SPL Guernsey ICC Limited and its Incorporated Cells v Addison
Royal Court
12th April 2018

JUDGMENT 19/2018

Breach of director's duties

IN THE ROYAL COURT OF GUERNSEY

(ORDINARY DIVISION)

BETWEEN:

(1) SPL GUERNSEY ICC LIMITED and its INCORPORATED CELLS, namely
(2) SPL REALISATION IC LIMITED
(3) SPL PRIVATE FINANCE (PF2) IC LIMITED
(4) SPL ARL PRIVATE FINANCE (PF5) IC LIMITED
(5) SPL PARALLEL PRIVATE EQUITY (PE2) IC LIMITED
(6) SPL TREASURY (AT1) IC LIMITED

Plaintiffs

-and-

ROBERT STEPHAN ADDISON **First Defendant**

Dates of hearing: 30th and 31st January, 1st to 3rd, 6th and 8th to 10th February 2017

Judgment handed down: 12th April 2018

Before: Richard James McMahon, Esq., Deputy Bailiff

Jurats: S M Jones Esq., D P L Hodgetts Esq., LVO and S J Morris Esq.

Advocate for the Plaintiffs: **Advocate P Richardson**
Advocate for the Defendant: **Advocate A C Williams**

Cases & legislation referred to:

The Royal Court (Reform) (Guernsey) Law, 2008
The Royal Court Civil Rules, 2007
The Companies (Guernsey) Law, 1994
The Incorporated Cell Companies Ordinance, 2006

The Companies (Guernsey) Law, 2008
The Protection of Investors (Bailiwick of Guernsey) Law, 1987
SPL Private Finance (PF1) IC Limited v Arch Financial Products LLP [2014] EWHC 4268 (Comm)
The Evidence in Civil Proceedings (Guernsey and Alderney) Rules, 2011
The Evidence in Civil Proceedings (Guernsey and Alderney) Law, 2009
Hollington v F Hewthorn & Co. Ltd [1943] 1 KB 587
Al-Hawaz v The Thomas Cook Group Limited (unreported, 27 October 2000)
The Control of Borrowing (Bailiwick of Guernsey) Ordinance, 1959
The Financial Services and Markets Act 2000 (United Kingdom)
The Companies Act 2006 (United Kingdom)
In re Med Vineyards Limited (in liquidation) (unreported, 25 July 1995)
The Companies Act 1862 (United Kingdom)
Flightlease Holdings (Guernsey) Limited v Flightlease (Ireland) Limited [2009-10] GLR 38
Howard Smith Ltd v Ampol Petroleum Ltd [1974] AC 821
Iesini v Westrip Holdings Ltd [2009] EWHC 2526 (Ch)
Extrasure Travel Insurances Ltd v Scattergood [2003] 1 BCLC 598
Regentcrest plc (in liquidation) v Cohen [2001] 2 BCLC 80
Re D'Jan of London Ltd [1993] BCC 646
The Insolvency Act 1986 (United Kingdom)
Re Barings plc (No. 5) [1999] 1 BCLC 433
Lexi Holdings plc (in administration) v Luqman [2007] EWHC 2652 (Ch)
Asic v Adler [2002] NSWSC 171
The Corporations Act 2001 (Australia)
Code of Practice – Company Directors
Lexi Holdings plc (in administration) v Luqman [2008] EWHC 1639 (Ch)
Weavering Capital (UK) Ltd (in liquidation) v Dabhia [2013] EWCA Civ 71
Kuwait Airways Corporation v Iraqi Airways Co. (Nos 4 and 5) [2002] 2 AC 883
Gwembe Valley Development Co Ltd (in receivership) v Koshy (No 3) [2003] EWCA Civ 1048
Omak Maritime Ltd v Mamola Challenger Shipping Co. [2010] EWHC 2026 (Comm)
McGregor on Damages (19th ed.)
Banco de Portugal v Waterlow [1932] AC 452
Jewelowski v Propp [1944] 1 KB 510
The Protection of Investors (Bailiwick of Guernsey) Law, 1987
The Companies (Guernsey) Law, 2008 (Commencement) Ordinance, 2008
The Companies (Transitional Provisions) Regulations, 2008
Perpetual Media Capital Limited v Enevoldsen [2014] GLR 57
Canada Steamship Lines Ltd v The King [1952] AC 192
Smith v South Wales Switchgear Ltd [1978] 1 WLR 165
Re Kirbys Coaches Ltd [1991] BCLC 414
Coleman Taymar Limited v Oakes [2002] 2 BCLC 749
Barings plc (in liquidation) v Coopers & Lybrand (a firm) [2003] EWHC 1319 (Ch)
Maelor Jones v Heywood-Smith (1989) 54 SASR 285
Re Duomatic [1969] 2 Ch 365
Queensway Systems Ltd (in liquidation) v Walker [2006] EWHC 2496 (Ch)
Re DKG Contractors Ltd [1990] BCC 903
Bishopsgate Investment Management Ltd v Maxwell [1993] BCC 120
Bairstow v Queens Moat Houses plc [2000] 1 BCLC 549

Introduction

1. Whether or not, as one of the witnesses described it, the situation relating to the Arch-Cru funds was "*the biggest financial scandal in the UK for many, many years*", it is beyond question that these events had a significant impact on many persons and that it has spawned substantial litigation, of which this case is a part. The present case focuses on allegations that the First Defendant, Robert Addison, breached the duties he owed to a Guernsey incorporated cell company and a number of the cells of that company in his capacity as director.

2. This judgment, which has been prepared in accordance with the provisions of section 16(5) of the Royal Court (Reform) (Guernsey) Law, 2008, contains the unanimous findings of the Jurats.

Background

3. The Cause in this action was first tabled against two of the four original defendants on 29 June 2012. The First Plaintiff is SPL Guernsey ICC Limited ("the ICC" or, in some instances, "the Company"). When it was incorporated it was named Arch Guernsey ICC Limited. The action has been brought by it and 18 of its Cells. As with the ICC, the names of those Cells originally began with "Arch". As against the First Defendant, the Cause was tabled on 6 July 2012 and adjourned for one week, when it was placed inscrite on his behalf and separately on behalf of the final of the four Defendants being actioned. There had previously been leave given to serve the First Defendant out of the jurisdiction. The Second and Third Defendants, Neal Meader and Peter Radford, were the two other directors of the Plaintiffs. The Fourth Defendant was Bordeaux Services (Guernsey) Limited ("Bordeaux"), with which the First Plaintiff had entered an administration agreement. Messrs Meader and Radford, but not Mr Addison, were also directors of Bordeaux. The Defenses of the Second to Fourth Defendants were tabled on 23 November 2012. The First Defendant's Defenses, to which was added a Counterclaim, were tabled the following week. Répliques to both defences, and a Defence to the First Defendant's Counterclaim, were filed on 18 January 2013. The First Defendant responded to the Plaintiffs' requests for further information on his Defenses on 23 August 2013. Responses by the Second to Fourth Defendants and by the Plaintiffs to requests for further information were also provided dated 2 October 2013 and 21 May 2014 respectively.

4. These pleadings cover a number of matters. There are sections in the Cause dealing with the parties and the duties said to be owed by the Defendants to the ICC and its Cells, which are of general application. Thereafter, each section in the Cause deals with a different complaint. Thus, Section C deals with investments relating to the Danube Delta Fund, Section D deals with investments relating to Cru Investment Management Limited, Section E deals with investments relating to Arch Group UK Limited, Section F deals with investments in the conversion of ships, Section G deals with investments relating to Lonscale Limited ("Lonscale"), Section H deals with investments relating to Nice Group Limited, Section I deals with investments relating to Noble Fund Managers Limited, Section J deals with investments relating to the Financial Partners group of companies and Section K deals with investments relating to Scapa Group plc. The total amount of damages sought under the Cause is £46,750,000, US$171,100,000 and €12,500.

5. Both the Plaintiffs on the one hand and the Defendants on the other proposed that, rather than trying the entirety of the Cause, a narrower approach was going to be sensible. The amounts claimed are unlikely to be recoverable in full from these Defendants. The parties did not, however, agree which aspects of the Plaintiffs' claim should be heard as a preliminary issue. The sections of the Cause originally identified for this purpose in the Order made on 28 November 2014 were subsequently changed by the parties agreeing how best to manage matters between them. Despite the parties agreeing that a preliminary trial should be confined to just two of the

ship conversions referred to in Section F of the Cause, by an application dated 27 November 2015, the Plaintiffs concerned applied for summary judgment in respect of Section G of the Cause (the investments relating to Lonscale).

6. On 19 April 2016, the proceedings against the Second to Fourth Defendants were dismissed with no order as to costs. It was explained to the Court that terms of settlement had been reached between the two sides. The settlement agreement is confidential as between the parties to it and so the Court has no knowledge of what the terms of settlement were. The proceedings against Mr Addison continued. For a period up to and including that time, Mr Addison was not represented by an Advocate.

7. The Plaintiffs' application for summary judgment was then withdrawn, but the matter to be dealt with as a preliminary trial was agreed between the Plaintiffs and the First Defendant to be the investments relating to Lonscale (as set out in Section G of the Cause). Revised case management directions for this purpose were given on 20 May 2016. Mr Addison was by this time again represented by Counsel. The choice of this subject-matter for a preliminary trial reflects what took place in other proceedings before the High Court of Justice in England and Wales, to which this judgment will refer shortly. It is this part of the action that was then tried in 2017 and with which this reserved judgment deals.

8. The names of some of the Cells involved have changed since the Cause was originally pleaded. The Cells involved with the investments relating to Lonscale were the Third, Fourth, Fifth, Sixth, Thirteenth and Fourteenth Plaintiffs. The identities of the proper Plaintiffs to this aspect of the action were clarified by way of an application pursuant to rule 37(1)(a) of the Royal Court Civil Rules, 2007 that was made and granted during the course of the trial. Some re-structuring of the ICC's Cells had taken place in March 2016, as a result of which various Cells, including the Fourth, Fifth, Thirteenth and Fourteenth Plaintiffs, had amalgamated with the Ninth Plaintiff and the Ninth Plaintiff had subsequently changed its name from SPL Private Equity (PE1) IC Limited to SPL Realisation IC Limited. This preliminary trial has, therefore, been conducted between the ICC (so far as it is engaged), the newly named Ninth Plaintiff (SPL Realisation IC Limited), the original Third Plaintiff (SPL Private Finance (PF2) IC Limited), the original Sixth Plaintiff (SPL ARL Private Finance (PF5) IC Limited) and the First Defendant. For ease of reference, we will refer to the original Third, Fourth, Fifth, Sixth, Thirteenth and Fourteenth Plaintiffs by the names by which they were known at the times prior to the most recent changes and how they feature in the pleadings, ie, after the changes from Arch-related entities to SPL-related entities. Those names are respectively: SPL Private Finance (PF2) IC Limited, SPL Finance Opportunities (PF3) IC Limited, SPL Structured Finance (PF4) IC Limited, SPL ARL Private Finance (PF5) IC Limited, SPL Real Estate Finance (RE1) IC Limited and SPL Real Estate 2 (RE2) IC Limited. In each case, for ease of reference, we will use the letters and number in parentheses in each case, ie, "PF2", "PF3", "PF4", "PF5", "RE1" and "RE2" respectively. During the course of this judgment, we will also refer to the Eighteenth Plaintiff, SPL Sustainable Finance (SO3) IC Limited ("SO3"), and the Nineteenth Plaintiff, SPL Treasury (AT1) IC Limited ("AT1").

9. The Plaintiffs are represented by Advocate Paul Richardson and the First Defendant by Advocate Williams. The Court is grateful to both of them for their assistance throughout and for their patience whilst waiting for this judgment to be prepared.

General directions

10. The Deputy Bailiff reminded the Jurats about their respective roles: the Deputy Bailiff is the sole judge of questions of law and procedure and the Jurats are the sole judges of questions of fact. The Jurats were directed that they must accept his directions on the law and follow them. The

Deputy Bailiff explained that to establish something on the balance of probabilities means to prove that something is more likely so than not so. Whilst the burden of proof generally rested on the Plaintiffs, insofar as the First Defendant sought to establish any fact, the burden of proof rested on him to prove that fact to the same civil standard.

11. The Jurats were to have regard to the whole of the evidence presented to the Court, and to form their own judgments about the witnesses, and which evidence they treated as reliable, and which they considered was not. They might take account of the arguments in the speeches they heard, but are not bound to accept them. If at any time the Deputy Bailiff appeared to express any views concerning the facts, or emphasise a particular aspect of the evidence, the Jurats were not to adopt those views unless they agreed with them. The Deputy Bailiff summarised that position by clarifying that, when it comes to the facts on the questions for determination in this case, it is the Jurats' judgment alone that counts.

12. The Deputy Bailiff emphasised the need for the Jurats to have regard to the cases pleaded by the parties because these formed the basis of the dispute between them. If the Jurats felt that they had heard evidence that did not concentrate on the central issues they were required to resolve, they could, save to the extent that such evidence went to the credibility of a witness, choose not to make any findings about what might be regarded as the surrounding circumstances of the case.

Pleadings

13. The Amended Cause first describes the parties. Mr Addison admits that the ICC was incorporated in Guernsey on 21 December 2006 under the Companies (Guernsey) Law, 1994. He also admits that between 21 December 2006 and 7 December 2007, the ICC established the Cells under the Incorporated Cell Companies Ordinance, 2006. In respect of his own roles, he admits that he was a director of the ICC from 21 December 2006 until 31 December 2009 and that he was a director of each of the Cells from its incorporation until 31 December 2009. He admits that he was an LLP Designated Member of Arch Financial Products LLP ("Arch") from 31 March 2006 onwards and the Chief Operating Officer of Arch. In respect of the Plaintiffs' contention that this position gave him responsibility *inter alia* for setting risk policy guidelines, Mr Addison draws a distinction between any investment decision process at Arch, which was the responsibility of others, and the risk management process, which he accepts was his responsibility. He accepts that he was a director of five, but not six as alleged by the Plaintiffs, further English companies within the Arch group.

14. Mr Addison accepts that the ICC and the Cells together constituted a series of closed end investment companies, the portfolios of which were intended to be invested by each Cell in accordance with the Scheme Particulars and the relevant Supplemental Scheme Particulars, but he denies the remainder of para. 6 of the Amended Cause referring to the way the portfolios were held. Apart from denying that the arrangements for holding and managing the Cells included any obligation for the open-ended investment companies incorporated in the United Kingdom to invest in the Cells, the First Defendant admits that investors subscribed for shares in those companies which, together with other investors, subscribed for shares in the Cells and that all of the Cells, except AT1, were listed on the Channel Islands Stock Exchange ("the CISX"). Mr Addison further accepts that there was between each Cell and Arch an investment management agreement ("IMA"), which set out the terms and conditions upon which Arch agreed to provide discretionary investment management services to each Cell, and under which Arch was responsible for managing the Portfolio (as defined) for each of the Cells. He highlights clause 4 of each IMA. He also admits that, under an administration agreement dated 28 December 2006 ("the Administration Agreement"), the ICC agreed with Bordeaux that the latter would act as administrator and company secretary to it and sponsor the listing of the Cells on the CISX and

that each Cell subsequently entered into an administration agreement with Bordeaux on similar terms.

15. At para. 10 of the Amended Cause, the following fiduciary and/or customary law duties are said by the Plaintiffs to be owed to them by Mr Addison by reason of his position as a director:

> "*a. a duty to act honestly and bona fide in the best interests of the Company and the Cells;*
>
> *b. a duty to exercise his powers in accordance with his own independent judgment and without regard to the interests of others (including Arch or Bordeaux);*
>
> *c. a duty not to act for any collateral or improper purpose in the exercise of his powers;*
>
> *d. a duty not to act in the affairs of the Company and Cells where there was a conflict between the duties owed to the Company and Cells and the other duties and interests of the Directors (or any of them), unless any such conflicting duties or interest had been properly disclosed by the Director concerned to the other Directors;*
>
> *e. a duty to exercise the care, skill and diligence with regard to the affairs and management of the Company and the Cells that would reasonably be expected of a reasonably diligent person with the general knowledge, skill and experience of the Directors;*
>
> *f. a duty to make or consider decisions on a rational basis giving due consideration to adequate material information (obtaining such information from others, where necessary);*
>
> *g. a duty properly to understand, monitor and oversee the management and business activities (including those business activities carried on through Arch) of the Company and the Cells.*"

All seven of these duties are admitted by Mr Addison, subject only to the qualification in respect of duty (d) that he relies on Article 35 of each of the Cells' Articles of Association and Article 26 of the ICC's Articles of Association and/or on the general disclosure of his conflict of interest in the Scheme Particulars and/or his disclosure at Board Meetings of the Cells and/or his recusal in respect of any investment discussed as part of a Cell's Board decision-making process, and to his contention, in respect of duties (f) and (g) that they are an incident of duty (e). The issues arising from Section G of the Amended Cause do not engage either of duties (b) and (c), but do rely on the five other duties.

16. In relation to that Section G, dealing with the investments relating to Lonscale, Mr Addison first admits some of the background, relating to Lee Barkman, who at all material times was a shareholder in and an agent of Foundations Capital Limited ("FCL"), a company incorporated in the British Virgin Islands. The Plaintiffs refer to there being a close business relationship between Arch and FCL from 2006, which Mr Addison denies, although he admits that Foundations Holdings Limited ("FHL") was incorporated in the Isle of Man on 15 December 2006 and that, from 27 December 2006, the shareholders in FHL were Arch Group UK Limited ("Arch UK") and FCL, their respective holdings being 35% and 65%, and that by 10 January 2007, Arch UK owned 280,000 preference shares in FHL. Mr Addison further denies that Arch

and FCL intended FHL to be the corporate vehicle for establishing an investment fund managed by FCL.

17. The Plaintiffs contend that in or about July 2007, FCL made Arch aware of an opportunity for some of the Cells to be involved in the acquisition of, and to invest in, Club Easy Group plc, Club Easy Property (UK) Limited and Hayes Limited, collectively known as "the Club Easy Group", which owned and operated student accommodation. In response, Mr Addison admits the Group's ownership, but refers instead to Mr Barkman approaching Arch to assist him in negotiating and structuring a purchase of the Group, using Arch's expertise as a corporate financier and negotiator to assist in progressing the discussions that were already underway with Jason Hayes, who was selling the Club Easy Group. Mr Addison denies that Arch was approached as a possible source of funding; his expectation being that Mr Barkman and his partners would provide all the necessary funding. During August 2007, Mr Addison states that Arch proposed that the acquisition of the Group be syndicated through AT1, which would issue certain asset-backed notes, which was a proposal that he understood to have been resisted initially by Mr Barkman.

