construction and use of the ATIC (see (e) in paragraph 340 above) the Defendants contended that the facility was built, that whilst some features were not yet included it was capable of being and was used successfully for the purposes for which it was of utility to Autonomy, and that there was nothing in the Claimants' case that the purchase was a contrivance to put MicroTech in funds.

355. The ATIC was under construction by MicroTech in the first half of 2011. Dr Channing, who was the main designer, developer and operator of the ATIC and was highly experienced with Autonomy software and an enthusiast about it, also gave evidence in the MicroTech case in the US in relation to the building and subsequent operation of the ATIC. The Defendants referred to the following points, which they maintained were not disputed by Mr Kalbag, who (they said) had *"positively endorsed"* some of them:

(1) The costs of designing, developing, building and operating the ATIC between 2011 and 2014 were in excess of $8m. Mr Kalbag confirmed: "*Well I saw it, so I can imagine that may be a fair price.*"

(2) As regards Autonomy being showcased without its competitors, Dr Channing's evidence was:

[39] Dr Lynch was keen to emphasise that the transaction was visible on Autonomy's ledgers, to which Deloitte had open access, and was not concealed in any way; and that Deloitte always had full access to Autonomy personnel.

> *"Q. Were any of Autonomy's competitors ever a part of ATIC?*
>
> *A. No. The many competitors for Autonomy were other discovery engines, like FAST that Microsoft had and some others, but we never -- no, we never had a competitor for Autonomy. That was always our number one search and discovery engine."*

(3) The centre first opened in July 2011. Demos were run for customers and the ATIC had around 1800 customers from 300 organisations. Contrary to the Claimants' assertion that the ATIC was not used, Dr Channing's evidence was:

> *"During the time that the facility was open, our best estimate from people signing in, we had about 1,800 visitors they were from about 300 different organizations and 21 different countries. And I did almost all those briefings."*

(4) Dr Channing confirmed that he got the basic form of IDOL to do live demonstrations, though (and it is of some note) he added (a) *"we didn't get any of the peripheral – we would keep asking…"* and (b) demonstrations were further restricted because *"…there was a portal that had numerous applications of Autonomy and they would not give us – we couldn't get access to that portal"* (unless an Autonomy rep. was present who could provide a log-in and password key). He added that Autonomy was in every briefing that he gave.

(5) Dr Channing pitched to commercial clients as well as Government clients, but the Government clients were the majority. The Government institutions to which Dr Channing gave demonstrations included all the "three letter organisations", by which he meant intelligence organisations. They also included health organisations, the Army and Department of Defence.

(6) Mr Kalbag accepted that the ATIC was built and he saw it. He thought it a *"great showcase"* (though see below).

(7) The ATIC was also visited and used by HP. There is also documentary evidence that HP and MicroTech were also planning various demonstrations of Autonomy software in the I2C (i.e. ATIC).

356. The Defendants accepted the Claimants' contention that some features or proposed functionalities of the ATIC were not built; but they submitted that the Claimants had exaggerated this and that in any event they had missed the point, which was that the main features of the ATIC were built. Thus, according to the Defendants:

(1) The Claimants referred to the fact that MicroTech did not construct the "mobile data center" for Autonomy, and sought to make some play of the events relating to this aspect of the facility: but the Defendants depicted this as immaterial on the ground that that part of the proposal was not even costed in the proposal. The Claimants dismissed this as misconceived.

(2) Certain *"more subordinate features of the facility"* were not built; but according to the evidence of Dr Channing in the MicroTech proceedings, the *"medical scientific research solution"* was not provided because MicroTech did not have the requisite licences; the Department of Defence record management and archiving solution was not installed because it was decided that the facility already had *"the ability, with resources, to implement most of the listed capabilities"*; and the Intelligence/Investigative Solution was not provided because, in the event, Autonomy did not want or support it. As to the test evaluation laboratory, Dr Channing's evidence was that this was built, and had IDOL software running on it (points which were glossed over by the Claimants), albeit that it did not have other Autonomy application software. The Defendants submitted that none of this impacted on the commercial rationale or fair value of the ATIC investment at the time that it was made.

357. In conclusion, the Defendants rejected the Claimants' criticisms of the merits and purpose of the ATIC purchase as *"misguided in any event"*. They depicted the Claimants' presentation as having *"ignored the fact that MicroTech did build the ATIC, and did employ the highly experienced staff who had been recruited for it"*. That is what the funds provided by Autonomy paid for; they did not fund repayment under VT13: the money could not be spent twice. In the round, they accused the Claimants of building a *"distorted case though their witness statements, in particular from Mr Kalbag"* and submitted that when it came to his cross-examination, *"he in fact accepted most of the propositions which undermined [sic] the Claimants' case."*

My assessment of the dispute re the ATIC

358. There was exaggeration on both sides of the record in their respective cases concerning the ATIC.

359. The Claimants' alleged that the ATIC was little if anything more than a room and a vehicle trailer, largely uncompleted, the only purpose of which was to demonstrate MicroTech's own capabilities and which was of no utility to Autonomy because all its demonstrations could be done more easily on a computer screen were overblown.

360. On the other hand, I do not consider that the Defendants' accusation against the Claimants of presenting a highly *"distorted case"* was appropriate or made good; and they never satisfactorily provided any realistic and reasonable explanation of why it was and how it was justified that alone among all the companies whose software was demonstrated in the ATIC, only Autonomy paid for the privilege, still less how the privilege of a three-year non-exclusive licence justified a price in excess of the entire build and most of the manpower bill. I address both sides of the argument in more detail below.

361. It seems clear, for example, that the Claimants' suggestion, based on Mr Kalbag's evidence in his witness statement, that the ATIC facility was not used by Autonomy or any of its customers, was exaggerated. The Defendants could point to a number of emails suggesting some use; and to the evidence of Dr Channing[40] that he demonstrated Autonomy software in the part of the facility referred to as the *"Emerging Technology Center"*, that there were many customers visiting the ATIC including all the *"three*

[40] Dr Channing stated in his US evidence in the MicroTech proceedings that *"People call me an Autonomy zealot because I super-believed in the software and capability and things that it can do for society and government"*.

letter" organisations[41], and that he mentioned Autonomy software in every briefing that he gave to visitors to the facility, which he numbered at about 1,800. However, the Claimants' broader point was that, in circumstances where Autonomy had spent \$9.6 million on the ATIC licence of just three years, one might have expected an urgent and major effort to use it and deploy all Autonomy's range there: but there is no evidence of any such effort at all.

362. To take another example: the Defendants submitted that the Claimants had miscast Mr Steve Truitt's evidence given at the US criminal trial that a purpose of the ATIC was to obtain funds with which to pay down MicroTech's debt to Autonomy. They submitted that the Claimants should have made clear that the idea had come from Mr David Truitt and was not that Autonomy should simply fund MicroTech but that MicroTech should come up with a genuine business transaction that would create value. However, Mr Steve Truitt's evidence (admitted as hearsay) gave the strong impression, to my mind, that the transaction was taken up by Autonomy as a useful funding mechanism, even if it may have had other potential advantages (for MicroTech itself especially):

> *"Q. Okay. And -- and is it correct that David Truitt said to you in substance that getting Autonomy involved in some way relating to the ATIC would be a way to get money -- would be a way to get Autonomy to pay money to MicroTech that could be used to pay down what was owed on paper with respect to the Vatican deal?*
>
> *…*
>
> *THE WITNESS: Yeah, in a nutshell.*
>
> *Q. Okay. And --*
>
> *A. The thought being that we could create value in excess of the cost, ideally, and that would be a way that we could do business with them directly that would allow us to earn the money to pay out from under these debts for the ones that weren't closing that we had taken on."*

363. It is dangerous to parse or read too much into hearsay evidence of this kind: but the impression I was left with, having regard to the context, was that funding was at least a major driver, and utility to Autonomy a subsidiary consideration. ATIC was a useful vehicle. That impression is in part informed also by the notably limp way in which Autonomy pursued any opportunity offered by the ATIC facility (see paragraph 361 above).

364. It is also informed by the clear coincidence between the payment made by Autonomy for the ATIC and the use of the funds by MicroTech to discharge MicroTech's debt. The Defendants characterised this as *"an insubstantial point"*. They contended that it was *"unsurprising that Autonomy would want to pay its debts promptly, and even more unsurprising that Autonomy would expect a debtor customer to pay Autonomy when*

[41] Signifying (as explained by Dr Channing in his evidence in the MicroTech proceedings in the US) intelligence services, health organisations, the Army and Department of Defense.

Autonomy made its own payment." I have not found this convincing: it smacked to me of special pleading and overlooks and seeks to deflect attention away from the manner and circumstances in which the price was agreed and then agreed to be revised, and the way the payment to MicroTech was made. In particular:

(1) As Dr Lynch accepted in cross-examination, in mid-December 2010 Deloitte were pressing to know when MicroTech would pay down its debt.

(2) I agree with the Claimants that the link between agreeing a purchase of an ATIC licence from MicroTech, and the collection of MicroTech's overdue Vatican Library balance, all before imminent year-end, is clear.

(3) The only evidence advanced in support of the price agreed for a one-year deal (of $3.3 million), and then $9.6 million for a three-year deal with a commitment to pay in 2010, was Mr Scott's evidence that this was the product of negotiation; but Mr Scott's evidence indicated that Mr Hussain was involved throughout and he stated at the criminal trial that the impetus behind the increase in the size of the deal came from Mr Hussain, who *"said to me he would like to do a larger deal with MicroTech in the 9 to 10 million-dollar range and asked me to take that back to Dave Truitt, at which point I did, and this reflects the larger deal that Sushovan had asked for".* That is not a negotiation at all. I see no reason not to accept that evidence, which I consider to be inherently plausible, especially given the pressure to ensure repayment. There was no real evidence of fair value.

(4) The only documentary basis for the ATIC transaction was a one-page purchase order referring to the ATIC as described in MicroTech's Proposal and providing for payment of $9,600,000 on 31 December 2010, without further terms. The Proposal was written in marketing language and made no attempt to define the parties' legal rights and obligations. Mr Scott made the point which I also accept, that typically an investment of almost $10 million would be the subject of detailed terms and conditions.

(5) The obvious inference is that none was needed because the product was not the principal purpose: it was the payment by the end of the year, and not the ATIC or the parties' plans in respect of it, which was the essence of the arrangement. Likewise, there was no specified requirement for, and no evidence was provided of, build progress or the like. MicroTech's "Proposal" for the ATIC was in the form and style of a marketing document, proposing an idea, not a business plan: but that is all Autonomy ever got.

(6) The purchase price covered (a) payment of the full salaries for three years after construction of five MicroTech employees who were to staff the ATIC and (b) the entirety of the construction costs of the ATIC facility, in circumstances where Autonomy got only a three-year non-exclusive licence to have its software displayed in that facility.

(7) Furthermore, the entirety was payable in advance, and was in fact paid in full in advance on 31 December 2010. I agree with the Claimants that none of this made commercial sense.

(8) The acceleration of payment, together with the immediate payment down of MicroTech's debt that same day, is also consistent with, and in my judgment in the context supports, the Claimants' case. So too does the fact that there was apparently no record of the five MicroTech employees (for whose services Autonomy supposedly paid $2,874,000) ever performing any material services for the Autonomy group. The Claimants suggested that the evidence of Dr Channing was that the principal person who was to undertake work was Dr Mayall, who had not spent anything like the 1500 hours per year on Autonomy-related projects that had been budgeted (and paid) for; and neither Mr Guzman nor Mr Kirsch had spent appreciable time on Autonomy-related projects either; and that in fact only some $200,000 had been spent on the salaries of two engineers who, with Dr Channing himself, did some Autonomy-related work. Yet Autonomy had made no complaint.

(9) In addition, and to my mind of particular importance, there was no evidence that any other company was prepared to or did pay anything in return for the usage of the ATIC. In his deposition in the MicroTech trial, Mr Steve Truitt professed not to know whether that was the case or not. Dr Channing was closely questioned about the issue in the MicroTech trial. It is fair to note that he made clear that he had nothing to do with cash receipts: but he did not make clear, and it was never mentioned, who did. In any event, it seems to me to be most unlikely that he would not have had any awareness at all about cash support for the project, even if he was not involved in accounting for it. He was not able to point to a single contribution from any of the various entities that had their products featured in the ATIC. These included HP: and if HP had contributed any money, it would have been easy for it to have provided evidence accordingly. I infer that it made no payment; and if it did not, the further inference is that others did not either. In other words, Autonomy paid $9.6 million for something for which the others in the non-exclusive group using ATIC paid nothing. That seems to me strongly supportive of the Claimants' case.

(10) Dr Lynch's perceived "trump card" was the notion that since MicroTech built and paid for the facility, the money paid cannot have been intended to be, and could not be, used to discharge indebtedness: as Dr Lynch put it: *"It's a real thing. It's really built"*: *"I don't understand how you spend money twice"*. This is not the answer Dr Lynch appears to have convinced himself it offers. To my mind, it presents another point against his case. There is nothing to suggest that the build costs of the ATIC had to be met immediately. It was a valuable asset in MicroTech's ownership. There is no reason to suppose it had no other means or facility to fund it. Even more obviously, the undisputed fact is that a substantial proportion (amounting to $6.3 million)[42] of the money paid by

[42] Of that $6.3 million, $1.89 million was used to settle MicroTech's debt on VT6 (end-user Honeywell) and $4.321 million was used as a part payment on VT13 (end-user Vatican Library). MicroTech made further payments in respect of the remaining debt by payments of $2 million in April 2011 and $2.4 million in early July 2011 (which the Claimants contended was paid using funds received by MicroTech from DiscoverTech, which, in turn, had been received from Autonomy in the context of VT30). The remaining $2.3 million of the total of $11.55 million was never repaid. Instead, it was written off as at 30 September 2011 (three days before the HP Acquisition completed).

Autonomy came back to Autonomy in discharge of MicroTech's debt that same day: it is certain that most of Autonomy's money did not fund the ATIC.

(11) Large parts of the ATIC as originally proposed were never built. Dr Channing testified in the MicroTech trial in the US that MicroTech did not construct (i) the mobile data centre featured in its original proposal; or (ii) the *"medical scientific research solution"* promised in that proposal; or (iii) the Department of Defence record management and archiving solution described in the proposal; or (iv) the intelligence investigation solution promised in the solution or (v) a test evaluation laboratory using Autonomy applications. Mr Kalbag confirmed that he was not aware of MicroTech having built any of this. Yet no-one from Autonomy ever pressed MicroTech to deliver any of these things, as Dr Channing confirmed in his evidence in the MicroTech trial in the US. Dr Lynch also told me in cross-examination in these proceedings that he took no steps to find out whether MicroTech had built what it had promised. That too is consistent with, and in my judgment supportive of, the Claimants' case that Autonomy did not need the ATIC and was largely indifferent to it: and that it was a funding operation not a commercial investment.

365. As in other contexts, I do not consider the fact that *"Deloitte analysed the transaction and were content with the rationale and price"* is the trump card that the Defendants suggested it was. Had Deloitte known, as I have found to be the case, that (a) Autonomy had no real need or intended use for the ATIC and/or (b) its real objective was to ensure that funds were available to MicroTech to enable it to pay down the majority of its liabilities to Autonomy, they would not have agreed to the accounting treatment accorded to it, as Mr Welham expressly confirmed.

366. The context tells against the depiction of the correlation between payment and repayment being an insubstantial point. The circumstances as a whole, as well as the back-history, tell against the ATIC deal being simply a self-standing arrangement born of a coincidence of interest and the payments and repayments made being in the ordinary course of trade; MicroTech plainly needed to find some way of funding its debt; it had always expected that Autonomy would find or accede to some means of achieving that; the correlation between payment and repayment was legitimately relied on by the Claimants as a further indication that the ATIC deal was the way that was found.

367. In my view, the Defendants' depiction of Mr Kalbag's evidence as in effect helping them more than it hindered them was based on an unfortunately selective reliance on evidence which in the round gave a very different picture. I can take a few examples to illustrate this:

(1) The Defendants submitted that Mr Kalbag *"ultimately agreed with most of the commercial rationale that Autonomy had at the time"*. But in fact, what Mr Kalbag told me was that *"it didn't make sense"*. He elaborated:

> *"I think in general there are many big integrators who have these showcases, so there's nothing wrong with having that. I think the issue is that for most of our software we would do the sales and even MicroLink would do the sales by going to the customer and being at the customer's site. Also Autonomy software was pretty much back end software, it wasn't something that was very exciting graphically.*

Autonomy specifically decided not to focus on user interfaces as much as possible, so the idea that putting in a very expensive demo centre where, you know, what you're trying to show is archiving or some other thing that you can show on a laptop, it just – to me, it didn't make sense, and at the time I wasn't even aware that we had paid for it so my impressions were based on what I saw when I went to see a demo of it, it didn't even seem applicable to what our sales people were trying to do."

(2) The Defendants cited Mr Kalbag's evidence that the ATIC was a *"great showcase"*; but they omitted to mention that he went on in the next phrase to say:

"The problem was that the majority of that…centre was focused on hardware and not our software. I mean, when I left that demo, I was like this is a great showcase for Microtech possibly - I didn't even know what their business was – but I did not feel that this was, you know – like I would have been super surprised that we had actually paid for it at that time…"

(3) Later in his cross-examination, though accepting that MicroTech would be *"leveraging its own ability to sell into the federal space and to provide services in the federal space"*, which might assist Autonomy when using MicroTech as a VAR, Mr Kalbag elaborated as follows:

"It might help them sell more hardware for Microtech and that was the impression that I left…it was that this is a demo centre for Microtech…this was a Microtech demo centre, and yes, there was a room with our technology in it, but I never brought a customer to it afterwards…I can tell you for sure that the impression that was left on me after seeing the demonstration…was that this was primarily around selling Microtech's capabilities…than the primary purpose being for Autonomy…"

(4) He responded to the arguments put to him that nevertheless Autonomy might be assisted as follows:

"So I mean, you know, I think all of your arguments and what you're asking me is in theory and I would argue, yes; <u>just when you add it all up it doesn't make sense to me.</u>" [My emphasis]

368. Even if Mr Kalbag tended to overlook that though primarily a showcase for MicroTech the ATIC could be and was a useful and successful display centre for others, there was no logic in Autonomy paying nearly $10 million for 3-years of rights and benefits other companies got for free without limit of time: that did not make sense. Although the Defendants sought to wrap this in the clothing of a business decision, it is still necessary to be satisfied what business rationale lay behind it: and I have not been persuaded that there was a business rationale for paying so much for what others paid nothing. Some other rationale must have driven that decision.

369. In short, I have concluded and find that the real point of the payment (for the ATIC), and its calibration, was to get as much by way of funding as possible to MicroTech to enable it to make payments in part payment of its obligations and in satisfaction of Deloitte's expectations and concerns.

Defendants' knowledge of VT13 and the ATIC transaction

Mr Hussain

370. The Claimants' principal submission with particular reference to Mr Hussain's role in VT13 was that he knowingly misled Deloitte (a) first, by giving them to understand that the Vatican Library had been informed that the licence was to be supplied through MicroTech: they alleged that he must have known that what he was telling Deloitte was untrue, and in any event, there was certainly no factual basis on which he could have believed it to be true; and (b) secondly, by representing to them during the FY 2010 audit that MicroTech had concluded a sale to the Vatican Library and that the only reason why Autonomy had yet to be paid was that the Vatican Library had yet to pay MicroTech.

371. As to (a) in the preceding paragraph 370, Mr Hussain relied on Dr Lynch's evidence that the fact of MicroTech's involvement was well known to the Vatican Library's agents (see paragraph 321 above). As to (b) in that paragraph 370, Mr Hussain made the point that it was quite apparent from, for example, the notes for the audit planning meeting and Dr Lynch's evidence that Deloitte were well aware that there was no deal between MicroTech and the Vatican Library.

372. I have determined (see paragraph 322 above) that Dr Lynch had no basis for supposing that the Vatican Library had been informed of MicroTech's involvement, and his evidence amounted to an acknowledgement that they should have been, in accordance with ordinary procedure. I find that as the Vatican Library later told HP (see their letter referred to in paragraph 306 above) they were not told, and that Deloitte were misled in being given to understand otherwise.

373. I have also determined that Deloitte were told that MicroTech had made a deal with the Vatican Library as end-user, that the Vatican Library had been informed that MicroTech was to be the supplier of the software sold, and that MicroTech would thus receive payment from the Vatican Library. Deloitte's working paper makes the above clear.

374. In my judgment, Mr Hussain knew the true nature of VT13 and did mislead Deloitte.

375. As to the ATIC, the Claimants contended that it was Mr Hussain who fastened on MicroTech's proposal (in an email from Mr David Truitt dated 5 November 2010, which Mr Scott forwarded to Mr Hussain that day) for Autonomy to purchase a licence to use the ATIC as a means of funding MicroTech under cover of a transaction which could be presented as having a separate commercial purpose; and that Mr Hussain's true objective was demonstrated by (a) his emails chasing for closing of the deal to enable MicroTech to make a payment which would assuage Deloitte's concerns about its outstanding obligations and (b) the impetus he gave to increasing the licence fee payable by Autonomy.

376. Against this, Mr Hussain adopted Dr Lynch's case that the ATIC transaction had a rational commercial purpose at the time it was made, and that no complaint could legitimately be

based on his part in representing the transaction accordingly to Deloitte. In his written closing submissions, Mr Hussain summarised the position as follows:

> *"it would be fair to say that Cs' case that Mr Hussain misrepresented that there was a commercial rationale for the transaction collapsed at trial. Sameer Kalbag conceded that AU was struggling to grow its federal business; that it had insufficient exposure to US government agencies; that the use of a demonstration unit was a recognised way to increase exposure and to showcase the functionalities of software; and that ATIC was a means of achieving these ends. When he was shown MicroTech's proposal document for the ATIC he agreed that it was a useful way of showing technology to customers. The furthest his evidence ultimately went was that it was a matter of business judgement whether the ATIC was the best route for addressing Autonomy's admitted need to improve its federal business, or whether there was an alternative or lower cost route. Indeed, it emerged during his evidence that his alternative proposal of demonstrating AU's software to US intelligence agencies on a laptop would not have worked: Mr Kalbag did not have any clearance level to do such a thing."*

377. For the reasons I have stated at some length above, I disagree with this assessment. Mr Hussain was, I consider, the principal proponent of the ATIC deal as the means of enabling a substantial payment down of MicroTech's debt before the year-end as Deloitte had emphasised was important and they expected. In my judgment, he knew that the ATIC deal was primarily a means of enabling MicroTech to pay and Autonomy to honour MicroTech's expectation that it would not be "left on the hook"; and Mr Hussain had "guilty knowledge" of the impropriety of the accounting treatment both of the ATIC deal and of VT13 accordingly.

Dr Lynch

378. Dr Lynch, who was cross-examined at some length about his knowledge and involvement in VT13, accepted that the project was certainly a contender for the *"biggest ever single deal done by Autonomy"* and that he was well aware of it at the time. He was also *"kept appraised of how it was going"*. He emphasised, however, that he *"wasn't at the level of actually negotiating it or doing the technical details…"*. He denied being aware of any impropriety in the transaction or the accounting treatment of it, and he submitted that the Claimants had not shown *"even the vestige of a case"* to show that he was.

379. I do not agree. In my judgment, it is more likely than not, and I find, that Dr Lynch was well aware that MicroTech's introduction into the Vatican Library deal as a VAR (of which he accepted he was aware at the time) was solely to enable Autonomy to book revenue from a transaction to which MicroTech was (except for the purposes of remuneration) in substance a placeman. Although Dr Lynch told me he thought that "agents" for the Vatican Library knew of MicroTech's involvement this did not carry conviction (and I have determined against it above).

380. I think it more likely than not, and I find that at the time (a) Autonomy had had to resort to a VAR precisely because funding for the Vatican Library project (from the unnamed *"Mexican billionaire"* from whom Dr Lynch told me a large donation had been on the brink) had fallen through, and the deal was bound to be substantially delayed since the

Vatican Library was unwilling to fund the project itself; (b) Autonomy had no intention of stepping back from the negotiations and no intention or expectation of MicroTech becoming involved from the US in any way in such negotiations (for which MicroTech was singularly badly placed and ill-equipped in any event); (c) MicroTech had limited reserves and could not realistically have taken on an $11 million risk without assurances that it regarded as water-tight (Dr Lynch's suggestion to me that he would have been happy on behalf of cash-rich Autonomy to pay such a sum for the opportunity of being involved in such an important project being entirely inappropriate in the case of cash-strapped MicroTech).

381. I also consider it more likely than not, from the available evidence and my own impression when Dr Lynch was cross-examined and sought to dispute what was put to him along these lines and to blame Deloitte that (i) Dr Lynch was aware that Mr Hussain had told Deloitte that the Vatican Library had been informed of the sale to MicroTech, and knew this was not correct; and (ii) he was also aware that Deloitte was consistently given the impression, which was reflected in their reports which were sent to Dr Lynch, that MicroTech was dealing with and expecting payment from the Vatican Library as end-user, and that this was untrue.

382. In summary, I have concluded and find that Dr Lynch knew that the sale to MicroTech was not intended or expected to result in any substantive change in the way Autonomy dealt with the Vatican Library in respect of the goods "sold", or in the way the goods would be made available to the Vatican Library if the sale still hoped for by Autonomy to the Vatican Library did eventuate. He knew further that Deloitte had been given to understand otherwise, because it was necessary for the purpose of their approval of revenue recognition that the "sale" to MicroTech should be regarded as having real substance. This was typical of a pattern of which he was more generally aware, and a further demonstration of his "guilty knowledge" in respect of all the impugned VAR sales.

383. The Claimants also cross-examined Dr Lynch in respect of the ATIC transaction, again at some length. I have set out the process by which the proposal was assessed and the sequence of steps leading up to approval of the proposal in paragraph 348 above. Dr Lynch's position was that:

(1) (as he put it in cross-examination):

"The decision by Autonomy to buy it had nothing to do with the collateral effect of creating cash flow for MicroTech, Of course MicroTech still has to spend all the money to build this thing, so it's not getting free money here. It can't use the money twice."

(2) He was not involved in the detail; for example, he maintained in cross-examination that he did not even know that the proposal was originally for a one-year deal.

384. Dr Lynch's more general involvement is clear. Also clear to me, from my observation of him when giving his evidence, was the particular pride and interest he had in the application and use of IDOL in the intelligence community and its usage in the *"secret*

squirrel" sphere[43]. I feel sure that had the purpose of the ATIC deal been, or predominantly been, to provide the means of marketing to the *"Five Eyes",* Dr Lynch would have made sure that he was closely involved in it. He liked what he called *"the spooky stuff"*.

385. As it was, however, Dr Lynch told me he *"wasn't particularly involved in the details".* He told me that he had no memory of the original one-year proposal because *"it wouldn't have been very useful for just one year"*, and said that would not really have been of interest. He rejected as inaccurate the suggestion put to him that *"it went from a one-year deal to a larger deal because Mr Hussain wanted to do a deal in the 9 to $10 million range"*; and he denied that Mr Hussain had explained to him that Autonomy needed to make a large purchase to put MicroTech in funds to pay down its outstanding debt, repeating once more (as he did again and again) that he could not see *"how you could use the money twice in that hypothesis".* He added that although payment of the debt by MicroTech was important *"you know, at the end of the day they can just have a provision."*

386. Dr Lynch thought he was more likely to have discussed the transaction with Dr Menell than any of Mr Hussain, Mr Chamberlain and Mr Kanter, since Dr Menell was cleared to a high level and had been identified by Mr Hussain as the person to make the recommendation on the transaction. He shrugged off Mr Kalbag's evidence as *"the sort of idle musings of a mid-level sales person…"* and Mr Kalbag's suggestion that Autonomy did presentations off a laptop as *"just crazy".*

387. Although he understood that the licence that Autonomy obtained was stated to be non-exclusive, so that there was nothing in it to stop a competitor company's software being showcased in the facility, he told me in cross-examination that there was *"an arrangement that they wouldn't put competitive software in there…"* He had not mentioned this before, and when challenged as to whether that was documented he explained that this was his *"understanding of the arrangement"* and saying that he was *"pretty sure that it was agreed at some point".* He added that in any event there was:

> *"also the de facto reality on the ground which is, if they had put a competitor in there, then they were reliant on us for their livelihood, it would have been the dog that bit the hand that fed it."*

388. There was, to my mind, something in this, notwithstanding that (as the Claimants remonstrated) it had not been a point made by Dr Lynch before, and it was advanced in a somewhat smuggled way. There was some support for this in the original Proposal and in the evidence of Dr Channing in the US MicroTech proceedings. In the Proposal, it was stated that *"MicroTech envisions the ATIC as the primary Autonomy solutions demonstration center on the U.S. East Coast".* Dr Channing's evidence (admitted in these proceedings as hearsay) was that (a) the reason why the licence was non-exclusive was because Autonomy's software needed hardware infrastructure (some of it supplied by EMC, but with other makes, according to Dr Channing, *"that our Government partners might be using"*); but that (b) none of Autonomy's direct competitors in unstructured data (such as Microsoft FAST) were showcased: MicroTech *"never had a competitor for*

[43] Dr Lynch explained in cross-examination: *"GCPD…represents a number of UK intelligence community systems and the reference to "secret squirrel" is a reference to classified items."*

Autonomy. That was always our number one search and discovery engine". In addition to the fact that Autonomy had few competitors in that particular niche anyway (Microsoft's FAST being the only one mentioned), I accept that showcasing them would have been most unwise for MicroTech if it valued its connection with Autonomy (as of course it did).

389. However, even if accepted, it does not dispose of the point that the ATIC was the showcase for a variety of hardware and hardware/software companies who made no payment at all. Nor does it address the point raised by Dr Lynch's own justification: if, because it valued its relationship with Autonomy, MicroTech would not have hosted and showcased a direct competitor, the payment did not secure Autonomy any more compliance than would have been afforded to it as a matter of MicroTech's commercial interest in any event. In my assessment, it is not likely that Dr Lynch did not appreciate these fairly self-evident points at the time.

390. On the question of fair value, Mr Kalbag had already given evidence to the effect that the price for all the component parts of the ATIC was reasonable (see paragraphs 346 and 347 above); the Claimants put to Dr Lynch that nevertheless the amount paid for a three-year licence was so disproportionate to the overall cost of the ATIC itself as to be commercially irrational. Dr Lynch did not accept this:

> "*No, I don't agree. What we had was access to the facility and that had a set of costs. Those costs actually pretty much line up with what we paid, plus a small amount of profit for MicroTech. And let's just remember, this thing was built. The leases were taken on, the equipment was put in, the systems were set up. People with stella-cleared CVs were employed and the whole thing existed. That cost the money and you can go through the costing and it would pretty soon come out to what we paid plus a bit of profit for the poor people that are doing the work and it was all done. You cannot spend the money twice, it's that simple."*

391. Dr Lynch was asked about Mr Kalbag's idea that a better solution for growing federal sales was to give a licence to an integrator which had its own demonstration centre. This was a question of business judgment, and Mr Kalbag's idea was in any event flawed. Dr Lynch explained this:

> **"***Q. Do you recall that Mr Kalbag said it would have been much cheaper to have given Autonomy software licence to an integrator which already had its own demonstration centre?*
>
> *A. Yes, again, what we're doing here is getting the sort of idle musings of a mid-level salesperson on what you might or might not do. Let me take you through why that's a bad idea.*
>
> *Q. No, let me ask my question. Do you accept that that is true, that it would have been much cheaper to give an Autonomy software licence to an integrator which already had its own demonstration centre?*

A. No, because that integrator would then control the customer and would take margin off of us which would cost us a lot of money and they may well bid our competitors against us which would also cost us a lot of money, so it would turn out to be a lot more expensive in the end. So the problem with these integrators is they have power with the customer, they control the customer and then they make their suppliers bid to supply them. So the reason why we have to have an independent channel is that we don't get squeezed like that. The point being that MicroTech was sufficiently dependent on its Autonomy business that if, for example, we'd seen them bid our competitor into a situation, we would have had them under control, whereas if, for example, it was Lockheed Martin, then all Lockheed Martin would do is it would go around four or five to get the lowest price from the suppliers and it would keep the margin for itself. So a wholly unrealistic understanding of the reality of how these things work.

Q. There's no evidence that anyone even thought about that alternative before deciding to pay $9.6 million to MicroTech?

A. I spent about a decade working with that alternative and continually them doing exactly what I've just described of using their power in the marketplace to cram down their suppliers. What was really important in these areas was to have an independent route that you controlled to the end customer. You needed to have people that could talk to the DIA or the CIA or the NSA or the NRO. As soon as you were going through Lockheed Martin, they would get you and the way they made money was to give a fixed price to the customer and then get the suppliers to bid against each other and you would lose all your margin because you didn't control the customer."

392. Dr Lynch was equally dismissive when asked about Mr Kalbag's evidence that he could demonstrate software on his laptop:

"Okay, I don't want to use the word "absurd" but in a first meeting in a normal commercial environment you might turn up and show something to someone on a laptop, but in terms of any normal part of the sales process for multi-million dollar software sales, you can't show it on a laptop. Actually in this market you can't even show it on a laptop because you're not allowed to take laptops into the customers. Because the customers are sensitive customers, you're not allowed to take in electronic equipment. So, for example, if you go and visit the DIA, or over here their equivalents, you have to leave your phones and your laptops and everything in a special building away from the main building because you can't take it in. When Meg Whitman -- when I took Meg Whitman in to meet these customers, even she had to leave everything and her bodyguard outside. So the idea that you do this business off of a laptop is just crazy. The

> *process for selling software like this is you may well have a first meeting and if it's not a cleared customer and you can show a laptop, you might put something on a screen. But then the normal procedure is to do a POC, which is a proof of concept, and a proof of concept is set up to show what the software can do, but also how it scales, how reliable it is, and that requires setting up a big server, and quite often you'll have to take data and show the customer what you can do with the data. That whole process of a POC can take three to four months. In the cleared case, what they will often do is give you analogous data, so data that's like their problem but it isn't actually their problem and then they want to do things like test scaling, so they want to test what it does under very large volumes, which of course you can't possibly put near a laptop."*

393. But in my assessment, Dr Lynch's aggressive attempts to dismiss Mr Kalbag's evidence was intended to deflect attention away from the unanswerable points mentioned previously: that no-one else paid to be showcased, that the primary beneficiary of the showcasing was MicroTech, and that the money it paid did not get Autonomy anything more than it had or had the means of obtaining already.

394. I accept that Deloitte approved the ATIC license deal. However, (a) there is no evidence that Deloitte were told or aware of the matters summarised in the preceding paragraphs, and they appear to have assumed that any entity which wanted to have the right to use the facility would have to pay a licence fee; and (b) Deloitte did not feel they had sufficient evidence[44] of fair value to opine, and left it instead to be dealt with by a representation letter confirming that the transaction "*was conducted on an arms' length basis and at fair value."*

395. In the round, I cannot accept Dr Lynch's case that he simply relied on others' assessment of the ATIC; and on what he knew he thought that it was a proper business transaction, and was entitled to do so. In my judgment, it is more likely than not that he was aware that the need and size of the payment was dictated by the necessity of providing funds to MicroTech to enable it to pay a substantial proportion of its outstanding debt at a time when Deloitte had expressed concerns. His suggestion that it was not a requirement, and that it was always an option simply to make a provision in the accounts, was disingenuous: the use of VARs to accelerate revenue when needed, which had become an essential part of the strategy to sustain the share price, would have been imperilled and probably fatally undermined.

Summary

396. I have spent some time on VT13 and the ATIC transaction, not only because of their size, and the extended analysis undertaken by both sides, but also because these transactions, and their inter-play, seem to me to illustrate in highly coloured terms features or characteristics of the VAR transactions more generally. The transactions were not typical; but they are illustrative.

[44] Deloitte stated that *"given the uniqueness of this purchase and the customer relationship being offered, we have no conclusive evidence, other than the signed contract and our knowledge of the sales potential of future deals into the US federal space to support this value further."* Since *"conclusive"* evidence in its literal sense must be rare in such a context, I take this to mean sufficient evidence on which to justify a conclusion. It is to be noted that there was no *"signed contract"* other than the purchase order.

397. In my judgment,

(1) VT13 was contrived to generate recognised revenue in a substantial sum to cover a shortfall in circumstances where, to the knowledge of the Defendants, there was no real prospect of an end-user deal in the near or medium term.

(2) MicroTech was retained as a VAR as a matter of urgency because it was a friendly VAR which could be relied on to take on an enormous payment obligation such as to pose an existential risk because it knew the payment obligation would never be enforced unless and until Autonomy found the means of either funding or dissolving it.

(3) The ATIC was the means found to fund the obligation, and the Defendants knew that that was its true primary purpose.

(4) No revenue should have been recognised from the VAR sale to MicroTech. Both Defendants knew that too.

VT25: MicroTech/DoI Q4 2010

398. By comparison with VT13, VT25 was a simple transaction, but it also exhibits many of the characteristics of that and other impugned VAR transactions. It is chiefly remarkable for (a) the desperation about the prospects for software sales that appears from email exchanges to have been the context for Mr Hussain's resort to a VAR transaction at the end of Q4 2010, and (b) the issue of credit notes to MicroTech when no end-user deal materialised.

399. In November and early December 2010, Autonomy had been negotiating with an existing client, the US Department of Interior ("DoI"), a potential deal for the restructuring of DoI's Digital Safe hosting arrangements for an upfront fee (which Autonomy could and intended to recognise as revenue). The prospect of a deal closing within Q4 2010 had seemed positive until (as recorded in an email dated 13 December 2010 from Mr Sullivan to Mr Hussain and others in Autonomy, but not Dr Lynch) DoI decided, for *"strategic"* rather than financial reasons, to *"pass"* on Autonomy's offer and instead undertake a full procurement exercise and then *"evaluate all options"*.

400. A deal with DoI had been one of three (the others being BofA and Deutsche Bank) on which Mr Hussain had been pinning his hopes of (in his own words) *"covering up"* a shortfall on revenue forecasts for the quarter in what he described in an email to Dr Lynch dated 10 December 2010 as bad trading conditions with revenue falling away *"completely"*, calling for *"radical action, really radical…"*.

401. There was a longer lead time than usual before a VAR transaction was arranged: but the evidence does not reveal what happened prior to the issue of a purchase order. The purchase order for the transaction ("the VT25 purchase order") was issued on 31 December 2010 and was (as usual in the case of MicroTech deals) governed by the terms of the June 2006 MicroTech VAR agreement which expressly provided that MicroTech was obliged to pay Autonomy for its orders irrespective of its sale to an end-user. The licence fee was $4,000,000, plus a first-year support fee of $200,000.

402. The VT25 purchase order contained a provision also found in substantially the same form in VT20 (with Capax Discovery, see paragraph 846 below), as follows:

> *"Although End-User and VAR currently anticipate entering into such a license transaction, in the unlikely event End-User, instead, enters into a direct agreement with Autonomy or its affiliate to licence the Software, then VAR shall distribute the Software to End-User upon receipt of written notice (which may be via email) from Autonomy ('Distribution Notice') of such direct license transaction. In the event distribution is accomplished by reason of a Distribution Notice, upon such time as Autonomy has received payment in full for such license fee and support fee, Autonomy shall pay to VAR an amount equal to the license fee paid by End-User to Autonomy less the Licence fee described above…, but in no event more than US$400,000, as full compensation in connection with VAR's efforts in securing End-User's procurement of a license of Autonomy software."*

403. The Claimants submitted that this language was misleading in that (a) (according to them) the DoI had no intention of contracting with anyone to buy the Autonomy software licence and had made (according to the email of 13 December 2010 referred to in paragraph 399 above) a *"final"* and *"strategic"* decision to *"pass"* on the deal; (b) if (hypothetically) the DoI had been going to buy Autonomy software, it would have done so directly from Autonomy and not from MicroTech; and (c) the software included Digital Safe: only Autonomy could implement, manage and service a Digital Safe Archive, and so MicroTech could not offer or provide any value to the transaction.

404. The Claimants further claimed that the language actually misled Deloitte. They relied on Mr Welham's evidence in his witness statement that the true facts would have been relevant to Deloitte's assessment of revenue recognition. The Claimants further claimed that Deloitte was also misled by untrue audit confirmation letters, signed by Mr Steve Truitt, confirming the absence of any side agreement or any continuing managerial involvement. They relied on Mr Steve Truitt's evidence in the US criminal trial (adduced as hearsay in these proceedings) as follows:

> *"Q. All right. With respect to where it says no side letters or other agreements, was that true?*
>
> *A. No, because of, again, the fact that I was no longer worried about somehow getting the money to pay them.*
>
> *Q. And in the bottom here they've added (reading): "We acknowledge that Autonomy Corporation PLC retains no continuing managerial involvement in the delivery of this product or service other than stipulated in the license agreement." Was that true?*
>
> *A. It was not true and to my discredit, I didn't even notice the language at the time. But, no, it was not true. …"*

405. The Claimants also stressed Mr Steve Truitt's further evidence at the same trial as follows:

> *"Q. After you signed this purchase order –*

A. Yeah.

Q. -- did you or, to your knowledge, anyone else associated with MicroTech attempt to sell this software to the Department of the Interior?

A. No.

Q. Did you help Autonomy in its efforts to attempt to sell this software?

A. No.

Q. Did you discuss with Autonomy what would be the terms of sale to the Department of the Interior?

A. We didn't.

Q. I'm sorry?

A. No.

Q. Okay. Did you – did Autonomy run by you terms that it was considering offering to the Department of the Interior or that it had offered to the Department of the Interior?

A. No."

406. As explained below, little was said of VT25 in Dr Lynch's submissions and there was little if any specific evidence suggestive of any participation in or knowledge of it after Mr Hussain's anxious email (see paragraph 400 above); but those submissions advanced the following correctives of what were described as the Claimants' *"tendentious"* criticisms of the transaction:

(1) It was contended that the Claimants were wrong to suggest that DoI had made a final decision such that a licence could not have been sold to them and that in fact the DoI were still considering purchasing a licence. I am not persuaded by the email provided in support of this since it appears from the email that the license concerned was not for restructuring of the DoI's Digital Safe hosting arrangement, but for a smaller deal (still in excess of $2,000,000 though) for an email archiving system. In my view, even if the DoI had not finally closed the door on any deal when writing in December 2010, they had made clear that it was uncertain that they would.

(2) The Defendants contended that the Claimants were also wrong to suggest that Mr Steve Truitt accepted in his evidence in the US criminal trial that the DoI would only ever have bought from Autonomy and not from MicroTech. Dr Lynch contended that the *"whole thrust"* of his evidence was that he was going on risk and intended to make the sales to the end-users with whom he would be establishing relationships. However, I cannot accept that either, at least in the general terms in which it was put. Later in the same transcript of Mr Steve Truitt's evidence, he was asked again about the DoI transaction; and he expressly accepted that that deal *"was Autonomy's to take care of*". He never envisaged negotiating with or concluding an end-user sale to DoI.

407. As it happened, and as was common ground between Dr Lynch and the Claimants[45], Autonomy failed to conclude any deal with DoI. Tellingly, the upshot of there being no end-user deal was not that Autonomy required payment from MicroTech. Rather, it was that on the last business day before the HP Acquisition closed, Mr Chamberlain emailed Ms Helen Ku (an Autonomy revenue manager) stating *"DOI – we need to credit the $4.2m (4 invoices) and invoice direct. Have we not invoiced the DOI directly."* The next day Ms Ku notified Ms Gustafsson and Ms Anderson: *"We will reverse this revenue tmr."* Four credit notes, each dated 30 September 2011, were then issued to MicroTech, writing off the entire amount of MicroTech's debt. The obvious explanation in the circumstances is that this honoured the assurance that had been provided, that one way or another MicroTech would not be left on the hook.

408. As usual, the Defendants relied on the approval of VT25 by Deloitte both as confirming its propriety and as an answer in any event (that is, whether Deloitte were right or wrong) to any suggestion that the Defendants knew that the accounting treatment of the transaction was improper.

409. Deloitte certainly reviewed VT25, including the provision referred to in paragraph 402 above (which they noted in their report was *"common to almost all VAR purchase orders"*). They were satisfied that revenue recognition was satisfactory. They do not, however, appear to have been told or aware that the end-user deal with DoI as originally contemplated was no longer on the cards, and that any surviving prospect of an end-user deal depended on the inherently uncertain outcome of a full procurement exercise.

410. The Claimants relied on Mr Welham's evidence in his witness statement that this *"would have been relevant to Deloitte's assessment of the revenue recognition criteria"* and that *"if it was aware of this, I would have expected Autonomy management to have told us this information"*. His evidence did not, and could not, anticipate what the result would have been; and I take it that in this context he accepted, as in other similar contexts, that the actual response would have depended on a *"whole series of conjectures about what might or might not have happened"* (to adopt the way Mr Miles put a similar issue to Mr Welham, and Mr Welham accepted). Deloitte were also unaware that MicroTech neither intended nor was it expected to negotiate with DoI, and it was not in its contemplation to on-sell to DoI.

411. In those circumstances, the fact of Deloitte's approval cannot assist the Defendants; on the contrary, the fact that they were misled in the ways indicated tells against them, particularly as regards the state of mind of anyone responsible for their instruction as to the characteristics of VT25.

412. I have concluded in the circumstances described above that it was wrong for the sale to MicroTech in VT25 to be treated as generating recognised revenue.

Did the Defendants have "guilty knowledge" about VT25?

413. I turn to the second issue, as to whether the Defendants had "guilty knowledge".

[45] There was a footnote in Mr Hussain's submissions which appeared to suggest otherwise; but it seems clear that Dr Lynch and the Claimants were right.

Mr Hussain

414. The Claimants asserted that Mr Hussain must have been aware of VT25 and its accounting treatment *"since it is he who had to approve the recognition of the revenue."* No further evidence was suggested that he knew that its accounting treatment was wrong than is summarised above.

415. I consider that by this time, late December 2010, the Defendants' obsession with meeting and beating revenue forecasts had become so ingrained that it displaced rational analysis of individual cases on the part of Mr Hussain and those concerned within Autonomy. The expedient of resorting to a friendly VAR if an anticipated end-user deal was delayed or likely to be delayed was now tried, tested, and virtually automatic. Mr Hussain had devised the template and would have expected it to be followed with such alteration as ensured revenue recognition in the quarter for which it had been anticipated, with any appropriate arrangements to be made to rescue and recompense the VAR if the deal went direct or did not eventuate.

416. The credit notes were issued on 30 September 2011. The Claimants contended that the scale on which Autonomy *"cleaned up unpaid debts"* during the *"Dark Period"* was so extraordinary that:

> *"it is inconceivable that Mr Hussain was not involved (as Ms Harris agreed she would have expected, and as Mr Scott's evidence of Mr Hussain's desire to make the VARs whole also implies)".*

417. I would accept the likelihood that Mr Hussain was involved, and that the person in direct control of the operation, Mr Chamberlain, was directed by Mr Hussain. I consider later, in the context of an analysis of write-offs in the *"Dark Period",* whether that in turn is further evidence of *"guilty knowledge"*.

Dr Lynch

418. Dr Lynch denied any involvement in the transaction. The Claimants did not allege that Dr Lynch had any specific knowledge of or involvement in VT25 (beyond the email from Mr Hussain mentioned above before any VAR deal, when a direct deal seemed on the cards). However, they invited me to infer that:

> *"Mr Hussain was acting within the scope of a broad authorisation from Dr Lynch to call upon friendly VARs as and when required to plug gaps in revenue."*

419. Further, and with reference to the release of MicroTech's liability after no end-user deal could be secured, they added that it was not:

> *"...plausible that write-offs and credit notes on such scale could have taken place without the agreement of Dr Lynch – whose authority, it will be recalled, was required for all purchases over $30,000."*

420. There was nothing else in the Claimants' Closing Submissions about this, and there was a dispute as to whether Dr Lynch had been cross-examined relevantly about the transaction. If by this it is meant that he was not asked questions about the transaction prior to the issue of credit notes, I think that the Defendants are right that any challenge to him about the specifics of VT25 was perfunctory. But the Claimants' real points, as summarised above, went to (a) the general issue as to whether Dr Lynch was aware of the overall use of VARs and his approval of it and (b) the more particular issue as to the issue of credit notes in the *"Dark Period"* to extract MicroTech from any exposure.

421. The Defendants dealt brusquely with the latter (the issue of credit notes), submitting that *"this was a post-transaction event, which could not have affected the original recognition of revenue."* They submitted further that:

> *"In circumstances where the end-user had chosen to deal directly with Autonomy so that Autonomy received payment for the software from the end-user it was a sensible business decision to cancel the reseller deal. The alternative would have been to leave the reseller on the hook despite Autonomy having taken the customer opportunity. That would have been damaging to the relationship."*

422. Those submissions are readily understandable but (at least in the context of VT25) ignore three important points. First, I agree with the Claimants that events post-transaction may (though they may not) reflect and expose the anterior intentions of Autonomy at the time of the VAR transaction. Secondly, in the case of VT25, there was no end-user deal, so the logic offered for cancellation of its exposure is inapplicable. Thirdly, the inapplicability of the logic offered is further confirmed by the fact that in VT25, there was never any question of the end-user electing as between MicroTech and Autonomy: MicroTech was, from its point of view, never involved at all.

423. In summary, I consider that even if Dr Lynch had no or little specific knowledge of VT25 at the time of the VAR transaction, the fact remains that he was well aware of and had approved the strategy of which VT25 was an example. I do not consider that it is likely, or even conceivable, that such a transaction would have been implemented without Dr Lynch's approval.

424. Further, even if (as I think is likely) Dr Lynch was not aware of the specific event of the issue of a credit note, the issue of credit notes and other means of extinguishing VAR liability of which again VT25 provides an example must have been approved by him. I consider later, in the context of an analysis of write-offs in the *"Dark Period",* whether that in turn shows awareness of some impropriety.

VT32 and VT33: MicroTech/Bank of Montreal and Xerox: Q1 2011

425. In March and April 2011, Autonomy had been negotiating with Bank of Montreal and Xerox Corporation ("Xerox") an Autonomy software sale, in the latter case with a view to Xerox on-licensing the software to General Motors Corporation ("GM").

426. In the case of the Bank of Montreal, the deal appeared to have been given the *"Green light"* (as Mr Sass informed Mr Hussain by email dated 23 March 2011, circulated to Mr Egan, to which Mr Hussain immediately replied *"yeehah"*). However, on 30 March 2011,

as the end of the quarter fast approached, the Bank of Montreal's representative (Ms Joanne Lafreniere) informed Mr Patrick Ryan (in Sales) at Autonomy that she had *"found out that the size of this contract with [sic] require the signature of our Group Head. We will not be able to get this done by eod tomorrow."* Although Mr Ryan sought to press by threatening in his email in reply that the *"deal dies tomorrow – and will cost BMO millions. No questions asked"*, Bank of Montreal was not to be moved away from its prescribed processes. When, on the evening of 31 March 2011, Mr Sass sent Mr Egan, Ms Eagan and Mr Hussain a status update on the transactions he was trying to close, he stated as regards Bank of Montreal *"not today"*. That same day, Mr Hussain sent Dr Lynch a blank email headed *"flagging a problem at Bank of Montreal – 3m – sass on his way there now."*

427. Similarly, Autonomy was not able to conclude a transaction with Xerox by the end of the quarter (Q1 2011). The reason given by Xerox, according to an email from Mr Sass to Mr Hussain and Mr Egan dated 28 March 2011 recounting a telephone conversation with Xerox, was that it could not approve the deal at that time, because of a spending freeze imposed in consequence of an earthquake in Japan, but that the freeze would not stop the deal and Xerox remained eager and expected closing to happen in early Q2.

428. On 31 March 2011, Mr Scott sent the following purchase orders to Steve Truitt, who duly (and it seems automatically) issued them on MicroTech's behalf:

(1) One for end-user Bank of Montreal, with a licence fee of $2.88 million plus $144,000 for annual maintenance and $50,000 for annual premium support (VT32); and

(2) One for end-user Xerox, with a licence fee of $1.17 million, plus $58,500 support and maintenance (VT33).

429. Both purchase orders were issued under the June 2006 MicroTech VAR agreement, summarised at paragraph 214 above.

VT32: MicroTech/Bank of Montreal

430. Mr Steve Truitt's evidence in his MicroTech deposition (admitted as hearsay in these proceedings) was that (a) prior to issuing the purchase order he did not contact Bank of Montreal to establish the prospects of a deal being concluded; (b) MicroTech did not refer Bank of Montreal to Autonomy; (c) MicroTech did nothing after submitting the purchase order to try to sell the software to Bank of Montreal and (d) MicroTech did not control pricing or any of the terms of the Bank of Montreal deal.

431. MicroTech provided written confirmations to Deloitte on 19 April, 12 July and 14 July 2011 that the invoices listed in the confirmations relating to the Bank of Montreal deal were proper and due, that there were no "*side letters or other agreements*", and that Autonomy retained no continuing managerial involvement.

432. A direct deal was concluded between Autonomy and Bank of Montreal in June 2011 for a licence fee of $2.8 million.

433. In August 2011, Autonomy issued credit notes to MicroTech in respect of the amounts owing under the March 2011 purchase order. The Claimants drew particular attention to

the fact that on 16 August 2011, Mr Steve Truitt emailed Mr Scott, subject "*Bank of Montreal*", stating, "*Just got three credit memos from Chris Chu for Bank of Montreal Invoices. What is the back story on those? Thanks*". The Claimants submitted that it was surely remarkable that Mr Steve Truitt should receive a credit from Autonomy worth $3 million and not even know why this had happened. Mr Scott asked Mr Chamberlain, who explained, "*We had to bill direct as the BMO deal closed directly. Deal credited from MT's books*". Mr Scott forwarded Mr Chamberlain's explanation to Mr Steve Truitt.

434. The Claimants further submitted that Mr Chamberlain would not have credited these sums back to MicroTech without, at least, the authorisation of Mr Hussain; and that the decision to credit these amounts demonstrates that MicroTech's role was to act as a placeholder, and remain entirely disengaged while Autonomy proceeded to negotiate an end-user deal.

435. As always, the Defendants sought to rely on Deloitte's approval. Deloitte had reviewed VT32 and approved the decision to recognise revenue in respect of it in the amount of the purchase price. However, the Claimants' case, based on Mr Welham's evidence at the US criminal trial, was that he did not see the direct agreement between Autonomy and Bank of Montreal until he gave his evidence in chief, and that when they undertook their review Deloitte were not aware of the direct deal. He said in his witness statement in these proceedings that Deloitte:

> *"routinely requested that Autonomy provide us with all copies of licence agreements over $100,000 and…we had made clear to Autonomy management our concerns about VAR transactions being replaced by direct agreements with the end-user".*

436. The Claimants submitted that in those circumstances Autonomy's management were required but failed to bring these matters to Deloitte's attention during their Q2 2011 review, and that this can only have been a

> *"deliberate attempt to circumvent Deloitte's earlier warnings about the serious consequences for Autonomy's revenue recognition practices if further VAR agreements were replaced by direct deals."*

437. However, according to the Defendants:

(1) The direct deal was not a revenue deal because no additional revenue was being booked (it had been booked in respect of the VAR deal).

(2) Although Deloitte had separately expressed an interest in knowing about earlier VAR deals being "cancelled" or credited following a deal going direct, Autonomy would not normally do this unless and until it had been paid for the direct deal.

(3) Deloitte were in fact made aware of the deal later in 2011, as Mr Welham had to accept under cross-examination when confronted with documentary evidence to that effect.

438. I consider the Defendants' attempts to justify not having disclosed the full relevant facts to Deloitte at the proper time to be far from satisfactory:

(1) Deloitte had made clear its concerns about VAR transactions being replaced by direct agreements with the end-user after observing the Kraft (VT3), ManuLife (VT7) and Morgan Stanley (VT8) deals discussed earlier in this judgment (see paragraph 2180 in the main body of the judgment). They had explained on the basis that such direct deals called into question whether it had been appropriate to recognise revenue at the point of the original VAR transaction.

(2) Deloitte had given express warning to the same effect in their report to the Audit Committee for the H1 2010 review. Autonomy had acknowledged this and assured Deloitte that those deals were exceptional.

(3) Deloitte had made clear how important this was in their Q3 2010 report to the Audit Committee noting that (so they understood) there had been no further reversals of transactions with VARs in the form of direct deals.

(4) The Defendants knew full well that Deloitte would have expected to be informed of any direct deals. The submission that the direct deal following VT32 was not reported because it was not a revenue deal since no additional revenue was being booked as it had been booked in respect of the VAR deal is nonsense.

(5) For the same reason the second point made by the Defendants is likewise nonsense.

(6) According to Mr Welham, whose evidence I accept, Deloitte were not made aware of the direct deal until October 2011, long after Deloitte's Q2 2011 review, and far too late.

(7) The Defendants' resort to reliance on Deloitte was misplaced: their conduct in failing to keep them properly informed is further confirmation of their awareness that if they had been so they would not have approved the recognition of revenue in respect of VT32.

Summary assessment

439. In summary, in my judgment, the 'sale' to MicroTech in VT32 had no substance, the only real sale being the direct sale to the end-users which Autonomy failed to advise Deloitte until far too late to make a difference to the way it was shown in Autonomy's accounts.

440. Mr Hussain's involvement and knowledge is clear. Dr Lynch's knowledge is, in my judgment, to be inferred from the 'pattern', from the unlikelihood that such a transaction would have been implemented without his knowledge and approval, and from the various factors I have identified in paragraphs 98 to 103 in the main body of the judgment as characteristic of the way he and Mr Hussain interacted and the business was run.

VT33: MicroTech/Xerox

441. After the issue by MicroTech of purchase order VT33, Autonomy continued to negotiate with Xerox, without any involvement by MicroTech. Thus, on 12 April 2011, in an email to Mr Hussain and Dr Lynch (among others), Mr Sass said that, as well as expecting

closure on Bank of Montreal that month, he (Mr Sass) was also "*pushing for GM as well*". Mr Steve Truitt confirmed during his deposition that MicroTech made no effort to achieve a sale to Xerox. It is plain that it was not expecting and not intending to do so: negotiations with, and any sale to, an end-user were left entirely to Autonomy

442. Nevertheless, MicroTech provided written confirmations to Deloitte on 19 April, 12 July and 14 July 2011 that the invoices listed in the confirmations were proper and due, that there were no "*side letters or other agreements*", and that Autonomy retained no continuing managerial involvement.

443. The negotiations were not concluded as rapidly as had been hoped. In the process, there was an episode during June 2011 when, in the course of Autonomy's ongoing negotiations with Xerox, Autonomy gratuitously inserted a reference to DiscoverEngine into the draft Xerox/GM contract, resulting in the need for Mr Avila to devise an explanation as to how that software would benefit GM. Although Autonomy had been hopeful of concluding a deal in Q2 2011, Mr Sass informed Ms Eagan and Mr Egan on 28 June 2011 that "*GM is a concern*".

444. In the event, it was not until 29 July 2011 that an Autonomy group company, Verity Inc, entered into a direct sale agreement with Xerox, for an amount of $1.3 million in respect of the licence fee plus support and maintenance, as well as a $14,175 fee for a Spanish module.

445. The direct agreement provided for Xerox to make payment, at Autonomy's express direction, to Autonomy's designated payee. On 1 August 2011, Ms Mickie Lee (an Autonomy lawyer) informed Xerox that MicroTech would be invoicing Xerox for the amount due. She explained that "*MicroTech is a minority and small business vendor*" (which suggests that Xerox had never heard of MicroTech). On 4 August 2011, Ms Lee sent a formal letter to Xerox in which Autonomy designated MicroTech as its payee. Ms Lee's covering email was copied to Mr Chamberlain.

446. On 26 October 2011, MicroTech paid Autonomy $475,572 and, on 23 May 2012, MicroTech paid $752,928, for a total of $1,228,500.

447. These payments were less than the sum payable by Xerox to MicroTech at Autonomy's direction. The difference was $85,675, which MicroTech retained. In addition to their reliance on VT33 in the context of their FSMA claims, the Claimants seek recovery of that amount as damages due to ASL or alternatively Verity Inc for the Defendants' breach of duty.

448. Deloitte again approved the accounting treatment of VT33, permitting revenue from it to be recognised as at the date of the VAR deal, and thus within the relevant quarter. Once more the Defendants placed reliance on this for the reasons explained above, and also on the fact that Deloitte had expressly considered and approved the provision for payment to a "*designated payee"* of which use was made in this context. However, Deloitte's approval of revenue recognition in respect of VT33 was based on the same mis-presentation as in the case of VT32 (see above). The only substantive difference was the utilisation of the "*designated payee"* mechanism.

449. My conclusion that the sale to MicroTech in VT33 had no substance and that the only real sale was that eventually negotiated and contracted with the end-user, Xerox, is based on

substantially the same considerations as my conclusion in respect of VT32. The same conclusion also follows that the recognition of revenue from the sale to the VAR was wrong, and would have been recognised as wrong by Deloitte had they been kept fully and timeously informed. The *"designated payee"* provisions, reminiscent of the early VAR deals in 2009, do not affect the substance of the VAR sale (or rather, the lack of it) and make no difference to my assessment.

Defendants' knowledge of and participation in VT32 and VT33 and direct deals

450. My conclusions about the Defendants' "guilty knowledge" likewise mirror my previous conclusions in the context of VT32.

Mr Hussain

451. It seems plain from email exchanges that Mr Hussain knew and approved the resort to a VAR transaction and the subsequent direct transaction in each case. It also seems more likely than not that he was aware that in neither case was the VAR expecting or intended to be involved in the negotiations that resulted in the respective direct deals.

452. It was not expressly alleged, but I take it to be implicitly suggested, that as part of the Autonomy management Mr Hussain was responsible for the alleged deliberate attempt to *"circumvent"* Deloitte's warnings in respect of direct deals by not revealing the fact of the direct deal between Autonomy and Bank of Montreal.

453. Further, the Claimants alleged that the arrangements for and the direction to Xerox to pay MicroTech as Autonomy's designated payee *"had no doubt been approved by Mr Hussain as well."*

454. In my judgment, Mr Hussain plainly had "guilty knowledge" that the accounting treatment of VT33 was improper.

Dr Lynch

455. The Claimants also submitted that the court should infer that these transactions *"fell within the broad approval granted by Dr Lynch to Mr Hussain to call upon a friendly VAR as and when required to plug gaps in revenue."*

456. Beyond that, however, the Claimants made no further particularised allegation of knowledge against Dr Lynch in respect of either VT32 or VT33, and they did not cross-examine him about them (or the direct deals) either.

457. Nevertheless, and once again for substantially the same reasons as I have given and referred to in the context of VT32, I have concluded that the sale to the VAR (MicroTech) and its accounting treatment would not have been proposed and implemented but for Dr Lynch's approval of the strategy pursuant to which they were so and the need to book revenue of which he was aware.

458. If he had no specific knowledge of the actual transaction and its accounting treatment, that would only have been because by now the pattern was well established and the implementation of VAR sales pursuant to it as and when Mr Hussain identified the urgent need to cover a shortfall had become all but automatic.

459. I am satisfied therefore that Dr Lynch too had "guilty knowledge" of the improper accounting treatment of VT33.

VT37: MicroTech/HP Q2 2011

460. In chronological terms, this June 2011 sale was the last of the impugned VAR transactions. It was a large sale for a fee of $7 million with an additional $350,000 for a single year's maintenance, and by June 2011 Mr Hussain was relying on it to achieve revenue forecasts. This can be seen, for example, from an email from Mr Hussain to Mr Egan on 7 June 2011:

> *"Stouffer – assume you are on your way to St Louis but where is the HP proposal?...If we don't close HP then we are *****d…"*

461. VT37 is complicated by the fact that the ultimate end-user was one of HP's existing clients, which Autonomy was seeking to persuade to adopt Digital Safe for its archiving needs instead of HP's own product (with which it was not happy). Autonomy pursued a dual-track strategy to this end, seeking either (i) to sell Digital Safe to HP for it to use to provide archiving services to its client, the United States Postal Service ("USPS") or (ii) to sell Digital Safe direct to USPS itself. In the end, no end-user deal involving either MicroTech or Autonomy eventuated before HP's acquisition of Autonomy, and it appears that after that acquisition, HP, which by then owned and/or controlled the Autonomy software, stepped in to do a direct deal itself.

462. The transaction is further complicated by the Claimants' associated allegations relating to Autonomy's purchase from MicroTech of the Federal Cloud platform for $8.2 million in Q3 2011: those allegations being to the effect that there was no commercial rationale for the Federal Cloud purchase and that it was executed solely to put MicroTech in funds to meet existing liabilities to Autonomy, including its liability (according to contract) under VT37. It is necessary for an understanding of its evolution and the ultimate failure to close an end-user deal to describe the background of the transaction.

463. Prior to Q2 2011, HP was the appointed technology provider to USPS which also used HP's software (an archiving offering called RISS) for archiving. Dr Lynch explained in his witness statement (and this was not challenged) that:

> *"HP's archiving offering was called RISS [which] was an earlier version of Digital Safe and was extremely outdated. In early 2011, USPS was involved in a number of lawsuits and needed a functional archive system and EDD system to preserve and review relevant data. Due to its track record, USPS was not convinced HP's offerings would be up to the task of helping USPS prepare for litigation. In Q2 2011, USPS abandoned its existing EDD solution and moved to Autonomy's software. Autonomy closed a multi-million-pound EDD deal with USPS in the quarter. It was my understanding that USPS also considered moving away from HP's archiving offering and considered Autonomy a frontrunner for the replacement. There were two possible ways that Autonomy could structure the deal. Either Autonomy could have sold archiving software*

> *to USPS directly or to HP who would use Autonomy software to improve its offering to USPS. Autonomy pursued both possible deals."*[46]

464. Dr Lynch's evidence in cross-examination was that (a) Autonomy had already recently done a good deal with USPS for e-Discovery which was working well (b) Autonomy were being told by USPS that *"they'd said yes already"* (c) USPS were exasperated with HP's archiving product *"that had failed and was losing things. And so there was big legal liability because the archive wasn't archiving"*; so that (d) according to him, a deal with USPS looked like a good prospect, the only problem being that HP (Mr Veghte) was *"giving us a bit of a run-around"*.

465. Mr Egan, on whose witness statement the Claimants principally relied in this context, explained the position as follows:

> *"As the end of the quarter approached, we were making good progress on the direct Postal Service deal, but not much progress on the HP side. Mr. Hussain asked me to take an HP deal to a reseller. I spoke to either David or Steve Truitt and asked that MicroTech take an HP deal. I explained the greater risk that MicroTech would be taking with respect to this deal because of the uncertainty of the end-user deals. I identified the paths that were available to get MicroTech paid. I said that we might be able to complete a sale to HP (but the prospects of such a sale were not in good shape at that time but that we would keep trying that route). Alternatively, we might be able to license the same software directly to HP's end customers like the Postal Service who had shown they were interested and needed the software as an alternative. In all events, I said we would use all efforts and means available to protect MicroTech from holding the bag."*

466. Apart from Dr Lynch's Counsel suggesting to Mr Egan (as he accepted) that it was more likely he spoke to Mr David Truitt (who the Defendants emphasised was not a MicroTech decision-maker) than Mr Steve Truitt, Mr Egan's evidence in this respect was not challenged in cross-examination.

467. Accordingly, I accept that (a) it was Mr Hussain who suggested to Mr Egan that a sale to a VAR should be arranged in light of difficulties or delays in closing a deal within the quarter with either USPS or HP; (b) Mr Egan made clear to MicroTech that there was more than usual risk that an end-user deal would not be achieved; and (c) Autonomy would *"use all efforts and means available to protect MicroTech from holding the bag"* (though Dr Lynch reminded me when he was cross-examined on the paragraph that *"the*

[46] Dr Lynch explained in cross-examination that USPS were unhappy with HP because the HP product for archiving *"had failed and was losing things. And so there was a big legal liability because the archive wasn't archiving. So USPS had basically told us that they were going to switch over to Autonomy which made sense because they'd just switched over the eDiscovery, and then they wanted us to work through HP who were their technology provider just like Dell was for Hyatt."*

contracts that they signed made it clear that they could only rely on what was in the contract and that did not put an obligation on Autonomy to do any such thing").

468. Nevertheless, MicroTech agreed to take the VAR deal without any prior assessment of the prospect of an end-user deal or of the risks to MicroTech. On 30 June 2011, Autonomy prepared, and Mr Steve Truitt signed, a purchase order that included a licence fee of $7 million, plus $350,000 for one year's maintenance. Autonomy recognised licence revenue of $7 million that same day.

469. The VT37 purchase order was governed, as usual in the case of MicroTech VAR deals, by the terms of the June 2006 MicroTech VAR agreement (see paragraph 216 above for a summary of its terms) which provided expressly that MicroTech was obliged to pay Autonomy for its orders irrespective of its sale to an end-user, and which confirmed that there was no other understanding or arrangement between the parties. The VT37 purchase order also incorporated the provision, noticed previously in other later MicroTech transactions, permitting a direct deal, but stating that the parties *"currently anticipate"* an onward licence transaction between MicroTech and HP.

470. This was not true: an onward sale by MicroTech was never in the contemplation of either MicroTech or Autonomy. In Dr Lynch's written closing submissions, it was argued that a sale of Autonomy software was still a good prospect because *"[t]he main question was not whether Autonomy software would be used but whether the deal would be done through HP as the continuing archive provider".* The thrust of the Claimants' case was that the only real prospect was of a direct deal between Autonomy and USPS, but that was uncertain given HP's interest and Mr Veghte's obvious wish to retain USPS for HP.

471. In any event, MicroTech was not in the frame at all. There was no real reason to suppose that HP would have entertained a sale from them. Mr Steve Truitt accepted in his deposition in the MicroTech proceedings in the US that it was *"a weak expectation at best"*. The Claimants described that as *"if anything, an overstatement"*, especially since the licence was for the use of Digital Safe software and MicroTech had never installed[47], nor could it have installed, Digital Safe. It seems to me that the reality was, and I find, that the prospect of an end-user deal between MicroTech and USPS was vanishingly small.

472. In an effort to explain how MicroTech could rationally have signed the purchase order and taken on the risk unless assured that Autonomy would see to it that the risk would, one way or another, be covered by Autonomy, Dr Lynch asserted that:

> *"the one thing we haven't mentioned is that they had the right to sell that software to any other party as well. So it wasn't – although we're talking about this as though it's an HP/USPS deal, they had the right to sell that software to anyone."*

473. But he was mistaken. The purchase order named HP as the "*End-user*" (item 1) and stated (item 3) that HP was licensed to deploy three separate instances of Digital Safe, with each instance to be used "*solely for the purposes of hosting and archiving data from a single Client's Internal environment for access solely by such Client. A "Client" is an end-user customer of End-User*". Thus, HP could use the software for up to three of HP's own customers. However, MicroTech was not free to sublicense the software to anyone other

[47] As Mr Steve Truitt acknowledged in his deposition in the MicroTech proceedings in the US.

than HP. When confronted with the terms of the purchase order, Dr Lynch said he was "*surprised*" and said he would "*have to go away and find out more as to why I have a different understanding*". No further explanation was subsequently provided.

474. The Claimants added to this what I can compendiously describe (meaning no underestimation of them) as the usual points in respect of these later impugned VAR transactions with MicroTech, to the effect that MicroTech never had or even attempted any contact with either HP or USPS, and it was never envisaged by either party to VT37 that they should.