18. The Plaintiffs refer to there being an agreement between Mr Barkman on behalf of FCL and Robin Farrell, who was the Chief Executive Officer of Arch, on its behalf that they would structure the acquisition of the Club Easy Group in such a way that Arch and FCL would each receive a payment in such identical amounts as would result in the total payments to them equalling the difference between the price paid for the Group by the purchaser and the value, or purported value, of the properties, less liabilities (including capital gains tax), or a substantial payment determined in another way. Further, those investors acquiring the Group, funding its acquisition and/or acquiring an investment interest would fund the payments made to Arch and FCL. The Plaintiffs state that it was the intention of Messrs Farrell and Barkman that Arch and FCL, and not any investors in the Group, would obtain the benefit of the purported surplus value arising from the acquisition. Mr Addison denies all of this, explaining instead that the purchase price was at a discount to the value of the Club Easy Group and that he understood there to have been a verbal agreement between Messrs Barkman and Farrell that Arch would receive from Mr Barkman fees representing one half of the difference between the acquisition price and the value of the Group with Mr Barkman retaining the other half. This payment was subject to an overall limit of £6 million. Mr Addison accepts that he knew before the Cells invested in Lonscale Limited that Arch and FCL (or Mr Barkman) would receive a substantial fee, although he did not know the amount or terms of any fee until after the Cells involved were committed to the investment. In particular, he did not know this in August 2007 and only subsequently discovered it between the commitment to invest and 15 November 2007. Any additional difference beyond the limit of £6 million would accrue to the benefit of Lonscale, AT1 and the purchasers of the notes issued by AT1.

19. Mr Addison admits that Lonscale was chosen as the vehicle for the acquisition of the Club Easy Group. That company was incorporated in the Isle of Man on 10 August 2007. He adds that this was done at the instigation of Mr Barkman. He also admits that by three share purchase agreements dated 17 August 2007, Mr Hayes agreed to sell the Group to Lonscale for a total consideration of £16,587,266. That consideration was reduced to £15,043,078 pursuant to an amendment agreed on 29 October 2007. The consideration as reduced was payable in three tranches. £1 million was payable on executing the agreements, £12,218,078 was payable on the completion date and £1,875,000 was deferred. Mr Addison further admits that the share purchase agreements duly completed on 29 October 2007 and, on the same day, the sole issued share in Lonscale was transferred from Mr Barkman to AT1.

20. Prior to 29 October 2007, the Plaintiffs allege that Messrs Farrell and Barkman agreed that the reduction in the consideration paid by Lonscale for the Club Easy Group would increase the

payments made to Arch and FCL and that both Arch and FCL (or Mr Barkman) would each receive £3 million from Lonscale, and that the Cells would fund these payments. Mr Addison denies this, repeating his contentions about what his knowledge of the agreement reached was at these times.

21. In terms of the arrangements made, Mr Addison admits that Arch arranged for AT1 to issue asset-backed notes in three classes, with a nominal value of £10,000 each and a maturity date of 30 April 2013, with the terms in respect of each class differing. Mr Addison adds that the notes were £21 million multi-class limited recourse asset-backed notes, and that the notes were secured against AT1's shareholding in Lonscale. He also admits that the notes were such that AT1's obligation and ability to make payments under them, and the Cells' investment returns on them, depended on the profitability and financial performance of the Club Easy Group, adding that there was an obligation under the class A and class B notes to make fixed coupon payments. He also admits that on or about 29 October 2007, the Cells invested varying amounts aggregating to £20.2 million in class B and class C notes and further that Arch subsequently arranged for some of RE1 and RE2's class C notes to be sold, with the result that both Cells received slightly more than they paid for those particular notes. However, the Plaintiffs' allegation that this all occurred in pursuance of the agreements between Messrs Barkman and Farrell so as to finance the costs of acquiring the Group and paying £6 million to Arch and FCL is denied.

22. Although Mr Addison admits that Arch received £3 million on or about 29 October 2007, he does not admit that this was paid by Lonscale, referring instead to it being paid from Cobbetts solicitors, who acted on behalf of Lonscale and/or Mr Barkman. Mr Addison further understands that Mr Barkman also received £3 million but, because he was not privy to that transaction, cannot plead to it. The Plaintiffs allege that Cobbetts LLP were instructed to hold that sum on behalf of FCL and/or to the order of Mr Barkman. The Plaintiffs allege that the Cells did not authorise either of those payments, to which Mr Addison responds that all payments made were properly payable pursuant to the agreement between Arch and Mr Barkman, and that these were matters that did not require authorisation by the Cells. Further, Mr Addison relies on clause 13 of the IMAs, providing that Arch was not liable to account to each relevant Cell for any profit, commission or any connected transactions.

23. In response to the Plaintiffs' allegations that these payments were funded by the proceeds of the notes purchased by the Cells and that Arch used these Cells' funds to make and/or fund those payments, Mr Addison denies them. He explains that the Cells acquired the notes, thereby advancing £20.2 million to AT1, with the net proceeds of the notes being advanced to Lonscale by AT1, and with Lonscale applying such funds in payment of the consideration due for the purchase of the Group.

24. Mr Addison denies that on or about 5 November 2007 FHL used part of the payment made to FCL to pay £556,152 to Arch UK to discharge liabilities under preference shares and/or loans. He accepts that on 9 November 2007 Arch UK sold 260,000 preference shares in FHL to Mr Barkman and 260,000 preference shares to Philip Montague, Mr Barkman's partner in FCL, for a total consideration of £556,152 and he makes no admissions as to the source of the funding used or as to what Arch had contemplated would happen.

25. At para. 175A of the Amended Cause, the Plaintiffs allege that, through his position as a member of Arch, with him holding finance, operations and compliance roles within Arch, Mr Addison knew, before the Cells invested in Lonscale, that Arch intended that it and FCL would receive the payments of £3 million each, or some similar substantial payment, upon completion of the acquisition of the Club Easy Group and that those payments would be financed almost entirely by the Cells. Mr Addison admits that he held finance, operations and compliance roles in Arch at

this time, and that, before the Cells invested in Lonscale, he knew that Arch and FCL (or Mr Barkman) would receive a substantial fee in relation to the acquisition of the Group, although the amount and terms were not known to him. Having initially understood that the Cells would not be participating, Mr Addison found out that they may invest around 10 to 17 August 2007, at which time he contacted his co-director, Mr Meader, to disclose to him the payment of a fee. Mr Addison infers that Mr Meader would have discussed this with their other co-director, Mr Radford. Mr Addison says that Mr Meader confirmed to him that he was content with the payment of a fee to Arch. Therefore, having become aware that the investment of the Cells could be used directly or indirectly to fund the fees payable, Mr Addison sought and obtained Mr Meader's approval. Mr Addison does not admit that he acquired his knowledge as a result of being a member of Arch. To the best of his recollection, he became aware of the substantial fee at some point between the commitment of the Cells to invest and 15 November 2007.

26. Mr Addison acknowledges that Arch realised that the Club Easy Group would require funding in the two years following its acquisition. He admits the various steps pleaded by the Plaintiffs, which involved RE1 and RE2 acquiring class A notes on a number of occasions (9 January 2008, 28 April 2008, 9 June 2008, 2 July 2008, 6 October 2008, 11 December 2008, 5 January 2009, 19 May 2009, 24 June 2009 and 13 August 2009). He also admits the re-structuring of the notes in March 2009, which had the effect that Lonscale assumed AT1's obligations under the class A and class B notes, the holders of class B notes were given equity notes in Lonscale and the interests of the holders of class C notes were converted into shares in Lonscale.

27. Mr Addison accepts that there was an agreement dated 26 March 2010, as amended in July 2010 and further amended on 15 April 2011 by which the Cells sold their interests in the notes and in the shares in Lonscale to Mr Barkman or a fund controlled or managed by Mr Barkman ("the Disposal Agreement"). The precise terms are in issue. All of this occurred after Mr Addison had resigned as director of the Plaintiffs. The Plaintiffs contend that this disposal took place so as to mitigate the losses sustained and the First Defendant argues that the disposal was at an undervalue. Mr Addison further refers to the investment strategies of the Cells having been altered, which resulted in the Cells' holdings being valued at zero prior to the sales, which had become widely known in the market and which perpetuated the losses within the Club Easy Group, because comparable investments in student accommodation did not suffer such losses over the same period. In their Réplique, the Plaintiffs point out that it was Arch that valued the holdings as at 30 September 2009 at zero and deny that the altered investment strategies resulted in the Cells' losses. Mr Addison does not admit the Plaintiffs' pleading as to what the Cells actually received under the Disposal Agreement.

28. Against those facts, about which there is comparatively little dispute between the parties, the Plaintiffs plead the following breaches of duty against Mr Addison. At para. 180, they allege that, in breach of duties (e), (f) and (g), the First Defendant failed properly to understand the investment which Arch proposed to make in Lonscale by the Cells and/or failed properly to monitor or oversee the conduct of Arch in proposing that investment and/or failed to give due consideration to adequate material information regarding the investment and/or failed to exercise reasonable care and skill in relation to his consideration of that investment. At para. 180A, they allege that, in breach of duties (a), (d) and (e), the First Defendant failed to act bona fide in the best interests of the Cells and/or acted in the affairs of the Cells without disclosing a conflict between the Cells and his interest as a member of Arch in Arch receiving the payment it did and/or failed to exercise reasonable care and skill with regard to the Cells. Mr Addison denies these alleged breaches of duty. In respect of the particulars of breaches given, he indicates where he was aware of certain matters but mostly denies them.

29. The summary of Mr Addison's case (in para. 2 of his Amended Defenses) denies that he acted in breach of duty, explaining that he gave full consideration to the investment made by the Cells, that he properly disclosed any conflict of interest he had, and that his role with Arch meant that he was able to leave it to Arch's investment management team to assess and approve investments. Mr Addison also challenges the existence of any causal link to the alleged losses of the Plaintiffs and, in any event, argues there was a failure to mitigate any loss or damage. He contends that, if he is otherwise liable for any loss or damage, he enjoys an entitlement to be indemnified under the terms of the Articles of Association of the ICC and the Cells.

30. In respect of para. 180 of the Amended Cause, Mr Addison states that, before the investments in Lonscale were made by the Cells, in his capacity as compliance officer for Arch, he considered the proposal to invest so far as it was relevant to compliance and he did not act in the decision-making process. After the investments were made, as a director, he reviewed the investment at board meetings. He asserts that there was no good reason not to make the payment of £3 million to Arch because, had it not been made, it would have been retained by Mr Barkman. In respect of para. 180A, Mr Addison asserts that he disclosed the facts and matters of which he was aware, complying with his fiduciary duties to the Cells. He also refers to Mr Radford subsequently confirming that he was also aware that Arch would receive a fee in respect of the investment. He accepts that he did not prevent the payments totalling £6 million being made, but denies that it was within his power to do so.

31. The losses claimed by the Plaintiffs are set out in para. 182 of the Amended Cause. Had Mr Addison complied with his duties, the Plaintiffs argue that Arch would have been directed not to cause any of the Cells to make the investment in Lonscale. Alternatively, the amount invested by the Cells would have been less and the payments of £6 million would not have been made. The losses for the Cells aggregate to £19,741,795.81. Those losses are not admitted by Mr Addison and, in any event, he denies that these losses were caused by any breach of duty by him. In doing so, he refers to a report that had been prepared by PKF in August 2007 estimating the potential net assets of the Club Easy Group at in excess of £30.5 million and which considered the business to be a substantial and dynamic group that had established a strong brand in the arena in which it operated. It was regarded by Mr Addison as an appropriate investment for the Cells to make. There was no good reason for him to direct the Cells not to invest, which is why he did not do so. Had he as a director not approved the investment in Lonscale, Arch could have procured the removal and replacement of him and his co-directors under Article 25 of the ICC's Articles of Association by reason of its shareholding in the ICC and, save for PF5, could have procured the issuing of a regulation to the directors directing them to approve the investment through its control of the majority of the voting rights in each Cell, with which the directors would have been obliged to comply pursuant to Article 36.1 of each Cell's Articles of Association. Mr Addison further denies that, had he made disclosure to Messrs Radford and Meader in the manner suggested by the Plaintiffs, the effect would not have been that the investments in Lonscale would not have taken place.

32. Mr Addison returns to the question of causation in Section L of his Amended Defenses, contending that Arch would have invested the funds of the Cells in accordance with the terms of the IMAs and, given the market conditions at that time, relating to the global financial crisis, it is probable that losses would in any event have occurred. Mr Addison also contends that the Plaintiffs failed to mitigate their losses (Section M). This arose following the replacement of Arch by Spearpoint Limited ("Spearpoint") on 30 November 2009 as the provider of investment management services to the Plaintiffs and Mr Addison contends that the fee structure in place thereafter incentivised Spearpoint to maximise cash proceeds from investment rather than

managing those investments. The Disposal Agreement meant that the investments in Lonscale were sold at an undervalue.

33. In the event that Mr Addison is found liable to the Plaintiffs, in Section O of his Defenses he raises his entitlement to set off that liability pursuant to his Counterclaim. In this regard, he refers to a right to indemnity contained in the various Articles of Association (Article 37 for the ICC and Article 49 for the Cells). In response, the Plaintiffs deny that there is any entitlement for him to be indemnified. Even if an indemnity is prima facie available, it does not assist Mr Addison by virtue of sections 157 to 159 of the Companies (Guernsey) Law, 2008 and/or section 10 of the Protection of Investors (Bailiwick of Guernsey) Law, 1987.

34. The final means by which Mr Addison seeks to be excused from any liability attaching to him in respect of the investments relating to Lonscale is by praying in aid relief pursuant to section 522 of the Companies (Guernsey) Law, 2008. He avers that he acted honestly and reasonably in all the circumstances and so should be excused from liability. The Plaintiffs deny that any such relief is available to him.

35. The Deputy Bailiff drew the attention of the Jurats to the issues that the parties had identified as arising from their respective pleaded cases as set out in the pre-trial memorandum. Amongst other things, they should consider the duties owed by Mr Addison to the Plaintiffs, which were largely admitted, and how, if at all, they were affected by the appointment of Arch as the investment manager. In general terms, they were to consider the practical arrangements made for managing and administering the operation of the Cells. In respect of the investments made in Lonscale, they might wish to consider how Arch and Mr Barkman inter-related, including FCL and FHL. They ought to consider what Mr Addison knew at the material times about the transaction and how it evolved, particularly in relation to the payment of the monies to Arch and to the order of Mr Barkman. They might wish to piece together chronologically the mechanics for that transaction. The Jurats might look at the value of the Club Easy Group and the problems, if any, that it faced and consider what plans, if any, Arch had and communicated to the Plaintiffs in relation thereto. They might wish to consider the due diligence undertaken, including whether it was adequate, and what options remained open to the Cells prior to completion of the transaction. They might wish to focus on the dispute about whether or not Mr Addison made any disclosure to Mr Meader and, if he did, when that was and whether it was sufficient disclosure for the purpose of complying with his duties. When they had found those facts, they would need to decide whether or not Mr Addison had acted in breach of any of the duties on which the Plaintiffs rely. If they found that there had been one or more breaches of duty, they would move on to consider whether the Plaintiffs had proved that the losses they claim to have sustained had been caused by any of those breaches. If satisfied that Mr Addison is prima facie responsible for some or all of that loss, the Jurats would then need to consider if Mr Addison had satisfied them that the Plaintiffs had failed to mitigate their losses when realising the investments made in Lonscale. To the extent that the Jurats found Mr Addison liable in any amount, they would proceed finally to consider whether or not he benefits from an indemnity under the ICC and Cells' constitutional instruments and, if not, whether to afford him relief in accordance with section 522 of the Companies (Guernsey) Law, 2008. Throughout their deliberations, the Jurats should revert to the way the case against Mr Addison has been pleaded on behalf of the Plaintiffs and his pleaded response to it.

The evidence

36. The Court was provided with a large number of documents. In the event, comparatively few of them were referred to at the trial and, in some instances, the Court was invited to look at an example of the documentation on the basis that the documents appeared in similar terms for each

of the Cells. Examples of this included the Articles of Association, the Scheme Particulars and Supplemental Scheme Particulars, the IMAs and the administration agreements. What appears to be a fairly comprehensive set of Board minutes and packs from 2007 to early 2010 have been supplied. From the many documents spanning that same period, those most relevant were helpfully extracted into a manageable core bundle. The Court was also provided with bundles relating to other proceedings in which Mr Addison has been involved. The first of those proceedings was the joined action by the ICC and the Cells against Arch and against Mr Farrell, which resulted in a judgment handed down by Walker J on 18 December 2014 (*SPL Private Finance (PF1) IC Limited v Arch Financial Products LLP* [2014] EWHC 4268 (Comm)). The second was the regulatory proceedings against Arch, Mr Farrell and Mr Addison brought by the Financial Conduct Authority, which resulted in a decision of the Upper Tribunal (Tax and Chancery Chamber) released on 19 January 2015 ([2015] UKUT 0013 (TCC)).

37. The Court heard evidence from five witnesses. The first was William Scott, a director of the ICC and the Cells, who was first appointed on 31 December 2009. His witness statement dated 29 July 2016 stood as his evidence-in-chief. He was cross-examined on behalf of Mr Addison by Advocate Williams for the morning of the second day of the trial and a little into the afternoon, and then re-examined by Advocate Richardson. The second witness for the Plaintiffs was John Davey, who had been the Chief Executive Officer of Spearpoint from 1 April 2008 until 31 March 2014, although Spearpoint changed its name to Brooks MacDonald Asset Management (International) Limited in November 2012. His witness statement dated 28 July 2016 similarly stood as his evidence-in-chief. He was cross-examined for the remainder of the second day and for half of the morning on the third day, and then briefly re-examined. The Court asked more questions of Mr Davey than it did of Mr Scott. The third witness was Mr Addison. His first witness statement dated 29 July 2016, subject to a handful of corrections he wished to make, and his second witness statement dated 25 January 2017 stood as his evidence-in-chief. He was then cross-examined by Advocate Richardson for the remainder of the third day of the trial and for the whole of the fourth day. On the morning of the fifth day, because Mr Addison had produced a document to substitute for a small part of his first witness statement (being a table in para. 27 thereof), Advocate Williams was permitted to ask him a few question about it, being treated as part of his examination-in-chief, and Advocate Richardson then resumed cross-examining him for the remainder of the morning. Mr Addison was re-examined by Advocate Williams at the beginning of the afternoon and the Court sought various points of clarification from him thereafter.