475. I need note only in this regard that on this occasion, Dr Lynch sought to contradict this, in that in the course of his cross-examination he stated his understanding to be that MicroTech, as a federal reseller, had *"their own federal relationship"* and did know *"some people in HP Federal and they had communications with them".* When further pressed, he named a Ms Amy Santucci and a Mr Tom Hempfield (both of whom worked at HP) as being those *"people".* He also referred very generally to *"quite a few emails"* with Ms Santucci (which so far as referred to related to a contact between HP and Autonomy but not with MicroTech).

476. Dr Lynch's evidence in cross-examination on the point was uncharacteristically vague and meandering, and he named no person at MicroTech involved in, nor any instance of involvement on the part of MicroTech in, negotiations of any kind with either HP or USPS. Eventually, after a particularly long and discursive answer by Dr Lynch, Mr Rabinowitz pressed him to identify who at MicroTech he said had been involved; he could not do so, and simply repeated the names of persons working for HP whom he thought might be known to MicroTech, before trying to deflect the question away by saying *"But the whole thing was just a disaster."* Even when confronted with the suggestion that his evidence was *"completely made up"* Dr Lynch could do little more than fall back on naming again Ms Santucci, and then revert to another discursive explanation of the complications at the time.

477. I cannot accept Dr Lynch's evidence that MicroTech was involved in any dealings or negotiations in the matter. It was unpersuasive in itself, and there was no other basis for it. I accept Mr Steve Truitt's own evidence in his deposition in the MicroTech proceedings that MicroTech made no approach or seek to sell the software to either HP or USPS. Accordingly, I take VT37 to provide another illustration that the VAR sale did not interrupt or impact Autonomy's negotiations with the end-user, nor the likelihood (or not) of a sale by Autonomy to the end-user eventuating. MicroTech simply signed the purchase order and then stepped back, as was the intention and expectation of both Autonomy and MicroTech.

478. Autonomy resumed its efforts in pursuit of its dual track strategy, with Dr Lynch's personal involvement. But these did not result in Autonomy reaching a deal with either HP or USPS. In his witness statement, Dr Lynch stated that MicroTech *"was not able to sell the software on to HP or USPS"* . When cross-examined on this, he tried to defend this as simply a statement of fact; but I consider that it was plainly intended to give the impression that MicroTech was involved and was intended to pursue and become the contracting party to any ultimate deal, which it was not, and (at least by the time of his witness statement) he knew it. (His contemporaneous knowledge is addressed later.)

479. As it was, email exchanges between Dr Lynch and Mr Veghte at the end of June 2011 seem to me to suggest that, though they also suggest that the process was complicated by the fact that HP felt restricted in its dealings with USPS in light of the danger of any breach of confidentiality about the proposal for HP to acquire Autonomy then under discussion, HP quite deliberately used this as the reason for (in effect) cutting Autonomy out of discussions with USPS. Thus, on 30 June 2011 Mr Veghte stated in an email to Dr Lynch:

> *"Circled with the HP team on the ground and we received instructions from USPS Procurement not to discuss the USPS environment with you directly and while this may be inconsistent with other communications from USPS, we do need to honour that request. In addition, USPS is raising awkward questions to our account team as to whether and what relationship HP and Autonomy may have or be developing and I think it is in our collective best interests to limit that speculation as I am sure you would agree.*
>
> *In consideration of this and other factors, HP believes it best if we proceed separately with respect to USPS…"*[48]

480. The question which then arose, however, was as to how, given that there was no end-user sale to generate funds, MicroTech was to be saved from its contractual payment obligations. The problem was both more pressing and more difficult because, as at 5 July 2011, MicroTech owed Autonomy in excess of $25,000,000, of which $10,300,000 was already overdue at 30 June 2011, as set out in a spreadsheet attached to an email of that date from Mr Chamberlain to Mr Egan, copying Mr Hussain and Mr Scott.

481. As Mr Steve Truitt put it in his deposition in the MicroTech proceedings, *"We needed a fix for all of it"*. He went on to confirm that Mr David Truitt asked him to develop a proposal as the path to resolving at least part of their outstanding obligations. In that deposition, he was asked whether Mr David Truitt had suggested a proposal relating to a Federal Cloud platform as part of a fix. He said:

> *"… don't recall it being a cloud solution, but, yes, he asked me to put together a proposal. I don't think it's important, though, that it's - whether it's cloud or not, but, yes, he did."*

Federal cloud purchase and the payment by MicroTech it enabled

482. The Claimants' case is that the proposal developed as the means of getting funds to MicroTech was the purchase by Autonomy from MicroTech in Q3 2011 of the *Federal Cloud* platform briefly mentioned above for a purchase price of $8,200,000. The Claimants alleged that there was no commercial rationale for this transaction, and it was

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[48] It is difficult not to sympathise with Dr Lynch's complaint that Mr Veghte *"was giving us a bit of a run-around"*, with HP trying to keep its client to itself, whilst improving its product by incorporating instead Autonomy software, in which HP ultimately succeeded (see above at paragraph 464).

executed solely to put MicroTech in funds to meet existing liabilities to Autonomy: it was the *"fix"* which MicroTech needed.

483. The Federal Cloud purchase is one of the six Reciprocal VAR transactions listed (as *MicroTech/HP*) in Schedule 12B to the RRAPoC. It is relied on by the Claimants as having been undertaken solely to put MicroTech in funds to meet contractual liabilities to Autonomy under impugned VAR sales. The Claimants relied on the Federal Cloud purchase both as exemplifying the variety of ways in which Autonomy contrived to ensure that VARs party to impugned VAR transactions were not *"left on the hook"*, and also as giving rise to transactional loss (which the Claimants seek to recover).

484. I have set out in greater detail in another part of this judgment the factual history and the respective positions of the parties in respect of transactions said by the Claimants to have been devised in order to fund on a 'friendly' VAR to enable it to appear to meet its contractual obligations under VAR contracts with Autonomy. That includes the six Reciprocal VAR transactions listed in Schedule 12B in respect of which the Claimants seek recovery of transactional losses, including the Federal Cloud transaction.

485. The following matters stand out, in my view, from the Claimants' submissions in respect of the Federal Cloud transaction in relation to the question now in issue:

(1) The impetus for the transaction initially came from Mr David Truitt and Mr Hussain. An email dated 28 July 2011 from Mr Hussain to Dr Menell and Mr Egan headed *"SSA contract"* introduced the matter by stating *"…as you both know we have a very large $24m plus deal with SSA via Microlink"* and went on to relate a conversation between Mr Hussain and Mr David Truitt about a proposal for Autonomy to purchase from MicroTech certain *"software and data facilities"* which Mr Hussain stated he believed would *"help us deliver our very large project"*. The project was in fact a contract between MicroLink and the US Social Security Administration ("SSA") for the provision of on-site (not cloud) information and e-Discovery solution.[49]

(2) No evidence was adduced suggesting that anyone in Autonomy's technical department had suggested a need for further software for the purpose of the project. The timing, the genesis of the proposal through Mr Hussain, and the lack of anything supporting technical need support the suggestion that the focus was not on the product but on a "fix".

(3) It is apparent from email evidence and the evidence of Mr Steve Truitt in his deposition in the US MicroTech proceedings that there was considerable but unexplained urgency attached to the preparation of the proposal.

(4) On 31 July 2011, Mr Steve Truitt sent Mr David Truitt and Mr Jimenez a draft "*Autonomy proposal*". On 1 August 2011, Steve Truitt sent the proposal to Mr Hussain, describing it in his covering email as a "*proposal from MicroTech to*

[49] The "*SSA*" is a US government agency. The "*SSA contract*" was a contract between MicroLink (by then an Autonomy subsidiary) and SSA for the provision of an email archiving/e-Discovery/email records management system, pursuant to a Blanket Purchase Agreement dated May 2011. As stated in an internal Autonomy email dated 20 May 2011, the scope of the project was that "*SSA plans to deploy an onsite end-to-end Information Governance and eDiscovery solution …*".

develop FISMA compliant hardware stacks and operational approaches to deliver Autonomy software solutions to US Federal clients from a cloud computing model". The attached proposal, which ran to 7 pages, was for Autonomy's software to be configured to support the requirements of the SSA for email archiving and, given the potential growth of archived data, "*the SSA could very easily decide that it makes sense to move both its email infrastructure and its email archiving to the cloud. Should that occur, MicroTech stands ready to assist Autonomy with the move to help maintain and enhance its relationship with a key Federal customer*".[50]

(5) However, and as the wording reflected on close reading, there was no reason to think that SSA was going to move this particular project to the cloud: Autonomy's brief was to create an onsite solution, not one based in the cloud. Further, Mr Kalbag's evidence was that a federal cloud platform was never discussed or even mentioned in his discussions with SSA, that SSA was an "*on premise*" customer with its own data centre, due to security concerns, and that so far as he was aware a federal cloud platform would have been of no interest to SSA. Apart from putting to him the general Cloud First policy of the US federal government, none of that evidence from Mr Kalbag was challenged in cross-examination. No document has been identified prior to August 2011 in which SSA expressed any interest in changing its archiving system from an on-premise arrangement to a cloud-based one.

(6) $8.2 million was what Mr David Truitt had told Mr Steve Truitt should be the purchase price: Mr Steve Truitt confirmed this and testified that he started with the end price and then worked backwards to identify the amounts of equipment and labour that would support such a price.

(7) The contractual terms were vague and unspecific, lacking any technical detail, and more in the style of a proposal than a serious commitment. Further:

(a) There was no defined deadline for the provision of the end-product. Indeed, Mr Steve Truitt's evidence was that Autonomy never asked MicroTech when delivery would take place; and there is no evidence to the contrary.

(b) Although the contractual documentation provided for services to be provided according to a "*schedule as mutually agreed by the parties*", no such schedule was ever proposed or agreed.

(c) The contract did require MicroTech to "*periodically document its efforts by furnishing written progress reports as request by Autonomy*". However, as Mr Steve Truitt testified, MicroTech never submitted any written progress reports, and was never asked for

[50] The proposal was for MicroTech (i) to deliver an Autonomy Solution Stack comprising IDOL Server, Zantaz Fetch Module and "other software" to meet the SSA's business requirements for a payment of $8.2 million and (ii) if Autonomy wanted to deploy an Autonomy Solution Stack for a second client, MicroTech would do so for a further payment of $7 million and (iii) an Autonomy Solution Stack for any subsequent Autonomy clients would be $6.2 million for each one. Mr Steve Truitt testified that Mr David Truitt had stipulated that the price should be $8.2 million, and so he had started with the end price and then worked backwards to identify the amounts of equipment and labour that would support such a price.

them. As it was, MicroTech never delivered anything to Autonomy, and Autonomy never requested delivery of anything from MicroTech.

(8) Moreover, although the contract specified that Autonomy had 30 days to pay, Autonomy paid the stipulated purchase price of $8.2 million immediately on the first day. Mr Steve Truitt testified that this was *"so that we could then retire some of the debt that we had with them"*.

(9) On 17 August 2011, one day after that payment by Autonomy, and also of course the day before the HP acquisition of Autonomy was announced, MicroTech paid the entire amount of $7.35 million payable under its VAR contract (in respect of VT37), in advance of the actual payment date.

486. The Defendants' answers to this can be summarised as being that:

(1) Autonomy expected SSA soon to need and require cloud-based storage and e-Discovery capability: in December 2010, the US Government had adopted a *"Cloud First"* policy under which Government agencies were obliged to identify three services to move to the cloud within three months, and then to move one within 12 months and two within 18 months.

(2) Under the SSA's blanket purchase agreement with Autonomy (through its MicroLink subsidiary) the contract spend was at the discretion of the SSA and it was structured as a "*call-off*" contract. As a result, MicroLink had to be able to provide the services at all times. The first stage of the project was a pilot which did not require a cloud solution, but given the Government's "cloud first" policy, Autonomy's management anticipated that a cloud solution would offer benefits to the SSA in the future.

(3) MicroTech, a company with which Autonomy had a good relationship, also thought that the SSA might be interested in a federal cloud solution because "*the SSA [were] doing lots of things that would make it hungry for storage*" and "*if we could figure out a way to make it convenient and cheap for them, they might bite at it*". Over the years, Autonomy had received Requests for Proposals from federal bodies requiring FISMA compliance.

(4) MicroTech's proposal "*to deliver Autonomy software solutions to US Federal clients from a cloud computing model*" (sent on 31 July/1 August 2011 – see paragraph 485(4) above) drew on the input of Roger Channing of MicroTech. MicroTech proposed that they would build a security-compliant data centre that could be used by one of Autonomy's customers with unlimited data storage for five years. The solution could be deployed at the customer's facility (where their data would be hosted by either the customer, Autonomy or MicroTech) or a security-compliant facility built by MicroTech (where the customer's data would be hosted by MicroTech). The proposal specifically noted Autonomy's contract with the SSA and highlighted that the business case for a federal cloud platform was supported by the fact that "*the SSA could very easily decide that it makes sense to move both its email infrastructure and its email archiving solution to the cloud*".

(5) There was support for the commercial rationale of a federal cloud solution in testimony at trial: (a) Mr Baiocco explained the interest that Capax also had in the federal cloud business; and (b) Mr Kalbag viewed this as a strong growth area and had generally confirmed that Autonomy did not have FISMA certification and that Autonomy needed to engage with a FISMA-certified third party in order to host data for federal customers. Indeed, Mr Kalbag agreed that it was becoming a must for Autonomy to have the ability to host its software on a FISMA-certified Cloud, and that it was going to be difficult for Autonomy to acquire federal clearance and run a federal cloud platform.[51]

(6) Although Mr Kalbag considered that it would have been more logical and economic for Autonomy to have partnered any of a number of businesses providing cloud storage, rather than to develop its own cloud, that was a commercial judgement: and Mr Kalbag *"was a middle-ranking salesman with no involvement in these kind of judgements"*.

487. The Defendants' case that a Federal Cloud solution was becoming essential was, to my mind, persuasive; and I agree that the choice of how to achieve that was a commercial judgment. Even so, I have not been persuaded that this disposed of the Claimants' case that the Federal Cloud purchase itself, at the time and on the terms it was made, was devised in order to place MicroTech in funds. In particular, in my judgment, the Defendants did not address satisfactorily:

(1) The fact (as for the avoidance of doubt I accept it to be) that the SSA contract itself provided for an on-site and not a cloud solution, and it was a matter of speculation whether the SSA would want a cloud solution in the immediate future;

(2) Mr Kalbag's further evidence in cross-examination that the SSA had expressly been asked whether they would be interested in a cloud offering but

> *"it was made clear to me at that time this had to be an on-site solution because of the sensitivity of the SSA data and they were very protective and were concerned with hosting that data outside of their own data centres…"*

(3) The fact that (a) whereas the Defendants focused on whether a federal cloud platform would be useful generally, under the terms of the proposal the solution offered at the price of $8.2 million was available only for the SSA, with cloud solutions for any other customers to be provided separately and at a significant additional cost; (b) Mr Hussain's suggestion in email correspondence that the proposed cloud solution was needed for the SSA contract was demonstrably wrong; and (c) having regard to Mr Kalbag's evidence described above, the prospect of SSA wanting a federal cloud platform was not illogical or misguided but it was speculative and it was not immediate;

(4) The urgency attached to generating a proposal, establishing a contract of purchase, and accelerating payment to enable MicroTech to pay down its debt

[51] Any idea of using MicroLink would have been hampered by the strict rules in place governing how Autonomy communicated with MicroLink (which were necessary to maintain MicroLink's security clearance).

is difficult to square with an anticipated but so far unexpressed and speculative generalised future need;

(5) Most important of all perhaps, not only was the product so insufficiently specified as to cast doubt on whether it was anything more than a proposal fashioned to give descriptive but not real substance to an idea, the fact is that it was never delivered at all.

488. Taken in the round, I accept the Claimants' contention that the Federal Cloud contract was primarily devised and implemented in order to put MicroTech in a position to pay down indebtedness to Autonomy. There is no evidence that Autonomy needed the goods for the contract with SSA, no evidence that the goods were ever provided, and no evidence that any complaint was ever made in that regard.

489. In my judgment, the context, the urgent genesis and the way the price was calibrated according to what Mr Dave Truitt thought was needed all smack, to my mind, of the "fix" which the Truitt brothers had conceived was necessary; and MicroTech's anticipation of Autonomy's collaboration in such a "fix", together with Autonomy's ready engagement, are, in my judgment, strongly supportive of the Claimants' case that it was well understood and intended that MicroTech would never really be at risk at all in respect of its contractual commitment under VT37.

490. I have concluded that the VAR sale in VT37 exemplified the pattern by then well established, and despite the usual legal trappings, it was not a sale in commercial substance at all. The only distinguishing feature of VT37 tended to embolden the pattern: whilst there was no intention to negotiate or conclude a sale by MicroTech, in this case there was also real doubt whether any end-user transaction would be concluded by Autonomy either, in which case (since MicroTech's legal obligation was either to be funded or forgiven) Autonomy stood to receive no 'new' money at all.

491. In my judgment, the VT37 VAR sale lacked substance and did not satisfy IAS 18.14: its accounting treatment as giving rise to recognised revenue was improper.

Knowledge and participation of Defendants in VT37 and Federal Cloud transaction

Mr Hussain

492. There is no doubt about Mr Hussain's detailed involvement in and knowledge of VT37: Mr Egan's evidence (which was not challenged in this regard and which I accept) was that it was Mr Hussain who asked him to take the deal to a reseller once it became clear that the envisaged deal with HP would not eventuate and HP were showing every sign of wishing to edge Autonomy out of any direct deal with USPS. It is plain from emails that Mr Hussain knew that the *"8a"* VAR chosen was MicroTech.

493. The 'pattern' for Autonomy and not the VAR to negotiate and contract with the end-user was devised by Mr Hussain, and I have seen nothing to suggest any reason for supposing otherwise in this instance. In any event, the overall likelihood is that he was well aware of it; Mr Egan's evidence was that the plain intention was that Autonomy would continue alone its efforts in that regard. The only evidence was of direct engagement between Autonomy and USPS, with no suggestion of any involvement on the part of MicroTech.

I find that Mr Hussain did not intend or expect MicroTech to play any active role in any onward sale.

494. I infer from this, from the pattern and from what actually transpired, that Mr Hussain knew that the introduction of MicroTech was as a placeholder and there was no real substance in the VAR sale. I also infer and hold from this and all the circumstances that Mr Hussain was aware that the prospect of any direct sale was weak, given the demonstration of HP's desire to keep the USPS relationship to itself.

495. Mr Hussain was a trained, experienced and commercially sophisticated accountant. He knew the rules relating to revenue recognition, and that they were required to be satisfied not just on paper but in reality. He knew that the 'sale' to MicroTech was not intended to have any substantive effect as regards Autonomy's efforts to sell the goods or as to the ultimate direct contract which was the objective. He had 'guilty knowledge'.

Dr Lynch

496. Dr Lynch said that he *"had limited involvement in the deal"* (VT37). In Dr Lynch's closing submissions it was stated that *"the Claimants had no basis for suggesting that Dr Lynch was aware of any impropriety or any false account with regard to the MicroTech/HP transaction."*

497. Dr Lynch's evidence was that although the end-user archiving deal did not close with either HP or USPS in Q2 2011 as had been hoped, he and those concerned at Autonomy all thought that (I quote from his first witness statement):

> *"…HP was still interested in Autonomy's archiving software because they had a very angry customer and they needed to provide USPS with a workable software solution. Thus, we were confident USPS would need Autonomy software."*

498. Dr Lynch accepted in cross-examination that he had been emailed by Mr Hussain on 2 July 2011 saying *"We got the edd processing deal and we got the hp digital safe deal via 8a"* and that he knew that a VAR had been used. The subject line of the email was simply *"usps"* which suggests that Mr Hussain thought it safe to assume that Dr Lynch understood the underlying end-user deal sufficiently to be aware of the connection with USPS. His evidence was that he was not involved in negotiating the terms.

499. The Claimants did not suggest to Dr Lynch in cross-examination that he knew the VAR was not at risk, or that the VAR sale was not genuine or improper; or that the revenue was improperly recognised. They did however cross-examine him on his understanding that MicroTech was not to be involved in the sale other than in a nominal capacity. It was put to him that Mr Steve Truitt had made clear that MicroTech had not made any approach to USPS nor any effort to onward sell to either USPS or HP: understandably, he said that he could not comment on what Mr Steve Truitt did or didn't do. But when it was put to him that he would not have expected MicroTech to make any such approach or effort I found his answer that he thought MicroTech had *"their own federal relationship"* (see paragraph 475) above unconvincing. No support for this was provided, nor any evidence found to support any contact between them at all. More generally, in my view, Dr Lynch's answers on the issue of whether MicroTech was intended to play any role did not carry conviction.

500. I have already addressed the uncharacteristically vague and meandering nature of the evidence that Dr Lynch gave in an attempt to support this. Suffice it to say that my impression was that Dr Lynch knew that MicroTech were to do nothing, and Autonomy were to continue negotiating and dealing with the software which USPS wanted and for which Autonomy had notionally sold MicroTech a licence as if that sale had never taken place. Although not a trained accountant, Dr Lynch was an experienced CEO intimately engaged in the direction and presentation to the market of Autonomy's business and well aware of the requirement that to qualify for revenue recognition it was essential that the sale be unconditional and effect a substantive transfer of risk and control. I find that he either knew that the VT37 'sale' to MicroTech in substance and commercial reality effected neither, or was reckless in that regard.

501. In light of my conclusions in paragraph 489 above, I find also that both Defendants were aware that the Federal Cloud purchase was pursued, and pursued with such urgency, because of the need to get MicroTech "off the hook".

DiscoverTech reseller deals

502. I turn to Autonomy's VAR sales to DiscoverTech in the Relevant Period (starting at the end of Q1 2010), other than VT5 (because I have already dealt with that transaction).

503. I have briefly described DiscoverTech in paragraph 1963(4) in the main body of the judgment. It will be recalled that it was established in December 2009 by Mr David Truitt (together with Mr Wharton) initially as a vehicle for the DiscoverPoint business spun out of MicroLink at the time of the MicroLink acquisition.

504. As with the other reseller deals, there was testimony from the main protagonists on both sides of the transactions between Autonomy and DiscoverTech, confirming that DiscoverTech was on risk.

505. Mr Egan's evidence (as described in paragraphs 1976 to 1998 in the main body of the judgment) related to the deals with DiscoverTech as it did to the deals with the other resellers. Mr Egan's evidence confirmed that the reseller was on risk, knew that it was on risk, knew that the reseller agreements were binding, and knew that any words of comfort that Mr Egan could offer were not intended to have any effect on the reseller's obligations to Autonomy.

506. Mr Egan's testimony on these points was corroborated by Mr David Truitt's hearsay testimony given in the US trial against Mr Hussain and in the MicroTech proceedings in the US (as described in paragraph 1999 in the main body of the judgment). In that evidence, he confirmed:

(1) That DiscoverTech was at risk, and would have to pay for the purchase whether or not it sold onto the end-user. DiscoverTech would be stuck with the purchase and the debt; and

(2) That there was never an understanding that DiscoverTech could cancel or otherwise walk away from the deals with no further obligation if the end customer did not purchase the software.

507. With regard to collectability, MicroLink had substantial debts when DiscoverTech was spun off; but MicroLink's debts were not assumed by DiscoverTech. In evidence

introduced by hearsay notice by the Claimants, Mr David Truitt confirmed that he had been paid $39,000,000 when the acquisition of MicroLink happened, and that he could fund the DiscoverTech business to the extent that he wanted to; and Mr Wharton as 20% shareholder could help him.

508. DiscoverTech's reseller transactions were governed by an individual reseller agreement for each deal. The agreements were all in materially the same terms, which included the following:[52]

(1) A provision binding the reseller irrevocably to the purchase, once executed:

> "*this Agreement including all Product Schedules attached hereto, constitutes a non-cancellable purchase commitment, all fees and expenses specified herein are non-refundable*".

(2) A wide entire agreement clause. Clause 6 provided:

> *"Any waiver, amendment, supplementation or other modification or supplementation of any provision of this Agreement shall be effective only if in writing and signed by both parties. If for any reason a court of competent jurisdiction finds any provision or portion of this Agreement to be unenforceable, that provision of this Agreement shall be enforced to the maximum extent permissible so as to effect the intent of the parties, and the remainder of this Agreement shall continue unmodified except as necessary to avoid unfairness. This Agreement, including the pricing set forth in Section 2, represents the entire Agreement between the parties hereto concerning the subject matter hereof and supersedes any and all prior correspondence, quotations and negotiations. VAR expressly agrees that this Agreement shall have priority aver any contrary terms or additional terms contained in any purchase order or other form hereafter delivered by VAR to Autonomy and any such inconsistent or additional terms shall have no effect."*

509. DiscoverTech also executed debtor confirmations in respect of its debts under the various purchase orders issued in respect of its impugned VAR transactions with Autonomy. These confirmed that the debts under the deals were owing, and that there were no side-agreements or side understandings.

510. The Defendants contended that there is no realistic basis for the Claimants' arguments that DiscoverTech was not fully on risk in respect of its purchases, or that the revenue was not properly booked; still less that the Defendants had "guilty knowledge" such as to found a claim under FSMA.

511. As to knowledge, the evidence of Mr Egan and Mr David Truitt was that Dr Lynch was not involved in any of the negotiations between Autonomy and DiscoverTech. Dr Lynch's case is that he was not aware of any of the detail of the underlying transactions between Autonomy and the reseller, nor was he involved in the accounting. He approved a MAF

[52] See, for example, the agreement in respect of the DiscoverTech/Citi deal.

payment to DiscoverTech in respect of just one of the eight deals, but even in respect of that he made clear at the time that he did not know the detail of the situation and needed to ask Mr Hussain about the proposal.

512. Mr Hussain submitted that in relation to the large majority of the VAR deals, the written contract was all that he ever saw, and he was entitled to rely on those contracts. He further submitted that he was never involved in the negotiations and had virtually no other contact with the principals of the VARs, emphasising that Mr Egan gave evidence that he had no recollection and no knowledge of Mr Hussain involving himself in negotiations or speaking to the VARs before deals were closed.

513. The Claimants maintained that both Defendants were well aware of the pattern and the particulars. I return to these issues in the discussion which follows of individual impugned VAR transactions, to which I turn.

514. Of the impugned VAR sales, 8 paired transactions were with DiscoverTech: VT11 (end-user Citigroup Technologies), VT12 (end-user Philip Morris International ("PMI"); VT23 and VT24 (end-user BofA); VT30 (end-user Prisa, a Spanish and Portuguese language media group), VT31 (end-user ThinkTech, Inc as contracting party for the brokerage firm TD Ameritrade), VT35 (end-user Abbott Laboratories, a healthcare company) and VT36 (end-user the Hyatt hotel chain via Dell as reseller).

515. I address below three pairs of transactions: VT11/12, VT30/31 and VT35/36. I have addressed the remaining pair of DiscoverTech impugned VAR transactions (VT23/24) in Part III of this Schedule. The reason for dealing with VT23/24 separately is because they formed part of a complex composite deal with BofA (or its subsidiaries of BofA) and it is convenient to deal with them together with the other transactions (VT16 and VT21, for which the VAR was Capax Discovery) in that composite deal (also in the same Schedule).

VT11: DiscoverTech/Citi Q1 2010

516. Citi was an existing Zantaz/Autonomy client which (according to Mr Goodfellow) had, by 2010, become one of Autonomy's largest accounts. During 2010 Autonomy was seeking to conclude a sale to Citi of archive storage cells (hardware with software embedded). The aim was to increase the capacity in Citi's archive which was at risk of running out of storage capacity.

517. Email exchanges in March 2010 show that Mr Hussain was personally involved, and that negotiations resulted in him putting forward what he described in an email to Mr Otto Chan of Citibank dated 18 March 2010 as *"a really special quarter end offer…of an additional 10% discount…in the spirit of partnership"* which (when that offer was not taken up) Mr Hussain then (by email of 25 March) further offered to improve if the deal was closed before the quarter end.

518. However, Citi did not accept the revised offer on that basis and on 27 March 2010, Mr Robert Mark (a director in Autonomy's Global Accounts department) notified Mr Crumbacher by email, that the deal was *"Dead for the quarter."*

519. In these circumstances, Mr Egan approached Mr David Truitt with a view to a VAR transaction for the end-user deal. According to Mr David Truitt (who it always must be borne in mind was also the CEO of MicroLink, by then a subsidiary of Autonomy) he perceived the deal to be exciting and advantageous to DiscoverTech in that (a) Citi was an existing client of Autonomy and it was hoped that it would lead to sales by

DiscoverTech of software and services to Citi and (b) DiscoverTech stood to earn a substantial margin or fee.

520. On 31 March 2010, DiscoverTech issued the VT11 purchase order for end-user Citi with a licence fee of $5,500,000 plus $275,000 for support and maintenance. The VT11 purchase order was for 62 "instances" of the smart cell software; it was thus confined to software and made no mention of storage cells, which constituted the hardware element of the package that Citi required. In light of DiscoverTech's recent incorporation, its limited assets and the history of MicroLink's indebtedness, Mr Egan asked for and DiscoverTech agreed to pay 20% of the licence fee upfront, funded by way of capital contribution from Mr David Truitt (as to $1,627,000) and Mr and Mrs Wharton (as to $406,000).

521. It is convenient briefly to peer ahead to set the context for the issues of primary focus in relation to VT11, after it became apparent that Citi needed not only the software the subject of VT11 but also storage cells (which DiscoverTech had not purchased and could not provide). Autonomy negotiated a special tripartite agreement, entitled a *"One-Time Reseller Processing Agreement",* entered as of 9 August 2010, to which (through Zantaz) Autonomy was a party, together with Citi and DiscoverTech, for the supply to Citi of the software and hardware which Citi required. This provided:

(1) By clause 1, that Autonomy would deliver Citi's purchase order to DiscoverTech, and that DiscoverTech would process it and facilitate delivery of the applicable products to Citi.

(2) By clause 2, that Citi would pay the applicable fees to Autonomy, but that Autonomy "*shall receive such payment on behalf of Reseller and … Autonomy shall be responsible for payment to Reseller of fees due to Reseller for the processing of the Order of Products as contemplated hereunder*".

(3) Clause 5 nevertheless confirmed that Autonomy "*shall remain responsible for its obligations*" under its Master Services and Software License Agreement with Citi.

522. Autonomy paid DiscoverTech a MAF (in this instance described as a *"Referral Partner commission"*) in the amount of $497,000, which was said in a letter from Mr Kanter to be *"as a result of Referral partner's direct and proximate participation in the account."*

523. Deloitte were aware of VT11 and the VT11 purchase order, and of the subsequent tripartite agreement. They were also aware of the payment of the "*Referral Partner commission*". They did not consider, at the time, that any of this raised any concerns about revenue recognition or other audit concerns, as Mr Welham confirmed in the course of his cross-examination (though he attached the gloss, *"Not for this isolated case, no"*).

524. Three particular issues arise in connection with VT11 which seem to me to merit special focus:

(1) What was the reason for, and significance of, the VT11 purchase order being confined to software when (it is common ground) the end-user also always needed the storage cells constituting the hardware component of what Citi had negotiated to purchase;

(2) What role DiscoverTech played after the VAR transaction was agreed, what the significance was of the special tripartite agreement, and whether Deloitte were misled into thinking that DiscoverTech had tried to make a direct sale to Citi and were only prevented from doing so for administrative reasons;

(3) Whether the payment of a MAF (in this instance described as a *"Referral Partner commission"*) was purportedly justified on a false basis suggesting impropriety.

525. As to (1) in paragraph 524 above, it is common ground that (a) the VT11 purchase order as issued by DiscoverTech on 31 March 2010 was for software only (the software component of the archive storage cells but without the cells themselves) whereas (as previously explained) the deal discussed with Citi included an element of hardware (the storage cells with software embedded).

526. The Claimants' argument was that the ostensible restriction of the purchase order to software was an expedient to enable revenue recognition in Q1 2010: it was necessary because by the time of the purchase order, the hardware element was no longer capable of being delivered within the quarter, whereas software could instantly be delivered electronically; and Autonomy wanted to recognise at least the lion's share of the revenue from a sale to Citi in the quarterly results for Q1 2010.

527. Mr Goodfellow explained this as follows (and his account was not challenged):

> *"I do not recall the events leading up to this conversation specifically but I believe that I received a phone call from Mr Crumbacher that day (31 March 2010) where he asked for the storage cells to be shipped immediately (to DiscoverTech). I would have explained that this was impossible as it required physical delivery of both hardware and software and we did not have the required hardware available to deliver. I confirmed that we could, though, deliver the software almost instantly. I recall that it was Autonomy's focus to deliver a product, whether hardware or software, by the end of the quarter to enable it to recognise revenue. Delivering software was the only means of achieving that."*

528. Following this telephone conversation, Mr Crumbacher sent Mr Egan and Mr Scott a further email, also dated 31 March 2010, in which he stated:

> *"Stouffer, Following up on my voicemail, I just talked to Chris G and understand this is no longer a hardware resale deal but, instead, a software resale. We'll be licensing Discover Tech 62 instances of Zantaz Digital Safe Smart Cell software. ..."*

529. The Claimants contended that all that had changed was the discovery by Mr Crumbacher that Autonomy would be unable to effect delivery of hardware to DiscoverTech that day, precluding revenue recognition for the entire purchase, and that this was what led to the DiscoverTech purchase order being confined to software, delivery of which could be effected instantaneously.

530. Thus, they submitted, the confinement of the DiscoverTech deal to software alone had nothing to do with any commercial reality, nor any specification or preference on the part of the VAR, and everything to do with Autonomy's desire to recognise revenue in Q1 2010.

531. This was put to Dr Lynch in cross-examination. He offered a simpler explanation:

> *"No, it's because DiscoverTech wanted to buy software, it didn't want to buy the hardware.*
>
> *...*
>
> *They had no interest in buying the hardware, from what I understand."*

532. When pressed as to the basis for this understanding, Dr Lynch's response was equally simple:

> *"I've never seen any – anything that leads me to believe that they wanted to buy the hardware.*
>
> *Q. So you have no basis one way or another?*
>
> *A. Well, I do, otherwise I would expect to see something saying that they want to buy hardware. I've never seen that, I think it's a very simple case of a reseller knows that there is software that has to go into a solution for a third party that can be sold to many third parties and does a deal to buy the software part of it. They're not buying the hardware part of it, they don't have to."*
>
> *...*
>
> *Q. Were you aware of this transaction at the time?*
>
> *A. I may have had it on a list, but I wouldn't have had any more involvement than that.*

533. It was then put to Dr Lynch that despite the change in the identity of the product being sold to DiscoverTech, as compared to the combined product offered to Citi, the price in the VT11 purchase order was essentially the same as the price Autonomy proposed to charge Citi for both the software and the hardware. Dr Lynch was taken to the following extract from Mr Goodfellow's second witness statement:

> *"However, I did not appreciate at the time, that the software was licensed under the DiscoverTech VAR Agreement for substantially the same price as the storage cell deal that was being discussed between Autonomy and Citi (which included hardware and software). This struck me as odd when I learned about it as I would have expected the price paid by DiscoverTech for the software alone to be materially less than the price which we had been discussing with Citi for delivery of the storage cells (which included the hardware on which the software was to be loaded)."*

534. Dr Lynch answered as follows:

> *"Q. So the point Mr Goodfellow makes is that, despite confining the DiscoverTech purchase order to software alone, the price remained substantially the same as the price Autonomy had been trying to get from Citi for the hardware/software combination and that was not challenged evidence. Do you dispute it?*
>
> *A. They bought more software than they would have done if they had bought the hardware and the software together.*
>
> *Q. Mr Goodfellow says he would have expected the price for the software alone to be materially less than the price of the combination --*
>
> *A. Not unless they're buying more software, which is what they did."*

535. As noted previously, one of the difficulties in assessing Dr Lynch's evidence is that he was routinely invited to comment or speculate on the reasons or motivation for things in which he had said he had not had any substantive part, and he took to answering from his research and understanding years after the event without invariably reminding the questioner that he was really providing not evidence of facts, but a subsequently informed gloss or *ex post facto rationalisation*. Dr Lynch's sometimes insouciant style tended to exacerbate the difficulty. In this particular context, a subsequent exchange in cross-examination clarified that Dr Lynch was simply offering an alternative explanation based on subsequent review:

> *"A. My understanding is that, yes, they were buying a higher amount of software.*
>
> *Q. What's the basis for your understanding?*
>
> *A. Because all the value is software. There's no hardware in that value*
>
> *Q. So you're simply looking at the value of the contracts and saying, well, they must have bought something different to what was being sold to Citi?*
>
> *A. I had a look at - - you know, as I say, with many of these things you're asking me about I wasn't involved at the time. I had a look at it as part of these proceedings and that was my understanding, so I could go back and have another look."*

536. In any event, and as the Claimants pointed out, Dr Lynch's *ex post facto* rationalisation was flawed. The unchallenged evidence of Mr Goodfellow was that Autonomy had been seeking a price of $5,488,538 from Citi for 64 storage cells. That would have required 64 instances of the software. However, DiscoverTech's purchase order was for only 62 instances of the software. The Claimants are plainly right, in my judgment, that DiscoverTech were not involved in the negotiations as to either price or quantity, whether before or after the VT11 purchase order; and the VT11 purchase order did not represent DiscoverTech's carefully refined view of what it wanted to buy and sell on: it was in all probability, as it seems to me, substantially dictated by Autonomy.

537. The Claimants depicted this as *"another attempt by Dr Lynch to mislead the Court."* I think it is more complicated and less stark than that. Dr Lynch has convinced himself of the righteousness of his position. From the premise that all was correctly done, he glossed events with a mixture of insouciance and plausible conviction. I doubt he told me many things he had not come to believe (though I am afraid that he did tell some). In this instance, he offered an explanation which evidence disproved. I would not, in this instance, say more than that.

538. In the circumstances, the Claimants submitted that their explanation that the hardware element had been stripped out of the VT11 purchase order because if it extended to hardware delivery it could not be effected before the end of the quarter, and thus revenue recognition would not have been defensible or accepted by Deloitte, was left beyond real challenge.

539. Their further implicit submission was that DiscoverTech's indifference to whether what it had purchased and had to sell met the requirements of the proposed end-user was a further illustration of the lack of any real substance in VT11: it was simply paperwork to justify revenue recognition: DiscoverTech did not care because once it had completed the purchase order its part was over, there never being any intention or expectation that any effort be made to achieve an onward sale by the VAR (as distinct from a direct sale by Autonomy).

540. I accept these submissions (express and implicit). The stripping out of any hardware content from the VAR transaction did reflect the need for immediate electronic delivery, in order to achieve a sale before the end of the quarter and justify revenue recognition in that quarter. That was impossible in the case of hardware. I also suspect that a VAR such as DiscoverTech would not have wished to hold (and thus have the burden of storing and then delivering) physical inventory. The purchase order was confined to software simply in order to enable revenue recognition which would otherwise have been denied in respect of the whole transaction. The Claimants are plainly right, in my judgment, that DiscoverTech were not involved in the negotiations as to either price or quantity, whether before or after the VT11 purchase order; and the VT11 purchase order did not represent DiscoverTech's carefully refined view of what it wanted to buy and sell on: it was in all probability, as it seems to me, substantially dictated by Autonomy. I do not accept Dr Lynch's *ex post facto* rationalisation.

541. As important, to my mind, as this further illustration of the use of friendly VARs to trigger revenue recognition is the apparent indifference of the VAR in question to what it ordered or the price: it had no interest in either since in reality the goods remained in Autonomy's control and the VAR would never be called to pay the price.

542. Turning to (2) in paragraph 524 above, the Claimants contended that DiscoverTech played no substantive role in any negotiations with Citi after the VAR deal was made, nor (though party to the tripartite arrangements recorded) in the transaction eventually concluded between Autonomy and Citi. They placed reliance in this regard on the evidence of Mr Goodfellow. This was to the effect that he would have expected to have known about it if DiscoverTech had played any role in the transaction between Autonomy and Citi, and as far as he was aware it did not. The Claimants relied also on the hearsay evidence of Mr David Truitt that DiscoverTech did not have any relevant contacts at Citi (nor at PMI) nor did it *"participate in any sales efforts"* on this account. By the time DiscoverTech became involved the issue of what was to be sold to Citi and at what price had already been

determined between Autonomy and Citi, and in that sense it was fair to say that Autonomy "*were in control*".

543. As a corollary of this, the Claimants submitted that from Citi's point of view, the tripartite document was meaningless, and the joinder of DiscoverTech as a third party an irrelevance. Citi was to deliver its purchase order to Autonomy, it was to make payment to Autonomy and it was to look to Autonomy for performance of all obligations owed to Citi. The mismatch between writing and fact is illustrated by the simple fact that DiscoverTech had no hardware to sell, and it was the unchallenged evidence of Mr Goodfellow that Autonomy delivered the storage cells directly to Citi.

544. The Claimants further submitted that the purpose of executing the agreement had:

> *"nothing to do with Citi's actual requirements and everything to do with Autonomy's revenue recognition manoeuvres. This piece of paper was designed to allow Autonomy to persuade Deloitte that the sale to Citi was made by DiscoverTech. However, as the chronology… makes clear, this was pure illusion. It was the unchallenged evidence of Mr Goodfellow that DiscoverTech played no substantive role in the transaction between Autonomy and Citi…That is consistent with David Truitt's testimony…that DiscoverTech did not "participate in any…sales efforts on either of these accounts." There is no evidence to the contrary."*

545. The Claimants coupled to this a further contention that Deloitte were indeed misled into thinking that DiscoverTech did try to engage with Citi and make an onward/end-user sale but were stymied simply by administrative impediments. The Claimants cited in support the history recorded in Deloitte's working paper (suggesting that what was stated there must surely reflect what Deloitte had themselves been told by their audit client), as follows (typographical errors are in the original):

> "*This debtor relates to a Q2 2010 Digital Safe licence deal sold to the end-user Citigroup, through the VAR Discover Technologies LLC.*
>
> *These balances have not been paid directly by Discover Technologies, but have been settled by Citigroup for the following reasons.*
>
> *Discovery Tech had not traded with CitiGroup before, and CitiGroup are very strict about only trading with approved suppliers. The processes to become an approved supplier takes a long time, and so it would not have been possible to make Discovery Tech an approved supplier before the due date on the invoice owed to Autonomy.*
>
> *Autonomy is however an approved supplier of CitiGroup, and so a 3 party agreement was created whereby CitiGroup would transact directly with Autonomy and settle the gross debt between them, bypassing Discover Tech. In the process, the debtor from DiscoverTech, which is aged here, would be forgiven."*

546. The Defendants disputed this, and they too relied principally on the evidence of Mr David Truitt. The Defendants particularly cited the following extract from his cross-examination in the US criminal proceedings:

> *"Q. In the…Citi deal, did Mr Cronin make a lot of effort to get involved with Citi?*
>
> *A. He definitely reached out to - to procurement folks that we were referred to. He – you know, there was a vendor list that we were attempting to try and get on. So there were conversations that he was having with some folk within Citi.*
>
> *Q. One of the reasons that DiscoverTech wanted to be the reseller on this Citi deal was that you hoped that it would lead to sales of software and services with Citi?*
>
> *A. Yes. That's correct.*
>
> *Q. And a small company getting a relationship with a big company like Citibank would be an advantage, as far as you were concerned?*
>
> *A. Absolutely.*
>
> *Q. And that's why you wanted to be a reseller in the deal?*
>
> *A. Yes. That was very enticing to us."*

547. The Defendants also relied on the following further extract, this time from Mr David Truitt's evidence in chief, which had been side-lined by the Claimants:

> *"Q. …Mr Cronin is writing (reading):*
>
> > *"It appears that a method is being worked where DT would be the reseller, Autonomy would be acting as a DT agent and executing an agreement with Citi directly."*
>
> *Can you help us understand what that means?*
>
> *A. Not – not specifically but, you know, they were -- we were looking to --- Discover was having conversations with procurement at Citi. We were trying to figure out what it would take for them to deal with us directly, and what we found was that they had concerns about that. It was a very long process…to get put on their approved vendor list…"*

548. The Defendants submitted on the basis of this evidence that:

(1) DiscoverTech did make efforts to be involved with Citi on the deal and both DiscoverTech and Autonomy were seeking to have Citi issue any purchase order to DiscoverTech; Autonomy was not seeking a direct sale to Citi. In the event, Citi's internal processes did not permit DiscoverTech to accede to approved purchaser status, and the best that could be done was the tripartite arrangement.

(2) Accordingly, the impression given to Deloitte that DiscoverTech had been trying to make a direct sale to Citi but had been prevented from doing so for

administrative reasons was not false: it was true. Mr David Truitt had explained these attempts in his testimony, marked up as hearsay by the Claimants themselves.

549. As it seems to me, a substantial part of what Deloitte appear to have been told as recorded in their working paper was true: DiscoverTech had not traded with Citi before, and Citi were strict about only trading with approved suppliers. The processes to become an approved supplier did probably take a long time, and so it would not have been possible to make DiscoverTech an approved supplier before the due date on the invoice owed to Autonomy. (See especially the third paragraph of the Deloitte note quoted at paragraph 545 above.)

550. What was not true, however, was that there was ever any real intention for DiscoverTech to negotiate with or sell to Citi: DiscoverTech never became part of the negotiations, and it was always intended to be a direct deal with Autonomy (or nothing). Mr David Truitt's evidence (see paragraph 547 above) was evasive and fell short of saying that it did. An email from Mr Mark of Autonomy to Mr Goodfellow dated 14 May 2010 starts with the words *"Citi won't do a reseller deal…",* Citi maintained the position through until August 2010.

551. Indeed, it seems clear that Citi were only persuaded to become party to the tripartite agreement on the basis that (a) it imposed no obligations upon them, made clear that, although delivery would be via DiscoverTech, Autonomy remained *"responsible for its obligations"* and provided for payment by Citi to Autonomy leaving the joinder of DiscoverTech as a matter essentially between Autonomy and DiscoverTech relating to invoicing and payment; and (b) Citi received a 40% discount (which Mr Hussain agreed expressly in an email to Mr Mark of Autonomy dated 5 August 2010, stating *"Alright if thru discovertech and close this week"*). The Claimants' closing submissions noted that Mr Hussain was willing to countenance a 40% discount in order to have DiscoverTech however notionally, in the loop.[53]

552. In my judgment, the tripartite agreement was put in place, not because Autonomy had to be brought in as an intermediary, but because Autonomy was the true seller, as principal, in a direct sale, which if apparent would have concerned Deloitte. The first sentence of the Deloitte note (see again paragraph 545 above) was simply false: there had been no sale through DiscoverTech to Citi, and given Citi's clear insistence that it would not entertain such a deal, none had ever been intended.

553. Further, in my judgment, the false impression given was intentional. It was supplemented by an equally false email (after the transaction and as part of the audit process) from Mr Chamberlain to Mr Welham and Mr Murray of Deloitte dated 13 October 2010, in which Mr Chamberlain stated *"Citi could not get DiscoverTech entered into their systems in time for a 30th sept close and so we had a three way agreement with us accepting payment on behalf of DT."* It achieved the result intended of heading off Deloitte's concern that, if

[53] It should be noted that Citi were very tough in the negotiation, and it would not be accurate to regard the 40% discount as entirely referable to Autonomy's need for the deal to be routed through DiscoverTech. At one point, Citi indicated that it was regarding Autonomy's efforts to maintain its price as *"a relationship issue",* and in an email dated 5 August 2010 even relayed a message from "Otto" who was in charge of the negotiation for them that *"He says he will spend every working minute to ensure that we get off the digital safe if we cannot get the discount he is asking for".* But the fact that Autonomy needed this special arrangement left them in a weak bargaining position.

a further VAR agreement were to be replaced by a direct end-user agreement, this would call into question whether the VAR had genuinely assumed the risks of ownership. What Deloitte understood, in the words of Mr Welham's witness statement, was that:

> *"it was for purely logistical reasons that DiscoverTech did not itself make the sale to Citi, i.e. because DiscoverTech, having negotiated with Citi, could not be added to Citi's supplier account listing in good time, thus resulting in Autonomy stepping in instead…This explanation distinguished the position from our understanding of the other direct deals that we had identified in our Q1 and Q2 Audit committee reports*[54] *(where we were concerned whether the VAR had in fact assumed the risks of ownership)."*

554. VT11 also illustrates how mechanical the role of a friendly VAR had become; and the friendlier the VAR, and the firmer its trust based on its experience that Autonomy would not leave it in the lurch, the less the need for any protracted or focused consideration of anything more than the potential upside from its point of view which I consider to have been very largely, and sometimes exclusively, the payment of a MAF (by whatever name called). The VAR contract was a necessary step. It had legal effect. The VAR was bound on the terms of its purchase order and the underlying VAR agreement. In his evidence in the US criminal proceedings, introduced in relevant part by the Claimants as hearsay evidence in support of their case, Mr David Truitt expressly agreed that he understood and accepted that DiscoverTech (a) owned the software (b) had full control of the software and (c) owed the money whether or not an end-user deal eventuated. But that did not represent the full understanding of the parties. Only in the technical sense of there being no formal agreement binding on Autonomy was there no side agreement. In substance, the parties knew that (a) DiscoverTech would never interfere or be allowed any say in the negotiations for onward sale and no onward sale by the VAR was ever intended (b) all the parties were subscribed to the assurance that Autonomy would never leave DiscoverTech on the hook, and (c) accordingly neither risk nor control ever in reality passed from Autonomy.

555. The third issue which I have identified in sub-paragraph (3) of paragraph 524 above is the issue as to the basis and propriety of the payment of what in the context of this transaction was labelled a *"Referral Partner commission",* similar to a MAF. In particular, my focus is on the way the payment was presented and sought to be justified.

556. An email dated 15 October 2010 from Mr Egan to Mr Kanter, copying Mr Hussain, recorded the agreement of Mr Hussain and Mr Egan that *"DiscoverTech is due 10% on the Citi deal"* and requested Mr Kanter to *"create the letter today and approve wiring funds for today."* Mr Kanter's letter to DiscoverTech of the same date (and dated accordingly) purported to formalise a *"prior discussion"* and evidence an agreement to pay DiscoverTech \$497,000 as a "*Referral Partner commission*". The letter provided in relevant part as follows:

> *"Referral partner will: (1) introduce Autonomy into the deals with Citi Group ("End-User"); (2) obtain quotes from Autonomy on behalf of the End-User;*

[54] It will be recalled that Deloitte were not told about the direct deal with the FSA in Q3 2010 (in which the VAR was Capax Discovery) either, and so in their Q3 2010 report to the Audit Committee Deloitte had noted that there had been no further reversals of transactions with VARs in the form of direct deals. Deloitte had expressly warned about its concerns if another deal went direct.

and (3) work with the End-User to assist in executing purchase orders and contracts with Autonomy.

Autonomy will: (1) pay Referral Partner commissions in the amount of $497,000, as a result of Referral Partner's direct and proximate participation in the account; (2) deliver products directly to the End-User; and (3) use reasonable efforts to provide mutually agreed upon sales assistance. With respect to any Lead (as defined below), including the End-User obtained by Referral Partner through Autonomy, Referral Partner agrees not to market or sell any products competitive with the Autonomy software to such Lead for the specific Lead opportunity identified and will promptly notify Autonomy is such Lead is considering a competitive product…".

557. The Claimants submitted that DiscoverTech had not performed any of these roles. As Mr David Truitt testified in the US criminal trial:

"Q. Did Discover introduce Autonomy into the deals with Citigroup?

A. We did not.

Q. (reading) "(2) Obtain quotes from Autonomy on behalf of the end-user." Did Discover Technologies do that?

A. We did not.

…

Q. Beyond signing the purchase order in March of 2010 and taking the risk as you described, did Discover Tech provide any marketing assistance to Autonomy?

A. No. Again, these existing customer deals, there really wasn't much to do. We did not."

558. Dr Lynch confirmed in cross-examination that he had no basis on which to dispute Mr David Truitt's evidence though (as elaborated below) he explained his different understanding of the letter, and he did not accept that, in the round, a false impression was given of DiscoverTech's role.

559. The Claimants also made the point that there is no evidence before the Court from Mr Kanter. They submitted that therefore there is no basis on which the Court could find that he (Mr Kanter) honestly believed the description in this agreement of DiscoverTech's role to be true, or that he had any basis for holding such a belief.

560. Accordingly, the Claimants submitted that the payment of a nearly $0.5 million fee was for doing *"nothing other than facilitating an improper acceleration of income."*

561. Against this, the Defendants contended that, even if the presentation was not entirely accurate, there was a clear rationale for the payment, as Deloitte accepted in their review. The letter from Mr Kanter contained standard form language and was capable of being

used, in that (a) the first obligation of Autonomy was to pay DiscoverTech for its *"direct and proximate participation in the account"* which covered DiscoverTech's planned and eventual role and (b) the agreement also had forward-looking obligations, including a restriction on competition from the VAR which Dr Lynch stated in cross-examination was of importance because:

> *"…in return what we want is the ability to have the relationship through them with the customer and them not to go along and do things like, for example, bring in our competitors and that sort of thing."*

562. When pressed by Mr Rabinowitz to accept that *"it's obvious that the letter from Mr Kanter gives a false impression of what role DiscoverTech was actually playing here"* Dr Lynch reiterated that this was not his understanding. The suggestion was then put to him that:

> *"the problem for Autonomy was that if it documented the real reason for paying a fee to the VAR, that would involve stating that the VAR was being rewarded for enabling Autonomy to recognise revenue improperly, correct?"*

563. Dr Lynch responded:

> *"I disagree. If the VAR letter had just said, "We're going to pay a marketing assistance fee" or, you know, "a fee", there would be nothing wrong with that. There doesn't have to be a specific reason given. Especially if the commercial reality is obviously the VAR wants to make a turn on its deal. Again, this is industry standard stuff, everyone does it, including HP."*

564. The Defendants thus dismissed the Claimants' point as a *"forensic rather than a real one"*.

565. The question, as it seems to me, is whether Mr Kanter's letter was really just a handy template, some broadly applicable to the facts, some not but adopted out of convenience and not to misrepresent; or whether the description of the services purportedly provided by DiscoverTech was intentionally crafted to secure approval from Deloitte and/or the Audit Committee. Did Mr Kanter intentionally exaggerate and misstate DiscoverTech's role? Dr Lynch said it did not.

566. In my judgment, the letter was all of a piece with the misrepresentation of the whole nature of the transaction. It was false because the whole notion that the VAR was doing anything at all was false. The letter was intentionally in terms which sought to bolster the appearance of, in the words of the letter itself, a commission being paid for *"direct and proximate participation in the account",* direct contact with and delivery to the end-user and *"reasonable efforts to provide mutually agreed upon sales assistance".* A fee would probably not of itself have been objectionable; nor do I think it has been established that it was known to be a reward for impropriety. It seems to me likely that Mr David Truitt's simple explanation that *"we took the risk by issuing the order, and…expected to be paid*

a margin when the deal closed" was the reality in this context, as in many similar VAR deals. But the letter was part of the entire presentation: and, in my judgment, whether template or made to measure, it was misleading, and known by Mr Kanter to be so.

567. Finally, I would note one further typical feature: Dr Lynch accepted that the deal did not ultimately result in follow-on work for DiscoverTech either. In seeking to justify a fee by reference to the need to secure loyalty in the context of that future work, Dr Lynch was once again speaking more theoretically than accurately. Moreover, the 'friendly' VARs tended to present the opportunity for future service work as both (a) the main commercial reason for the VAR undertaking the risk and also (b) a valuable prospective contribution or *"added value"* from Autonomy's point of view, since its objectives included minimising its own service business (and relying on sub-contractors or partners instead) and maximising its software licence sales.

Defendants' knowledge of and participation in VT11

568. There is no issue as to Mr Hussain's knowledge of and participation in VT11 and in offering a discount in exchange for agreement to the subsequent tripartite agreement and payment of a *"Referral Partner commission"* or MAF (which Mr Hussain approved). He appears to have been sent a copy of Mr Kanter's letter of 15 October 2010.

569. Dr Lynch's case was that he (Dr Lynch) knew of but was not involved in the negotiation of this reseller deal, nor in the accounting for it. Nor was he involved in the later tripartite arrangement, or in the MAF payment. Dr Lynch was cross-examined on this transaction:

(1) Dr Lynch understandably said that he would not know whether DiscoverTech had a relationship with Citi.

(2) He was asked why he had not mentioned either this transaction or the one with PMI in his evidence; he replied by saying *"I don't think there's anything wrong with a willing buyer buying software off you in the hope of selling it on.*"

(3) It was put to Dr Lynch that he was aware that "*Autonomy was proposing to get DiscoverTech to submit a purchase order for end-user Citi to enable Autonomy to recognise revenue of $5.5 million in the quarter*". Dr Lynch answered: *"I think that's the goal, yes".*

(4) The Claimants put to Dr Lynch their argument about the Citi deal ultimately including hardware and software as well. Dr Lynch made clear that he was not involved in or aware of any of this detail at the time. He said: *"I may have had it on a list, but I wouldn't have had any more involvement than that.*" He was not challenged on this evidence.

(5) Dr Lynch was asked about the wording of Mr Kanter's MAF letter. It was not suggested that Dr Lynch had played any role in preparing this letter, or that he had even seen it at the time. When asked questions about it, however, Dr Lynch did not accept that the letter was misleading: he explained that these were standard terms which contained a forward-looking element. He also made the point that this was a standard way of compensating a reseller in the industry, and that resellers did in fact assist in marketing continually.

570. Dr Lynch submitted in the round that none of the points raised by the Claimants in cross-examining came near to justifying the contention that he was aware of any impropriety or false accounting with respect to this transaction.

571. In my judgment, Dr Lynch plainly knew of the use of DiscoverTech as a VAR for the transaction. On 31 March 2010 Mr Hussain had notified him of this by an emailed note which summarised the *"Route to 25c requires $200m"* and had an entry *"Citi – Disc tech 5.5"*. But there is little transaction-specific evidence to tie him to the various subsequent events described above.

572. Nevertheless, and given the usual course of monitoring of deals identified as necessary to enable forecasts to be met, I think it more likely than not that Mr Hussain did keep him informed of the progress towards a deal; and in light of their usual practices, and Mr Hussain's personal need and tendency to share such matters with Dr Lynch, I also think it likely that Mr Hussain told Dr Lynch of (a) Citi's threat to walk away from the relationship if not given a discount (see above), (b) Mr Hussain's agreement to 40% and (c) the accommodation agreed in the form of the tripartite agreement (which Dr Lynch would have known would be presented to Deloitte). More generally, in my judgment, Dr Lynch knew that the VAR was expected to do nothing in every case. Once again I would in addition refer to and read in paragraph 2192 to 2195 in the main body of the judgment *mutatis mutandis*. Given the $30,000 approval policy, I consider also that Mr Hussain would have referred to Dr Lynch before approving a payment out as a MAF of some $0.5 million.

573. All in all, therefore, I have concluded that both Mr Hussain and Dr Lynch knew that VT11 had no real substance, and the recognition of revenue from it in Q1 2010 was wrong and that Deloitte were giving approval in ignorance of the true nature of the transaction (and in particular, its lack of any real substance).

574. VT11 (in Q1 2010) seems to me to illustrate well the strategy of using 'friendly' VARs to make good revenue shortfalls and the pattern adopted (with variations to suit particular exigencies) to implement it, which involved the VAR in doing nothing beyond accepting a legal risk and thereby enabling Autonomy to present the 'sale' as mandating revenue recognition whereas in truth the only real sale was any which Autonomy could negotiate and agree with an end-user.

VT12: DiscoverTech/PMI Q1 2010

575. VT11 was transacted in tandem with another impugned VAR transaction (VT12) between Autonomy and DiscoverTech for prospective end-user Philip Morris International ("PMI"), the tobacco company.

576. The VT12 purchase order was issued subject to a reseller agreement on substantially the same terms as that used for VT11, which I have summarised at paragraph 508 above. It was set out in a letter dated 31 March 2010 from Autonomy to DiscoverTech, signed by Mr Kanter and counter-signed by Mr Malcolm A. Hyson (as Vice President) for DiscoverTech. The agreement expressly provided that it constituted the parties' entire agreement and put DiscoverTech fully on risk. The licence fee was $4,185,000 (with $878,850 payable immediately upon execution) plus a first-year support fee of $209,250.

577. Mr David Truitt's evidence was that the PMI deal presented an opportunity he wanted to participate in. He wanted to provide services to the end-user, and assumed the risk of the transaction in order to do so. He also funded the first instalment payment from his own resources. Mr David Truitt's evidence corroborated Mr Egan's evidence that DiscoverTech was on risk.

578. The only issue on which I need to focus in respect of VT12 seems to me to concern the circumstances in which PMI entered into a direct deal with Autonomy, rather than a deal with DiscoverTech.

579. The Claimants focused in this regard on an email dated 4 August 2010 from Mr Hussain to Mr Kanter (copying Mr Egan) seeking approval for a payment of a MAF to DiscoverTech, in which Mr Hussain explained the history and sought to justify the payment of a MAF on the basis of:

> *"the history being that because PMI were so concerned about compliance that they placed the order direct so the DiscoverTech PO was replaced."*

580. The Claimants contended that this explanation was contrived and untrue, *"as all those involved in the exchange would have known"*. In truth, they contended, PMI had:

> *"placed its order with Autonomy because it had been negotiating with Autonomy all along and had no relationship with DiscoverTech."*

581. The Claimants relied on a sequence of emails demonstrating that it was Autonomy which pushed for the deal it eventually struck with PMI to be *"pushed through DiscoverTech"*. At one point, in early June 2010, this appeared to be nearly agreed since PMI at that time contemplated itself dealing through its "partner", SHI. But PMI changed its mind because that idea was causing internal problems for it. At that point, Autonomy continued to press for the deal with PMI to be "pushed through" via DiscoverTech, and put this forward in what the emails described as a *"higher level approach"*; but in the same email it was recognised within Autonomy that if that higher level approach failed, they would *"need SH to approve the direct route"*. That effort did fail: PMI declined to place an order with DiscoverTech and insisted that any deal be direct with Autonomy; and a direct deal was then concluded. The Claimants submitted that this transaction thus followed the standard 'pattern', with the irrelevant exception that at one point, and at Autonomy's urging, the end-user did toy with the idea of dealing via DiscoverTech. None of this signified that there was any real intention for DiscoverTech to take any active part in the negotiation or execution of a transaction with PMI; it was always to be entirely passive, in accordance with the 'pattern'.

582. The Defendants, on the other hand, presented the background to be, in summary, as follows. After the VAR deal had closed, PMI wanted to use its own partner for the deal, SHI. Autonomy was content with this provided that PMI's partner dealt through Autonomy's partner, DiscoverTech. As at 4 June 2010, DiscoverTech were waiting for a purchase order from SHI, and would be shipping them the software that had been shipped to DiscoverTech by Autonomy (using Automater) in the previous quarter.

583. In the event, PMI changed its mind with regard to having any partners on the deal and the purchase was implemented as a direct deal. In circumstances where Autonomy had taken the opportunity and the purchase order directly, leaving DiscoverTech without the end-user prospect envisaged, a credit note was issued to DiscoverTech and a MAF was paid. The amount of the MAF reflected the margin between the sale to DiscoverTech and the subsequent end-user sale.

584. In effect, the Defendants sought to contend that the direct deal between Autonomy and PMI was an unexpected substitute for an expected end-user sale by DiscoverTech to PMI, necessitating and justifying the credit note as the means of making good DiscoverTech for the direct deal having caused DiscoverTech to miss out on the end-user sale for which it had purchased the software. The sub-text was that the sale to the VAR was a substantive sale in the expectation of an onward sale by the VAR to PMI.

585. I cannot accept that an end-user sale was ever the expectation; and even if PMI had agreed to sell to DiscoverTech (which, as has been seen, it did not) the reality would have been that this would simply have been a convenient means of settling Autonomy's direct sale. Vis-a-vis PMI the seller was always Autonomy. The objective of the negotiations was always a direct sale. Autonomy's urgent recourse to a VAR in order to trigger revenue recognition in the desired quarter did not alter either the negotiations or their objective. The Defendants' depiction of VT12 as having been entered into with a view to DiscoverTech entering into an onward end-user sale to PMI is inconsistent with the chronology and the emails I have referred to above.

586. I agree with the Claimants, therefore, that VT12 was another exemplar of the usual pattern. It follows, and I find, that Mr Hussain's email of 4 August 2010, in giving the impression that only concerns about compliance issues had led to the direct sale, was false.

587. There is no dispute as to Mr Hussain's knowledge of VT12, and he was kept informed at every stage after it which ultimately resulted in the proposed onward sale by DiscoverTech to PMI's partner, SHI, being replaced by a direct sale by Autonomy to PMI and the issue of a credit note by Autonomy to DiscoverTech. Mr Hussain also approved the payment of a MAF.

588. Dr Lynch did not address VT12 in his witness statements. He explained in cross-examination that he had *"almost no involvement"* in either PMI or Citi, or in their accounting treatment. He accepted that he knew that a VAR was to be involved, and he made clear that he was content with that:

> *"As I've said, I would have had no issue about a deal that we were working with an end-user, a VAR becoming involved in that and that sale happening to the VAR if the end-user deal was delayed or the VAR gave us other advantages."*

589. I would repeat *mutatis mutandis* what I have said in paragraphs 568 to 574 above in relation to VT11 and the Citi deal, and the Defendants' "guilty knowledge" and express the same conclusion.

590. The only further point I need note in respect of the transaction is the Claimants' assertion that:

> *"Thereafter, the Defendants were more careful to ensure that Deloitte was kept in the dark about the phenomenon of VARs being reversed and replaced by a direct end-user deal. Until Q3 2011 – a quarter that was not reviewed by Deloitte – Autonomy developed other ways to protect the relevant VARS."*

VT30: DiscoverTech/Prisa Q1 2011

591. Promotora de Informaciones SA ("Prisa") was (and is) an IT service management and media company operating in Spain, Portugal and (so Dr Lynch thought) Latin America. It was an existing Autonomy customer with which Autonomy was in discussions during 2011 with a view to a hosting transaction under which Autonomy would *"swipe the hosting business away from IBM",* as Mr James Murray at Autonomy described it in an email dated 15 March 2011 to Mr Hussain and Mr Wyse, which was copied to Dr Blanchflower. In the same email Mr Murray noted that Prisa understood that Autonomy *"would try to squeeze it into this quarter."*

592. The possibility of such a transaction was initially described by Mr Hussain in an email to Dr Lynch dated 17 March 2011 as a *"real long shot"*. However, after a meeting in Madrid, Mr Hussain emailed Dr Lynch on 24 March 2011 saying *"Prisa going well. Need bbc"*, and again on 28 March 2011 to say the prospects were 50/50. However, when Dr Lynch requested a further update from Mr Hussain on 30 March 2011 (which is demonstrative of the frequent contact and process of updating that apparently was the norm between Dr Lynch and Mr Hussain), Mr Hussain's spreadsheet sent in reply no longer mentioned Prisa; and in the event, however, no deal had transpired before the end of the quarter.

593. The collapse of the prospect of the Prisa deal in Q1 2011 gave rise to the risk of a shortfall of quarterly revenue (compared to forecast). Prisa became one of several deals in respect of which Autonomy resorted to a VAR transaction with DiscoverTech, the terms of which were set out in a letter agreement bearing the date 31 March 2011. Those terms were substantially the same as the terms set out in earlier letter agreements between Autonomy and DiscoverTech, and included the provisions referred to in paragraph 508 above (including the provisions for the passing of risk and control, and an entire agreement clause).

594. Looking ahead, no deal in relation to this software was eventually concluded with Prisa, by either DiscoverTech or Autonomy. The Claimants' position is that although DiscoverTech satisfied its obligations in respect of this deal[55] it was only enabled to do so by a 'reciprocal' transaction which they sought also to impugn.

595. To return to the VAR transaction itself, the Claimants' complaints in relation to this transaction, VT30, had four principal strands (though one related to the hardware case rather than the VAR claims):

    (1) First, there was an allegation of backdating. It was said that Mr Hussain only asked Mr David Truitt (via Mr Egan) to take a deal for Prisa as prospective end-user some time in the week <u>after</u> the end of Q1 2011, that the Prisa deal was in

[55] The Claimants complain about the purchases by Autonomy of DiscoverEngine software. See section C.5.12 below.

fact not entered into until 4 April 2011, and the letter agreement was backdated to the quarter end so that revenue could be booked as earned in the quarter (Q1 2011), which in truth it had not been;

(2) Secondly, the deal was also said to illustrate the use of hardware sales as a discretionary fund, use of which could be calibrated with VAR sales;

(3) Thirdly, the Claimants contended that there was never any real prospect of a sale to Prisa because Prisa had no need for the software offered;

(4) Fourthly, the Claimants contended that although DiscoverTech did pay its debts to Autonomy on the deal (despite there being no end-user sale), DiscoverTech was enabled to do so by Autonomy purchasing DiscoverTech's *"DiscoverEngine"* software.

Alleged backdating

596. The Claimants' case that the Prisa VAR deal was dishonestly backdated to 31 March 2011 (see paragraph 595(1) above) was principally based on the evidence of Mr Egan in these proceedings and on Mr David Truitt's testimony when cross-examined in the US criminal proceedings. They also relied on more limited evidence from Mr Scott also given in the course of the US criminal proceedings.

597. Mr Egan described the circumstances of the VAR deal (VT30) in his witness statement as follows:

> *"In early April 2011, Mr Hussain told me that he needed a deal to make up for a revenue shortfall in Q1 2011. He asked me to get DiscoverTech to take a deal for PRISA as end-user. He told me that the deal documents had to be dated March 31, 2011. I called David Truitt. I asked him, as a favor and as a one-time request, to do a deal that would be backdated to March 31. On April 4, 2011, I sent Mr. Truitt a letter agreement dated March 31 that gave DiscoverTech a license to sublicense to PRISA certain identified eDiscovery and archiving software. The license fee was $3.6 million, plus $200,000 for support and maintenance. I asked that a signed purchase order be sent to my personal email, rather than my Autonomy email address, so that I could separate the signed license agreement (dated March 31) from the electronically dated covering email (which would be dated April 4 or 5) and could then provide a copy of the license agreement only to Autonomy for its records.*
>
> *Mr. Truitt said that he was uncomfortable with this request. I said I was equally uncomfortable with it. Nevertheless, Mr. Truitt agreed to have his CTO Malcolm Hyson sign the letter agreement. The signed agreement was sent to my personal email address. I countersigned the agreement and dated my signature March 31, 2011. …"*

598. The Claimants contended that Mr Egan's account was also borne out by an instant messaging chat on 4 April 2011 between Mr David Truitt and Mr Hyson. Mr David Truitt was confused by Mr Egan's request to "*pdf me an email*" and sought Mr Hyson's advice on what it meant. He explained that "*Autonomy wants me to PDF an order, said that it will not change the date on the document if it is PDF?*". The Claimants contended that the reason for a PDF was to conceal the fraudulent backdating.

599. When he was asked by Counsel for Mr Hussain in these proceedings why he had not revealed the backdating earlier to HP's lawyers (and only then when trying to get an immunity deal), and why he had made no mention of it in his letter to the US Air Force in relation to the Prisa deal, Mr Egan's evidence was that he felt "*uncomfortable*" about the backdating, that he *"buried it"* as a "*very unpleasant memory*". He accepted that *"in the truest sense of the word"* he had not forgotten it and would "*never forget about it*". He said, "*I felt at the time when I was doing it that it was the wrong thing to do*".

600. His explanation for not having mentioned the backdating earlier to HP's lawyers was that he was not asked about the DiscoverTech/Prisa transaction and was not volunteering information on transactions he was not asked about:

> *"I really wasn't volunteering any information in general. I was asked to and really advised to answer everything and anything asked of me truthfully."*

601. When asked whether he accepted that it was possible that his recollection *"might have been affected by the threat that you might be prosecuted and imprisoned"* he said he did not accept that, adding that he *"never felt as though there was any prospect that [he] was in that kind of jeopardy"*. He did accept, however, that it was possible (*"a truism in the world"*) that his recollection might have been affected by the process of talking to lawyers.

602. Mr David Truitt's evidence in the US criminal proceedings was that the backdating was for him too *"very concerning because it was out of the norm of what I knew business to be"*. Mr David Truitt also said that he *"reached out to both Mr Egan and Mr Scott and let them know that I was concerned about what I had been asked to do;"* he *"wanted to make sure that I wasn't doing anything improper. I did not want to put myself in a situation where I could be in trouble."*

603. Mr David Truitt's evidence was that it was in light of his concerns that a meeting took place between Mr Egan, Mr Hussain and himself on 14 April 2011, in respect of which he sought reassurance. The Claimants and the Defendants presented the nature and effect of the discussions very differently.

604. In summary, the Claimants painted a picture of Mr Hussain reassuring Mr David Truitt that since Autonomy traded out of the UK, it was not within the purview of the US Securities and Exchange Commission and that international accounting principles allowed "*some flexibility*", but that in light of Mr David Truitt's misgivings, it would not happen again. The forensic impression the Claimants sought to create was that the reassurance was in effect that the backdating was unlikely to be discovered by the regulators, and Autonomy would not run the risk again.

605. The Claimants dismissed the suggestion made on behalf of the Defendants that Mr David Truitt's discomfort was alleviated by the reassurance given that the documenting of a previously reached agreement was permissible under IFRS; they submitted that the suggestion was *"inherently implausible, uncorroborated by any contemporaneous documents, unsupported by any evidence from Mr Hussain, and Mr Egan did not have any memory of it"*. The Claimants made the point that if the purpose of the purchase order was merely to record a previously concluded oral agreement, it is hard to see why the documentation could not simply have said so: it would have been easy for the document

to have borne the genuine signature date but stating that it was memorialising an oral agreement reached in March 2011.

606. The Defendants, on the other hand, depicted Mr David Truitt's concern as having been that for accounting purposes the relevant date was not when the transaction was agreed but when it was formalized in writing, and that therefore his signature on a backdated document had resulted in substantively improper accounting, (which, he said, *"is why I was concerned"*). The Defendants contended that this concern was misplaced. It was based on a misunderstanding as to the effect under IFRS of papering a deal agreed within a given quarter, but not reduced to writing until after the end of the relevant quarter. It was their case that the relevant date for IFRS purposes was the date of agreement, and not the date of the paper recording or evidencing agreement. On that basis, the backdating of the document had no substantive effect in terms of revenue recognition in Q1 2011 if the date on the document reflected the date of an earlier oral agreement.

607. The factual premise of the Defendants' presentation was thus that the relevant Prisa deal had in fact been agreed before the end of the quarter, as one of many in a *"slate of deals"* agreed orally. However, neither Mr David Truitt nor Mr Egan could be sure of this. In a sense it offered Mr David Truitt a graceful exit; for Mr Egan it was more dangerous, first, because if there was a prior agreement, it could be said that it was his own failure to get the paperwork done which had caused the problems, and secondly, because his approach to the US prosecuting authorities was to confess and avoid, and hope they would pursue bigger fish; and, further, his deal with the US authorities required him to maintain consistency with the version of events he agreed with them.

608. Mr David Truitt's evidence was that Autonomy had approached him within the last days of the quarter. They had offered a *"slate of deals"* which Mr Truitt agreed to do; he thought that the Prisa deal *"very well could have been"* in that slate of deals, but he could not say for certain one way or the other. He thought that he and Mr Egan were talking about the slate of deals on the Thursday (the last day of the quarter); the paperwork for the Prisa deal was not completed until the Monday.

609. Mr Egan accepted that he could not be sure, or anywhere near sure, that David Truitt's recollection was wrong. He accepted that his own memory of the meeting and what specifically was said was vague; but whilst accepting that it was possible that Mr David Truitt's recollection was right, he did say *"It's not my memory";* and he subsequently added:

> *"...My feeling was I did not feel as though we had done the deal, so I had bad feelings about papering it after the end of the quarter."*

610. That encapsulates the factual difference: the dispute is not as to whether the document was backdated but whether before the document was executed the parties were already in fact in agreement on the terms of the deal.

611. The evidence given by Mr Scott in the US criminal proceedings is of some relevance in this context. He confirmed that Mr Hussain had asked late on 31 March 2011 for a list of *"8a deals"* which he had taken to be a request for a list of the VAR deals that Autonomy had executed on 31 March 2011. When Mr Scott responded (on 1 April 2011) listing the deals for which purchase orders had been issued, he identified two DiscoverTech deals, neither of which was a Prisa deal. No explanation was offered by the Defendants as to

why, if done by then, the Prisa deal was not included in the list. There was no documentary evidence to support the theory that Prisa was proposed to and agreed by DiscoverTech on or before 31 March 2011.

612. I have reached the conclusion, on the balance of probabilities, that the Prisa deal was presented to DiscoverTech after the end of the quarter. It seems to me probable that it had been omitted in error from the "slate of deals" presented to DiscoverTech, and that when the error was discovered (perhaps after the list obtained from Mr Scott did not mention it) the error was sought to be cured by the wrongly dated letter agreement: given that Mr Hussain had earlier pressed hard for a direct deal with Prisa before quarter-end that seems to me more likely than the alternative explanation of it being an after-thought. In my judgment, therefore, VT30 was backdated, and the backdated document did not evidence any prior finalised oral agreement.

613. It would follow that revenue was prematurely recognised in an earlier quarter than was justified.

614. Ironically, in fact the revenue from VT30 was not required to achieve the quarterly revenue forecast. That leads on to another facet of the Claimants' contention that the Prisa deal shows *"that, for the Defendants, the revenue recognition decision was to be reverse-engineered from the target figure for total revenue, regardless of the underlying facts."*

Calibration with hardware sales: two levers to manipulate revenue?

615. This aspect of the case ties in with parallel allegations in the context of the Claimants' claims in relation to hardware sales to the effect that Autonomy was treating the revenue from hardware sales as a discretionary fund that could be recognised as and when it was needed to meet quarterly targets, and that the figures were manipulated by Autonomy after the quarter-end.

616. In the context of the Prisa deal, the Claimants focused on two emails in particular. The first was an email from Mr Hussain to Dr Lynch dated 11 April 2011, with the subject "*Q/e*", stating:

> *"If we defer prisa then we are at 218.1m but 24c and 85% [gross margin]. If we don't defer prisa but defer equiv low margin we are at same revs but now at 25c and 88%. To discuss when I land or you can discuss with steve [Chamberlain]."*

617. The reference to *"equiv low margin"* was to low margin hardware revenue, which the Claimants contended was turned on and off according to whether it was needed to meet revenue forecasts. In short, the Claimants contended that in this email Mr Hussain was identifying various options that he considered might be adopted in relation to revenue recognition at this time, and in particular was questioning whether to recognise revenue in Q1 2011 on the DiscoverTech/Prisa transaction (which was, in fact, not entered into until early April 2011, but was backdated to 31 March 2011), <u>or instead</u> to recognise hardware revenue – the benefit of the former course being the advantageous effect it would have on gross margin and earnings per share (given the comparatively low margin or loss on hardware sales).

618. In cross-examination, Dr Lynch stated that he did not accept that Mr Hussain was "*saying that there's necessarily a choice in all of this*". However, the Claimants submitted that it is plain from Mr Hussain's email that Mr Hussain was doing precisely that: he was making clear to Dr Lynch that they could do one thing ("*defer prisa*") or the other ("*defer equiv low margin*"). Moreover, if Mr Hussain was not presenting a choice, there would be nothing for Dr Lynch to discuss with Mr Hussain or Mr Chamberlain on the back of the email ("*To discuss when I land or you can discuss with steve*"). That is plainly correct: I accept it[56].

619. The second email exchange relied on was on the following day. Mr Chamberlain's email to Mr Hussain the following day, 12 April 2011, with the subject "*Numbers*" read as follows:

> *"Three options:*
>
> *1) recognize Prisa, defer $3.6m Hardware - $218.1m, 88%, 24.8c*
>
> *2) Defer Prisa, recognize $3.6m HW - $218.1m, 86%, 23.7c*
>
> *3) recognise BBC $1.6m, defer Prisa, recognize $2.0m HW - $218.1m, 87%, 24.2c*
>
> *Need to speak asap to lock this down. We announce in 9 days and if we don't stop moving I cannot deliver timetable."*

620. Thus, according to the Claimants' reading of the email, Mr Chamberlain presented "*Three options*":

(1) The first option was to recognise the Prisa VAR transaction and to defer the equivalent amount of hardware revenue ($3.6 million), which would result in total revenue for the quarter of $218.1 million, a gross margin of 88%, with earnings per share of 24.8 cents.

(2) The second option was to defer Prisa and instead recognise hardware revenue of $3.6 million, which would result in the same overall revenue ($218.1 million), but a lower gross margin (86%) and earnings per share (23.7 cents) due to the hardware deals being loss-making.

(3) The third option was to recognise a transaction with the BBC with revenue of $1.6 million, again defer Prisa, but recognise hardware revenue of $2 million, which would generate the same overall revenue, but mean that gross margin and earnings per share were at 87% and 24.2 cents respectively.

621. The Claimants submitted that the fact that these were intended to form options is reinforced by Mr Chamberlain's concluding paragraph, in which he said that he needed to speak to Mr Hussain as soon as possible so as "*to lock this down*".

622. Dr Lynch told me that this was not how he interpreted the email. Dr Lynch did not accept that Mr Chamberlain was really presenting a choice between options: rather, he suggested

[56] This is also relevant to the hardware claim, as it shows hardware was seen as a flexible mechanism to meet revenue targets.

that the email identified the various ways in which revenue would be affected according to whether it was possible to recognise revenue from the various transactions identified, which would depend on a review of whether or not the accountancy criteria were satisfied.

623. Dr Lynch also sought to distinguish between on the one hand, picking and choosing what revenue to recognise (which he had accepted was not permissible under IAS 18.14) and, on the other hand, determining by reference to criteria whether it was permissible to recognise the revenue by reference to accountancy criteria such as collectability, or whether delivery had successfully been completed. Thus, Dr Lynch rejected the suggestion put to him that the email demonstrated "*a willingness to pick and choose what revenue to recognise which you knew was improper*". He maintained that his understanding was that this was explicable as one of the legitimate judgements that have to happen after the quarter end and before the finalisation of the quarterly report: in particular:

> *"A. ...After the end of the quarter, my understanding is there are a series of judgments that have to be made. One of them is to do, for example, with creditworthiness, and in this quarter DiscoverTech had submitted three orders and there was a judgment to be made about whether DiscoverTech's credit was worthy of having three or two or one, or which of the two, and that decision had to be made.*
>
> *At the same time there was also issues about whether all of the necessary proof to meet all of the acceptance criteria about hardware had been met. And this is part of the normal process that happens past the quarter end where all of the paperwork and the terms and the evidence is reviewed."*

624. Dr Lynch further elaborated this as follows (in a passage which I also consider reinforces my conclusion that the backdating was to cover an oversight) when pressed as to whether he understood the process at the time:

> *"I would definitely have understood at the time the general principle I just outlined to you because what happened at the quarter end was there would be complete chaos in the last couple of days of the quarter as the deals are done, then the deals start to come in, the paperwork, over the next few days. Then they go through legal and finance, so legal will check that there's no amendments that make it not recognisable or acceptance criteria, whatever. Then finance will look at it. As we've seen, Mr Chamberlain then has to get together evidence for whatever –"*

625. This has, in general terms as opposed to particular application, the ring of truth and practical reality. In the parallel context of the recognition or deferral of hardware revenue, both Mr Bloomer (Audit Committee Chairman from September 2010) and Ms Harris (Autonomy's Financial Controller) confirmed that there is nothing improper in reviewing, after the quarter end, whether to recognise revenue in the previous or subsequent quarter according to a judgment as to the satisfaction or not of revenue recognition criteria. As Mr Bloomer said:

> *"…it's normal in any company, when you finish a quarter or a half-year or year, annual accounts, to have a -- there are always things that need sorting out after the end of the period…[such as]…did things actually get delivered in the quarter or the next quarter, the bad debt provision always gets sorted out after the quarter-end…I'd want and would expect the auditors to look at that as part of their review of cut-off and be comfortable that whatever decisions were made were appropriate for the end of the period and what should fall into the next period."*

626. Ms Harris also stressed that any late post-quarter or other accounting period changes, and especially revenue recognition changes, would be scrutinised with special care by auditors, who typically remained on site in the weeks after the quarter-end.

627. I accept the evidence of Dr Lynch, Mr Bloomer and Ms Harris that post-accounting period review and alterations were plainly normal, appropriate and indeed necessary, especially as regards revenue recognition (whether in respect of sales of hardware or software). But the real question is whether that was the process recorded or invited by the emails to which I have referred. The Claimants contended that it was not, and they dismissed Dr Lynch's further justifications as not credible.

628. I have concluded that the email exchanges referred to above cannot satisfactorily be explained away as showing merely the usual and proper process of checking that revenue recognition criteria (such as completed delivery or achievement of designated 'milestones') have been satisfied prior to the end of the quarter. The impression I have formed is, and I find, that by early 2011 Mr Chamberlain and Mr Hussain had begun to think of the revenue recognition criteria, especially in their application to hardware revenue, as being malleable. Further, the 'options' adumbrated by Mr Chamberlain demonstrated that, by then, the two of them (at least) were prepared occasionally to stretch the normal process of revenue recognition review after quarter-end to extend to some fluid self-serving review, which could be described as manipulation, of the timing of revenue recognition, perhaps taking advantage of a certain fluidity and chaos, to suit the objectives of (a) meeting and beating revenue forecasts, (b) achieving healthy gross margins and (c) maximising earnings per share.

629. Given that (as was common ground) IAS 18.14 not only permits but requires revenue recognition if the criteria it identifies are satisfied, so that, as Mr Welham put it in his witness statement, *"[e]ither the revenue was earned in Q1 2011, or it was not"*, a determination of the timing of revenue recognition after the end of a quarter in which it was apparently earned which is influenced and even driven by such objectives is a departure from the approach stipulated, as well as being obviously improper. It is not consistent with IAS 18.14, as all concerned must have known.

630. In the event, revenue from the DiscoverTech/Prisa VAR transaction was allocated to and recognised in Q1 2011. A comparison between the hardware revenue that Mr Sullivan achieved in Q1 2011 ($22.1 million) and the amount recognised in that quarter ($20.1 million) indicates that some $2 million out of $3.6 million of hardware revenue was

deferred. The upshot was that Autonomy was able to report total revenue for the quarter of $220 million, gross margins of 88% and adjusted earnings per share[57] of 26 cents.

Never any intention that DiscoverTech would negotiate or conclude an end-user sale

631. The third strand of the Claimants' case on the Prisa deal (see paragraph 595(3) above) was their assertion that there was never any real prospect of any onward sale to Prisa, and that there was never any real intention either that DiscoverTech should even attempt to effect such a sale.

632. The Claimants relied in this context on the evidence of Mr Rahul Puri ("Mr Puri"), who was between May 2010 and September 2013 Managing Director of Innovation and Chief Software Architect at Prisa (based in Madrid). Mr Puri, who also gave evidence at the US criminal trial, stated that he only learned of Autonomy's agreement with DiscoverTech (VT30) in the context of that criminal trial, and had never heard of DiscoverTech before then. He stated that:

> *"DiscoverTech did not at any time contact Prisa and, in particular, did not attempt to license any Autonomy software or to sell any Autonomy services to Prisa. All of my interactions were with Mr Murray and his colleagues from Autonomy."*

633. Furthermore, Mr Puri added that the software licence which was the subject matter of VT30 would not have been of interest to Prisa. His evidence was:

> *"I have been shown a copy of the agreement between Autonomy and DiscoverTech. The software in question, including e-Discovery software, was of no interest to me or Prisa. I am confident that, if Prisa had made an acquisition of Autonomy software for a sum as large as $3.6 million, or had a need for such software, I would have known about it. Furthermore, I note that the only language listed in the agreement was English. However, this would have been of little use to Prisa. As I have already explained, the key languages from Prisa's perspective were Spanish and Portuguese."*

634. It was suggested to Mr Puri in cross-examination that Prisa would have been interested in a hosting platform that "*could handle litigation if it arose*". However, Mr Puri said that the initial purpose of the hosting platform was for Prisa's media assets and media content, not the back office. It was also suggested to him, giving as an illustrative example of standard needs of a large media group, an agreement between Zantaz and Sony Pictures Entertainment, which included a licence of Introspect (e-Discovery software). Mr Puri answered "*Depends on the company and depends on the need*" and rebuffed any suggestion that Prisa would need such software. There was no challenge to Mr Puri's evidence that Prisa's interest would, in any event, have been in Spanish- and Portuguese-language versions of the software.

635. As well as stressing their general point that the likely level of Prisa's interest was something for which, having purchased the software, DiscoverTech was bearing the risk,

[57] Adjusted for conversion of loan notes.

the Defendants contended that the Claimants' argument (a) inaccurately and unfairly characterised the deal with DiscoverTech which was not just for electronic discovery software and (b) was dependent on evidence from Mr Puri which overstated his involvement with the hosting part of Prisa's plans and should be treated with considerable caution.

636. As to (a) in the preceding paragraph 635, the software purchased under VT30 included not only e-Discovery software but also a complete "Archive Solution", which included Autonomy Consolidated Archive ("ACA"), Software for Microsoft Exchange, ACA Mail, Autonomy Legal Hold and Autonomy Investigator for use with ACA software. Mr Puri accepted that this package would, for example, have permitted archiving of emails: and it was not disputed that Autonomy was in discussion with Prisa about selling it archiving software (and indeed Mr Puri himself had been "supportive" of a deal which he knew Autonomy wanted to squeeze into Q1 2011). Further, Prisa's needs were broad-based: it was looking to consolidate all management and infrastructure across the group and had put out an RFP for a hosting platform for content. As Mr Puri accepted in cross-examination, this amounted to a *"platform migration for the whole of the Prisa infrastructure"*. Mr Puri also accepted in cross-examination that Autonomy continued to discuss a possible hosting deal with Prisa after the end of the quarter.

637. The Defendants added that even as regards the electronic discovery component of the sale to DiscoverTech, the Claimants' arguments were exaggerated. Prisa was (and is) a vast Spanish media conglomerate with, amongst other things, its own in-house legal counsel (included in the shortlist for The Lawyer's Global In-house Lawyer of the Year in 2018). Contrary to the evidence given by Mr Lucini in his witness statement, electronic discovery software was in principle a suitable product for a large media company (as exemplified by the sale of EAS Discovery to Sony Pictures Entertainment in 2007).[58] Prisa was always likely to be a good prospect for purchasing EDD software. In cross-examination, the furthest Mr Puri could go was to say only that litigation software was not the primary technology purchased by media groups (which is unsurprising), and he admitted that EDD software could be a normal thing to include, depending on the company and the need.

638. As to (b) in paragraph 635 above, the Defendants submitted that Mr Puri's evidence as to the scope of Prisa's hosting and archiving requirements must be treated with considerable caution: although when cross-examined in these proceedings he repeatedly sought to emphasise the importance of his role and his oversight of all aspects of what he called *"the transformation"*, it became clear that he was neither the decision maker nor an attendee at the key meetings relating to the transformation of Prisa's managed services infrastructure (the key decision maker, who controlled a separate budget, being a Mr Luis Garcia). Indeed, in the US criminal proceedings Mr Puri said he *"wasn't really interested in the hosting project"*; and he accepted that he knew at the time that Prisa *"was going through a process of looking at their managed services infrastructure, but I was not directly involved in the process…"*.

639. My impression of Mr Puri was of an eager witness who tended to overstate his involvement in areas of the "transformation" for which he did not have immediate responsibility. I do not accept his evidence that Prisa had no need for the software which was included within VT30; and I do not accept the implicit suggestion that Autonomy

[58] See also the sale of EAS Discovery to Fox Entertainment Group in 2008. EAS Discovery was another legal e-discovery product: see Goodfellow.

foisted on DiscoverTech software which it had no basis for thinking Prisa had any need, and thus built a reseller deal around a fabricated prospect. As Deloitte noted in their own review, the purchase of a suite of software including an archiving and e-Discovery solution is commonplace for a large firm operating globally with the ever-present threat of litigation. The commercial need for such software is all the more understandable in the case of a company with a traditional but global media business which was undertaking a transformation from analogue to digital and introducing new systems across its entire infrastructure.

640. However, even if there might have been some prospect of a sale to Prisa, the prospect would not have been realised by DiscoverTech but by Autonomy. As usual, and in accordance with the pattern, the VAR was not expected or intended to have any say or participation in the negotiations for a sale to the end-user, and all that was in contemplation was a direct sale by Autonomy. As to this:

(1) Mr David Truitt testified in his deposition in the MicroTech proceedings in the US that, at the time, he had never heard of Prisa, thus had no contacts with it, and (wrongly) believed it to be a New Jersey rather than a Spanish media company. Dr Lynch said he suspected that he (i.e. Mr David Truitt) *"knew very little about them."*

(2) Mr Puri's evidence in these proceedings that DiscoverTech *"did not at any time contact Prisa, and, in particular, did not attempt to license any Autonomy software or to sell any Autonomy services to Prisa"* was not challenged, and Dr Lynch told me he did not dispute it.

Was DiscoverTech let off the hook by funds from purchases by Autonomy?

641. The fourth strand of the Claimants' case on VT30 (see paragraph 595 above) was their allegation that although DiscoverTech did appear to satisfy its contractual payment obligation to Autonomy under the VT30 purchase order (despite there being no end-user sale), DiscoverTech was only enabled to do so by Autonomy making two purchases, first of a licence for and then further instances of software source code in respect of DiscoverTech's *"DiscoverEngine"* software[59]. (Those purchases also provided the funding to enable DiscoverTech to pay what it contractually owed under VT31 (see below), a VAR deal for end-user ThinkTech.) This strand of the Claimants' case requires something of a detour before I return to the main issue as to the overall propriety of VT30.

642. It may be recalled that the DiscoverPoint business, of which DiscoverEngine was a product, had been spun out of MicroLink before the acquisition of MicroLink by Autonomy. DiscoverEngine was a certified Microsoft SharePoint connector (SharePoint being a content management system produced by Microsoft). At the time of the spin-off, Mr Hussain and Mr Kanter advised the board of Autonomy in a memorandum dated 16 December 2009 that Autonomy's management did not believe there was *"a material business in DiscoverPoint"*, or at any rate that it was *"materially different from technology Autonomy already has."*

643. Autonomy's first purchase in respect of DiscoverEngine, of a licence, took place on 30 June 2011. The price for the DiscoverEngine licence, which Autonomy paid the very same

[59] Sometimes referred to as *'DiscoverPoint Engine'*

day, was $4,400,000 ("the Q2 2011 DiscoverEngine purchase"). The subsequent purchase of additional software and also the source code at a cost of $3,200,000 was in September 2011 ("the Q3 2011 DiscoverEngine source code purchase").

644. The Claimants' case was that Autonomy had no need for a licence to use DiscoverEngine, and certainly had no need to purchase the source code, since it already had its own offering of three different SharePoint connectors, including 'AIS Fetch' (which it owned through MicroLink), and that the purchases were in each case simply the solution arrived at as a means of channelling funds to DiscoverTech to enable it to settle its debt to Autonomy. Further, in light of the advice at the time of the spin-off, the amounts paid appeared over the odds.

645. It is necessary in this context to distinguish between (a) whether DiscoverEngine, as a product, had any utility (b) whether there was any real need for Autonomy to purchase it and (c) whether need for the product or the objective of putting the VAR in funds was the determinant of the price and the purchases at the times they were made.

First DiscoverEngine purchase: Q2 2011

646. The main thrust of the Claimants' case in relation to the Q2 2011 purchase can be summarised as follows:

(1) Especially given the assessment at the time of the spin-off of the DiscoverPoint business, to the effect that there was nothing in it *"materially different from technology Autonomy already has"* (see paragraph 273 and 642 above) some evaluation of the functionality of DiscoverEngine as compared to Autonomy's own products would be expected before making such a purchase and paying such a price. But it appeared to be accepted by the Defendants that none was conducted within Autonomy: there was no assessment made as to (a) how another third-party SharePoint connector differed from Autonomy's existing SharePoint connectors or (b) whether any such differences could readily be matched by making adjustments to one or other of those existing Autonomy connectors.

(2) The impetus for the purchase came, not from Dr Menell or anyone within Autonomy with knowledge of any potential advantages of DiscoverEngine compared with Autonomy's own similar products or of any technical shortcomings in the latter, but from Mr Hussain.

(3) The suggestion repeatedly made by Dr Lynch that the DiscoverEngine licence was specifically needed for specified Autonomy customers, namely, Bloomberg, National Bank of Canada and MetLife to solve a problem which needed to be solved, so that the purchase would be a prelude to a "sell-through" to them for commercial advantage, was untrue.

647. As to paragraph 646(1), the Claimants relied particularly on the evidence of Mr Greenwood[60], who, at the time of trial, worked for MicroFocus International plc as

[60] Mr Greenwood became "Head of Connectors" at Autonomy in 2005 and in the period 2005 to 2011 he had oversight of two connector teams, one in Cambridge (where he was based) and the other in Calgary, Canada. He reported to Mr Darren Gallagher, the Head of Development at Autonomy. The only member of Autonomy's senior management with whom he had occasional contact was Dr Menell.

"Connector Team Lead" and who started his working life as a software developer at Autonomy focusing on the development of what were then referred to as "fetches" and are now more commonly known as connectors.[61] There was no challenge to Mr Greenwood's evidence that (a) the Autonomy Connector was capable of evolution and did evolve in line with succeeding versions of SharePoint without difficulty (he estimated it would have taken only a week for his team to re-configure the 2007 version to be compatible with the 2010 version of SharePoint); (b) he conducted no evaluation of DiscoverEngine prior to its purchase from DiscoverTech and he was "*not involved in or aware of*" the purchase of a DiscoverEngine licence, had no contemporaneous familiarity with the product, and no knowledge of his own of it being used at any time during or after the Relevant Period; and (c) he was not aware of Autonomy having had any particular problem with Microsoft during the Relevant Period which might have affected his team's ability to develop connectors to SharePoint or any other Microsoft product, and they had the access they needed through a MSDN subscription. There was no evidence that DiscoverEngine was the subject of any evaluation by anyone else in Autonomy's technical department in June 2011 either. When Deloitte approached Dr Menell in July 2011 for an explanation as to the technical/commercial rationale for the DiscoverEngine purchase, he (Dr Menell) did not know what it was. Mr Welham stated in his email dated 19 July 2011 to Mr Hussain and Mr Chamberlain:

> *"Purchase of DT software – we talked to Pete M about this today but he was not aware of the technical/commercial rationale for the purchase. We need to understand this so that we can be sure that it makes commercial and technical sense and is at fair value."*

648. The Claimants also relied on that email, together with Mr Chamberlain's reply, as evidence that the impetus came from Mr Hussain (see paragraph 646(2) above). Mr Chamberlain responded on 20 July 2011 with the following explanation:

> *"Pete may not be the best person to talk to this. This related to the DiscoverPoint engine which was included in sales to Bloomberg, National Bank of Canada and Metlife. Sushovan can provide more background on the call."*

649. As to paragraph 646(3) above, Dr Lynch said in his first witness statement that Autonomy bought the DiscoverEngine licence "*for customers Bloomberg, National Bank of Canada, and MetLife*". That was also the understanding given to Deloitte. Deloitte were told that DiscoverEngine was needed for Autonomy customers; and when they reviewed the DiscoverEngine transaction, they noted that it was being sold through to customers and expensed to costs of sales (COGS).

650. According to the Claimants, the presentation that customers needed the specific functionality offered by DiscoverTech and Autonomy acquired that software to meet customer need was untrue. They contended that at the direction of Mr Hussain, Autonomy simply foisted the product onto customers by inserting references to DiscoverEngine into deals that Autonomy was negotiating in June 2011 in circumstances where the customer

[61] A "fetch" or "connector" is a tool which extracts data from one system and transfers it to another.

had no need for the product, or even any understanding of what the product offered or why it was being supplied. They gave an example as the MetLife contract.

651. Thus, on 17 June 2011, Mr Ivan Rothman, an Autonomy lawyer, said that he understood that SharePoint Connector (a mistaken reference to DiscoverEngine) needed to be added to the draft MetLife contract. Mr Sass, the salesman for the MetLife deal, said he had "*no clue what you are talking about*", prompting Mr Rothman to explain that it was his understanding that the connector should be given to MetLife (and Bloomberg) for free:

> *"My understanding is that Sush has decided we should give this connector to MetLife and Bloomberg (for free) as a way to promote this product. Hence, I was asked by [Mr Crumbacher] to include a reference in both documents. Do you have any objection to that?"*

652. Mr Sass replied saying that he would "*call Sush*". Later that day, Mr Sass confirmed that Mr Rothman could add DiscoverEngine to the MetLife contract (see paragraph 3712(4) in the main body of the judgment). Mr Rothman said he had "*added the language Sush requested re the connector (actually called "DiscoverEngine", not "SharePoint")*".

653. The Claimants relied additionally on an email dated 17 June 2011 from Mr Crumbacher to Mr Scott regarding DiscoverEngine, which added a new name to those to be provided with DiscoverEngine (Tracfone) and read as follows:

> *"FYI, information on the product to be inserted into MetLife, Tracfone, National Bank of Canada, and Bloomberg. Dave Truitt describes it as multi-tenant Sharepoint connector, and it's called "DiscoverEngine." Dave said he provided Sushovan with a proposal for reselling the product and wanted to send to me ... I told him that I wasn't told I'd be managing or even involved in that transaction, so he should hold off sending me anything with $$ in it.*
>
> *McCarthy has been made aware of its existence, so hopefully we'll minimize all the stress and wasted time his sky-is-falling response to third party software products would cause. Michael [McCarthy] did say that, when third party software is included, he has to [sic] the billing team know what the cost to us is, for commission purposes. Alex and Ivan are putting this into Bank of Canada, Bloomberg, and MetLife, and I'll put it in Hung's Tracfone schedule.*
>
> *Again, you might want to reconsider including Tracfone as one of the customers to get this connector. I don't see anything that has [sic] says "sharepoint'' to me in the call center and Explore software they licensed. In its place, we could consider Morgan Lewis (draft attached is Internal ediscovery software and already has a Sharepoint connector, LF $1.1M), and if Morgan's a no-go, I can do some research to come up with others. But, since Sushovan asked you, personally, to come up with the customers and since I don't know what criteria were given in choosing them, I'll follow your lead."*

654. The Claimants submitted that Mr Crumbacher's email makes clear that he, a lawyer, had been tasked with plucking customers out of the air on whom DiscoverEngine could be foisted, as distinct from responding to any customer demand or need for that software. Dr Lynch maintained in cross-examination that Mr Crumbacher's email "*may be the understanding of the lawyers sitting in San Francisco but it's not the basis on which this is being done*". The Claimants dismissed this too as inherently implausible.

655. The pattern continued with an email dated 24 June 2011 from Mr Hussain to Mr Scott reminding him to ensure DiscoverEngine was included in a number of deals "*particularly MetLife and BB [Bloomberg]*". Mr Hussain asserted also that "*UBS definitely need it*"; but the need was not explained and there is no document that indicates that Mr Hussain had been prompted to say this by some input from the technical department, the sales team or from UBS. In an email the same day (24 June 2011), Mr Crumbacher instructed Ms Julie Dolan (an Autonomy lawyer) to include DiscoverEngine in the UBS deal because "*Sushovan has asked*".

656. To this the Claimants added a number of other examples (including a potential contract with Xerox which the Claimants put forward as particularly striking) showing, as they contended, that DiscoverEngine was being inserted into draft contracts, willy-nilly, at the dictation of Mr Hussain, without any request from the customer, or even any understanding, whether on the part of the customer or the salesman, of its use and still less need.

657. The Claimants' punchline in this context was that it could not be clearer that, in and after June 2011, Autonomy was, on Mr Hussain's instruction, including DiscoverEngine in draft contracts with customers, regardless of customer demand or technical need; and that this strongly suggests that Autonomy's reasons for purchasing the DiscoverEngine licence were <u>not</u> based on a genuine customer need. Mr Hussain was insisting that DiscoverEngine be included in customer contracts, despite the absence of demand for its functionality, in order to justify the purchase (on a false basis) to Deloitte.

658. The Claimants further submitted that it also follows that Deloitte were misled. Deloitte's understanding was that DiscoverEngine was needed for the three Autonomy customers (Bloomberg, National Bank of America and MetLife). Deloitte was not aware that DiscoverEngine was inserted gratuitously into IDOL licence sales to customers who had no interest in it.

659. Likewise, the Claimants submitted that the Audit Committee was also misled in the same way. Mr Bloomer's evidence was as follows:

> *"Q. So you were told that Autonomy paid this $4.4 million because it needed DiscoverPoint to complete IDOL licence sales to Bloomberg, National Bank of America and MetLife, yes? Sorry, National Bank of Canada and MetLife, yes?*
>
> *A. Yes.*
>
> *Q. And that was your understanding at the time?*
>
> *A. Yes.*

Q. You were told that those three customers required DiscoverPoint, yes?

A. As part of the product, yes.

Q. And that's what you understood?

A. Yes.

Q. If it was the case that those three customers did not need DiscoverPoint, that would have been contrary to your understanding at the time, yes?

A. If that was the case, yes.

Q. If, for example, DiscoverPoint had simply been inserted into the contracts with those three customers, without any suggestion that the customers needed or wanted it, you would have wanted to understand why Autonomy was paying $4.4 million for DiscoverPoint, yes?

A. Yes, and given again Deloitte's commentary down below that they specifically looked at the rationale and the linkage with the sales above and discussions with the group's chief research officer, et cetera, given your presumption or assumption, the conflict between those."

660. The Defendants painted a very different picture, though (to carry on with the metaphor) Dr Lynch retouched the painting markedly in the course of cross-examination. Initially, they presented DiscoverEngine as a substantially superior product in terms of functionality and efficiency to anything Autonomy could offer or was likely to be able to offer without considerable further diversion of resource and delay. They emphasised also the importance of the fact that it was a Microsoft-certified connector, with a materially higher level of encryption.

661. They dismissed the notion that it was comparable to Autonomy's own connectors, and explained the views expressed at the time of the spin-off as in effect overtaken by subsequent events and developments. They pointed out that in June 2010, before either of the impugned transactions, Autonomy had in fact entered into a *"Software Distributor Agreement"* giving it a 3-year renewable licence to copy, install and integrate DiscoverPoint, including DiscoverEngine, within a *"Bundled Module"* (defined as *"Autonomy's software products which incorporate some or all of the Licensor's Software Products"*) and it should be assumed to have been considered useful. They asserted (it was not clear to me what the evidential basis was, and none of this appeared in Dr Lynch's witness statements) that *"…the DiscoverTech business and DiscoverEngine product had obviously developed significantly since its early stage status in Q4 2009. It had acquired other customers by 2011".*

662. When taken to the Rothman/Sass exchange (see paragraphs 651 to 652 above) in cross-examination, Dr Lynch asserted that this *"is another example of looking to the wrong area for understanding things"* and that this email was between people who "*really have no idea what is going on*" (though, as the Claimants pointed out, Mr Sass was the

salesperson who was dealing directly with MetLife[62] and the exchange was between a salesperson and a lawyer, suggesting little reason to doubt that these individuals understood what was going on).

663. In cross-examination, Dr Lynch shifted the explanation towards the need being driven, not by customer demand, but by Autonomy's appreciation of inadequacies and frailties in its own offering and the resulting need to make available a more satisfactory replacement. On this revised version, the Defendants contended that:

(1) The decision was largely based on the perception of an urgent need to catch up with the huge growth in popularity and use of SharePoint and to provide Autonomy customers with a certified, encrypted, and working connector in place of a product which was not certified, had deficient encryption, and which Autonomy recognised had quite serious deficiencies and problems which Autonomy had tried, and over some time failed, to resolve (as above described). For example, and as the Claimants did not dispute, if a customer wanted to index its cloud-based SharePoint system (then called BPOS), it needed a Microsoft certified connector. Certification was a long process and Autonomy had never achieved it. Autonomy needed a quick fix to provide functionality and certified and encrypted connection to SharePoint that customers needed, without the risk of customer complaint and dissatisfaction: DiscoverEngine offered it.

(2) Further, according to Dr Lynch, a confidential fact, which was not appreciated by the salesmen or the lawyers at Autonomy, and which Dr Lynch had never mentioned before, was that Autonomy's own offering had been hacked. This concern was compounded by the fact that (a) it had not been certified for connection to Microsoft; (b) any damage caused to a customer's software or equipment would not be covered and (c) MicroLink's security clearance could be put at risk.

(3) Dr Lynch accepted that prior to the licence purchase there was no formal "buy versus build analysis"; but the reality was that Autonomy had problems with its own connector which over a considerable period it had tried and failed to fix. Further, the aged architecture of that connector would have had to be replaced, with substantial consequential delay. Dr Lynch stressed that DiscoverEngine was a very different product, with (for example) *"efficiency ratios of the fetching of the two products which [were] phenomenally different"*; but he summarised the real problem as being that:

> *"We can keep going on for a very long time down into the weeds and the minutiae on this one, but the simple – to bring it back to the simple level, Autonomy's SharePoint connector was not fit for purpose and was likely to have Autonomy put in a position of significant liability due to data loss or missing regulatory information."*

[62] The Claimants pointed out also that Mr Sass is a current Darktrace employee, and that he was not called as a witness by Dr Lynch so as to offer a different explanation for what they submitted was the plain meaning of this email exchange.

(4) According to Dr Lynch's evidence, Autonomy wished to overcome this problem by moving its customers off its own product and onto DiscoverEngine, analogous to repairing a faulty part:

> *"What we were trying to do was quietly move over to something that was quality and worked and was tested and would deal with that problem…"*

(5) Dr Lynch accepted that he did not, when approving the first purchase on the basis that Autonomy was selling DiscoverEngine through to Autonomy customers, mean that he understood there to be purchase orders for the product; he understood Autonomy to be meeting known customer requirements for a working connector and did not expect that customers would have been asking for DiscoverEngine specifically. His understanding was (and he stressed that he was not involved in the negotiations nor in any technical assessment of DiscoverEngine) that there were existing customers of Autonomy which wanted a SharePoint connector with full access, and that DiscoverEngine would be supplied to them as (a) the best functioning product that Autonomy could supply and (b) as a substitute for an Autonomy product which had potential flaws as explained above. He did not regard it as either surprising or problematic if (as he suspected) Mr Hussain had gone down the list of everyone who had been supplied with Autonomy's own connector with a view to providing DiscoverEngine instead. He rejected the Claimants' allegation that DiscoverEngine was, at the instance of Mr Hussain, provided *"willy-nilly"* to customers for nothing to give a false appearance of its profitable deployment at the customer's request.

(6) The Defendants relied on the evidence of Mr David Truitt in the US criminal trial to the effect that DiscoverTech was offering the licence at what Autonomy's management perceived to be a substantial discount representing a very good price. Mr David Truitt also explained that Autonomy purchased the instances of DiscoverEngine at a much lower price than other purchasers, and as the manufacturer of the software that DiscoverEngine supported, Autonomy could sell to all its customers:

> *"So to give you some perspective, though, we sold to Glaxo and to Lockheed Martin -- an instance cost $25,000. The deal that we ended up cutting with Autonomy averaged $5,000 per instance.*
>
> …
>
> *Not only did they get a good deal, but they were not any other customer. They were the manufacturer of the software that we were trying to support. So they had all of the Autonomy customers that they could go and give this solution to."*

664. In relation to (1) and (2) in the preceding paragraph, it is, I think, worth quoting Dr Lynch's explanation in full during the course of his cross-examination:

"If I could explain what this is all about. So Autonomy had a connector basis, which connected to a thing called SharePoint. SharePoint was a Microsoft product and, unlike most corporate IT where the system is set up by IT centrally and run by them SharePoint was a product that ordinary people could set up in a department without having to go near IT.

So at this time there was an absolute explosion in SharePoint because people in companies were tired of waiting for IT to do things and it didn't work, so SharePoint became a major movement in the industry and appears everywhere. And suddenly our customers have a big problem in that when they get a legal investigation, they have an obligation to bring all the documents that are relevant to the court or the Senate, or whatever. And that's relatively easy when you have a system that's run by IT and that you know where everything is and you go there and you get it.

But with SharePoint the problem was that there were vast numbers of these things. So you may recall Mr Lucini when he was talking about it talked about a SharePoint forest. Some people talk about weeds or a forest, but the idea is vast numbers of these things everywhere. And in order to meet legal requirements you've got to go and look at all of them.

So it was a big problem. The difficulty we had was our own SharePoint connector, which was what was going into this arrangement, had some difficulties in that it had been hacked and we'd had a little scandal that we'd managed to keep under control of it being a security risk. It was also not certified, which meant that if it did any damage to the customers' systems, then – well, technically it wasn't allowed to be used by the customers and it also wasn't encrypted.

Then it also had another problem, which it was highly inefficient. So that the SharePoint connector that we had could only do – go to a place, get everything and bring it all back. And whilst that's okay when you've got a centralised system, with SharePoint it means that you've got to go everywhere and bring everything back. So even though you might only want documents about this particular employee who was fired, say, for a legal matter, you have to bring back every document in the company centrally and it meant that it took a horrendous amount of time and slowed the network down.

So we had a whole series of issues that we were quietly trying to clear up here, and the idea was that we were going to drop in our – take our faulty product and supply these customers with the new one and was certified and thus avoids the problems.

The product was much better and didn't have the problems which we had which were pretty fatal, actually."

665. To this he added later in his cross-examination, when asked whether Autonomy could not have completed IDOL-based sales without this product, the following:

> *"I don't think so. I think taking into account the efficiency issue, I think we'd have had very, very unhappy customers if they were trying to backhaul SharePoint on the size that these people were thinking of doing it, using our technology. And that's before you take into account the liability we'd have had if we'd put in the insecure product and then they'd been hacked. Imagine MetLife, an insurance company, if all its customer data had been extracted through our leaky SharePoint connector. We'd have had a major issue on our hands.*
>
> *So we were very happy to quietly shift everything over to something that was reliable and secure."*

666. As to the price paid, Mr David Truitt's evidence explained that he considered that Autonomy made a good deal on the software and purchased it for much lower than the price that was offered to other customers. The Claimants did suggest that the number of instances sold by DiscoverTech was not enough to establish a market price. That would not be sufficient to justify an allegation that the transaction was not at fair value. Nor did the Claimants suggest that Dr Lynch knew that there was (allegedly) no market price. Dr Lynch rejected the suggestion in any event. Mr David Truitt expressed the view that there was an established price and that Autonomy had received a good deal.[63]

667. In my judgment, however, and even though I accept that DiscoverEngine was a potentially useful connector, what had driven the purchase was the need to fund DiscoverTech so that it could pay down its debt to Autonomy.

668. No documentary evidence was put forward to support the new suggestion of flaws, inadequate security and hacking issues; and very little, if any, of this was in Dr Lynch's witness statement. It was put to him that as he could so easily have explained that his case was that Autonomy's SharePoint connector was not fit for purpose and was likely to expose Autonomy to complaint and liability, his failure to do so suggested that it was an afterthought (with an implication, though the cross-examiner's challenge faltered, of unreliability at best). Dr Lynch retorted that the claim against him was not particularised in this aspect, and in any event, he had since collated other views and been able to set out in more detail why the decision was made. He added that he had sometimes had difficulties in understanding the true extent of the claim *"because it diverges from the reality that I know…"* and was unsure what detail to put in to answer it. He suggested, a little sardonically, that the next time he did a witness statement he would *"try harder to put more and more detail in"*. This was not convincing.

669. The notion that there was an appreciation within Autonomy of flaws and a history of hacking of a particular product without there having been generated any customer complaints, nor any report by Autonomy or any other documentary evidence of a cyber security breach, is not an easy one to accept. That is especially so given the delegation of

[63] See paragraph 4504(6) above. See also David Truitt's evidence: "*A: We could certainly sell and did sell to other customers. We had sold prior to that to customers, and that software was more valuable to Autonomy because they had the customers. It was built for Autonomy technology. So they could distribute that software to thousands of customers. So it was very valuable, in my opinion, to them*."

the task of identifying customers which might need or be interested to Mr Crumbacher and Mr Scott, who were not in a position to know (see paragraph 653 above).

670. Further, examples given by the Claimants of the reaction of a customer and/or a salesman to being told that DiscoverEngine was to be included in the deal struck me as telling. I have referred in paragraphs 655 to 656 above to certain customers; another related to the Tracfone contract mentioned in paragraph 653 above. When on 20 June 2011, another Autonomy lawyer, Mr Hung Chang, was negotiating the contract with Tracfone (see paragraph 653) he mentioned to the relevant sales executive (Mr Dipan Patel) that he understood that *"we are adding some kind of Discovery Engine to the PQ"*. Mr Patel answered that this was news to him, and that he had no idea what it comprised or why it would be included. Mr Chang responded that he too would be interested to know *"as it was a directive from Sushovan."* When Mr Patel enquired more widely about DiscoverEngine, none of his sales colleagues knew what it was either and thought it must be a mistake.

671. It is also interesting to compare the price agreed by Autonomy in June 2010 under the Software Distributorship Agreement (see paragraph 661 above) which was $224,000 for up to 5,000 users with that to which it committed under the Q2 2011 purchase of $5,500 per instance up to 800 instances.

Second DiscoverTech purchase (Q3 2011): source code

672. In Q3 2011, Autonomy purchased additional *"instances"* of the DiscoverTech software[64] and also what Dr Lynch described as a *"pared-down version"* of the source code for $3.2 million. These purchases coincided with an urgent need for Autonomy to tidy up its books and obtain payment or other discharge of any debts owed to it prior to completion of its imminent acquisition by HP.

673. In the US criminal trial, Mr David Truitt testified that these further purchases arose out of a discussion he had with Mr Hussain following the announcement of HP's acquisition. The discussion related to DiscoverTech's various outstanding contractual commitments (including in respect of VT30 and VT31). Mr David Truitt's evidence placed the second purchase firmly in the context of the need to find a way to discharge those commitments. He said:

> *"…we had a discussion regarding potentially more instances of our product, which would enable me to then pay down some of that obligation.*
>
> *They did go back, and over a period of a week or two, they determined, you know, how much more they could buy, and we did a few more of those purchases over the next month or so."*

674. The original proposal from DiscoverTech for this further transaction had been for a purchase of the product itself, with unlimited distribution rights, for $10.35m. The document explained the commercial basis for this:

[64] An *"instance"* means the number of servers on which the software could be run.

> *"Autonomy is currently authorized to distribute one copy of DiscoverEngine for each copy of IDOL server shipped to Autonomy customers as well as existing IDOL customers under Autonomy annual support. Autonomy's current purchase price for DiscoverEngine is at an average price of $2,700,000 per 500 hundred instances plus an annual maintenance fee of $270,000 dollars for each bundle of 500 DiscoverEngine instances. Discover Technologies is offering to sell to Autonomy the DiscoverEngine product and allow unlimited distribution as an Autonomy owned product for $10,350,000. Autonomy's IDOL software exists in hundreds of thousands of environments throughout the world. The purchase of the DiscoverEngine product under the proposed terms will allow Autonomy to significantly reduce its costs to distribute the DiscoverEngine while providing value to a larger segment of Autonomy's customer base."*

675. A review of the software was undertaken by Mr Lucini and Mr Chen (an Autonomy systems engineer). Dr Menell summarised and forwarded their findings to management. Their assessment was fairly low-key:

> *"Basically if we wanted to [purchase] it could be used within the Control Point suite as part of data triage and set up. Its [sic] workmanlike and utilitarian so difficult to get enthusiastic about…Does what it says on the tin even if it's a dull tin. We could obviously do this but would need to drop other more important pushes."*

676. The assessment did not mention the existence of Autonomy's own SharePoint connector and contained no analysis of any similarities or differences between that and DiscoverTech's product, even though on Dr Lynch's argument that was the main task. As in the context of the first purchase, there was no mention of any problems such as hacking, or customer dissatisfaction with Autonomy's own product. Nor was there any mention of any experience that Autonomy might have garnered from its first licence purchase.

677. Mr Lucini accepted that when first instructed he was asked to identify what overlap there was with Autonomy's own products, but that this was soon cut down by Dr Menell simply to assessing its utility. No assessment of the comparative time and cost to develop Autonomy's own product appears to have been undertaken either. The Claimants submitted that this was because Dr Menell had warned Mr Lucini off a comparative approach knowing that it would undermine the rationale for any purchase. Mr Lucini's line was that (a) he had not been asked to assess and comment on any overlap with Autonomy products and did not do so, and (b) in fact in a conversation after an initial brief, Dr Menell had given express instructions, which he felt he had to accept, that the assessment should not make any *"head-to-head"* comparison with Autonomy's own products. The fact that such a comparison seems obviously necessary and yet there is nothing to suggest that Dr Menell or Mr Hussain thought that the report was deficient, or that Mr Lucini had not done what was required of him, gives credence to Mr Lucini's version of events in this respect.

678. However, the Defendants submitted that there was nothing to support this subsequent alleged instruction, and that Mr Lucini had invented it. The Defendants argued that, on the contrary, it was because it was clear that DiscoverTech did offer advantages over

Autonomy's product, and certainly did not duplicate it: they suggested that if the field engineering team and Mr Lucini had thought the product simply replicated Autonomy's own product they would surely have said so. The Defendants' case is that Autonomy's technical engineers gave independent and objective consideration to the second purchase and confirmed to Autonomy that DiscoverEngine was a useful and valuable source code to buy.

679. In an email on 15 September 2011 to Dr Lynch and the rest of the core management team in response to Dr Menell's confirmation of the product's utility, Mr Hussain suggested that he was thinking of a price of between \$8m and \$10m for the source code (i.e. a discount from DiscoverTech's proposal), or a purchase of more limited software for \$6m. Dr Lynch responded, "*that is too much*". Mr Hussain replied, thanking Dr Lynch *"for the direction"* and stating that he would negotiate, he believed Autonomy were in a strong position, and he would aim for below \$2 million. This extreme and off the cuff reduction in the price to be offered, and especially (a) Mr Hussain's alacrity in moving from his initial estimate to one which was one-fifth of it, and (b) Dr Lynch's suggestion of the lower price without any explanation, suggests to me that the price they determined to offer was calibrated according to some more general considerations than its list price or true value. It also suggests a certain confidence that Autonomy would not be rebuffed.

680. Emails ensued as follows:

(1) On 21 September 2011 Mr Hussain emailed David Truitt, stating:

> "*Hi Dave – technical have evaluated and we want to buy but we can only pay \$1.6m"*.

(2) On 23 September 2011 Mr David Truitt provided a revised proposal. The new proposal stated that: "*We have reduced our price significantly down to 3 million dollars and have reduced the components of the DiscoverEngine solution accordingly*".

(3) Mr Truitt went on to explain what was now included and not included in the new proposal. His email made clear that key points from the earlier proposal were still present (including all the points highlighted by the field engineering team and Dr Menell), concluding: "*The value proposition is still compelling in that the ability to distribute to SharePoint 2010 customers as well as leverage our Microsoft certification is still included*".

(4) On 26 September 2011 Mr Hussain forwarded the revised proposal to Dr Menell and Mr Scott, saying "*we are prepared to pay \$1.7m max*". Dr Menell said in response to this that "*price is a commercial call I can't really advise"*, but did not dissent from Mr Hussain's approach, and gave a positive indication of the potential market for the product.

> "*It's very dull but Rafiqs point about Open Deploy, bank of America and the utility space is the market for something simple, done well and with a compliant slant is large especially if coupled with an umbilical cloud distribution channel as large as ours (which by the way and needless to say I imagine is only going to get dramatically bigger with HP!)*".

(5) On 27 September 2011 Mr Scott requested approval from Mr Hussain, Mr Kanter and Mr Chamberlain for the purchase of 285 additional instances of DiscoverEngine for $1.5m. Mr Scott explained that most of the prepay had been used up and that Autonomy needed to purchase additional volumes for the customer deals it was tracking.

(6) On 27 September 2011 David Truitt gave Mr Scott DiscoverTech's "*best and final proposal*" for the source code sale. This stated:

> *"Our price has been reduced to 1,700,000 dollars contingent on Autonomy purchasing an additional 285 instances of the DiscoverEngine for resale distribution under our current Software Distributor Agreement prior to 9/30/11."*

(7) On 27 September 2011 Mr Scott forwarded DiscoverTech's updated proposal to Dr Lynch, Mr Hussain and Dr Menell. The email made clear that DiscoverTech had reduced its price for the source code from the $3m proposal, in consideration of the fact that Autonomy was purchasing the additional instances of the software. The email also indicated that Autonomy had customers for the additional purchases. It should be noted that the additional instances would be of the full DiscoverEngine product in a form ready to be shipped to customers. The source code that Autonomy was purchasing was more limited or *"pared-down"*, following the reduction of the scope of the sale explained in David Truitt's email of 23 September 2011.

(8) Dr Lynch approved the purchase in response to Mr Scott's email, saying "*ok this is much better*".

681. Mr David Truitt's evidence with regard to the sale of the source code was that this was something he "*wasn't a big fan of doing*" because his company was selling its know-how; but he felt he had no alternative. He said:

> *"So effectively I had to give up a product that we had built and that, you know, had high hopes for, but, you know, I was willing to do it because we were able to clear our debt.*"

682. Dr Lynch summarised the position as he understood it at the time in his first witness statement:

> *"296. Autonomy bought a pared-down version of the source code, which did not include all DiscoverEngine functionality, for a competitive price. The price was further discounted because Autonomy agreed to purchase additional instances of DiscoverEngine around the same time. It made commercial sense to purchase the additional instances because Autonomy had used up most of its prepaid instances, but still had customers interested in the functionality offered by the product. The additional instances included all DiscoverEngine functionality (unlike the source code Autonomy had purchased) and it could be shipped to customers immediately.*

> *297. The UK management team approved these purchases. I gave the final approval. I approved the purchases because I understood that we needed the product and was informed that we had customers lined up to which we could sell it. In my opinion, these purchases were in Autonomy's interest and we exercised sound commercial judgment in buying the DiscoverEngine software. We were able to sell the products on to customers."*

683. A considerable time was spent on the competing submissions as to the utility of DiscoverPoint and its source code, and as to whether Autonomy might itself have developed its own enhanced and improved product. The Defendants also criticised the Claimants for muddling the two purchases, and also for failing to be clear as to what part of the purchase price of the Q3 2011 purchase related to instances and how much to the source code.

684. I do not think either criticism alters the analysis; and I do not consider it necessary to go through this evidence: as it seems to me, what the Defendants' justification came down to was the simple but substantial point made by Dr Lynch in cross-examination that, irrespective of specific request or individually identified need, Autonomy naturally wished to provide customers who asked for a SharePoint connector with the best functioning connector that Autonomy could supply, and that was not its own connectors but DiscoverEngine. No specific customer request or need was on that basis necessary, and nor was any sale of the connector since it would simply be included as "best of breed" in the overall solution sold; as Dr Lynch put it in one of his many analogies in the course of his cross-examination:

> *"They didn't request it. DiscoverEngine is a very technical piece of software that solved a particular problem. Those customers needed that problem solved but they didn't – it's a bit like you buying a car. You don't request a carburettor, but you have to have a carburettor in order for the car to go. So it was a necessary piece of technology for what these people wanted to do."*

685. The problem from the Defendants' point of view was the lack of evidential underpinning for this explanation. Furthermore:

    (1) This explanation was not the same as or even consistent with that given by Dr Lynch in his witness statement, which was very much based on sales of the connector to satisfy individual customer specific requirements. As Dr Lynch put it in his first witness statement:

    > *"I approved the purchases because I understood that we needed the product and was informed that we had customers lined up to which we could sell it"*;

    (2) Whilst the explanation might have covered the first purchase of a three-year renewable licence, it was difficult to fit with the second purchase of further 'instances' for customers which were never identified;

(3) Although Dr Lynch advanced theoretical justifications for preferring a buy-in (diversion of valuable talent and delay) these seemed to me insufficient to explain why Autonomy did not develop its own enhanced connector, especially given Autonomy's avowed policy of supplying its own products if at all possible;

(4) No coherent explanation was offered as to the basis on which Autonomy sought to include (for free) the DiscoverEngine connector rather than any of its own in solutions for customers: Dr Lynch suggested that this was primarily driven by Dr Menell who had the expertise, but there is no support in the evidence for that suggestion, and the signs are that it was driven by Mr Hussain, who had no such expertise and whose eyes were on the financial objective of clearing outstanding indebtedness; and

(5) The lack of any paper record of (i) complaints or concerns about Autonomy's connectors and (ii) why it would be better to buy in, added to the impression that the second purchase, like the first, was driven primarily by some other consideration.

686. In summary, my conclusions on both DiscoverEngine purchases are as follows:

(1) DiscoverEngine was a serviceable product, probably superior to Autonomy's and advantageous to customers because of its certification.

(2) But Autonomy did not need it: I do not accept Dr Lynch's evidence that the frailties of its own product were such that Autonomy had to substitute DiscoverTech in its place irrespective of customer demand or identification to them of any issue.

(3) The price was excessive, in comparison to (a) the likely costs had it needed to develop its own product (including any costs of diverted software expertise), (b) what Autonomy paid for its June 2010 licence and (c) the value placed at the time of the spin-off; and it seems clear that it never did sell on to customers who had a genuine need / had requested it.

687. As in the case of the first purchase (see paragraph 645), it is necessary in this context to distinguish between (a) whether DiscoverEngine, as a product, had any utility (b) whether there was any real need for Autonomy to purchase it and (c) whether need for the product or the objective of putting the VAR in funds was the determinant of the price and the purchases at the time it was made.

688. In short, I have concluded that the predominant driver for both purchases was the need to assist DiscoverTech; it was the method selected to achieve the objective in a way which could be presented in such a way as to pass muster with Deloitte and the Audit Committee, and albeit contrived (in the sense that but for its true primary purpose it is unlikely that Autonomy would have entered into it) it was not fanciful (in that DiscoverEngine was useful and could be presented as being so).

My assessment re VT30 and the DiscoverEngine purchases in the round

689. Having come to the end of that detour, I turn to my assessment of the Prisa (VT30) VAR transaction as a whole.

690. In my view, VT30 was typical of Autonomy's deals with DiscoverTech, demonstrating what was by early 2011 Autonomy's almost automatic recourse to a 'friendly' VAR to cover revenue shortfalls in a quarter:

    (1) There was no other purpose in the introduction of a VAR, and DiscoverTech in this case, than to book recognised revenue; and it was never expected or intended that the VAR should have any active part to play at all, nor even that it would be a contracting party to any ultimate sale to the prospective end-user.

    (2) The VAR (in this instance, DiscoverTech) never acquired any autonomous control of the software notionally licenced to it. Any onward sale would be negotiated and (if the negotiations were successful) closed by Autonomy. The VAR was dependent on Autonomy for both reimbursement and reward.

    (3) The DiscoverEngine purchases, despite their factual complications, had the simple predominant objective of making good Autonomy's commitment to DiscoverTech (as to all its 'friendly' VARs) to see to it that they were not left 'on the hook'. The fact that the purchases may well have had other legitimate purposes demonstrates no more than that the 'rescue' transactions were well chosen to obtain approval from Deloitte and the Audit Committee.

    (4) In consequence, the role of the VAR (DiscoverTech in this case) was nominal: there was no real transfer of risk or control, which was in reality retained by Autonomy.

691. In my judgment, recognition of revenue from VT30 was improper.

692. The backdating of the VT30 VAR agreement was an additional but egregious (though not unique) impropriety. The email exchanges between Mr Hussain and Mr Chamberlain relating to the possible deferral of revenue (see paragraphs 619 to 621 above) demonstrate also that by that time, Mr Hussain and Mr Chamberlain (at least) were prepared to allocate revenue flexibly in the week or so following quarter-end. This echoed similarly improper manipulation of revenue as in certain of the hardware sales, and further demonstrates what in my judgment is the impropriety of VT30 as a whole.

Defendants' knowledge of and participation in VT30 and backdating

693. In my judgment, the use of 'friendly' VARs, and in the Prisa case, DiscoverTech, for this purpose was well known to the core management group in Autonomy and in particular not only to Mr Hussain but also to Dr Lynch. They also knew that if no end-user sale eventuated, Autonomy would need somehow to finance or absolve the friendly VAR.

694. I have also concluded that both Defendants knew that the DiscoverEngine purchases were devised as the means of financing DiscoverTech.

695. The position against Mr Hussain is reasonably clear; he was directly involved.

696. Dr Lynch was at one remove. However, he did approve both purchases. I have concluded that (a) this is something on which Mr Hussain would have forewarned and consulted with him about and (b) his one-line approvals without feeling the need for any further enquiry, coupled with the quite extraordinary grasp of the detail of which he manifestly was capable, and his exceptionally close control of the company, suggest that he was aware of the true drivers of the purchases. I think it is more likely than not that he knew enough to know that the purpose of the purchases was predominantly to fund DiscoverTech to enable it immediately to pay down its debt and enable Autonomy to take DiscoverTech's outstanding indebtedness off its books.

697. Neither Mr Hussain nor Dr Lynch can have thought this use of VARs to be a proper basis for recognising revenue from delayed and inherently uncertain deals.

698. In my judgment, both Defendants knew that the sale in VT30 lacked substance and in reality transferred no risk or control of the software. Both Defendants had "guilty knowledge" of the accounting impropriety accordingly.

Defendants' knowledge of backdating

699. Mr Hussain's defence to the allegation of backdating of VT30 was not that he did not know but that the Prisa deal was amongst the 'slate of deals' approved on 31 March 2011, and that the documentation properly memorialised the earlier agreement.

700. However, I have held that the Prisa deal was not on the 'slate': see paragraph 612 above, and the question therefore is whether, on a balance of probabilities, Mr Hussain knew that. I consider it more likely than not that he did.

701. I consider also that Mr Hussain's email to Dr Lynch of 11 April 2011 presenting a choice whether to *"defer Prisa"* (see also paragraph 616 above) some two weeks after the end of the quarter demonstrates that Mr Hussain was willing to adjust the record to reflect whichever option was agreed, and it would have fallen to him to arrange whatever needed to be done, even if the doing of it was delegated.

702. In the round, I have concluded on the balance of probabilities, that Mr Hussain was aware of and probably directed the backdating of VT30.

703. In considering the position of Dr Lynch it is necessary to take full account of the fact that he was involved in the mechanics of the deals much less than Mr Hussain was, even though (as I have found) he was aware of the strategy and its impropriety.

704. In his closing submissions Dr Lynch dismissed the claim that he was knowingly involved as *"more forensic froth"* and contended that the exchanges between Mr Hussain and Dr Lynch did not identify any knowledge or involvement on Dr Lynch's part in the terms of the deal, and certainly did not identify any knowledge of backdating or involvement in it. Insofar as they sought to rely on the email (see paragraphs 619 to 621 above) from Mr Chamberlain to Mr Hussain of 12 April 2011 (as they had in opening, but seemed only elliptically to do so in closing) Dr Lynch made the point that none of it had anything to do with backdating and he was not in any event a party to it. He suggested further that neither he nor Mr Hussain had any motivation to backdate the Prisa deal, because *"the contemporaneous documents show that there was no shortfall in revenue"*. By contrast Mr Egan had a plain motive because he had:

> *"missed his target…So I think this is more likely the case that Mr Egan, for whatever reason, didn't get the paperwork done when he should have done and then realised he was going to miss his personal number and did the number."*

705. That does not seem to me adequately (or at all) to explain Mr Hussain's email to Dr Lynch of 11 April 2011 (which I have quoted in paragraph 616 above)[65] nor why, almost two weeks after the end of Q1 2011, Mr Hussain was discussing with Dr Lynch whether revenue should be reported for Q1 2011, as though this was discretionary, and in circumstances where there was no documented deal between Autonomy and the end-user at that time. That presupposes that according to the option elected there may be a need to demonstrate earlier revenue recognition. The later emails of 12 April and thereafter, which I have also referred to earlier, seem to me also to reinforce the likelihood that Mr Hussain and Dr Lynch were not troubled by the actual factual sequence in determining whether or not to "defer" Prisa. Dr Lynch's evidence that Mr Hussain would not have *"operated in that manner"* (that is backdated documents) needs to be considered in that light.

706. Dr Lynch's justification for his own acceptance that the question whether to recognise revenue in Q1 2011 from VT30 was even in April 2011 still elective or optional was that these were typical matters of judgement that had to be made (for example, if doubts had emerged about the VAR's credit-worthiness, or as to whether all acceptance criteria had been met) in the immediate aftermath of every quarter. But although I have accepted the necessity and commonplace nature of the process in general terms I have not felt able to accept that it explains the emails. I consider that Dr Lynch was aware that Mr Hussain would take steps necessary to ensure recognition of revenue or not according to the election made, and that this would depend on whether the revenue was needed in the previous quarter to make up a shortfall, or was better reserved for the subsequent quarter.

707. In such circumstances, although it may well be that Dr Lynch did not know how the election would be documented, and it is possible that Mr Hussain did not refer back to Dr Lynch before finalising that (the die having already been cast), I cannot accept that Dr Lynch was not aware that the decision was going to be made on the basis not of chronological truth but revenue need, and that if the latter prevailed, any documentation of the decision would be false.

VT31: DiscoverTech/ThinkTech Q1 2011

708. In March 2011, Autonomy was seeking to conclude a transaction with the brokerage firm TD Ameritrade ("Ameritrade"), for which the contracting end-user would be its subsidiary, ThinkTech, Inc ("ThinkTech"). The desired transaction was an amendment to ThinkTech's existing Digital Safe hosting arrangement so as to add a licence for Zantaz Supervisor (S6).

[65] *"If we defer prisa then we are at 218.1m but 24c and 85% [gross margin]. If we don't defer prisa but defer equiv low margin we are at same revs but now at 25c and 88%. To discuss when I land or you can discuss with steve [Chamberlain]."*

709. However, the transaction could not be concluded within the targeted quarter. On 23 March 2011, Robert Sass notified Mr Hussain that the deal was "*highly unlikely for March*", though Mr Hussain encouraged him to "*keep pushing*". Then, on 29 March 2011, it emerged that Ameritrade had "*said 'no' – not why, not later, just 'no'*". The Claimants contended that this bad news was doubtless relayed to the Defendants, given Mr Hussain's recent involvement in pushing for the deal to be concluded.

710. As had become habitual (or what I have called the pattern) when a targeted deal which Autonomy needed to satisfy revenue forecasts was delayed, Autonomy sought to set up a sale to a friendly VAR. On 31 March 2011, DiscoverTech signed an agreement with Autonomy Inc for a licence of the same software, for the same end-user, ThinkTech. The licence fee was $1.8 million plus $180,000 support and maintenance. Autonomy recognised the licence fee as revenue immediately, that is to say, in Q1 2011.

711. The VAR letter Agreement dated 31 March 2011 was on the usual terms which stipulated that DiscoverTech was on risk irrespective of whether an end-user sale was concluded, and that the agreement represented the entire agreement between the parties. Mr David Truitt confirmed in his evidence in the US criminal proceedings that he understood that DiscoverTech was on risk.

712. The Claimants' central point relates to the fact that on 29 March 2011 there was an email from the indirect end-user which the Claimants referred to as the "just no" email. In that email, which was part of an internal Autonomy exchange reporting on the status of certain deals that Mr Hussain was pressing should be closed before the quarter-end, an Autonomy sales manager reported as follows:

> *"TD Ameritrade said "no" – not why, not later just "no"*
>
> *We are working to get more info"*

713. The Claimants (who did not quote the second sentence of the email) construed this as denoting Ameriprise/ThinkTech's categorical withdrawal; and they relied on the fact that, in the end, no licence was sold to ThinkTech as further support for that construction. On that basis they advanced the argument following:

> *"The question that immediately arises is this: why would DiscoverTech take on a liability to pay $1.8 million, in the hope of selling a licence to ThinkTech, in circumstances in which, as noted above, ThinkTech had already said it did not want one….*
>
> *…*
>
> *In fact, the only sensible explanation for this otherwise irrational behaviour on the part of DiscoverTech is the existing of the intention described in Chapter 6 [the side agreement] as well as the promise of a MAF."*

714. The Claimants also sought to rely on evidence given by Mr David Truitt in the US criminal trial which they portrayed as having been as follows:

(1) DiscoverTech probably would not have had the ability to pay for the order, in the absence of an end-user sale.

(2) Autonomy exercised control over what to sell to ThinkTech, when, and at what price.

(3) It was Autonomy that would be responsible for consummating any sale with ThinkTech: Mr David Truitt observed during his testimony, "*That is the way it worked.*"

715. The Claimants emphasised that Mr Welham was unaware of the "*just no"* email at the time and that there was nothing to suggest that either Mr Hussain, or anyone else, drew it to Mr Welham's attention. In Mr Welham's witness statement he said that had he known about this email, he would have wanted to understand the commercial rationale for the sale to DiscoverTech, given such remote prospects of an end-user sale.

716. To all this, the Defendants submitted that the real answer to the Claimants' rhetorical question was the one actually given by Mr David Truitt in a passage the Claimants themselves had marked up as hearsay evidence that they wished to adduce and rely on: his recollection was that Mr Egan had given him an *"indication that they were very close to closing"*.

717. The Defendants contended also that the Claimants' portrayal of Mr David Truitt's evidence was unfair and out of context:

(1) Mr David Truitt's evidence was in fact that DiscoverTech <u>could</u> have been put in funds to meet all its sales obligations.

(2) As to the contention that Autonomy had control over the goods, the quoted passage of Mr David Truitt's deposition evidence in the US criminal proceedings was only making an observation about what he understood from the restrictions in the <u>reseller agreement</u>. Their line was that those provisions did not suggest that Autonomy exercised managerial control for the purposes of IAS 18.14.

(3) They asserted (though Mr David Truitt did not say this) that the idea of the relationship with Autonomy was that DiscoverTech would be the contracting party with the end-user, enabling it to commence a relationship under which it would provide services.

718. The Defendants also contended that, to the extent relevant, the *"just no"* email did not mean at all that there was no prospect of a deal being done with the end-user, contrary to the Claimants' case. Less than a month later on 26 April 2011, there is documentation showing that negotiations continued, and that Autonomy's salesmen were forecasting a "50% plus probability" for a deal with Ameritrade (though what deal and at what price is not disclosed).