38. The Court also heard expert evidence on behalf of Mr Addison from Andrew Tyrtania and on behalf of the Plaintiffs from Simon Moore. Their field of expertise is investment management. Permission was given to the parties pursuant to Part II of the Evidence in Civil Proceedings (Guernsey and Alderney) Rules, 2011 to rely on their evidence to assist on matters of loss. They both gave their evidence on the sixth day of the trial. The Court heard first from Mr Tyrtania, whose reports dated 8 September 2016 and 6 January 2017, the latter being a response, stood as his evidence-in-chief. He was cross-examined by Advocate Richardson and very briefly re-examined by Advocate Williams. Similarly, Mr Moore's report dated 11 November 2016 stood as his evidence-in-chief. His cross-examination by Advocate Williams occupied the remainder of the morning and was more extensive than the cross-examination of Mr Tyrtania. Mr Moore was briefly re-examined that afternoon. Both experts also confirmed that the Note of the discussion, which took place at a meeting on 27 January 2017, reflected the areas on which they agreed and where there remained aspects of disagreement.

39. The Court has noted that both witnesses of fact giving evidence on behalf of the Plaintiffs were not involved in the transaction relating to the Club Easy Group in 2007. Accordingly, as

explained in Advocate Richardson's written opening submissions, the Plaintiffs rely on the facts that have been admitted and the documentary evidence generated at the material times, and the expert evidence. Advocate Williams points out that there is no one to contradict the evidence of Mr Addison about the events to which he was a party. The Deputy Bailiff directed the Jurats that such a submission accurately reflects the fact that the witnesses for the Plaintiffs and the First Defendant overlapped only very briefly in respect of the matters under consideration but the Jurats still needed to form their own views on whether the evidence of each witness was reliable and credible.

40. The Deputy Bailiff further directed the Jurats that they were not to speculate on what might have been said by others who were involved in 2007 and thereafter had they been called to give evidence. By way of example, there has been no evidence from Messrs Meader and Radford. It was open to either of the parties to adduce evidence from one or other of these people, but that has not happened. The facts that they have pleaded in their Defenses have not been supported by sworn evidence and they have not been tested under cross-examination. The Jurats were directed that what they pleaded could be regarded as hearsay evidence, but the relevance and the weight to be accorded to such evidence is very much for the Jurats to assess. There has also been no evidence given by Mr Farrell or Mr Barkman, but they both feature quite prominently in the documentary exchanges. Neither has had the opportunity to explain what is written down and the Jurats were reminded not to attempt to guess what any explanations might have been, whether from these two gentlemen or from the authors of any of the other documents placed before the Court.

41. The impression that each of the witnesses heard at the trial had on the Jurats is as follows. They observed that Mr Scott is an experienced, professional non-executive director. He dealt with questions in a calm, articulate manner and gave the impression of dealing with matters honestly and providing complete answers in a simple manner. At times his style was overly formal, but the Jurats accept his evidence as truthful. The Jurats recognise that Mr Davey is an experienced, professional investment manager. He responded clearly to questions relating to the decisions reached to dispose of the investment in Lonscale once Spearpoint had been appointed to replace Arch. The Jurats found his answers to the lengthy questioning of him about his reasons for providing personal loans to Lonscale following its disposal to be sound and in the best interests of the ICC and the Cells. The Jurats regard his evidence as clear and cogent and it was accepted as truthful. Neither Mr Scott nor Mr Davey shifted their positions on their evidence as a result of being cross-examined. Mr Addison appeared to the Jurats to have been less well-prepared than he might have been, particularly at the start of his evidence. Some of his answers to questions struck them as evasive. The Jurats were left with the impression that Mr Addison was anxious to minimise his own role in respect of the process that was followed to conclude the investments in Lonscale. In particular, the Jurats were unimpressed at him appearing to feign ignorance about documents he must have seen at the time and which he should have reviewed before giving his evidence. In relation to his role as a director of the ICC and the Cells, the Jurats find that his previous experience had not adequately prepared him for the role that he was to fulfil in that capacity and that he had not acted in the manner that he should have. In general, the Jurats consider that Mr Addison was out of his depth. They were unpersuaded by his answers on the topic of how he managed his conflict of interest, finding them unconvincing. They felt that Mr Addison chose not to be candid with the Court in relation to the extent of his knowledge about the transaction involving Lonscale, believing that he set out to mislead the Court about this. Overall, they do not accept all the evidence given by Mr Addison and treat his evidence generally, even where no evidence has been given directly contradicting it, with some caution.

42. Turning to the two experts, the Jurats note how the initial report of Mr Tyrtania had been prepared without having had sight of documents that he really needed to review before opining. However, once he saw those documents, his opinion changed. The position reached between him and Mr Moore after they met is viewed by the Jurats as being a reasonable and credible position for them to adopt. In particular, the Jurats regard their agreement as to the value achieved on the disposal of Lonscale as being particularly helpful. Mr Moore was observed to have been well prepared throughout the process. His report was comprehensive and dealt with the issues that needed to be addressed in a manner that the Jurats find clear and understandable. His evidence offering explanations about the method of valuing a business such as the Club Easy Group and his analysis of its value at the time of acquisition and subsequently, albeit he recognised that a larger sample of comparable property values would have been desirable, is considered by the Jurats to be both credible and compelling.

Relevance of previous proceedings

43. The Deputy Bailiff directed the Jurats about the limited use that could be made of the materials that related to the proceedings in England and Wales before Walker J and the regulatory proceedings culminating in the decision of the Upper Tribunal in the following terms. This had been an issue he addressed at the pre-trial review held on 19 December 2016 and 4 January 2017, but which had been left open, in accordance with the agreed pre-trial memorandum until the trial. It was only at the trial that the Plaintiffs decided not to pursue the reliance that had previously been indicated would be made on these decisions as raising an estoppel. The Plaintiffs' written opening submissions also contained arguments that it would be an abuse of process for Mr Addison to be permitted to re-litigate matters that had already resulted in findings being made rejecting the contentions he wished to repeat. Finally, it has been submitted that the findings made should be regarded as prima facie evidence and something compelling by way of new evidence is required for this Court to reach contrary findings. Because the approach taken at trial by Advocate Richardson was different, the Deputy Bailiff does not have to resolve those questions, however interesting they may be, and so was able to confine himself to some general directions to the Jurats.

44. The fact that Mr Addison had participated in the proceedings as a representative of Arch and that judgment had been entered by Walker J against Arch (and against Mr Farrell) was obviously a matter of public record and known to the Jurats, but it did not mean that they were being invited simply to rely upon the findings made as establishing the matters with which they were charged by virtue of sitting on this trial. Instead, they were directed that they needed to reach their own conclusions on the basis of the evidence adduced before the Court at this trial. In particular, just because Arch had been found to have breached its fiduciary duties to the Plaintiffs and to have been negligent did not mean that Mr Addison had breached his duties as a director of the ICC and the Cells. Further, the facts found by Walker J were based on the evidence that that court had heard and considered which might not be the same as the evidence before this Court. A similar approach needed to be taken in respect of the decision of the Upper Tribunal. The focus in those proceedings was about Mr Addison's role within Arch and not his role as a director of the ICC and the Cells. Although there were inevitably significant overlaps in the matters that had already been considered in those sets of proceedings with the facts underlying the allegations made against Mr Addison before this Court, the Jurats were reminded of the need for each of them to approach the evidence they had to consider as if there had not been any prior findings in another jurisdiction.

45. At the pre-trial review, the Deputy Bailiff largely rejected an application made on behalf of Mr Addison dated 22 November 2016 by which he sought to exclude these decisions as being inadmissible evidence. He did so because the decisions themselves were admissible by virtue of

section 15 of the Evidence in Civil Proceedings (Guernsey and Alderney) Law, 2009 to prove the outcomes of those proceedings and Advocate Williams had not opposed including the transcripts in the trial bundles because it was acknowledged that they were capable of being used for the purposes of cross-examination anyway. The distinction drawn at that time was as to the use to which any of these documents was to be put. The question of whether there was an estoppel on which the Plaintiffs could rely raised further issues, including the extent to which the rule in *Hollington v F Hewthorn & Co. Ltd* [1943] 1 KB 587 applies as a matter of Guernsey law, which no longer need to be determined. The Deputy Bailiff did, however, adopt the position set out in *Al-Hawaz v The Thomas Cook Group Limited* (unreported, 27 October 2000), in which Keene J identified that the principles from the *Hollington* case:

> "*... prevent the findings made in earlier civil cases from being used subsequently as evidence of the facts found. They do not in themselves operate as a bar to the findings being put by way of cross-examination as to credit, subject to the control of the court ...*".

Accordingly, in respect of the trial, the Deputy Bailiff directed the Jurats that the extent to which there had been questioning of Mr Addison about his involvement in the previous proceedings was an aspect of his evidence to which they were entitled to have regard for the purposes of assessing his overall credibility but not as a means of endorsing any findings about which he was asked. Their findings needed to be reached independently of the answers Mr Addison gave to any such questions and to be based on other evidence and not, for example, result in them concluding that, if they did not believe his answer, it followed that the finding made about which he had been asked must be made by them without more ado. In reaching any conclusion about Mr Addison's credibility and how that affected the Jurats' assessment of the remainder of his evidence, they were reminded that the findings in the decisions themselves were not being relied upon directly against Mr Addison. In other words, they were directed not to consider the findings themselves and then whether there had been any new evidence pointing to alternative findings being appropriate but rather to concentrate on the evidence placed before them, including Mr Addison's responses in cross-examination, before deciding what factual findings they were each minded to make.

46. The Deputy Bailiff also directed the Jurats that they should generally disregard section IV of the Plaintiffs' written opening submissions. In particular, they were not to concern themselves with any possible suggestion that Mr Addison was abusing the process of the Court. The Plaintiffs had chosen not to pursue the lines of argument set out in that section and were relying instead on the Court making findings that would support their case that Mr Addison had been in breach of his duties as a director of the ICC and the Cells and that those breaches caused the losses in respect of which the Plaintiffs sought damages.

Overview of issues

47. When they were considering the evidence and making factual determinations, the Jurats were reminded by the Deputy Bailiff that the Plaintiffs' claim was based on the duties set out in the pleadings, which were largely admitted to exist, which meant that the first matter to consider was whether the Jurats found that Mr Addison had breached any one or more of the duties in the manner claimed. If there were to be no findings of breach, the Plaintiffs' action would have to be dismissed. However, if the Jurats found one or more breaches of duty, they would proceed to consider whether any one of those breaches (or possibly a combination of them) led to the losses claimed (or any part of those losses). If they found that there was such a causal link, prima facie, the Plaintiffs would have proved their case. The order in which they chose to consider the breaches was entirely a matter for them, but the issue on which the Plaintiffs had concentrated at the trial was the question of whether Mr Addison had, as he claimed, made disclosure to his

fellow directors of the ICC and the Cells of the conflict of interest of Arch (and by extension his own conflict of interest) or not. If the Jurats were to find that there had been no disclosure at all, they might find that it followed that the breach of duty had been established. However, if they found that there had been some disclosure, they would proceed to consider whether that disclosure was adequate or not. In doing so, they would need to consider what knowledge Mr Addison had at any time. If Mr Addison did not make the level of disclosure that he should have, they would then be able to conclude that a breach of duty had been established by the Plaintiffs. The Jurats were reminded that they could have regard to the explanations offered by Mr Addison at various times. Throughout the process, they were deciding what was more likely than not and had to recognise that the Plaintiffs had the burden of proving their case.

48. If they were satisfied that any given loss resulted from Mr Addison breaching his duty as a director, they would have to turn to the question of whether Mr Addison was correct that the Plaintiffs had failed to mitigate some or all of the loss that would otherwise be found by them. In this regard, the evidence of the expert witnesses plays a more central role. The Jurats were invited to ask themselves whether they were satisfied that Lonscale had been sold at an undervalue. Any finding of a failure to mitigate the Plaintiffs' losses could extinguish or reduce Mr Addison's liability for the losses established. If the Jurats considered, after addressing the question of mitigation, that Mr Addison was liable to the Plaintiffs for some loss, they should turn to the indemnity provisions and, subject to the directions of the Deputy Bailiff on how the indemnity provisions fall to be construed and any impact of the provisions of the 2008 Law, decide whether Mr Addison had brought himself within the terms of any indemnity available to him. Finally, if the Court remained of the view that Mr Addison had some liability towards the Plaintiffs, the Jurats would turn to whether or not this was an appropriate case, as submitted by Advocate Williams, in which to afford Mr Addison the relief available under section 522 of the 2008 Law.

Facts

49. Many of the facts are supported by references in the documentation to which the Court has been referred. Where applicable, references to the document in question are given using square brackets identifying within the page numbering found in volumes F and G of the trial bundle and, very occasionally, by reference to where else within the trial bundles the document can be located.

2004-2006

50. The genesis of Arch is explained by Mr Addison in his first witness statement. Arch was incorporated in November 2004. Mr Farrell, as its CEO and the person who had a substantial beneficial interest in the business of more than 80%, began a structuring and corporate advisory business, but intended to diversify into a number of business lines including investment management.

51. Mr Addison joined Arch in March 2006. He believes that Mr Farrell asked him to join. His previous experience included working for NatWest Markets and during part of that period of employment he had been authorised as an investment adviser only for two or so years before leaving in 1997. He subsequently worked for UBS, when he was authorised by the Financial Services Authority ("the FSA"). He was made redundant by UBS in 2003. He then did some self-employed consultancy work, when he was not regulated, and worked for a couple of other companies, and held an authorisation during the second of those periods of employment.

52. Mr Addison took on the finance, operations and compliance roles within Arch. He describes his involvement as being focused on facilities and human resources functions. He was authorised by the FSA to perform an advising/marketing function but had no authorisation to perform any discretionary investment function. Arch itself was authorised by the FSA to carry on regulated investment management activities. Mr Addison was a partner of Arch. He held a 0.1% beneficial interest in Arch. He was also a shareholder in Arch UK. Between 29 June 2006 and 25 April 2007 his interest was 0.178% and from 25 April 2007 until when he resigned as a director of the ICC and the Cells, his interest in Arch UK rose to 0.206%, which continued to be the size of his shareholding in Arch International Group Holdings Limited, which was created as the holding company of Arch UK from about February 2008. It is apparent that his beneficial interest was dwarfed by the dominant beneficial interest of Mr Farrell. Mr Addison states that his income over the period from December 2006 to March 2009 was approximately £265,000.

53. In 2006, Arch developed and launched a series of investment funds. An open-ended investment company ("OEIC"), known as CF Arch Cru Investment Funds, was used. Capita Financial Managers Limited ("Capita") was appointed in July 2006 to act as the Authorised Corporate Director ("ACD"). Capita delegated the investment management role to Arch. There were two sub-funds. Arch subsequently took over the investment management role for a second OEIC authorised by the FSA, which was renamed CF Arch Cru Diversified Funds. Capita was once again appointed as the ACD and the investment management role was delegated to Arch.

54. During 2006, Arch became aware of the type of fund structure permissible in Guernsey through using an incorporated cell company. The Incorporated Cell Companies Ordinance, 2006 was made by the States of Deliberation on 26 April 2006 and entered into force on 1 May 2006. Section 5 of that Ordinance provided that an incorporated cell company could, by special resolution, incorporate one or more incorporated cells. Section 9 provided that an incorporated cell is a company and has the same registered office and directors as the incorporated cell company. The assets and liabilities of the incorporated cell company and each of the cells had to be kept separate (section 10). Arch considered that this type of structure could be used to provide the two OEICs and other investors with the opportunity to invest in shares in entities holding a more diversified range of assets than might otherwise have been possible. The ICC was incorporated on 21 December 2006.

55. In the meantime, a relationship had been commenced between Arch and Mr Barkman's business interests. By way of example, on 18 October 2006, Mr Barkman sent an e-mail to Mr Addison attaching some notes prior to a meeting scheduled for 20 October 2006, which Mr Addison then forwarded to Mr Farrell [pp. 1948-51]. Mr Barkman referred in his notes to FCL and saw opportunities for FCL and Arch to work together in a number of ways. In accordance with Heads of Agreement [pp. 1971-1987] signed by Mr Barkman and Philip Montague, described therein as the Principals, FCL, identified as a BVI company with a registered office in Hong Kong, and Arch UK and Arch on 30 November 2006, those parties intended to enter into a joint venture, a "NewCo" to be incorporated in the Isle of Man, owned 65% by FCL and 35% by Arch UK and Arch. Reference was made in that document to FCL's associated investment vehicles, the Foundations Program plc and its initial subsidiary FPA Limited, noting that FCL had been loss-making whilst setting up this structure. The long-term strategic plan for this NewCo was to expand it with a view to an IPO or sale of it over a period of five years or so. The ordinary shares to be subscribed for by FCL would be of a different class to the shares to be subscribed for by Arch UK and Arch, which would also subscribe for 1,160,000 cumulative redeemable Preference Shares bearing a dividend of 10% per annum. It was envisaged that Mr Addison would join Messrs Barkman, Montague and Farrell as directors of the NewCo. The timetable for the venture

was to finalise and sign all documentation on 13 December 2006 with the first subscription of £280,000 to be made two days later. This is what became FHL.

56. Mr Addison explained that Arch had initially looked at opportunities in Jersey, but found that it did not meet that jurisdiction's requirements, so they contacted a number of administrators in Guernsey to speak with them with a view to selecting one with which to work. One of the entities contacted was Bordeaux. Mr Meader was very amicable, inviting representatives from Arch to come to Guernsey and then showing them around. Mr Meader was very proactive and Bordeaux's fees were regarded by Arch as reasonable. By the end of October 2006, Mr Addison was in e-mail correspondence with Mr Meader addressing the use of Moore Stephens as auditors and commenting on draft scheme particulars that had been provided by the firm of Advocates, Carey Olsen. On 2 November 2006, Mr Addison sent to Mr Meader an e-mail attaching a draft IMA that he suggested each cell would enter into with Arch [p. 1955]. The following day, Mr Addison provided updated scheme particulars for the ICC and one cell to *inter alia* Mr Meader [p. 1968], from which it is apparent that Mr Addison was proposing changes to the content, eg, at the end of his message, he wrote:

> "*... we describe two material contracts of the ICC being the administration agreement and investment management agreement with schedules for each cell company. Given the unique and untested nature of the legal identity of the ICC structure I would prefer to see a separate agreement entered into with each cell to maintain the integrity of the separate legal identity of each cell.*"

On 14 December 2006, Carey Olsen provided to Messrs Addison and Farrell constitutional documents for the ICC and one cell and indicated *inter alia* that they were finalising the administration and investment management agreements [p. 1992]. Within minutes, Mr Addison replied stating that "*We have already done the investment management agreements and don't require Carey's input on those.*"

57. Mr Addison stated in his evidence that he was taking his guide from Mr Radford and Mr Meader as to how the ICC should be run. Obviously, they wanted the majority of the decision-making to be taken offshore, but he did not know whether it was his own idea or an idea of Mr Farrell that he should be the Arch-nominated director. He accepted that it was probably an idea of one of them.

Incorporation of ICC and Cells

58. When the ICC was incorporated on 21 December 2006, six cells were also incorporated. They were Arch Cru Private Finance IC Limited (the original Second Plaintiff, "PF1"), PF3, Arch Cru Private Equity IC Limited (the original Ninth Plaintiff, "PE1"), Arch Parallel Private Equity IC Limited (the original Tenth Plaintiff, "PE2"), Arch Sustainable Opportunities IC Limited (the original Sixteenth Plaintiff, "SO1") and Arch Cru Sustainable Opportunities IC Limited (the original Seventeenth Plaintiff, "SO2").

59. Article 5 of the Articles of Association of the ICC provides:

> "*The Directors may appoint as Investment Manager and Administrator any suitably qualified corporations to manage the company's administrative and/or secretarial affairs and the Investments of each of its Cells and may entrust to and confer upon the Investment Manager and Administrator so appointed any of the relevant functions, duties, powers and discretions exercisable by them as Directors, upon such terms and conditions, including the right to remuneration payable by the Company, and with such*

powers of delegation and such restrictions as they think fit and either collaterally with or to the exclusion of their own powers."

Article 5 of the Articles of Association of each Cell similarly provides:

"*The Directors may appoint as Investment Manager and Administrator any suitably qualified corporation to manage the Cell's administrative and/or secretarial affairs and its Investments and may entrust to and confer upon the Investment Manager and the Administrator so appointed any of the relevant functions, duties, powers and discretions exercisable by them as Directors, upon such terms and conditions, including the right to remuneration payable by the Cell, and with such powers of delegation and such restrictions as they think fit and either collaterally with or to the exclusion of their own powers.*"

60. Article 25 of the Articles of Association of the ICC makes provision for the retirement and removal of directors. The office of director must be vacated if the director is removed from office by ordinary resolution (Article 25.1.7) or if he is requested by a majority of the other directors (not being less than two in number) to vacate office (Article 25.1.6).

61. Article 37.1 of the Articles of Association of the ICC provides:

"*Subject to the Law, the Directors, agents, Secretary and other officers or servants for the time being of the Company and every one of them, and every one of their heirs and executors, shall be indemnified and secured harmless out of the assets and profits of the Company from and against all actions, costs, charges, losses, damages and expenses in respect of which they may lawfully be indemnified, which they or any of them, their or any of their heirs or executors shall or may incur or sustain by reason of any contract entered into or any act done, concurred in, or omitted in or about the execution of their duty or supposed duty in their respective offices or trusts, to the extent that due care and diligence had been exercised and the amount for which such indemnity is provided shall immediately attach as a lien on the property of the Company and have priority as between the Shareholders over all other claims.*"

Article 49.1 of the Articles of Association of each Cell makes similar provision, save that the reference is to "the Cell" rather than to "the Company".

62. On 12 January 2007, the ICC and the six Cells that had been incorporated each held its first board meeting. Mr Addison attended all seven by telephone. Messrs Radford and Meader attended in person. The minutes produced show that the business of each meeting was largely formal. At each meeting, an instrument dated 21 December 2006 appointing Messrs Radford, Meader and Addison as the first directors of the company was produced. Bordeaux was appointed as company secretary. Fortis Bank (CI) Limited ("Fortis") was appointed as custodian. Moore Stephens were appointed as auditors. The two shares that had been subscribed in each were transferred to Geoffrey Tostevin and Jacqueline Fallaize respectively. The authorisations of the ICC on 8 January 2007 and the Cells on 12 January 2007 by the Guernsey Financial Services Commission ("the GFSC") were noted. In respect of each, the Scheme Particulars and Supplemental Scheme Particulars were tabled and each meeting noted that they had been approved by the GFSC. At the meeting of the ICC, there was a report that the CISX had requested some alterations to the Scheme Particulars to comply with their listing requirements, to which Mr Addison commented that "*they required the initial funds to be listed prior to the end of January*". In respect of each of the Cells, there was a resolution that application be made to the CISX for the listing of an unlimited number of participating preference shares. Mr Addison noted

that the launch date for each Cell, with the possible exception of PF3 (although the minute in respect of SO2 is the only one to refer to a possible delay), would be 22 January 2007. The administration agreements for each with Bordeaux were tabled and, for each Cell, an investment advisory agreement with Arch and a custodian agreement with Fortis were tabled. The timings recorded, however, are rather odd, showing some overlaps. The meeting in respect of PF3 began at noon and lasted 30 minutes [p. 523]. The meeting in respect of SO1 began at 2 pm and also ended at 2 pm [p. 526]. The meeting in respect of the ICC began at 3 pm and lasted one hour [p. 521]. The meeting in respect of PE1 also began at 3 pm and lasted 40 minutes [p. 515]. The meeting in respect of SO2 began at 3.10 pm and lasted 10 minutes [p. 529]. The meeting in respect of PF1 began at 3.40 pm and lasted 30 minutes [p.518]. The meeting in respect of PE2 began at 4 pm and lasted 20 minutes [p. 512].

63. The IMA between PF3 and Arch, which was executed on 28 December 2006, provides the template that was used subsequently in respect of the other Cells [p. 363]. It states that its governing law is English law. Clause 4(a) of the IMA provides that:

> "*The Investment Manager will manage the Portfolio within the investment objectives and investment policy as set out in the Prospectus. Subject to such objectives and restrictions, the Investment Manager, will have complete discretion for the Company's account (and without prior reference to the Company) to buy, sell, retain, exchange or otherwise deal in investments and other assets, enter into derivative transactions including contingent liability transactions, effect short sales, deal in physical commodities, make deposits, subscribe to issues and offers for sale of, and accept placings, underwritings and sub-underwritings of, any investments, effect transactions on any markets, take all day to day decisions and otherwise act as the Investment Manager judges appropriate in relation to the management of the Portfolio. The Investment Manager may also provide assets of the Portfolio as collateral or margin against certain transactions and positions undertaken by it on behalf of the Company.*"

By clause 1.3, "Portfolio" is defined as "*all the assets (including uninvested cash) of the Company and entrusted from time to time by the Company to the day-to-day discretionary management by the Investment Manager.*" By clause 1.4, "Prospectus" is defined as "*the offering document hereby [sic] shares in the Company are offered to investors and any supplemental or replacement documentation having similar effect.*" Clause 4(d) draws the Cell's attention specifically to the risk warning notice in schedule B and recommends it to consult an independent advisor if any matter is not clear. The risk warnings in schedule B state that they need to be read in conjunction with the risk warnings set out in the Prospectus. They cover futures, swaps, options and contracts for differences, noting that these can be highly volatile, short selling and borrowing and identify that certain investment positions may be illiquid.

64. Clause 6 of the IMA is headed "Instructions and Communications" and provides:

> "*a) Instructions from the Company (other than instructions to amend this Agreement to which paragraph 3 applies) shall be acknowledged by the Investment Manager acting upon them unless the Company is advised that the Investment Manager believes such compliance may not be practicable or might involve either party to be in contravention of any law, rule or regulation.*
>
> *b) The Investment Manager may rely and act on any instruction or communication which purports to have been given (and which is reasonably believed to have been given) by or on behalf of any person notified by the Company from time to time as being authorised to instruct the Investment Manager in respect of the Portfolio by*

whatever means transmitted and whether or not in writing and, unless the Investment Manager shall have received written notice to the contrary, whether or not the authority of any such person shall actually have been terminated.

c) Subject to b) above, any instruction or communication to be given to the Investment Manager under this Agreement shall be in writing and sent to the registered office or otherwise as notified to the Company and shall take effect upon actual receipt by the Investment Manager."

65. Clause 13 of the IMA is headed "Potential Conflicts of Interest and Disclosures" and provides:

"*The Investment Manager may without prior reference to the Company, effect transactions in which or provide services in circumstances where the Investment Manager has, directly or indirectly, a material interest or a relationship of any description with another party which may involve a potential conflict with the Investment Manager's duty to the Company. The Investment Manager shall not be liable to account to the Company for any profit, commission or any connected transactions and the Investment Manager's fees shall not, unless otherwise provided, be abated thereby. For example, such potential conflicting interests or duties may arise because:-*

a) the Investment Manager undertakes business for other clients;

b) any of the Investment Manager's directors or employees is a director of, holds or deals in securities of or is otherwise interested in any company whose securities are held or dealt in on the Company's behalf;

c) the transaction is in securities issued by a client;

d) the Investment Manager may act as agent for the Company in relation to transactions in which it is also acting as agent for the account of other clients;

e) the Investment Manager may have regard, in exercising its management discretion, to the relative performance of other funds under its management;

However, the Investment Manager shall at all times have due regard to its duties owed to the Company and the Company [sic] and where a conflict arises it will endeavour to ensure that it is resolved fairly. Furthermore, where the Investment Manager could:-

(i) allocate an investment between two or more funds or accounts which it manages (including the Company); or

(ii) make a disposal of investments held by two or more such funds or accounts,

it will act fairly as between the relevant funds or accounts in making such allocation or disposal, having regard to, inter alia, factors such as cash availability and portfolio balance."

66. The fees payable to Arch under the IMA were set out in schedule A, to which reference is made by clause 14. Those fees comprised a management fee equal to 1% per annum based on the net asset value of the Cell, which accrued monthly and was to be paid monthly in arrears, as well as a performance fee, paid quarterly in arrears following the end of each quarter of a calendar year. The performance fee payable by the Cell to Arch was 10% of any increase in the net asset value per share of the fund by reference to any previous quarterly performance period or £1. Payment

was subject to the rate of return of the fund not falling below the cumulative hurdle rate (Sterling LIBOR plus 4%) in respect of the performance period in question.

67. The Scheme Particulars of the ICC are dated January 2007 [p. 116]. The link to Arch is explained in a number of places, including (on page 17):

> "*Investment management agreements (the "Investment Management Agreements") dated on or around 28 December 2006 are entered into between the ICC's first Cells and the Investment Manager whereby the Investment Manager has been appointed to be responsible for the management of each Cell's assets on a discretionary basis. Under the Investment Management Agreement, the Investment Manager has the authority to delegate the discharge of some of its functions under the agreement to an Investment Adviser. Each agreement will continue until terminated by either side on six months' notice or on shorter notice in the event of, inter alia, breach of contract or insolvency.*"

In respect of fees, these Scheme Particulars acknowledge that "*The ICC has agreed with the Investment Manager that the Investment Manager shall be entitled to fees from each Cell for its services under the Investment Management Agreement*" and "*The Investment Manager is entitled to pay a trail fee out of the investment management fee it receives to any intermediary*".

68. There is a section in the document about the management and organisation of the ICC, which includes the following description of Mr Addison (on page 16):

> "*Mr. Addison is Chief Operating Officer for the Arch Group and a member of the Risk Committee. He has responsibility for the implementation of the Arch investment funds and products. Mr Addison has sixteen years of investment experience with a particular focus on specialist funds, structured products, operations and risk management.*
>
> *Prior to joining Arch in 2005, Mr Addison managed his own structuring and derivatives consultancy where he oversaw the development and launch of a number of innovative investment funds. From 1997 to 2003 Mr Addison served as Director of Risk Management Products at UBS Investment Bank, dealing in equities, equity derivatives and alternative investments. He worked in a similar capacity with NatWest Markets from 1990 to 1997.*
>
> *Mr. Addison has authored numerous articles in the trade press and several book chapters on structured products and employee share schemes. He is an Economics graduate of University College, London.*"

69. The Scheme Particulars begin by referring to the risk factors, highlighting the high degree of risk involved and the possibility that there may be significant losses. This is emphasised by the concluding paragraph in bold type (on page 11):

> "*Potential investors who are in any doubt as to the risks involved in investment in the ICC's Cells are recommended to obtain independent financial advice before making an investment. Investment in any Cell should be made only after consulting with independent, qualified sources of investment and tax advice. Each investment in a Cell is speculative involves a higher degree of risk and may result in the loss of the entire investment. Such investment is only for sophisticated investors who understand the risks involved and who have no need for liquidity of investment.*"

This section also includes the following statement:

"*Investors should be aware that the Investment Manager, Investment Advisers, their affiliates or employees may have positions in the Cells or in the assets of each Cell. They may also advise other clients on the same or similar assets to those held by a Cell. Such positions may involve a conflict of interest which shall be resolved by the Directors using their judgement as to what is in the best interests of those investors.*"

70. Within the section providing Additional Information, on the topic of Directors, these Scheme Particulars state (on page 31):

> "*4) A Director may be a director, managing director, Investment Manager or other officer, employee or member of any company in which a Cell might be interested, which may be promoted by a Cell or with which a Cell has entered into any transaction, arrangement or agreement and no such Director shall be accountable to the Cell for any remuneration or other benefits received thereby.*
>
> *5) Provided the nature and extent of any material interest of his is or has been declared to the other Directors, a Director notwithstanding his office:-*
>
> *a) may be a party to, or otherwise interested in, any transaction or arrangement with a Cell of the ICC, or in which the Cell or the ICC is otherwise interested; … and*
>
> *d) shall not by reason of his office, be accountable to the ICC or a Cell for any such benefit which he derives from any such office or employment or from any such transaction or arrangement or from any interest in any such body corporate and no such transaction or arrangement shall be liable to be avoided on the ground of any such interest or benefit.*"

Further, it was explained (on page 35):

> "*At the date of this document, no Director of the ICC has any interest, direct or indirect, in any assets which have been acquired or disposed of for the account of any Cell or are proposed to be acquired or disposed of by any Cell, nor is there any contract or arrangement subsisting at the date of these Particulars in which a Director is or may be materially interested and which is significant in relation to the business of the ICC save that:*
>
> *a) Robert Addison is also a partner of the Investment Manager; and*
>
> *b) Neal Meader and Peter Radford are directors and shareholders of the Administrator.*"

71. The Supplemental Scheme Particulars for a Cell state that they should be read and construed in conjunction with the Scheme Particulars relating to the ICC dated January 2007. By way of example, the Supplemental Scheme Particulars for PF3, which are dated January 2007 [p. 1], indicate that application had been made to the CISX for shares in the incorporated cell, referred to as "the Fund", to be listed, with the first dealing day expected to be on or about 22 January 2007. The investment objective is "*to provide Shareholders over the medium to long term with capital appreciation through an economic exposure to a wide range of investments in private finance selected by the Investment Manager*". The explanation given of what "private finance" involves includes:

"*Private financing is generally employed where companies need to borrow but are either unable or unwilling to source financing from a bank and/or do not have the infrastructure, the credit rating or the inclination to approach the public market. The borrower may need funds to finance their business inventory, or have a temporary or seasonal need for cash while awaiting payment for goods/services already delivered. Nimble lenders in the private finance arena, who understand the prevailing business and legal environment, can advantageously offer funds to a borrower with strong collateral or asset backing. Typical collateral includes inventory (e.g. stock, equipment), real estate, accounts receivable, contract receivables (e.g. royalties) and the intrinsic value of a company.*"

72. There is a section in these Supplemental Scheme Particulars headed "Conflicts of Interest", which states:

> "*The Investment Manager or its employees and affiliates may provide investment advisory and management services to other clients in addition to the Fund. The Investment Manager, its employees and its affiliates will act in a fair and equitable manner in allocating investment opportunities among the Fund, other Cells of the ICC, other investment vehicles managed by them and the accounts of their other clients, although situations may arise in which the account activities of the Investment Manager or other clients may disadvantage the Fund. The Directors and the Investment Manager will endeavour to ensure that any conflict which does arise, will be resolved fairly.*
>
> *Subject to the provisions of the law, and provided that he has disclosed to the other Directors the nature and extent of any material interest of his, a Director shall be counted in the quorum and may vote in respect of a transaction or arrangement of the Fund in which he is materially interested.*"

73. The management fee payable to Arch and the performance fee to which it may be entitled are explained. The other fees payable are also described. One element is that an initial charge of 2% of subscription monies received will be paid to the Investment Manager, which "*may pay any part of this charge on to intermediaries as commission*". In respect of Directors' fees, Mr Addison is recorded as having agreed to waive his fee. The Supplemental Scheme Particulars also contain a section on risk factors, part of which sets out that:

> "*The Investment Manager's entitlement to the performance fee may create an incentive to select managers that engage in transactions or make investments that are riskier or more speculative than would be the case in the absence of such a performance fee. The performance fee is in addition to the monthly management fee and any fees and performance based profit allocations paid on the underlying investments selected by the Investment Manager.*"

74. Under the heading "Additional Information", it is explained that "*The Fund was incorporated with an authorised share capital of £2 divided into 2 Management Shares of £1.00 each, (the "Management Shares") both of which have been allotted and issued to the Investment Manager credited as fully paid up, and an unlimited number of participating shares of no par value. The Management Shares have been created in order that the Shares may have a preference over some other classes of share capital.*" The voting rights attaching to the shares were to be (a) on a show of hands, equal for each person present, and (b) on a poll, equal to the number of shares held for each person present or acting by a proxy. This reflects the provision made by Article 31 of the Cell's Articles of Association. Reference is also made to the contracts that had been entered into by the Fund, namely the IMA, administration agreement and custodian agreement.