719. The Defendants did not deal specifically with the fact that Deloitte were not told of the "just no" email. It is not clear when Deloitte undertook their review of the revenue deals for Q1 2011; and, more particularly, whether negotiations for a deal had re-started or were on-going (such that the "just no" email was no longer of any material relevance). As usual, Deloitte focused on the VAR agreement and concluded that all the relevant criteria were

satisfied to enable and require revenue recognition. As to the end-user all they noted was as follows:

> *"The end-user, ThinkTech Inc is a subsidiary of TD Ameritrade, a large listed stockbroking firm. The purchase of a compliance archiving product with Bloomberg integration appears to be a rational purchase for such an entity."*

720. The Claimants also relied in the context of VT31 on the DiscoverEngine software purchases for the same reasons and on the same basis as they had in the context of VT30: they contended that the purchases were simply a means of passing money to DiscoverTech to make good on the agreement or understanding they alleged.

My assessment re VT31

721. In my view (and I find that) at the time that the VAR deal with DiscoverTech was entered into:

(1) Autonomy's sales department had been told, and Mr Hussain (who had been keeping an eye on and had been pushing for the deal to be concluded) would have been informed and appreciated, that the prospect of a sale to Ameritrade/ThinkTech was very slim. It is more likely than not that Mr Hussain would have informed Dr Lynch, who also monitored closely the likelihood of deals which were part of the means of achieving the quarterly revenue target eventuating.

(2) Deloitte should have been told of the *"just no"* email; and it is more likely than not that it was withheld deliberately, lest it prejudice revenue recognition in the targeted quarter, at the instance of Mr Hussain.

(3) DiscoverTech would have had great difficulty in meeting its contractual obligations under VT31 out of its own resources, and it was never in reality expected or intended by either Autonomy or Mr David Truitt that it would be required to do so.

(4) DiscoverTech was not intended or expected to participate or be involved in any way in any future effort to conclude a deal with ThinkTech, the objective of which would continue to be a direct deal between Autonomy and ThinkTech. DiscoverTech was never intended or expected to deal with or use the software notionally 'sold' to it in any way.

(5) The 'sale' was a device with no economic substance to enable revenue recognition, regardless of whether or not any sale to ThinkTech ever eventuated.

722. In my view, VT31 is a further demonstration of the by now habitual and routine way or pattern in which Autonomy resorted to friendly VARs, and especially DiscoverTech, to bolster quarterly revenue. Further, it shows that by now at least, Autonomy was prepared to exaggerate the prospects of an end-user deal, and trust in some other mutually beneficial commercial solution to preserve the loyalty of the VAR and reward it for taking on risk if no end-user sale eventuated. A further aspect of the pattern appears to be emerging: recognition of revenue even in circumstances which at the time of such recognition there appeared to be little likelihood of the putative end-user deal eventuating at all.

723. In my judgment, this is the pattern well established by now. It is inconsistent with proper revenue recognition.

Were the Defendants aware and involved?

724. Mr Hussain's involvement and 'guilty knowledge' is plain.

725. I accept that Dr Lynch was not involved in the detail of this deal. But I consider that it is more likely than not that he was informed that it was, as at the end of Q1 2011, most unlikely to result in a deal with Ameritrade/ThinkTech, and that there was at least real doubt whether it would ever eventuate in the then proposed form and price. Accordingly, it is more likely than not that Dr Lynch was aware that a VAR was being introduced solely for the purpose of triggering revenue recognition, without any intention of the VAR being involved in any way or dealing with the software notionally sold, and (in the particular case of VT31) regardless of whether in the end any revenue in fact was generated. He was aware also, since with Mr Hussain he was an architect of the practice of resorting to 'friendly' VARs in order to recognise revenue in a targeted quarter where there was a delay in closing the prospective end-user deal, of the tacit understanding shared with all the 'friendly' VARs, that though legally at risk, they would never be expected or required to pay out of their own resources. That, in my judgment, constituted "guilty knowledge".

VT35: DiscoverTech/Abbott Labs Q2 2011

726. In an email to Dr Lynch dated 11 June 2011 (subject: update) Mr Hussain referred, as one of three new potential deals, to the *"chance of a $15m software deal"* with Abbott Laboratories ("Abbott"), a healthcare company which was an existing customer of Autonomy. Though this was, as Dr Lynch accepted, a large deal (he cavilled at *"very large"*), he had not mentioned it in his witness statements; and his position was that he did not think he had had any involvement in it (apart from being updated occasionally as to its status by Mr Hussain).

727. It is clear that the prospective Abbott deal was large enough to become of increasing concern as the end of June approached without its successful agreement. When Mr Sullivan informed him on 27 June that Abbott *"say they need till tomorrow",* Mr Hussain almost immediately responded *"Fingers and toes crossed we need it".*

728. In the event, Abbott would only agree to a substantially reduced deal, and demanded very extended payment terms, which Mr Hussain agreed. Mr Wilner of Autonomy reported to Mr Sullivan by email dated 30 June 2011 as follows:

> *"Sr. Atty* [negotiator for Abbott] *veto'd by GC* [General Counsel] *who says (and has said in the past) that they will 'never authorise forward-looking commitment levels.' Nothing left to be done.*
>
> *Utterly ridiculous conclusion to a ridiculous process. Wish the news were better. Sorry we couldn't get this one done."*

729. Later that day, Mr Hussain updated Dr Lynch by email as to the "state of play", reporting in relation to the Abbott deal as follows:

> *"Abbott – 2 deals being worked – a $2.5m deal direct (we negotiated this last night, not on good terms though) and one thru partner".*

730. It appears, therefore, that when the larger deal with Abbott that it had hoped to close by the end of the month failed to materialise, Autonomy decided to resort to a VAR in accordance with its usual practice in such circumstances. On 30 June 2011, DiscoverTech issued a purchase order for the licence that Autonomy had been trying to sell Abbott. The licence fee was the very precise sum of $8,611,011.07, which Autonomy recognised as revenue immediately. The total amount payable under the purchase order, taking account of additional sums for hosting and support and maintenance, was $9.45 million.

731. As in other DiscoverTech VAR deals, the reseller agreement placed DiscoverTech on risk irrespective of whether an end-user sale was concluded, and contained a clause stipulating that the contract represented the entire agreement between the parties. This was a further transaction on which DiscoverTech understood that it assumed the legal risk, and the evidence from Mr David Truitt and Mr Egan confirmed that.

732. Mr David Truitt gave further evidence about this transaction specifically in the US criminal trial. He said that Mr Egan convinced him to do the deal and that he accepted the risk and DiscoverTech owed the money on the deal:

> *"Q. Let's talk a little bit about the Dell Hyatt and Abbot Labs deals in the third quarter of 2011.*
>
> *Again, this is all Mr. Egan. Mr. Egan came in and convinced you to do it; right?*
>
> *A. Yes.*
>
> *Q. Told you that these deals were about to close?*
>
> *A. Yes.*
>
> *Q. Told you that these were long-term customers of Autonomy who were going to have to buy eventually --*
>
> *A. Yes.*
>
> *Q. -- right? And persuaded you that this was something that you wanted to do?*
>
> *A. Yes.*
>
> *Q. And to the extent that -- you didn't talk to Mr. Hussain about the Abbott deal, did you?*
>
> *A. No.*
>
> *Q. Mr. Egan didn't tell you that the -- they were having problems getting the general counsel to agree to a license?*
>
> *A. No.*
>
> *Q. Okay. Did you know that eventually they did get Abbott to agree to a license?*
>
> *A. No.*
>
> *Q. But, again, these were deals that you accepted the risk on and you owed the money on?*
>
> *A. Yes, sir."*

733. Earlier in his testimony David Truitt had also made the same points. His evidence was that Mr Egan told him that "*the deal was going to happen sometime soon*". There was consensus between the parties that if Mr David Truitt had been told that Abbott had vetoed a forward-looking commitment, he would not have done the deal. The Defendants indeed relied on this evidence, which had been marked up by the Claimants as hearsay evidence upon which they relied, as confirmation that Mr David Truitt regarded DiscoverTech as on risk, and as thus being inconsistent with the Claimants' case.

734. However, the real thrust of the Claimants' case in respect of the Abbott deal (VT35) was that it was *"devoid of economic substance"* and even *"absurd"*. The Claimants contended that:

(1) DiscoverTech had no ability to pay, absent an end-user transaction, and there was no real prospect of an end-user transaction with Abbott in light of it having been vetoed by its General Counsel.

(2) Mr David Truitt was not told about the General Counsel's veto.

(3) DiscoverTech was to have no involvement in any negotiations with the end-user and made no effort and was not expected or intended to effect a sale itself: after the VAR 'sale' as before, any sale to Abbott was intended to be a direct sale by Autonomy. That demonstrated Autonomy's *de facto* continuing managerial control of the software sold which would disqualify revenue recognition. Mr David Truitt was asked in his cross-examination in the US criminal proceedings whether he would say Autonomy exercised control over what to sell to Abbott and on what terms; his answer was unequivocally "yes".

(4) Mr Hussain then misled Deloitte about the rationale of the proposed end-user deal (DiscoverTech/Abbott) in (a) telling Deloitte that it was using DiscoverTech because it had 8A status, knowing that it did not; and (b) keeping back from Deloitte the fact that Abbott's General Counsel had vetoed any deal involving a *"forward-looking commitment"*.

(5) When no onward sale to the end-user eventuated, Autonomy, at Mr David Truitt's request, simply "cancelled" and wrote off the obligations under VT35. The Claimants placed great reliance in this context on an email dated 30 September 2011 from Mr David Truitt to Mr Scott under the subject heading *"Cancellation of VAR agreements"* in support of the allegation that according to Mr David Truitt, this is what Mr Egan had at the outset agreed should be done if no end-user deal eventuated. That email read as follows:

> *"Hello Mr. Scott, I am writing to formally request that VAR agreements signed on June 30th, 2011 between Discover Technologies and Autonomy, regarding Abbott Laboratories and Dell/Hyatt be cancelled. Per my discussions with Stouffer Egan, under the condition that the end customer did not ultimately license the proposed Autonomy software, the agreements would be cancelled with no further obligation on the part of Discover Technologies. Thank you for your attention and prompt response".*

(6) Such a cancellation and write-off in the aggregate sum of $15 million would not have been made without the approval of both Defendants.

735. The Defendants' responses were:

(1) Whether or not DiscoverTech was good for the amounts for which it assumed an obligation to pay was an issue of collectability. Collectability was a judgmental area, was assessed by Deloitte, and was considered satisfactory. In any event, this would not render the transaction *"devoid of economic substance"*. Mr David Truitt's answer to the question whether DiscoverTech had sufficient money to pay for the purchase order if the end-user sale failed was *"No, not within the company"*. But Mr David Truitt and his partners had funds; and he confirmed that they could put DiscoverTech in funds to pay the DiscoverTech reseller deals.

(2) It was common ground that Mr David Truitt was not told of the alleged veto by Abbott's General Counsel. That may explain why he proceeded, and the Defendants argued that, if anything, the point tends to undermine rather than support the Claimants' contention that Mr David Truitt was to be held harmless in any event.

(3) Further, (and this is relevant also to (1) above), Dr Lynch did not accept that the General Counsel's "veto" was really such as to preclude a further deal. He explained that while this was not good news he had seen deals in this position come back, and that he had experienced this kind of thing before as a negotiating tactic. Dr Lynch also observed correctly that Abbott did in fact come back subsequently. With regard to the Abbott deal and the reseller deal generally, Dr Lynch also explained that this was a very sizeable opportunity with a very large demand from Abbott for e-Discovery. Dr Lynch's analogy was that rather than selling Abbott the multiple deliveries of milk they would need, Autonomy was offering the cow, and was likewise offering the cow to the reseller (who could itself supply either the cow or the milk to the end-user).

(4) The criterion in IAS 18.14(b) is about whether the seller retains managerial involvement or control over the goods.[66] Under the reseller deals Autonomy had no continuing contractual obligations in respect of the software and no rights to control what happened to it. The fact that the reseller may have left it to Autonomy to carry on negotiations, with a view to a sale of the goods by the reseller to the end-user does not mean that the criterion was not fulfilled. Mr David Truitt's evidence in fact confirmed repeatedly that DiscoverTech did have managerial control: there was a true sale under which managerial control of the goods passed without qualification. When asked in more detail about managerial control, Mr David Truitt's understanding was that the preservation of managerial control by Autonomy arose out of the terms of the reseller agreement (which in fact provided the opposite).

(5) DiscoverTech does not appear to have been a section 8A business; and the Defendants accepted that it was recorded as being so on a Deloitte workpaper after a discussion between Mr Hussain and Mr Welham relating to the Abbott

[66] The experts on accounting matters were agreed that this criterion generally goes hand-in-hand with the transfer of the risks and rewards of ownership of the goods.

deal, but erroneously so. However, the Defendants contended that there was no evidence to explain why this was so, still less that Deloitte had been deliberately misled whether by Mr Hussain (whom the Claimants implicated) or anyone else. Mr Welham had no recollection himself; and though he was not challenged on his evidence that he *"would be surprised if we wrote it down incorrectly"* there was nothing to gainsay the suggestion that *"the person who gave you the information may have been muddled".* The Defendants referred in that connection to an email from Mr Scott to Mr Hussain in April 2011 which referred to two DiscoverTech deals on a list of "8A deals", which might have given rise to a misunderstanding on Mr Hussain's part.

(6) Although the Claimants took Dr Lynch to Mr David Truitt's email dated 30 September 2011, they did not take him to Mr David Truitt's evidence about it. Mr Truitt had in fact confirmed in his testimony in the US criminal proceedings, which the Claimants themselves put forward as their evidence, that there was *"never an understanding that if an end customer didn't buy, that I could cancel the deals with no further obligation".* Dr Lynch also confirmed that that was not the arrangement with the resellers: the contracts were clear and the resellers were on risk. It was not as Mr Chamberlain understood matters either: his immediate response to Mr Truitt's email was *"must be a mistake"*.[67]

(7) As to the writing off of the debt, although Dr Lynch was not involved in it, and would like to have been consulted about it, he did not see it as remarkable in circumstances where Autonomy was being acquired. He thought the decision would have been a commercial one. Further, in his perception, everything was transparent and Autonomy's books were always going to be open to HP.

My Assessment of VT35

736. In assessing the Claimants' case that the transaction was *"devoid of economic substance"* the essential questions, as it seems to me, are (a) whether it was ever expected or intended that DiscoverTech would negotiate and itself conclude a deal with Abbott and (b) whether Autonomy's agreement to cancel the deal (VT35) was to honour a pre-existing arrangement between Mr Egan and Mr David Truitt to cancel the deal if no end-user sale eventuated in order to persuade DiscoverTech to undertake a more than usually large and uncertain VAR transaction; or whether alternatively, it was an *ad hoc* response agreed subsequently to deal with an (until then uniquely) unusual situation.

737. As to (a), and as noted above, Mr David Truitt accepted unequivocally that Autonomy not DiscoverTech had and was expected to exercise control over what to sell to Abbott and on what terms; his answer was unequivocally "yes". He also confirmed that DiscoverTech never did make any efforts to negotiate with Abbott. That is an illustration of the usual pattern that the VARs in impugned VAR sales were not expected or intended to negotiate or themselves be party to a sale to the prospective end-user. Although the Defendants sought to ascribe this to Mr David Truitt's understanding of the terms of the VAR agreement, I am satisfied that his evidence shows what he understood to be the position in reality.

[67] As Dr Lynch put it in his testimony "*A. So Mr Chamberlain knows there's a contract but makes it absolutely clear that, even if Mr Egan has given some strange assurance, that it's worthless*."

738. As to (b), I do not accept, in light of the subsequent negotiations culminating in a deal (albeit a smaller one) and the undisputed evidence as to Abbott's real need for substantial software to organise its material and data to respond to a huge investigation into it by the US Department of Justice, that Abbott's General Counsel's "veto" entirely put an end to any prospect of an end-user deal apparently envisaged in the VT35 purchase order.

739. However, I accept that (i) even if a deal could be struck, there was a real risk that only a lesser price would be achieved, (ii) the prospect of such a deal was very uncertain, and (iii) since the amounts at stake were notably large, DiscoverTech was more than usually exposed, especially given its other outstanding commitments. The size of the deal meant that the risk undertaken by DiscoverTech, if real, was an existential one. Both that and the easy agreement of Autonomy to write off such a sizeable debt does suggest a previous arrangement that Autonomy would make sure the legal obligation was satisfied or released in some other way.

740. I have taken into account that, as the Defendants much emphasised, in a passage of his testimony in the US criminal proceedings in part relied on and adduced in evidence by the Claimants themselves, Mr David Truitt disavowed any pre-existing arrangement and sought to explain his email referring to his discussions with Mr Egan as connoting that there was one (see paragraph 735(6) above) as simply his misunderstanding of what Autonomy had wanted him to write. However, all I have read Mr David Truitt as saying was that there was no pre-agreement as to the manner in which Autonomy would ensure that DiscoverTech would be released from legal risk, and no formal writing such as to constitute in his eyes a side agreement. He was not saying that he had been given no assurance that DiscoverTech would not be required to pay out of its own resources.

741. I am also satisfied that Mr Hussain had no reason to think that DiscoverTech had 8A status; and in representing to Deloitte (as I am also satisfied he did) that DiscoverTech did have such status, Mr Hussain was seeking to encourage Deloitte to approve revenue recognition by depicting the VAR as contributing to the transaction and as the company likely to enter into the contract with Abbott, knowing all of that to be false.

742. All in all, I accept the Claimants' case that VT35 lacked any real substance. To my mind, it once again exemplifies Autonomy's use of VAR deals predicated on an end-user deal even if those responsible knew the prospects of an end-user deal to be weak simply to plug gaps in revenue. It is a further illustration of a well-established pattern and its latter stage development of taking revenue even when the prospect of any real receipt was uncertain.

743. I am also satisfied that both Defendants (a) knew that the VAR sale was not intended to effect any real change in the way that Autonomy dealt with Abbott nor was it ever to result in a sale by DiscoverTech to Abbott; and (b) approved the arrangements by credit notes to dissolve DiscoverTech's substantial legal obligations. In the latter context ((b)), I accept that Dr Lynch may not have been consulted about the specific write-off and credit notes; but I do not accept that it would have been done without his overall approval for the process.

VT36: DiscoverTech/Dell/Hyatt Q2 2011

744. At the same time as the negotiations with Abbott, Autonomy was also negotiating a separate transaction with the Hyatt hotel chain in which it was envisaged that Autonomy

would licence to Dell, which would in turn sublicence to Hyatt. The price which Autonomy hoped for was some $5,000,000.

745. After encouraging signs in early June 2011, by 11 June 2011 Mr Hussain was telling Dr Lynch that he was *"nervous"* about the prospect; and by 18 June 2011 Mr Hussain was reporting to Dr Lynch that the transaction was *"OUT"*. On 30 June 2011, Mr Hussain advised Dr Lynch in another *"state of play"* email, that in relation to Dell, he had *"received draft order from partner"* (signifying a VAR).

746. The purchase order for VT36 (stating a licence fee of $5,333,914 plus $266,696 for support and maintenance) was issued pursuant to a letter agreement dated 30 June 2011 which included the usual terms which placed DiscoverTech on risk irrespective of whether an end-user sale was concluded, and stipulated that the agreement represented the entire agreement between the parties. Mr David Truitt gave further evidence about this transaction specifically when dealing with this deal together with the Abbott deal. He said that Mr Egan convinced him to do the deal and that on that basis he accepted the risk and DiscoverTech had a legal obligation to pay Autonomy.

747. The Claimants' case with respect to VT36 was substantially the same as their case with respect to VT35: that (a) the VAR transaction lacked any economic substance (there being, it was said, no real prospect when it was made of any sale to Dell/Hyatt, and none of DiscoverTech itself entering into a sale since in the unlikely event of any sale at all it would be direct by Autonomy); that (b) arrangements were made for the deal to be cancelled when no end-user deal eventuated, and that (c) Mr Hussain lied to Deloitte about the rationale for transacting with DiscoverTech (its supposed 8A status).

748. Likewise, the Defendants' response mirrored that in relation to VT35.

749. In such circumstances, I do not think it is necessary to rehearse the detailed facts and competing contentions. I have concluded for like reasons as in the context of VT35 that VT36 followed the same pattern and the VAR sale lacked any real substance. The following passage from Mr David Truitt's evidence in cross-examination in the US criminal proceedings illustrates that the essential requirement in IAS 18.14 that risk and management control should pass to the purchaser and not be retained by the seller were not fulfilled:

> *"Q. Did Discovertech have any relevant contacts at Dell or Hyatt?*
>
> *A. No, sir.*
>
> *Q. Did it make any efforts to resell them software?*
>
> *A. No.*
>
> *Q. Would you say that Autonomy exercised control over what to sell to Dell or Hyatt and on what terms and at what price?*
>
> *A. Yes."*

750. The Defendants submitted that the questions were *"broad and imprecise"* and posed without any reference to the accounting concepts under IFRS, and that the answers did not undermine or detract from the legal position that risk and control had passed. I do not

agree: the substance of the position was that the VAR was not intended to have anything more to do with the software, or its sale, and that it would be dealt with by Autonomy as if there had been no such sale.

751. As the Claimants submitted any confirmation required that VT36 lacked substance just as VT35 had lacked substance was provided by the arrangements made to release the VAR's ostensible indebtedness when in both cases (and as was by now becoming predictable) no end-user deal eventuated.[68]

752. Once again I am satisfied that both Defendants (a) knew that the VAR sale was not intended to effect any real change in the way that Autonomy dealt with Dell/Hyatt nor was it ever to result in a sale by DiscoverTech to Dell/Hyatt; and (b) approved the arrangements by credit note to dissolve DiscoverTech's substantial legal obligations.

753. In the latter context ((b)), I accept that Dr Lynch may not have been consulted about the specific write-off and credit notes in either VT35 or VT36; but I do not accept that it would have been done without his overall approval for the process.

VT18: FileTek and USDVA Q3 2010

754. FileTek, it may be recalled from paragraph 1963(5) in the main body of the judgment, specialized in the archiving of structured data, and was (amongst other activities) the developer of the StorHouse and Trusted Edge software.

755. Autonomy had learned in May 2010 that USDVA[69] were going to issue a Request for Proposal ("RFP") for a large deal including archiving. Autonomy wanted to secure the archiving component. It could only do so by bidding and partnering with a US Government pre-approved vendor. USDVA was a repeat customer of Autonomy which had been working with Autonomy on an email archiving system, but Autonomy was not a pre-approved vendor and under US regulations could not supply it directly. It could only do so in conjunction with or through a pre-approved vendor.

756. According to Dr Lynch's evidence in his witness statement, a number of pre-approved vendors were planning to bid on the RFP, and of those the majority were willing to partner with Autonomy and include its software. Autonomy decided on that course.

757. Mr Hussain had hoped that the process would proceed fairly quickly, and that it would be possible to include revenue from a sale in the Q3 2010 figures. On 7 August 2010, Mr Hussain had sent Dr Lynch an email entitled *"latest revenue"* stating that projected revenue for Q3 2010 was $215 million and projected earnings per share were $0.30, and that he would *"need VA and most probably one other"*.

758. The size of the deal, its importance in terms of Autonomy's revenue figures, and Dr Lynch's management style and active supervision are all demonstrated by a vigorous email response from Dr Lynch that same day (7 August 2010) to Mr Hussain and a number of other Autonomy personnel (Mr Still, Mr Egan, Dr Menell, Mr Mooney, Mr Sullivan and Mr Bryan Rellinger) as follows:

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[68] On 29 September 2011, Autonomy Inc issued DiscoverTech with credit notes for $9.45 million and $5.6 million, representing the entirety of what was ostensibly payable under VT35 and VT36 respectively
[69] United States Department of Veteran Affairs

> *"…this is the biggest deal in the quarter and the idea that some no-name proserv guy is allowed to potential f this up and we are even having debates about charging them is a MAJOR MANAGEMENT FAILURE. THIS CANNOT BE DELEGATED. ALL of you own this.*
> *Jim, stoff,mikem,mikes,bryan,pete you need to be minute to minute experts on this deal, nothing is said to the customer with out it being cleared by someone senior, no meetings occur with out someone with a brain present, NO F-ing abdications of responsibility or delegation. If there is any problem I WANT TO KNOW ABOUT IT IN A F***ING MILLISECOND from all of you.*
>
> *We cannot act like muppets on a deal of this size … break the rules and do it right.*
>
> *AND we will bid with anyone the customer wants us to, none of this Autonomy favoured nation shit anymore".*

759. Nevertheless, this vigour expressed to Autonomy employees could not of itself galvanise USDVA, and by mid-August 2010 it was becoming clear that, unless government agency financial rules compelled USDVA to hurry to issue a RFP (which would trigger the tender process) and move forward with speed, there was little prospect of any deal before Q4 2010. When Dr Lynch asked Mr Hussain in an email dated 13 August 2010 (a) *"how sure are we will win?"* and (b) *"how sure are we it will be q3"* Mr Hussain's replies were (a) as there were what he termed *"EAS issues"* and he had not yet seen an RFP he was not able to assess the prospect, but his overall feeling was that *"it's a low probability"*, and (b) on timing and whether the deal could be done in Q3 2010, he said: *"I can't see it unless they have to spend the funds"*.

760. By 25 August 2010, no RFP had yet been issued. Through late August and September, the prospect of a deal in Q3 2010 further receded. On 8 September 2010 Mr Hussain reported to Dr Lynch by email that the deal was *"AT RISK – Need RFP to come out to have a hope"*. On 15 September 2010 Mr Hussain reported again to Dr Lynch, this time removing USDVA from the list of expected revenue for Q3 2010.

761. It was nonetheless a large deal, and an important prospective revenue source. Mr Egan's unchallenged evidence was that he and *"Mr Hussain…discussed the need to be able to take the deal to a VAR in order to be able to recognise revenue in the quarter."* At that stage, Mr Hussain and Mr Egan were discussing using MicroTech and MicroLink as a *"partner"*. It is not clear why, on 28 September 2010, they turned to FileTek.

762. Autonomy had established a close relationship with FileTek through a number of deals, including two which the Claimants impugned as *"reciprocal"* or *"round trip"* transactions (and which are addressed later in the main body of the judgment in the chapter on alleged 'Reciprocal Transactions')[70]. None of those deals, however, was a

[70] The two transactions with FileTek impugned as reciprocal transactions (both referred to in the RRAPoC, in Schedule 5, as "RT 3") were (1) a purchase in Q4 2009 by Autonomy from FileTek of a licence for FileTek's StorHouse software for integration with Digital Safe at the same time as (and alleged to have been made in order to enable) a purchase by FileTek of a license for IDOL and (2) a purchase in Q1 2010 by Autonomy from FileTek of a further licence for StorHouse and a purchase at the same time by FileTek from Autonomy of a further licence for IDOL in Q2 2010.

VAR deal. FileTek was not a VAR[71]; as Mr Szukalski confirmed in cross-examination, being a reseller was not part of FileTek's business and it had never resold Autonomy software. VT18 was the only VAR transaction FileTek ever entered into with Autonomy.

763. Indeed, when Autonomy contacted FileTek almost at the end of Q3 2010 with a view to its participation as a *"partner"* in VT18, Mr Szukalski had not initially been keen on the idea because he did not consider it was FileTek's business model to resell other companies' software. He had suggested to Mr Egan that Autonomy might instead use a company called Centennial, a VAR that FileTek had a relationship with and that was accustomed to handling these types of deals. However, Autonomy was not familiar with Centennial and *"Mr Egan or others at Autonomy wanted FileTek to be involved, because Autonomy knew FileTek and had dealt with it over several years"*. Mr Egan also suggested that Centennial *"did not pass the eligibility criteria for our resellers*", and Autonomy reverted to FileTek: but this was not further explained.

764. Following a call with Mr Hussain and Mr Egan on 30 September 2010, Mr Loomis of FileTek recorded in an email that "*We will be licensing through a prime contractor. Autonomy will coordinate for us*". In his witness statement, Dr Lynch described the purpose as being *"to de-risk the deal."* But the need for revenue in the quarter was plainly the driving reason.

765. VT18 was, in legal terms, governed by a letter agreement dated 30 September 2010, which granted FileTek the right to sublicence the specified Autonomy products either directly or through an agreed prime contractor to the USDVA or an Alternate Licensee (subject to the terms of clause 3). The licence fee was $10,000,000 and there was a first-year support fee of $500,000.

766. The VT18 agreement was in the form of a counter-signed letter dated 30 September 2010. As was part of the pattern, it provided:

(1) (by clause 1) that once executed by FileTek the agreement constituted a non-cancellable purchase commitment on the part of FileTek;

(2) (by clause 7) that the agreement represented the entire agreement between the parties concerning its subject matter and any discussions outside the four corners of the agreement would not have any legal effect.

767. Only clause 3 of the letter agreement was more unusual in expressly providing for FileTek to have the ability to sell to other end-users within a prescribed time (90 days from 30 October 2010). That right was, however, subject to the proviso that the VAR agreed:

> *"not to sublicence and distribute the Autonomy Software Products and Maintenance Services hereunder to any party or entity that sells, licenses, or distributed [sic] products, services, software, or offerings competitive with the products, services, software and/or offerings of Autonomy or its affiliates."*

[71] As elaborated in the chapter of this judgment on Reciprocal transactions, FileTek's specialisation was in the archiving of structured data and its development and sale of its two principal products (*"StorHouse"* and "*Trusted Edge"* software)

768. As was also required and invariable, FileTek countersigned audit confirmation letters verifying its indebtedness, confirming that there were no *"side letters or other agreements in respect of the subject matter of this request, except as noted…"* and acknowledging that Autonomy retained:

> *"no continuing managerial involvement in the delivery of this product or service, other than stipulated in the licence agreement."*

769. It was common ground that Mr Egan had given FileTek (through Mr Loomis) assurances of assistance if no deal with USDVA eventuated. Mr Egan's evidence in his witness statement, with specific reference to VT18, was that the gist of what he said at the time that the VAR transaction was entered into was:

> *"Autonomy would be responsible for arranging a licensing transaction with the winning contractor; FileTek would not engage in the actual sales efforts. If, for some reason, the VA deal was not completed, Autonomy would use all efforts to find another end-user for the same software or some other way to make sure that FileTek would get paid and could then pay Autonomy."*

770. As may also be recalled (and see paragraphs 1991 and 1993 in the main body of the judgment), Mr Egan elaborated some of this by reference to VT18 as follows:

(1) All he meant by *"backfilling"* was that he was going to *"take other deals from Autonomy's forward-looking pipeline and then give them to the reseller to backfill…in other words, basically substitute another deal for it…"*; and in the meantime

(2) Unless and until a substitute deal was arranged *"they had to make their payments in line with payment terms",* not least because

(3) Any assurance given by him was not legally binding on Autonomy and was not intended to affect the legal obligation to pay (*"No, 100% not"*).

771. There was something in these explanations for both sides, resulting in considerable dispute as to the extent and status of these assurances. The Claimants relied on VT18 as a further exemplar of the 'pattern'; but the Defendants themselves also placed emphasis on VT18 as a good test of the furthest extent of the assurances given in the context of the impugned VAR transactions. Indeed, this appears to have emboldened Dr Lynch to state in his written closing submissions that:

> *"Of all the reseller transactions the evidence in respect of the FileTek transaction in fact takes the Claimants' case the furthest. But even if the conversation had run as Mr Egan suggested (and…this is a very big if), what he said would not have undermined revenue recognition."*

772. Aunt Sally or litmus test? I turn to the details of the transaction. In this section I focus primarily on (a) the evidence given by Mr Loomis in the US criminal proceedings (which was admitted into these proceedings under a hearsay notice) (b) the evidence of Mr Szukalski in these proceedings (c) particular distinguishing features of the transaction and

(d) Autonomy's purchase of StorHouse software from FileTek, which the Claimants alleged was contrived to save FileTek from *"holding the bag"* when, in the event, no end-user deal with the USDVA was ever concluded.

773. Mr Loomis's evidence in the US criminal proceedings in relation to FileTek's role in VT18 was in outline as follows:

(1) He said that he understood that FileTek was at *"full risk"* in that *"FileTek owed the money once they agreed to it"* and was aware that FileTek provided signed audit confirmation letters to Deloitte confirming its indebtedness. He also understood that there was an entire agreement clause applicable;

(2) The risk was considered proportionate and acceptable because (a) USDVA was already a current customer of Autonomy (b) Mr Loomis's understanding was that Autonomy would have closed the deal itself without any recourse to a VAR but for delays *"because of government procurement issues"* (c) Autonomy *"were very confident that it was going to be concluded shortly"* and (d) FileTek on completion of the deal would get a mark-up or margin on the licence sale to the USDVA of 10% equating to about $1,000,000;

(3) Thus, FileTek was *"an investor"* (as he put it) in the proposed end-user sale because FileTek *"would be dependent on the closure of that sale to the Veteran's Administration for us to receive a revenue"*;

(4) When asked whether it would have been a problem for FileTek if the sale to the proposed end-user *"dragged on and didn't close for months at a time"*, Mr Loomis replied *'yes'*, and some form of reassurance was sought from Autonomy in this respect. In an email dated 30 September 2010 from Mr Loomis to Mr Bill Thompson summarising the proposed transaction, reference was made to three scenarios having been considered, which were (i) completion of the end-user sale as planned in Q4 2010, or (ii) deferral of the end-user sale to Q1 2011 or (iii) *"Disaster: something fully unexpected either further delays or eliminates the opportunity"* in which case *"Our plans for each are as per our telephone conversation"*, it being noted also that *"We have ability to reassign the license";*

(5) Mr Loomis was not asked about his conversation with Mr Thompson but confirmed that he had a telephone conversation with Mr Hussain and others at Autonomy at the very end of September 2010. He professed that his recollection was *"vague"* but that the purpose of the conversation with Mr Hussain was to hear from someone at Autonomy with the stature of Mr Hussain *"the same story that we were hearing from Stouffer Egan";*

(6) Beyond a statement that the conversation was reflected in the email referred to above, the content of that *"story"* was not explored in either examination or cross-examination in the US criminal proceedings. However, whatever was discussed appears to have satisfied Mr Loomis; and the concern he expressed about what would happen if the end-user sale collapsed focused on the loss of the margin of $1 million, not the exposure to risk in respect of the VAR purchase;

(7) Mr Loomis became concerned when after 45 days or so the end-user deal had not completed, and became frustrated by Autonomy's lack of communication about its progress and prospects: it was clear that FileTek played no part in the process or the negotiations;

(8) After a small initial deposit, Mr Loomis determined not to make and did not in fact make any payments to Autonomy because (a) *"it was a lot of money"*; (b) *"we did not have status updates"; and (c) "it was a way to help leverage the status update…";*

(9) His evidence was that when by June 2011 the end-user deal had not eventuated, it was agreed that Autonomy would buy StorHouse software from File Tek and

> *"the arrangement was that we would take the proceeds from the sales and utilize those proceeds or a substantial portion of those proceeds to pay down the liability we had to Autonomy for the VA transaction".*

774. In summary, and it is obviously an assessment made on a transcript, rather than on the basis of 'live' cross-examined evidence, the impression given in the transcript is that, however this was conveyed to him, Mr Loomis had no intention of paying Autonomy unless and until the end-user deal closed, and if it did not eventuate, he never envisaged FileTek being left to pay down its indebtedness out of its own resources: some arrangement would be made.

775. Mr Szukalski's evidence in these proceedings in relation to VT18 may be summarised as follows:

(1) His understanding from Mr Loomis was that FileTek was on risk, but that Mr Loomis was comfortable proceeding because (a) the end-user deal was likely to proceed and take place well within 45 days and before any further payments would be due from FileTek; (b) under the terms of the transaction, FileTek was able to sell the software to any customer, and Mr Egan had told Mr Loomis, and Mr Szukalski and Mr Loomis believed, that *"Autonomy would help us out by putting us in contact with another buyer in the unlikely event that the USDVA deal fell through for some reason"*;

(2) He did not expect FileTek to play any active part in the sale of the software on to the end-user, and his understanding was that Autonomy was going to coordinate the licencing of the software through a prime contractor acting merely as a *"fulfilment partner"*:

> *"Q. And the reason why Autonomy would help prepare the purchase schedules is that FileTek didn't know what Autonomy software the USDVA might be interested in buying?*
>
> *A. This was just a fulfilment transaction quite frankly in the sense that we were told that there was a deal at the USDVA, Department of Veteran Affairs, that was going to close in approximately 45 days, was the number that we were given, and that would we mind holding the paperwork for those 45 days and in exchange we'd earn a certain margin on the deal. I think the number turned out to be around $1 million worth of - - to do that.*

So that's what we were asked to do. Again, I would have rather this gone through Centennial but it went through FileTek.

Q. And apart from holding the paperwork, FileTek wasn't going to be expected to do anything else?

A. That was it. We really were told there were several bidders on this particular transaction and it was just a matter of awarding the deal to one of those bidders and all of them was bidding Autonomy software so it would be a, you know, no brainer/slam-dunk kind of transaction."

(3) Mr Szukalski repeatedly emphasised that FileTek:

> *"had no contact with the [USD]VA and…no contact with the six primes that were bidding on the deal.*
>
> *Autonomy gave us the assurance that this particular transaction was going to happen through one of those bidders, it was going to include IDOL, and it would happen in the next 45 days. That's the summary of basically what we had. So we didn't have any contact with those systems integrators."*

(4) He told me later in the course of his cross-examination that in his experience it was not unusual in the industry for there to be a reseller partner which had no expertise in selling the technology, which would do no more than *"just push paper"* and which took a margin for their role without adding value beyond acting as a "fulfilment partner": but see further paragraph 785 below.

(5) In his witness statement, Mr Szukalski had given the impression that all that FileTek could expect from Autonomy if the USDVA sale failed was that Autonomy would help by finding an alternative buyer, but that in the meantime Autonomy would be entitled to enforce its rights. However, when cross-examined, he made clearer that he did not expect that FileTek would ever have to find a replacement end-user itself: Autonomy would find a replacement end-user, failing which the intention and expectation was that Autonomy would find some other way of enabling FileTek to discharge its legal obligation (and would not press for payment in the meantime):

> *"Q. So Mr Loomis' expectation was that Autonomy would find a way to ensure that FileTek got paid so that FileTek could pay Autonomy?*
>
> *A. That is correct also.*
>
> *Q. And Mr Loomis trusted Autonomy to honour that assurance?*
>
> *A. He did but this particular transaction didn't come without*

> *risk, obviously, in that disaster scenario. It was different than the other transactions.*
>
> *Q. And the risk was that Autonomy doesn't honour the assurance that had been given to Mr Loomis?*
>
> *A. That is correct."*

(6) In response to the Claimants' suggestion that FileTek wanted to use the audit confirmation letters, which were marked for Mr Szukalski's attention but signed on behalf of FileTek by one of three others (namely, Ms Leslie Levy, FileTek's "Controller", Mr Howard Patrick, FileTek's General Counsel and contracts negotiator, and Mr Bill Loomis), as leverage over Autonomy, the gist of Mr Szukalski's evidence was again that FileTek's was a real debt, that they wanted the USDVA deal and were prepared to accept the risk for that and the reward by way of margin:

> *"A. So as I said before, we used certain milestones, whether it was a payment date or an auditor letter in this case, to kind of trigger or get Autonomy to respond to our request for where are we in this process, because we feel very, very uncomfortable signing this auditor letter or moving forward without, you know, continued update or assurances that the [USD]VA deal is real and coming through.*
>
> *Q. Or that Autonomy would find you someone else who would buy the software for more than $10 million –*
>
> *A. Yes, at this time we really didn't focus our efforts on that. We really wanted that [USD]VA deal and that is a continuing theme throughout the next several months that I'm sure we'll get to, but that was -- that there was a VA deal and it was real."*

776. Mr Szukalski had not been shown the transcript of Mr Loomis's testimony or Mr Egan's witness statement (although he told me that someone had given him the gist of the latter) before signing his witness statement evidence and so did not address either. Nor (save for one email) was he shown any contemporaneous documentation at that time. The result was that Mr Szukalski's evidence in cross-examination differed from some parts of his witness statement. I agree with the Claimants that his oral evidence was more reliable. However, the inconsistencies were not such that the essential message of his evidence was unclear.

Particular points on VT18

777. Five points about VT18 were particularly emphasised by the Claimants, as indicating its lack of substance and the fundamental ways in which it failed to satisfy the criteria for revenue recognition.

778. The first such point related to the true nature of the assurances given by Mr Egan as to how the legal risk which the VT18 agreement undoubtedly imposed on FileTek would be covered in the event of no sale to USDVA, or a long delay before such a sale could be concluded; the central question in this, as in all the other impugned VAR sales, being whether the reseller would be called upon to pay out of its own resources.

779. According to the Claimants, the basis of the VAR transaction was that from its inception, and with the consensus of both parties, FileTek had received an assurance that in reality Autonomy would cover its risk and FileTek had entirely abdicated from any continuing managerial involvement to the degree usually associated with ownership of the goods sold: accordingly, it was Autonomy, and not FileTek, which had the significant risks of ownership and effective control of the goods sold, thus disqualifying revenue recognition because of IAS 18.14(a) and (b), as well as because the 'sale' lacked any real substance.

780. The Claimants further supported this conclusion on the basis that, in any event, FileTek had none of the information or expertise to negotiate and effect an end-user sale: it had never previously sold Autonomy software to anyone; the software purchased included Digital Safe, which FileTek had no experience in implementing, nor any ability to maintain. For the same reason, clause 3 of the VAR Agreement governing VT18, which appeared to give FileTek some latitude to sell to another end-user if the USDVA deal failed, was largely illusory: the prospects of FileTek being able to find a third party buyer for this software at a price of $10 million were very remote.

781. The following passage from Mr Szukalski's evidence in cross-examination (which I have quoted in part in paragraph 775(1) above) elaborates these points:

> *"Q. ….In the disaster scenario, the plan was that Autonomy would help you to reassign the software licences to another potential customer?*
>
> *A. That is correct.*
>
> *Q. Yes. So Autonomy would find a different customer who was willing to pay at least $10 million for the software?*
>
> *A. That is correct.*
>
> *Q. And then Autonomy would put FileTek in touch with that customer?*
>
> *A. Or Autonomy would act on our behalf and we would be just the fulfilment partner, again, not adding a lot of value in terms of selling but the paperwork would go through FileTek. So again very common practice. We don't have to necessarily have the expertise in IDOL or Autonomy software, we would leverage the expertise of Autonomy but the paperwork, the contractual paperwork would have gone through FileTek.*
>
> *Q. So Autonomy would draw up a contract with this other customer but it would then insert FileTek as either the*

contracting party or the party who would receive the payment?

A. That is correct.

Q. And then after that was done, this other customer would pay FileTek and then FileTek would use that money to pay Autonomy?

A. That is the reassignment, yes.

Q. And that's what you understood Mr Loomis expected to happen here on the basis of his discussions with Mr Egan and Mr Hussain?

A. That is correct.

Q. So Mr Loomis' expectation was that Autonomy would find a way to ensure that FileTek got paid so that FileTek could pay Autonomy?

A. That is correct also.

Q. And Mr Loomis trusted Autonomy to honour that assurance?

A. He did but this particular transaction didn't come without risk, obviously, in that disaster scenario. It was different than the other transactions.

Q. And the risk was that Autonomy doesn't honour the assurance that had been given to Mr Loomis?

A. That is correct."

782. Furthermore, in the event of a deal in the conclusion of an end-user delay extending beyond instalment payment dates, it was not intended or expected that Autonomy would call upon FileTek to pay. In cross-examination, Mr Szukalski told me that he understood that Mr Loomis's plan was to pay Autonomy only after FileTek received the money. He told me:

> *"…that kind of a structure in terms of payment after we get paid from a transaction where we are the fulfilment partner is a standard kind of reseller transaction. That's not something unusual to this transaction. That is something that, if you're a reseller fulfilment partner that often is the case."*

783. Indeed, and the second point emphasised, his understanding was that FileTek did not have the financial resources to meet its obligations under VT18 unless the end-user deal was closed and paid within the 120-day payment terms applicable to the VAR deal (i.e. VT18). Mr Chamberlain shared that understanding (as is apparent from an email from him to Mr Egan copying Mr Hussain in October 2010). The Claimants contended that the deal was inordinately risky for FileTek unless it was given the assurances they alleged, and it could be reasonably sure that in the meantime it would not be called upon to pay (which it never was and never did).

784. The Claimants further supported this point by referring to an email dated 1 February 2011 from Mr Szukalski to Mr Loomis, reporting on a discussion with Mr Egan after it became clear that the end-user deal with USDVA was in trouble. This included a paragraph stating: *"He wanted to ensure [sic, presumably assure] us that there is no risk to us"*. As regards that statement, Mr Szukalski's evidence was as follows:

> *"Q. So that reflects the assurance that Mr Egan gave you that there was no risk to FileTek?*
>
> *A. That's correct.*
>
> *Q. What that means is that there is no risk to FileTek that Autonomy will fail to honour the assurances that had been given to you at the time of signing the purchase order?*
>
> *A. That is correct.*
>
> *Q. And you trusted that assurance?*
>
> *A. We did. We had trust but it didn't come without a little bit of agita and concern that we were still on the hook for $10 million.*
>
> *Q. If Autonomy fails to honour the assurance?*
>
> *A. That is correct."*

785. The third point emphasised by the Claimants was that FileTek was to have no further involvement in the sales effort to close the prospective deal with the USDVA. Mr Szukalski told me in cross-examination:

> *"A. …One thing I do want to say again is that is not an unusual -- there are reseller partners that act as pure fulfilment partners. What I mean by that is it's just a contractual vehicle by which to sell -- resell software through. So there are partners who have no expertise in the technology or selling technology but they're just used as a simple contractual vehicle and they get a certain percentage of margin like we did. So to some extent I hear your questioning and it sounds a little bit like this is an unusual thing where we had no expertise in selling IDOL and in the world of -- the reseller world, there are partners called fulfilment partners that do just -- just push paper, that's all they do. They have no expertise, they don't add value and in this case, for this transaction, FileTek was acting as a fulfilment partner on behalf of Autonomy."*

786. The fourth point was that, according to Mr Welham, the arrangements for FileTek to have no further involvement in the sales effort to close the prospective deal with the USDVA were not disclosed to Deloitte. Deloitte were invited to and did approve VT18 on the basis of a misapprehension, which the Audit Committee (on the basis of what they were told) also shared, that FileTek would be attempting to conclude a deal with the USDVA, when in truth that was not the agreed plan. The Claimants relied in this regard on the evidence of Mr Welham in answer to a question put to him in re-examination whether:

> *"[i]f Autonomy retained sole charge of commercial negotiations with the end-user without any involvement by the VAR, that would have been relevant to Deloitte's audit judgement on whether to recognise that revenue on the sale to the VAR?";*

787. The relevance of this was basic:

> *"Because then it would suggest that the risk hadn't passed, if the VAR has to do nothing and Autonomy has to do everything".*

788. The fifth point emphasised by the Claimants relates to the same email (referred to at paragraph 784 above): the Claimants contended that Deloitte were never told that Mr Egan had given an assurance that there was *"no risk"* to FileTek. They suggested that Mr Welham's evidence to that effect was not challenged, and nor was his further evidence that, had Deloitte been aware of this, Deloitte would have wanted to understand whether there was some form of side agreement or understanding which meant that the risks and rewards of the USDVA transaction remained with Autonomy, which in turn would have prevented the recognition of revenue.

789. The Defendants countered each of these points as follows. With reference to the first (see paragraph 778 above), although the Claimants seized on Mr Szukalski's acknowledgement that he had been given *"assurances",* the Defendants maintained that the *"assurances"* to which Mr Szukalski was referring were limited to Mr Egan making every effort to "backfill" (as described above). They contended that there was no support for the vague reference in Mr Egan's witness statement to Autonomy promising that it would find *"some other way to make sure that FileTek would get paid and could then pay Autonomy"* (see paragraph 769 above).

790. Further, the Defendants insisted that there was never any understanding that FileTek would not be required to pay unless itself paid. Although the Claimants also sought to rely on Mr Szukalski's answers when cross-examined on this, which were to the effect that a "pay only when paid" structure was *"a standard kind of reseller arrangement"*, the Defendants pointed out that Mr Szukalski never suggested any actual agreement or assurance of that kind, simply an intention on the part of FileTek and an expectation that this would not be out of the ordinary. Likewise, in asserting that FileTek would not pay until paid the Defendants stressed that Mr Loomis was referring to *"my plan"*, rather than any bilateral agreement or shared understanding; and, since (they submitted) that would not suffice, that this undermined rather than supported, the Claimants' case.

791. The Defendants sought to deflect the Claimants' second point, that FileTek could not have paid $10 million out if its own resources if no end-user sale eventuated (see paragraph 783 above) by pointing out that (unusually) FileTek paid Autonomy $500,000 on the day the VT18 agreement was concluded and thereafter did in fact make payments in discharge of its contractual debt of $1.5 million in March 2011, $1 million in April 2011, $1.5 million in June 2011 and the remaining $6 million in August 2011, which in an Autonomy Accounting Update Memo on *"September 2010 to August 2011 Transactions"* were described as *"funded over time as cash flow became available"*. How that cash flow was generated, however, was the subject of dispute: the Claimants' case being that it was generated only because Autonomy bought software from FileTek for which it had no real need (the StorHouse purchases): see below.

792. As to the third point (see paragraph 785 above), the Defendants broadly accepted that FileTek was not to participate in negotiations with USDVA to close the proposed transaction: the points they emphasised were that (a) the role of 'fulfilment partner' (which was how Mr Szukalski openly and straightforwardly described FileTek's role) was standard in the industry (b) it was common practice that nothing was necessarily expected of such a fulfilment partner, except that the paperwork would go through it (c) similarly, it was entirely normal that the supplier (here, Autonomy) would negotiate and draw up the end-sale contract and then simply insert the fulfilment partner as either the contracting party or the party who would receive payment, as Mr Szukalski confirmed, see paragraph 781 above.

793. As regards the (admitted) intention that Autonomy was to carry on the negotiations with the USDVA, and even assuming (as Mr Welham and the expert witnesses were invited by the Claimants to assume) that it was to have "sole charge" of such negotiations, the Defendants stressed the difference between a situation where that was done because the VAR (here, FileTek) recognised that the prospect of closing the end-user deal was more likely if Autonomy, with its experience of and previous contact with the end-user, continued the negotiations it had started and was simply content to leave it to Autonomy, and on the other hand, a position where Autonomy retained the right and/or the responsibility under the VAR deal to close the end-user deal. Mr Miles took me in his oral closing to detailed cross-examination where, contrary to the Claimants' suggestion that Mr Welham had not been cross-examined on this, that point was put to Mr Welham, who accepted that what he had in mind was a *"further performance obligation…to close the deal with the end-user"*, whether expressly stipulated or to be inferred from the circumstances. The Defendants submitted that neither an express stipulation nor any inference of a commitment to the same effect had been demonstrated.

794. That also was the Defendants' answer to the Claimants' fourth point (see paragraph 786 above), which was to the effect that the Audit Committee was invited to consider and Deloitte were invited to and did approve VT18 on the basis of a misapprehension that FileTek would be attempting to conclude a deal with the USDVA, when in truth that was not the agreed plan. The Defendants distinguished between who was negotiating the final deal and who was intended to be the contracting party to it when closed, which the Claimants had elided. They contended that the Claimants' assumption that FileTek was not to be a contracting party was contrived and incorrect:

(1) Although Autonomy wished to pursue the negotiations with the USDVA itself, the Defendants insisted that FileTek was intended to be the contracting party in any deal ultimately concluded with the USDVA;

(2) That deal was considered to be *"on the cards"* (to use the Claimants' expression) and indeed that was the basis on which FileTek had agreed the VAR transaction (as Mr Szukalski repeatedly made clear).

795. On the Defendants' case, this also answered the fifth point emphasised by the Claimants (see paragraph 788 above), based on Mr Welham's evidence in his witness statement that Deloitte were never told that Mr Egan had given an assurance that there was *"no risk"* to FileTek. No disclosure was necessary: the risk passed in the usual way.

796. The Defendants also sought to turn against the Claimants their reliance on Mr Szukalski's 1 February 2011 email and Mr Szukalski's agreement in cross-examination that the email was saying that there was *"no risk to FileTek that Autonomy will fail to honour the assurances that had been given to you at the time of signing the purchase order"* (in further support of their third point, see paragraph 792 above). The Defendants' argument was that that answer, which was much relied on by the Claimants as being supportive of their basic case that the legal transfer of risk under the VAR agreement was illusory and that the deal lacked substance, had to be understood by reference to what Mr Szukalski meant by the *"assurances"*. If all the reference to FileTek not being at risk connoted was that Autonomy would do what it could to put FileTek in contact with another end-user, they submitted that it is extremely difficult to accept the Claimants' argument that it had a bearing on risk and reward.

Collapse of the USDVA deal and its aftermath

797. Before assessing these competing contentions, it is convenient to address what the Claimants described in their written closing submissions as the *"Unravelling of the FileTek VAR transaction"*.

798. In his email of 30 September 2010 (see above) explaining the VAR deal to Mr Thompson, Mr Loomis stated that:

> *"Three scenarios have been considered: (a)VA orders as planned, i.e. in Q4, (b) VA order is deferred to Q1, (c) Disaster: something fully unexpected either further delays or eliminates the opportunity. Our plans for each are as per our telephone conversation. We have ability to reassign the license."*

799. In the event, "disaster" occurred (though it was perhaps not *"something fully unexpected"*): no deal was concluded with USDVA by either FileTek or Autonomy. As foreshadowed above, the Claimants alleged that FileTek was only enabled eventually to discharge by instalments its debt under the VAR agreement to Autonomy because of an allegedly contrived transaction pursuant to which Autonomy acquired from FileTek the StorHouse and Trusted Edge software for which it had no real use at an overvalue.

800. As explained in paragraph 2735 and footnote 317 of the main body of the judgment, the purchases of software by Autonomy from FileTek in March, June and August 2011 ("the 2011 StorHouse transactions") were the last in a series of such purchases. The earlier purchases (in Q4 2009 and Q1 to Q2 2020) were impugned as improper "circular", "round trip" or "reciprocal" transactions (labelled together as "RT 3"). The 2011 StorHouse transactions were not labelled and impugned by the Claimants as "reciprocals", in that their alleged vice was not that they were a purchase by Autonomy to fund a sale by

Autonomy (as in the case of the "reciprocals" in RT 3, which did not involve a VAR) but the means of funding VT18 (labelled by the Claimants as "Reciprocal VARs"). The 2011 StorHouse transactions were also alleged to give rise to transaction-based losses which were identified at Schedule 12B and sought to be recovered from Defendants as part of the Claimants' breach of duty claims against the Defendants.

801. The purchases comprised:

(1) Two Q1 2011 purchases of software for on-sale to HP and to Morgan Stanley, for \$1.76m and \$739.8k respectively.

(2) A Q2 2011 purchase for \$1.596m for three specific customers in respect of the Iron Mountain data centre migration.

(3) A Q3 2011 purchase for \$7.5m of an unlimited licence for use in the Iron Mountain data centres.

802. It is not disputed that in cashflow terms FileTek was assisted in making payments due under VT18 by its receipt of the sale proceeds; nor that FileTek thereafter paid \$1.5 million in March 2011, \$1 million in April 2011, \$1.5 million in June 2011, and the remaining \$6 million in August 2011.

803. The Claimants addressed each of these StorHouse transactions in considerable detail in their written closing submissions in seeking to make good their over-arching allegation that it was obvious that these payments were:

> *"the means by which Autonomy honoured Mr Egan's assurance, given at the time of the VAR transaction, that FileTek would not be left holding the bag."*

Q1 2011 StorHouse purchases

804. The Claimants contended that Autonomy's justification for the two Q1 2011 StorHouse purchases, which was that they were made with a view to on-sale to Morgan Stanley and HP, was false. As to that:

(1) They submitted that there was no supporting documentation or any evidence from Morgan Stanley itself to show that Morgan Stanley needed and wanted to acquire FileTek software as part of a package also comprising licences for other Autonomy hosted software. They suggested that StorHouse software had been added onto an existing order from Morgan Stanley without any specific request for it; and they rejected Dr Lynch's explanation (when cross-examined):

> *"Q. You are not aware of any suggestion that Morgan Stanley wanted to be supplied with any StorHouse–based capability, are you?*
>
> *A. Well, they wanted the functionality it brought. I doubt if they would have known, without looking into it, the name of the product, but they certainly wanted the ability to load structured data.*

> *Q. It very much looks as if StorHouse is being given new software, even though it's not something Morgan Stanley had asked for, would you agree?*
>
> *A. No. Morgan Stanley is a sophisticated purchaser. It would check everything, it had a whole series of tests it would have to do, for example to do with whether there was restricted encryption and things like that, so they wouldn't accept something they didn't have some basis for understanding why it was there."*

(2) They contended that Autonomy already had existing StorHouse licences to use StorHouse for its hosted customers, and so Morgan Stanley, being a hosted Digital Safe customer, had no need for any further licence for itself. They again rejected Dr Lynch's evidence, when cross-examined, that this analysis was:

> *"incorrect, because Morgan Stanley liked to own its own licences so it had done a deal where it owned its own software licences and so it wanted the full set of licences so that it had the option if it wanted not to be hosted. So it owned its licences which it in effect lent back to us to host. We could not allow Morgan Stanley, even if we were running it in a hosted environment, to own their licence."*

(3) The Claimants contended that the suggestion that HP wanted StorHouse was even less credible. HP had a competitor product to StorHouse. In January 2010, Dr Lynch had asked HP for a quote for that product, which presupposed that the HP product could be substituted in place of StorHouse; and (the Claimants submitted) it is implausible to suggest that HP decided to pay Autonomy to purchase from FileTek a licence of software that competed with HP's own software.

(4) The Claimants relied also on the correlation between the payments Autonomy made to FileTek and the payments then made by FileTek to Autonomy as demonstrative of their primary purpose as alleged. Thus:

(a) On 31 March 2011, Autonomy paid the $1.769 million in respect of the HP invoice but did not pay the approximately $740,000 in respect of the Morgan Stanley invoice.

(b) Then, also on 31 March 2011, instead of paying $2.5 million to Autonomy, as Ms Leslie Levy's (who worked in FileTek's accounts department) email a day before had foreshadowed, FileTek paid Autonomy the lesser sum of $1.5 million, in respect of FileTek's debt under the VAR agreement. FileTek's payment was just less than the $1.769 million that FileTek received from Autonomy that day.

(c) What FileTek did, as regards the balance of $1 million that Autonomy was expecting to receive, was to write a cheque for $1 million, which FileTek then held pending receipt of further funds from Autonomy.

(d) On 6 April 2011, FileTek received an auditor debtor confirmation letter from Mr Chamberlain. Mr Szukalski's evidence was that he used Autonomy's need for the auditor confirmation letter as leverage in order to obtain information from Autonomy about the progress of the USDVA deal or any alternate deal that could be used to put FileTek in funds.

(e) The next day, 7 April 2011, Autonomy paid FileTek the sum of about $740,000 in respect of the Morgan Stanley invoice. Once this money had arrived, FileTek had received an aggregate of $2.508 million and Mr Loomis therefore authorised the $1 million cheque to be sent to Mr Scott.

805. In relation to the Claimants' case on the Q1 2011 StorHouse purchases, the Defendants countered the Claimants' assertion that neither of those companies (Morgan Stanley nor HP) had any use for or had ever wanted the software and that Autonomy had simply added it on to the Autonomy software supplied to each as a way of showing its actual deployment on the following basis:

(1) The suggestion that Autonomy had simply insinuated StorHouse as part of the package of licences acquired by each of them was unrealistic. Both Morgan Stanley and HP would have had a use for FileTek. Moreover, both were sophisticated purchasers who would have known what they were purchasing and scrutinised their contracts. They would not have acquired software unless they wanted to.

(2) The documents supported this, showing that:

(a) numerous individuals were involved in the inclusion of this software, including Mr Avila and Mr Guiao, as well as Mr Crumbacher, Mr Chamberlain, Mr Scott, Mr Egan and Dr Menell;

(b) in the case of HP, there were specific communications highlighting the FileTek software, and its appropriate location in the contractual software list.[72]

(3) Mr Scott's suggestion in his evidence in the US criminal proceedings that Autonomy did not need a licence in order to resell to Morgan Stanley, because of the existing Autonomy licence for use in the hosted environment was simply incorrect. Although the Claimants put to Dr Lynch that this was correct, the Defendants submitted that it was in fact wrong, and obviously so: the existing licence for Autonomy to use StorHouse in its hosted environment could never have permitted Autonomy to sell a licence to Morgan Stanley, which Morgan Stanley could then take and use onsite and/or in a third party data centre.

(4) Although the Defendants suggested that this was another example of the dangers inherent in the Claimants' selective reliance on hearsay evidence that Dr Lynch has never been able to test, they also noted that in this instance, Mr Scott did in fact qualify his evidence significantly in cross-examination, which

[72] HP also appear to have understood that there was a structured data focus.

the Claimants did not go to with Dr Lynch (even though they marked up the passage as being their own hearsay evidence).

> *"A. My one hesitation is without looking at and reading through all of the agreements and trying to understand exactly how they fit together, I can't be certain; but based on the way that you've presented the facts, if Autonomy has a license where only Autonomy can use it internally and we want to give a customer the right to use this software on their own outside of the Autonomy environment, I believe that wouldn't be covered by the first license.*
>
> *Q. All right. And so you'd be wrong when you said it was gratuitous?*
>
> *A. I would be wrong in that case."*

(5) The Claimants had at one time also suggested that the purpose of the email from Mr Chamberlain to Ganesh Vaidyanathan (who worked within the Autonomy finance team), copying Mr Scott and Mr Hussain, on 31 March 2011 was to create a "false paper trail", but the documents do not support that, and it would not have appeared that way to anyone at the time.

806. As to the inference that the Claimants had submitted should be drawn from the correlation between the payments made by Autonomy and the payments made by FileTek to reduce its outstanding debt, the Defendants submitted that it was only to be expected that Autonomy's payment to FileTek was followed by a payment to FileTek to reduce its existing indebtedness. This was a normal business practice.

Q2 2011 StorHouse purchase

807. Similarly, in relation to the June 2011 StorHouse purchase, the Defendants' averred justification was that Autonomy had been asked to obtain such software for three customers, namely, Barclays Capital, BofA and Morgan Stanley. The Claimants rejected this also; they pointed out that in an internal email dated 18 July 2011 Deloitte had confirmed that no licence sales to those customers had in fact taken place and derided Dr Lynch's response that he did not mean that such sales were to be completed immediately as *"another example of Dr Lynch being prepared to say anything that he thought might suit his case."*

808. Further, the Claimants alleged that none of the three customers ever needed the product, all being hosted customers; and they pointed also to Mr Wang's reaction to the news of the further purchase, being:

> *"What's the deal, we're buying more FileTek licenses".*

809. The Claimants also noted that, though it had negotiated a discount, Autonomy in fact paid, without any suggested reason, the full undiscounted amount of $1.596 million, and that on the same day FileTek used the money it received to pay $1.5 million on that same day.

810. In the case of the Q2 2011 StorHouse deal, Dr Lynch's understanding, as he explained in his witness statement, was that the expected use of StorHouse for which licences were

required was to try to make Iron Mountain data centres more efficient and profitable and bring them into line with Autonomy's profitable data centres: Iron Mountain data centres, which had come under Autonomy's control when it acquired Iron Mountain's digital archiving business in Q2 2011, and which had a considerable amount of stored data, had been operating at 0% operating profit, compared to the 40% operating profit expected in Autonomy's own data centres. The Defendants noted that it was not suggested to Mr Szukalski that the sale was not at fair value (or that he did not understand there to be a genuine requirement for StorHouse for these Iron Mountain customers).

811. As to the further points made in relation to the Q2 2011 StorHouse deal, the Defendants argued that:

(1) The Claimants' suggestion that, after Autonomy's acquisition of Iron Mountain Autonomy may not have needed the licence because its existing 2010 licence to use StorHouse in its data centres could have included using StorHouse in Iron Mountain data centres was not how Dr Lynch perceived the position at the time. He told me that his belief was that this was not permitted and had been so advised (though he could not say who by). Mr Loomis likewise assumed that Autonomy needed a further licence. The Defendants suggested also that it was also noticeable that the Claimants did not put this point squarely to Mr Szukalski.

(2) Secondly, the Claimants' suggestion that Dr Lynch would have discussed this transaction with Mr Hussain and would have been told that this transaction was channelling funds to FileTek was misplaced. Dr Lynch rejected this, and indeed explained that it was unlikely that he would have discussed the transaction at all with Mr Hussain.

(3) Thirdly, in answer to the suggestion that no onward sale had taken place at the time of the purchase, there was no requirement that it should have done so.

Q3 2011 StorHouse purchase

812. As to the third and last of the 2011 StorHouse purchases (in August 2011), the Claimants portrayed as coming *"apparently out of the blue"* an email dated 1 August 2011 from Mr Hussain to Mr Egan, copying Dr Menell, which was blank except for a subject line which read *"also please on FileTek for expansion to IRM* [Iron Mountain] *data centres"*.

813. The Claimants submitted that:

(1) The fact that the email was otherwise blank suggested that this was:

> *"a reminder for Dr Menell to say something about the need for FileTek in an Iron Mountain Digital context that Mr Hussain had already discussed with Dr Menell."*

(2) The exchange which followed was confected. The email duly prompted Dr Menell to send an email asking whether the existing StorHouse licences covered the Iron Mountain Digital data centres. Mr Hussain replied, "*Can we get a proposal please*".

(3) The purchase price was calibrated to ensure that FileTek would have enough to discharge the outstanding debt. Thus, Mr Egan approached FileTek for another quote for more StorHouse software for Iron Mountain Digital customers. Mr Egan gave Mr Szukalski a range of $6.9 to $7.1 million for the amount that Autonomy was willing to pay. These figures exceeded, by approximately $1 million (the amount of the margin promised to FileTek), the outstanding debt owed by FileTek to Autonomy in respect of the USDVA VAR transaction ($6 million). The Claimants submitted that this was surely not a coincidence.

814. The Claimants also relied on the urgency demonstrated by Autonomy to effect the purchase. Mr Szukalski said that Mr Egan indicated that he needed a quote for the StorHouse licence the next day, as a matter of some urgency. Mr Szukalski sensed that urgency, though not any particular reason for it; and whilst FileTek needed a solution to its indebtedness urgently too, resolved to use it as leverage to obtain a better deal for FileTek in relation to its sale of StorHouse and the maximisation of its revenue whereby to pay down its indebtedness under VT18 (it being the shared expectation of the parties that the sale proceeds would be so applied). Thus:

(1) On 15 August 2011, Mr Hussain wrote to Dr Menell and Mr Egan, copying Mr Kanter and Dr Lynch, stating:

> *"Gents – we have I believe completed the negotiations on the Filetek software for the Digital data centres. Based on Digital run rate revenues of around $150m a year the final number which is approximately $7m is fine. Remember that we have paid larger amounts for our data centres. Again I am asking for Pete's final tech sign off and either Andy or MRL for counter sign off to my sign off."*

(2) Dr Lynch gave his approval by email dated 16 August 2011. Dr Lynch said in cross-examination that, before doing so, he would have discussed it with Dr Menell.

(3) The next day, Mr Scott asked Mr Szukalski for an invoice and said that, if it could be provided shortly, "*we may be able to pay today*". Mr Szukalski obliged and Mr Chamberlain asked Ms Harris to "*process payment asap*" .

(4) Evidently, Mr Chamberlain was very concerned to ensure that the money was sent to FileTek that day: and there are email exchanges within the finance department showing his irritation when there were some minor delays. The only plausible explanation for this sense of urgency was that Autonomy needed to channel money to FileTek on 17 August 2011, so that FileTek could pay off its VAR debt, prior to HP's announcement of the Autonomy acquisition on 18 August 2011.

(5) Autonomy did indeed pay FileTek $7.569 million that day (17 August 2011), and the next day, (18 August 2011), FileTek paid Autonomy the entirety of its outstanding debt of $6 million under the VAR agreement in accordance with what Mr Szukalski had agreed with Mr Egan.

(6) The same day (18 August 2011), Mr Loomis sent Mr Thompson the news that HP was to acquire Autonomy. Mr Thompson responded, "*Now you have the explanation*". Similarly, Ms Levy (of FileTek) remarked in an email dated 22 August 2011 that the HP acquisition was "*why we probably got the deal mid quarter ... Just to close it out before new mgmt*".

815. The Defendants, however, rejected the Claimants' allegations that the funding of FileTek was the true rationale of the sequence of purchases of StorHouse licences by Autonomy.

816. They contended that all the StorHouse deals were genuine independent sales, and that StorHouse was a good and cost-effective database storage product for customers with large commercial databases which Autonomy needed to be able to offer as part of its objective of becoming a force in the market for hosting and searching structured data.

817. The features of StorHouse which made it valuable to Autonomy are elaborated in the chapter on Reciprocal Transactions in the main body of this judgment, where I also set out the facts relating to a further dispute as to whether there was ever any proper assessment made by Autonomy of the product prior to the various licence purchases. For the present it suffices to say that the Defendants maintained strongly that StorHouse was a product of great potential value and use to Autonomy, which Autonomy could not readily have built it itself, and which it did in fact deploy, and that each of the various purchases had a strong commercial rationale.

818. As to the last in the sequence of StorHouse transactions, the Q3 2011 StorHouse purchase, which was of an unlimited licence use in Iron Mountain data centres and which extended Autonomy's ability to use StorHouse to all customers operating in the Iron Mountain hosted environment (as well as the DRC-CM product, Iron Mountain's hosted products, included LiveVault, which was a cloud-based back-up and disaster recovery product). As to this, the Defendants' position was:

(1) Dr Lynch explained in his witness statement that Autonomy had initially purchased the licence for a few customers but subsequently decided it made sense for there to be a full overhaul of the data centres.

(2) Dr Lynch approved the Q3 2011 StorHouse purchase by email on 16 August 2011. This email chain showed Dr Menell's prior request for the licence for to cover the expected use of FileTek in the Iron Mountain data centres, as well as Mr Hussain's prior confirmation that the price was "*fine*". Dr Lynch was asked to confirm Mr Hussain's sign off and told that Mr Scott and Mr Egan had "*done the negotiations and the legals*". Dr Lynch wrote: "*yep if this gets their zero op margin stuff to our architecture*". As stated above, Dr Lynch's witness statement explained his understanding that Iron Mountain were operating their data centres at a 0% operating profit, while Autonomy's data centres operated at a 40% operating profit.

819. Dr Lynch rejected the suggestion that this transaction was done solely to put FileTek in funds, and that his own approval was a "false paper trail". The Defendants contended that it is impossible to square the allegation with (a) the acceptance by the Claimants' witnesses that the StorHouse product was in fact used to migrate customers on the DRC-CM product, and (b) the fact that Mr Lucini was enthusiastically promoting the use of StorHouse in LiveVault both to customers and to analysts in the market.