75. Further Supplemental Scheme Particulars for PF3 are dated December 2007 [p. 81]. These refer to "Placing Shares", but the terms contained therein are no different from the terms used in the Supplemental Scheme Particulars dated January 2007 to which reference has already been made. The document explains that, as at 31 August 2007, the total number of fully paid shares in issue was just below 13 million. Placing Scheme Particulars dated April 2008 [p. 254] appear to be a different version of the same document.

76. PF2 was also incorporated on 21 December 2006. This is explained in the Supplemental Scheme Particulars dated January 2007 [p. 15], which are materially no different from those in respect of PF3 and by inference from the minutes of a meeting of the Board of Directors held on 30 January 2007, which refers to "*minutes of the 12th January 2007*" [p. 534]. There are revised Supplemental Scheme Particulars dated September 2008 [p. 170 and also p. 293], in which there were no changes to the section on conflicts of interest. Its initial shares were listed on the CISX on 31 January 2007. By September 2008, there were nearly 64 million shares in issue.

77. PF4 was incorporated on 15 March 2007 following a written special resolution of the ICC passed on 13 March 2007 [p. 544]. As shown by the minutes, its first board meeting, lasting one hour, took place on 21 March 2007 [p. 545]. Mr Addison attended by telephone. Its initial shares were listed on the CISX on 30 March 2007. As at 31 August 2007, approximately 15½ million shares were in issue. Supplemental Scheme Particulars dated December 2007 [p. 98], in much the same terms as those for PF3, refer to "Placing Shares". The explanation given of what "structured finance" involves is as follows:

> "*Early stage structured finance, also referred to as venture finance, is the provision of capital usually on a fully secured basis, to small to medium size businesses who are looking to expand their business operations. Typically there will be at least one venture capital institution invested in the equity of such firms, providing them with additional financial and management support.*
>
> *Late stage structured finance is the provision of capital, again usually on a fully secured basis, to mid-market or medium size businesses who are looking to grow through expansion, acquisition or other means. Such companies tend to be more established firms with predictable cash flows to service debt repayments. The capital provided typically represents the last round of finance prior to an initial public offering, trade sale or other corporate event.*
>
> *In both of the above cases, the lenders are often able to negotiate participations in the growth of such companies, typically in the form of equity warrants, as part of the financing arrangements. In the case of early stage structured finance this is commensurate with the general higher risk perception attached to such financing. In the case of late stage companies where the risk is lower, the equity-linked upside is reflective of the stronger likelihood of realising value and the strategic nature of the assistance provided.*"

Placing Scheme Particulars for PF4 dated April 2008 [p. 334] continue to contain broadly the same content.

78. SO3 was incorporated on 21 May 2007 following a written special resolution of the ICC passed on 14 May 2007 [p. 578]. As shown by the minutes, its first board meeting, lasting 30 minutes, also took place on 21 May 2007 [p. 582]. Mr Addison attended by telephone.

79. AT1 was incorporated on 25 June 2007 following a written special resolution of the ICC passed on 20 June 2007 [p. 593]. The Supplemental Scheme Particulars for AT1 originally dated November 2007 were substituted by new Particulars dated August 2008 [p. 155] (by way of a written special resolution dated 3 September 2008 [p. 152]). The principal change appears to be relating to the frequency at which the net asset value of this Fund would be calculated, moving from monthly to quarterly. The investment objective of this Fund was said to be "*to provide Shareholders over the medium to long term with capital appreciation through an economic exposure to a diverse range of treasury-related investment strategies, employing various risk management techniques selected by the Investment Manager.*" The section dealing with conflicts of interest is in similar terms to the comparable section in the Supplemental Scheme Particulars for PF3. The fee structure for the Investment Manager is different in that it refers to the possibility of customising them for each issue of securities. However, the fees payable to Bordeaux as the Administrator, to the auditors and to the custodian were all described in similar terms to the arrangements for PF3. Mr Addison explains that AT1 was established for the purpose of "warehousing" and syndicating deals.

80. PF5 was incorporated on 13 July 2007 following a written special resolution of the ICC passed on 10 July 2007 [p. 615]. As shown by the minutes, its first board meeting, lasting 20 minutes, took place on 2 August 2007 [p. 630] Mr Addison attended by telephone. Its initial shares were listed on the CISX on 30 March 2007. Supplemental Scheme Particulars dated July 2007 [p. 234] contain much the same terms as those for PF3. Further Supplemental Scheme Particulars dated October 2007 [p. 313] envisage the first dealing day to be on about 30 October 2007 when 49½ million shares were expected to be in issue.

81. RE1 was incorporated on 3 August 2007 following a written special resolution passed on 31 July 2007 [p. 628]. As shown by the minutes, its first board meeting, lasting 20 minutes, took place on 12 October 2007 [p. 642]. Mr Addison attended by telephone. RE2 was incorporated on 4 September 2007 following a written special resolution of the ICC passed on 3 September 2007 [p. 634]. As shown by the minutes, its first board meeting took place on 16 October 2007 [p. 645]. Mr Addison attended by telephone. The Supplemental Scheme Particulars for both RE1 and RE2 are dated August 2007 [p. 62 and p. 43 respectively]. They are in similar terms. The investment objective is "*to provide Shareholders with capital appreciation over the medium to long term through economic exposure to a diverse range of real estate investment opportunities selected by the Investment Manager*". The document further explains that "*In order to obtain exposure to real estate and property related investments the Fund may invest in a variety of instruments including but not limited to physical assets, property related companies, single strategy funds or fund of funds, debt and equity instruments, and derivative products*" and that "*Investors should therefore be aware that it may take time for the fund to become fully invested. Monies waiting to be invested in real estate investments will be invested in a variety of short term deposits, other money market instruments and financing related investments.*" The elements dealing with conflicts of interest and fees are in similar terms to those in the Supplemental Scheme Particulars for PF3. Further Supplemental Scheme Particulars for RE1 and RE2 are dated April 2008 [p. 191 and p. 212]. There are no apparent material changes from the earlier Supplemental Scheme Particulars, although in respect of RE2 there is the explanation that the initial shares were listed on the CISX on 31 October 2007 and, as at 11 January 2008, there were just over 18.2 million shares in issue.

2007, including acquisition of the Club Easy Group

82. On 8 January 2007, Mr Radford was informed by letter that the ICC had been granted consent pursuant to the Control of Borrowing (Bailiwick of Guernsey) Ordinance, 1959, as amended, to

raise up to £1 billion by the issue of shares [p. 79 in bundle I]. Various conditions were attached to that consent.

83. On 10 January 2007, FHL, the "NewCo" envisaged by the Heads of Agreement signed on 30 November 2006, which had been incorporated in the Isle of Man on 15 December 2006, adopted new Memorandum and Articles of Association and, by way of a written resolution signed by Mr Barkman and Mr Addison [p. 2092], resolved that the 65 issued shares held by FCL be re-designated A Shares and the 35 issued shares held by Arch UK be re-designated as B Shares. On the same day, FCL transferred to FHL the 1,999 shares it held in Foundations Program plc [see p. 2152]. The final issued share continued to be held by Mr Montague.

84. On 22 June 2007, Mr Addison informed Mr Meader, through an e-mail [p. 2163], that he had indirectly purchased some shares in Arch Private Finance IC Limited. It would be a long-term holding as part of his pension. He apologised for not having informed Mr Meader and Mr Radford for only doing so after the trade, recognising that "*at least out of courtesy if nothing else*", he should have informed them before the event. Mr Meader's response was to note the information provided.

85. On 20 July 2007, Mr Addison attended a board meeting of the ICC held in Guernsey. Mr Radford was also present, but Mr Meader tendered his apologies. Also present were Mr Farrell and Jacqueline Fallaize. The meeting lasted 90 minutes. Mr Radford made a file note [p. 2187] and minutes were also prepared [p. 620]. The file note suggests that both Mr Addison and Mr Farrell explained their plans to Bordeaux, whereas the minutes record, under the heading "*Review of Incorporated Cells (New Cells)*":

> "*Mr Addison gave a broad overview of likely developments for the Scheme over the next 6 months.*
>
> *He noted that Arch were planning to expand the NAVs of most of their existing cells by a total of £80 million through various placings.*
>
> *Mr Addison advised that Arch had attracted their first large institutional investor, Royal Liver Insurance. A new Incorporated Cell had been set up for their investors and it was likely to have an initial Net Asset Value of £50 million.*
>
> *Other projects in the pipeline included a Wine Fund, to hold the wine stock currently held in other ICs, a Shipping Fund and a Global Forestry Fund.*
>
> *Draft documentation is also in progress for the creation of an IC investing in residential property in the East and South of London.*
>
> *Mr Addison also confirmed that they were in the process of finalising arrangements for an Asian Energy Fund. This fund would be denominated in US Dollar and likely to be in the region of US$100 million.*
>
> *A second BMS Fund, BMS Private Equity had recently been incorporated.*
>
> *Mr Addison drew the Board's attention to plans for a new non CISX listed vehicle Arch Treasury IC Limited. The shares in the Cell will be issued to the Arch Partners and possibly others.*
>
> *The Cell will be used to streamline cash management and investment processes of other cells. It is likely that the accounting for this entity will become quite complex.*

It was noted that they would also like the Arch Treasury structure to issue asset backed securities, some of which may be listed. It was noted that fees would be charged on Gross Asset Value on this type of structure."

86. On 25 July 2007, Mr Addison and Mr Farrell held a meeting with Mr Barkman in London. It was at this meeting that Mr Barkman referred to a potential deal to acquire the Club Easy Group, which owned and rented student accommodation in parts of England. Mr Addison says he understood from what was said at the meeting that Mr Barkman planned to fund the investment through FCL and its Foundations Program and through a new fund and that any fee generated would accrue to FCL, Mr Barkman or Mr Montague. Although Mr Farrell enquired as to whether investment from the Cells was feasible, Mr Addison understood that Mr Barkman wished to involve Arch only with purchase negotiations and the structuring of the deal. Mr Farrell made handwritten notes [p. 2192]. Although some of them appear random and the overall page presents as rather chaotic, these notes offer some insight into what Mr Farrell considered relevant. The beneficial owner of the Club Easy Group, Jason Hayes, is mentioned. The locations of the student accommodation, Hull/Lincoln and Exeter/Durham/Loughborough, and the size of the operation, being 2477 bedrooms, are noted. There is reference to "*£35M excess EQ on property*" and a vendor price of £19.5 million. There is also reference to a dividend of £12 million, of which £4.3 million had been taken and the remainder would be waived. In the middle of the page, the property value is said to be £120 million, with debt of £89 million and other assets at £2 million, resulting in £33 million excess. Three entities are mentioned, being Cobbetts, PKF and Storeys, against each of which is a reference to legals, members and buildings respectively. It also says in relation to them "*1 wks in so far – to be done 3rd wk of August*". There is also a note relating to a loan of £9 million secured against the equity from Barclays in the Isle of Man. There is a little diagram showing an Isle of Man holding company above the four existing United Kingdom special purpose vehicles. At the bottom of the page "*Mutual fund*" is in a box with a reference to FPP alongside it. "*33 excess*" is circled, below which Mr Farrell has written "*take 5*" with an arrow towards 28. A little above that is a further reference to "*£5M Upfront*" with an arrow to FHL in a circle.

87. An e-mail timed at 12:31 on 25 July 2007 from Mr Montague to Mr Farrell and Gary King (also of Arch) attached some documentation relating to the Club Easy Group [pp. 2194-2282]. Mr Montague explained that Mr Barkman had been admitted to hospital as he had been feeling unwell and referred to the best way to follow up the meeting, the implication being that this message was sent after the meeting with Mr Addison and Mr Farrell earlier that day, being to share what Mr Montague described as "*the starting point then jump to the current position of what has proved to be different so far after looking more closely*". The attachments were a Student Housing Report prepared by Savills, a confidential information memorandum pertaining to the proposed sale of the Club Easy Group, some financial information and projections provided by Alan Blythe of Blythe Financial, a report from Storeys dated 18 May 2007, which had been prepared for a bank in respect of a portfolio of properties in Lincoln, Hull and Hornsea, and the latest balances by reference to the lenders involved. By a further e-mail just five minutes later, Mr Montague provided further information about the Club Easy Group to Mr Farrell and Mr King. It included projections on the profit and loss account to 31 July 2007 showing an annualised loss of £577,000, and a balance sheet as at 30 April 2007 with net assets of a little under £26 million. Mr Montague followed up with an e-mail to Mr King and Mr Farrell on 27 July 2007, in which he explained that Mr Barkman was recovering well but likely to remain an in-patient over the weekend, and that "*This has been Lee's project*", with Mr Montague only becoming involved quite recently. He added that "*The decision is either walk away or proceed on the basis of a lower price.*"

88. There is a further handwritten note of Mr Farrell's dated 1 August 2007 and headed "*Lee B/Martin T*" [p. 2296]. Along with some names of people in the Isle of Man, there is reference to a price assumption of £18.5 million, with FPP support. Under "Structure" there is a list of Barclays loan, Arch Notes, and Mutual Fund. Capital gains tax is noted as £8 million, with an assumption of £12 million, together with "*£33+M balance sheet / some upside according to appointed valuer*". At the top of the second page there is a diagram of layered boxes, against which the entries, from the top downwards, are Mutual Fund, Arch, Barclays (senior debt), with "*Excess EQ*" appearing in the bottom box. In the vicinity, "*FHL deal*" is circled. Lower down, there is a reference to "*£1M down (from FPP)*", then six months to finalise, and references to Cobbetts and Storeys, following the latter of which Mr Farrell has noted "*Cap-growth in interim*" with an arrow to "*Fund/Arch/team*". There are some figures against PKF, Storeys and Cobbetts and the further note that 35% of costs to date borne.

89. 1 August 2007 is also the date on which Ian Gibson of Storeys signed a Memorandum of Valuation Instructions given by Mr Barkman and subsequently confirmed by Mr Blythe [p. 2336]. The valuation date would be 1 August 2007 and the report would be completed by 31 August 2007 but, if required, could be completed by 17 August 2007. This document, along with others, was forwarded by Mr Montague to Mr King on 2 August 2007. By an e-mail timed at 13:06 on 2 August 2007, Mr Montague informed *inter alia* Margaret Ferris and Craig Martin of PKF and Piers Burgess and Tracy Hall of Cobbetts, asking them to "*note that Arch Group Limited are now partnered with us on the due diligence and acquisition of Club Easy Project*", and he provided contact details at Arch.

90. On the evening of 2 August 2007, Mr King raised various points about the Club Easy Group project in an e-mail sent to Mr Farrell, Peter Jeffs (also of Arch) and Alex Hay at Flintoak Partners [p. 2370]. His first point was:

> "*Since the trade is virtually a "purchase price = gross property value – debt – CGT – what we can take out of it" trade, we need to get a very good handle on the gross property value. I presume worst case CGT can be calculated, and we will know debt with accuracy, so valuation is the weak link. I am concerned that valuations in the spreadsheet are on the basis of # rooms * a number = property value. The valuation mandate is unclear on what specs are required. I think we need a more robust valuation.*"

The reply from Mr Hay the following day [p. 2372] indicates his agreement with this point and offers a number of further observations, including that he assumed the deal to be a short-term trade of 12 to 24 months because of the risk of occupancy competition in Hull/Durham due to new construction already underway in those locations and that "*The proposal to purchase is predicated on adding additional units in Exeter & Loughborough*". Mr Farrell forwarded Mr Hay's response to Mr Barkman the same day [p. 2375].

91. During the afternoon of 3 August 2007, Adam Smith (also of Arch) sent an e-mail to Mr King [p. 2379], copying it to Mr Farrell and Silash Ruparell (again also of Arch) explaining that "*Robin asked me to fund AT with £8m of cash so that it is ready for the Club Easy real estate investment early next week.*" He further explained that the total was made up by PE1, PE2 and PE3 taking notes at 8% with a five-year maturity for £2.3 million, £4 million and £1.7 million respectively. Early the following day, Mr Farrell replied, offering his thoughts about AT funding [p. 2380]. Along with other matters being covered, Mr Farrell wrote:

> "*Club Easy is still in negotiation but want to make sure the cash is physically in situ at AT, rather than be part of an ongoing competition for available cash at the time – the 8%*

carry cost can be accrued monthly & only gets paid annually – need to move some cash into AT equity at some point so company is not technically insolvent! (think this is late August realistically as tax needs to be optimized). Lee B is authorized to negotiate with Club Easy up to 15M (this may be technically a full price per student accom vs resi valuations, but reality is Club Easy has 33m official value on balance sheet+CGT liabilities can be eroded through time. So ability to extract lots of cash P&L upfront is good). AGL's loan to FHL gets repaid early as a by-product. RE1 and RE2 likely to share some of Club Easy (and Nice EQ) once deal is fully settled."

A little later the same day, Mr Farrell responded in similar terms to a query from Mr Jeffs [p. 2383].

92. On 6 August 2007, Mr Barkman replied to the issues raised in Mr Hay's response to Mr King's queries [p. 2385]. Mr Barkman began with the comment that he knew there was a lot of due diligence to come and that "*at this point we need to know that the vendor is willing to accept a more reasonable price before we spend on completing the due Diligence*". In respect of Mr King's assessment of the trade, Mr Barkman drew attention to having "*asked Storeys to value based on what the assets would sell for if the company were cleaned up*", commenting that many of the properties are exactly alike so that "*if a full trouser down valuation"* of a given property produces a figure per bed, "*the same holds true for the rest of the Clubeasy owned houses in that area*". In relation to the points raised by Mr Hay, Mr Barkman agreed with the first and, commenting on the deal length, drew attention to the sensitivities to location, noting that students nearly all walked from home to classes, with Hull and Lincoln having very confined areas in which rentals will be attractive. He added that "*growth in the market is totally outstripping the new supply*" and that "*We are certainly looking at bringing in a top flight outsource company to clean up Clubeasy, deal with CGT etc as best as is possible and sell it. Inversely we need to keep open the idea of making a substantial company of it through the use of Foundations Mutual.*" Mr Barkman further commented that "*the cities that need additions the most are Exeter and Durham. We could however simply vend off the holdings there and concentrate where we are strongest.*" On the other issues, Mr Barkman indicated that Cobbetts and PKF were looking into matters and on others he would seek clarification. He provided an update on the position he was in with Barclays, noting that "*Barclays have not given a formal offer as yet, that said, when I met with them last week they were impressed that Arch would be involved and are looking forward to discussions with Arch/Robin in assessing the appropriate terms.*" Finally, Mr Barkman added a summary:

> "*There are issues with this company, but then the price and the time to pay reflects the vendor's understanding of this. If it were squeaky clean we would not be looking at a substantial gap in the value to balance sheet, or the opportunity to cleanup and flip a company for the sort of profit levels available here. All of us are going in with eyes open, but, at the right price, there is a substantial profit to be made.*"

93. Mr Farrell's response to Mr Barkman the same day was for him to proceed, "*giving you more ammo to do said extraction!*" [p. 2397]. Mr Farrell also informed Mr Jeffs and others at Arch that Mr Barkman would hopefully be agreeing a price basis that day [p. 2394].

94. On 7 August 2007, Mr Barkman relayed to Mr Farrell, Mr King and Mr Montague the outcome of his conversation with Mr Hayes about the acquisition of the Club Easy Group [p. 2406]. Mr Hayes was "*suitably upset by our offer*" but would accept £17 million based on completion of a share purchase agreement on 17 August 2007. Mr Barkman recommended proceeding with a deal with Mr Hayes but offering a lower figure of £16.5 million or £16.75 million if it included their costs. His primary reason for doing so was:

"*The balance sheet is going to come in at over £33 million leaving more than £16 million over the sale value. Storeys (the property valuation company) have indicated that a conservative capital appreciation on the portfolio would be 3% pa or £3.6 million. Though the company is only breaking even at this point it must be noted that there is sufficient infrastructure to add 1,400 beds with only two more staff, (current complement is 52), therefore there is a very high degree of efficiency to be gained by the addition of new capital to buy more properties. …*

I see the structure of the deal from our end as follows.

1) Foundations Program Plc buys the £1million in August to consummate the deal. It also buys £250,000 to cover costs.

2) October payment of £15.5-.75 is made by a combination of Arch producing a note that bears an appropriate interest rate and gains a portion of the extracted profits and lending from a bank. Both Barclays and Investec are in the frame here. Neither has said yes at this point as they need to see the due diligence, but both have provided valid expressions of interest. There are also other banks.

3) Foundations Capital Ltd constructs a fund which is both sold by it [sic] sales staff and bought by the Foundations Program plc. The proceeds from this serve to 1) give us a method of extracting a portion (if not all) of the balance sheet, 2) add to the property portfolio of the company, 3) and, over time, retire the Arch note."

Mr Barkman further commented that:

"*The split between Arch and Foundations looks set for a 50/50 deal, as we brought the deal forward, progressed it to a very advanced point and are injecting cash through the Program and our sales force. Arch are supplying the backing to make certain the payments are made, adding structuring skills and general skill sets in terms of making the company a saleable entity in the end. …*

While we are not achieving the desire price of £15 million, we have received a substantial discount and there is still considerable meat left on the bones, (at least £8 million) both of our companies will accelerate their growth patterns as a result of this capital injection. There is scope to take more than that from this deal …

… this deal offers the combination of Arch/Foundations the opportunity to use their unique abilities to turn a profit and, given the size of the deal, turn heads."

95. In his reply the same day [p. 2410], Mr Farrell offered just one change to the structure proposed, being that "*the arch real estate fund(s) can go alongside the foundations fund as well – so that take up is certain*". Later on, Mr King sent an e-mail to a group of people at Arch, including Mr Addison [p.2414] raising some issues. Mr King had spoken to Mr Barkman and been told Mr Hayes was unlikely to accept less than £17 million, but would accept a deposit of £1 million, £14 million on completion in October 2007, and then two later payments of £1 million in each of the following years. Mr King noted:

"*Worst case on this is £119m [property valuation] less £89m [loans] less £10m [max CGT] = £20m. At £17m purchase price, this leaves us at least £3m upside, and potentially £5+m [more if we manage CGT well, improve the business, inject more properties etc.]*."

On that basis, he supported making an offer for the Club Easy Group of up to £17 million. He asked "*Re 50/50 income split of this up-front bump-up with Foundations – has this been agreed or is Lee's dream?*"

96. On 9 August 2007, Mr Addison sent to a generic internal e-mail address, re@archfunds.com, some snippets that he had gleaned from a meeting on unrelated matters with Barclays Wealth in the Isle of Man [p. 2420], including that "*A £9m loan from them would be too much they would be more likely to lend £3m (they offered the figures not us) and would want anyone else such as Arch to be subordinate to them.*". Mr Farrell forwarded this to Mr Barkman, who replied on 10 August 2007 [p. 2422], copying in Mr King, indicating that everyone was now working towards exchanging contracts the following Thursday. Part of Mr Barkman's response read:

> "*We all realise that there is some clean up work to do on the company but we are getting a cracking discount to do that, or hire someone to do that.*
>
> *I am working on the basis that this is an Arch/Foundations JV where the current pref shares are retired, (this would normally be taken from Arch's cut of FHL and therefore represents a bonus to Arch), each of our respective funds will take what they need and we split anything we take out above that on a 50/50 basis.*"

Also on 10 August 2007, Mr Addison corrected himself to Mr Farrell, Mr Barkman and Mr King, explaining that he had meant to refer to Barclays being more likely to lend £6 million and not £3 million [p. 2425].

97. Lonscale was incorporated in the Isle of Man on 10 August 2007. Mr Farrell agreed to be a director.

98. Mr Addison says that it was around this time, shortly after his meeting with Barclays in the Isle of Man, that Mr Farrell told him that the potential funding shortfall meant it was possible for the Cells to become involved in the Club Easy Group acquisition and that he had suggested to Mr Barkman that AT1, which had recently been established, could be used as the syndication vehicle. Mr Addison also understood that Arch would be entitled to a fee for its structuring work, which had been discussed with Mr Barkman at the initial meeting about the project.

99. Cobbetts circulated a revised draft share purchase agreement on 12 August 2007 [p. 2427], which led to an exchange on 14 August 2007 between Tracy Hall and Mr Barkman about the objection raised on behalf of Mr Hayes to the provision that would make the purchase conditional on property due diligence [p. 2429]. In her opinion, accepting the removal of this clause would be "*a bold move when this is, in essence, a property deal in a corporate wrapper*". Mr Barkman's view was that enough property due diligence had already occurred by means of the Storeys' valuation process, recognising that all properties were mortgaged and the lender must have carried out due diligence and been satisfied. On 14 August 2007, Mr Barkman also received an e-mail from Margaret Ferris, which he forwarded to Messrs King and Farrell [p. 91 in bundle I], in which some headlines were given in advance of PKF sending its written report. The e-mail identified a number of issues, including the declared but as yet unpaid dividend to Mr Hayes, monies being owed to the companies, a difference of £1.6 million between the property value used in the accounts and the list of valuations PKF had seen, although the latter would be superseded by the Storeys' valuation, and there being a difference in respect of inter-company balances. Mr Barkman offered his comments on each of these adding that:

> "*As long as storeys [sic] comes in at the right number I think we are there. Please realize that further due diligence will be undertaken during the period prior to*

completion on October 26th. This may give us scope to negotiate further, but I believe at this point that further delay in exchanging contracts will seriously jeopardize the seller's willingness to continue on an exclusivity basis. We need to remember we were one of five bids."

100. Mr Farrell and Mr Barkman also exchanged e-mails on 14 August 2007 about the proposed 50/50 split [p. 2439]. Mr Farrell first wrote:

> "*Let's get more specific on splits then – Agree on the principle of 50/50 for upfronts – 50pct to arch treasury (our risk taking/warehousing entity) and 50pct to foundations holdings – which can then use the cash to expand + pay down pref shares as it goes (0.48m to date? Plus interest) – presume thats what you mean by retired?. To the extent fhl/fcl are to expand there will be an increase in base costs so we should retain cash within fhl for this (and agree magnitude thereof)*
>
> *Ongoing fees/upside will reside with arch treasury, arch real estate funds + foundations mutual (is this one all-purpose fund? Is it open-ended? Jurisdiction guernsey ?Do you want arch to create?). We can also structure warrants for the deal creators, in recognition of what was required to put the deal in place – this could involve arch + foundations people. I need to have a session with the team to determine exact terms but this should be a sensible way forwards for all.*"

Mr Barkman replied:

> "*I agree with the 50/50 aspect, and also agree that the cost of repaying the Preference shares should be taken out of the initial earnings. This represents a £270k bonus to Arch.*
>
> *That said, we can't agree to the idea of our end being paid into FHL. This is not an FHL deal as your end of the initial earnings doesn't sit inside that vehicle therefore ours should not be treated in that way.*
>
> *It is our intention to retain a sizeable amount of the earnings in FCL to bolster its growth pattern – good for both of us, but we are also using a portion to pay down internal debts and to bonus staff (based on performance) and importantly Philip and myself.*
>
> *As this is no longer a FHL deal, we also need to look at a payment to Alan Blythe (who guided the deal in our direction) prior to the 50/50 split. When we originally talked, it was to be an FHL deal giving us a larger amount to pay Alan out of our end, that is no longer the case.*"

101. On 16 August 2007, the draft due diligence report of PKF dated August 2007 (but also dated July 2007 internally) was provided by Margaret Ferris to Mr Barkman and Mr Jeffs at lunchtime [p. 2453]. Later that day, PKF sent a letter to Mr Jeffs by e-mail, setting out the role it would take in relation to the acquisition of the Club Easy Group, the results of which would be addressed to FCL, which had already agreed to engage PKF, (and the draft report refers to an engagement letter dated 12 July 2007), and to Arch, asking that it be signed [p. 2506]. Mr Addison signed on behalf of Arch the same day, accepting the appointment of PKF [p. 2445].

102. The executive summary of the draft PKF report states:

> "*Clubeasy is a substantial and dynamic property based group which has established a strong brand in the arena in which it operates the provision of quality student accommodation.*

The financial highlights demonstrate the significant growth of the business in both property value and rental income over recent years as a result of the efforts of the owner and his team. The Group achieves high occupancy levels which are one of the key elements to maximising income from its property portfolio.

However in this executive summary we have focused not on detailing the positive aspects of the Group, which we believe are recognised by the potential purchaser, but on key issues which may have a negative impact on the transaction or the business, or issues which should be resolved in the contract process of exchange and completion.

The recent history of the Group shows that the interest burden which accompanies the current level of borrowings exceeds the operating profit of the Group and results in a small loss making position. A new financing structure in terms of capital and loans can address this and we understand that this is planned in the short term.

The net asset position of the Group is very important in the pricing of the transaction. We show in the above table an adjusted net asset position as at 30 April 2007, starting with management figures and highlighting a number of adjustments which could potentially reduce the net assets from £33.5 million to £30.6 million. The mechanism which will provide greater assurance of the net asset position is audited accounts for all the target companies as at 31 July 2007 and completion accounts as at the completion date. We recommend the requirement for those is incorporated into the sale and purchase agreement."

The table to which reference is made starts with the net assets at the end of April 2007 being a little under £26 million, to which is added the loan account waiver of around £7½ million, before reductions are made to adjust the net assets downwards for the reasons mentioned in the e-mail from Margaret Ferris on 14 August 2007, leaving approximately £31.6 million. As a result of intangible assets, trade debtors of more than 90 days and unpaid rents from 2005/6, a further £1 million or thereabouts would result in the potential net assets figure being £30.552 million. The profit and loss summary shows how the Group went from a positive cashflow of more than £4 million in the year to 31 July 2005 to a negative position of approximately £5.7 million for the nine months to 30 April 2007. One of the key points identified relates to profitability ("*The Group as it stands is very highly geared and, as a result, there is a significant interest burden that has been exaggerated by recent interest rate increases. Due to this apparent over-gearing, the group has been unable to generate sufficient profits to cover interest payable and has therefore been loss-making in recent years.*"), on which PKF's observation was that "*A further injection of capital is required to reduce the gearing of the Group and we understand that this is proposed in the funding structure that will be used to finance the proposed transaction.*"

103. According to an e-mail sent from Cobbetts to Mr Barkman on 16 August 2007, a draft power of attorney appointing Mr Jeffs to act on behalf of Lonscale was to be executed by Mr Farrell and Mr Barkman [p. 2451]. Mr Farrell's comment in an e-mail to Mr Jeffs and Mr King that day was that "*Lee will want his upside defined in a HoT at the same time*". The next day, Mr Barkman and Mr Farrell both attended a board meeting of Lonscale by telephone, at which three engrossed sale and purchase agreements between Lonscale and Mr Hayes for the acquisition of the three entities forming the Club Easy Group were produced and discussed. There are two versions of the minutes of that meeting. Both versions refer to the acquisition being "*funded by a mixture of equity and debt*" and that the directors "*agreed to the proposal that Arch Treasury IC Limited should subscribe for 8 million £1 ordinary shares in the Company and should propose a debt facility which would be available for draw down at completion of the Agreements and to fund the working capital requirement of the Company for the following 3 years*". In the signed version [at

p. 81 of the Core Bundle], it is further recorded that "*The Directors also discussed payment of an introduction commission to the introducers of the Project to the Company and appropriate structuring / arrangement fees to be invoiced in due course.*" In the unsigned version [eg, p. 2550], what is further recorded is that "*The Directors also discussed payment of an introduction commission of £6 million to the introducers of the Project to the Company.*"

104. The three share purchase agreements ("the SPAs") were executed on 17 August 2007. They contain similar terms, with the differences reflecting the minor differences between the entities concerned. In respect of Clubeasy Property (UK) Limited, the SPA [p. 2554] provides that the purchase price of the two ordinary shares will be £165,872. In respect of Clubeasy Group plc, the SPA [p. 2634] provides that the purchase price for the 50,000 ordinary shares will be £11,942,803. In respect of Hayes Limited, the SPA [p. 2724] provides that the purchase price for the 100 ordinary shares will be £4,478,551. In clause 4.1 of each SPA, the aggregate of these purchase prices, prior to adjustments in accordance with each agreement, is £16,587,226. Amongst the conditions set out in clause 3 of each SPA is the same condition at clause 3.1.7:

> "*The aggregated net asset position of the Clubeasy Group (being the sum of the net assets / liabilities for each company within the Clubeasy Group when taken from Condition 3.1.6 Accounts) (the "**July 31 Net Asset Value**") being not materially less (material in this context meaning £750,000) than £33,087,500 (in other words not being less than £32,337,500 (the "**Target CE Group Net Assets Amount**"))*".

The reference to the "Condition 3.1.6 Accounts" refers to the preceding condition, requiring the Seller to procure that "*audited accounts are prepared for each company within the Clubeasy Group (irrespective of whether or not such company is required to have such accounts audited) for the 12 month period ending 31 July 2007 and all such accounts … (a) containing an unqualified opinion from their respective auditors and (b) being fully signed off and filed prior to Completion*". By clause 6.1, completion was fixed for 26 October 2007. Clause 3 in each SPA continued:

> "*3.4 Subject to clause 3.5 below, if any Condition has not been satisfied on or before 10.00 am on the date set for Completion in Clause 6.1 the Buyer may by notice to the Seller:-*
>
> *3.4.1 postpone Completion to such date as the Buyer specifies being not more than 10 Business Days in which event the provisions of this Agreement apply as if that other date is the date set for Completion in Clause 6.1; or*
>
> *3.4.2 terminate this Agreement in which event the provisions of Clause 9 apply.*
>
> *3.5 If the Condition set out in at [sic] clause 3.1.7 has not been satisfied on or before 10.00 am on the date set for Completion in Clause 6.1:*
>
> *3.5.1 the Seller shall have the right (exercisable at any time within 5 Business Days (or such longer period as the parties agree) of the date set for Completion) to accept a revised Consideration, being [x%] of such amount as is then agreed between the Seller and the Buyer for the Clubeasy Group as a whole (based around the July 31 Net Asset Value) and if the Seller accepts such a revised Consideration then:*
>
> *(a) the Consideration for the purpose of this agreement shall be adjusted accordingly and specifically the amount stated in clause*

4.2.2(a) to be paid by the Buyer at Completion (and its actual payment obligation in clause 6.5.1) shall be reduced by appropriate amount; and

(b) the Condition set out in clause 3.1.7 shall be deemed to have been satisfied; and

3.5.2 if the Seller chooses not to exercise his right set out in clause 3.5.1 above or fails to exercise such right within the timescale for its exercise then the provisions of clause 3.4 shall apply.

3.6 The Buyer may by notice to the Seller waive, to such extent as it thinks fit, compliance with any of the Conditions on or before the date set for Completion but without prejudice to any other right which it may have under this Agreement."

(The actual percentage in clause 3.5.1 of each of the SPAs is 1%, 72% and 27% for Clubeasy Property (UK) Limited, Clubeasy Group plc and Hayes Limited respectively.) Clause 9 of each SPA covers Lonscale's remedies in the event of it terminating the agreement pursuant *inter alia* to clause 3.4.2, which include that the Seller shall forthwith telegraphically transfer to the Buyer's Solicitors' Client Account the initial consideration, which aggregated to £1 million and was divided across the SPAs in the same proportion as referred to in clause 3.5.1.

105. On 17 August 2007, Mr King gave an instruction to Bordeaux by facsimile for it to pay £1 million to the client account of the solicitors acting for the vendor in respect of the Club Easy Group, with the payment to be made by AT1, explaining that it was "*settlement of a loan note issue by a client of the payee. The coupon rate is 8% and matures on 26th October 2007*", emphasising that payment needed to be made that day [p. 2525].

106. On 17 August 2007, Mr Addison wrote to Mr Blythe about the proposed purchase of the Club Easy Group [p. 2800], explaining:

> "*You have requested some comfort as to the financial means and ability of Lonscale Limited to complete the above transaction. Lonscale is backed by the financial resources at the disposal of the Arch Group and Foundations Capital both as principals and agents.*
>
> *Arch Financial Products is a UK based limited liability partnership which is regulated by the Financial Services Authority and subject to its capital adequacy requirements at all times.*
>
> *We currently manage around $700m worth of assets in both open and closed end vehicles which have a combination of upfront and annual management charges together with performance fees that are paid quarterly. Current inflows into the funds from the retail sector are running at approximately £1m every two days. The closed end nature of the majority of our funds, together with the emphasis on investing in private markets means that we are sheltered from the turmoil that is currently besieging the public equity and bond markets.*
>
> *Arch as a principal, and as an agent for its funds, has completed a number of investment transactions of this size and complexity in a number of sectors including UK residential property management, shipping financing and fund management companies. We have 26*

full time employees and partners with a vast array of finance and structuring experience from all the major investment banks."