820. The Defendants also relied especially on:

(1) Mr Szukalski's evidence to the effect that Mr Egan had approached FileTek with the transaction, and the expectation was that the funds would be used to pay down the USDVA debt. It was not suggested to Mr Szukalski that the StorHouse licence was at anything other than fair value. Nor was it suggested that he understood the desire to have StorHouse for Iron Mountain to be anything other than a genuine business desire on Autonomy's part. Mr Szukalski's testimony had in fact been that FileTek was excited about the opportunities for adding StorHouse to Autonomy's product offerings. Mr Szukalski was not prepared to agree with the conclusion that was put to him, that it was unlikely that FileTek would have received the extent of StorHouse orders from Autonomy that it did in 2011 if it had not entered into the USDVA contract (though he did accept that it was Mr Bill Thompson's conclusion).

(2) Mr Scott, who had negotiated the Q2 and Q3 2011 purchase transactions, and whose evidence in the US criminal trial suggesting that Autonomy did not need any further licence in order to resell to Morgan Stanley because of the existing Autonomy licence for use in the hosted environment the Claimants much relied on in the context of VT18, did not consider he was doing anything illegal in making the purchases: and that was the Claimants' own hearsay evidence.

821. In their cross-examination of Dr Lynch in relation to StorHouse the Claimants questioned the extent to which StorHouse was ever eventually used. I have already addressed this issue when dealing with the other StorHouse purchases discussed in the chapter on Reciprocal Transactions in the main body of the judgment. For the present I need only mention that amongst the questions put particularly relevant to the 2011 StorHouse transactions were (a) whether there were in fact any sales, including to Morgan Stanley and HP, in addition to the inclusion of StorHouse in the database connector and (b) whether StorHouse was ever in fact set up in Autonomy's data centres.

822. In addition to their overall submission that this involved a high level retrospective view on subsequent events which had little bearing on the merits of the earlier purchase decisions at the time they were made, the Defendants contended as follows:

(1) There were in fact sales of StorHouse, including to HP and Morgan Stanley, in addition to the inclusion of StorHouse in the database connector. Moreover, StorHouse was used for the DRC-CM migration, actively offered to a number of other archiving customers, and discussions progressed to an advanced stage with Kraft before Kraft's priorities changed.

(2) In addition to installation in Pleasanton, the evidence shows that Mr Lucini was purchasing hardware in order to install StorHouse in all the Iron Mountain data centres. It is unclear how far the installation in the individual data centres progressed. However, Mr Lucini felt able to include a reference to the StorHouse/LiveVault integration in the literature for LiveVault customers, as well as to promote it to customers as part of the LiveVault structured data offering.

(3) Again, in each case, what matters is what people thought at the time, not hindsight. StorHouse was incorporated into Autonomy's product line and made

available to customers. It was seen as a valuable product for that purpose at that time.

My assessment of VT18 and the 2011 StorHouse transactions

823. The FileTek/USDVA transaction (VT18) was a particularly stark one in the sense that FileTek was not a VAR and there was never any suggestion that FileTek would do anything more than be a "fulfilment partner"; all it was to do was to *"hold the paper"*. Further, it was not disputed that Mr Egan did give Mr Szukalski certain assurances, both at the time of and after the VAR transaction.

824. There were inconsistencies between them, and between Mr Szukalski's evidence in his witness statement and in cross-examination, as emphasised by the Defendants. But it seemed to me that Mr Loomis and Mr Szukalski largely agreed on what they understood to be the fundamentals of the deal. I consider that, notwithstanding certain other inconsistencies, the fundamental message of both witnesses (Mr Loomis and Mr Szukalski) was clear:

(1) FileTek, though it had assumed legal risk, both expected to receive the proceeds of the end-user sale before its payment obligation arose, and was assured that if there was some delay, or no end-user sale eventuated, Autonomy would (a) not press for nor expect payment by FileTek out of its own resources and (b) find another end-user without FileTek having itself to make any effort to do so, to enable FileTek to pay Autonomy out of the proceeds in due course or if the worst came to the worst, Autonomy would find some other way to ensure that FileTek got paid so that FileTek could then pay Autonomy.

(2) FileTek would have no contact with either the pre-approved systems integrators or the ultimate end-user in any event: it was simply a *'fulfilment partner'*.

825. By this I consider they meant that, all FileTek conceived it had to and in the event did do, was to act as intermediary between the supplier (here, Autonomy) and rival pre-approved suppliers of a Federal agency (here USDVA). Its assumption of legal liability was a risk, but one covered by the assurances given; and it was not intended to interrupt or affect in any way Autonomy's ability to negotiate and contract with the ultimate end-user with whom it had a long-standing relationship and which it hoped to persuade to accept a bid from one of the pre-approved systems integrators bidding for the large deal which was using IDOL software.

826. It probably does not ultimately matter whether there is a difference in the market between a fulfilment partner and a VAR. I suspect there is in the market: but in this case, there was not: however classified, none of the 'purchasers' from Autonomy under VAR sales was intended to play any active role. Further, there is danger in looking at such questions though the lens of IFRS accounting standards: any market distinction may have been agnostic in that regard. Nor without more do I accept, though it was neatly expressed, Mr Rabinowitz's submission in his oral closing that *"the clue is on the tin. Value added resellers. They add value…""* and that *"If the VAR just sits there and does nothing, then you cannot recognise revenue"*. Revenue recognition under IAS 18.14 does not depend

upon the characterisation of the parties, but on the substance of the transaction, and its substantive effect (if any) in terms of the transfer of risk and management control in respect of the goods the subject of the transaction from which revenue is said to have been generated.

827. That said, to satisfy the revenue recognition criteria it seems to me to be clear that there must be some change in the substantive economic relationship of the seller in relation to the goods apparently 'sold'; and concomitantly, the purchaser must in substance and in reality take over, not only custody, but control of the goods apparently 'sold', and either use them or have effective control of their disposition or retention.

828. In the case of VT18, it is clear, in my judgment, that FileTek never had control of the goods sold in any substantive sense. Autonomy retained managerial control, and the shape of the arrangements was such that (reflecting the words of IAS18.14(b)) it remained managerially involved to a degree usually associated with ownership. Whatever FileTek was to do, it was to do at Autonomy's direction: it was (and the words on this tin are instructive) a fulfilment partner, its task being to fulfil according to Autonomy's direction the contract which Autonomy would negotiate and conclude. The relevance of the fact that FileTek was intended and expected to do, and did, nothing except *"push paper"* is that it demonstrates that effective control and management involvement was never passed to FileTek.

829. The question as to the passing of risk in this context (as in the context of all the impugned VAR transactions) is not as straightforward. The passing of risk is primarily a legal concept, and (as noted previously) the various examples given in IAS18.16 and 18.17 lead the eye to legal tests. Even so, there was ultimately no disagreement to the proposition that accountants must determine accounting treatment according to the substance of a transaction; and the question is whether in substance FileTek took on the risks and rewards of ownership of the goods. A unilateral expectation on the part of the purchaser, or even an assurance given to it, that the vendor will "see him right" does not necessarily negate the passing of the risk of ownership or remove its rewards.

830. The real question is whether in economic reality it was Autonomy or FileTek which was expected and intended to suffer the consequences or enjoy the benefit if the proposed sale to USDVA failed. In my judgment, the assurances given to FileTek reflected the reality that one way or another it would be Autonomy which would have to sort out the mess. That is undoubtedly the understanding given to FileTek and equally undoubtedly what FileTek expected, albeit with a *"little bit of agita"* (see paragraph 784 above) about the residual risk of legal liability. I accept the Claimants' case that without that assurance and expectation, FileTek's risk would have been obviously disproportionate.

831. More generally, it seems to me to be clear that VT18 was not intended to transfer to FileTek any of the incidents of ownership: it was intended to be simply the means of booking revenue in advance of a sale by Autonomy, rather than in substance a sale to FileTek. The 'sale' was a legal fact but a nominal arrangement: the real sale from which Autonomy sought to be rewarded was the direct sale by Autonomy to the USDVA. Further, or perhaps another way of expressing the same basic point, Autonomy had no grounds to suppose, nor any intention or expectation, that FileTek had the means to pay out of its own resources or any real ability to fund its obligations by a sale of the product it had nominally acquired.

832. Also in accordance with a different aspect of the pattern, the Defendants emphasised that Deloitte had approved the accounting treatment of VT18. However, as in other contexts, I do not consider this reliance was justified. I agree with the Claimants that Deloitte were not given a fair and proper description and understanding of VT18, or, in particular, of Autonomy's continued exclusive control of the negotiations with USDVA and FileTek's essentially nominal role. Their approval of revenue recognition does not, in such circumstances, assist.

833. Given the conclusion that follows that VT18 did not satisfy the requirements of IAS18.14 or even the basic test that there should be in substance a true 'sale', so that it was not proper to recognise the 'sale' price as revenue, it is not strictly necessary for me to determine in this context whether the only real or at least the driving purpose of the 2011 StorHouse transactions was to fund FileTek in order to clear its indebtedness (a matter of particular and growing importance to Autonomy in preparation for completion of the HP acquisition). However, I can for present purposes summarise my views as follows:

(1) The evidence has not persuaded me that Autonomy had no need or use for StorHouse, but

(2) A powerful driver of the purchases was the objective of providing funds to FileTek.

(3) The 2011 StorHouse transactions provide further supportive evidence of my conclusion that VT18 was not a true 'sale' and no revenue should have been recognised from it.

Defendants' knowledge of and participation in VT18

834. Mr Hussain's direct involvement in VT18 is clear. Mr Egan's evidence was that it was he and Mr Hussain who told Mr Loomis and Mr Szukalski in their discussion on 30 September 2010 that Autonomy would be responsible for arranging the end-user deal and FileTek would not engage in the actual sales effort, in terms quoted in paragraph 769 above. That evidence was not challenged; and having regard also to the general matters previously referred to (including his part in the genesis of the strategy and the development of the pattern) I consider and find that Mr Hussain knew about and was responsible for Autonomy then handling the continuing negotiations with the USDVA itself and knew that FileTek had no real part to play except to *"push paper"* and act in accordance with Autonomy's directions.

835. In my judgment, Mr Hussain cannot have thought that the criteria for revenue recognition were satisfied; and his failure to see to it that Deloitte had a fair picture of what truly was FileTek's role reinforces my view that he knew it was difficult to square with any true sale: he had "guilty knowledge" that the recognition of revenue from VT18 was improper.

836. As was usually the case, Dr Lynch appears to have been kept or kept himself at one place removed. Dr Lynch accepted in cross-examination that he "*may well have been*" aware of the reseller deal before the deal was signed. He thought that this information *"would come normally from Mr Hussain*". But though interested and kept informed at a high level there was no transaction-specific evidence that he was involved in the actual selection of FileTek, or in any conversation with FileTek (and it is not suggested, for example, that he was aware of the discussion between Mr Egan, Mr Hussain and FileTek on 30 September 2010). Nor was there any transaction-specific evidence of his involvement in or

knowledge of any arrangement that FileTek should not participate in any of the ongoing negotiations between Autonomy and the end-user nor of the fact that it did not.

837. I do not therefore consider that the evidence specific to VT18 advances materially the Claimants' case that Dr Lynch had "guilty knowledge". However, the evidence is consistent with my more general conclusion that the programme of which the impugned VAR sales, including VT18, were examples, was devised by Dr Lynch and Mr Hussain together for the purpose of making good shortfalls in revenue.

838. It is clear from email exchanges that Dr Lynch did continue to take an interest in the USDVA deal; and Mr Hussain was in *"nearly daily"* contact with those concerned pressing for a deal in Q3 2010. The USDVA deal was, as Dr Lynch accepted in cross-examination, *"Definitely a big deal for Autonomy".* Dr Lynch's anger when it appeared that the deal had been imperilled or delayed because someone at Autonomy had irritated the USDVA by charging them for minor expenses to fix a fault on Autonomy's software is evident from the email dated 7 August 2010 from Dr Lynch to Mr Hussain, Mr Still, Mr Egan, Dr Menell, Mr Mooney, Mr Sullivan and a Mr Bryan Rellinger which I have quoted in paragraph 758 above. The email betrays his supervision and interest, as well as his hands-on management style, exemplified by his demand that if there was a problem with the potential USDVA deal, "*I want to know about it and, you know, at a high level I'd expect to be kept informed*".

839. In all the circumstances of the transaction itself, and taking into account also his approval and encouragement of the strategy and knowledge of the pattern, in my judgment, Dr Lynch knew that the sale to FileTek was in a commercial sense illusory, that Autonomy retained risk and control and that it was improper to recognise revenue from it; and that constituted "guilty knowledge" on his part.

PART II OF SCHEDULE OF IMPUGNED VAR TRANSACTIONS

840. In this Part II of the Schedule, I consider four further impugned VAR transactions with Capax Discovery which followed VT10 (see paragraph 47 in the first part of this Schedule). These were VT20 (in Q4 2010, for end-user DKO), VT27 (in Q1 2011, for end-user McAfee), VT28 (in Q1 2011, for end-user UBS), and VT34 (in Q2 2011 also for end-user UBS).

841. In my judgment, these further impugned VAR transactions with Capax Discovery:

(1) further illustrate the pattern of using a VAR as a *"placeholder"* evident from VT2, 3, 4 and 10 and the complicity of the 'friendly' VAR, Capax Discovery;

(2) provide further examples (in each case) of the basic objections to revenue recognition, being (in summary) that the sale to the VAR was illusory and the VAR, despite the legal trappings, was (a) not to be involved in any onward sale negotiations nor in any end-user sale that eventuated (save in certain cases as the passive recipient of the proceeds of a direct sale between Autonomy and the relevant end-user to enable it (the VAR) to make good its outstanding payment obligation to Autonomy) and (b) never to be required to meet any payment obligation until put in funds by Autonomy (or an end-user sale contracted directly between Autonomy and the end-user);

(3) also provide further examples of involvement and in any event knowledge of impropriety on the part of both Defendants in respect of (a) the payment of large MAFs and (b) most importantly improper revenue recognition and false presentation of the performance and position of Autonomy in its published information.

Four further impugned transactions with Capax Discovery

VT20: Capax Discovery/DKO Q4 2010

842. VT20 was a VAR transaction between (or originally between) Capax Discovery and the US Department of the Army, acting through a portal known as Defence Knowledge Online ("DKO").

843. Once again, Capax Discovery was introduced as a VAR at the very end of a quarter, in this case Q4 2010, when the prospect of finally concluding a prospective deal, in this case between Autonomy and DKO, before the end of the quarter collapsed. This was the other VAR transaction on New Year's Eve which Mr Baiocco described as *"particularly memorable"*: see paragraph 1044 below.

844. As with previous Capax Discovery VAR deals with Autonomy, VT20 was entered into on the terms of the June 2009 Capax Discovery VAR Agreement (the principal provisions of which are summarised above). The relevant purchase order was prepared for Capax Discovery by Autonomy, and was for a licence fee of $1,950,197 plus $292,530 for support and maintenance. Such sums were payable in instalments as follows: $747,575.66 on 31 March 2011, $747,575.67 on 29 June 2011 and $747,575.67 on 27 September 2011.

845. The features of VT20 relied on by the Claimants, in addition to their general points, as demonstrating particular adaptations of the 'pattern', and that there was not really a sale to the VAR at all, were:

(1) A special provision in the purchase order contemplating and making provision for, but describing as *"unlikely"*, a direct deal with Autonomy: the Claimants described the provision, and another provision in the same purchase order for the payment of a MAF *"as full compensation in connection with VAR's efforts in securing End-User's procurement of a licence of Autonomy software"*, as *"a work of fiction"*;

(2) After the negotiation of a direct sale between Autonomy and DKO, its implementation by a series or convolution of sales of the relevant software licence, first by Capax Discovery to MicroTech, followed by a sale from MicroTech to DKO, necessitating also certain amendments to the terms of the Capax Discovery purchase order; and

(3) The family connection between the Autonomy salesperson (Mr Dan Truitt) and his brother Mr Steve Truitt (COO of MicroTech).

846. As to (1) in paragraph 845 above, the purchase order contained, just before the signature block, a provision like that in VT23 (discussed below) as follows:

> *"Although End-User and VAR currently anticipate entering into such a license transaction [i.e. with one another], in the unlikely event End-User, instead, enters into a direct agreement with Autonomy or its affiliate to license the Software, then VAR shall distribute the Software to End-User upon receipt of written notice (which may be via email) from Autonomy ('<u>Distribution Notice'</u>) of such direct license transaction. In the event distribution is accomplished by reason of a Distribution Notice, upon such time as Autonomy has received payment in full for such license fee and th[r]ee years of support fees, Autonomy shall pay to VAR an amounts [sic] equal to the license fee and three years of support fee paid by End-User to Autonomy less the Licence Fee and Annual Support Fee (for three years) described above, but in no event more than US$224,272.00, as full compensation in connection with VAR's efforts in securing End-User's procurement of a license of Autonomy software."*

847. The Claimants depicted this provision as *"a work of fiction"*, on the grounds that in fact:

(a) Capax Discovery and DKO did not anticipate entering into a licence agreement with one another. They had had no contact with one another. They never did have contact in respect of the licence. It was Mr Baiocco's unchallenged evidence that "*we did not expect Capax Discovery to have any dealings with DKO*". The Claimants submitted that there is no reason to suppose that DKO even knew of Capax Discovery's existence, still less of its involvement in respect of what Autonomy was negotiating to sell it.

(b) A direct agreement between Autonomy and DKO, though by no means assured, was much less "*unlikely*" than an agreement negotiated between Capax Discovery and DKO, which was never going to happen.

(c) Capax Discovery was not intended to expend, and did not expend, any "*efforts in securing End-User's procurement of a license of Autonomy software*" and there was no basis for it being compensated as if it had. Capax Discovery had only learned of the potential DKO transaction earlier the same day (31 December 2010).

848. The Defendants did not accept any of the above criticisms of the provisions. Dr Lynch submitted that:

(a) The new provision was a clause inserted into other reseller deals in the quarter.

(b) Deloitte reviewed the clause and were satisfied that it did not undermine revenue recognition. Deloitte's Defence to the FRC's Formal Complaint, which it still stands by, reads as follows:

> *"The clause therefore envisaged that on occasion Autonomy might enter into a transaction with a VAR, but subsequently deal directly with the end-user. In those circumstances, once Autonomy had received payment from the end-user, it would pay a fee to the VAR.*
>
> *The audit team concluded that this new clause did not affect revenue recognition. Upon the VAR entering into the agreement, it had accepted the risks and rewards of ownership. It had possession of the licence, and the ability to sell it to the end-user without requiring the involvement of Autonomy. It was legally required to pay Autonomy. The existence of the new clause did not change the analysis is respect of IAS 18 paragraphs 14(a) and (b) as the risk remained with the VAR, unless a direct deal was concluded with the end-user, a risk the VAR could not control."*

(c) The Claimants' criticisms of the clause were overblown. As regards the wording in the purchase order to the effect that Capax Discovery and DKO *"anticipate entering"* into a licence agreement they were misplaced. The words were standard rubric but in any event the clause reflected the expected arrangement at the time of the deal, namely that Capax Discovery would enter into the deal with the end-user, as Mr Baiocco confirmed. Dr Lynch contended that there was no basis for asserting that an agreement between Capax Discovery and DKO was *"never going to happen"*. Capax Discovery entered into the deal with the aim that it would happen, and it was assuming the risk on the faith of it.

(d) The Claimants' criticism of the reference to *"efforts"* was also misplaced. The clause was prospective, and it was clear from Deloitte's memo that Deloitte well understood the commercial rationale for the proposed compensation of the reseller.

(e) As to the provision for the payment of compensation *"in connection with VAR's efforts in securing End-User's procurement of Autonomy software"*, Mr Chamberlain had expressly made clear to Deloitte that in previous cases where

Autonomy had signed directly with the end-user as a matter of goodwill Autonomy had paid the resellers their lost margin: Deloitte were thus fully aware of that and had made no objection. Deloitte also made the point that the previous direct deals, before the introduction of the provision,

> *"highlighted the issue of risk for the VARs – relying only on the goodwill of Autonomy towards its resellers rather than formal legal recourse was deemed to be too high, and hence the clause was agreed."*

849. As to (2) in paragraph 845 above, the arrangements made in the aftermath of Autonomy's ultimately successful negotiations with DKO, and in particular, the interposition of MicroTech in place of Capax Discovery so that MicroTech could deliver to DKO the software which Autonomy had agreed to sell it, certainly invited enquiry:

(1) After hearing what was proposed, Mr Crumbacher sent an email dated 7 June 2011 to Joel Scott in response to a request that he (Mr Crumbacher) should ask Mr Dan Truitt *"to address paperwork"*:

> *"I'll call him. I think I know it already. Something about we took through one reseller and now we're replacing it with another. Brilliant."*

(2) Whether that email was intended to be admiring (or much more likely) ironic, the unusual nature of the insertion of MicroTech seems to have struck Mr Crumbacher. It was also not straightforward. Mr Crumbacher had become concerned about a mismatch between Capax Discovery's payment terms to Autonomy, under its DKO purchase order, and MicroTech's entitlement to payment from DKO under the direct deal. Mr Crumbacher explained this issue to Mr Scott in an email dated 8 June 2011:

> *"MicroTech is going to be told to pay in full net 75 days (otherwise Dan [Truitt, the Autonomy salesperson for the DKO transaction] doesn't get paid, and we all know that's the driving factor here). Capax doesn't have to pay in full for two years. It seems to me Capax should be paying as soon as they get paid by MicroTech, but their order doesn't state that, and now there's absolutely no incentive (other than good will) for Capax to revise their payment terms."*

(3) The solution arrived at was to amend the terms of the Capax Discovery/DKO purchase order. On 13 June 2011, Mr Crumbacher wrote to Mr Baiocco, stating:

> *"John, per Joel (who spoke with Sushovan), I'll be revising the amendment to the DKO PO's I sent Friday such that Capax will be paying for the DKO PO in full by the end of June. Can you please confirm? If this is not your understanding, can you please contact Sushovan to come to agreement on these payment terms? Thanks."*

(4) An evidently puzzled Mr Baiocco forwarded the exchange to Mr Hussain, adding the comment "*???*" and requesting a call. Mr Hussain responded, "*No worries I was hoping you could pay early*". Mr Baiocco asked when MicroTech would be paying Capax Discovery (he understood in 75 days' time). The Claimants submitted that this was a further demonstration that Mr Baiocco's understanding remained that Capax Discovery would not pay until it had been put in funds by Autonomy.

(5) That day (13 June 2011), Mr Kanter and Mr Baiocco executed an amendment to the Autonomy/Capax Discovery purchase order. It retrospectively expanded the classes of products that had been licensed to Capax Discovery, stipulating that certain further types of software were "*deemed to be included*" in the earlier purchase order, but there was no change in price. The change in the description was necessary, however, to bring the Capax Discovery purchase order into line with the terms of the direct agreement that had been made between MicroTech and DKO.

(6) The amendment also provided (by clause 1):

"Notwithstanding anything in the Purchase Order to the contrary, in the event CAPAX receives payment in full for the Software and Services from End-User or from an agent or reseller procuring the Software and Support on behalf of or for distribution to End-User, CAPAX agrees to remit payment in full to Autonomy of the total amount due under the Purchase Order not less [sic: more] than one (1) business day after the date it receives such full payment, regardless of any payment terms otherwise set forth in the Purchase Order."

(7) Thus, it appears to be clear that the intention was that Capax Discovery should use the funds it received from MicroTech to make immediate payment to Autonomy. The intention was duly fulfilled. In July 2011, MicroTech paid Capax Discovery, and Capax Discovery paid Autonomy, $2,242,727.

(8) On the same day, 13 June 2011, Mr Crumbacher sent Mr Dan Truitt a "*draft purchase order from MicroTech to Capax for the DKO order*". This was another demonstration of the lack of any semblance of independence between the contracting parties: one Autonomy employee was sending another Autonomy employee the paperwork for a deal that was purportedly to be concluded between two independent third parties; furthermore, the relevant Autonomy salesperson, Mr Dan Truitt, was the brother of MicroTech COO, Mr Steve Truitt.

850. The Defendants again rejected this summary as *"a highly selective and unfair presentation"* which *"ignore[d] a number of background documents in this context."* As to the interposition of MicroTech, the Defendants contended that:

(1) The Claimants had ignored the fact that this was a federal contract, and the involvement of MicroTech as an approved 8A reseller was a normal commercial event.

(2) It was not sudden or unplanned. As from February 2011 it had looked likely that MicroTech would play a material role in the DKO deal. As early as March 2011, Autonomy's federal sales team were expecting that MicroTech would be contracting directly with DKO, but that MicroTech would purchase from Capax Discovery:

> "*DKO will be bought by DITCO (the govt contracts shop) via MicroTech, but then needs to go through Cap X.*"

(3) MicroTech were proposing to deal directly with DKO on terms that offered them financing. This meant that they would be interposed as reseller, and could expect reseller fees. According to the Defendants' theme, Autonomy found it commercially normal that it should be paying two reseller fees in these circumstances; for example Mr Crumbacher stated in an email dated 8 June 2011:

> *"The government is actually paying Microtech somewhere north of 2.9M, but it's paid over three years and includes both the margin they make on our software as well as finance charges for MicroTech financing the government's purchase (as an aside, I'm a little concerned, being a US citizen, that the Truitt brothers are now in the business lending money to my federal government). Because its lumped in with their three-year pay out, I don't see how we can get around a double-dip on reseller fees here. And…frankly…we're using two resellers, so we shouldn't be surprised at paying two reseller fees."*

(4) None of the adjustments to the Capax Discovery purchase order made necessary in consequence was sinister or surprising, or altered the fact that Capax Discovery was on risk.

(5) Capax Discovery's payment terms to Autonomy under the deal were brought forward by mutual consent. The commercial background to this was set out in an email to Mr Scott from Mr Crumbacher. In short, MicroTech was going to be paying Capax Discovery in a shorter period than Capax Discovery was due to pay Autonomy, so Autonomy wanted to bring Capax Discovery's payment terms forward if Capax Discovery would agree (which they did). (In other words, according to the Defendants' analysis, the Claimants had wrongly asserted that this evidenced that Capax Discovery would only pay when paid: on the contrary, Capax Discovery was being invited to pay <u>early</u>).

(6) The Capax Discovery purchase order was also subject to an adjustment to the wording as to the software included.

851. As to (1) in paragraph 845 above and the payment of compensation to Capax Discovery for its *"efforts in securing End-User's procurement of a license of Autonomy software"* (in effect, a MAF of 10% of the Capax Discovery purchase order amount), the Defendants submitted that:

(1) This was to be expected in circumstances were there was the interposition of another reseller: the usual reseller margin was effectively taken by MicroTech,

meaning that Capax Discovery would not obtain any margin on the deal absent a MAF payment (see Mr Crumbacher's email referred to above);

(2) The Claimants' criticism of the wording of the MAF letter as being "entirely false" in its description of Capax Discovery's contribution (on the basis that it wrongly suggested that Capax Discovery was to introduce Autonomy into deals with DKO) was *"an overblown forensic point"*: the MAF letter was drafted by a lawyer, Mr Crumbacher, was in standard form and in any event stated:

> "*Autonomy will: (1) pay Referral Partner commissions in the amount of US$224,275, as a result of Referral Partner's direct and proximate participation in the account*".

(3) Moreover, Deloitte well understood and accepted that a MAF could be paid in situations like these where a reseller could not otherwise obtain its margin.

852. The Defendants also sought to draw support from the fact that VT20 and DKO's transaction with MicroTech was dealt with in the Goldberg Segalla letter (which, it will be recalled, Mr Baiocco confirmed was accurate). That letter had stated that Capax Discovery was on risk, and that both the reseller sale and the subsequent sale to MicroTech were normal commercial transactions:

> *"Paragraph 14.c. of the memorandum accompanying the show cause letter ("Memorandum") indicates that Capax was involved in a transaction involving a Government end-user. The Government end-user business opportunity was brought to Capax in late December 2010. Although this opportunity was brought to Capax near the end of a fiscal quarter, the timing was not uncommon because Autonomy would have been working diligently to close the deal prior to the end of the quarter, just like many companies tend to do.*
>
> *Capax decided to pursue this opportunity and agreed, on December 31, 2010, to buy the software for $1,950,197, in addition to product support of $95,510 per year, for a total of $2,242,727. As originally contemplated, this transaction involved the sale of certain software by Autonomy to Capax, as the VAR, with the Government end-user ultimately receiving the software and related product support services. The purchase order reflecting this transaction is at CAPAX000015-CAPAX000017. When the purchase order was signed, the financial risk of the deal was transferred to Capax. Paragraph 14.c of the Memorandum states that "the Autonomy sales representative, nor his supervisor, nor the Government agency were made aware that Autonomy had 'closed' the deal in Q4 2010." Capax does not have any knowledge of the Autonomy sales representative's and supervisor's or the Government end-user's knowledge regarding when the deal closed. Capax was dealing with Autonomy's U.S. CEO and executive level counsel to close the deal on December 31, 2010.*
>
> *Under this agreement, Capax, as the VAR, would receive a commission from Autonomy upon the closing of the deal between Autonomy and the Government end-user. In the event the deal with the Government end-*

> *user did not close, Capax would own the software licenses and ultimately have to pay Autonomy for them. Capax was aware of this consequence from the advice of counsel, Frank T. Gaglione, Esq. In the event that the transaction did not materialize, Capax's only option would be to resell the software licenses to another customer. Capax evaluated this risk and decided the upside was worth the inherent risk.*
>
> *Autonomy later informed Capax in June 2011 that the Government end-user preferred to purchase the software through MicroTech, instead of Capax, because it had previously worked with MicroTech, which has significant sales to the Government. The transaction ultimately closed on June 3, 2011. On June 15, 2011, MicroTech sent Capax a purchase order for the amount at which the deal closed, $2,315,959.40, which was slightly higher than the original purchase order between Autonomy and Capax. The purchase order reflecting this transaction is at CAPAX000018-CAPAX000019. Capax subsequently invoiced MicroTech, received payment in full from it, and then paid Autonomy in full.*
>
> *Capax's invoice to MicroTech is at CAPAX000020. On June 30, 2011, Capax invoiced Autonomy for its commission of $231,595.94 under the terms of the VAR agreement. Capax's invoice to Autonomy is at CAPAX000021-CAPAX000022. Capax received $224,275 in July 2011, an amount less than it invoiced, which corresponded with the value of the purchase order between Capax and Autonomy.*
> *Communications regarding this amount and payment are at CAPAX000023-CAPAX000027.*
>
> *Paragraph 14.c. of the Memorandum states "there was no indication that Capax participated in this deal." This is inaccurate. Capax was the original VAR in this transaction and took on the risk inherent in. it. As described in greater detail above, this risk included the possibility that the deal with the Government end-user would not materialize, leaving Capax responsible for ultimately paying Autonomy for the software without a definite end-user."*

853. The Defendants offered no explanation as to why, if MicroTech was a more suitable on-seller because of its approved status and ability to offer flexibility of finance, they originally selected Capax Discovery to act as the VAR. The reason for the choice is all the more interesting in light of the fact that Mr Mooney had originally asked Mr Hussain whether he wanted to go through MicroTech, Mr Hussain had said no, on the ground that he did not believe MicroTech would be bidders on DKO's Request for Quotation ("RFQ") and wanted to consider companies who would be bidding: but when Mr Mooney replied MicroTech was expected to bid, Mr Hussain steered him away to *"other bidders"*; yet when it came to the last minute, Capax Discovery, though not a bidder, was selected.

854. In my view, it is difficult to escape the conclusion that Capax Discovery was the most compliant of Autonomy's usual VARs, and the most flexible and least likely to ask any questions about the proposed end-user transactions when time was really short, and revenue was urgently required.

855. Perhaps more importantly, however, the Defendants' vigorous defence of the interposition of MicroTech tended to distract attention from what seem to me to be the real points, neither of which they answered:

(1) The event which was relied on for the purpose of revenue recognition was the sale to Capax Discovery. That sale lacked substance and did not satisfy IAS 18.14. The interposition of MicroTech at the direction of Autonomy in order to effect delivery from an 8A vendor after Autonomy had alone conducted the negotiations with DKO confirmed that it was Autonomy, and not Capax Discovery or indeed MicroTech, which had control and retained risk, and showed how little substance there was in the original VAR sale.

(2) The requirement for Capax Discovery to pay early was not a sign of it being on the hook: quite the reverse because part of the arrangement was that Autonomy had to arrange for Capax Discovery to be put in funds for that purpose. That once more conformed to the pattern, and demonstrated that the payment obligation in the contract was all show and no substance.

856. The Goldberg Segalla letter was an unreliable reed to grasp. I have already explained that it too was contrived and misleading.

857. In my judgment, VT20 was part of the pattern. Recognition of revenue from the VAR sale to Capax Discovery was improper.

Defendants' knowledge of false accounting in respect of VT20

Mr Hussain

858. Mr Hussain was involved throughout. It was he who expressed himself to be *"dumfounded" [sic]* when the DKO deal faltered and clearly could not be completed in the quarter, and who emailed Mr Mooney and Mr Egan on 23 December 2010, stating *"Obviously we should consider partners"*, meaning the use of a VAR. It is fairly clear to me that this was in order to recognise revenue.

859. It is less clear whether Mr Hussain actually chose Capax Discovery: it was Mr Egan who contacted Capax Discovery so late in the day; but it seems to me to be more likely than not that Mr Hussain and Mr Egan were aware of each other's preference.

860. Mr Hussain was kept informed of the negotiations. He knew that Capax Discovery was the VAR. Mr Hussain was involved in the amendments to the Capax Discovery/DKO purchase order, as apparent from an email on 13 June 2011 from Mr Crumbacher to Mr Baiocco recording the fact of a conversation on the matter between Mr Hussain and Mr Scott. He must have been aware from that process of the interposition of MicroTech. He was also aware of and involved in the payment to Capax Discovery of a MAF after Autonomy had received from Capax Discovery what in an email to Mr Crumbacher dated 8 July 2011 he described as *"the dko cash",* which Mr Hussain had stipulated to be a condition a week earlier. At Mr Hussain's request, the final payment had to be, and was, sanctioned by Mr Kanter. When the deal was done: Mr Mooney so informed Mr Hussain by email on 3 June 2011. The email contained no message except the subject heading: *"DKO done"*. The deal

needed no introduction or explanation, reinforcing my view that Mr Hussain knew all about it.

861. Mr Hussain cannot have thought that the recognition of revenue from the 'sale' to Capax Discovery as a 'placeholder' was proper in this context. In my judgment, he had "guilty knowledge".

Dr Lynch

862. Dr Lynch appears to have had very little personal involvement in VT20, except that he was emailed by Mr Hussain on 23 December 2010 indicating that the deal with DKO was unlikely to happen that quarter and complaining that *"This is just unbelievable. I bet you no one in the US actually visited DKO"*.

863. No transaction-specific evidence of substance was put to Dr Lynch in cross-examination; he was asked to comment on aspects of the transaction as it developed, but he was insistent he had no direct involvement. Thus:

(1) Dr Lynch was asked in cross-examination whether he knew of the VAR deal at the end of December 2010: he said he did not know, but would not have been surprised to hear of it.

(2) He denied seeing the Capax Discovery purchase order; and when it was put to him that the statement in it that *"…end-user and VAR currently anticipate entering into such a license transaction"* was not true, he said he was not involved and could not comment or speculate as to what was anticipated.

(3) As to the provision for payment of a MAF for *"VAR's efforts in securing End User's procurement of a license of Autonomy software",* when it was put to him that this *"deliberately gives a wrong impression of what Capax's role was to be"* he stated:

> *"As I've said, first of all, this was a relatively small deal in a subsidiary, in the US, being run by other people at a level that I have no knowledge other than having seen the name on a list. So I can't comment on this for you."*

(4) Later, when pressed whether he would have expected Capax Discovery *"to have exactly the same role as I suggested that it had in other deals we've looked at"* he responded:

> *"Again, you're asking me to comment on things. I have no idea whether Capax did or did not have involvement with the end-user or, indeed, whether or not that is a relevant question to ask under IFRS. My understanding is it isn't."*

(5) Dr Lynch was not involved in the MicroTech deal, or how the opportunity arrived, and was not challenged on this. He was nonetheless shown the email of 13 June 2011 from Mr Crumbacher to Mr Dan Truitt explaining that he had drafted a purchase order from MicroTech to Capax for the DKO order by reference to the directions of Mr Hussain (see paragraphs 849(8) and 860 above) and it was suggested that Mr Hussain was "*pulling the strings here and is causing MicroTech to buy something from Capax Discovery so that MicroTech*

can make the sale to DKO which has been negotiated between Autonomy and DKO". It was not explained what relevance this would have to the original revenue recognition, but Dr Lynch did not accept it. His speculation as to what was happening was fair:

> *"A. I think what's going on here is that we have one of our resellers who has the stock and has been given the opportunity to sell to DKO. We have another one who, my understanding, had a very close relationship with DKO and knew them well, and what we're doing is putting the two parties together so that the transaction happened, which is obviously in our commercial interests and in the commercial interest of the two parties and presumably in DKO's commercial interests."*

(6) Dr Lynch was asked about the amendment in respect of the software component to the Autonomy/ Capax Discovery purchase order, but Dr Lynch was not involved in that, and (beyond speculating) he said that he could not answer the question without looking at the amendment, which was not shown to him.

(7) He was also asked about the amendment to the payment terms, but was not involved in that, and thought it extremely unlikely that he would have been told of the amendment to the purchase order.

(8) Though he was not involved at the time, Dr Lynch observed when asked about the deal that there was nothing unusual in the commercial situation represented by this deal:

> *"... my understanding is it's a straightforward situation of Autonomy sold to Capax, so Capax is Autonomy's customer, and Autonomy recognises that revenue. Then Capax sells to MicroTech, and then MicroTech sells to an end-user, DKO. And, again, there's nothing remarkable in that.*
>
> *... Again, this to me is perfectly normal commercial trading. Party sells something to one party, who then sells it to another party who sells it to an end-user and the money flows back up the chain. Almost not worthy of comment but very obvious."*

(9) It was not put to Dr Lynch that he was involved in the payment of the MAF or aware of it at the time, or involved in or aware of the letter documenting the MAF. However, Dr Lynch rejected the idea put to him that this was a false paper trail:

> *"A. First of all, I don't think it's a false paper trail. The MAF document is a standard form document that's been used for years and years and years, and I'm sure it was just picked off the shelf and used and I don't believe there's any attempt here to create a false paper trail."*

864. In summary, Dr Lynch submitted that in any event there is no basis for the allegation that he knew of or participated in any improper accounting for the VT20 revenue.

865. In my judgment, Dr Lynch was correct to focus on the 'sale' to Capax Discovery (see paragraph 863 above). He accepted that, even if he did not know about it (and he emphasised this was a relatively small deal) he would not have been surprised to hear about it. In my judgment, that is because all these impugned VAR sales were taking place as part of the strategy to cover shortfalls in revenue; and the pattern which implemented the strategy usually involved a 'sale' to a "friendly VAR". I have little doubt that Mr Hussain would have told him the constituent elements of the revenue achieved: Mr Hussain reported that to Dr Lynch almost as obsessively as he pursued revenue.

866. In my judgment, it is more likely than not that Dr Lynch knew that VT20 fell into the pattern and I find that he had "guilty knowledge" accordingly.

VT27: Capax Discovery/McAfee Q1 2011

867. In Q1 2011, Autonomy was seeking to conclude a $5,000,000 licence sale to McAfee, a software company well known for its computer virus protection products. Dr Lynch told me in cross-examination, and I accept, that McAfee was an established customer of Autonomy.

868. On 25 February 2011, Mr Hussain emailed Dr Lynch saying: "*So overall $200m needs 1 big deal in Europe (it'll come from the middle east probably), DB from Stouff and McAfee and Rand from Mooney plus a deal from Axicom*". On 3 and 6 March 2011, Mr Hussain sent further updates to Dr Lynch by email.

869. On 10 March 2011, Mr Hussain updated Dr Lynch that "*Mooney is running mcafee (for the deal to happen either you or i may need to meet with Dewalt) ...*". As the Claimants submitted, this suggests that the Defendants (or at least Mr Hussain, without apparent objection from Dr Lynch) considered that this proposed transaction merited their personal attention. The stream of updates confirms this.

870. On 15 March 2011, Mr Hussain sent an email update to Dr Lynch, noting that McAfee was "*progressing*". On 16 March 2011, Mr Hussain emailed Dr Lynch to say that the McAfee transaction was progressing well and that he (i.e. Mr Hussain) was "*all over every deal right now*".

871. However, on 17 March 2011, Mr Hussain told Dr Lynch that there had been "*no material progress today*" on the McAfee transaction. On 30 March 2011, Mr Mooney emailed Mr Hussain to say that the McAfee transaction was "*dead for the quarter*".

872. The same day (30 March 2011), in response to a request from Dr Lynch for "*Update pls*", Mr Hussain sent Dr Lynch his summary revenue spreadsheet. This stated, "*Took out McAfee 5*". Dr Lynch accepted that he "*would have had a look*" at this spreadsheet. Dr Lynch said that this "*doesn't mean that it's necessarily gone as a total chance. It's just that it's not what he's [Mr Hussain is] putting his route in*".

873. Just after midnight at the start of 1 April 2011, Mr Hussain sent Dr Lynch a further version of the summary revenue spreadsheet, subject "*update before I turn in*". This now included a new transaction "*8A (stouffer) 5.0*". The Claimants produced a table (as below) to illustrate the juggling that went on (red arrows added for ease of reference):

closed	183.4		
8A (stouffer)	5.0		
MS (Stouff)	5.0	25th mar activity	
Bank of Montrea	3.2	EMEA weaker - 3 deals o	1
HMRC	0.9	Management - d&t out	1
Ameritrade	2.0		
8A (stouffer)	6.0	28th mar activity	
Herbalife	1.1	Took out Goldmans	0.5
		Took out DB EU	1.6
Rafiq	0.1	Took out GM	1.3
Neal	2.6		
Sass	1.0	29th mar activity	
EMEA	0.4	Took out McAfee	5
Mikes	0.1	Took out QVC	2.5
SE	3.0	Rafiq small deals	1
Sanjay	0.1		
MGMT IB	0.0		
FX upside	0.5		
TOTAL	214.2		13.9

874. Dr Lynch accepted in cross-examination that he looked at this update. He would have understood the reference to "8A (Stouffer) 5.0" to refer to a reseller deal to be obtained by Mr Egan. Dr Lynch said he did not know if this was related to McAfee or not, but in my judgment, it is likely he did understand this given that the amount of revenue ($5 million) was identical to the amount stated next to "*McAfee*" in Mr Hussain's 30 March 2011 spreadsheet which he (Dr Lynch) had reviewed.

875. Although especially well illustrated, the pattern is familiar. VT27 was yet another impugned VAR transaction done on the last day of a quarter in hurried circumstances when an expected direct deal could not be closed in time before the end of the quarter. Again, Autonomy resorted through the ever-co-operative Mr Baiocco to a (particularly) "friendly" VAR, Capax Discovery.

876. On 31 March 2011, Capax Discovery issued a purchase order under the June 2009 Capax Discovery VAR Agreement summarised in paragraph 60 above for intended end-user McAfee for a licence fee of $5,000,000 plus a first-year support fee of $250,000. The licence fee was payable in two tranches in July 2011 and September 2011.

877. The Claimants alleged non-compliance with IAS 18.14(a) (no transfer of risk of ownership), (b) (retention by Autonomy of managerial control) and (d) (collectability). For the most part, the argument proceeded on familiar lines and was answered in the familiar way, though Mr Baiocco and Dr Lynch both told me that Capax Discovery also had a previous relationship with McAfee, and that Mr Baiocco was therefore pleased that this new VAR transaction could further assist his relationship. The Claimants relied on the transaction as further illustration of the 'pattern' they claimed was characteristic of the impugned VAR transactions.

878. However, VT27 was another example where no end-user deal was ever closed, either by Capax Discovery or Autonomy, leaving Capax Discovery notionally exposed and in need

of the assistance which it was the basis of its participation Autonomy would somehow arrange to be provided.

879. It was the way this exposure was dealt with which was the focus of the Claimants' attack on the overall transaction and which the Claimants relied on as specific evidence that Autonomy and Capax Discovery had agreed that whatever happened, Autonomy would always see to it that its VAR was never left *"holding the bag"*.

The 'staging tools' transaction

880. The Claimants' case was that to enable Capax Discovery to pay the $5,250,000 debt under the McAfee purchase order, Autonomy contrived a purchase by ASL from Capax Global of a licence to use what Mr Baiocco described in his witness statement as *"a tool set that improved or facilitated the e-Discovery process"* which Capax Global had developed and which it called "Staging Tools".

881. The licence fee was $6,000,000, which Autonomy paid on 12 August 2011 the day after receiving an invoice from Capax Discovery (11 August 2011). It was this receipt, according to Mr Baiocco, which enabled Capax Discovery to pay the sums due under VT27; and it is clear that Capax Discovery did then make two payments of $2,625,000 to Autonomy, one on 15 August 2011, and the second on 1 September 2011 (though the latter payment was not due until 27 September 2011).

882. The Claimants contended that Autonomy had no genuine commercial rationale for purchasing the Staging Tools, and that its real purpose was to put Capax Discovery in funds.

883. The Claimants also referred in this context to Mr Baiocco's evidence in his witness statement that he was concerned lest the staging tools purchase was a scam and not a real deal; and that he had raised this with Mr Egan on the telephone who (he said) *"reacted angrily to my statement that there was something suspicious about the deal"*. Mr Baiocco's witness statement also stated that it seemed to him *"as if Autonomy was urgently seeking to clean up its books",* causing him to call Mr Hussain on 17 August to ask him if Autonomy was about to be acquired, but Mr Hussain *"did not give anything away"*.

884. The Defendants submitted that Autonomy's urgent need for the staging tools, far from being a contrivance to assist Capax Discovery, was real and urgent, and that there was no basis for Mr Baiocco's purported suspicion or for the Claimants' complaint in relation to Autonomy's purchase.

885. Although highly critical of Mr Baiocco's evidence in his witness statement, they adopted in this context with some enthusiasm his evidence in cross-examination. They offered the following context and explanation, based on evidence given by Mr Baiocco of his understanding (and was subject to his warning that he was *"not a tech – not even a little"*):

(1) The staging tools were tools developed by "Capax Discovery" (in fact, according to the licence agreement between it and Autonomy (see below), by Capax Global) to improve the user operability of Autonomy's Introspect 6 software. According to Mr Baiocco's understanding, "Capax Discovery" had created a set of 9 modules designed to improve the performance of the platform. The tools improved the EDD process, speeded it up and made Autonomy's Introspect software more efficient. The "Capax Discovery" engineering team who had developed the software were experienced IDOL and Introspect experts,

as was evident from their biographies (provided on an email from Capax Global). "Capax Discovery" engineers were demonstrating the tools to Autonomy by March 2011.

(2) Autonomy had itself experienced difficulties with the Introspect platform and delays in meeting performance and quality control requirements which were causing backlogs[73] and customer dissatisfaction.

(3) Further, in Q1, Q2 and Q3 2011 Autonomy was engaged in the Deepwater Horizon discovery project for BP. This was one of the largest e-Discovery projects (if not the largest) to date. Autonomy had been encountering difficulties in meeting quality control requirements under the contract, which were similarly causing performance and quality control issues.

(4) Autonomy shared some of its difficulties with Mr Baiocco and invited Capax's assistance. The solution offered involved the configuration and implementation of the nine modules for Autonomy's specific use, as described in a letter to Autonomy from Capax Global dated 27 July 2011 which Mr Baiocco told me was written for him by his technical team.

(5) Mr Baiocco recalled that high importance was being put on the staging tools for the BP e-Discovery work at the time.

(6) A Commercial Software License Agreement agreed between Autonomy and Capax Global in respect of the staging tools (dated 11 August 2011) granted not only a licence but also *"EDD workflow management and reporting – "Chain of custody" and "job" tool extension"* to assist Autonomy and its customer, BP, further in e-Discovery work for the BP project.

(7) The urgency for Autonomy was illustrated by Autonomy's request that Capax Discovery get people out to Chicago to get on with the process as quickly as possible. Mr Baiocco was *"pretty sure"* that his people did go out to Chicago.

(8) In short, Autonomy badly and urgently needed the staging tools to recover ground and perform properly its enormous e-Discovery project in relation to the BP case: and the Staging Tools met that need.

886. As to "fair value", Mr Baiocco's technical team told him that the "Capax Discovery" tools could be worth more than the $6 million being paid by Autonomy:

> *"Q. And they said that the Capax tools resulted in much faster results and could be worth 6 million because of the amount of data Autonomy was processing, do you remember that?*
>
> *A. That's what they said to me, yes.*
>
> *Q. And did they say to you that they could have been worth more than the 6 million paid by Autonomy?*

[73]This was Mr Baiocco's understanding from what he was told at the time. Mr Sullivan also confirmed that Autonomy was encountering difficulties keeping up with what was a "*very challenging case*".

A. They did.

Q. Who did you ask that? Were those people like Mr Tucker, Mr Balam, Mr Ferbert, those characters we've seen?

A. It would have been more Mr Gurney and Mr Williams"[74] .

887. Further, the task of configuring and implementing the nine modules was a complex and substantial one, some requiring more than 15 man-days each and the use of highly qualified software engineers: having initially queried what Mr Miles meant when he suggested this, Mr Baiocco accepted this. Mr Miles emphasised that the only evidence that the Court has on fair value was that given by Mr Baiocco: the tools could have been worth more than Autonomy was paying,[75] and there was no evidence to suggest that they were worth less.

888. Cross-examination also revealed errors or inaccuracies in the witness statement evidence of Mr Baiocco in relation to this transaction. In particular:

(1) Mr Baiocco's witness statement suggested that an email of 13 June 2011 comprised a request for a proposal from Capax Global to license Autonomy staging tools, and pitch the licence fee at around $5 million or $6 million. Mr Baiocco's evidence was that he had been surprised that *"Mr Hussain suggested these arbitrary numbers without any prior discussion or negotiation"*; and that although Mr Hussain did not explicitly make the link to Capax Discovery's debt to Autonomy under the McAfee transaction, it seemed to him that this was a way of paying down the McAfee debt. Mr Baiocco referred also to having had a heated telephone discussion with Mr Egan *"around this time"* after Mr Baiocco had asked *"whether the staging tools purchase was a real deal or a scam."*

(2) However, as Mr Miles brought out, the email of 13 June 2011 did not relate to staging tools: the references there were to Stratify and DRCCM assets which were part of Iron Mountain Digital, whereas staging tools were for Introspect e-Discovery.

(3) When faced with this point in cross-examination Mr Baiocco's evidence was described by the Defendants as *"incoherent and evasive"*. Mr Miles portrayed it to him as a *"serious error"* and Mr Baiocco was patently uncomfortable.

(4) The muddle in the witness statement replicated his examination in chief in Mr Hussain's US criminal trial, where Mr Baiocco had made the same bad points: the Defendants suggested that this was *"no doubt following his preparation sessions with the DoJ"*.[76] When it was put to him that this *"was something that someone put into your witness statement and you just signed up to without thinking"*, Mr Baiocco offered no coherent response except to reiterate that he

[74] Mr Baiocco told me that Mr Stephen Williams was an EDD expert and Mr Gurney was trained by him.
[75]See paragraph 886 above.
[76]In his cross-examination in this trial Mr Baiocco suggested that this was his mistake, but it was obvious from Mr Baiocco's evidence in Mr Hussain's US criminal trial that this was a prepared question from the examiner in chief. Mr Baiocco was expressly asked, "*Q. Can you tell us what happened in terms of the proposal on NearPoint and on the staging tools that you had the email communication with him about?*"

stood by the fact that Autonomy had indeed purchased the staging tools for $6,000,000.

889. The Defendants submitted that the upshot was that such evidence as Mr Baiocco gave in his witness statement on the staging tools purchase was wholly unreliable and shown to be so by his own answers in cross-examination. In that context, and contrary to what he had said and intimated in his witness statement, Mr Baiocco had confirmed both that the staging tools were seen as useful and important at the time and that his team considered that they could be worth more than Autonomy was paying.

890. This was all enthusiastically supported by Dr Lynch (who had not mentioned VT27 in his witness statement) when he explained in his cross-examination his understanding of the reason for the purchase. He confirmed that he considered it to have been done for good commercial purposes and dismissed the suggestion that the reason for the transaction was *“quick payment…simply to put Capax in funds to pay down what it owed Autonomy on end of quarter VAR deals”* as follows:

> *“No, the purpose of the money being sent was to pay Capax for something that we needed very urgently because of our BP crisis that was going on. If they used that money to pay down their VAR debt, then great. They've managed to produce something that's useful to us. Just one thing to keep context here, these resellers, their business is about taking our software and adding things which they then sell to customers. Every so often they actually make something useful and we have the ability to buy that from them. So it's not -- you know, they are actually in effect almost an extension of our R&D operation in that they're doing these things. They continually pitch the work they've done to see if we'll buy it because they've already written it for their own customers. Often the reason they've written it is it's something that's missing from our product, otherwise they could just sell our product. So we get pitched with these and we buy them and this one, the reason I know more about this one is that this was central to a very large crisis that we had at the time where we were doing British Petroleum's Deep Horizon well litigation, which at the time was the largest litigation in the world, and we were failing to the point where we'd been called into the headquarters of BP and told that they were switching to a competitor because we kept making silly quality control mistakes. So, for example, we didn't actually provide some of the documents for a deposition until after the deposition. I sent out an edict in the March to Mr Sullivan to do whatever it took to fix it and he started creating something called a new fire engine, as he called it. Then we had another showdown with BP and they threatened to pull the plug on a 10 million deal that we did, so we bought these tools and these tools were specifically designed -- they'd been around a while -- to stop these quality control problems of losing documents and things like that.”*

891. Dr Lynch’s understanding also reflected the information given to him in the emails going to him in connection with his approval of the purchase:

(1) On 5 August 2011 Mr Egan notified Mr Kanter and Mr Hussain that he had finalised negotiations with Capax Discovery, describing the tools purchased.

Mr Hussain included Dr Lynch, Dr Menell and Mr Chamberlain on the thread, stating:

> *"Thanks Stouffer. There has been a lot of emails on this and i am glad we can get to a close now.*
>
> *I need approval from Pete on the technology····· please provide via email*
>
> *I approve the cost side but need one of Andy and Mike to counter approve given its size. For your information these products are being used against the delivery for BP so will be expensed. We have so far received $22m from BP, are charging them nearly $1m a month, the project is getting bigger as I am negotiating a $4m backup deal and a $6m disaster recovery plus 99.9% uptime deal.*
>
> *Steve- could i please ask you to put this into a PO form, and append the approvals by printing the relevant emails.*
>
> *Stouffer ····· I am keen to get the software today so lets get this wrapped."*

(2) Dr Menell stated in the same thread (copying Dr Lynch):

> *"These tools will need to be customised and configured to our environment so not only do Chicago and Camb need the sw asap we will need bodies from Capax to work alongside dev to get this done. Presumably we can get Capax crew in without being hit by another bill! Given dev is now into double figures on the versions of Dashboard we have built without success we cannot be left without help as this type of tool needs a great deal of background to manipulate and operate effectively- background self evidently we don't have. I see this as key if it's to have any impact on BP in a time frame that makes a difference. Stouffer will need your help to press Capax to fly troops asap or at least point us to who can help."*

(Mr Baiocco confirmed that the "Capax crew" did fly into Chicago.)

(3) Mr Hussain subsequently asked Dr Lynch for approval, replying on the same email thread. Dr Lynch wrote *"yes"*.

892. Turning to my assessment, the evidence was obviously rather inconsistent, and sometimes confused. My impression when Mr Baiocco was cross-examined on this transaction was that he was struggling with the evidence in respect of it attributed to him in his witness statement. I would accept that the picture that emerged from cross-examination was rather different from the neat presentation in his witness statement pointing inexorably at the staging tools transaction being suspect as to purpose and inflated as to price.

893. I do not think that Mr Baiocco was being dishonest. I regard this part of Mr Baiocco's evidence as illustrating the dangers that evidence may be polluted by rehearsal and

repetition at the instance of lawyers with a forensic objective, just as much as its accuracy may be eroded by lapse of time, and the gradual replacement of real memory by nurtured assumptions and the desire for consistency with what the witness comes to believe he or she has said before. This was a salutary reminder to me, and I have at all times borne in mind, that I need to consider disputed witness statement evidence from the Claimants' VAR and other witnesses on impugned transactions with particular care and a degree of scepticism.

894. That does not of itself, however, resolve the question as to the operative purpose of the staging tools transaction, or the issue as to fair value.

895. As to the purpose of the staging tools transaction, it seems to me to be reasonably clear that the proceeds were used, and were probably always intended to be used, by Capax Discovery to pay down instalments due under the McAfee transaction. That was the consequence of the transaction, and as I find, an important part of its intended effect.

896. However, I consider that the email evidence did suggest also that Autonomy urgently needed staging tools (or some similar product), especially in the context of its e-Discovery work for BP and the difficulties it was experiencing in that context. The email exchanges were all within the cabal of Dr Lynch, Mr Hussain, Dr Menell, though usually involving also Mr Egan. To my mind, there is a whiff of artifice in some of the points in favour of the purchase which were made in those exchanges and the possibility that they were pre-textual has lingered in my mind. But I do not consider the evidence goes so far as to show that they were, and I therefore proceed on the basis that Autonomy's need for the staging tools was real and not contrived.

897. It is not easy to determine which was the predominant purpose. I have in mind also that, whilst Autonomy needed the tools, it may not have needed so many: and though there is some evidence that the order exceeded the need, it was sketchy. In the end, however, I have concluded that I need not assess the comparative weight of the two purposes: for, in my view, the vice in the transaction was that the price was contrived to enable Capax Discovery to make payment under VT27 which was part of the purpose of the purchase, with enough surplus to fund also a MAF. In a sense, Mr Baiocco was right, even if for the wrong reason.

898. I have had very much in mind, in reaching this conclusion, Dr Lynch's point that the only evidence on the issue of fair value was provided by Mr Baiocco in cross-examination, and that evidence was that Mr Baiocco had been told by experienced e-Discovery personnel within Capax Global that the staging tools could be worth $6 million, or perhaps even more.

899. However, what on analysis stands out from that evidence is that Mr Baiocco made clear that he had not asked those he had consulted (it may be noted, quite informally) *"how much they were worth upfront"*. The question he thought he had asked was *"are they worth the price they're paying"*, and the answer he was given (according to the cross-examination evidence on which Dr Lynch relied) was *"yes"* and that this was *"because of the amount of data Autonomy was processing."* In other words, the only evidence was as to what the experts thought the staging tools would be worth to Autonomy, which in light of the use Autonomy could make of them in the context of an enormous job for which it was being or stood to be paid (literally) millions, could even exceed that. That was the distinction implicit in Mr Baiocco's distinction between "worth upfront" and whether the tools would be worth <u>to Autonomy</u> the amount they were prepared to pay; and that was why the amount

of data which Autonomy was processing would feed into what Autonomy would be prepared to pay.

900. It is important to have regard both to the nature and limits of the evidence, and the actual question asked. There was no list or recommended price, nor any other mechanism to establish price. The evidence, such as it was, of "fair value" was not a formal assessment, nor was it made by those with commercial or market experience of making an assessment of "fair value". The question asked was, in effect, whether the price could be justified according to the value to be extracted from the staging tools by the particular customer. I infer and find that at some point Mr Hussain suggested the convenient figure of $6 million; and that being the price Autonomy was prepared to pay, and in the view of those with experience of e-Discovery products in general and the staging tools in particular, not being excessive according to its benefit, Mr Baiocco adopted it.

901. Put shortly, the price paid was defensible because the staging tools would be worth that to the user; but its amount was calculated by reference to Autonomy's other purpose.

902. I have concluded that the staging tool transaction was a further example of Autonomy making good on the fundamental understanding which underpinned all the impugned VAR transactions that one way or another the VAR would not be "left on the hook" or "holding the bag".

903. The Claimants also complained about the payment of a MAF (in the sum of $525,000) to Capax Discovery in respect of VT27, focusing again on the way the payment was presented, as appears from the letter dated 1 September 2011 that Mr Baiocco was asked to sign, which referred to Capax Discovery having purchased from Autonomy certain products and services for resale to McAfee, and continued:

> *"Such contemplated resale is referred to herein as the "Transaction."*
>
> *Capax has submitted to Autonomy invoice no. 1282, in the amount of $525,000.00, due from Autonomy as payment to Capax for marketing assistance services related to the Transaction. Such payment from Autonomy shall be deemed full and final payment of any and all fees due to Capax from Autonomy as a result of the Transaction, or otherwise in connection with Capax' resale of products and/or services to McAfee."*

904. The Claimants submitted that this *"was another work of fiction"*. There had been no sale by either Autonomy or Capax Discovery to McAfee. Capax Discovery had never contemplated itself making a "*resale*" of the Autonomy products to McAfee. Nor had Capax Discovery provided any "*marketing assistance services*" to Autonomy in relation to such a resale. In reality, the only service provided by Capax Discovery was the submission of a purchase order, which Autonomy used to recognise revenue improperly in Q1 2011.

905. Again, the Defendants' answer was that the payment of a MAF was unobjectionable for the reasons previously given above.

906. I do not accept that. In my judgment, payment of the MAF was part of the pattern: it was the price levied for signing up to nominal legal liability, and keeping out of the way thereafter.

907. Taking all the features of these transactions together, in my judgment, VT27 was another exemplar of the pattern. The sale to the VAR was illusory and effected no change in control or transfer of risk; no revenue should have been recognised in respect of it.

Defendants' knowledge

Mr Hussain

908. As always, Mr Hussain was directly involved. His usual obsession with plugging shortfalls to enable him to meet forecast prompted the transaction. He knew it was contrived. Likewise, he knew that the staging tools transaction was at the price necessary to rescue Capax Discovery and was in the know throughout. The transactions were, to his knowledge, exemplars of the strategy he devised. In my judgment, he had "guilty knowledge".

Dr Lynch

909. Dr Lynch submitted that there was no basis for the allegation that he knew of or participated in any improper accounting of the transactions. His evidence was that:

(1) He was aware of efforts being made to close a deal with McAfee in Q1 2011, but he was not involved in the reseller deal, and certainly had no information to suggest that there was a deal with a reseller where revenue was being improperly recognised. When cross-examined he was shown documents which the Claimants suggested could have led him to infer that Capax Discovery was coming in for McAfee, but he did not accept that such a link was obvious and confirmed that he had certainly not made it.

(2) He was made "*distantly aware*" of continuing discussions between Autonomy and McAfee after Q1 2011; but he told me that he did not know whether or not Autonomy was negotiating with McAfee without Capax Discovery's involvement;

(3) He did approve the later purchase of staging tools from Capax Discovery, but he understood that he was approving a transaction put together and recommended by others and had no reason to think other than this was a sound purchase at fair value (which it was) for good commercial reasons.

(4) In any event, he did not accept the causality and linkage between the staging tools purchase and the McAfee repayment suggested by the Claimants' simplified slide and maintained that no one at Autonomy had suggested a link to Mr Baiocco at the time.

(5) He was not involved in the discussions between Autonomy and Capax Discovery regarding prompt payment (which amounted to early payment by Capax Discovery). But, asked about it in cross-examination, he saw it as unproblematic:

> *"If we had agreed to pay early in return for being paid early, then that would be a reasonable commercial action."*

(6) Further, he told me that Autonomy would naturally expect prompt payment by Capax Discovery in return, and this reduced Autonomy's days sales outstanding. Other companies took a netting approach but Autonomy did not:

> *"No, because, as we've discussed before, when someone owes you money and you owe them money, what you normally can do is just net it instantaneously, which is in both parties' interests because their day sales are outstanding, are reduced by that and it also helps their credit rating if they require credit. In our case we did actually send the money back and forth because we practise something called cash transparency, but we would only send the money on the understanding that the money would come straight back. It was equivalent to it being netted."*

(7) He was not involved in the MAF payment or letter. He told me he did not accept that the MAF was paid on his authority unless that was documented on the emails (which it was not). Although Dr Lynch was not involved in this payment, he rejected the idea that it connoted anything improper.

910. In his written closing, it was also submitted that it was not squarely put to him that he knew about the revenue recognition or knew that the revenue recognition was improper.

911. However, in my judgment:

(1) The McAfee deal was carefully monitored by Mr Hussain, and Dr Lynch was continuously updated by Mr Hussain about its status.

(2) The emails sent by Mr Hussain to Dr Lynch included information which I consider and find Dr Lynch would have appreciated meant that (a) the prospective deal with McAfee would not be closed within the quarter, (b) a sale to a VAR would be made instead, (c) the VAR would in all likelihood be a "friendly" VAR, (d) the sale would not involve real risk for the VAR nor any real change to Autonomy's dealings with McAfee thereafter and (e) the way the matter thereafter proceeded would conform to the pattern implementing the strategy over which he had from its inception presided and encouraged (and would not involve the VAR in any dealings with McAfee at all).

(3) Dr Lynch knew also of and approved the staging tools transaction. I reject the notion that he simply signed because others had, which would have been entirely contrary to (a) the requirement for his approval which his own rules stipulated, (b) the way he ran Autonomy and (c) his nature as I came to assess it.

912. The Claimants' case was adequately put to Dr Lynch: he knew that what was being put against him was the case summarised in the preceding paragraph.

913. In summary, in my judgment, Dr Lynch knew that the sale to the VAR was, as usual in the case of these large VAR transactions in the Relevant Period, illusory; and that the staging tools transaction was in substantial part required to relieve Capax Discovery from the hook.

914. The payment of a MAF would have been part of the usual pattern; but I accept that the decision to pay and the implementation of it appears to have been carried out by others (all others in fact) in the cabal, and Dr Lynch was not ostensibly involved.

915. However, I need make no determination of that: I am satisfied without a finding about the MAF, and find, that Dr Lynch had "guilty knowledge".

VT28: Capax Discovery/UBS Q1 2011 and VT34: Capax Discovery/UBS Q2 2011

The first Capax Discovery/UBS purchase order

916. In January 2011, Autonomy was seeking to negotiate a deal with UBS, the well-known bank. On 13 January 2011, Mr Hussain emailed Mr Egan and Dr Menell, copying in Dr Lynch that the negotiations were going "*v well*". Even at that time, however, there was a note of caution: the email forwarded one from Mr Glenn Perachio, another Autonomy employee, headed *"Need to speak about UBS and rumours there re Deloitte"* and Mr Hussain advised that *"…UBS legal got negative feedback from Deloitte US and it's causing concern…"*

917. In March 2011, Mr Hussain learned from an internal email (circulated to the legal department as well as Mr Hussain) that the *"quick hits"* had *"turned into an ongoing saga…and constant growth in what UBS wants us to show"*; and that UBS's demands for proofs of concept (evidence that the performance of a desired task was feasible) meant that it would "*take us several quarters to even get all of this up, running, and POC'd, let alone get them to buy anything*". There was no hope of concluding a deal in time for the end of Q1 2011.

918. On 31 March 2011, the last day of the quarter, at Mr Egan's request, Capax Discovery sent to Autonomy a purchase order for UBS as end-user. The licence fee payable was $8 million, with an annual support and maintenance fee of $400,000. The money was to be paid in two equal instalments, on 4 July 2011 and 29 July 2011 respectively.

919. Mr Scott included "*Capax – UBS*" within a list of "*8A deals*" he sent to Mr Hussain, at Mr Hussain's request, on 1 April 2011.

The second Capax Discovery/UBS purchase order

920. Despite these difficulties, negotiations between Autonomy and UBS continued in Q2 2011. On 9 June 2011, Mr Hussain sent Dr Lynch an email, subject, "*I need 2 out of the top 3 or 8 out of the top 10*". Third in his list of deals, with an expected fee of $8 million was UBS.

921. On 27 June 2011, Mr Hussain sent UBS a proposal with revised payment terms. That day, Ms Sarah Wilkinson of UBS sent an email to Mr Hussain, querying "*the offer you made associated with the leverage of an 8A payment agent*" and (since she had *"never heard of this construct previously"*) requesting "*a little more colour and background on this proposal*". Mr Hussain immediately forwarded the emailed to Mr Egan (copying in Mr Kanter) stating only *"Please help"*. In the meantime, Ms Julie Dolan (an Autonomy lawyer) contacted her UBS counterpart with some information. When UBS asked whether Autonomy was proposing that UBS contract directly with the 8A entity, Ms Dolan said, "*No, not at all. All agreements will be between Autonomy and UBS. We are asking that the*

third party entity acts as a paying agent only. All invoice and payments are pass through the third party".

922. On 28 June 2011, Mr Hussain sent a further proposal to UBS. That day, Mr Hussain sent Dr Lynch an email entitled "*quick updates*", which stated, "*Ubs – no further news, we got everything over to Sarah, we have a final legal call tomorrow*". On 30 June 2011, Mr Hussain informed Dr Lynch, "*UBS – paperwork all done (1 am last night), michelle trogni for final signing this am*".

923. However, on 30 June 2011, Ms Wilkinson wrote to Mr Hussain to say that, "*Regrettably, despite huge efforts, it has just not been possible to complete the internal consultation and approval processes in time*". Mr Hussain forwarded the message to Dr Lynch and Mr Kanter without comment.

924. It would therefore have been clear to Dr Lynch and Mr Kanter that any VAR agreement in respect of a UBS deal would have to be implemented on the very last day of the quarter. Plans to do that were already on foot.

925. On 30 June 2011, Mr Scott sent Mr Hussain, Mr Egan and Mr Chamberlain a draft purchase order to be submitted by Capax Discovery, for UBS as end-user, and requested approval. Approval must have been given, because Mr Scott then sent the draft purchase order to Mr Baiocco. At this point, the licence fee was stated to be $5.5 million. However, less than an hour later, Mr Scott sent a revised draft purchase order with a higher licence fee of $6.5 million. On 1 July 2011, a yet further draft was sent, with a yet higher licence fee of $7,644,132 (plus an annual maintenance fee of $383,206.60).

926. No changes were made to the software ordered. There is no evidence of any objection, or indeed any response at all by Capax Discovery to these sudden substantial increases (of over $2 million) in the ostensible payment obligation for the same products. Nor is there any evidence of Capax Discovery ever speaking to UBS or doing anything else to determine that on-sales, much less on-sales totalling more than $16 million, could actually be achieved.

927. Mr Baiocco signed this last version, which was dated 30 June 2011 despite the fact that it was not signed until 1 July, the first day of the next quarter. Mr Baiocco gave the following unchallenged evidence about the two Capax Discovery/UBS purchase orders:

> *"As with the other VAR transactions, the terms of the purchase orders were given to us by Autonomy. Capax Discovery was not involved in the efforts to license the software to the end-user (UBS). Autonomy handled all of the negotiations with UBS."*

928. In accordance with that and the established pattern, these further negotiations with UBS were carried out by Autonomy alone (and overseen by Mr Hussain).

929. Autonomy's proposal to UBS was that UBS should contract directly with Autonomy but make payment via an 8A entity (Autonomic Resources LLC, an affiliate of Capax Discovery) as paying agent. Autonomy suggested that participation in this way in a US Federal Government-promoted scheme offered a number of benefits, especially in terms of goodwill. Autonomy also offered UBS a 3% discount for participation.