The genesis for this letter of comfort appears to have been the request, repeated in an e-mail from Mr Blythe to Mr Jeffs on the morning of 17 August 2007 [p. 2803] that confirmation to the Seller would be provided that Arch was "*effectively underwriting the transaction*" and capable of doing so, which had been one of the conditions of the revised price agreement and had been promised by Mr Barkman. Mr Jeffs sought Mr King's or Mr Farrell's agreement that it was permissible to send such confirmation.

107. On 18 August 2007, Mr Farrell sent to Mr Addison a confidential e-mail [p. 2807] setting out how Arch and AT1 would be likely to benefit from various types of transaction and how others would participate in them. The latter included "*Arch Guernsey ICC funds/other Arch funds e.g. PF, PE, SO, RE, NR funds*" before concluding:

> "*As such Arch Treasury is collectively charged with arranging of syndicate transactions, prior to re-structuring & syndicating as appropriate, to give the syndicate the requisite tranched exposures or customized risk/return. AT will price these deals to be attractive, in order to achieve good take-up for the dealflow, retaining upside for its own balance sheet/risk capacity.*
>
> *Any of the entities/partners might bring deals and be an arranger/originator, and thus share in the upside of an individual deal e.g. Foundations – Club Easy …*".

Mr Farrell largely repeated this view of AT1 in a file note set out in an e-mail from him dated 20 August 2007 [p. 2808], which expanded slightly what he had written to Mr Addison, which included "*The closeness of relationships/sharing of info within AFP should not lead to a "cut off nose to spite face" analysis of individual deals – AT is the vehicle set up to optimally manage these situations & pricing will always be set to be advantageous to the funds*" and "*Any of the entities/partners & third parties might bring deals and be an arranger/originator, and thus share in the upside of the individual deal e.g. LB/Foundations – Club Easy, specific RE/Shipping deals etc. – AT facilitates these efficiently and pays upsides as appropriate.*"

108. On 21 August 2007, Cobbetts provided to Arch a draft of its legal due diligence report on the acquisition of the Club Easy Group [p. 2812]. This draft report was forwarded by Mr Jeffs to the generic "RE" e-mail address, to which Mr Addison responded within a matter of minutes [p. 2873] commenting that "*There is some important follow up for us to put into place here, some before and some after acquisition*" and asking who would be coordinating that. The draft report, addressed to Lonscale (see schedule 1 to it) had been prepared on the basis of reviewing the 146 documents set out in Appendix 3. In respect of a number of the lenders to the Club Easy Group, the report notes that a change of control would amount to an event of default, unless consent were obtained, under the terms of those loans. In relation to the land, Cobbetts had been supplied with the Land Registry entries for the properties but stated that they had "*not been instructed to and have not undertaken any detailed due diligence in respect of any specific properties*" adding further that:

> "*We have not been asked to and have not reviewed:*
>
> - *any title information, searches, construction documentation, replies to enquiries raised of the owner, planning, environmental or any other information normally associated with a full review of title on a detailed due diligence exercise in respect of any individual Property; or*

- *any residential tenancy agreements in relation to the student lettings of the individual Properties (or any documentation which might be supplemental to those letting arrangements); or*

- *the licensing situation in respect of any houses which might be affected by the regulations governing houses in multiple occupation under the Housing Act 2004 (or any other regulatory or statutory requirements such as compliance with the requirements of fire or other statutory authorities); or*

- *any business or other tenancy arrangements the Group has entered into (either as landlord or tenant); or*

- *any other documentation relating to property related commitments which the Group might have taken on and which bind the Group creating liabilities either past, present or future.*"

109. On 22 August 2007, Mr Blythe raised with Mr Barkman, Mr Montague, Mr Farrell, Mr Jeffs and Mr Hayes that the lenders in respect of the various properties within the Club Easy Group would need to agree to their facilities continuing on a change of owner of the Group and he proposed a series of meetings the following month at which they could be briefed on relevant matters [p. 2877]. Later that day, Mr Jeffs highlighted for the benefit of Mr Farrell and Mr King that it was one of the conditions in the SPAs that consent letters be obtained from each current lender before completion of the acquisition takes place.

110. On 23 August 2007, Mr Addison and Mr Farrell attended a meeting with Richard Symington of Methuen Consulting on the topic of conflicts of interest. A solicitor, Charles Douglas, was also present. From the file note of that meeting [p. 2879], which Mr Addison has signed, it is apparent that its purpose was that:

> "*Arch sought external advice on how to correctly manage conflicts of interest that are likely to occur between investment funds/vehicles where Arch acts as Investment Manager/Adviser, including funds/vehicles in which Arch shareholders have a beneficial interest.*"

The note also includes:

> "*Internal arrangements – it was considered sensible and pragmatic for the various funds to agree to work together as a syndicate, through AT, in order to foster such attractive transactions. It was also raised by RF and noted by RS that the ability of AT to earn a return meant that Arch was able to attract and reward structuring talent that can source more underlying direct transactions, with higher IRRs than the current range of investments in the funds. Without this the funds would be worse off in terms of returns, even after allowing for the retention of benefits at AT level.*
>
> *RS commented that for each case we should document the reasons for undertaking a transaction via AT, so that there is a clear paper trail for the dealing of the conflict in a fair manner. RF highlighted that internal processes had already been upgraded to record the rationale for each transaction undertaken by the funds. In practical terms a different fund manager to the funds would represent AT in the consideration of such opportunities.*"

This document was presented to the directors of Arch UK at a board meeting held later the same day, at which Mr Addison acted as the secretary [p. 2882].

111. On 24 August 2007, a draft report from Storeys was provided to Mr Barkman and Mr Montague, with the latter forwarding it to Mr Farrell, Mr Addison and Mr Jeffs later the same day [p. 2888]. This draft report is addressed to FCL and dated 1 August 2007. It explains that Storeys have had previous and ongoing involvement with the properties, which extended to undertaking secured lending valuations for Mr Hayes, which meant they had inspected a number of properties over the preceding year, which they would not re-inspect, but that they had inspected almost all of the properties in Durham and Exeter and such further inspections in Loughborough and Lincoln, as appropriate. In accordance with the instructions given to them, they arrived at their valuation on the basis of Market Value – "Investment Value". The methodology is further explained at para. 10.5 ("*We have elected to value the properties individually and in respect of the overwhelming majority of the stock have adopted a straightforward straight line Gross All Risks Initial Yield approach*") and para. 10.6 ("*This simply involves capitalising the Gross Income Stream at a yield which reflects the inherent risk and also takes into specific consideration Facilities Management costs and the like*"). The valuation summary given was:

> "*We are of the opinion that the value of the 943 student bed spaces in Hull, housed within the various properties summarised within the appendices at the rear of this report, enjoying a total gross rental income per annum of £2,493,488, assuming full occupancy, as at the 2007/2008 academic year, is in the sum of £33,250,000.*
>
> *We are of the opinion that the value of the 861 student bed spaces in Lincoln, housed within the various properties summarised within the appendices at the rear of this report, enjoying a gross rental income of £2,691,179 per annum, assuming full occupancy, as at the 2007/2008 academic year, is in the sum of £38,670,000.*
>
> *We are of the opinion that the value of the 401 student bed spaces in Loughborough, housed within various properties summarised within the appendices at the rear of this report, enjoying a gross rental income of £1,578,744 assuming full occupancy, as at the 2007/2008 academic year, is in the sum of £22,100,000.*
>
> *We are of the opinion that the value of the 185 student bed spaces in Exeter, housed within various properties summarised within the appendices at the rear of this report, enjoying a gross rental income of £185,818.70 assuming full occupancy, as at the 2007/2008 academic year, is in the sum of £11,950,000.*
>
> *We are of the opinion that the value of the 143 student bed spaces in Durham, housed within various properties summarised within the appendices, enjoying a gross rental income of £575,280 at the 2007/2008 academic year, assuming full occupancy, is in the sum of £8,820,000.*
>
> *We are of the opinion that the value of the various non student/commercial properties in Hull, Lincoln and Loughborough which are summarised within the appendices along with corresponding annual rentals, is in the order of £4,640,000.*"

The gross rental income figure in respect of the Exeter properties appears to have been incorrectly transcribed, because in para. 5.7 it is said to be £818,670. The aggregate of these valuation amounts is £118,480,000. At para. 1.1, the draft report states "*We estimate that the average bed space value in Hull equates to £35,964, in Lincoln £41,436, in Loughborough £54,899, in Durham £63,878 and in Exeter £65,491.*" At para. 5.22 it explains that "*we have valued the properties taking into consideration the strength of the Clubeasy brand name and caution that should any of these properties be sold individually as investment that they may not necessarily achieve the yields articulated herein since they would not enjoy the wider benefits that being*

within the Clubeasy Group affords in terms of University accreditation, management and maintenance policies, and so forth."

112. As at 31 August 2007, as Mr Addison points out in his second witness statement, Arch, through the UK Funds, controlled 100% of the issued shares in PF3, 80.17% of the issued shares in PF2 and 85.09% of the issued shares in PF4. In respect of PF5, it controlled none of the issued shares and, although RE1 had been established by then, no shares had been issued and RE2 had not then been established. However, by 28 September 2007, the UK Funds, through Arch, controlled 100% of the share capital of both RE1 and RE2. On 22 October 2007, the percentage of the issued shares controlled by Arch in this way in PF4 had risen to 92.26% and in PF2 had risen to 84.73%, although by the end of October 2007 the percentage in respect of PF2 dropped to 83.9%. The percentages changed again by the end of November 2007, resulting in those for PF2 and PF3 dropping to 83.69% and 95.25% respectively and 3.2% of the shares in PF5 then being controlled by Arch. There were further changes by the end of December 2007, in that in respect of PF2 and PF3 the percentages dropped to 83.05% and 93.25% respectively, whilst the other percentages remained as they had been the previous month.

113. On 4 September 2007, a revised draft due diligence report was sent by PKF to Mr Jeffs and Mr Barkman [p. 2974].

114. On 10 September 2007, Mr Blythe forwarded to Messrs Barkman, Jeffs and Farrell an e-mail exchange he, and before him Mr Hayes, had been having with Susan Witton, a mortgage credit analyst at Paragon, which was one of the institutions lending to the Club Easy Group [p. 144 in bundle I]. It sets out Paragon's need to understand the changes that would be made within the board of directors of the borrower, even if the entity itself would remain unchanged. It also refers to an issue about whether or not Mr Hayes would be released from his personal guarantee. The earliest message in the string, sent on 4 September 2007 in the context of acknowledging receipt of documents from Mr Hayes providing background information on Arch, refers to an earlier letter dated 27 June 2007 from Mr Hayes to Paragon in which he had advised that he had identified FCL as a purchaser for Club Easy Group plc.

115. On 17 September 2007, Mr Jeffs wrote to the board of directors of Lonscale with his recommendations, arising from his review of the due diligence from PKF, Cobbetts and Storeys, and his own research and evaluation, for what needed to be done immediately post-acquisition of the Club Easy Group [p. 3045]. He proposed that an integration team, led by him, be put in place, part of its role being to ensure that the risk areas identified by PKF and Cobbetts be dealt with promptly and effectively, all as part of the transition from the Group being owner-managed to being institutionally owned. He suggested that approximately £250,000 would cover the envisaged expenses for a three-month period to the end of January 2008.

116. On 20 September 2007, Mr Jeffs sent an e-mail to Mr Barkman and Mr Farrell [p. 3057] offering a different valuation of the properties in the Club Easy Group from that provided by Storeys, because he believed that the valuation for net asset purposes should not be based on the following year's projected revenue, but on the expected revenue for 2007, and then using the same yield. The position in respect of one property (Molly Hayes) would be unchanged and was removed from his calculation and then added back in. As a result, the valuation of a little over £119 million of Storeys would reduce to a little over £106 million, as shown on the attachment to the e-mail [p. 148 in bundle I].

117. The finalised report from PKF dated October 2007 was provided to Mr Jeffs under cover of an e-mail from Margaret Ferris on 8 October 2007 [p. 3068]. Mr Jeffs forwarded it to Mr Barkman straightaway [p. 3121]. Although there were some changes to the text from the draft provided

two months previously, eg, also referring to the letter of engagement dated 16 August 2007, the passages already quoted, and the figures mentioned, taken from the executive summary, all remained unchanged.

118. On 13 October 2007, Mr Farrell set out in a "file note" style e-mail [p. 3238] his updates on a number of matters, one of which referred to Mr Addison being a director of a real estate venture being undertaken by Arch UK with Mr Hay and Mr Douglas. Another topic addressed was Lonscale/Club Easy, with Mr Farrell commenting that:

> "*… this deal is scheduled to complete on Oct 26th. Before then we need to sign the terms of the Lonscale restructuring, management & control & ownership, so that Lee Barkman cedes to ARCH Treasury in return for upfront structuring fees as agreed. Some re-structuring required & expansion of the Club Easy Group in Exeter & Durham. 1000 beds already identified.*"

From his end, Mr Barkman, on 15 October 2007, relayed to Mr Farrell by e-mail [p. 3240] a possible way of minimising their tax exposure about which he had been told by an adviser. It was predicated on Mr Barkman owning Lonscale and, as a Guernsey resident, selling that Isle of Man company without being liable for CGT. That would mean the profit for both AT1 and FCL could be in his hands tax-free. He then buys shares in or from any entity or person that Arch instructs "*for the value that Arch is to receive*", following which he would cede control of and any income or sale rights in the shares but retain them in his name so far as the Revenue is concerned. He did not know if there was any merit in such a proposal.

119. On 15 October 2007, Storeys produced its finalised report and sent it *inter alia* to Mr King, Mr Jeffs, Mr Farrell, Mr Barkman, Mr Hayes and PKF [p. 3241]. As a result and from further discussions, later that day Mr Jeffs was telling Mr King [p. 3293] that Arch "*Should have firm numbers from Foundations by Thursday this week. As before the backstop is Arch doing 100% of purchase if funds slow in getting across to Arch.*"

120. The finalised Storeys' report uses 1 August 2007 as the valuation date. The number of bed spaces referred to has increased in some cases, resulting in the valuation summary now being:

> "*We are of the opinion that:*
>
> 1. *The value of the 1,000 student bed spaces in Hull, housed within the various properties summarised within the appendices at the rear of this report, enjoying a total gross rental income per annum of £2,679,100, assuming full occupancy, as at the 2007/2008 academic year, is in the sum of £35,350,000.*
>
> 2. *The value of the 867 student bed spaces in Lincoln, housed within the various properties summarised within the appendices at the rear of this report, enjoying a gross rental income of £2,731,073 per annum, assuming full occupancy, as at the 2007/2008 academic year, is in the sum of £39,130,000.*
>
> 3. *The value of the 404 student bed spaces in Loughborough, housed within various properties summarised within the appendices at the rear of this report, enjoying a gross rental income per annum of £1,589,544, assuming full occupancy, as at the 2007/2008 academic year, is in the sum of £22,110,000.*
>
> 4. *The value of the 185 student bed space in Exeter, housed within various properties summarised within the appendices at the rear of this report, enjoying a gross rental*

income of £818,670 assuming full occupancy, as at the 2007/2008 academic year, is in the sum of £11,950,000.

5. *The value of the 143 student bed spaces in Durham, housed within various properties summarised within the appendices, enjoying a gross rental income of £575,280 as at the 2007/2008 academic year, assuming full occupancy, is in the sum of £8,820,000.*

6. *The value of the various non student/commercial properties in Hull, Lincoln and Loughborough which are summarised within the appendices along with corresponding annual rentals, is in the order of £5,140,000.*

The aggregated total of the aforementioned properties in the various locations amount to the sum of £122,500,000."

121. The changes to the number of bed spaces and corresponding valuations mean that para. 1.1 of the report now states "*We estimate that the average bed space value in Hull equates to £35,351, in Lincoln £45,131, in Loughborough £55,112, in Durham £54,593 and in Exeter £64,594.*" Despite the increase in the valuation of the non-student/commercial properties, para. 1.18 still refers to £4,640,000. The other aspects of the report to which reference has been made in relation to the earlier draft remain unchanged.

122. Late on 19 October 2007, the financial statements for the year ended 31 July 2007 of the Club Easy Group, although not including those for Hayes Limited, were provided to Mr Blythe by e-mail. He forwarded them on 23 October 2007 to Mr Jeffs, Mr Barkman, Mr Hayes and PKF [p. 3311]. Mr Jeffs forwarded this message to Mr Farrell and Mr King and, within a matter of minutes, Mr Farrell had noted that the net asset value referred to (£29.9 million) was below that specified in the SPA [p. 3431]. Mr Jeffs further pointed to the condition at clause 3.1.7 in the SPAs. During the evening of that day, Mr Farrell informed Mr Barkman by e-mail about how he envisaged completion of the acquisition of the Club Easy Group working [p. 3433]. On the completion date of 26 October 2007, AT1 would pay the residual balance, allowing for the £1 million deposit already paid, of around £20 million. Mr Barkman would:

> "*... transfer the entire share capital of the acquisition SPV Lonscale Ltd ("Lonscale") to AT. AT understands that, in consideration for this and for Foundations jointly bringing and co-structuring the transaction with ARCH Financial Products, Lonscale will compensate both parties for 50% of the difference between syndication proceeds and acquisition cost ("Structuring Fees").*"

Mr Barkman would procure his Foundations side of things to participate in senior and junior notes as soon as practical, for which Barclays in the Isle of Man had agreed to provide funding. Foundations Program plc would subscribe for £1 million of junior notes, with AT1 being reliant on that funding being in place to complete the transaction. The board of directors of Lonscale would be expanded to include a further director from the Isle of Man. Post-completion, Foundations Program plc would subscribe for a further £4 million of notes, on which AT1 would also be relying to complete the transaction.

123. Mr Barkman's reply the following morning [p. 3437] proposed variations on Mr Farrell's proposal. Part of this response was:

> "*A) FPP portfolio invests £1 million per the class C notes. B) I take a note "differed [sic] completion non interest baring [sic]) back for our end of the structuring fees, (£3 million). Arch can pay itself per its internal decision. On this point, I think that given the*

original structure of the Preference shares repayments through FHL, we should look at adding the value of the preference share to the £6 million such that it looks more in line with the original repayment split."