930. UBS did not favour this. It expressed concerns about the proposal that UBS should make payment under a direct deal with Autonomy to an 8A payment agent. It appears from an email dated 19 July 2011 from Ms Wilkinson of UBS to Mr Hussain (copying three individuals working for UBS) that these primarily concerned any credit risk in payment to an intermediary; but there appeared also to be an undercurrent of concern as to the basis of interposing a paying agent at all and Ms Wilkinson noted that UBS could not *"see that the use of one of these entities purely as paying agent would support the aims of the SBA [Small Business Administration] program"*.[77] Ms Wilkinson's email concluded: *"On this basis, I have asked Sharon to ensure that the clause on the use of payment agents is removed from the contract."*

931. That proved to be the sticking point. As his annotations which he made on the email from Ms Wilkinson when forwarding it to Mr Kanter show Mr Hussain regarded all the other concerns as resolvable (for example, by Autonomy agreeing to hold UBS harmless); but he would not accept the deletion of the paying agent provision and told Mr Kanter to tell UBS *"Sorry it stays in"*. The Claimants asked me to infer from this obduracy on a point which would not otherwise have benefitted Autonomy that Mr Hussain had to have the provision for payment to a Capax Discovery affiliate so that monies could then flow to Capax Discovery to be used by it to pay its debt under the purchase orders for end-user UBS to which Capax Discovery had committed.

932. That same day (19 July 2011) Mr Kanter advised Ms Wilkinson by email accordingly. By email sent only two minutes later, Ms Wilkinson responded:

> *"Having submitted this three times to our internal legal team, and had it rejected three times, I think we're done on this.*
>
> *Sorry that we couldn't oblige, but the decision is now final."*

933. That was that: there was to be no end-user deal to generate receipt from which Capax Discovery could have paid Autonomy and discharged its indebtedness. Something else had to be done to get Capax Discovery off the hook.

934. The solution Autonomy found was a re-packaged deal with UBS. Autonomy entered into a direct agreement with UBS on 20 July 2011, with a total contract value of approximately $24,000,000, of which $13,489,860 related to the provision of Autonomy software. Under that direct deal, UBS paid Autonomy directly. There was no paying agent involved. However, Mr Chamberlain instructed Ms Ku (cc Ms Poppy Gustafsson) to issue credit notes to Capax Discovery for the two UBS purchase orders, explaining that since UBS had required their purchase to be invoiced directly Autonomy needed *"to remove these as they are no longer payable by Capax."* The Claimants contended that this made no sense, especially since if Capax Discovery was genuinely at risk, its liability would not in law be affected by any subsequent agreement to which it was not a party.

935. The Claimants submitted that this series of transactions fell into the well-established pattern:

[77] In an earlier email, dated 27 June 2011, Ms Dolan of Autonomy legal had explained to UBS that the SBA was a program supported by the US Federal Government in which a number of authorised Autonomy resellers were involved. Autonomy had offered UBS a 3% discount if it participated though an authorized reseller.

(1) A sale to a friendly VAR at the last possible moment (or in this case, it appears, beyond it) to make good the revenue which had been expected from a 'real' sale.

(2) Complete indifference on the part of the VAR as to the purchase price from Autonomy, or the sale price which might be expected from an end-user.

(3) No contact by the VAR with the proposed end-user either before or after the VAR sale to determine the prospect and likely price range of an end-user sale;

(4) Legal documentation emphasising the absolute and unconditional nature of the VAR sale and the obligations imposed.

(5) The continuation after the VAR sale of negotiations for an end-user sale as if the VAR sale had never taken place: in this case, only Autonomy was negotiating with UBS, and the only contract in contemplation was one between Autonomy and UBS.

(6) The absence of any suggestion of the VAR being asked still less required to pay.

(7) Efforts by Autonomy to ensure an apparently legitimate route to pay the VAR the proceeds of any end-user sale successfully negotiated.

(8) If the negotiations failed and no end-user sale eventuated, the negotiation and implementation by Autonomy of other means of ensuring that the VAR was not left on the hook.

936. In the case of VT28 and VT34 the colours on the pattern were in some ways particularly vibrant:

(1) The remarkable indifference of Capax Discovery to a sequence of unexplained and substantial increases in the purchase price for the second Capax Discovery/UBS purchase order (VT34);

(2) Mr Baiocco's casual signature on 1 July 2011 of a purchase order prepared and provided to him by Autonomy unseen which had to be completed before the end of the quarter (30 June 2011);

(3) Autonomy's insistence on interposing an 8A payment agent in the Capax Discovery group (Autonomic Resources LLC) to be used as a channel for the purchase price under the end-user sale to be recycled and repaid to discharge Capax Discovery's own indebtedness;

(4) When that eventually drove UBS away from the original deals, Autonomy's immediate engagement in selling the same software to an end-user (in this case, the same end-user, UBS) whilst the VAR (which notionally owned the software) did nothing.

(5) The payment of a MAF to the VAR (in this case of $1,644,733) for doing nothing except lending its name to notional legal liability.

937. The Defendants responded that:

(1) The fact that the VAR transactions were each made at the end of a quarter does not signify anything improper if (as was the case, and Mr Baiocco confirmed) Capax Discovery was unconditionally on risk: the question was not whether the risk was wise but whether it was assumed;

(2) Mr Baiocco was keen to establish a relationship with UBS and saw the reseller deals as the way into that;

(3) Mr Baiocco confirmed the truth and accuracy of the parts of the Goldberg Segalla letter which specifically dealt with these transactions, including statements that (i) Capax Discovery took on risk and if the end-user transaction did not materialise Capax Discovery's only option would have been to resell to another customer (ii) this particular transaction also promised to be of significant benefit to Capax Discovery in that it represented a large professional services opportunity for Capax Discovery to install, integrate and implement Autonomy's software, (iii) such service opportunities and ongoing management being the basis for the strong partnership maintained between Capax Discovery and Autonomy (and subsequently HP);

(4) The arrangements for Capax Discovery to be credited with the value of the direct deal ultimately made between Autonomy and UBS up to the amount of the VAR deals (and paid a MAF) were commercially similar to those in the Kraft deal (VT3) and equally unobjectionable.

938. In my judgment, the Defendants' responses fell well short of a satisfactory answer; for the reasons identified by the Claimants and apparent from the facts as described above, VT28 and 34 fell within, and to my mind provide further striking examples of, the pattern; the 'sales' were illusory, neither risk nor control passed, and no revenue should have been recognised from them.

Knowledge of the Defendants

Mr Hussain

939. There is no dispute that Mr Hussain was involved in the UBS transactions and oversaw VT28 and VT34. He knew all the facts and matters set out above, and that revenue recognition could not be justified. He had "guilty knowledge."

Dr Lynch

940. The position was, as usual, not as clear in relation to Dr Lynch. Further, not only was no transaction-specific evidence shown or put to Dr Lynch, but the Claimants did not cross-examine him on VT28 and VT34 at all.

941. The Claimants sought to answer the fact that they did not cross-examine Dr Lynch for lack of time; and they (a) pointed out that Dr Lynch said nothing about either transaction in his witness statement, and (b) submitted that given the usual roll call of senior individuals involved – Mr Hussain, Mr Kanter, Mr Chamberlain, Mr Egan and Mr Scott – the Court should infer that the two Capax Discovery/UBS purchase orders fell within the general authorisation given by Dr Lynch for VARs to be used as placeholders, to enable the improper recognition of revenue, as and when required.

942. It was for the Claimants to use their time as they saw fit: whilst not endless it was sufficient. It is understandable why they should have decided not to devote any part of it to cross-examining Dr Lynch on a subject on which he had given no evidence. But the result was that Dr Lynch had no opportunity to traverse or set in a kinder context, the particular features of VT28 and VT34 and either to explain them or contradict the Claimants' case that he was aware of them.

943. The question is whether, because the Claimants did not cross-examine Dr Lynch on the particular transactions, they are precluded from reliance on evidence put to him and his answers on their general case as to the overall strategy of using VARs as placeholders to enable the improper recognition of revenue and its implementation by way of the pattern; and if not, whether they were able to show in a way which did not call for a fresh response from Dr Lynch that these particular transactions fell into that pattern.

944. It seems to me that the Claimants cannot rely on transaction-specific matters which they did not put to Dr Lynch as evidence of his knowledge. But I do not accept they cannot rely in relation to these transactions, on general matters common, or alleged to be common, to all the impugned VAR transactions and his responses when confronted with them, simply because they were not once again rehearsed by reference to the same basic pattern in these transactions.

945. The Claimants had plainly and repeatedly put their general case to Dr Lynch on his "guilty knowledge"; that he presided over and encouraged the strategy and encouraged its implementation in the way disclosed by the pattern. He had ample opportunity, which he took, to seek to explain why if there was any pattern, none of the features said to reveal and comprise it were such as to make revenue recognition improper, and that in any event he was well removed and was not told and did not see anything such as to fix him with knowledge of impropriety.

946. In my judgment, it is clear that Dr Lynch did preside over and encourage the implementation of the general strategy; it was not disputed that he had been told and kept informed by Mr Hussain of the fact of these transactions, and the fact that no end -user deal within the relevant quarter had proved possible and that Autonomy had resorted to a VAR. The more difficult question is whether Dr Lynch might have had some basis in fact to dispute that he had knowledge that the particular transactions were "pattern" transactions.

947. In my judgment, the general case fairly put to Dr Lynch included that transactions which (a) were of a size that Mr Hussain was depending on them to meet revenue targets (b) had failed to complete within the quarter (c) were being remitted to a VAR and (d) handled by the 'team' of Mr Hussain, Mr Kanter, Mr Chamberlain, Mr Egan and Mr Scott, were transactions within the strategy, and would follow the pattern. By now, in 2011, he had seen it all so often before. I have concluded that Dr Lynch had "guilty knowledge" of the improper recognition of revenue from VT28 and VT34.

948. I would add, however, in case I am wrong in that approach or conclusion, that:

(1) Whether or not Dr Lynch had "guilty knowledge" of VT28 and VT34 has not affected at all my analysis of his knowledge in respect of the other impugned VAR transactions.

(2) Although individually large, the sums involved are not such as would affect my ultimate decision as to the value of Autonomy at the date of the Acquisition or the price that HP would have paid.

PART III OF SCHEDULE OF IMPUGNED VAR TRANSACTIONS

949. In this Part III of this Schedule, I address the VAR transactions comprising the parts into which a very large composite deal with BofA (or subsidiaries of BofA) was split in circumstances described below. Two (VT16 and VT21) were with Capax Discovery and two (VT23 and VT24) were with DiscoverTech.

The Bank of America ("BofA") transactions: VT16, VT21, VT23 and VT24

950. In Q3 2010, Autonomy began working on a very large deal with BofA, described by Mr Hussain in emails to Dr Lynch as *"the big one"*, with an aggregate value of some $20 million. This was not concluded in Q3 2010: but it became a vital part of Mr Hussain's planned route to achieving the forecast of US revenues of $45 million in Q4 2010. In comments on an email dated 31 October 2010 from Mr Egan (which was sent to him and Mr Mooney but also circulated to Mr Scott and Dr Lynch) he stressed its importance (together with another large deal with an entity called Acxiom) as one of *"2 deals that could swing the quarter massively for us"*.

951. The importance of the large BofA deal became a consistent theme of Mr Hussain's communications with Dr Lynch during the quarter. I have taken the following factual summary very largely from the detailed account in the Claimants' written closing submissions:

(1) On 4 November 2010, Mr Hussain sent Dr Lynch and Dr Menell an update on the "*big deals*". As regards BofA, he said, "*want to do a deal by end of q. will be big*" and that he will "*be chasing*".

(2) On 7 November 2010, Mr Hussain sent a group revenue update to Dr Lynch and others. His update identified the "*key deal*" as being BofA at circa $10 million to $20 million.

(3) On 8 November 2010, Mr Hussain emphasised to Mr Mooney (copying Dr Lynch) that getting the pricing proposal to BofA as soon as possible was the "*most important thing we should be doing*".

(4) Mr Hussain provided further updates to Dr Lynch (and others) on 10 November 2010, 11 November 2010, and 14 November 2010. In an update on 17 November 2010 sent to Dr Lynch and Dr Menell, Mr Hussain expressed concern about Mr Egan's management of the deal and said that he (Mr Hussain) personally would focus on it "*as this is key for q*".

(5) By 19 November 2010, Mr Hussain told Dr Lynch that the figure for the licence fee was currently between $24-26 million and that BofA "*seem to be very engaged*".

(6) In an email dated 20 November 2010 (circulated to Dr Menell, Mr Kanter and Mr Chamberlain), Mr Hussain reiterated that "*BofA and VMS are the key to the quarter*".

(7) On 2 December 2010, under the subject heading *"More positive update",* Mr Hussain told Dr Lynch: "*BofA – accountants and lawyers to sit in a room on Tuesday. Deal is definitely on*".

(8) By 7 December 2010, Mr Hussain informed Dr Lynch that he was including $17 million in revenue from BofA during the quarter, and that three days of discussions with BofA had been scheduled.

(9) On 9 December 2010, Mr Scott asked Dr Lynch to approve a memorandum setting out the contemplated terms. Dr Lynch gave his approval in principle that day (stating *"This looks fine to me in principle if people have done their homework on the details*"), adding a comment on the cost structure.

(10) On 17 December 2010, however, expectations of a Q4 2010 deal were pegged back after Mr Egan was told by Mr Vince Debban of BofA that the agreement would not receive the requisite internal approvals in time for it to be concluded in 2010. Mr Egan's email to Mr Hussain stated, "*I don't know what to say*". Mr Hussain raised the matter with Dr Lynch and replied to Mr Egan suggesting a form of messaging that Mr Egan should adopt with BofA, describing the deal as a "*massive opportunity for the bank*" which could not be repeated in 2011. Mr Egan's response was despondent, stating *"…but you do realize that that's it. It is not really a matter of finance being unwilling. We have watched exceptional process unfold for 10 days. You saw it first hand."* Mr Hussain's reply to that was:

> *"We have to beg and beg again.*
> *We can't have the same deal next quarter."*

952. The urgency and importance ascribed to trying even at this stage to get revenue which could be recognised within the quarter was reflected in Mr Hussain's request on 18 December 2010 that Dr Lynch and others join an "*All hands call today*", and in the activity afterwards to try to reinstate the deal:

(1) Mr Hussain again proposed messaging to BofA to the effect that there could be no deal in 2011 in the same form as the deal then under consideration, because Autonomy's auditors would require such a deal in 2011 to be disclosed and explained. Notably, Mr Hussain asked Dr Lynch whether this accounting point passed Dr Lynch's "*smell test*".

(2) Dr Lynch replied the same day, "*I would avoid using words auditor and audit*" and instead suggested different messaging:

> *"More: as previously disclosed to the market we are increasing and restructuring disclosure and this will set an unworkable comp under this new model, so this Is [sic] a unique point in time to do this deal".*

(3) Mr Hussain prepared a draft email for Autonomy's BofA deal team (which he copied to Dr Lynch), outlining the proposed message to BofA, and invited comment. The draft email, which stated in the subject heading *"Possible email that can be forwarded to the BofA team…"* and was obviously drafted for BofA's consumption, commenced in terms loyally reflecting (with a little bit of

translation) the high-pressure "now or never" message that Dr Lynch had suggested:

> *"I realize that the BofA team is having some difficulty in getting all approvals in time for 2010, but I have to stress to you that this deal is not possible for us to sign in Q1 2011. As Autonomy has previously disclosed to the equity market we are increasing and restructuring our accounting disclosure in 2011, and doing the deal in 2011 will set an unworkable comparative under this new model. So this is a unique point in time to do the deal. Our additional disclosure of a "commitment" figure in 2011 will show major movements in a 2011 BofA deal which we will need to disclose and explain – and we won't do this."*

It then set out various figures to try to persuade BofA that, on analysis, it would not actually be committing (net) more than $10.5 million, and asked for one last effort to "*get the deal over the line*". Mr Hussain continued to keep Dr Lynch apprised of his efforts with BofA on 19 December 2010 and 20 December 2010.

953. These efforts were unsuccessful. On 21 December 2010, Mr Ronald Johnson of BofA emailed Mr Hussain:

> *"Thank you for the note. Andy*[78] *and I both spent several hours on this late into the day yesterday. We met with Tom Korzik and decided collectively that because the entire deal structure was being re-written, the approval is actually against the full $48MM transaction. Even from a "complete transparency" perspective, we all felt like we would want the full leadership team to be aware of our activities.*
>
> …
>
> *We aren't able to give you an official response this morning but to be very honest, this is a long shot given the holidays and the number of educational conversations that would need to occur. The leaders at the top of our house frown on these last minute transactions. The perception they have of us is one of unorganized and no process rigor. Accordingly, this might be the right thing to do for BAC, just the wrong timing*".

954. Mr Hussain forwarded the news to Dr Lynch, stating only "*Oh s**t*".

955. Even then, the Defendants were not yet ready to give up. On 21 December 2010, Mr Hussain emailed Mr Egan (copying Dr Lynch) telling him "*I spoke to ron [of BofA] – he was just out of the shower, not really happy to hear from me*" and suggesting that "*Stouffer reaches out to Carol [of BofA] for one last try even if we get a smaller deal it might be worthwhile*". That same day, Dr Lynch prepared a draft email intended for BofA which stressed that the transaction "*has to be done this quarter as it requires us to take an option on some excess capacity which is not possible next year*" and stated that, "*at the last minute we have unexpectedly hit a bureaucratic hurdle*" because the relevant finance person at BofA was on holiday. The draft email requested advice on how to overcome the issue. Later

[78] Possibly Mr Andrew McGowan of BofA. Mr Korzik, I assume, was part of BofA.

that day Dr Lynch sent the email to Mr Simon Mackenzie-Smith. Mr Mackenzie-Smith was Head of BofA in London.

956. Later still, in the evening of the same day, Mr Egan forwarded to the Defendants an email he had sent to BofA recording that Mr Hussain had authorised "*a further $2M reduction in the license fee currently on offer for execution in 2010*". Mr Egan observed,

> "*I'm on the roof but will stay away from edge until we hear back.*"

957. Dr Lynch accepted in cross-examination that Mr Hussain, for his part, was also in a state of high anxiety as to whether the potential BofA transaction would be concluded.

958. On 22 December 2010, Dr Lynch continued his correspondence with Mr Mackenzie-Smith, saying that he "*would great[ly] appreciate any subtle help*" that Mr Mackenzie-Smith could give to the matter.

959. It seems, however, that BofA had concerns "*over the value of the licenses and does this deal pass the smell test*". Mr Egan sought to address this by sending BofA an email (dated 23 December 2010) with a note emphasising that *"the answer is yes absolutely"* but pointing out that the deal *"must be thought of as a Program not just a 'Client Access License' purchased"* and explaining (interestingly[79] in the context of the Claimants' 'Hosting case', as to which see the Hosting section in the main body of this judgment) that the benefits of the purchase of the licence which the deal entailed included (primarily) the following:

> *"1. $73m without the deal; $48m with the deal*
>
> *2. $19m license fee is offset against the volume and delivery credits, so its* ***<u>$10m net new</u>*** *investment to* ***<u>access</u>*** *the savings. For this BAML gets unlimited software plus lower fees.*
>
> *3. A 50% reduction in archiving costs which come from massive lowering of archiving fees and supervision services for free + no expense on the 900tb legacy data…"*
>
> (Emphasis as in original)

960. On 28 December 2010, Mr Hussain forwarded to Dr Lynch an email which suggested the odds of getting the deal approved by 31 December 2010 were 50/50.

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[79] By way of very brief explanation, this is interesting in the context of the 'Hosting Case' because the essential claim in that part of the case is that the licence sold as part of what was termed a *"hybrid hosting solution"* (which had two elements, (i) a licence to software and (ii) hosting services) was presented and accounted for as conferring a right separate from the advantage it also brought in terms of reduced data storage fees. That accounting treatment enabled immediate recognition of the revenue from the licence fee whereas if the licence could not properly be regarded as separable, the revenue from its sale would be lumped together with the revenue from hosting services, and would be required to be spread over the length of the hosting contract. The interest of the explanation given to BofA is that the licence is described simply in terms of offering access to savings, and there is not a whisper in the headline description of its separable value. That would support the Claimants' case that the licence was an accounting artifice and the revenue recognition of fees from its sale was improper.

961. On 29 December 2010, with the quarter end fast approaching, Mr Krakoski emailed Mr Hussain stating that he had put calls and emails into BofA but that it was all quiet: "*Will advise on activity as soon as they [BofA] surface*". Mr Hussain forwarded this email to Dr Lynch, adding only the observation "*Almost unbearable!!*".

962. On 30 December 2010, Dr Lynch continued to make direct contact with senior individuals at BofA in the hope of concluding a deal. On 31 December 2010, Mr Mackenzie-Smith responded, "*I have emailed my colleagues in the US plus UK to give this one last push. Fingers crossed*". Dr Lynch forwarded this response to Mr Hussain.

963. However, on 31 December 2010, Mr Debban of BofA stated that an agreement would not be executed that day. Mr Hussain thanked the BofA team for their efforts and asked whether even part of the deal could be approved as a favour. Nothing eventuated.

964. As a result, there was a significant gap in revenue that needed to be filled.

Splitting up of the BofA deal into smaller pieces sold to VARs

965. It was the unchallenged evidence of Mr Egan that, when it became apparent at the very end of the year (2010) that no BofA deal would be signed during Q4 2010, Mr Hussain instructed Mr Egan to break down the deal into smaller pieces and sell the pieces to different VARs. That was necessary because of the size of the overall deal: it was too large for any single VAR (including MicroTech) to take on alone. The splitting up of the deal and the resort to VARs were plainly expedients to generate recognised revenue in Q4 2010 to cover the shortfall left by the failure to close the BofA transaction. Dr Lynch accepted in cross-examination that he knew that, prior to 31 December 2010, no VAR had been involved in Autonomy's negotiations with BofA, though he sought to distinguish this from other VAR deals, stating that *"Obviously we did other things with them…"*.

966. VT16 and VT21, together with VT23 and VT24, comprised these "smaller pieces" which were parcelled out amongst the selected VARs, namely Capax Discovery and DiscoverTech:

(1) VT16 was originally a VAR transaction in September 2010 between Autonomy and Capax Discovery in respect of which the named prospective end-user was Amgen. Ultimately, Amgen dropped out[80] and was substituted by BofA.

(2) VT21 was a VAR transaction in December 2010 between Autonomy and Capax Discovery in respect of which the named prospective end-user was Merrill Lynch, which had become a subsidiary of BofA in January 2009 (in the wake of the financial crisis precipitated by the collapse of Lehman Brothers).

(3) VT23 and VT24 were sales by Autonomy to DiscoverTech for end-user BofA. Much as in VT16 and VT21, the software sold to DiscoverTech in VT23 and VT24 was ultimately sold by Autonomy to BofA as part of the overall BofA transaction.

[80] VT16 was originally a separate transaction concluded before Autonomy entered into initial discussions for the deal with BofA. It originally had nothing to do with the BofA transaction. It only became part of it when Amgen dropped out and was substituted by BofA in respect of the purchase of software specified in VT16. Autonomy then concluded a direct deal with Amgen in Q4 2010 for different software, rubric *"OT 3", "Repurposed"* (see below) as a BofA deal, VT16 then became a constituent element of the overall composite BofA arrangements.

967. These constituent elements of the BofA transaction were, in a sense, corralled together by the introduction of a "lead reseller" namely, MicroTech (see further below). MicroTech acted, in effect, as the conduit for Capax Discovery and DiscoverTech to be paid their respective shares from Autonomy's direct sale to BofA.

968. Looking forward in the story, when (as had always been intended) Autonomy eventually concluded a direct deal with BofA in February 2011 (which included the software that it had parcelled out to the selected VARs) arrangements were made to ensure that the selected VARs received what they would have received had they themselves on-sold to BofA (though in fact it was never intended that there should be, and there never was, any end-user sale by any of the selected VARs).

969. Thus, under the direct agreement between Autonomy and BofA, it was provided that payment was to be made to Autonomy or its designated payee. Autonomy designated MicroTech as its payee, and BofA then paid the total $19,500,000 licence fee (minus an early payment discount agreed of $500,000) to MicroTech rather than Autonomy. MicroTech then paid out $10,000,000 to DiscoverTech and $9,000,000 to Capax Discovery.

970. As a result, Capax Discovery received (via MicroTech) in the case of each of VT16 and VT21 a share of the aggregate amounts paid by BofA, much as if it had on-sold the software it had acquired under its VAR transactions to BofA. Likewise, DiscoverTech received its share (via MicroTech) as if it too had on-sold to BofA.

971. The reconstituted, large composite direct deal which Autonomy eventually completed with BofA in February 2011, and which included a further restructuring of BofA's Digital Safe hosting arrangements, was of an aggregate value of some 8.9% of reported revenue in Q1 2011.

972. Although all four VAR deals came together as summarised above, I shall adopt the same basic approach as the Claimants, and focus first on the Claimants' allegations in respect of VT16 and VT21, which I deal with in tandem, albeit that those two transactions took place in different quarters of 2010, whereas VT21 was contemporaneous with VT20 (as to which see paragraphs 842 to 866 above).

973. Accordingly, I first address the Claimants' basis for impugning VT16 and the Amgen deal as it was originally conceived. I then explain the Claimants' allegations relating to how that deal was *"re-purposed"* and became part of the complex arrangements for the ultimate sale to BofA (which brought in VT21) and for the parcelling out of the BofA sale proceeds to all the three VARs concerned in VT16 and VT21. I then discuss the Claimants' allegations in respect of the cancellation of any further payment obligation on the part of Capax Discovery under VT16 and VT21, and also the controversy concerning the payment of two sets of MAFs to Capax Discovery (and also to DiscoverTech). After that, it will then be necessary for me to deal with certain features of the DiscoverTech transactions, VT23 and VT24.

974. It will also be necessary to consider the issue of 'guilty knowledge'. The Claimants contended that the size and importance of these deals, and especially of the composite BofA deal for which (on the Claimants' case) they were the interim arrangements, is evident from and commanded the particularly close personal involvement of the Defendants.

VT16: the original Capax Discovery/Amgen deal in more detail

975. VT16 and the background to its *"repurposing"* can be summarised as follows. In Q3 2010, Autonomy was hoping to sell a software licence to Amgen (see paragraph 966(1) and footnote 80 above). The deal was a large one, and important to Autonomy in terms of revenue requirements for the quarter. However, despite offering Amgen a discount to close the deal within the quarter, on 30 September 2010 Amgen's Chief Information Officer, Mr Tom Flanagan ("Mr Flanagan") emailed Mr Egan (who was handling the matter, though Mr Hussain was also closely involved) to say that they could not do the deal in that quarter but could in the next. That email was forwarded by Mr Egan to Mr Hussain, and also to Dr Lynch (who had been sent an earlier email also, and who accepted in cross-examination that he *"may have known something"* about the deal, though he denied any involvement in the negotiations or other details).

976. In order to recognise revenue in Q3 2010, Autonomy, with the usual urgency, engaged Capax Discovery (through Mr Baiocco) to act as a VAR right at the end of the quarter. On the same day as Mr Flanagan's email and at Mr Egan's request, on 30 September 2010 (the last day of Q3 2010), Capax Discovery issued a purchase order with a licence fee of \$9,000,000 plus one year's support of \$450,000, for on-sale to end-user Amgen. Dr Lynch accepted in cross-examination that he knew that Autonomy resorted to Capax Discovery in order to obtain recognised revenue on a purchase order issued before the end of the quarter (though as usual he intimated he became aware only after the event, which I do not accept).

977. The purchase order stated that Capax Discovery was to pay 10% of the purchase order price (\$945,000) within 30 days, i.e. by 30 October 2010, with the balance to be paid in two tranches of \$4,252,500 within 90 and 120 days respectively, i.e. by 29 December 2010 and 28 January 2011 respectively. Unusually, the purchase order expressly gave Capax Discovery qualified permission (expiring after 12 months) to sell to another end-user if a sale to Amgen could not be completed. Otherwise, the purchase order was on the terms of the June 2009 Capax Discovery VAR Agreement summarised in paragraph 60 above.

978. After issuing the purchase order, Autonomy continued its negotiations with Amgen. Capax Discovery was not involved at all. The Claimants contended that, consistently with the 'pattern' common to the impugned VAR transactions, there was never any intention that Capax Discovery should participate in negotiations with the (then) prospective end-user in any way, and certainly it never did so.

979. VT16 then took an atypical turn. Revenue having been recognised in respect of it, it was, in effect, moth-balled (or as it was put *"repurposed"*) to be brought out of the cupboard as part of the composite BofA deal. In the meantime, Autonomy entered into a direct but different deal with Amgen in December 2010 for a total of \$14,882,076: but this was made up largely (as to \$11,382,076) of hosting and servicing fees; the licence fee was much less: \$3,500,000. The Claimants called this the *"other Amgen transaction"* with the rubric "OT 3", and they alleged that "OT 3" was also accounted for wrongly, not by reference to any VAR involvement but because it was (so they alleged) wrong to recognise revenue up-front in respect of the deal in Q4 2010: I address this separate and differently based allegation in the section in the main body of the judgment that deals with the "Other Transactions". Thus, VT16 had in a sense two incarnations: and both are illustrative of Autonomy's use of 'friendly' VARs.

980. In the present context, the following aspects of VT16 and its *"repurposing"* are of particular interest in terms of the 'pattern' asserted by the Claimants:

(1) What Deloitte and the Audit Committee were told about the circumstances of VT16 and the subsequent negotiations with Amgen: it being the Claimants' case that both Deloitte and the Audit Committee were given a very different impression as to what the respective roles of Capax Discovery and Autonomy were to be in the transaction than was in fact the case, and were thus misled.

(2) The substitution of BofA in place of Amgen as the intended end-user, and its presentation as the *"re-purposing"* of VT16, which provided a mechanism to ensure that Capax Discovery was not left "holding the bag" in respect of its payment obligation under the VT16 purchase order.

(3) The justification advanced for payment of a MAF of nearly $1 million.

(4) The backdating of the documents recording and providing for the substitution of BofA *vis-á-vis* Capax Discovery.

(5) Deloitte's understanding of the transaction (including the *"repurposing"*).

Whether the VAR's role in respect of VT16 in its first incarnation was misrepresented to Deloitte and the Audit Committee

981. As regards the first of those contentions (see (1) in paragraph 980 above), Mr Baiocco's unchallenged evidence[81] in his witness statement was that Capax Discovery *"had no involvement in the negotiations with Amgen, which were conducted by Autonomy both before and after Capax Discovery issued its purchase order."* There is no evidence that Capax Discovery participated at any time, or in any way, in Autonomy's efforts to reach an agreement with Amgen.

982. The Claimants relied on Deloitte's report to the Audit Committee for Q3 2010 to support their case that this was not the impression given to Autonomy's Audit Committee. That report included the following statement (which I infer was based on information supplied by Autonomy):

> *"This is a $9.0 million Digital Safe licence deal sold to this end-user via the value added reseller Capax Discovery LLC ("Capax"). Autonomy have introduced this customer to the value added reseller in order for them to carry out the professional services implementation work required to migrate Amgen from EAS mail to DS mail. On the basis that Capax are up-to-date with their payments on the majority of the Eli Lilly sale discussed in Q2 2010, management has concluded there are no concerns over recoverability that would impact revenue recognition."*

983. The Claimants relied also on Mr Bloomer's responses as to his understanding of this statement (and in particular, its second sentence):

> *"Q. So you were told that Autonomy had introduced Amgen to Capax Discovery, yes?*

[81] Dr Lynch was asked in cross-examination whether he had any basis to dispute this evidence: he confirmed he had not, adding *"I'm not involved at that level"*.

A. Yes.

Q. And that is what you understood at the time?

A. Yes.

Q. You were told that Capax Discovery had agreed with Amgen that Capax Discovery would carry out professional services implementation work for Amgen, yes?

A. That was the implication of this, yes.

Q. It would have been your understanding that Capax Discovery would be the entity selling to Amgen, yes?

A. Well, based on the introduction from Autonomy, there was clearly an implication that Autonomy may have done the sale or agreed with Amgen [what] they wanted a reseller to do – my understanding was that the resellers did the professional services which Autonomy didn't do and hence this one where Autonomy have agreed a sale but there's a reseller needed so they've introduced Capax to do that role. That was my understanding of this one.

Q. Yes, the first sentence says that the licence has been sold via Capax, so your understanding would have been that Capax was the entity in the relationship with Amgen, yes?

A. Certainly that the bill was going to go to Capax, the invoice, and then the invoice from Capax on to Amgen, but the fact of the introduction, my recollection at the time was that Autonomy had the relationship with Amgen but that there was a reseller needed to do professional services and Autonomy introduced Capax to fill that role, and therefore the sale went through Capax. That was my recollection at the time.

Q. And if Capax never had any dealings with Amgen in relation to this transaction at any time, that would have been contrary to your understanding, yes?

A. If Capax never had –

Q. Any dealings at all with Amgen?

A. That would have been surprising given this commentary here.

Q. Yes. And it would have been something that it would have been relevant for you to know, yes?

A. I'd have wanted to know that to have the discussion both with management and the auditors about the transaction as a whole."

984. Even taking into account Mr Bloomer's suggestion that Autonomy's introduction of the VAR might have been with a view to the VAR providing services to the end-user in due course (which I do not think he can have taken to be a sufficient contribution of itself), he plainly took the statement to mean that Capax Discovery was always the party at interest and that the objective was always an end-user sale by Capax Discovery to Amgen.

985. The Claimants' case, which I accept, was that neither was the reality. The truth which was not told was that the sale to Capax Discovery was not intended to, and did not, make any difference to the negotiations carrying on between Autonomy and Amgen with a view to a sale by Autonomy directly to Amgen. In this first incarnation of the deal (as indeed in its second, after it had been *"repurposed"*) Capax Discovery was always intended to be entirely passive, with the assurance of some mechanism at the end of the day to release it from liability or give it the means of its discharge, and (as its rationale from Capax Discovery's viewpoint) the expectation of a handsome reward for its passivity. The perceived necessity to obscure (at best) the truth tells its own story against those responsible within Autonomy for misleading Deloitte, and through Deloitte, Autonomy's Audit Committee.

986. The Defendants sought to blunt the effect of this by presenting the intent and fact of a VAR's engagement (or not) in negotiations with the end-user as immaterial in determining whether the sale to the VAR qualified for revenue recognition. They relied especially on Mr Bloomer's evidence in the course of his re-examination, as follows:

> *"Q. Did you understand from your discussions with Deloitte whether there was any requirement that Autonomy itself must not negotiate with the end-user after the VAR deal had been entered into?*
>
> *A. No, not at all.*
>
> *Q. Did you understand from your discussions with Deloitte that there was any requirement that the VAR itself must conduct negotiations with the end-user?*
>
> *A. No, not necessary."*

987. However, that evidence did not answer why an accurate presentation had not been made to the Audit Committee; and nor did it properly address, let alone neutralise, the real point. Even if non-participation by the VAR in negotiations for an onward sale might not of itself demonstrate lack of substance, or no passing of risk or control for the purposes of IAS 18.14, the position is very different if the truth is that the VAR was to have not only no role but no interest, because the negotiations were not for a sale by it but for a direct sale by Autonomy. That would be a strong, usually determinative, manifestation of the reality that the VAR had not assumed any risk nor acquired any control of the goods, and its contractual obligations to Autonomy would be covered, not by onward sale proceeds, but by or via Autonomy itself (whether out of the proceeds of a direct sale by it or otherwise). Further, any remaining argument that even this might not be fatal if Autonomy could be said to be acting as the VAR's agent or quasi-agent would be disposed of if, as was also the case, the negotiation was not for an onward sale by the VAR, but the direct sale as principal by Autonomy for which Autonomy had always negotiated.

988. I have concluded that the role of Capax Discovery in VT16 (in its first incarnation) was not properly represented to the Audit Committee (or to Deloitte), and the fact that it was not gives rise to the inference that those responsible in Autonomy knew that the reality had to be disguised in order to obtain approval for the revenue recognition that was required.

989. That conclusion is fortified by at least one email: the one I have in mind was sent by Mr Hussain to Mr Egan and Mr Mooney dated 8 October 2010 stating that Capax Discovery were *"obviously… heavily involved"* which seems simply to be contrary to the facts. Such

pretence invites enquiry as to why it was thought necessary. Of course, Mr Hussain might have offered a different interpretation had he given evidence: but he did not.

The "re-purposing" of VT16 and its second incarnation

990. The second aspect of VT16 of particular note concerns the steps taken by Autonomy, after Autonomy had made a different deal with Amgen and Autonomy wanted to set up a separate deal with BofA for the purchase of the same software as was covered by Capax Discovery's original VT16 purchase order, to ensure that Capax was not left "holding the bag" in respect of the payment obligation under the VT16 purchase order.

991. The need for such steps was particularly acute because (despite its overall value) Autonomy's direct sale to Amgen for a licence fee of $3.5 million left a considerable shortfall of some $5.5 million on the original VT16 deal (in which the licence fee was $9 million). Something had to be done if Capax Discovery was not to be "left on the hook" or "left holding the bag" for at least the shortfall, even if Autonomy accounted to it for the full amount of the revised Amgen deal: and in fact, under the direct deal between Autonomy and Amgen, Amgen was to pay the fees to Autonomy, not Capax Discovery. As the Claimants put it the question was:

> *"How, then, to provide for the payment of the $9.45 million Capax Discovery order?"*

992. Mr Baiocco's unchallenged evidence was that Autonomy decided to do what it first called a "swap":

> *"Mr Egan told me that Autonomy had decided that this transaction would be replaced with one relating to [BofA], in what I recall Mr Egan described as a "swap" deal involving the cancellation of our Amgen deal and its replacement with a BofA deal."*

993. This swap was dictated by Autonomy. The introduction of BofA was entirely at the instance of Autonomy. BofA was Autonomy's customer. Capax Discovery had not had any dealings with BofA regarding any potential sale of Autonomy software. Mr Baiocco's evidence to this effect was not challenged.

994. Mr Egan explained the *"re-purposing"* or "swap" in his witness statement in these terms:

> *"In January 2011, Mr. Hussain asked me to determine how payments that were to be made by Bank of America under our then-anticipated deal with Bank of America could be used to fund payments by the VARs to Autonomy on their "at risk" deals with Autonomy. This gave me an opportunity to solve the problem of getting money to Capax Discovery to allow it to satisfy its payment obligation under an "at risk" deal for Amgen (in the total sum of $9.45 million) as end-user done in Q3 2010. Autonomy drafted a letter for Capax in which Capax requested that its license to sell software to Amgen be converted to a license to sell software to Bank of America. The price remained the same. Capax then signed, and Autonomy approved, that request."*

995. It seems clear that within Autonomy there was some uncertainty as to what this required and entailed. Mr J. Livius Guiao ("Mr Guiao"), an Autonomy lawyer who was tasked with preparing a draft of the letter that Mr Egan had in mind, sent the letter to Mr Chamberlain, under cover of an email dated 18 January 2011 copied to Mr Scott which stated:

> *"Attached is a draft letter from Capax to AUTN, requesting that we approve 'replacement' of the Amgen PO with a PO for BofA. Note, I left the amount blank, as I am not quite sure as to the overall structure of what we are doing."*

996. Evidently, Mr Baiocco did not know quite what was happening either. On 25 January 2011, Mr Egan asked Mr Baiocco to sign and return the letter. The letter was dated 31 December 2010. Mr Egan said: "*Please sign, as is, and importantly scan vs fax*[82] *(i'm on a plane) and email return*". Mr Baiocco wrote back to Mr Egan seeking clarification as to the effect of the letter:

> *"So once I sign this.*
>
> *I no longer owe Autonomy for Amgen/*
>
> *I will still get the 950k sales referral fee?*
>
> *I will then owe Autonomy 9.5 for B of A? This is on top of the deal we sold/did 12/31/10 for around 2 mil."*

997. Thus, Mr Baiocco (who seems from the email hardly have been able to believe it) wanted assurances that Capax Discovery would no longer owe Autonomy and yet be paid the 10% MAF (i.e., "950K") for his Amgen purchase order. His reference to the $2 million 31 December deal was a reference to Capax Discovery's Merrill Lynch purchase order (VT21) described later. His understanding at that time was that his obligation to Autonomy would then be in respect of the BofA transaction, rather than the Amgen transaction: not that it appears that he minded, so long as any risk was removed and his commission payments were safe.

998. Mr Egan responded, "*No you will not owe au for bofa. I will call you when I land. Wait till then.*" Later that day, Mr Chamberlain clarified the position in an email to Mr Egan and Mr Guiao:

> "*Livius is correct, They are repurposing. They will absolutely owe the cash for the $9.45m. They are selling to BofA instead of Amgen but the $9.45m must be paid."*

999. On 26 January 2011, Mr Baiocco sent Mr Egan some questions about the proposed swap which also demonstrate both his focus on his commission and confusion as to the nature of the legal position as regards Capax Discovery's obligations:

[82] The Claimants ascribed this stipulation to an intention to backdate: *"The problem with a fax, of course, is that it would immediately have revealed the fact that the letter was backdated."*

> *"Upon signature Autonomy will provide me the letter of release on Amgen (ala Kraft) immediately? We will get the PO for the commission/payable in 2 weeks or whatever you stated.*
>
> *We will get a PO from Microtek for the full amount of both deals for B of A. We will get commission for B of A signed on 12/31. Po?*
>
> *Why the 30 days payment guarantee?"*

1000. Mr Baiocco then signed and returned the letter that Autonomy had drafted for him. On 26 January 2011, Mr Egan forwarded a copy of the signed version to Mr Scott and Mr Chamberlain. The signed version, as noted above, bears a date of 31 December 2010, even though it was only drafted in mid-January 2011 and signed on 26 January 2011. It stated:

> *"As you know, Capax Discovery LLC ("Capax") and Autonomy, Inc. ("Autonomy'') are parties to that certain Value added Reseller Agreement dated as of May, 2009 (the "Agreement"). Pursuant to such Agreement, Capax submitted to Autonomy a purchase order dated September 30, 2010, relating to Capax' resell of certain Autonomy products to Amgen, Inc. (the "Amgen Purchase Order").*
>
> *Capax hereby requests that Autonomy agree to cancellation of the Amgen Purchase Order, subject to Autonomy's acceptance of this letter, which shall serve as a purchase order from Capax for Autonomy products to be provided to Capax by Autonomy and resold by Capax to Bank of America, N.A. The amount payable for such Autonomy products shall be US $9,450,000.00, invoiced immediately and due and payable from Capax within thirty (30) days from the date of such invoice. For avoidance of doubt, this letter shall serve as a purchase order from Capax in the aforementioned amount, which shall be governed by the terms of the Agreement.*
>
> *Please sign below and return an executed version of this letter to Capax, to acknowledge agreement by Autonomy to the terms set forth above."*

1001. It was put to Mr Egan in cross-examination that the substitution of BofA as end-user in place of Amgen "*took place in accordance with that contractual term*", namely the term of the Capax Discovery/Amgen purchase order that permitted Capax Discovery to sell the licence to an alternate licensee if no end-user deal eventuated within 90 days. In my view, this letter cannot be regarded as involving an exercise by Capax Discovery of its contractual right under its Amgen purchase order dated 30 September 2010.

1002. The provision in the Amgen purchase order which gave Capax Discovery a qualified right to sell the software licence to a different end-user was in the following terms:

> *"Notwithstanding anything herein to the contrary, in the event the [sic] Amgen fails to issue a contract, award, or order within ninety (90) days of the Effective Date by which it licenses the Autonomy Software Products and procures the Maintenance Services otherwise described hereunder, VAR shall have the right, upon written notice to Autonomy, to sublicense the Autonomy Software Products and distribute the Maintenance Services to an alternative end-user ("<u>Alternate Licensee</u>"), subject to the terms hereof ... Notwithstanding the*

> *foregoing, VAR's right to sublicense and distribute the Autonomy Software Products and Maintenance Services to an Alternate Licensee shall expire twelve (12) months from the Effective Date hereof, and VAR's failure to sublicense the Autonomy Software Products and distribute the Maintenance Services to an Alternate Licensee during said period shall not relieve VAR of its obligations hereunder."*

1003. The purchase order thus posited a situation where Capax Discovery, having failed to persuade Amgen to buy, might, after 90 days, find someone else willing to buy the licensed software. What happened here was very different. In summary:

   (1) During the initial 90-day period, Capax Discovery made no attempt to sell to Amgen. Instead, during that period, Autonomy sought to sell to Amgen.

   (2) Indeed, Autonomy was successful in achieving a sale of the licensed software to Amgen during the initial 90-day period, resulting in the direct Autonomy/Amgen deal dated 21 December 2010, albeit for a much lower licence fee;

   (3) Autonomy then found an alternative buyer of Autonomy software, namely BofA.

   (4) Autonomy drafted a request (backdated to 31 December 2010) from Capax Discovery to cancel the Amgen purchase order and treat the letter as a new purchase order for end-user BofA at the same price and for the same products.

   (5) Though Mr Baiocco was not sure what it all meant, Capax Discovery followed Autonomy's directions and signed and sent that request.

1004. The Defendants did not fully explain their attempts to present the "swap" or "repurposing" of VT16 as effected pursuant to the provision mentioned. It was not clear to me what point Dr Lynch thereby sought to make. I have deduced that it was in order to present the substitution of BofA to Deloitte and the Audit Committee as being at the instance and pursuant to a legal entitlement on the part of Capax Discovery, rather than as an *ad hoc* means of funnelling funds to Capax Discovery to enable it to pay Autonomy. It appears to have been of importance to Deloitte that it should so appear, and it seems that Deloitte accepted the presentation: see further below. In my judgment, the fact that such disguise was perceived necessary tells against the Defendants. The reality was that far from involving the exercise by Capax Discovery of its contractual rights, this episode involved Mr Egan honouring the assurance he had given to Mr Baiocco at the outset: namely, that in the absence of an end-user deal that made Capax Discovery whole, then Autonomy would find a different buyer of the software and slot Capax Discovery into that different deal. BofA was, in Mr Egan's language, the "*backfill*" to ensure that Capax Discovery was not left "*holding the bag*" in relation to its Amgen purchase order.

1005. The mechanism thus adopted met its objective of covering Capax Discovery's exposure and safeguarding the recognition of revenue from VT16 in its first incarnation. The broad effect was that Autonomy proceeded with its smaller sale to Amgen, repackaged the software sold under VT16 and sold it to BofA as part of the composite deal, and thereby held Capax Discovery harmless.

1006. Thus, in the event:

(1) As explained below, Autonomy ultimately concluded the larger composite deal with BofA on 9 February 2011 and designated MicroTech as the payee under that deal. On 11 February 2011, Mr Guiao then drew up the invoice for MicroTech to send BofA, as well as (among other things) a purchase order for MicroTech to submit to Capax Discovery.

(2) BofA paid $19 million to MicroTech, which then paid $9 million to Capax Discovery (the remainder going to DiscoverTech).

(3) On 4 March 2011, Mr Baiocco wrote to Mr Guiao stating:

> *"WE have received the monies into our account from the B of A deal. Can we please get all the necessary paperwork in place to close this out?*
>
> *1 Executed letter we sent requesting replacement of Amgen purchase with BOFA.*
>
> *2 relief letter for 450k you have received direct.*
>
> *3 our sales referral commission letter for 945k."*

(4) The reference to a "*450k*" was to the support and maintenance component of the original Amgen purchase order, as to which Capax Discovery was to receive "*relief*", i.e. release of indebtedness. Mr Baiocco also wanted Capax Discovery's $945K "*referral commission*" in respect of the deal even though Capax Discovery had made no referral.

(5) On 7 March 2011, Autonomy Inc issued a credit note to Capax Discovery, dated 28 February 2011, for $450,000. Mr Baiocco queried whether the credit note should refer to BofA rather than Amgen. Upon being reassured by Mr Scott, Mr Baiocco asked whether he would get a copy of the "*executed amgen BOFA swap letter back*". Mr Scott raised that issue with Mr Kanter, asking whether it was "*OK to send back to him?*" Mr Kanter's reply was, "*If Sushovan is happy with the transaction and the accounting treatment, the language of the letter is fine*". The signed swap letter was then sent to Mr Baiocco. Evidently, therefore, both Mr Kanter and Mr Hussain – as well as Mr Scott, Mr Chamberlain and Mr Egan – were kept informed of what was happening *vis-à-vis* Capax Discovery.

(6) On 15 March 2011, Mr Scott informed Mr Chamberlain and Mr Hussain that Capax Discovery had not yet paid the $9 million due on the backfilled-BofA purchase order and said "*I think that they may be holding it up because they want a MAF associated with the Amgen/BofA transaction*".

(7) On 18 March 2011, Mr Chamberlain emailed Mr Egan, Mr Hussain and Mr Scott, subject "*Capax*", to say, "*Need to resolve today. They owe $9m on BofA deal which is stalled. Joel – did MT pay Capax or do MT still hold the BofA funds?*". Mr Scott replied that MicroTech had paid Capax Discovery, and Mr Egan added that "*Capax wants to pay us*". Mr Egan then suggested that the reason for non-payment was that Mr Baiocco "*does not have clear instructions*

on whether to deduct MAF or expect separately". Mr Chamberlain replied by email which Mr Egan then forwarded to Mr Hussain:

> *"Stouffer – let's be very clear here. I have no wish other than getting my $9m, I have not agreed any MAF.*
>
> *Any MAF will only have been discussed with John by you and it will need SH to be onboard. From my perspective he owes me the $9m."*

(8) In his email dated 24 March 2011 to Mr Chamberlain, Mr Baiocco stated "*We have received the monies from the BofA deal. I will work on getting them to you.*" Mr Egan responded the same day, "*Please send us invoice for the 10% of the original invoice amount and please wire the gross BofA amount to us. We will turn around your invoice immediately*".

(9) Mr Chamberlain drew the issue to Mr Hussain's attention: "*need you to approve the $945k commission to Capax for BofA/Amgen. As I indicated earlier he is holding our $9 million payment pending resolution of this issue*". The Claimants submitted that the oddity of Capax Discovery, which had effectively been relieved of a very substantial obligation and did nothing whatever to effectuate either the Amgen or the BofA transaction, nonetheless holding out for a near $1million marketing assistance fee would be glaring, if one were not aware of the "*handshake agreement*". However, Mr Baiocco was doing nothing more than insisting that the handshake agreement be honoured; and it was.

(10) Capax Discovery then paid the $9 million – which Capax Discovery had received from MicroTech – to Autonomy in discharge of its obligations to pay licence fees of $9 million under what had originally been the Amgen purchase order. It was not left "*holding the bag*".

1007. On the Claimants' case, that was a principal[83] point of the manoeuvring. They submitted that, far from involving an exercise by Capax Discovery of its contractual rights, the episode demonstrates the extent to which Mr Egan and those concerned within Autonomy's management would go to honour the assurance that underlay all the impugned VAR sales that the VAR would not be left "holding the bag".

1008. The Defendants accepted that the wording of the *"re-purposing"* letter was *"clumsy, in the way that it described a cancellation of the original purchase, and the treatment of the letter as a fresh purchase order"*: but, they countered that the fact remained that Capax Discovery was entitled to redeploy to a different end-user under the original purchase order, and the letter should be treated as recording the implementation of that right, and not the cancellation of the purchase order itself (which was never intended).

1009. Dr Lynch explained this further in the course of his cross-examination, emphasising that nothing that was done affected the recognition of revenue at the point of sale to the VAR:

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[83] See below for the other main objective served which was to support the appearance of the software covered by the VT16 purchase order being sold by Capax Discovery to BofA, whereas in fact Autonomy sold the same software directly to BofA.

"My understanding…is that the original deal wasn't cancelled and the revenue was left in the original area.

What happens in this deal is that the American office doesn't understand this process under IFRS, and so it produces this form of letter. But actually the auditors completely understand the process that's gone on here and it's mentioned in the audit committee pack and explained to the audit committee.

The basic principle – I don't know what the technicalities are about whether you consider a PO cancelled or not, but the basic principle is the deal is not cancelled. So the deal – the transaction which was done at the time with Capax, that revenue stays in the books. What actually happens is that the software – and this was an explicit term of the deal – is actually dealt somewhere else, but there's no new revenue recognised or put in the books. So there's no actual transaction as far as Autonomy is concerned.

The transaction as far as Autonomy is concerned was with the sale to Capax originally and all that is happening is that Capax stock is being given to MicroTech/Bank of America. As I say, it's covered in quite a lot of detail, I understand in the audit committee pack from Deloitte.

Q. Capax became involved in the Bank of America deal because Mr Egan had used Bank of America as backfill to ensure Capax got paid for its Amgen purchase order?

A. I wouldn't use the word "backfill". What it is is that Capax had stock and Mr Egan introduced the Bank of America opportunity and they could sell that stock to Bank of America, which was written explicitly in their deal.

…

Q. In fact 9 million gets paid to Capax as the proceeds of the Bank of America deal and that 9 million is then used to discharge Capax's debt under the purchase order for a different customer, Amgen, correct?

A. Correct, but as Deloitte make absolutely clear, Autonomy's deal is with the reseller, the reseller is the customer. What then happens to that software, especially if there's a clause that explicitly allows it to be sold to anyone, is really not Autonomy's business."

1010. I address Deloitte's involvement later. In the meantime, it seems to me that Dr Lynch put forward a well-worked summary of the theoretical mechanics, premised on the notion that the true intention which was lost in the inaccurate drafting by the American office of the *"re-purposing"* letter was that Capax Discovery should continue, after the *"re-purposing"* as before, to be liable to Autonomy under the original Amgen purchase order, and not under the substituted BofA deal. However, the practical realities undid the theoretical analysis.

1011. As I have explained above, the reality is that Capax Discovery never had anything to do with BofA, either before or after the "repurposing". The deal was simply fed to it: Mr Baiocco simply had to sign and willingly did so once satisfied that Capax Discovery's obligations had been dealt with and it was going to receive the nearly $1 million as a MAF.

There is nothing to support Dr Lynch's apparent belief that BofA's requirements were satisfied out of stock held by Capax Discovery, and there is no evidence of delivery by Capax Discovery to BofA. As noted previously, software is easily and infinitely capable of being reproduced; and Autonomy simply had to press a button on Automater to deliver what BofA required. Dr Lynch's analysis did not address the reality or the true intention, which was that Capax Discovery should be and was released from liability because it was (albeit indirectly) relieved of it by Autonomy.

1012. In summary as to this aspect, in my judgment:

(1) The idea and impetus for the *"re-purposing"* came from Autonomy, and it was Autonomy which provided a ready-made end-user deal into which Capax Discovery was insinuated.

(2) This achieved two objectives. One was to hold Capax Discovery harmless from exposure in the Amgen deal. The other was that in its second incarnation, VT16 could be (as it was) used to present the sale on to BofA of the software described in the VT16 purchase order as a sale by Capax Discovery, whereas in truth it was a direct sale by Autonomy (see further below).

(3) The suggestion that the "re-purposing" was effected pursuant to the exercise by Capax Discovery of a right under the original purchase order was made for presentational reasons but lacked any basis in fact or law.

(4) The fact that a false presentation was perceived to be necessary, even though in the particular circumstances there was, to my mind, a more basic justification for taking steps to release Capax Discovery in respect of a purchase order (in that by its direct sale to Amgen, Autonomy had cut out Capax Discovery and destroyed the prospect of the intended end-user by reference to which Capax Discovery had issued its purchase order), is a measure of the concern of those involved within Autonomy about Deloitte's warnings that any pattern of direct deals would be likely to upset revenue recognition of VAR deals, and the determination to adopt a mechanism which did not fit and reveal that pattern.

(5) Mr Baiocco's acceptance of a solution which also appeared to secure the MAF which was the real focus of his interest is an illustration of the passive and subservient role played by Capax Discovery and the other 'friendly' VARs in all the impugned VAR transactions.

MAF

1013. As regards the MAF, on 25 March 2011, Mr Chamberlain informed Mr Hussain: "*Good news. The $9m is in. Need to get approval on the MAF now. Please advise"*. Mr Hussain replied, copying Mr Kanter, "*Approved. Per our agreement 10% on the invoiced amount after cash is received. I spoke to stouffer"*.

1014. An internal discussion then followed between Mr Hussain, Mr Chamberlain and Mr Egan as to whether the correct amount of the MAF was $900,000 (10% of the $9 million licence fee) or $945,000 (10% of the total amount originally payable under the $9.45 million Amgen purchase order, albeit that Autonomy subsequently credited Capax Discovery for the $450,000). On 29 March 2011, Mr Hussain informed Mr Chamberlain (copying Mr Egan and Mr Kanter), "*Stouffer will be sending an email for confirmation which andy and i will need to approve but it is $900k*".

1015. On 29 March 2011, Mr Egan wrote to Mr Kanter and Mr Hussain regarding "*Final MAF for Capax*", stating:

> *"I wanted to submit for approval the MAF to Capax for their involvement in the BofA deal. It is a standard 10% fee identical to the terms an [sic: as] past MAFs paid for similar channel involvement and value add for a deal in which they added considerable value.*
>
> *We received payment in full early as well."*

1016. This was, at best, formulaic. The *"channel involvement"* was a euphemism for signing a contract and awaiting release from it, with no active participation by the VAR in the end-user deal. Nevertheless, Mr Hussain gave his approval for the MAF the same day (29 March 2011), stating, "*Ok We have received the cash from capax*". Mr Chamberlain forwarded Mr Hussain's approval to Ms Harris, noting "*Need approval from Andy*". Mr Kanter must have given approval because, on 1 April 2011, ASL paid the $900,000 fee.

1017. Some months later, on 14 July 2011, Alex Jackson of Deloitte asked Mr Chamberlain about the invoice for the $900,000 fee: "*Do you have a bit more info on this, exactly what Capax did/will do in respect of marketing etc ... and where this is living on the balance sheet/P&L*". Mr Chamberlain's response was, "*Believe this is included in marketing fees. Relates to their assistance on managing the BofA relationship*". This was untrue. Capax Discovery had done nothing to manage Autonomy's BofA relationship.

1018. The Audit Committee was informed simply that *"VARs from time to time provide goods and services to Autonomy in areas such as marketing assistance…During the quarter Autonomy has paid Capax….$0.9 million for marketing assistance services in managing the Bank of America relationship…".* Mr Bloomer told me that he would have assumed that Capax Discovery did provide some form of services and was being paid this fee in accordance with the master agreement between Capax Discovery and Autonomy. The assumption was natural; but false.

1019. Although he maintained that he was not asked to approve these payments, and would not have known about them, Dr Lynch nevertheless rejected any suggestion that the MAF payments were improper:

> *"Q. I suggest you knew it was improper to pay Capax a fee here which was being paid to enable Autonomy to recognise revenue prematurely.*
>
> *A. No. And the other thing that we mustn't lose sight of in all of this is these are real deals. So this software is sold, it's sold through a reseller. Ultimately it ends up with an end-user who install it and thousands and thousands of people across the world use it, and we get paid against the revenue. And so there's absolutely nothing improper here. The fact that the structure of these deals is that the onsale is done at the same price as the purchase means that the MAF model is used to give the reseller in effect the margin that keeps them part of the ecosystem and gives them a reason to do business with Autonomy. Every software company I know in the world runs that model just as they run the mark-up model as well."*

1020. This defence of MAFs in general was stated with apparent conviction; but it focused on general practice in contexts where VARs were actually performing a service, not on the particular case, where they had performed none. It did not explain why it was thought necessary to pretend that Capax Discovery had played a part in the BofA deal which it had not played, added *"considerable value"* when it added none, provided marketing services which it had not provided, secured a deal which it had done nothing at all to negotiate or secure, and arranged payment to Autonomy *"early"* which had nothing to do with it.

1021. Mr Egan's justification for paying a MAF on the basis that Capax Discovery had *"added considerable value"* was plainly contrived. As Mr Kanter and Mr Hussain would have known, Capax Discovery had not been involved in the BofA deal. It had added no value, let alone "*considerable value*", to the BofA deal. The fact that Autonomy received payment "*early*" had nothing to do with Capax Discovery: the timing of payment was the result of Autonomy's direct deal with BofA, which (via MicroTech) put Capax Discovery in funds to pay Autonomy.

1022. Dr Lynch sought to sweep this aside, much as he had swept aside a similar pretence in the context of VT10 (Capax Discovery/FSA) as having *"made too much of the language of the emails"*, but he offered no answers and ultimately relied on his assertion that he was not personally involved anyway. I would tend to accept that 'gilding the lily' in justifying large commission payments is a commonplace of commercial life, but in the context, and all the circumstances here, it is a further illustration of a disturbing culture within the management of Autonomy and an unsettling and unsatisfactory approach to disclosure on the part of Dr Lynch himself.

Backdating?

1023. I have considered whether the backdating of the *"re-purposing"* letter may be another illustration of this culture. The Defendants did not seek to contradict the fact that the *"re-purposing"* letter stated on its face an incorrect date (31 December 2010); and it is not disputed that the letter was not drafted until 18 January 2011.

1024. The Claimants submitted that the backdating was intentional, and in a somewhat obscure passage of their closing submissions, appeared to suggest that when asking Mr Baiocco to sign and return the letter on 25 January 2011 Mr Egan's covering email, in stating *"Please sign, as is, and importantly scan vs fax (i'm on plane) and email return",* sought to disguise the fact, suggesting that the *"problem with a fax, of course, is that it would immediately have revealed the fact that the letter was backdated."*

1025. The Defendants did not accept the suggestion that this was dishonest backdating (as distinct from an error). They pointed out (*inter alia*) that (a) the letter was drafted by Mr Guiao, an Autonomy lawyer in the US and when Mr Guiao sent the draft to Mr Egan it already bore the date of 31 December 2010, (b) the reason why Mr Egan asked Mr Baiocco to scan rather than fax the signed version was the reason stated in Mr Egan's email: he was on a plane (and presumably could not receive a fax), and (c) the dating of the letter was irrelevant to revenue recognition: the revenue in respect of this sale had already been recognised on the Q3 2010 sale to Amgen and was not going to be recognised again. Further, backdating would have implicated both Mr Guiao (a lawyer against whom no suggestion of impropriety was made) and Mr Baiocco: and Mr Baiocco was clear in his testimony that he never thought he was engaged in anything fraudulent (or criminal). Further, no reason for backdating was suggested.

1026. I am not satisfied that there is sufficient evidence of intentional backdating of the *"re-purposing letter"*. That is so even though it is also a relevant consideration that in other contexts (and in particular, the Vatican Library deal and the Prisa deal) I have concluded that management did backdate documents dishonestly, Mr Egan admitting to remorse and anxiety in that regard.

Deloitte's understanding of the transaction

1027. As is apparent also from his evidence as quoted in paragraph 1009 above, Dr Lynch placed some considerable reliance on the fact that Deloitte were well aware of the salient features both of the original VAR sale and its *"re-purposing"* and were content that it did not affect revenue recognition at the point of the original sale to the VAR for the purposes (then) of the anticipated Amgen deal.

1028. The Defendants' case in more detail was that:

(1) Deloitte reviewed the original sale to Capax Discovery for end-user Amgen, took notice of the clause permitting a change of end-user, and were satisfied with the revenue recognition, treating Capax Discovery as the customer.[84]

(2) They were aware of the switch to enable Capax Discovery to sell to BofA instead of Amgen, as apparent from Deloitte's Q1 2011 report to the Audit Committee:

> *"We note that a licence previously sold to Capax Global in Q3 2010 for onsale to Amgen ($9.5 million), has been re-assigned in the quarter to enable a sale by Capax Global to Bank of America, as part of the large Q4 2010 revenue deal previously reported to the Audit Committee. No revenue has been recognised on the re-assignment of this licence and the outstanding receivable has been received during the quarter."*

(3) Deloitte were given a breakdown so that they understood how the Amgen-BofA repurposing fitted in with the other amounts in the large BofA deal, in which Capax Discovery was not the only reseller involved.

(4) As explained at greater length below, Deloitte also specifically understood and represented in the Q4 2010 Audit Committee report, (a) that the BofA deal was going through MicroTech as the lead reseller which would be the direct seller to BofA, (b) that as of Q4 2010 there was not yet a BofA purchase order, and (c) that the same software that would ultimately be purchased by BofA had been sold to both Capax Discovery and DiscoverTech.

(5) Deloitte were also aware of payment of the MAF to Capax Discovery, following the repurposing of VT16. Deloitte understood the commercial

[84]It should be noted that the Claimants appeared to be advancing a separate complaint that the software in the Q3 2010 Amgen transaction was the same as in an earlier Q2 2010 Amgen transaction. This was the subject of an assumption that Mr Welham was asked to make. This proposition was factually incorrect. The correct position was explored with Mr Welham. He accepted that the assumption was wrong and that the conclusion that he had reached on the basis of the false assumption needed to be revised. This point was not taken up with Dr Lynch in his cross-examination.

position, and the revenue remained as recognised under the Q3 2010 agreement. Deloitte were satisfied that the revenue was properly booked.

1029. In short, the Defendants sought to stress that Deloitte knew all the material features of the transaction: and (they added) more than Dr Lynch could ever have known. Yet, contrary to the Claimants' case, Deloitte had no problem with the transaction, or the recognition of revenue. On the Defendants' case, if Deloitte were the Defendants' conscience, it would be clear.

1030. The approval of Deloitte, if given on a properly informed basis, is obviously, in this context as in all other contexts calling for accountancy assessment and judgment, a powerful point in the Defendants' favour.

1031. However, the Claimants sought to turn the point against the Defendants by demonstrating critical areas in which Deloitte (and the Audit Committee) were misinformed or misled, arguing that the impropriety (as they saw it) of the transactions was easily illustrated by what was kept back or misrepresented, and at the same time undermined reliance on Deloitte's approval. I have concluded that there is force in the Claimants' point both in theory and in application.

1032. As to sub-paragraph (1) of paragraph 1028 above and the initial VAR sale (VT16 itself), I have already referred in paragraphs 981 to 989 above to the way that the Audit Committee were misled by Deloitte's report to the Audit Committee for Q3 2010, and in that context inferred that the report was based on misleading information provided to Deloitte by Autonomy. In my judgment, that is sufficient to undermine the Defendants' position that they did, and were entitled to, rely on Deloitte's approval of the transaction.

1033. In the particular context of the *"re-purposing"* or reincarnation of VT16, the Claimants contended that both Deloitte and the Audit Committee were materially misled. Although told of the money flows for the omnibus or composite BofA deal, the Claimants contended that neither Deloitte nor the Audit Committee were told that all of the VAR deals, including the Amgen deal, had been replaced by direct deals between Autonomy and BofA without any participation on the part of the VARs (except, in the case of Capax Discovery, signature on a pre-prepared letter). They drew my attention to Mr Hussain's memorandum to the Audit Committee for Q1 2011 (copied to Dr Lynch) which made no mention of the direct deal that had been concluded during that quarter. It simply stated:

> *"In q4 the Bank of America deal ($21m) went through two 8A partners and £$19.3m cash has been received."*

1034. Mr Welham's evidence was that Deloitte did not appreciate that VT16 (and also the other component parts of the overall BofA deal, VT21, VT23 and VT24) *"had been replaced by a direct deal between Autonomy and BofA"*.[85] Mr Hussain's email as quoted above certainly did not reveal that.

[85] In Deloitte's Defence in the FRC proceedings, Deloitte's understanding was stated to be that *"DiscoverTech and Capax were to sell these licences to Microtech, which would sell them to Bank of America. In this way, Bank of America would be able to contract with a s8A accredited business (MicroTech). In addition, in Q1 2011, Capax sold to Bank of America the $9m licence it had acquired from Autonomy on 30 September 2010 (at*

1035. The picture is less clear in respect of the overall BofA deal. An email dated 15 April 2011 from Mr Chamberlain to Mr Welham had attached a copy of the direct agreement between Autonomy and BofA of 8 February 2011, which Mr Chamberlain had provided in response to a request from Mr Welham asking for *"the final agreement for the Bank of America deal…"* to assist in his efforts to *"work back to cash receipts, what we recorded in Q4 as revs and taking account of the old Amgen deal with Capax"*. Further, in the same email thread, Mr Chamberlain set out the amounts to be paid to the VARs concerned in respect of the BofA deal (including $9m to Capax Discovery).

1036. The Defendants contended, and Mr Miles put to Mr Welham in cross-examination, that having been provided with the BofA agreement, and the relevant numbers, Mr Welham had the information disclosing the fact of a direct deal, even if he had not appreciated its full import at the time. The Defendants took from all this that Mr Chamberlain and Autonomy would legitimately have considered they had properly disclosed the arrangements and were entitled to rely on Deloitte's approval: it was not their fault if Deloitte misunderstood the position.

1037. Mr Welham agreed that he had been provided with this, but nevertheless maintained that the information did not, to his mind at the time or now, disclose a direct deal in its true sense. By this I took him to mean that it did not disclose that in reality the VARs were entirely by-passed by Autonomy, and received payment to make good the deal they had lost, rather than for a contract by them for onward sale. Mr Welham acknowledged that the agreement between Autonomy and BofA included a *"designated payee"* provision, which provided an explanation of the payments to the VARs (as he also acknowledged); but at the time he had taken the payments to connote that the VARs were actually involved in negotiating and concluding the sales and would supply the software to Bank of America via MicroTech, so as to distinguish the position from true direct deals (an example of which, he suggested, was the Capax Discovery/Kraft deal).

1038. A further factor to be taken into account is the evidence of Mr Bloomer as to the Audit Committee's understanding. He too assumed that it was the VARs who would supply the software and that their deals with Autonomy remained in place.[86] He did not understand that Autonomy was negotiating and contracting directly with BofA to the exclusion of the VARs. He made the further point that in any event a direct sale did not:

> *"rule out the revenue recognition at the original point as long as you meet the relevant accounting tests at that point and have the right to the goods passed, its collectability and so on…"*

1039. That is a useful reminder, as it seems to me, that the ultimate question is whether risk and control passed under the original sale by Autonomy to the VAR: a subsequent direct sale

that time, for onward sale to Amgen). No additional revenue was of course recognised by Autonomy in respect of Capax's sale to Bank of America. An agreement was signed between Autonomy and Bank of America on 8 February 2011, which contained a provision that enabled Bank of America to submit a purchase order to Microtech, as intended. In due course, Autonomy received the due payment from the relevant VARs (Capax and DiscoverTech)."

[86] Unlike the usual position, it seems likely that because of the need for an 8A supplier (which was the reason for MicroTech's introduction as *"the lead reseller who has the overall contract with Bank of America")* Deloitte thought that MicroTech would actually be supplying the software as an approved 8A supplier to BofA. (There is no doubt that BofA accepted MicroTech as an 8A supplier.)

does not alter revenue recognition unless the fact and circumstances of it demonstrate that the original sale had no substance and/or that the sale to the VAR did not result in any substantive change in the way Autonomy conducted itself with respect to the software it had 'sold'. Looked at in that way, it seems to me that what Mr Welham and Deloitte really meant was that they did not understand the agreement between Autonomy and BofA to signify that the original sales to the VARs were a dead letter, because they continued to assume that the VARs would be the suppliers of the software to BofA (under what was, in effect, an umbrella agreement reached by Autonomy).

1040. In my judgment, the question is not whether Deloitte and the Audit Committee should have understood from the material with which they were provided that Autonomy had dealt with BofA as if its original sales to the VARs could be ignored. It is whether they understood that, contrary to what would be the natural assumptions, (a) Autonomy, in making the various agreements, never had any intention that the VARs should have any say in dealings thereafter with the software licences apparently sold to them; (b) that in reality, the onward sale to the end-user of the software nominally sold to the VARs was exclusively negotiated and contracted by Autonomy with full effective control, and not the VARs, and (c) that the VARs received not the proceeds of onward sale, but compensation from Autonomy in lieu of it; in other words, that software was parked with VARs and dealt with and disposed of by Autonomy.

1041. In my judgment, Deloitte and the Audit Committee were likely to and did make the assumption that the VARs were in control of the sale process and were in a real sense the sellers and suppliers of the licences required first by Amgen and then by BofA in its place, and were misled accordingly.

VT21: Capax Discovery/Merrill Lynch: Q4 2010

1042. VT21 was, notionally at least, a VAR transaction with Capax Discovery for end-user Merrill Lynch, an affiliated company of BofA, for a licence fee of $1,830,600 (which included a two-year support and maintenance fee). It too was a constituent part of the big overall BofA deal: that was the real deal. The purchase order was, as usual, issued under the June 2009 Capax Discovery VAR Agreement, summarised in paragraph 60 above.

1043. The Claimants' criticisms of VT21 and their contention that it lacked any real substance focused principally on the following:

(1) The extreme haste of the transaction, showing that Capax Discovery had no input into, or time to measure the risk of, the transaction before signing, and was simply given a purchase order prepared by Autonomy to sign;

(2) The fact that Capax Discovery was not intended or expected to, and did not, have any involvement at the time, or make any contribution thereafter;

(3) The fact that Capax Discovery did not meet any of the instalment dates for payment, was never pressed to pay on the relevant dates, and in the end, made no payment to Autonomy at all, before ultimately being released from its payment obligation altogether;

(4) The fact that the software apparently sold to Capax Discovery for onward sale was always intended to be sold directly by Autonomy to BofA when the BofA sale which had been broken into smaller pieces was reconstituted;

(5) The fact that Capax Discovery's liability under the original Merrill Lynch purchase order was released, and that such release was effected as part of what the Claimants depicted as a concerted *"clean-up exercise"* that occurred after the HP acquisition was announced and whilst *"crucially"* (they said) Autonomy remained in control of its finance function in Q3 2011 (which during HP's later investigations became known, and which the Claimants labelled, as the *"Dark Period"*)[87];

(6) The payment of a MAF of $183,060 for "assistance" which Capax Discovery had never in fact provided, and which the Claimants submitted could only have been for Capax Discovery's willingness to act as a placeholder so as to enable Autonomy, wrongfully, to recognise revenue on what, in this instance, was a revenue acceleration transaction.

1044. As to (1) in the preceding paragraph, VT21 was one of the two transactions (the other being VT20, as described above) which Mr Baiocco said he found *"particularly memorable"* (see paragraph 843 above) because he first learned of a potential BofA/Merrill Lynch transaction on the afternoon on New Year's Eve when staying at a hotel in Pittsburgh to watch a professional hockey game. He recalled that he had signed purchase orders prepared by Autonomy for each of the two transactions shortly before midnight that very last day of the quarter (Q4 2010), New Year's Eve. As regards VT21, there can have been no time for Capax Discovery to assess the prospective end-user sale, what the software comprised (which was Zantaz Supervisor S6) and what opportunities for servicing it might offer, or whether, and if so how, it could assist or add any value at all as a VAR. The Claimants submitted that this, together with Autonomy's own frantic resort to Capax Discovery, demonstrated clearly the pattern they asserted, and the true character of the entire transaction as a 'placeholder' arrangement involving no real sale, no substantive transfer of risk, and the substantive retention by Autonomy of the managerial control of the goods sold.

1045. As to (3) in paragraph 1043 above, Mr Baiocco's evidence, which was not challenged, was that though Autonomy did invoice Capax Discovery, Capax Discovery did not pay any of the fees stated in the Merrill Lynch purchase order on the instalment dates, or at all. The Claimants submitted that this further demonstrated the lack of substance and the real attributes of a substantive sale.

1046. As to (4) in paragraph 1043 above, I have already explained that, with the *"repurposed"* VT16, and also VT23 and VT24 (which I describe later), the quartet of VAR deals and the superimposition of MicroTech, were all pre-packaged *"smaller pieces"* of the overall BofA deal (see paragraphs 965 to 974 above). In each case, the software notionally sold was parked with the VAR awaiting onward sale to BofA by Autonomy under a direct deal. That left each VAR with no autonomy, no control, and nothing to do.

1047. As to (5) in paragraph 1043 above, the Claimants contended that it was not until 26 August 2011 that Mr Chamberlain informed Ms Ku that "*we need to credit the below invoices as we have now invoiced directly*" and referred to the two invoices issued under the Capax Discovery/Merrill Lynch purchase order. The same day, Autonomy issued two credit notes for $915,300 each to Capax Discovery, thereby cancelling the entirety of the amount stated

[87] Mr Baiocco's unchallenged evidence was that in the period from August to September 2011Autonomy issued credit notes to Capax Discovery totalling $21.6 million.

to be due under the Merrill Lynch purchase order. Mr Scott sent copies of the credit memos to Mr Baiocco that day. The Claimants depicted all this as plainly improper, done to "clean up" Autonomy's accounts in the period of time following the announcement of the HP acquisition on 18 August 2011 during which Autonomy retained control of its accounting function and was safe from scrutiny because it was not subject to quarterly review in Q3 2011 either by Deloitte or by the Audit Committee.

1048. The Defendants sought to meet these criticisms of VT21 on the same grounds as in other impugned VAR transactions and rejected as irrelevant and misplaced the dark interpretation of its aftermath urged by the Claimants. They contended that:

(1) The introduction of a VAR at a late stage when an end-user sale stalled at a late stage was not objectionable, provided the VAR went on risk and that risk was not qualified or negated by side agreement or understanding. The Defendants' position in this, as in every one of the impugned VAR transactions, was that the VAR (in this case, Capax Discovery) was indeed on risk: the VAR agreement unequivocally stated so, and Mr Baiocco accepted that Capax Discovery was on risk and signed audit confirmations which he provided to Deloitte on 15 January, 6 April and 12 July 2011 expressly confirming Capax Discovery's liability, that the invoices were proper and due, and that there were no *"side letters or other agreements"*.

(2) Mr Baiocco also confirmed in cross-examination a statement in the Goldberg Segalla letter (see paragraphs 2020 to 2029 in the main body of the judgment) making clear that he regarded the risk as attenuated by the consideration that Autonomy would not want Capax Discovery to go to the wall because Capax was a *"major service and support provider to Autonomy's clients."*

(3) Non-payment did not signify or evidence a side agreement or understanding: simply commercial forbearance on the part of Autonomy. In any event, such post-transaction events did not alter the quality of the VAR transaction or undermine the decision made at the time to recognise revenue, which furthermore, Deloitte approved.

(4) The credit notes issued in August 2011 were justified: they reflected the reality that the Zantaz S6 software purchased by Capax Discovery under the purchase order for resale to Merrill Lynch/BofA had in the event been sold by Autonomy to BofA directly under the arrangements described above and which had been reviewed and approved by Deloitte. The Defendants clarified that it had originally been contemplated that BofA would pay for that software immediately and that its payment would flow through to Capax Discovery via MicroTech. In the event, however, BofA were not willing to pay immediately since they regarded the S6 software as an extension to a licence, which should not be invoiced until a later date. BofA was then not invoiced until August 2011, whereupon soon after the decision was taken to issue the credit notes, resulting in a commercial outcome substantially the same as in the Kraft deal, and equally unobjectionable. Any subterfuge was denied.

(5) The Defendants repeated their general line that no adverse inference that the payment was a reward for enabling improper revenue recognition should be drawn from the payment of a MAF. Such payments were common in the software industry, and something HP itself employed; and Deloitte were aware

that Autonomy paid MAFs where the deal went direct and the reseller was being compensated for loss of margin.

1049. Once again, the fundamental problem with the Defendants' contentions is that they brush over the particular characteristics in this and (to a greater or lesser extent) all the impugned VAR sales which mark them out: the Defendants did not face up to the 'pattern' identified by the Claimants and, in particular, the inconsistency of this pattern with there being any real substance in the VAR sale or any substantive transfer of risk and management control of the licensed software.

1050. Looked at in the round, VT21, like VT16 and the other constituent packages brought together in the BofA transaction, provided a striking example of the use of a VAR without any intention or expectation of any involvement in the negotiation or contract for the onward sale, which was already pre-packaged, controlled and intended to be implemented as a direct deal by Autonomy with the end-user, with the VAR sale having no substance or economic effect save as a trigger for revenue recognition and as the origin of a counter-obligation in effect imposed on Autonomy to hold harmless the VAR in the event of some failure of the pre-packaged deal.

1051. The Defendants' contentions miss their mark because they are based on a premise of (i) a risk which was in substance illusory and (ii) intended and actual involvement by the VAR in the control of the licenced software for the purpose of an onward sale which is belied by the facts.

1052. Further, VT21 provides another example to negate the suggestion in the Goldberg Segalla letter that the prospect of future servicing business was a factor of benefit to Capax Discovery which might have justified the enormous risk: in only two deals (the TXU and FSA deals) did Capax Discovery's involvement lead to any servicing work.

1053. More generally, in my judgment, the Defendants were never able satisfactorily to answer the two fundamental points, which infected every aspect of Autonomy's business with its 'friendly' VARs, that (a) the risk assumed by the VAR (in this case, Capax Discovery, on New Year's Eve) without any assessment of the prospects of an end-user sale and no previous relationship with that end-user was entirely disproportionate unless an assurance which Mr Baiocco considered reliable had been given that Autonomy would always find a means of holding Capax Discovery harmless against it; and (b) at no stage did Capax Discovery ever do anything consistent with it having more than nominal ownership: it never had or asserted any control over any onward sell; and it ceded to Autonomy the exclusive right to negotiate and conclude a deal with the end-user, not as agent for Capax Discovery or otherwise on its behalf, but as principal, and it was never involved actively in that context from the moment of the purchase order until the moment of completion of whatever stratagem the Claimants had adopted to ensure that it was not left on the hook. VT21 was a particularly clear illustration of a VAR acting as placeholder: the real deal was the direct deal between Autonomy and BofA when the constituent elements parcelled out to the VARs were brought together.

VT23 and VT24: DiscoverTech/Bank of America Q4 2010

1054. As explained above, the other "smaller pieces" into which the BofA deal was temporarily parcelled up were VT23 and VT24, which were VAR transactions with DiscoverTech (for end-user BofA), both in December 2010.

1055. Both VT23 and VT24 were, though "smaller pieces" of an even larger overall deal, relatively large deals. VT23 was for a licence fee of $3,675,000 (including support for the first year); and VT24 was for a licence fee of $7,000,000, plus a first-year support fee of $350,000. Although numbered in that way, in fact VT24 preceded VT23, as will be seen.

1056. In addition to the complex arrangements whereby all the "smaller pieces" were brought together in, or perhaps more accurately, unravelled and replaced by the large direct deal, the following claims by the Claimants in seeking to impugn these VAR transactions require analysis in relation to VT23 and VT24:

(1) That the VT23 purchase order was backdated by nearly one month in order to capture recognised revenue for the Q4 2010 account;

(2) That DiscoverTech did not have the ability to pay the purchase price for these large VAR deals if it could not resell the software, and it made no sense for DiscoverTech to have taken such a risk if Autonomy genuinely intended to require DiscoverTech to pay (which the Claimants maintain it never did intend);

(3) That the DiscoverTech purchase orders for VT23 and VT24 contained misleading language which gave a false impression of DiscoverTech's role in order to justify both its involvement and the substantial payments to it;

(4) That Autonomy then failed to disclose the direct deal to the Audit Committee and Deloitte and instead misled them into believing that the VARs had achieved their own onward sale to BofA;

(5) That Autonomy contrived arrangements for the sums payable by BofA under the direct deal to be routed and used to fund payments to Autonomy by the VARs in respect of their obligations under VT23 and VT24 (as well as VT16 and VT21) so that (according to the Claimants) *"Autonomy's own money was used to pay off debts ostensibly owed to Autonomy by DiscoverTech (and Capax Discovery)"*;

(6) That Autonomy made a payment, purportedly as a MAF, which was improper because DiscoverTech never provided any marketing assistance of any kind.

1057. The allegation of backdating (see paragraph 1056(1) above) concerned the VT23 purchase order, which the Claimants alleged was in fact issued on 25 January 2011 and then dishonestly backdated to show a date of 31 December 2010.

1058. It was not disputed that the VT23 purchase order for an additional $3.5 million (plus maintenance and support of $175,000) was not issued until 25 January 2011, and that until the last moment it was not clear whether the order should come from DiscoverTech or MicroTech. Thus:

(1) According to Mr Egan's witness statement, on 25 January 2011, Mr Egan asked Mr David Truitt (at Mr Hussain's request) whether DiscoverTech would *"take an additional $3.5 million licence…"* (additional, in other words, to the $7 million covered by VT24).

(2) An email from Mr Egan to Mr Hussain and Mr Scott on 24 September 2011 was in terms that suggested that right up to that moment it had not been decided whether to use MicroTech or DiscoverTech for this:

> *"I'll get the signatures. Don't you want the $3.6m from micro tech? Or do you want it through DT as well?"*

(3) By e-mail dated 25 January 2011 Mr Livius Guiao (an Autonomy lawyer) sent Mr Egan *"an additional one-time reseller agreement to be signed by DiscoverTech"* which Mr Egan sent on to Mr David Truitt under cover of a message which stated that:

> *"It will be important that it be signed as is with no additions or modifications late today and scanned and emailed back. This covers the excess amount of the order…"*

(4) Mr Egan's message appears not to have got through because Mr Hyson, DiscoverTech's CTO, sent back a signed version on which he had dated his signature *"25 Jan 2011"*.

(5) Autonomy reacted to this by supplying DiscoverTech with a fresh draft which had the date of 31 December 2010 physically typed into the signature line, which Mr Hyson then signed and returned.

1059. Dr Lynch stated that he was not at all involved in this episode. Mr Hussain gave no evidence; but he was directly and closely involved, as is apparent from the fact that he was a recipient of Mr Egan's email on 24 January 2011 (see paragraph 1058(2) above) and an email which he sent to Mr Egan, copied to Mr Scott, on 26 January 2011 in which he berated them for delay:

> *"Thought I had made it clear multiple times that I had asked for the amendment and the revenue confirm last night. Nothing received."*

1060. Mr Hussain relied on evidence given in the US criminal proceedings as follows:

(1) Mr Egan gave evidence there to the effect that he thought what was done was unexceptional and *"perfectly legal"* because he believed (and believed that Mr Hussain believed) that it involved in reality only an amendment to an existing purchase order which he considered to be common-place and unexceptionable, and the replacement of the document showing a later date was necessary *"just so there wouldn't be conflicting dates"*.

(2) Mr David Truitt gave evidence that he *"honestly wasn't"* concerned by this because *"it was simply adding to the original deal"*; but it is of some note that Mr David Truitt then continued far more equivocally, suggesting that it did not occur to him that *"this could be a – you know, we're trying to squeeze it in the later quarter scenario"*.

(3) Mr Scott, who was also directly (and he sought to convey, uncomfortably) involved, also gave evidence that he had had concerns, but had been to some extent (but, he made clear, not wholly) reassured by Mr Hussain's assurances that he would be entirely transparent with Deloitte and abide by their view whether the amount in the VT23 purchase order could be allocated as revenue to Q4 2010 or would have to be postponed to Q1 2011.

(4) Mr Welham's uncontradicted evidence, however, was that this was not something of which he was even aware or had any inkling at the time. Nor was the Audit Committee told anything about it.

1061. In my judgment, the VT23 purchase order plainly was backdated, and those concerned (including Mr Hussain, Mr Chamberlain, Mr Egan, Mr David Truitt and Mr Scott) were aware that it was so. No persuasive justification for what was done was ever put forward. There is no evidence that the VT23 purchase order was intended to correct an error in the VT24 purchase order and/or agreement (which perhaps might have justified what was done). Mr Egan and Mr David Truitt appear to have to some extent persuaded themselves that all that was being done was an expansion of an earlier order and that such a thing was commonplace: but whilst that may be permissible if the amendment is within the same accounting period, I am by no means persuaded that it could be permissible where the amendment is in a subsequent accounting period. Mr Scott was to some extent comforted by the promise of full disclosure to Deloitte: but he had serious misgivings. In the event, Mr Hussain entirely neglected and failed to make good his promise of disclosure to Deloitte.

1062. I cannot accept Mr Hussain's position in his closing submissions that *"there is no indication that Mr Hussain asked anyone to do anything that should be regarded as wrong."* It plainly was wrong: which is no doubt why Mr Hussain did not disclose it to Deloitte or the Audit Committee. In my judgment, Mr Hussain was, by this late stage, so driven by his obsession with meeting revenue forecasts, that he was prone and indeed eager to persuade himself of any justification that seemed arguable, and on this occasion that all that was being done was a correction or amendment to a previous order, which was simply not the case.

1063. I accept that there is no separate or transaction-specific evidence that Dr Lynch was personally involved. When cross-examined on the point, he denied firmly that he was involved. He told me he thought now that Mr Hussain believed it was *"a correction and an amendment to a purchase order for a different quarter"*. But this was speculation uninformed by the evidence. In these circumstances, the Claimants could not do more than to rely on the evidence of Mr Hussain's pattern of consistently reporting to Dr Lynch on revenue targets and how they were to be accomplished, and to invite me to infer from that and from the evidence of Dr Lynch's insistence on overall control that *"Mr Hussain would not have taken this extreme step without authorisation from Dr Lynch"*.

1064. The BofA deal of which this was a constituent but individually large element was of prime importance in the quarter; and the BofA deal was a subject of regular report (as noted above). Especially in light of the size and importance of the BofA deal, the amount involved in the backdated transaction itself ($3,675,000) and the evidence that Mr Hussain kept Dr Lynch continuously updated about it, I consider that the inference the Claimants invite me to draw is justified. I accept that it is considerably more likely than not that Mr Hussain explained the position (and the prescription) to Dr Lynch. Further, if Mr Hussain had truly thought that the additional purchase was a correction to regularise an initial error he would have wished to report its successful resolution to Dr Lynch; if he knew that it was simply a ploy to boost recognised revenue for Q4 2010 which had succeeded he would have wished to share the coup with Dr Lynch. In any event, it was not in Mr Hussain's character as it appears from the evidence available to keep such things from Dr Lynch. I cannot accept Dr Lynch's denial.

1065. The second point relating to VT23 and VT24 is that Mr David Truitt testified in the US criminal proceedings that, at least without recapitalising the company, DiscoverTech did not have the ability to pay some $7 million if it was unable to resell the software. In other words, it was taking an existential risk. The Claimants contended, and put to Dr Lynch in cross-examination, that it cannot reasonably be supposed that it would have taken the risk if it had not been assured that it would never be called upon to pay.

1066. Dr Lynch refused to accept this. In rejecting it, he explained why a reseller could well conclude that this was a good risk to buy into. This included that the VAR would know that BofA's regulatory archive was running on Autonomy software, that this would lead to the prospective benefit of repeat purchases (and, he might have added, service opportunities) from a huge bank and could be

> *"actually pretty certain that there would be a purchase from Bank of America [in the] not too distant future…It's actually a pretty good bet for a VAR, this one."*.

1067. This answer, delivered with Dr Lynch's usual appearance of calm assurance and initial plausibility, is, in my judgment, falsified by the artificiality of the whole arrangement:

> (1) DiscoverTech had no previous dealings with BofA, and it was not intended that it should deal with BofA in any way, certainly prior to the conclusion of the prospective BofA deal (and see further as to this below).
>
> (2) The deal in prospect was not one to which DiscoverTech would be a party: it was always intended to be, and in the event resulted in, a direct deal between Autonomy and BofA.
>
> (3) The VAR's purchase did nothing to assist it establish or deepen a relationship with BofA which would lead to any further purchases or work: the $10.65 million or more bought it nothing which it could not legitimately hope to benefit from without any such payment.

1068. The notion that the newly incorporated DiscoverTech, or any of the 'friendly' VARs, would have incurred a potentially existential risk in such circumstances without assurances that the risk would be covered by Autonomy, is very difficult to accept, and I do not accept it.

1069. In reaching that conclusion in this as in other contexts concerning impugned VAR transactions, I have taken careful account of the arguments always advanced on behalf of the Defendants that it was plausible for the VARs to subscribe the risk simply relying on Autonomy having proved itself reliable in the past, and on the commercial calculation that Autonomy would never wish or perceive it to be in its interests to *"burn a partner and leave them in the dust",* as Mr Egan had put it. But I have concluded that this was not the basis on which the VARs proceeded. In my judgment, the understandings between Autonomy and its VARs in these and other impugned VAR transactions went well beyond an expectation on the part of the VAR of loyalty and self-interest on the part of Autonomy. The patterns revealed the real deal: the VAR would co-operate by doing nothing, Autonomy would retain entire control, rescue the VAR if it became necessary, and would never demand payment out of the VAR's own resources.

1070. As to (3) in paragraph 1056 above, the DiscoverTech purchase orders ended with the following language (which had also newly been introduced into Capax Discovery purchase orders prepared by Autonomy in and after December 2010):

> *"Although End-User and VAR currently anticipate entering into such a license transaction, in the unlikely event End-User, instead, enters into a direct agreement with Autonomy or its affiliate to license the Software, then VAR shall distribute the Software to End-User upon receipt of written notice (which may be via email) from Autonomy ("Distribution Notice") of such direct license transaction. In the event distribution is accomplished by reason of a Distribution Notice, upon such time as Autonomy has received payment in full for such license fee and support fee, Autonomy shall pay to VAR an amounts [sic] equal to the license fee paid by End-User to Autonomy less the license fee described in Item 2 above, but in no event more than $816,000.00, as full compensation in connection with VAR's efforts in securing End-User's procurement of a license of Autonomy software."*

1071. This language was misleading. DiscoverTech did not "*currently anticipate*" entering into a licence transaction with BofA nor was the possibility of a *"direct agreement"* with Autonomy *"an unlikely event"*; Autonomy was the entity negotiating with BofA, and which was to continue negotiating with BofA, without any involvement by DiscoverTech, and with the objective, not of an end-user deal, but of a direct deal, as in due course eventuated. The provision for Autonomy to cover DiscoverTech's costs, together with an uplift, was the essence of the deal: there was never any intention or realistic prospect of DiscoverTech itself generating revenue from an onward sale (since there was never to be one).

1072. This language (also adopted in Capax Discovery purchase orders) was also the first time that a purchase order made any reference to the possibility of Autonomy rewarding the VAR for its involvement. However, it will be noted that what Autonomy was to pay DiscoverTech was the difference (if any) between the end-user's licence fee and DiscoverTech's licence fee, subject to a cap (here $816,000); this was not an agreement that Autonomy should pay $816,000, nor was it an agreement to pay 10% of the end-user licence fee. Furthermore, the purchase order stated that any such amount was to be paid as compensation "*in connection with VAR's efforts*" to secure an end-user sale. In reality, neither Autonomy nor DiscoverTech intended that DiscoverTech should make any such efforts.

1073. In addition to the pretence in the wording of the purchase orders, I have already explained in the context of the *"repurposing"* of VT16, that:

    (1) Mr Hussain's memorandum to the Audit Committee for Q1 2011 (a copy of which was sent to Dr Lynch) made no mention of the direct deal that had been concluded during that quarter. Instead, it stated, "*In q4 the Bank of America deal ($21m) went through two 8A partners and $19.3m cash has been received*".

    (2) Mr Welham did not appreciate that the VAR deals had been replaced by a direct deal between Autonomy and BofA. Although it is clear from their working papers that Deloitte were told of the overall structure, including the use of MicroTech and *"other regularly used VARs"* as *"middle men"* in the overall

deal, it is also clear that the understanding that Deloitte were given and had was that the VARs would be expected to be parties to end-users sales.

(3) The Audit Committee was misled into believing that the VARs had achieved their own onward sale to BofA. Mr Bloomer's evidence was as follows:

> *"Q. So you would have understood that to mean that the 19.3 million cash had been received from the two resellers with whom the deal had been done in Q4, yes?*
>
> *A. Yes.*
>
> *Q. Either from their own resources or because they did a deal with Bank of America, yes?*
>
> *A. Yes.*
>
> *Q. And there's no mention here that in Q1 2011, Autonomy concluded a direct deal with Bank of America?*
>
> *A. Not on this, and I don't recall that being mentioned at the time*
>
> *Q. And presumably you were also unaware that under that direct deal, Autonomy designated a third reseller, MicroTech, as its payee?*
>
> *A. No.*
>
> *Q. Were you ever told that, pursuant to that agreement between Autonomy and Bank of America, Bank of America then paid MicroTech which in turn paid the two VARs: Capax and DiscoverTech?*
>
> *A. No. That was a level of detail we wouldn't have gone into.*
>
> *Q. And if that is what had happened, it's not something you would have understood at the time, no?*
>
> *A. No, as I say, it's a level of detail we wouldn't have gone into at the time.*
>
> *Q. And you would have remained of the understanding in Q1 2011 that no deals between Autonomy and a VAR had been resigned directly between Autonomy and the end-user, yes?*
>
> *A. Yes.*
>
> *Q. And no instances of that occurring were drawn to your attention, were they?*
>
> *A. Not that I recall.*
>
> *Q. If that had in fact happened in Q1 2011, that would have been contrary to your understanding at the time?*
>
> *A. Yes."*

1074. The Claimants also contended (see (5) in paragraph 1056 above) that Autonomy contrived arrangements for the sums payable by BofA under the direct deal to be routed and used to fund payments to Autonomy by the VARs in respect of their obligations under VT23 and VT24 (as well as VT16 and VT21) so that (according to the Claimants) *"Autonomy's own money was used to pay off debts ostensibly owed to Autonomy by DiscoverTech (and Capax Discovery)"*.

1075. It was Mr Egan's unchallenged evidence that, in January 2011, in anticipation of the direct BofA deal, Mr Hussain asked Mr Egan to determine how the payments from BofA could be used to fund payments to Autonomy by the VARs in respect of their BofA deal-related payment obligations. On 25 January 2011, Mr Egan asked Mr Hussain and Mr Chamberlain, "*Assume you want cash flows to be bofa/mt/dt/au not add another route?*". Mr Hussain did not dissent. The Claimants also contended that "*It is inconceivable, given the size of the amounts involved, that Dr Lynch would have been unaware of the overall plan, whether or not he knew the details."*

1076. Under the direct agreement between Autonomy Inc and BofA, payment was to be made to Autonomy or its designated payee. Autonomy designated MicroTech as its payee, ostensibly because of MicroTech's 8A status. BofA therefore paid the $19.5 million licence fee (minus the early payment discount of $500,000) to MicroTech rather than Autonomy.

1077. The impetus for involving MicroTech plainly came from Autonomy, not BofA. Indeed, on 25 January 2011, Reagan Smith of BofA asked Mr Egan to explain, "*What service, specifically, will they [MicroTech] offer as part of this?*". Mr Egan responded that MicroTech "*are not truly providing a service in the classic sense other than reselling the software*".

1078. As explained by Mr Egan, what happened next is that:

(1) MicroTech paid $10 million to DiscoverTech.

(2) DiscoverTech paid $9 million to Autonomy (having already paid Autonomy $1 million in January 2011), in substantial discharge of its "*obligation*" to pay licence fees of $7 million and $3.5 million under VT23 and VT24 respectively.

(3) The remaining $9 million was paid to Capax Discovery and used by it to pay $9 million to Autonomy.

1079. This demonstrates the circularity relied on by the Claimants; but, given the express provisions of the purchase orders, I am not persuaded that these money flows do more than give effect to the provisions ostensibly agreed for the VARs to be compensated in the event of a direct sale. To my mind, a more telling point than the contention that *"Autonomy's own money was used to pay off debts ostensibly owed to Autonomy by DiscoverTech (and Capax Discovery)"* is that the presentation of the composite arrangements, by apparently treating the VAR's obligations to repay as substantive, bolstered (artificially) the notion that the VARs were actually transacting substantive business and undertaking substantial risk. The money flow was a further means of giving substance to the illusion.

1080. In the same context, the Claimants also contended that Autonomy's justification for the introduction of MicroTech was false. Deloitte's working paper records that Deloitte were told that Autonomy had *"chosen to use Microtech, albeit through two separate VARs, to lead and integrate this produce [sic] on behalf of the end-user"* and to avail itself of

MicroTech's 8A status. The Defendants queried what Deloitte had been told but accepted that the summary was *"broadly correct"* and that *"BofA were enthusiastic about paying MicroTech as an 8A. MicroTech were also going to provide services and did indeed do so."* The evidence relied on by the Defendants demonstrated acceptance not enthusiasm; and as the Claimants submitted there was no evidence that BofA had suggested the need for an 8A entity to be involved (nor was there), and neither was there evidence that BofA had requested the involvement of the VARs. No reason for this falsity as to the introduction of MicroTech was suggested to me; but, as it seems to me, it justified the payment flows, and assisted their presentation as connoting VAR end-user sales; and that may have been its purpose.

1081. The sixth and last specific criticism of VT23 and VT24 concerned the payment of MAFs to DiscoverTech. As to this, the Claimants' case was that:

(1) Autonomy paid a \$1.1 million MAF to DiscoverTech. On 8 March 2011, Mr Egan said (in an email copied to Mr Hussain) that DiscoverTech should be paid a 10% MAF on the \$7 million licence fee, a \$400,000 fee for "*distribution*", but no margin on the \$3.5 million licence fee.

(2) Mr Hussain was asked for and gave his approval to the \$1.1 million MAF, as did Dr Lynch. Dr Lynch said in cross-examination that he approved the payment of this fee "*because it would have been agreed at the time that the deal was done with DiscoverTech*". However, there is nothing in any written contract at the time of these VAR transactions which entitled DiscoverTech to such a fee.

(3) The fee was invoiced as a MAF on 8 March 2011, even though, as both Defendants knew, DiscoverTech had not provided any marketing assistance of any kind.

1082. In all the circumstances, I find it difficult to accept that a payment of a MAF, let alone a payment of some \$1.1 million, was justified. When his first answer about a prior contractual commitment failed, Dr Lynch talked once more in cross-examination about encouraging *"our ecosystem of partners"* and of the need to provide them with an *"incentive for doing the business"*. This was unimpressively general; but it is also necessary to consider what the ecosystem and the business being done in it really was. It was not the usual ecosystem: and Dr Lynch's evidence that such fees were common was an exercise in extrapolating a justification from a very different context. Usually, VARs make some sort of contribution. Here, the *"ecosystem"* was comprised of a small coterie of VARs whose contribution was limited to signing paperwork prepared by Autonomy to provide a ticket for revenue recognition. The BofA arrangements provided a particularly glaring example of the inactivity required of them. The incentive was for them to act as placeholders, as they did: that did not, in my judgment, justify payment of a MAF. The basis for payment of a margin or MAF was as set out in the purchase order: it depended on *"VAR's efforts in securing End-User's procurement of a license of Autonomy software."* None of the criteria was met.

Defendants' alleged knowledge of false accounting in respect of the BofA deals

Mr Hussain

1083. It is clear from the documentary evidence that it was at Mr Hussain's suggestion that the big BofA deal was parcelled into smaller pieces and 'sold' to VARs to be warehoused until the real (BofA) deal could be completed. It was inherent in the objective of the arrangements that the VARs selected should do nothing, and Mr Hussain must have known that. As previously noted, the VARs were never intended to exercise, and never did exercise, any independent right of disposition in respect of the software notionally 'sold' to them. The only real sale of the software took place when the direct BofA sale was concluded. Especially as a trained accountant and experienced CFO, Mr Hussain cannot have thought that the sales to the VARs had any real or economic substance such as to legitimately warrant revenue recognition.

1084. Mr Hussain cannot have taken any real comfort from Deloitte's approval. He knew that they did not know that the BofA sale was the only real sale, and that the VARs were not intended or expected to do anything, and never did anything, except wait for payment in due course.

1085. I find that Mr Hussain had "guilty knowledge" that the recognition of revenue from VT16, VT21, VT23 and VT24 was (in each case) improper.

1086. Further, I find that in the circumstances set out in paragraphs 1056 to 1061 above, Mr Hussain was aware of and complicit in the backdating of the VT23 purchase order, and that therefore on that ground also the recognition of revenue in respect of VT23 in Q4 2010 was improper.

1087. Mr Hussain also must have known that in such circumstances the justification put forward for the payment of large sums purportedly by way of MAFs (i.e. that the VARs' assistance had made a valuable contribution), which he personally approved, was without foundation and indeed false.

Dr Lynch

1088. Dr Lynch accepted that he was aware of and involved in the efforts to close the deal with BofA in Q4 2010[88]; but he maintained that he was not involved in or aware of the "smaller pieces" VAR deals, the implementation of the BofA deal after its closing, the payment flows to the VARs, or the MAF payments.

1089. The Claimants offered very little transaction-specific evidence of his involvement at the operational level and his knowledge, though in cross-examination he did ultimately accept that (a) he *"may have known something"* about Autonomy's efforts to do a deal with Amgen in Q3 2010 and did know that when it could not be closed, Autonomy ended up involving a VAR and recognising revenue on a purchase order from Capax Discovery in respect of VT16; (b) it was *"quite possible"* that he did discuss with Mr Hussain the latter's wish to bring in VARs, and would have had *"no issue"* with that; and (c) no sale to BofA had been closed in Q4 2010 and that instead Autonomy had made sales to VARs. He also explained his understanding to be that *"the stock from the resellers was sold to Microtech as part of this deal."* He explained this further when it was suggested to him that "*Mr Egan had used Bank of America as backfill to ensure Capax got paid for its Amgen purchase order*". He answered:

> *"A. I wouldn't use the word "backfill". What it is is that Capax had stock and Mr Egan introduced the Bank of America opportunity and they could sell that stock to Bank of America, which was*

[88] including intervening with the head of BofA in London to try and get the deal done.

written explicitly in their deal."

1090. He also had to accept that he had approved the payment of the MAF to DiscoverTech, his position being (at least initially) that he would have approved it because *"it would have been agreed at the time the deal was done with DiscoverTech"* and because he was happy to encourage *"our ecosystem of partners"*.

1091. Apart from this, he repeated that he was not involved at any level of detail. In particular, when it was suggested to him that Autonomy negotiated with BofA without any involvement by the VARs, and that he would have known that they were not involved, he answered that he would have expected Autonomy to continue to be involved with BofA, which was a very large repeat customer of Autonomy's; that he did not know whether or not the VARs were involved in negotiations with BofA; but that in any event, he would not *"be at that level of knowledge in any case"*, given that this was taking place well below his level and in the US with a US subsidiary.

1092. Notwithstanding Dr Lynch's unusual degree of control and tendency to descend suddenly to micro-manage matters of particular interest or concern to him, I would be inclined to accept that the details of who participated in negotiations and when were not within his knowledge. However, the decision to involve VARs in the context of an especially large deal like the BofA deal seems to me to be of a different order, about which I consider he is more likely than not to have been consulted. Mr Hussain would not have wished to fragment such a deal and commit to substantial payments without first consulting Dr Lynch. Similarly, it seems to me likely that both Mr Hussain and Dr Lynch would have been careful and vigilant to ensure that nothing upset the balance with BofA. In my judgment, it is more likely than not that the strategy of involving VARs to obtain revenue recognition but keeping them altogether removed from the negotiation and closing of the ultimate prospective deal would have been discussed and developed by the Defendants. Put another way, Dr Lynch with Mr Hussain set the pattern, adapting it as necessary to the particular circumstances.

1093. I have concluded, on the balance of probabilities, that Dr Lynch did know that the sales to the VARs were expedients to trigger revenue recognition which were intended to result in no substantive change so far as Autonomy's negotiations with BofA were concerned, nor any independent control of or dealing by the VAR with the software sold. I have concluded further that Dr Lynch knew that only on paper could what occurred be termed a sale; that what mattered was ultimately substance not form; and that the VARs' involvement was underpinned by their knowledge that though to fulfil the objective of the dealings their legal obligations had to be recorded, Autonomy would, one way or another, see to it that they were covered or extinguished.

1094. In my judgment, Dr Lynch had "guilty knowledge" that the only real deal was Autonomy's direct BofA deal and that recognition of revenue from the VAR deals which preceded it was improper.

PART IV OF SCHEDULE OF IMPUGNED VAR TRANSACTIONS

Other impugned VAR transactions where side-agreements are alleged

1095. Eight of the impugned VAR transactions were between Autonomy and counterparties other than Capax Discovery, FileTek and the Truitt companies. Of these, five were *"pure collectability VAR transactions"* (VT9, VT17, VT19, VT22 and VT29) where no side-agreement or the like was alleged and the issue is only whether the requirements of IAS 18.14(d) were satisfied.

1096. I deal later, in Part V of this Schedule, with those *"Collectability VARs",* pausing to note here only that for two of the five (VT9 in Q4 2009 and VT22 in Q4 2010) it was common ground between the accounting experts that the requirements of IAS 18.14(d) were not satisfied and that therefore no revenue should have been recognised.

1097. Two of the transactions I discuss in this Part IV (VT15 in Q2 2010 and VT26 in Q4 2010) were alleged to have displayed the same 'pattern' as in the case of the other impugned VAR transactions, even though the VARs concerned appeared independent, were not in the small group of 'friendly' VARs, and the agreements were not transacted through Mr Egan. The VARs concerned were (a) in the case of VT15 in Q2 2010 for proposed end-user Credit Suisse, a company called Realise Limited ("Realise"), and (b) in the case of VT26 in Q4 2010, a company called Tikit Limited ("Tikit") for proposed end-user KPMG.

1098. The Claimants' case was that the Court should infer in the case of VT15 and VT26 that, as in the case of the other impugned VAR transactions with 'friendly' VARs, the 'pattern' was consistent only with there having been a side agreement that the VAR should not either make any efforts to on-sell nor ever be required to pay Autonomy from its own resources, and that the recognition of revenue was thus improper.

1099. A third transaction with an apparently "independent" VAR was part of the larger projected transaction with the Vatican Library (VT14 in Q1 2010), which Deloitte refused to approve for revenue recognition and was impugned on the narrow basis that though no side agreement was alleged, it was never intended that the relevant VAR (called Auxilium) should make, and it never did make, any efforts to on-sell the licence. I deal with VT14 last in this Part IV before addressing the *"pure Collectability VARs"* in Part V.

VT15: The Realise/Credit Suisse deal Q2 2010

1100. On 18 June 2010, with the end of Q2 2010 approaching, Mr Hussain sent Dr Lynch (only) a revenue summary spreadsheet identifying the key transactions for Q2 2010. These included a transaction for $2.7 million with Credit Suisse, subject to the observation that "*sign off 29th so tight*".

1101. On 29 June 2010, Mr Hussain sent Dr Lynch an updated revenue summary spreadsheet. The proposed Credit Suisse transaction was now stated to be worth $2.4 million and Mr Hussain included the comment "*Steering committee signed off on Friday, now race to get paperwork*".

1102. On 29 June 2010, Mr James Murray asked Credit Suisse to confirm its agreement to a letter of intent, which it did on 30 June 2010, though Mr Dominic Frischknecht of Credit Suisse emphasised in his covering email that, "*we are only confirming that we are* *interested to close a contract in future but at this point not able to confirm any terms of the deal*". The letter of intent stated that Credit Suisse:

> "*plans to enter into a software license purchasing agreement under which – and provided that Credit Suisse gives approval to [sic], Autonomy's chosen partner shall provide software licenses to Credit Suisse AG no later than July 31st 2010.*"

1103. That same day (30 June 2010), Mr Murray wrote to Mr Andy Lamond of Realise, forwarding a copy of the Credit Suisse letter of intent, saying "*Thanks for your time today at very short notice. The attached letter specifies the amount that Credit Suisse are prepared to pay*". That evening, Mr Murray informed Mr Hussain and Mr Chamberlain, "*Realise will sign the deal tonight. Please liaise with Andy Lomond*". Realise appears to have been a substantial UK technology company: *'The Scotsman'* reported its sale for £40,000,000 in 2014. It was a significant UK partner of Interwoven. The evidence did not reveal quite why or when Realise was selected. None of Mr Hussain, Mr Chamberlain or Mr Kanter gave evidence in these proceedings (or at all). There was no witness evidence as to what was said to induce Realise to act as a VAR, or why Realise was chosen.

1104. Also on 30 June 2010, Mr Rafiq Mohammadi of Autonomy emailed Dr Lynch, reporting that "*we did not get Credit Suisse but James [Murray] was able to find one large and one medium that added up. CS is his next quarter – so we have not lost anything*". Dr Lynch forwarded the email to Mr Kanter and Mr Hussain. Dr Lynch accepted in cross-examination that he did learn before the end of the quarter that no Credit Suisse deal could be concluded in the quarter ("*Yes, I guess so*"); but he emphasised more than once that he was not really involved in it or in the VAR deal that followed. The frequency with which he was updated in the last days of the quarter suggests that even if not involved directly, he was kept very closely informed.

1105. On 30 June 2010, ASL entered into a One-Time Reseller Agreement with Realise, for end-user Credit Suisse Securities (USA) LLC, for a licence fee of €1,463,000 (USD equivalent $1,987,096) plus €365,750 (USD equivalent $496,774) for support and maintenance and €102,500 in consulting fees. Mr Kanter signed the agreement on behalf of ASL. The amount of the proposed deal to Credit Suisse exceeded the amount of the VAR deal and thus gave the VAR (Realise) margin on the deal.

1106. The One-Time Reseller Agreement placed Realise unequivocally on risk as a matter of law:

(1) Clause 1 provided:

> *"<u>Products Licensed and Services Provided.</u> Upon VAR's execution of this Agreement, Autonomy shall license to VAR for sublicense to the End-User the Autonomy Software. Once executed. This Agreement including any Product Schedules attached hereto, constitutes a non-cancellable purchase commitment. All fees and expenses specified herein are non-refundable. …"*

(2) Clause 9 provided:

> *"Any waiver, amendment, supplementation or other modification or supplementation of any provision of this Agreement shall be effective only if in writing and signed by both parties.*
> *…*
> *This Agreement, including the Exhibits, represent the entire Agreement between the parties hereto concerning the subject matter hereof and supersedes any and all prior correspondence, quotations and negotiations. VAR expressly agrees that this Agreement and the Exhibits hereto shall have priority over any contrary terms or conditions contained in any purchase order or other form hereafter delivered by VAR to Autonomy… VAR expressly agrees that this Agreement and the Exhibits hereto shall have priority over any additional or inconsistent terms contained on such purchase orders or other forms hereafter delivered by VAR to Autonomy."*

1107. Realise provided written confirmation to Deloitte on 30 June 2010 that the invoice listed in the confirmation they had requested was proper and due (although part-paid) and that there were no *"side letters or other agreements"*.

1108. In the event, no deal was ever concluded with Credit Suisse, by either Realise or Autonomy. In December 2010, Realise paid Autonomy in total £626,990 (representing £533,609 plus VAT) in respect of the June 2010 deal, but no further amounts.[89] A bad debt provision was made for the full amount of the remaining outstanding receivables (some £1,299,342 inclusive of VAT). That amount (£1,299,342) was finally written off long after the acquisition, in September 2012.[90]

1109. The Claimants suggested that, in the absence of any evidence from Mr Hussain, Mr Chamberlain or Mr Kanter, and *"no witness evidence, therefore, as to what Autonomy said to induce Realise to act as a VAR",* the Court should:

> *"infer, however, that the same assurances were given to Realise as were given to Autonomy's preferred VARs – in particular, that Realise was not expected to make efforts to sell the software to Credit Suisse and that Autonomy did not intend Realise to pay for the software from its own resources."*

1110. In their written closing submissions, the Claimants relied on the following in support of that inference:

(1) When on 15 October 2010, after Realise had not paid the first instalment (of €200,000) which fell due on 28 September 2010, ASL's credit control department sent an email to Mr Chamberlain and Mr Stephan asking whether they could *"chase them for payment yet???",* Mr Chamberlain immediately forwarded it to Mr Hussain with the message (marked High importance) simply stating *"Need guidance"*. There is no record of a response; but Realise was not

[89] It is evident that this payment was directly related to the Credit Suisse deal because the invoice number on the cash receipt – 5006 – matches that on the invoice issued to Realise in on 30 June 2010.
[90] As the Claimants have accepted at Schedule 3 to their Particulars of Claim.

chased for payment. When the remaining sum of €1,628,750 plus the consulting fee fell due on 28 October 2010 that was not paid by Realise either.

(2) When no end-user deal eventuated, Autonomy agreed (by an agreement dated 20 December 2010) to purchase a stake in Realise Holdings Limited (for £2,607,208) and to *"pre-purchase professional services"* from Realise (for the sum of £570,000 plus VAT), conditional on receiving from Realise payment of £533,609 plus VAT in partial satisfaction of its debt; and all this was arranged, not because Autonomy needed or it was in its commercial interests to acquire either Realise or professional services, but to put Realise in funds to pay down part of its outstanding debt to Autonomy.

(3) Realise never paid any sums to Autonomy except as and when it received payments made by Autonomy on the understanding that Realise would use the receipts to pay down instalments. By 9 August 2011, no further payments had been made by Realise except those for which it was put in funds to make as briefly described in (2) above. When on 9 August 2011, after Realise had sought to re-activate its CSS (Customer Support Site) support account, Autonomy's credit control department asked what should be done about their overdue invoice of 300+ days, Mr Chamberlain referred the matter to Mr Kanter, stating:

> *"Need guidance here. When I spoke to them (Andy Lamond) he directed me to you and stated that they "did not need to pay". I can't give them access to a support account when they have not paid."*

(4) Mr Kanter replied (copying Mr Hussain) *"Bs. Haven't spoken to him in six months"*, whereupon Mr Chamberlain informed them both that he would stop access to their accounts and send the outstanding account to legal absent objections. Yet on the last business day (30 September 2011) before HP's acquisition of Autonomy became final, and after negotiations in which Realise made clear its understanding that it *"did not need to pay"* unless and until funded, a bad debt provision was made for the full amount of the shortfall between the funds thus far provided by Autonomy and then remitted to Autonomy by Realise and the total amounts due from Realise under the One-Time Reseller Agreement, which then was $2,030,611 (equivalent to £1,299,342 inclusive of VAT). This was (considerably) later written off in full.

(5) All the while, Realise never made any attempt to negotiate or conclude an end-user sale; it was instead Autonomy which continued to seek a deal with Credit Suisse.

1111. As to (2) in the preceding paragraph, the Claimants focused especially on Autonomy's agreement to pay Realise in advance for professional services (at a stated rate of £950 per man day for 600 days) in support of their case that the deal was contrived simply to fund Realise to enable it to repay Autonomy, and that Autonomy's moneys *"went round in a circle"*. The Claimants contended that:

(a) Autonomy had never provided any evidence as to why it had any need to purchase two years of professional services paid for in advance, except for Mr Kanter's description of the arrangement in an email to Dr Lynch and Mr Hussain dated 19 December 2010 as being *"part of the process of bringing the two* *companies closer"* and *"to bring [Realise] into key customers"* and an assertion by Dr Lynch when cross-examined that Autonomy *"had continual need for services"*. Mr Kanter might have elaborated; but he was not called.

(b) When in September 2011, during the period between HP's offer and the completion of the HP acquisition of Autonomy, a question was raised as to whether a credit was applicable to Autonomy in respect of the service days promised, Mr Murphy of Realise sent an email to Mr Hussain dated 19 September 2011 stating:

> *"We rebated £533,609 + VAT (£626,990) against the service days in Dec and it was our understanding that this concluded the deal…"*

(c) No professional services were ever in fact provided.

1112. The Defendants, noting also that the Claimants had withdrawn their claims in October 2018 only to reinstate them in December 2018, but without any pleading, evidence or particulars of the side-agreement they purported to allege, dismissed any suggestion that the VAR deal with Realise lacked economic substance and could only be explained by reference to some sort of side-agreement.

1113. They referred at some length to the exchanges between Credit Suisse, Realise and Autonomy in support of their contention that Realise intentionally assumed the risk on the purchase unconditionally under its reseller agreement because it was confident of the prospects of the Credit Suisse deal closing, especially given Credit Suisse's letter of intent (see above), and there was a generous reseller margin. They relied also on:

(1) Mr Murray was engaged in speaking to Mr Lamond of Realise. The Claimants did not suggest that Mr Murray was engaged in wrongdoing.

(2) Ms Haverfield sent Mr Lamond of Realise a draft of the One-Time Reseller Agreement 27 minutes after that, copying Mr Murray and Mr Chamberlain. The Claimants have not suggested that she was engaged in wrongdoing.

(3) At 20:03, 39 minutes later, Mr Lamond said he was happy with the draft and that Mr Murphy (the CEO) would be signing it on behalf of Realise that night. Mr Lamond had evidently read and approved the terms of the document. He was the Finance Director, so was well-placed to understand what it was that Realise were signing up to.[91] Ms Haverfield sent Mr Murphy the execution copy 20 minutes later. Mr Murphy signed and returned the agreement at 22:00, saying:

> *"Please find enclosed the signed pages of the Autonomy One Time Reseller Agreement as per your email.*
> *I also enclose a combined whole signed document in one pdf for your records."*

(4) The signed agreement sent back by Mr Murphy placed Realise unequivocally on risk.

[91]Mr Lamond's role as Finance Director can be seen from his email.

1114. As to the matters relied on by the Claimants as summarised above, the Defendants contended that:

(1) First, the email of 15 October 2010 in which Mr Chamberlain said to Mr Hussain "*need guidance*" on the question of whether to chase Realise for payment was neither sinister nor suggestive of a side-agreement. Autonomy had sold this deal to Realise on the parties' mutual expectation that the Credit Suisse deal would go through. As at October 2010 it had not yet gone through. It was not until later, in April 2011 on the Claimants' case, that Credit Suisse decided to look at a competitor product. In these circumstances, the Defendants contended that it was hardly surprising from a commercial perspective that Autonomy was not automatically hounding Realise for payment in Q3 2010.

(2) Secondly, the email exchanges in August 2011 occurred after the transaction in which Autonomy had taken a stake in Realise, and after the Credit Suisse opportunity had not come to fruition. The email from Mr Chamberlain telling Mr Kanter and Mr Hussain that "*Mr Lamond directed me to you and stated that they [Realise] "did not need to pay*"" did not show that there was a side-agreement in Q2 2010. If anything, it appeared to show Realise seeking to avoid payment to their minority shareholder in circumstances where the commercial opportunity had been lost. Further Mr Kanter had rejected the suggestion that Realise need not pay as *"Bs"*.

(3) Thirdly, the fact that Autonomy continued to negotiate with Credit Suisse was immaterial. Even assuming that Realise was simply acting as fulfilment partner on the transaction, providing it was genuinely assuming the risk the revenue was correctly recognised. In this regard, the Credit Suisse approved letter of intent made it clear that the plan was for the software to be provided by Autonomy's partner.

(4) More generally, the Defendants submitted that the Claimants' arguments involve a fallacy which (as previously observed) is repeated elsewhere in their submissions: the fact that Autonomy may have continued in negotiations does not mean that the reseller was never intended to be a party to the end-user deal. On the contrary, the aim was that the end-user <u>would</u> execute the deal with the reseller, as per the Credit Suisse letter of intent.

(5) Fifthly, the fact that a deal with Credit Suisse could not ultimately be concluded (referring to events in April 2011) was not an "indicium" of a side-agreement. At the time of the reseller transaction the Credit Suisse deal was seen as a good prospect and the letter of intent approved by Credit Suisse confirmed that.

1115. The Defendants contended further that the Claimants' depiction of Autonomy's transactions with Realise after the transaction, under which Autonomy (i) sold a minority stake in a company named Okana to Realise (which was pursuing an acquisition of Okana), (ii) took a minority stake in Realise and (iii) purchased 600 man days of professional services from Realise for a total of £570,000 whereupon Autonomy agreed with Realise that Realise would make a payment of £488,000 against their existing debt, as artificial was illegitimate, distorted and misplaced.

1116. The Defendants relied on the following:

(1) The approach from Realise to Okana and Autonomy's decision to invest in Realise were patently genuine. On 25 October 2010 Mr Hampson of Okana wrote to Dr Lynch as follows. (This email also shows the substance of Realise as a reseller):

> *"I've developed an excellent relationship with Interwoven Partner, Realise, and in particular their ChiefExec, Tony Murphy, over the last 18 months. This came about as part of our strategy to open up new channels for our core IDOL capability as chaining has become the norm. Realise look after the likes of Fidelity, Standard Life, Nikon and Channel4.*
>
> *Our joined-up thinking and exact-same view of the phenomenal market opportunity you've created for Autonomy Partners has now reached critical mass and Realise have taken a natural next step to look to acquire Okana. A cash and shares offer for 80% of the company has been tabled, this being at a valuation which Bob and I are comfortable with and would like to accept. Not only do we believe this represents the best possible outcome for Okana at this point, we are also extremely excited by the power and growth potential of a joined-up Okana/Realise organisation. We firmly believe that this is the right thing for us to do.*
>
> *Ultimately, this is all small beer to Autonomy but following the support you've given to Okana, and to me personally, I'd be delighted if we can work to have all shareholders accept the same deal, this keeping Autonomy in as a minority shareholder. Okana would become part of the Realise Group, which as you probably know, also now includes Realise Capital Markets headed up by Nick Hough-Robbins. Coverage of the combined unit would grow to span a great many facets of the Power, Protect and Promote sectors."*

(2) Mr Hussain wrote to Dr Lynch in relation to this. Mr Hussain was clearly interested in acceding to Mr Hampson's request, provided Autonomy retained shares in Realise, and was interested in a minority investment in Realise. Mr Hussain did mention the outstanding debt, but the Defendants contended that this plainly was not driving his thinking, and Dr Lynch would not have seen it that way:

> *"We need to know the valuation. Gut feel (although I could be well out) says it's being valued at £1.5m or so ex cash and £2m inc. cash. We own 18% or so of Okana so our stake would be worth c. £400k on this valuation. I'll have to check but I think we invested around £80k.*
>
> *The last 3 years has seen the following:*
> *- Revenues Mar '1 0 (£808k), Mar '09 (£795k), Mar '08 (£1 ,028k)*
> *- Operating profit £101 k, £146k, £164k*
> *- PAT £80k, £123k, £144k*
> *Cash at hand is £465k*

> *Since Realise is proposing to pay in cash and shares I would be happy to accept shares only to keep my ownership level meaningful.*
>
> *I would be prepared to invest in a minority stake in Realise and like Okana continue to put more services through them.*
> *Please note that Realise owes us £1.2m which is slightly overdue so this would work as long as the current debt was paid off.*
> *I need to know the valuation for Okana and the valuation established for the Realise shares."*

(3) The transaction was completed in December 2010. Although Autonomy secured a repayment of part of its debt out of the overall transaction there is nothing sinister in that, nor in the notion that money "went around in a circle". The Claimants did not suggest (and had not adduced any evidence) that either the stake in Realise or the professional services which were purchased were overvalued.

(4) As regards the professional services, as Mr Hampson's email made clear, Realise were a major professional service provider in connection with Autonomy's Interwoven business. Realise were a UK partner for Autonomy and there is no basis for suggesting that these were other than at fair value. The Defendants contended that the Claimants were seeking to read too much into Mr Murphy's later email in September 2011 which referred to an amount being *"rebated"*, and that amount concluding the professional services aspect of the deal: this was simply part of Mr Murphy's attempt to minimise his obligations in September 2011: Mr Kanter's response (not referred to by the Claimants) was that he was *"a little distressed"* about what he had read in Mr Murphy's email, and plainly did not agree with him.

(5) The Claimants' apparent complaint about the admitted fact that the debt was *"later written off"* was misconceived: that happened in late 2012, and was a decision of HP. In any event, the Defendants argued, these post-transaction events could have had no bearing on the earlier revenue recognition.

My assessment of VT15

1117. Realise was a longstanding service partner of Autonomy in connection with Autonomy's Interwoven business; but it was not a "friendly VAR". That, and the fact that (unlike the position in, for example, VT18 and the 'fulfilment' transaction with FileTek) Mr Egan was not in any way involved are obvious departures from the pattern.

1118. There are serious gaps in the evidence. As noted previously, the selection of Realise was unexplained; and I was provided with no details of its business, still less whether it included reselling or being a 'fulfilment partner'. In contrast with the position relating to all the other VAR transactions discussed above, where evidence had been given on behalf of the VAR in the US even if not in these proceedings, I had not the merest glimpse into the intentions or expectations of Mr Lamond or anyone else at Realise, save what was revealed by the factual sequences and coincidences I have described, and the documentation.

1119. In my view, those factual sequences and (for the most part) the documentation do give rise to an inference that Realise never expected to pay instalments under the One-Time Reseller Agreement out of its own pocket, and was obdurate in refusing to do so when the end-user deal it had expected to be completed virtually immediately did not eventuate. Those sequences and that documentation also demonstrate that Autonomy contrived a number of transactions to rescue Realise. Furthermore, it is the undisputed fact that Realise did nothing after the sale to it to negotiate with Credit Suisse or otherwise assist in establishing an end-user sale: it was wholly passive and dependent on Autonomy in that regard.

1120. The transaction did exhibit certain features characteristic or at least reminiscent of the pattern. However, it departed from the pattern in important respects additional to those already identified above. In particular, it seems plain that it was intended and expected to be the contracting party to the end-user deal; and it was from a margin on resale (which had been carefully quantified by reference to the price expressly confirmed in Credit Suisse's letter of intent) that it was to be rewarded and not by a MAF. Further, the documentation is not all one way: although the references in the exchanges in 2010 to Mr Chamberlain needing guidance could suggest some high-level understanding, the exchanges between Mr Kanter and Mr Chamberlain in 2011 appear genuine and indicate that neither understood any assurances to have been given by Autonomy that Realise did not need to pay.

1121. In my judgment, there is an alternative explanation for the fact pattern. This is that on the one hand, Realise (a) was content to accept uncovered risk on the deal because it was assured, and Credit Suisse's letter of intent confirmed, that the end-user deal with Credit Suisse was virtually certain and imminent and (b) regarded the minimal risk as it perceived it to be at the time, of Credit Suisse in effect going back on its statement of intent to be commercially justified in light of the margin it was to obtain, and (c) felt let down, justified in declining to pay, and in any event determined not to do so; whereas on the other hand, Autonomy (i) felt it in its own interests to try to remove the signs of a failed VAR deal and (ii) as time moved on, had an extra incentive in that regard in not wishing anything to unsettle the presentation necessary for the sale to HP.

1122. At the front of my mind, and the question I have consistently returned to and do again now is: what distinguished VT15 from the other successfully impugned VARs? I would summarise the differences as follows:

(1) The evidence on the transaction was sparse (there was no mention of it in the witness statements at all), and (as previously noted) did not explain why Realise was selected. However, Realise was a substantial UK technology company with well-established credentials in servicing and looking after major companies including Fidelity, Standard Life, Nikon and Channel 4 with no special relationship with Autonomy. Its choice as a VAR, even if only as a 'fulfilment partner' was not, on the evidence put before me, impugned in any way.

(2) There was never any suggestion of any impropriety whether on the part of anyone in Realise or on the part of those who negotiated the transaction at Autonomy.

(3) Even though Realise was not intended to negotiate with Credit Suisse, it is clear that Credit Suisse expected to contract with Realise, and there is nothing to suggest that Realise did not intend to contract with the end-user: its MAF was

dependent on the margin between what it paid Autonomy and what it would charge the end-user. I see no sufficient basis for concluding that risk and control was retained by Autonomy.

(4) It was not plausibly suggested that Mr Kanter's email response (*"Bs. Haven't spoken to him in six months"*) to Mr Lamond's suggestion that Realise *"did not need to pay"* was contrived, and the exchange is inconsistent with any known side agreement of the sort alleged.

1123. Even then, it has been a close run thing, especially given the track record prior to this deal of confected VAR arrangements; but I have not in the end been persuaded that the very limited available evidence necessarily demonstrates on a balance of probabilities that Realise entered into VT15 on the basis of a side-agreement or similar arrangement which in effect negated, or promised its release from, its contractual obligations.

1124. In case, however, I am wrong, and the inference asserted by the Claimants is on review held to have been warranted and established, I should state my conclusions on the Defendants' knowledge.

Defendants' knowledge of and participation in VT15 and the Realise acquisition

1125. Mr Hussain was directly involved. If, contrary to my assessment, revenue was improperly recognised from VT15, Mr Hussain would have been aware of the facts giving rise to the impropriety and their consequences in terms of the substance of the transaction and the criteria in IAS 18.14. He would thus have had "guilty knowledge".

1126. Dr Lynch did not say anything about VT15 in either of his witness statements. He told me in cross-examination that he had very little involvement in this transaction. He accepted that he was given some, but he stressed very limited, information in relation to the progress of the Credit Suisse deal, but the information given to him in an email update on 30 June 2010 indicated that it was a good prospect for a subsequent quarter. He told me he did not recall that Autonomy had taken the deal to a VAR and had no recollection of being involved in the sale to Realise, the sale terms, or in the accounting for it.

1127. Later in 2010, he was aware of and involved at a high level in considering taking a stake in Realise, which Autonomy subsequently did. It was suggested to Dr Lynch that he and Mr Hussain "*saw this as an opportunity to address Realise's debt on its VAR transaction*". The Defendants contended that this would not be improper even if correct, but Dr Lynch rejected the proposition. Dr Lynch also explained about his understanding of the transaction as follows:

(a) The transaction involved the acquisition by Autonomy of an approximately 20% interest in Realise conditional on Realise paying £533,609 to Autonomy, and a payment by Autonomy to Realise upfront of a fee for professional services for a specified number of days in the sum of £570,000. It was an opportunity to combine two of his services partners, Realise and Okana (which Realise was about to acquire or had acquired). Autonomy would have wanted to see the debt paid off in the process.

(b) The purchase of professional services was at market rates. The Claimants did not challenge Dr Lynch's evidence on that, except to question whether Autonomy had any actual need for professional services from Realise, and to suggest that in fact Autonomy never intended to call on Realise to provide them.

(c) Dr Lynch's answer was that Autonomy had a continual need for services. Further, he did not accept the proposition that Realise was not in fact expected to provide professional services: he did not know, after such a long time, *"whether they had services days already on the books or not"*. It will be recalled that in September 2011 Mr Kanter also did not agree with the summary of Realise's obligations given by Mr Murphy in the email relied on by the Claimants.[92]

1128. Whether or not when giving his evidence he could recall having been aware of it at the time, I have little doubt that Dr Lynch was kept informed of the Credit Suisse deal, the need to close it before the end of the quarter to bring in revenue to meet forecasts, the race to close it, the ultimate delay, and the usual last-minute resort to a VAR or 'fulfilment partner'. By the same token, it seems to me likely, however, that he would have known also that (a) Realise was not a 'friendly' VAR (b) Mr Egan was not involved (c) Credit Suisse had signed a letter of intent, the only glitch had been tightness of time, and the deal could confidently be expected to close in the next quarter.

1129. However, it seems to me that it is to be borne in mind that although it is an abiding curiosity of this case, and I suspect an omission for which each side may have a conflicting forensic explanation, that I was told next to nothing about other "innocent" VAR deals, it does seem that there was a large number of them both before and during the Relevant Period. The necessary inference is that some were entirely innocent.

1130. On balance, I do not think the evidence is sufficiently clear in this particular context to establish that Dr Lynch considered this deal to be a 'pattern' deal; and I would therefore have declined to conclude that he had "guilty knowledge".

VT26: Tikit/KPMG Q4 2010

1131. As was pointed out at the outset of the section in Dr Lynch's written closing submissions addressing this transaction (VT26), VT26 differed from all the other VAR transactions which the Claimants sought to impugn in this case, since it is common ground that it was in writing: there was a collateral letter agreement.

1132. The Claimants' principal complaint is that the side-letter should have been disclosed to Deloitte and was not, and that if it had been disclosed as and when it should have been, revenue recognition would not have been approved by Deloitte. The Claimants also alleged that revenue recognition was improper because Tikit was never intended to on-sell to the named prospective end-user, KPMG. The factual background can be summarised as follows.

1133. Autonomy's forecast revenues for Q4 2010 were $236,000,000. A potential deal with KPMG was listed in an email dated 15 October 2010 from Mr Hussain to Dr Lynch under the stated subject *"getting to 236"* as one of seven "big deals" which Autonomy hoped to close before the end of the quarter. The deal related to an Interwoven product called "iManage". KPMG were an important iManage customer, and the proposed transaction in Q4 2010 was a renewal deal.

1134. Mr Hussain kept Dr Lynch regularly updated on progress, including by emails dated 4 November 2010 and 10 November 2010. Dr Lynch accepted in cross-examination that he

[92] See paragraph 1116(4) above.

knew that Autonomy was trying to conclude this direct deal, and that he knew it was a "*big deal*".

1135. Autonomy was very open about the fact that it needed the transaction to close within Q4 2010. On 10 November 2010, Mr Robert Sass, Autonomy's Senior Vice President, North America Sales, made plain to KPMG that "*In terms of timing, the opportunity to reach contracts by end of year is very key to us*", expressing the hope that the paperwork could be executed in December 2010. His KPMG counterparty, however, said he would be "*surprised if KPMG will move to purchase the solution before the end of the year*".

1136. This was prescient: on 13 December 2010, Mr Mooney informed Mr Hussain that "*KPMG said no*" and that a direct deal with KPMG would not be possible by the end of the year but would be considered in Q1 2011. He added: *"Can pay maintenance. May consider "search" but probably Q1"*. Mr Hussain relayed the bad news to Dr Lynch the same day. On 15 December 2010, Mr Hussain told Dr Lynch that the transaction was "*at risk in my opinion*", though he prefaced this by saying that *"feedback is that they are still working it – getting sign offs"*. He sent a further update on 17 December 2010.

1137. On 23 December 2010, Mr Hussain suggested involving Tikit to Mr Neil Araujo (CEO Protect, Professional Markets at Autonomy). Mr Hussain explained that KPMG were "*squeezing us hard*" and that the decision had therefore been made to wait until Q1 2011 to do a deal. Tikit was (and is) a substantial, publicly listed, technology services company. Dr Lynch's evidence in his witness statement was that it was a long-standing reseller of iManage, an Interwoven product, with a large team of professionals who sold, implemented and supported the product.

1138. On 27 December 2010, Mr Hussain asked Autonomy's in-house lawyers to draw up a contract with Tikit and specified the terms of the contract. The same day (27 December 2010), Mr Hussain wrote to Dr Lynch and Mr Araujo, subject "*tikit deal*", suggesting that it would be a good idea for Mr Araujo to be in the UK to close the transaction and asked "*Agree?*". Mr Hussain plainly expected Dr Lynch to understand what was meant by the "*tikit deal*", i.e. a VAR agreement in circumstances where KPMG had said 'no' to concluding a deal within the quarter. When this obvious point was put to him in cross-examination, Dr Lynch gave what the Claimants said were *"cagey answers"* and claimed, "*I don't know what I knew at that time*" (which the Claimants invited me to find was not so).

1139. On 29 December 2010, Mr Hussain was overseeing the drawing up of contractual documentation with Tikit. He said he needed "*a side letter (which will be disclosed)*", providing that, in the "*highly unlikely event that KPMG do not extend then tikit can resell similar software, part of partnership etc. start with the fact that tikit has been an autonomy partner for many years, many customers…*" . Dr Lynch agreed in cross-examination that the reference to disclosure is likely to have meant disclosure to the auditors.

1140. On 31 December 2010, Tikit issued a purchase order to ASL, for resale to KPMG, with a lower licence fee of £3,847,500 (plus £202,500 support and maintenance). Autonomy recognised the licence fee revenue immediately. The same day, ASL entered into a side letter with Tikit. Illustrating his direct personal involvement, Mr Hussain signed for ASL. After an introduction reciting that Tikit's purchase of Autonomy WorkSite technology was for resale to KPMG, it provided:

> *"In the event that Tikit does not consummate the original transaction to at least the value set forth in the PO by 30 March 2011 then such PO shall be deemed a binding pre-purchase obligation, and Tikit shall be permitted to utilize pre-purchased software under the PO and offset amounts due to Autonomy (to a maximum of £3.1 million) under other orders placed by Tikit related to such software and maintenance under the Agreement for the period between 1 January 2011 and 30 June 2012."*

1141. The Claimants contended that the notion of Tikit consummating a deal with KPMG was a fiction. Tikit was never going to be involved. Rather, it was Autonomy, with the close involvement of Mr Hussain, which continued to negotiate with KPMG in an effort to conclude a direct deal. This provision served to insulate Tikit against the risk that Autonomy failed to conclude an end-user deal with KPMG.

1142. The side letter went on to provide:

> *"Further in the event that Tikit does not consummate the original transaction to at least the value set forth in the PO by 30 March 2011 then Autonomy and Tikit shall enter into an arrangement whereby Tikit shall be appointed as the second line support and maintenance provider to KPMG under the existing maintenance arrangement between KPMG and Interwoven for three quarters from 1 January 2011 for a fee of up to £320,000 per quarter."*

1143. The Claimants invited me to find that this provision for Autonomy to transfer to Tikit support and maintenance fees of up to £960,000 (three quarters @ £320,000), which would otherwise have been payable by KPMG to Autonomy, was simply a mechanism introduced for the sole purpose of putting Tikit in funds to pay its debt to Autonomy, so that *"Once again, Autonomy was going to get (part) paid using its own money."*

1144. Despite Mr Hussain's indication in his email of 29 December 2010 that the side letter would be "*disclosed"*, Mr Welham's evidence was that Deloitte did not see it during its 2010 annual audit. The Claimants sought to suggest deliberate concealment by reference to the alleged falsity of a representation letter dated 22 February 2011 signed by Mr Hussain, in which the directors of Autonomy represented to Deloitte that there were no side letters. The Claimants contended that it followed that the representation in the representation letter was false, must have been known by Mr Hussain to be false, but was relied on as being accurate by Deloitte.

1145. They submitted further that given that the representation was made on behalf of all of the Autonomy directors, the Court should infer that Mr Hussain would have told the relevant facts to Dr Lynch before signing it. They sought also to rely, as further demonstrating concealment, on the fact that it was only much later that the Tikit side letter came to light, not because of any action taken by the Defendants to disclose it, but because Tikit, quite properly, qualified their audit confirmation letter dated 6 July 2011 (which contained a representation that there were no side letters) by attaching a copy.

1146. Mr Welham's evidence in his witness statement was that Deloitte relied upon that representation. Mr Bloomer also said that the Audit Committee was not aware of the letter at the time, and that it would have been relevant to consider its revenue *"implications"*.

1147. The Claimants' case was that the reason for concealing the side letter from Deloitte was that the side letter transformed the nature of the risk being undertaken by Tikit by virtue of its purchase order: on the Claimants' interpretation, instead of making an outright purchase of the software specified in the purchase order and assuming the risk of its resale, Tikit was being insulated by Autonomy against the risk that a resale would not eventuate. The Claimants submitted that the consequence was that risk never passed and that the recognition of revenue was improper accordingly.

1148. The Claimants contended further that the steps proposed and then abandoned, revised and then taken, after the VAR sale to relieve Tikit from having to satisfy in cash its obligations under the VT26 purchase order further demonstrated Autonomy's *"general practice…that [the VAR] should not be left holding the bag"*. They painted a picture of ever-changing but (as they characterised them) invariably improper efforts to unravel VT26:

(1) When in due course Autonomy was approaching the conclusion of a direct deal with KPMG, Autonomy needed to solve the problem of Tikit's outstanding debt. Autonomy therefore proposed to KPMG that contractual language be included whereby Tikit was Autonomy's designated payee. However, KPMG refused to agree. On 10 February 2011, it emerged that the KPMG board was refusing to have a third party such as Tikit introduced into the contract, regarding this as a "*red flag*" and a major problem. The problem was escalated to Mr Hussain. Dr Lynch's evidence that KPMG did not wish to purchase from Tikit because it audited Tikit's accounts was not challenged.

(2) In light of the deal going direct to KPMG without (at KPMG's insistence) Tikit's involvement, Mr Hussain appears to have been willing at one stage simply to cancel Tikit's obligations. On 7 March 2011, Mr Scott emailed Mr Kanter and Mr Chamberlain stating that "*Sushovan asked me to prepare a cancellation notice for Tikit in connection with its KPMG order... Sushovan also asked me to have a look at what we did with Capax/Kraft an [sic] Capax/Eli and to use that as a model*", and attaching a draft termination letter. As the Defendants observed in their written closing submissions, this would have resulted in a similar outcome, and for similar reasons, as the Capax Discovery/Kraft deal in Q3 2009 (VT3), which Deloitte had reviewed and understood. But in the event this route was not adopted.

(3) Instead, and after an Autonomy entity, Verity Benelux BV, had entered into a direct agreement with KPMG for $10,796,860 on 21 March 2011, the arrangements envisaged in the side letter were restored. On 28 April 2011, Mr Chamberlain (copying Mr Hussain) asked Ms Julie Dolan, Autonomy Senior Corporate Counsel, to draft a letter to be signed by Tikit and Autonomy. He explained the rationale as follows:

> *"When they issued the PO in Dec we also signed a letter effectively allowing them to repurpose if the KPMG deal did not close via them. They have received a bunch of orders for circa £1.5m. They want to offset those against the o/s debt which we are happy to do. Effectively the £4m will act like a prepay and they will allocate orders to burn through it. Need a document that captures this."*

(4) The Claimants submitted that this explanation makes little sense. They submitted that to say that the £4 million would act as a "*prepay*" overlooks the obvious problem that Tikit had, to date, paid nothing (disregarding the offset of Autonomy's own entitlement to maintenance fees from KPMG). It had not prepaid but rather incurred a debt: far from Tikit discharging that debt by placing further orders from third parties for Autonomy software, on its face, such orders would create additional debts on the part of Tikit, rather than discharging a pre-existing debt.

1149. What in the event happened is that a series of letter agreements were entered into between ASL and Tikit, which recited the provision of the side letter and then set out various lower value deals which Tikit had concluded for sales of Autonomy software to many different end-users. The letter agreement then recorded that the value of those lower value deals would be offset against Tikit's obligations under VT26. There are two such letter agreements dated 27 May 2011, and subsequent letter agreements dated 7 June 2011 and 20 June 2011. The offsetting process seems to have continued until 28 November 2011 until the figure of £3,089,825 (i.e. the total amount due under the purchase order less £960,000 treated as already paid, as explained below) had been reached.

1150. As part of its direct deal with KPMG, Autonomy agreed to pass to Tikit the benefit of £960,000 in maintenance and support fees that would otherwise have been received by Autonomy from KPMG. Rather than have the money going round in a circle, Tikit was not paid the £960,000; rather, Autonomy simply offset the £960,000 against the monies due under VT26. The Claimants maintained that there is no evidence that Tikit actually provided maintenance and support to KPMG; and that indeed, the provision of such services would fly in the face of KPMG's opposition to the interposition of a third party. The Defendants reminded me that Tikit's business was as a service provider for iManage, and that KPMG's opposition was simply to acquiring software from Tikit, not services, but did not provide further evidence. It seems to me more likely than not, and I find, that this was a means devised by Autonomy in order to ensure that Tikit was not exposed.

1151. The Defendants, on the other hand, submitted that the Claimants had misunderstood: the commercial intent was in line with the side letter; Tikit was able to repurpose the software purchased under the Tikit/KPMG agreement towards other orders, up to the agreed value.

1152. The essential points stressed by the Defendants, and which they suggested had been overlooked or mis-appreciated by the Claimants, were that (a) Deloitte were in fact aware of the side letter in April 2011, but even if they were not (b) the side letter did not make any difference to the revenue recognition, and (c) when in 2012 Deloitte re-reviewed it, they expressly confirmed that it did not. The Defendants contended that (d) Tikit remained liable for the debt under VT26, though it would have the repurposed sales to fund the debt partially.[93]

1153. These points were supported by submissions on the part of the Defendants that:

(1) The Claimants' suggestion with regard to the side-agreement that "*the notion of Tikit consummating a deal with KPMG was a fiction*" is misplaced. The overwhelmingly likely view on the evidence is that both Tikit and Autonomy

[93] D1 closings suggests still liable and could repurpose up to agreed value, but not that it was to fund the debt.

did envisage that Tikit would receive a purchase order from KPMG. The Claimants' fallacy (here and elsewhere) was to assume that the fact that Autonomy may have continued in negotiation with the end-user meant that it was not contemplated that the reseller would be involved in the end-user deal.

(2) Neither the side letter, nor the subsequent arrangements made further to the side letter after a direct deal was reached between Autonomy and KPMG, affected the initial recognition of revenue in respect of VT26. None affected the initial incidence of risk: Tikit as the VAR was on risk until released by the offsetting arrangements *pro tanto.* None of the arrangements affected Tikit's control of the goods; and it is to be noted that Tikit recorded the Autonomy software in its audited accounts as inventory, reflecting its understanding that it was on risk and the owner of the software.

(3) When Autonomy made a direct deal with KPMG in respect of substantially the same software as was the subject of VT26, from which Titkit was excluded at KPMG's insistence, it was only right that Titkit, having been deprived of its prospective end-user deal, should in some way be made good. A solution might have been simply to forgive the debt due under the VT26 purchase order, on the lines of what happened in VT3 (the Kraft deal), which Deloitte had approved. However, given the specific terms agreed at the outset in VT26 in the side letter, that was the route eventually taken.

(4) Contrary to the Claimants' efforts to present what was done as making no sense, the arrangement contemplated in the side letter and implemented broadly in accordance with it was an entirely proper and rational arrangement which, in effect, enabled Tikit to sell on software that it had acquired, and thereby with the proceeds of sale reduce its indebtedness to Autonomy (up to a pre-specified limit).

(5) The offsetting arrangements were proper and practical; and they were carefully documented. Mr Chamberlain provided Deloitte with the running state of the offsetting arrangements between Autonomy and Tikit, showing Autonomy invoices to iManage customers which had obtained software from Tikit.

(6) The subsequent sales were correctly and properly treated by Autonomy as pre-paid: having already received and recognised revenue under the original VAR sale in VT26, it would have been double-counting to recognise revenue in respect of the subsequent sales of the same software albeit that Autonomy invoiced for them.

(7) Although the Claimants had omitted altogether to mention it, when in 2012 HP asked Deloitte to reconsider the revenue recognition of VT26 in the light of the side letter which Mr Welham stated they had not seen at the time, Deloitte specifically endorsed the revenue recognition decision and confirmed that the side letter did not make any difference to revenue recognition. Mr Welham also confirmed in cross-examination that his conclusion was that the revenue should not be adjusted as at 31 December 2010 because the criteria under IAS 18.14 had been met. Although Mr Welham suggested in his witness statement that the side letter "*cast doubt on whether all of the revenue on the transaction with Tikit could be recognised*", he confirmed in his testimony that the side letter would not in fact have made any difference to the revenue recognition. That was

his view both in 2012 and now.[94] He explained this in cross-examination as follows:

> *"That's correct, because ultimately we saw this as a pre-payment, but they could only on-sell the software they had, which is an important point, so yes, in that case it doesn't affect it."*

(8) If, as Mr Welham stated in evidence, Deloitte were not provided with the side letter to review during the 2010 annual audit, that was not deliberate concealment: it was a regrettable oversight on the part of Autonomy's finance department. All Autonomy's files were open for inspection for Deloitte, and the Defendants submitted that there was no evidence of any deliberate attempt to conceal the side letter. As explained below, Autonomy were open with Deloitte about the side letter in subsequent months. Mr Welham accepted that Deloitte would in any event have known about the side letter in Q1 2011 if they had required earlier audit confirmation.[95] Tikit, entirely properly, identified the side letter in its audit confirmation letter to Deloitte dated 6 July 2011.

(9) Furthermore, the evidence suggests that Deloitte understood about the side letter and its terms by or before July 2011. When Deloitte were considering whether revenue could be recognised on Autonomy's direct deal with KPMG their review stated:

> *"It was noted that in Q4 2010, a £4 million license (c. $6 million) was signed with KPMG via the VAR Tikit Limited (documented in PY Q4-8130c). Deloitte has compared the software purchased in Q4 with the current deal and noted that the majority of the Q4 software purchased, including the maximum number of named users (WorkSite, AES, IUS Enterprise) has also been included in the current deal, which is a direct sale with KPMG. This direct sale by Autonomy therefore replaces the sale previously being made by Tikit to KPMG. PDW Steven Chamberlain (VP Finance), as stated in the December 2010 VAR agreement, the VAR may resell the software to another end-user and it has the legal obligation to pay for the license fee and therefore it is up to the VAR to reassign the software if required. Given that under the current deal, Autonomy has delivered the software to KPMG and we have assessed the recoverability of this Q1 deal as being satisfactory (see below), the current contract meets the requirements of IAS18 and therefore the revenue recognition is considered satisfactory."*

The point in this context is that the right to "resell the software to another end-user" that Deloitte were referring to was contained in the side letter (and

[94] Mr Welham was also asked to assume that Autonomy had cancelled its purchase order with Tikit in March 2011. In fact, Autonomy did not do so, so the assumption was misplaced. In any event, however, Mr Welham thought that it was hard to say what difference it might have made if this had happened.

[95] "*Q. Now, if you had required a confirmation in Q1, no doubt you would have found out about this letter at that point? A. That's likely, yes.*"

only there), strongly suggesting that Deloitte must have seen the side letter before July 2011.

(10) In summary, the initial revenue recognition was proper at the time; it was considered proper when later reviewed; and nothing in the subsequent arrangements affected that or, more generally, was itself improper or lacking in commercial rationality.

My assessment of VT26

1154. In my view, the propriety of revenue recognition in this VAR transaction primarily hinges on whether the Claimants' allegation that the notion of Tikit consummating a deal with KPMG was a fiction and that Autonomy, directed by Mr Hussain in this regard, always intended that Autonomy itself would conclude a direct deal with KPMG. If so, it seems that what Autonomy intended was that Tikit's introduction was simply to enable Autonomy to book revenue, without any expectation of an end-user sale by Tikit, rendering Tikit's ownership economically nominal. Further, on that basis, the side letter contained a plain and intentional misrepresentation, casting a darker shadow over Autonomy's failure, if proved, to disclose it to Deloitte and the Audit Committee.

1155. If, in addition, Deloitte were also subsequently misled as to the effect of the side letter that would, of course, further exacerbate the position, and remove a plank of the defence.

1156. As in the case of VT15, the evidence was sparse: Mr Welham did address VT26 (he had not addressed VT15); Dr Lynch mentioned it too, and so did Mr Bloomer; but no-one gave evidence in these proceedings or elsewhere on behalf of Tikit, nor for KPMG, in respect of the transaction. The documentary record was more revealing generally; but it too was sparse as to the nature and objectives of the discussions between Autonomy and KPMG.

1157. I do not consider that the available evidence demonstrates that Tikit understood that it was not to be involved in any resale, though I think read as a whole it suggests that it is more likely than not that it had no intention or expectation of being so. However, more importantly, it does seem to me more likely than not, having regard to the documentary evidence as a whole, that Mr Hussain always envisaged and intended a direct deal between Autonomy and KPMG: a resale by Tikit to KPMG was never seriously in his contemplation. The side letter he caused to be prepared, which gave the clear impression that a direct sale was perceived and understood by both parties to be the less likely result, was misleading: I would indeed accept that, as far as Mr Hussain was concerned it was a fiction.

1158. Whether or not Deloitte somehow came to know of the side letter in 2011, it should have been but was not disclosed to them. There is no plausible satisfactory explanation, to my mind, why Mr Hussain did not cause the side letter to be disclosed to Deloitte, having given an express assurance that it would be. Of course, in a busy life, oversights are possible, even frequent; but on the Defendants' own case, a side letter was highly unusual and ordinarily proscribed, and a representation letter is a serious matter, and it is to be inferred, in my judgment, that in signing the representation letter he would surely have been aware or reminded of the assurance he had given. I accept in its favour that Autonomy did have an "open files" policy; but that did not negate or satisfy the assurance Mr Hussain had given that the side letter would be disclosed to Deloitte or justify the terms of the representation letter given by Autonomy's Directors to Deloitte.

1159. Having (as I have) rejected oversight as the explanation, I consider it more likely than not that it was considered by Mr Hussain to be easier to present the VAR deal without the side letter, even if he might have been reasonably confident that if revealed, it was sufficiently equivocal that it could be presented as not affecting the result, as indeed Deloitte concluded when eventually it was disclosed by Tikit.

1160. Quite how Deloitte interpreted the letter and came to its view that it made no difference to revenue recognition is not easy to understand. It was certainly acted upon by Tikit as effectively permitting them to set against the amounts owed in respect of VT26 any sales of Autonomy software they thereafter negotiated. What in the event happened is that a series of letter agreements were entered into between ASL and Tikit, which recited the provisions of the side letter and then set out various lower value deals which Tikit had concluded for sales of Autonomy software to many different end-users. The letter agreement then recorded that the value of those lower value deals would be offset against Tikit's obligations under VT26. In other words, the original deal was, in the language of Mr Chamberlain "repurposed". The "offsetting" process seems to have continued until 28 November 2011 until the figure of £3,089,825 (representing the total amount due under the purchase order less the £960,000) had been reached. But it is not clear whether (a) the software sold by Tikit came from its own 'inventory' or from Autonomy or (b) whether any receipts were actually paid over by Tikit to Autonomy.

1161. Certainly when the position was reviewed in October 2012 Ms Antonia Anderson (formerly of Deloitte but by then employed by HP) assumed no such payment, her understanding being that:

> *"…as Tikit submitted additional orders, Autonomy delivered software for these orders but did not charge Tikit and created zero value orders and invoices as these orders were fulfilled. The attached excel shows which orders were set against the prepay. As you can see there was a large number of small orders."*

1162. However, this made no sense: there had been no "prepayment" by Tikit under VT26. When consulted by Ms Anderson in October 2012, Mr Welham gave a different explanation of the side letter. He said that, in his view, the side letter as written permitted Tikit to resell the <u>same</u> software to users other than KPMG. Even allowing for confirmation bias and the considerable pressures on Deloitte (and Mr Welham personally) by that time to confirm the decisions on revenue recognition which had by then been made and acted upon, I do not consider that the evidence gainsays this assertion of Deloitte's own understanding. Right or wrong, the point is that Deloitte's understanding of what was permitted was not what occurred; and on that basis its approval of revenue recognition was based on a mistaken understanding.

1163. I have concluded, though not without hesitation, that the reality known to Mr Hussain was that the economic risks of ownership and management of the software were retained by Autonomy, and in the event that happened, Tikit was (not unnaturally) content that this was so.

1164. In my judgment, revenue should not have been recognised from VT26.

Defendants' knowledge of and participation in VT26 and subsequent arrangements

Mr Hussain

1165. The Claimants submitted that Mr Hussain, again, knew all the relevant facts. Moreover, they submitted that *"he must have taken the decision not to disclose the side letter to Deloitte, as he unquestionably should have done."*

1166. Mr Hussain could not dispute his knowledge of the facts, but he did dispute the allegation of deliberate concealment. He submitted that there was no reasonable basis on which to draw an inference that there was any concealment by Autonomy. Dr Lynch sought to assist him in the course of his own cross-examination:

> *"…by the way, it wouldn't have been Mr Hussain that was responsible for handing over that file. That would have been the legal department."*

1167. I do not accept that Mr Hussain did not himself hold the letter back. He had promised its disclosure. It was for him to see that this was done. In my judgment, Mr Hussain was personally and directly involved at all relevant stages. I have already found (see paragraph 1157 above) that as far as Mr Hussain was concerned the side letter was to an important extent a fiction. I think it more likely than not that he chose to keep it back from Deloitte for fear that it would prejudice revenue recognition: and I so find.

1168. In my judgment, it follows also that Mr Hussain knew that revenue should not have been recognised from the transaction and he had "guilty knowledge".

Dr Lynch

1169. As regards Dr Lynch, the Claimants submitted baldly that:

> *"the likelihood is that Mr Hussain kept Dr Lynch informed or, at the very least, was acting within the scope of what Dr Lynch had authorised him to do, namely to recognise revenue improperly, as and when required."*

1170. Dr Lynch accepted that he received occasional updates on the status of the KPMG renewal deal. He may also have been aware that Mr Araujo of Autonomy was meeting with Mr Lumsden of Tikit. However, he told me that he was not involved in the sale to Tikit, did not participate in the negotiations and neither reviewed nor approved the terms of the transaction.

1171. Dr Lynch said that he did not recall knowing about the side letter at the time but on reviewing it for his witness statement he did not regard it as untoward. His position was that he was not involved in the revenue recognition, and had no reason to think there were any material issues with the accounting.

1172. Dr Lynch was cross-examined about this transaction:

(1) He did not accept the proposition that Mr Hussain's email dated 13 December 2010 forwarding Mr Mooney's email of that same date headed *"KPMG said no"* (see paragraph 1136 above) meant that KPMG would not do the deal. He pointed out that KPMG were still a prospect later in December (as emails later in December confirmed).

(2) It was not suggested that Dr Lynch had seen or reviewed the side letter.

(3) Dr Lynch was referred to Mr Hussain's representation letter at paragraph 1144 above. As to this:

(a) Dr Lynch did not think he would have reviewed this letter at the time. The Claimants did not identify or put to him any document demonstrating that he did do so.

(b) Although he was not involved in this aspect, when asked about it, Dr Lynch did not accept that the side letter had not in fact been disclosed to Deloitte. As explained at paragraph 1153(9) above, Deloitte did seem to know of the terms of the side letter, at least by April 2011. In any event, he suggested that this was in substance a representation about there being no undisclosed side letters and that disclosure would have been a matter for the legal department.

(c) Dr Lynch was asked "*Would Mr Hussain have discussed with you whether you should sign this representation letter despite the existence of a side letter from Tikit?*" Dr Lynch rejected this; and no evidential basis was advanced for it.

(4) It was suggested that Dr Lynch knew that "*no revenue should have been recognised on the Tikit transaction*". The Defendants submitted that it was unclear how Dr Lynch could have known this, given that:

(a) it was not suggested to him that he knew of the side letter, and

(b) when Deloitte (who were the experts) did consider the side letter they did not think that the revenue should not have been recognised.

(5) When it was put to him that he *"knew, just as with those earlier transactions, no revenue should have been recognised on the Tikit transaction either"*, Dr Lynch summarised his position as follows:

> *"A. That's incorrect, and of course when Deloitte -- when it's not in dispute that Deloitte do see the amendment which is a quarter later, they consider it has no effect on the revenue recognition and the revenue stands in any case. And then, when HP takes over Autonomy, it puts a lot of pressure on Deloitte to reverse this revenue and move it into the future, into their future books, and Deloitte resist that and they say that the revenue was fine. So everything I've seen about this transaction leads me to believe that actually whether or not Deloitte saw the paperwork, all of it, at the time -- and I believe they did -- that it made no difference anyway."*

1173. In my assessment:

(1) It is unlikely that Mr Hussain did not inform Dr Lynch of the side letter, though he may not have detailed its terms. It was an important feature of the transaction, in which he was keeping Dr Lynch otherwise informed, and which was a large

one. It would have been both risky for him and unnecessary, given their shared objectives and strategy, to keep this from Dr Lynch.

(2) I do not accept that it was not sufficiently put to Dr Lynch that he knew of the letter. The thrust of the questioning was to demonstrate that he did know of it and (for example) should have made reference to it in the Directors' representation letter to Deloitte.

(3) I do not accept either that Dr Lynch was unaware of the relevant part of the representation letter. The way matters were presented to Deloitte was an important part of the VAR strategy, and I think it more likely than not that Mr Hussain would have alerted him to it. But even if he did not read it and was unaware of its content, my view that he was aware of the thrust of the side letter would still stand.

(4) Both Dr Lynch's quick intelligence and his opportunism were displayed by the debate he had with Mr Rabinowitz as to whether the representation contained a typographical error of some significance. The relevant representation, as it appeared, read as follows:

> *"No revenue deals containing side letters of ongoing Autonomy performance requirements…"*

It was suggested to him that the word *"of"* was an obvious typographical error and should have been *"or"* and that was how Mr Welham had understood it also. After the smallest pause to read, Dr Lynch said *"No, I think it's 'of'"*. He added that:

> *"Again, I'm reading this now but I think it's a clause to make sure that Autonomy doesn't have ongoing performance requirements that it hasn't disclosed."*

This was ingenious, but not, in my view sustainable: there was an obvious error. Corrected, it was an obvious misrepresentation, all of a piece with the desire that the letter not be disclosed.

1174. In my judgment, though there is, not unusually, little transaction-specific evidence of Dr Lynch's involvement or of what he was told or saw, the Tikit transaction (VT26) fell within the pattern which implemented the strategy instigated and encouraged by Mr Hussain and Dr Lynch, in the context of which Mr Hussain habitually reported regularly to Dr Lynch. In my judgment, it would be contrary to their usual *modus operandi* for Mr Hussain to have kept from Dr Lynch the fact of the side letter arrangements; and even had he done so, it would be more likely than not, in all the circumstances, that Dr Lynch would have assumed something similar to have been put in place in accordance with the usual pattern.

1175. Having regard to the standard of proof, I have concluded that Dr Lynch also had guilty knowledge that VT26 should not have been accounted for as giving rise to recognised revenue at the point of the VAR sale.

VT14: Auxilium/Vatican Library (Q1 2010)

1176. In addition to the MicroTech VAR deal for end-user Vatican Library in Q1 2010 (VT13), ASL entered into a VAR deal dated 31 March 2010 with Auxilium Tech SrL ("Auxilium", another Italian reseller). The VAR Agreement was signed on behalf of ASL by Mr Kanter.

1177. A Product Schedule was signed by Mr Kanter bearing a Commencement Date of 31 March 2010 (clause 20). That stated a licence fee of €2.5 million plus €125,000 for support and maintenance (clause 17), both payable within 120 days. The authorised use of the software in the Auxilium purchase order was limited to the Vatican Library digitisation project (clause 8), permitted 10 concurrent users (clause 10) and the territory of software installation was the Vatican Territory (clause 11).

1178. It appears that, as at 31 March 2010, the total licence revenue recognised by Autonomy on this purchase was only €1,300,000 ($1,858,024), and that no further revenue ultimately ended up being recognised as at the end of Q2 2010.

1179. As noted in their Report to the Audit Committee on the Q1 2010 Review dated 20 April 2010, Deloitte considered that any revenue recognition at all on this transaction and a transaction with another Italian reseller should be deferred until *"management has more clarity on recoverability".* Autonomy management, and in particular Mr Chamberlain rejected this, but failed to persuade Deloitte otherwise.

1180. In the event, Auxilium never did pay any amount to Autonomy, and the whole invoice value was written off in ASL's general ledger on 30 September 2011 (bad debt provisions having previously been recorded).

1181. Although falling within the description of a *"Collectability VAR"*, in that the Claimants did not aver any side-agreement and relied principally on Auxilium's doubtful ability to pay and thus an alleged failure to satisfy IAS 18.14(d) in respect of VT14 as the ground for impugning it, the Claimants also argued that neither IAS18.14(a) nor IAS18.14(b) was satisfied either. Their position was that, contrary to the way in which Mr Chamberlain presented the transaction to Deloitte (he asserted that Auxilium would be receiving payment from the end-user before it became liable to pay Autonomy), there is no evidence that Auxilium ever had any involvement with the Vatican Library, let alone any basis for expecting to be paid by it.

1182. The Claimants invited me to conclude that it was never intended that Auxilium should make any attempt to achieve a sale to the Vatican Library and, in any event, that Auxilium did not in fact make such an attempt. That fed into the Claimants' primary allegation that the debt was not collectible contrary to IAS 18.14(d) (since on that basis, Auxilium could not expect to receive any imminent payment from an end-user) but also was contended to show that in fact Autonomy retained risk and control, contrary to IAS18.14 (a) and (b). Thus, collectability and the other provisions of IAS 18.14 are inextricably linked, as Mr MacGregor acknowledged.

1183. This is illustrated by the way that Autonomy sought to persuade Deloitte of the credit-worthiness of Auxilium. Mr Chamberlain described Auxilium to Deloitte (in an email dated 16 April 2010) as *"a reasonably sized VAR with significant revenues and assets".* This, together with the knowledge he asserted from being *"very close to the negotiations of the end-user deal with BAV"* that *"they are expecting to receive payment from BAV on May 15th"*, which he stated *"provides us with the comfort to recognise the deal."*

1184. In fact, and contrary to what he told Deloitte, the financial information about Auxilium available to Autonomy was slim: and Mr Chamberlain had that same day (16 April 2010) described its 2008 financial statements to Mr Corrado Broli ("Mr Broli"), the Autonomy sales executive covering Italy, as *"not strong enough to support revenue recognition on their own"*.

1185. Even so, that same day (16 April 2010), Deloitte's refusal to approve revenue recognition and their production of an updated misstatements schedule, which included the revenue on the Auxilium purchase order provoked an immediate and aggressive response from Mr Hussain. Despite Mr Chamberlain's acknowledgement in his email to Mr Broli that revenue recognition could not be supported on the basis of the 2008 financial statements on their own, Mr Hussain wrote to Deloitte the very same day (16 April 2010) pressing for full recognition:

> *"Auxilium- No way am I accepting this as a judgmental item, you have the financials, you have the confirmations. These companies have quite sizeable revenues ($15m) and are profitable. They can resell $2m of software and we can't simply assume that a properly signed contract is not recognizable when there is good evidence. Many private companies keep small amounts of cash but are profitable and cash generating."*

1186. This was bluster. The truth is that Auxilium had never produced, and in the event never did produce, robust financial information. The impression of frailty was reinforced by Auxilium's failure to provide more up-to-date accounts, which even Mr Hussain described as *"very disappointing"*.

1187. Further, Mr Chamberlain's assertion that Auxilium was expecting to receive payment from the Vatican Library on 15 May was also not true. As I have found in relation to VT13 (the MicroTech/Vatican Library VAR transaction), all efforts to conclude a contract for the Vatican Library digitisation project were being undertaken by Autonomy with a view to a co-ordinated direct deal between Autonomy and the Vatican Library. I consider and find that there was never any real intention or expectation of Auxilium re-selling to the Vatican Library, and thus no real prospect of receipts from such a sale.

1188. Although I accept that this would not ordinarily affect a decision on grounds considered sufficient at the time to recognise revenue, the fact is that Auxilium did not meet its payment obligation under VT14 due on 29 July 2010. Even so, Mr Hussain continued over that time to seek to persuade Deloitte to reverse their decision to refuse recognition. In the event, Auxilium never made any payments to Autonomy at all. The whole invoice value was written off in ASL's general ledger on 30 September 2011 (bad debt provisions having previously been recorded). The correctness of Deloitte's contemporaneous view was thereby reinforced; and Mr Hussain and Mr Chamberlain's efforts to overturn it appear reckless.

1189. Mr Holgate arrived at the same conclusion as Deloitte that no revenue should have been recognised. Mr MacGregor did not go further in his expert report than to say that *"there was insufficient information to reach the conclusion that Autonomy's accounting treatment in respect of the licences was inappropriate"*: allowing for the benefit of hindsight, I do not agree. There was at the time no sufficient basis for revenue recognition, as the misrepresentation of the actual position to Deloitte suggested.

1190. This conclusion is also supported by the curiosity identified by the Claimants in their written closing submissions that all of the software identified in clause 1 of Auxilium's Product Schedule – LiquidOffice, FITS PlugIn, SPE, Mediabin and Archive Solution – was already included in the MicroTech for end-user Vatican Library purchase order (VT13) signed on the same day and for exactly the same authorised use. The MicroTech purchase order permitted 200 concurrent users (clause 9), which reflected the number of users in the draft licence agreement that Autonomy hoped to conclude with Postecom. The Claimants' (readily understandable) point is that it is difficult to understand, therefore, what the point would have been of selling Auxilium a licence to use a subset of identical software, but for an additional 10 users, and that they would have wished to explore this with Mr Zanchini in cross-examination, given Mr Zanchini's personal involvement in the Vatican Library project, but for Dr Lynch's decision not to call him. All of this appears to me to confirm the artificiality of VT14.

Defendants' knowledge that revenue should not have been recognised from VT14

1191. In my judgment, Mr Hussain knew that in reality Auxilium was not expected to enter into an end-user deal which was its only realistic prospect of being able to pay Autonomy under the VAR agreement. He had "guilty knowledge".

1192. The Claimants' case that Dr Lynch also had such knowledge is once again based on the submission that Mr Hussain was *"acting within the authorisation he had received from Dr Lynch to use non-creditworthy VARs to recognise revenue improperly"*. I would not accept that Dr Lynch gave such authority in such unlikely terms. No evidence was ever produced showing or even suggesting his involvement in the collectability judgement made. However, that does not conclude the matter.

1193. I have found that Dr Lynch did know that the VARs were used as placeholders. Given his close interest and involvement in the Vatican Library deal, it seems to me more likely than not that he appreciated that Auxilium would not be entering into any end-user deal and more generally had nothing to offer and no role to play except as a placeholder. He had no reason to believe that Auxilium could pay out of its own resources; and I consider it very unlikely that he was not told of Deloitte's decision to refuse revenue recognition, and Mr Hussain's reckless and unsuccessful efforts to make them change their mind. In my judgment, this amounts to "guilty knowledge", and I find accordingly.

PART V OF SCHEDULE OF IMPUGNED VAR TRANSACTIONS

The "Collectability VARs": VAR deals impugned but no side agreement is alleged

1194. As regards five of the impugned VAR transactions the criticism the Claimants made of the revenue recognition is on collectability grounds. No side agreement is alleged to have been made. The Claimants based their claims on the basis that the requirement of IAS 18.14(d), being that *"it is probable that the economic benefits associated with the transaction will flow to the entity"* was not satisfied.[96] The Claimants referred to these as the *"Collectability VARs"*.

[96] Though in the case of VT29, a support and maintenance contract, the relevant equivalent provision is IAS 18.20(b).

1195. The Defendants sought generically and quickly to dismiss these claims as misplaced on the basis that collectability was a judgemental issue; and that, as they put it, if there were any errors in the judgements made, it is not easy to see how this is the territory of a fraud claim.

1196. Further, Dr Lynch submitted that in any event there was no evidence to show that he was involved in the collectability judgement and in point of fact he was not. Collectability judgements were being made by the finance department and scrutinised by Deloitte. In such circumstances, there could be no basis for a claim of dishonest participation against Dr Lynch.

1197. The "Collectability VARs" as described in Schedule 3 of the RRAPoC were:

(1) Sales Consulting SRL / Poste Italiane (Q4 2009) (VT9);

(2) Comercializadora/ TV Azteca (Q3 2010) (VT17);

(3) Red Ventures / Poste Italiane (Q3 2010) (VT19);

(4) Comercializadora/CISEN (Q4/2010) (VT22); and

(5) Computer Trading / Poste Italiane (Q1 2011) (VT29).

1198. Although I address these individually below, certain introductory remarks in relation to this category of impugned transactions may assist to set the scene:

(1) In none of these cases did an end-user deal eventuate; whilst that could not be known in advance, the fact is that in each of them, the prospect of any such end-user deal appeared problematic and unlikely. Revenue from an ultimate end-user sale was thus uncertain at best; and last-minute recourse to the VAR was not in real anticipation of an end-user sale but simply to book revenue regardless. The onus was on collectability from the VAR.

(2) Whereas Dr Lynch characterised collectability as a judgmental issue for the finance department, in the context of which a difference of view, and even a plain error of judgement, would not of itself begin to constitute fraud, the Claimants contended that the real vice was that those directing the transactions at Autonomy knew that the VARs in question obviously had not the means to pay, never did pay, and in one case at least may not even have existed.

(3) The essence of the Claimants' case is thus that in fact all Autonomy was doing was "parking" deals with companies for which there was no or no sufficient evidence of creditworthiness or substance simply because of an urgent need to book more revenue: the focus is really on whether the deals were contrived rather than on collectability as such.

(4) The Defendants also stressed that the issue of collectability and the judgements made at Autonomy which were questioned were not concealed or misrepresented, but discussed openly with both the Audit Committee and Deloitte. The Defendants contended that such openness destroyed the Claimants' case of dishonesty, and also emphasised the immaterial amounts (in an accounting sense) which were involved ($10,716,796 in aggregate). The Claimants answered this by contending that misrepresentations were made to both the Audit Committee and Deloitte, and in any event, Autonomy repeatedly

went against Deloitte's advice, demonstrating determination to take revenue from these VAR deals notwithstanding clearly expressed doubts. According to the Claimants, the figures might be immaterial but the light cast on the practices allegedly directed and sanctioned by the Defendants respectively was not.

(5) There was also a dispute as to the burden of proof, on which the parties' respective experts also appeared to differ. In essence, the Claimants contended that since under IAS 18.14(d) the burden lies on the party seeking to recognise revenue, if there was no evidence put forward now to support collectability, the burden should not be treated as discharged, and recognition should be regarded as improper. On the other hand, the Defendants and Dr Lynch's expert, Mr MacGregor, contended (in effect) that the presumption should be that there was sufficient evidence at the time, and the burden should be on the Claimants to dislodge the judgement made at the time.

(6) The Claimants cross-examined Dr Lynch relatively briefly on the Collectability VARs, and the documentation they put forward did not overtly show or suggest any involvement on his part. In answer to the Defendants' submission that there was no evidence of Dr Lynch's involvement or knowledge, the Claimants contended that though questions of collectability were primarily considered by Mr Hussain and Mr Chamberlain, often alongside Mr Kanter, rather than by Dr Lynch, it is not credible to suggest that Mr Hussain, Mr Chamberlain and Mr Kanter would have acted in the way that they did in relation to these transactions, unless they believed that Dr Lynch had authorised them to do so. Accordingly, the court should infer that Dr Lynch authorised Mr Hussain to call upon non-creditworthy VARs as and when required to deal with shortfalls in Autonomy's revenue targets, and to recognise revenue improperly on the basis of transactions with such VARs notwithstanding failure to comply with the requirements of IAS 18.14(d). Put shortly, the Claimants' case against Dr Lynch relied on the proposition that:

> *"It is not credible to suggest that Mr Hussain, Mr Chamberlain and Mr Kanter would have acted in the way that they did in relation to these transactions, unless they believed that Dr Lynch had authorised them to do so."*

VT9: Sales Consulting SRL / Poste Italiane (Q4 2009)

1199. In October 2009, Mr Corrado Broli ("Mr Broli"), the Autonomy sales executive covering Italy, reported by email to Mr Hussain that he was pursuing two potential deals involving Poste Italiane, the Italian postal service. Mr Hussain observed in an admonishing response that only one had any prospect of coming to fruition:

> *"Corrado - you have not sold a deal with standard cash collection for the last few years - this is very bad. The only deal that is worth forecasting is the Interwoven deal which I am uncomfortable allowing any commission share. All the other deals have been forecast for many many quarters and I do not believe any of them. This is a serious issue which I want you and Nigel to address and come back to me as to the solution."*

1200. The evidence is sketchy: but it seems likely that Mr Broli's response was to engage a reseller to establish a sale with a view to on-sale to Poste Italiane. On 4 January 2010, Mr Broli sent the purchase order dated as of 31 December 2009 in the sum of €1,725,000 (including €225,000 for maintenance) to an Autonomy lawyer and asked her to "*convert*" it into what he called a "*one shot*" agreement.

1201. This resulted in the execution of an "*Autonomy One-Off Reseller Agreement*" between ASL and Sales Consulting for end-user Poste Italiane. The letter agreement stated at the top, "*effective 31 December 2009*". However, it must have been executed on or after 4 January 2010 (since it was not until then that an Autonomy lawyer was asked to draft it).

1202. In both their opening and closing submissions, the Claimants appeared to be suggesting that the letter agreement was improperly backdated. But this was not pleaded, and no such allegation was put to Dr Lynch. Further, the letter agreement is not otherwise dated and there is no pretence that it might have actually been executed on the effective date. As was emphasised in Mr Hussain's written closing submissions, and as Mr Welham accepted in cross-examination, an agreement in writing is not required for the purposes of revenue recognition pursuant to IAS 18.14, and there is nothing in itself wrong in documenting a transaction after the quarter end if the substance was agreed in the previous quarter. I do not consider that a suggestion of improper backdating is available to the Claimants, and I draw no inference of impropriety in respect of this aspect of the matter.

1203. Nevertheless, the VT9 transaction was somewhat haphazard from the start. The One-Off Reseller Agreement stated that "*Reseller should only place an order with Autonomy when Reseller has received an order from an End-User*". The Agreement also required proof of "*sell through*" by Sales Consulting to Poste Italiane on all orders in excess of $100,000. Shipment was to be made "*upon receipt of a valid purchase order*". No proof of "*sell through*" to Poste Italiane was provided to Autonomy. Thus, the purchase order did not meet the contractual requirements established by Autonomy for a valid order in the first place. There was no evidence of any effort to put in place a *"sell through"*. There is no substantial evidence that there was ever any settled prospect of a sale to Poste Italiane (and none eventuated).

1204. The somewhat haphazard documenting of the transaction was matched by the makeshift and unsatisfactory correspondence with Sales Consulting after the sale. It seems clear that there were difficulties in pinning Sales Consulting down from the start. In January 2010, Autonomy made several attempts to obtain an email address for, and financial information regarding, Sales Consulting:

(1) On 11 January 2010, Mr Chamberlain asked Mr Broli to provide an email address for it. Mr Broli provided a gmail address. On 12 January 2010, Mr Chamberlain responded, "*I cannot use a gmail address. If this is a proper organization they will have a proper e-mail address. I need that please*".

(2) On 13 January 2010, Mr Chamberlain emailed Mr Broli (copying Mr Hussain) to say, "*desperately need financials and evidence of how good they* [Sales Consulting] *are for the money. Also, still need a proper email address*". Mr Hussain followed up on the 18 January 2010 in similar vein: "*We have no information on this company ...*"

(3) On 21 January 2010, Mr Broli reported that Sales Consulting had been founded on 30 July 2009 (five months before the Sales Consulting deal) and had revenues in 2009 of €1.8 million and €6.4 million projected for 2010. No information about profitability was provided.

(4) Mr Chamberlain responded, "*sorry, this does not help*" and requested further information.

(5) On 21 January 2010, Mr Chamberlain requested that Mr Broli provide evidence of "*sell through*" to the end-user. None was provided.

1205. The evidence about the likelihood of payment by Sales Consulting further deteriorated thereafter. On 19 April 2010, Mr Hussain emailed Mr Broli, copying Mr Chamberlain, complaining that no debtor's confirmation for Sales Consulting had been received, nor any up-to-date financials, and that this was "*very disappointing*".

1206. Dr Lynch, in the course of his very light cross-examination on the transaction, put this all down to business practices in Italy. But the difficulties do seem strange given that Sales Consulting was a subsidiary of BNP Paribas, a large bank.

1207. The Claimants submitted that the reality is that it is plain from this evidence that Sales Consulting was not a creditworthy counterparty for a €1.75 million transaction. That was also Deloitte's conclusion: in its Q4 2009 report to the Audit Committee, Deloitte proposed that the revenue should <u>not</u> be recognised "*as we have not seen persuasive evidence that this amount is recoverable*". However, Deloitte recorded that "*Management are comfortable that the customer has a sound financial position based on its knowledge of the customer's reputation and position in the industry*" which was said to include Sales Consulting's status as a subsidiary of BNP Paribas but added that *"…the absence of further persuasive evidence means that we are unable to reach the same position at this time."*

1208. In the event, Sales Consulting did not pay and went into liquidation. By a letter dated 24 May 2010, Sales Consulting stated (emphasis in original):

> *"Dear Steven Chamberlein, [sic]*
>
> *as anticipated through Mr Corrado Broli, on May 6th 2010 the company Sales Consulting Srl, in Via Nicolò Tartaglia 11, Rome,* ***was placed in liquidation*** *in accordance with the legislation in force in Italy.*
>
> *The reasons that led the propriety [sic] to that decision are:*
>
> *Budget losses recorded in fiscal and financial management 2009;*
>
> *Very strong market restrictions and competition from large corporations due to the global financial crisis;*
>
> *Massive cuts in spending budget of the public administration and as a consequence of private too;*
>
> *Moreover the customer named Poste Italiane SpA, who had already expressed some difficulties with its delays (which we communicated to you in the email*

> *dated in April), is not in the right condition to acquire software applications and related services throughout 2010.*
>
> *It is therefore with great regret that our company cannot maintain the conditions for the acquisition of the rights to the software registered by you on December 31st, 2009. …"*

1209. On 5 July 2010, a representative of Sales Consulting emailed a copy of the letter direct to Mr Chamberlain and Mr Broli. Mr Chamberlain forwarded a copy to Mr Hussain and Mr Kanter, stating "*Not seen this before*". The same day, Mr Kanter contacted Rachel Haverfield, an Autonomy lawyer, to ask whether Autonomy could terminate its contract with Sales Consulting "*under the bankruptcy clause*".

1210. Autonomy did not provide a copy of Sales Consulting's letter to Deloitte. It was the unchallenged evidence of Mr Welham that Deloitte "*certainly should have been told about it*", because it would have meant that what Deloitte had hitherto been content to regard as a "*judgemental adjustment*" had now become a "*known adjustment*".

1211. The Claimants pointed out that no explanation has been advanced by the Defendants as to why the letter was not forwarded to Deloitte. However, it is also to be noted that by that stage Autonomy's management had determined that the individual effect of this transaction, and the aggregate effect of the adjustments necessary to reverse the revenue recognition in respect of all prior transactions impugned on collectability grounds, was not material in the context of the financial statements as a whole.

1212. On 21 July 2010, Ms Anderson (then of Deloitte) asked Mr Chamberlain about the status of Sales Consulting. Mr Chamberlain did not tell Deloitte of Sales Consulting's bankruptcy.

1213. In an email dated 26 July 2010, Ms Rachel Haverfield, an Autonomy in-house lawyer, summarized the situation with Sales Consulting: "*In Dec 2009, one of our smaller resellers (Sales Consulting) purchased a licence on behalf of an Italian company, Poste. It appears that Poste did not go ahead with the project, so the reseller did not get paid.*" She mentioned that Mr Kanter was exploring whether Autonomy could terminate the contract on the basis of the liquidation.

1214. When, in October 2010, Deloitte raised, as an outstanding audit issue, the need for evidence of the recoverability of the Sales Consulting debt, Mr Chamberlain told Mr Hussain to "*Ignore Sales Consulting, this is not valid*". However, that position was never relayed to Deloitte either.

1215. In Q3 2011, after the HP acquisition was announced, but before it became effective, Autonomy wrote off the then-outstanding balance.

1216. As previously mentioned, the experts agreed that (in retrospect at least) revenue should not have been recognised on this transaction: so little was known or ascertainable about Sales Consulting in terms of its financial information and trading history that it could not be said that there was a sufficient basis for a conclusion that the debt was collectible and IAS 18.14(d) was not satisfied.

1217. The immateriality of the transaction in accounting and financial terms, whether looked at singly or in aggregate with other "Collectability VARs" (as confirmed by Deloitte), means, to my mind, that any significance to be attributed to it depends upon whether the circumstances I have described support the Claimants' case that the Collectability VARs, in common with all the impugned VAR transactions, were in effect contrived simply to recognise revenue regardless of their true viability and substance, and improperly.

1218. The principal question in that regard, in my view, is whether either of the Defendants were aware, at the time of revenue recognition in respect of VT9, that Sales Consulting was not creditworthy.

1219. It seems clear from the email exchanges between Mr Chamberlain and Mr Broli that (a) Mr Chamberlain was concerned to obtain proper details (as was Mr Hussain) but (b) nothing useful was received from Mr Broli (who seems to have been unable or unwilling to understand what was required, but whenever prompted painted a picture of a company quickly expanding in terms of revenue and gave repeatedly unfulfilled assurances of the provision of imminent further financial information) leaving Mr Chamberlain (and Mr Hussain) very disappointed and having (c) to hold on to the fact that Sales Consulting was a subsidiary of BNP Paribas.

1220. The Claimants submitted that in such circumstances there was no basis on which Mr Hussain could genuinely have been satisfied, as at the date of publication of the Q4 2009 results (2 February 2010) or the 2009 Annual Report (22 February 2010), that Sales Consulting was more likely than not to pay the amount specified in the purchase order, which was the effect of the condition stipulated by IAS 18.14(d).

1221. I have concluded as follows:

(1) In light of the expert evidence and the clear view of Deloitte, it was wrong to recognise revenue in respect of VT9, as later events confirmed.

(2) The likelihood is that Mr Hussain's criticism of Mr Broli that he so seldom brought forward any realistic prospective transactions caused Mr Broli to resort to a quick VAR deal and to overlook, and then prevaricate and in effect cover up, the VAR's inadequacies.

(3) The broken promises of financial information, and the frailties revealed by the little information that was provided, must have increasingly concerned Mr Chamberlain and Mr Hussain (who, the evidence would suggest, were not gullible by nature). But the VAR deal having been done, and the revenue recognised, they were plainly averse to any write-off until the apparent became the blindingly obvious; and when added to a corporate or institutional mind-set of maximising the amount of recognised revenue this caused them to subordinate their real concerns, and place erroneous reliance on Sales Consulting's apparent financial umbrella (BNP Paribas).

(4) That was wrong; the question then is whether it was dishonest. It is important to bear in mind the time line. Deloitte's Final Report on the 2009 Audit, in which they proposed an adjustment of $2.2 million since they had *"not seen persuasive evidence that this amount is recoverable"* but noted that *"Management are comfortable that the customer has a sound financial position based on its knowledge of the customer's reputation and position in the industry"*, was dated

1 February 2010. By that stage, Mr Chamberlain plainly had real concern and was voicing it to Mr Broli (and sharing it with Mr Hussain); and such concern was exacerbated after there was no satisfactory response to his email to Mr Broli of 21 January 2010 (copied to Mr Hussain) asking him to get hold of evidence of sell through arrangements that the one-off reseller agreement stated had to be provided. Although even in April, the expression on the part of Mr Hussain that no debtor's confirmation or up-to-date financials had been provided was one of disappointment (see paragraph 1205 above). But by then it seems to me plain that neither Mr Chamberlain nor Mr Hussain would have been able to say that they had confidence in Sales Consulting's ability to pay. They were, at the least, reckless.

(5) In short, I accept the Claimants' case that as at 1 February 2010 (when Deloitte recorded the difference in view between it and Autonomy's management) and/or as at 22 February 2010 (the date of the 2009 Annual Report) Mr Chamberlain and Mr Hussain had no honest belief that Sales Consulting would be able to pay.

Defendants' knowledge of wrongful revenue recognition in respect of VT9

1222. Mr Hussain was directly and personally involved. He knew the salient facts. In my judgment, he must have known it was wrong to press for revenue recognition. This conclusion is reinforced by his failure (which the Claimants said was otherwise inexplicable) to ensure that news of Sales Consulting's insolvency was promptly relayed to Deloitte. He had "guilty knowledge".

1223. As so often, the case against Dr Lynch was less clear. The Claimants accepted that there is no documentary evidence of Dr Lynch's direct personal involvement in relation to this transaction. However, they submitted that it is not credible to suggest that Mr Hussain, Mr Chamberlain and Mr Kanter participated in this transaction, without Dr Lynch's authorisation. As stated above, they urged the court to infer that Dr Lynch authorised them to recognise revenue on non-creditworthy VARs, as and when required.

1224. I do not accept that the evidence supports that inference in that form. I do accept, however, that the general policy condoned by Dr Lynch was that, if necessary to meet forecast for revenue, VARs should be used as placeholders without proper regard for their ability to pay out of their own resources and in the knowledge that they would not receive anything from resale.

1225. Further, I think it more likely than not that Mr Hussain would have kept him regularly informed; and I think it likely that Mr Hussain would have warned Dr Lynch of Deloitte's conclusions, and of the proof that they were justified when Sales Consulting's bankruptcy became known to him.

1226. In my judgment, the likelihood is that Dr Lynch was told of the serious doubts and was prepared to turn a blind eye. In any event, he had condoned the policy: that amounts to recklessness as to whether or not the accounting might be untrue and misleading; and that is sufficient for FSMA purposes.

VT17: Comercializadora/TV Azteca Q3 2010

1227. In September 2010, Autonomy was hoping to conclude a sale to TV Azteca, a Mexican multimedia conglomerate. However, on 30 September 2010, at the end of Q3 2010, Mr Hussain sent Dr Lynch an email stating that the deal was in trouble. Almost immediately thereafter, Mr Neil Goldfarb, an Autonomy representative for Latin America Sales, sent an email marked urgent to Mr Crumbacher stating that he needed a *"one-off reseller agreement for my TV Azteca order"* and asking whether it would be possible to get this *"in template form"* for him simply *"to fill in the contact and address etc."*

1228. Email exchanges show that such an agreement was completed within the day with an entity named as Comercializadora Cobal SA de CV ("Comercializadora"). Thus, on 30 September 2010, Autonomy entered into a VAR agreement with Comercializadora for a licence fee of $1,500,000 plus $150,000 support and maintenance on the terms of a letter agreement containing the usual provisions previously noted. Payment was due on 29 December 2010.

1229. Comercializadora never paid. In Q2 2011, a bad debt provision of $549,945 was made; and in Q3 2011 Autonomy wrote off the entire debt.

1230. The Claimants' case is that at least by the time of publishing Autonomy's 2010 Annual Report, Autonomy had such doubts as to the substance of Comercializadora that provision should have been made against the debts; that Autonomy did not inform Deloitte about such doubts; and that VT17 (like VT22, another VAR deal with Comercializadora which I deal with below) is a further demonstration of serious impropriety of which the Defendants were well aware.

1231. It is not apparent who selected Comercializadora to be a VAR: Autonomy had not engaged with it previously. Deloitte (which initially pronounced the recognition of revenue in respect of VT17 to be satisfactory) noted the following about Comercializadora in its working papers:

> *"Comercializadora Cobal's is a new customer and therefore there is no payment history available. Financial statements as at 31 Dec. 2009 shows that it has cash of $5.3m in hand and its net assets amount to around $16m. Total sales of 2009 is around $24m and net profit around $8.2m…"*

1232. However, the Claimants contended that by the time of the 2010 Annual Report, evidence had come to light which cast considerable doubt on the financial substance (and even existence) of Comercializadora and on the collectability of the debt, but which (according to Mr Welham, who was not cross-examined on the point, avowedly because the point was not pleaded) was not shared with Deloitte. In particular, on 5 November 2010, Mr Richard Eads (Global Procurement officer and Director of Credit and Collections) of Autonomy notified Mr Chamberlain of "*some issues*" with the Comercializadora account:

> *"We may have some issues with this account as follows:*
>
> *1) the phone number provided on the order is no longer working.*
>
> *2) the email address provided on the order is no longer working.*
>
> *3) the domain name www.cobalsco.com.mx is not active.*
>
> *4) the email at the bottom of this thread was send from a hotmail account.*

> *5) we have reason to believe that Gilberto Alvarez used to work for Itegrar.*
>
> *Would you like us to continue researching here in Dallas? Or should we bring legal into the mix?"*

1233. That was a formidable list. On 10 November 2010, Mr Chamberlain wrote to Ivan Rothman, Autonomy's Senior Corporate Counsel, noting that there were "*early indicators that the reseller did not exist or has gone underground*".

1234. On 19 January 2011, Mr Gilberto Alvarez (signing as Comercializadora's Legal representative) sent an email to Mr Goldfarb attaching Accounts for 2010 which showed Comercializadora as having $4.2 million in cash, but (except for the email referred to in paragraph 1249 below) any attempts to contact Mr Alvarez and Comercializadora further were unsuccessful, and in an email to (amongst others) Mr Eads, Mr Rothman and Mr Goldfarb dated 20 January 2011, Mr Stephan wrote:

> *"Neil – I don't understand. They can't pay us even half the cash from their Q3 deal without raising bank financing yet they have $4.2m in cash? Excuse my cynicism but either these financial statements have been falsified or they should be paying us the full balance from Q3 immediately. What's the true story here?"*

1235. The evidence is at best patchy as to how the issue of revenue recognition and any appropriate provision was thereafter dealt with, except that Deloitte's Report to the Audit Committee for the year ended 31 December 2010 (dated 26 January 2011) proposed a judgmental adjustment (and bad debt provision accordingly) of $2.7 million to cover both VT17 and VT22 *"given the long overdue nature of the balance and lack of recent correspondence".* The same report noted additionally, however, that this was not material in the context of the financial statements as a whole.

1236. Although Mr Welham was not cross-examined on the point (on the apparently erroneous basis that it was not pleaded) it was suggested in Mr Hussain's closing submissions that it was untrue that Autonomy had kept Deloitte in the dark about the difficulties it was having in contacting Comercializadora, as Mr Welham appeared to suggest, since Deloitte's 2010 year-end Report to the Audit Committee (see paragraph 1235 above) commented on management having to chase overdue balances and the *"lack of recent correspondence".*

1237. Further, and as was pointed out in the written closing submissions on behalf of Mr Hussain, Deloitte's *"Evaluation of Misstatements"* document records a discussion with Mr Chamberlain, Mr Hussain and the Audit Committee on 26 January 2011 about Deloitte's proposed judgmental misstatements and the reasons for them (including, I think I should assume, the doubts that Mr Eads had expressed to Mr Chamberlain in his email of 5 November 2010).

1238. Nevertheless, the depth of the difficulties and Autonomy's concerns were still not shared with Deloitte, and were entirely inconsistent with any attempt to contradict Deloitte's own doubts.

1239. To complete the picture, no sale to TV Azteca was achieved: the evidence was sparse in this regard but there was little or nothing to suggest that it was ever likely. The result of the recourse to the VAR was thus not to accelerate but to fabricate revenue which was never in fact received from any source.

1240. In my judgment, VT17 was another illustration of what by the end of 2010 had become a propensity on the part of Autonomy to resort to a VAR as a means of booking revenue with very little analysis on its part either of the VAR's ability to pay or the prospect of the direct sale by Autonomy to an end-user from which alone there was any prospect of actual revenue receipt.

1241. It is also an illustration of the mismatch between Autonomy's speed to recognise revenue and its reluctance to (in effect) reverse any part of it even in the face of widespread doubt as to collectability.

1242. The truth is that in these cases, revenue was recognised when in reality the expectation of any receipt was uncertain (and in the event, none eventuated). In my judgment, the recognition of revenue was unjustified and indeed reckless.

Defendants' knowledge of improper revenue recognition in respect of VT17

1243. Mr Chamberlain plainly knew the relevant details. The Claimants' case that Mr Hussain knew the relevant facts is based on the proposition that *"Given his* [Mr Chamberlain's] *close working relationship with Mr Hussain, it is likely that he kept Mr Hussain informed of them."* The Claimants also relied on the fact that neither Mr Chamberlain nor Mr Hussain had attended trial to offer evidence to the contrary. I accept this: it is unlikely that Mr Chamberlain proceeded without keeping Mr Hussain informed.

1244. Dr Lynch was not cross-examined on the transaction, and no transaction-specific evidence of his involvement was provided. The only basis on which Dr Lynch was said to be implicated was that he had (it was alleged) given general authorisation for transactions with non-creditworthy VARs. As in the context of VT9, I do not think he knew of the particular transaction; but he condoned the policy.

1245. In my judgment, as I have held to be likely, Mr Hussain would have kept Dr Lynch informed. But even if that were not so, Dr Lynch had condoned the policy: that amounts to recklessness as to whether or not the accounting might be untrue and misleading; and that is sufficient for FSMA purposes.

VT22: Comercializadora/CISEN Q4 2010

1246. Although slightly out of chronological sequence (since another Collectability VAR, VT19, preceded it) I next discuss the second transaction with Comercializadora, which was entered into in Q4 2010. The transaction comprised a VAR sale in the sum of \$1,000,000 (plus \$100,000 support and maintenance) for end-user Centro de Investigacion y Seguridad Nacional ("CISEN", the Mexican intelligence agency).

1247. This second Comercializadora deal revealed the same pattern and traits as the first (including the very late introduction of the VAR right at the end of the relevant quarter, and the complete failure to pay followed by a \$366,630 bad debt provision in Q2 2011, followed by a 100% write-off in Q3 2011). Its principal interest is in the fact that by the time that it was made Autonomy was well aware of serious doubts about Comercializadora's financial position (and even, existence), and, although Deloitte declined to approve revenue recognition, Autonomy recognised the revenue regardless.

1248. Again, the difficulty in this transaction is the sparseness of the evidence: indeed, the evidential position is materially less clear than in the case of VT17. The Claimants relied on the experts: but the experts relied on assumptions as to the facts and do not assist in assessing how it was that Autonomy came to resort to this doubtful VAR and persuade itself that revenue could properly be recognised.

1249. In my judgment, what emerges from the very limited documentary evidence, and especially an email from Mr Gilberto Alvarez (breaking his previous silence) to Mr Ray Corado (an Autonomy Financial Analyst) and Mr Goldfarb, dated 26 January 2011, is that Comercializadora was not in a position or intending to pay unless and until its end-user paid. The Claimants never suggested any side agreement to that effect: it was simply the position Comercializadora (or, if it was not an existent entity, those speaking for it) took. Thus, when the Mexican Treasury suspended resourcing of open projects, Mr Alvarez appears to have taken it as read that Comercializadora would not pay Autonomy notwithstanding the terms of the VAR Agreement (again in a letter with the usual terms).

1250. Deloitte's working papers record satisfaction that the requirements of IAS 18.14 as to the transfer of risk and reward, managerial control and economic benefits had been satisfied, except that they proposed that an adjustment be made to defer revenue recognition, stating as follows under the heading "Collectability":

> *"Based on Comercializadora's historic dealings with Autonomy and the fact that the most recent available financial information (as at 31 December 2009) on Comercializadora shows that it has insufficient means by which to pay this current deal and the Q3 2010 deal of $1.65m. As such, we conclude that there is sufficient doubt over the recoverability of this deal such that revenue should be deferred."*

1251. The Claimants alleged further that *"Autonomy recognised the revenue regardless"*. Although Deloitte advised an adjustment to defer recognition of revenue, Autonomy stuck to its view. Deloitte were less than robust despite the obvious red flags, and ultimately the resolution appears to have been that the effect of the difference in view was immaterial to the accounts. However, for present purposes what is important is that once again recourse had been made to a VAR, and the 'sale' proceeds booked in full as recognised revenue, without any sufficient prospect of revenue ever being received.

1252. As it was, Comercializadora never did make any payment to Autonomy on this transaction. By Q2 2011, a bad debt provision of $366,630 had been recorded. In Q3 2011, the invoice was written off in full. No sale to CISEN ever eventuated.

Defendants' knowledge of improper revenue recognition in respect of VT22

1253. Again, the Claimants' case is that Mr Chamberlain knew all the facts. He was expressly warned by Mr Eads that the deal was *"complete nonsense…We have no reason to believe that this [is] a good order…"* I think it more likely than not he would not have withheld any of this from Mr Hussain. He did not, of course give any evidence to gainsay that. Mr Hussain himself knew about the contemplated transaction with CISEN: it is documented that he pressed for updates on its progress, and that he also knew that it had proved, before year-end *"a heroic failure"* and that a VAR was to be involved to book revenue, the transaction being (as described by Mr Scott *"a big one that we are counting on"*). In my judgment, Mr Hussain had "guilty knowledge".

1254. Dr Lynch maintained that he was not involved[97] and that the revenue recognition decisions were made by Autonomy's finance department. He was not cross-examined at all on either VT17 or VT22; but since his position was that he could give no evidence that is more understandable.

1255. As in the case of the other impugned Collectability VAR transactions, I accept that there is no transaction-specific evidence of Dr Lynch's personal involvement. I doubt he knew the details: but he had condoned the policy, even in its extreme form where revenue was booked without any real prospect of receipt. That was not honest. Again, the question is whether Mr Hussain would inevitably have informed him, despite the relatively immaterial amount involved, or whether if not it suffices that Dr Lynch had condoned this sort of transaction.

1256. In my judgment, Mr Hussain would have kept Dr Lynch informed. But even if that were not so, he had condoned the policy: it amounts to recklessness as to whether or not the accounting might be untrue and misleading; and that is sufficient for FSMA purposes.

VT19: Red Ventures/Poste Italiane Q3 2010

1257. On 30 September 2010, Mr Kanter, on behalf of ASL, signed a VAR agreement with Red Ventures srl ("Red Ventures"). The agreement appointed Red Ventures to act as a VAR on behalf of four end-users in Italy, namely Poste Italiane, the Italian Ministry of Justice, the Italian Ministry of Health and Terna (the operator of the Italian transmission grid).

1258. The agreement provided, by clause 2, for a sale of software licences, with licence fees of €2 million and one year's support fees of €100,000. The payment terms were 90 days from invoice.

1259. Autonomy recognised the licence fee revenue at the time of the VAR Agreement. The Claimants contended that it was clear even at that time that Red Ventures was not good for the money and that *"the recovery of this licence fee was never probable"*.

1260. It appears from email exchanges that Autonomy had some difficulty in obtaining any financial statements from Red Ventures, despite repeated efforts by Mr Hussain and Mr Chamberlain to obtain them. There is no indication that adequate financial statements were ever produced.

1261. Deloitte's working paper said it had "*not seen any persuasive evidence that this deal is recoverable*", with the consequence that it had been recorded as a "*likely misstatement*". Similarly, Deloitte's Q3 2010 report to the Audit Committee stated Deloitte's belief:

> "*that there is currently insufficient evidence of recoverability and therefore that it is not appropriate to recognise revenue at this stage*".

1262. In the event, Red Ventures never did make any payment to Autonomy on this transaction. On 13 April 2011, Mr Kanter was sent an update on non-payment, which noted that, "*There is a telephone number [i.e. for Red Ventures], but it doesn't answer*". By Q2 2011,

[97] In closing submissions it was submitted Dr Lynch was not involved in the collectability judgments being made by the finance department and Deloitte. Dr Lynch said he had no role in the post-quarter collectability judgments that were made.

a bad debt provision of $965,213 had been recorded and, on 30 September 2011, the total invoice was classified as a bad debt and written off.

1263. The Claimants submitted that the court should accept Mr Holgate's evidence that, on the facts assumed by him, this transaction did not satisfy the requirements of IAS 18.14(d). Mr MacGregor did not agree. He concluded that he did "*not have enough information to conclude whether IAS 18.14(d) was met*" and that on that basis, there was "*insufficient information to reach the conclusion that Autonomy's accounting treatment in respect of the licences was inappropriate*". However, the Claimants submitted that on that basis he should have reached the opposite conclusion that the absence of sufficient information to satisfy IAS 18.14(d) should prevent a finding that Red Ventures was more likely than not to pay Autonomy. The Claimants contended that this was therefore *"another transaction where Deloitte never approved the recognition of revenue, despite which Autonomy nonetheless went ahead and recognised it anyway"*.

1264. This latter contention is not quite accurate. It conflates three separate accounting events: (a) the recognition of revenue at the time of the VAR sale in September 2010; (b) the subsequent Q3 2010 review of and Audit Committee report on that decision by Deloitte proposing reversal of revenue as a "judgemental adjustment"[98]; (c) the determination of materiality and whether and how to reflect the results of the review in the Q3 2010 reported results.

1265. As to (a) in the preceding paragraph 1264 above, there appears to have been little or no evidence available to Autonomy as to the standing and financial position of Red Ventures. It remains unclear why Red Ventures' was chosen as a VAR. Insofar as Red Venture's ability to pay depended on a successful re-sale to end-users, it appears that the contracting party was proposed to be Poste Italiane, although other Italian governmental or quasi-governmental departments or entities were intended users. As in previous contexts, the one-off VAR agreement (dated 30 September 2010) expressly provided that *"VAR should only place an order with Autonomy when VAR has received an order from End-User or its authorized agent."* No such order from End-User was received at the time or thereafter. The evidence was sparse: there was none that an end-user deal was a probability, or even on the cards; and Poste Italiane had proved unreliable in the past.

1266. As to (b) in paragraph 1264 above, the Defendants stressed that Deloitte's proposal subsequently that an accounting adjustment should be made to reverse the value of Autonomy's sale to Red Ventures (and the corresponding debtor balance) does not of itself impact on the original decision to recognise revenue: it reflects the different view they took, presumably once the difficulty in obtaining information emerged and also (it would appear) in light of some specific (but unexplained) concern about one of the end-user's (Poste Italiane's) ability to pay.

1267. As to (c) in paragraph 1264 above, it appears that the decision not to include the adjustment in the Q3 2010 reported results was because (a) Autonomy's management still hoped that payment could be made and (b) Autonomy's management considered, and Deloitte concurred, that the adjustment would not have had any material effect on the financial statements taken as a whole.

[98] Which Mr MacGregor explained as being *"the difference in judgment between Deloitte and Autonomy's management at the time"*.

1268. In my judgment, VT19 is another example of Autonomy tending to take advantage of any leeway available and to stick by its judgement to recognise revenue unless and until unequivocally required to reverse it. Autonomy was prepared to take a clear risk of never receiving revenue for the immediate advantage of booking revenue to meet target. That was not honest. The transaction was flawed and no revenue should have been recognised from it.

Defendants' knowledge of improper revenue recognition in respect of VT19

1269. The Red Ventures VAR deal was signed by Mr Kanter. Although there is no evidence of his involvement before then, it was Mr Hussain who pursued (entirely unsuccessfully) financial information about Red Ventures after the event. It is more likely than not that he knew (from Mr Kanter) about the deal and its frailty. He was responsible for its revenue recognition and the lack of any substantial basis for it. I consider that this amounted to "guilty knowledge".

1270. The Claimants did not put any transaction-specific evidence nor indeed any case of specific dishonest knowledge to Dr Lynch in relation to this transaction. Again, however, it is more likely than not that Mr Hussain kept him abreast; and in any event, even if he did not know the details, he had condoned the policy, even in its extreme form where revenue was booked without any real prospect of receipt.

1271. In my judgment that amounts to recklessness as to whether or not the accounting might be untrue and misleading; and that is sufficient for FSMA purposes.

VT29: Computer Trading/Poste Italiane Q1 2011

1272. The last, and in value terms least, of the Collectability VAR transactions was a purchase order from an Auxilium group company called Computer Trading dated 10 February 2011 for support and maintenance services and support on IDOL products for a period of 15 months (1 January 2010 to 31 March 2011) for end-user Poste Italiane. The price was €340,000. There would probably have been a governing agreement, but it was not shown to me and I note that Mr MacGregor had not seen a copy either.

1273. A notable feature of VT29 for present purposes is that Autonomy recognised the sum of €340,000 as licence revenue in its income statement on 31 March 2011, despite this transaction relating to the sale of maintenance and support services. It appears from ledger extracts referred to in Mr MacGregor's Supplemental Report that Autonomy originally recorded the transaction in full as support revenue, but that this was reversed the same day and transferred to licence revenue in the income statement: but the reason for this was not explained. Mr MacGregor postulated that perhaps the reason was that the services were to be and perhaps had in fact been provided over the prescribed period, and on that basis he considered that:

> *"…it is reasonable that the revenue was recognised in full by that date, although ordinarily I would expect for this revenue to have been spread over the period in which services were provided…".*

1274. It appears from Mr Broli's email to Mr Hussain dated 10 February 2011 that Computer Trading (Auxilium) had been required and had promised to pay €340,000 upon receipt of Autonomy's invoice. Mr Hussain had insisted they pay *"since they already owe us for BAV we can only recognise on cash received."* In the event, Computer Trading paid nothing until it paid the lesser sum of €70,000 on 19 October 2011. No further payments were received and the remaining balance was written off in September 2012. The Claimants focused on the alleged lack of financial evidence of Computer Trading's ability to pay as the basis for impugning VT29.

1275. The Claimants alleged, supported by the evidence of Mr Holgate, that the recognition of revenue in respect of VT29 was not compliant with IAS 18.20(b), which applies to the supply of services. IAS 18.20(b) requires that *"it is probable that the economic benefits associated with the transaction will flow to the entity"* in order that revenue shall be recognised. Mr MacGregor did not accept this because he was *"not able to reach a conclusion as to the appropriateness (or otherwise) of Autonomy's accounting treatment for this transaction"*.

1276. As in the case of VT19 (Red Ventures), the Claimants submitted that "*the absence of evidence means that the requirement of a 51% likelihood of payment was not satisfied."* In my judgment, the question is broader than that: it is whether at the time when the decision to recognise revenue was made there was a sufficient basis in the contemporaneous information available to Autonomy for concluding reasonably, even if ultimately wrongly, that the VAR would pay within a reasonable time.

1277. As Mr MacGregor noted, there is no witness statement evidence, nor any Deloitte working papers, specific to this transaction. The transaction was not mentioned in Deloitte's Report to the Audit Committee for Q1 2011, presumably because it was immaterial. The sparseness of the evidence available in this context makes an assessment now of the judgment then very difficult.

1278. The Defendants' position was that as the Claimants bear the burden of proof in the proceedings, the lack of evidence is fatal to their claims. I do not agree. In my judgment, having regard to all the circumstances including the demonstrated unreliability of Poste Italiane and the 'pattern' evident of recourse to a VAR without prospect of payment, the lack of evidence of a likelihood of payment suggests that IAS 18.14(d) was not fulfilled. Further, and more specifically, the VAR deal itself required payment immediately upon receipt of Autonomy's invoice; and none was made. In such circumstances, in my judgment, the evidence that revenue should not have been recognised is clear.

1279. I would regard this transaction as being all of a piece with the other Collectability VARs: there was no evidence of any proper basis for recognising revenue from it.

Defendants' knowledge of improper revenue recognition in respect of VT29

1280. Although it was a relatively small transaction, Mr Broli kept Mr Hussain updated about it. Mr Hussain had stipulated payment against invoice; and it must be likely that he knew this had not been fulfilled. He had "guilty knowledge" accordingly.

1281. I accept that there is no transaction-specific evidence of Dr Lynch's personal involvement. Again, the question is whether Mr Hussain would inevitably have informed him, despite the relatively immaterial amount involved, or whether if not it suffices that Dr Lynch had condoned this sort of transaction.

1282. In my judgment it does: it amounts to recklessness as to whether or not the accounting might be untrue and misleading; and that is sufficient for FSMA purposes.

Overall conclusions as to the Collectability VAR claims

1283. In summary, in my judgment, the Collectability VARs demonstrate a pattern of knowing improper recognition of revenue simply to book revenue to meet targets without any sufficient regard to whether any revenues would in due course be received.

1284. Both Defendants were implicated and had "guilty knowledge" of the wrongful accounting and consequent false depiction in Autonomy's published information.