Mr Barkman's annotation to what Mr Farrell had written about "Structuring Fees" was "*Should we raise the amount of the note back to myself in order to allow leeway in how much we take in the case where all goes well. I can always sign off an [sic] pre-agreement to waive the additional if not appropriate to take it.*" Mr Farrell's response later that day [p. 3448] expresses a level of disappointment in Mr Barkman and his promises that come to nothing, pointing out that "*For Arch to take on the whole deal has required a lot of juggling to say the least*". Mr Farrell recognised that Mr Barkman's proposal could work, provided that there was confirmation that Foundations Program plc would take the £1 million note before AT1 agreed to send the completion monies. He added "*After receipt of AT syndication proceeds, Lonscale pays structuring fees = 50% of (syndication proceeds minus acquisition cost) to AFP and Foundations (which entity? FCL?)*". In respect of what Mr Barkman had mentioned about the new fund established from his side, which he referred to as "FM1", Mr Farrell commented "*FM1 looks like one month away still. Robert says it need [sic] to be an Experienced Investor Fund – does this pose a problem?*"

124. The apparent shortfall in the net asset figure was also being addressed at this time. Mr Farrell and Mr Jeffs were communicating with Mr Hayes about how the figures affected the price that should be paid for the Club Easy Group. Those exchanges continued into 25 October 2007. Mr Hayes proposed some adjustment to the format of the consideration set out in the SPAs.

125. On 26 October 2007, FCL provided a letter of intent about how it would participate in the acquisition of the Club Easy Group [p. 3474]. It refers to timing issues because of delays in getting confirmation of the borrowings from Barclays. A commitment to subscribe for £2 million of class C notes is given, with £800,000 for immediate settlement and the balance deferred. The letter, signed by Mr Barkman and Mr Montague ends with the hope that these commitments are found to be acceptable so that AT1 could go ahead with the acquisition as soon as possible.

126. On the same day, AT1 began the process of issuing notes: PF2 subscribed for £3.9 million; PF3 for £2.9 million; PF4 for £3.9 million; and PF5 for £2.3 million, in each case of class B notes. Foundations Program plc subscribed for £2 million of class C notes, of which £1.2 million was to be settled on or before 14 November 2007. RE1 and RE2 each subscribed for £3.6 million of class C notes. AT1's final terms [p. 3483] set out that the issue date was 29 October 2007, with the maturity date being 30 April 2013, subject to the issuer's call options in para. 25. Class A notes, carrying interest of 6.5% per annum, were to rank first, although none was issued at this time. Class B notes, of which £13 million were being issued, would rank second, carrying 12% interest per annum, and holders would receive equity warrants as set out in para. 21.1. Class C notes, of which £8 million were being issued, would rank third, but carry no interest and be settled in accordance with para. 21.2. The collateral was 100% of the shares in Lonscale, described as "*a real estate investment company*" with its current activities being "*owning and renting residential accommodation to students across a number of cities in the UK*", with instrument holders having security over these collateralised assets according to the ranking of the classes. Paragraph 36 permits AT1, on 2 business days' notice, to issue additional class notes ranking *pari passu* with existing notes. The reason for the offer was said to be that "*The net proceeds of the issue of the Notes will be used for the general corporate purposes of the Issuer*".

127. Discussions also took place on 26 October 2007, as shown by the e-mail sent by Mr Jeffs [p. 3492], between Lonscale and Mr Hayes, which resulted in the consideration under the SPAs reducing from £16,587,226 to £15,159,073. This reduced purchase price for the Club Easy Group

and other modifications to the SPAs were dealt with in a Supplemental Agreement executed by Mr Hayes and Lonscale on 29 October 2007 [p. 3525].

128. In an e-mail copied to Mr Jeffs and Mr Hayes on the evening of 26 October 2007, Mr Blythe was corresponding about the need for Yorkshire Bank/Clydesdale Bank to approve the change of ownership from the companies owned by Mr Hayes to Lonscale. It is apparent that the required approval had not by that stage been given. Mr Blythe included in his message that "*When the sale of the Clubeasy group to Lonscale Limited was first mooted it was agreed that as the prospective purchasers (the Arch Group) are based in the West End of London, the relationship should be transferred to Knightsbridge office of Clydesdale Bank.*"

129. Mr Barkman and Mr Farrell, who attended by telephone, held a meeting of the board of directors of Lonscale on 27 October 2007 at 10 am to consider and approve the financing for the acquisition of the Club Easy Group. The unsigned minute [p. 3516] records that Mr Barkman noted that in order to complete the acquisition and provide Lonscale with further working capital it should borrow £13 million from AT1 via the 12% Mezzanine B class loan note and accept from AT1 a subscription of £8 million for 8 million £1 ordinary shares in Lonscale.

130. The final terms of Lonscale's corresponding issue of £21 million of multi-class notes, with the same maturity date of 30 April 2013 are dated 29 October 2007 [p. 3518]. The document appears to be signed by Mr Farrell. Reference is made to class A and class B notes only. The reason for the offer was said to be that "*The net proceeds for the issue of the Notes will be used for the acquisition of property assets*". AT1 subscribed for £13 million class B notes [p. 3524].

131. Following a request from Arch [p. 3557], Bordeaux gave directions to Fortis by way of facsimiles sent on 29 October 2007 [p. 3534 and p. 3536] in relation to the movement of monies between PF2, PF3, PF4, PF5, RE1 and RE2 on the one hand and AT1 in respect of the loan note subscriptions, by virtue of which AT1 received £20.2 million, and between AT1 and Lonscale, by which £19,983,750.34 was sent to Cobbetts' Clients Account. The explanation given to Bordeaux by Mr King for this payment by AT1 [p. 3559] was that it was "*settlement in a range of tranches of equity and debt in the company "Lonscale" backed by property*". The difference between £21 million received by AT1, confirmation being given to Mr Jeffs by Wajid Ali in an e-mail at midday [p. 3561] that the £800,000 due from Foundations Capital plc had been received, and the monies sent to Cobbetts' Clients Account is due to deducting the amount of the deposit of £1 million, plus accrued interest, which was to be repaid to SO3. Early that afternoon, Mr Addison sent to Mr Montague and Mr Barkman his calculation of the amount to be paid to Arch UK in respect of the preference share payment, which he explained was £556,152, although his attachment shows it as £556,142 [p. 3566]. Within minutes, Mr Farrell sought to clarify that the process was for Cobbetts to pay FCL, which in turn would repay its FHL loans and FHL would repay Arch UK [p. 3568].

132. Although the minutes are not dated at the top, other than by reference to the month, there are signed minutes of meetings of the board of directors of Lonscale, one of which has 29 October 2007 written on, dealing with the approval of the SPAs, as varied, and approving the transfer of the sole share in Lonscale from Mr Barkman to AT1 [p. 3931 and p. 3933]. Together with the signed stock transfer form [p. 3934], these documents were provided to Mr Barkman by Mr Jeffs in an e-mail on 6 December 2007 [p. 3927]. In respect of the transaction, the minute records that:

> "*The Directors considered the SPAs and* ***Resolved****:*

*3.1 It still remained in the Company's interest to proceed with the purchase of the Clubeasy Group on the terms of the SPAs as varied by an agreement (the "**Variation Agreement**") with Jason Hayes;*

3.2 That the Variation Agreement, a draft of which was produced and considered, be and is hereby approved and that Peter Jeffs, as duly appointed attorney on behalf of the Company be and is hereby authorise [sic] to execute it as a deed in behalf of the Company;

3.3 That Alan Blythe, who had consented to act, be and is hereby appointed as an additional director of the Company;

3.4 That upon successful completion:

3.4.1 that the following structuring fees by paid by the Company:

3.4.1.1 £3 million to Arch Financial Products LLP; and

3.4.1.2 £3 million to Lee Barkman;

3.4.2 That all associated costs of the purchase be settled; and

3.4.3 That an introducers fee of 1% of the total consideration to be paid by the Company for the Clubeasy Group be paid to Alan Blythe."

133. Also on 29 October 2007, Mr Farrell sent a letter on behalf of Arch to Piers Burgess at Cobbetts LLP [p. 3596 and p. 3601] explaining the amount that would be received into the firm's client account "*for completion of the acquisition of the Clubeasy group of business by Lonscale Limited*" and instructing that, upon successful completion of the acquisition, structuring fees of £3 million each were to be paid to Arch and to the order of Mr Barkman. On 5 November 2007, Mr Addison followed this up with Mr Burgess, indicating that Mr Barkman would be consenting to the release of funds to Arch and seeking their immediate release on receipt of Mr Barkman's authorisation [p. 3595 and p. 3599]. Mr Burgess informed Mr Addison the following day that the funds had been sent as requested [p. 3602], although they were being treated as a loan at that stage, pending further discussions between those involved, as noted in e-mail exchanges on 20 and 21 November 2007 [p. 3679].

134. On 8 November 2007, Mr Barkman enquired of Mr Addison the account to which payment should be made in respect of the preference shares [p. 3604], adding that he intended to instruct that the required amount be paid from what was held at Cobbetts. When Mr Addison reminded Mr Barkman that the account details had already been provided by him on 29 October 2007, the following day, Mr Barkman instructed Mr Burgess to make payment from the funds held to the order of FCL, which Mr Burgess then did, although he indicated in an e-mail that he wished to speak with Mr Addison about the nature of the payment [p. 3623].

135. On 15 November 2007, Mr Addison sought input from Mr Farrell and Mr Jeffs on whether a letter he had drafted to send to BDO Stoy Hayward LLP ("BDO") about the acquisition of the Club Easy Group "*correctly sets out Arch's role*" [p. 3635]. Later the same afternoon, Mr Addison submitted a modified version of the letter, duly signed, to BDO, along with accompanying documentation, seeking VAT advice [p. 3648]. The letter includes:

"*Arch Financial Products recently received a fee of £3m from an Isle of Man company from [sic] assistance in acquiring another group of companies. I would like to confirm our understanding how we should treat this payment for VAT purposes.*

Background

In July 2007 Arch was made aware by a company called Foundations Capital Limited (FCL) of an opportunity to purchase a group of companies involved in the student accommodation and letting business in the UK. The vendor is an Isle of Man resident individual.

The intended purchaser of the transaction could not complete the transaction at the time and so Arch was approached by FCL with a view to finding an alternative purchaser for the group of companies.

Arch introduced and acted on behalf of Arch Treasury IC Limited a Guernsey investment company to which Arch has an investment management agreement.

As there were a number of companies in the UK and the Isle of Man under common ownership that were being sold, it was recommended that a separate Isle of Man holding company was set up to purchase the various businesses and so Lonscale Limited was set up by FCL and Arch as a holding company to hold the disparate companies under the Clubeasy umbrella, and Arch Treasury IC Limited purchased Lonscale.

There is no formal letter appointing Arch. Arch acted on behalf of Arch Treasury IC Ltd under the terms of the investment management agreement between the parties. …

Arch and FCL undertook the following activities

- *Negotiated the price with the vendor*
- *Negotiated the terms of the sale and purchase agreement*

We understand from the above that the entire fee is therefore classed as financial intermediary service and as such no VAT is due on the invoice.

Payment has been made to us in November by Cobbetts but I have not submitted a formal invoice yet, and attach a draft invoice for your consideration to ensure that it correctly describes the work undertaken and the appropriate VAT treatment."

The draft invoice provided by Mr Addison was a modified version of a document previously dated 29 October 2007 [p. 3523] being "*for £3,000,000 for the provision of intermediary services in relation to the acquisition of the Clubeasy group of companies*" by way of a letter from Mr Farrell [p. 3653].

136. The response from BDO dated 23 November 2007 [p. 4621] confirms that the services provided by Arch fall within the exemption from VAT available to financial intermediaries. That letter sets out BDO's understanding of the position, apparently from Mr Addison's letter and a subsequent conference call, as follows:

"*I understand that Arch FP provides fund management services to a Guernsey based investment company, Arch Treasury IC Ltd (Arch TIC)). Arch TIC recently incorporated an Isle of Man subsidiary company, Lonscale Ltd, which purchased a group of*

companies. Arch FP together with a third party FCL, acted as an intermediary in arranging and brokering the deal which resulted in the acquisition.

FCL had previously acted as an intermediary in arranging an acquisition by an alternative purchaser but the deal fell through. FCL then approached and invited Arch FP to introduce a potential purchaser and assistant [sic] in negotiating/arranging the deal between the two parties.

Arch FP introduced the purchaser (Londscale [sic] Ltd) to the vendor, helped raise funds for the acquisition and together with FCL negotiated the terms of the sales/purchase agreement and price for the shares. Arch FP is now entitled to a commission of £3Million payable by Londscale [sic]. FCL is also entitled to commission. These commission payments were contingent upon the successful completion of the deal. In the event that the acquisition had not completed both parties would not have been entitled to a commission. ...

In this instance I understand that Londscale [sic] Ltd has paid separately for those services and that Arch FP's commission only relates to its services of introducing and brokering the deal."

137. On 22 November 2007, Mr Addison was in Guernsey for a board meeting of the ICC. The minute [p. 655] records that Mr Farrell was also in attendance. It also records that Mr Addison gave a brief overview of developments since the previous meeting. Mention is made of RE2 being launched in October 2007 alongside RE1, but nothing is recorded about the transaction involving the Club Easy Group. That morning, apparently prior to the meeting, Mr Farrell was engaged in e-mail correspondence with others within Arch about lower net asset values for some funds "*due to the equity market tumble of recent days*" [p. 3688]. Mr Farrell wrote to Mr Smith that they needed a formal way to value Lonscale, suggesting using the Storeys' valuation minus the reserve for restructuring "*(Of which x, y, z attribution and profit expected but not taken yet – copnfoidentially [sic] this helps to later justify level of str fees etc)*". They also touched on how to deal with the non-payment from Mr Barkman's end of £240,000 of the £1.2 million due as deferred payment for the class C notes, which is something that Mr Barkman had already explained to Mr Addison on 14 November 2007 [p. 3686].

138. Mr Smith raised the issue of liquidity planning in an e-mail on 19 December 2007 to a number of people within Arch, including Mr Addison. His comments included:

> "*RE1 and RE2 still need more cash in the short-term. £2m each will cover them until the end of January and they will need a further £4m each to carry them through Feb. This is assuming £8-9m of spending on Lonscale through February, which is probably too conservative.*"

At around this time, just before Christmas, Mr Farrell and Mr Barkman were commenting on how they would put in place an action plan for the Club Easy Group [eg, p. 3950]. Mr Jeffs forwarded a draft Abbreviated Business Plan for the Club Easy Group to Mr Farrell on 4 January 2008 [p. 3981 and, eg, p. 4022].

2008

139. Because Lonscale did not have sufficient monies to meets its liabilities [p. 3981], on 9 January 2008 it requested from AT1 as its shareholder a loan of £1 million for the purpose of injecting working capital into Clubeasy Group plc [p. 3986, although there is a second such letter, but this time signed only by Mr Blythe rather than by him and Mr Barkman at p. 3993]. This request was

granted by AT1 subscribing for £1 million of class A notes [p. 3988], with RE1 and RE2 each subscribing for £500,000 of class C notes issued by AT1 [p. 3985], all of which also took place on 9 January 2008.

140. In January 2008, PKF undertook a completion account review in respect of the acquisition of the Club Easy Group [p. 3968]. In commenting on the net asset position in section 4, PKF noted that "*The net asset position in the completion accounts amounts to £25.5 million, a significant shortfall on the £32.3 million defined in the sale and purchase agreement as The Required Completion Net Asset Value.*" Even with adjustments, there was a net asset shortfall of £1,587,000. PKF suggested that there needed to be a reduction in the total consideration of £2,239,000. (On 30 January 2008, Margaret Ferris of PKF forwarded to Mr Jeffs an addendum engagement letter for this work, explaining that it was necessary because this was work commissioned by Lonscale rather than FCL, which had been the basis on which PKF had previously been working [p. 4064].) As a consequence of this report, Lonscale sent to Mr Hayes a letter, as required under the SPAs, informing him of the shortfall shown in the completion accounts, resulting in no deferred consideration being payable and even a repayment due to Lonscale [p. 4079].

141. On 4 February 2008, Wajid Ali forwarded documentation relating to the methodology for the asset valuation of Lonscale to Mr Meader, copying in Mr Addison, to which Mr Meader indicated his concurrence the following day [p. 4203]. Mr Montague was corresponding with Mr Addison at this time about how to treat the preference share repayment that had been made in November 2007 [p. 4191].

142. The minutes of the ICC show that Mr Addison attended in Guernsey on 26 March 2008. There are two minutes from that day [p. 691 and p. 695]. (Rather surprisingly, Mr Addison attended a meeting of a Cell not involved in these proceedings on the same day, but by telephone – p. 692.) The first of those minutes deals only with ratifying the change of investment advisor from BMS Finance Limited to BMA Finance Asset Management LLP. The second set of minutes covers more business and appears largely to be a periodic update from Mr Addison about the activities of the various Cells. By way of example, in respect of RE1 and RE2, "*Mr Addison remarked that there was currently a lot of property available for purchase although they were not expecting much activity for the time being as the valuation process was time consuming, although they may purchase though Real Estate Ventures/Finance.*" These minutes repeat the ratification of the change in investment advisor dealt with by the other minute. Finally, under Any Other Business, Mr Addison sought prior approval to make an investment into one of the incorporated cells through his SIPP. It was resolved to approve that request. Two days later, the members of the ICC, represented by Bordeaux staff, held the annual general meeting, which appears to have lasted for one hour and 15 minutes and records that the first accounting date of the ICC would be 31 March 2008, with reports and financial statements to be tabled at the next general meeting to be held in 2009.

143. On 28 April 2008, there was a further round of funding of Lonscale, again involving subscriptions to class C notes issued by AT1 involving RE1 and RE2 and then a corresponding subscription by AT1 to notes issued by Lonscale. On this occasion, Lonscale was provided with £200,000 [p. 4450] originating from RE1 and RE2 subscribing for £100,000 each [p. 4449]. On 9 June 2008, the next round of funding on a similar basis took place. RE1 and RE2 each subscribed for £300,000 of class C notes issued by AT1 [p. 4495] and, in turn, AT1 subscribed for £600,000 of Lonscale notes [p. 4497]. Shortly thereafter, on 2 July 2008 RE1 and RE2 each subscribed for £550,000 of notes and AT1 for £1.1 million of Lonscale notes [pp. 162 to 165 in bundle I]. Following Mr Addison alerting Mr Jeffs on 1 October 2008 that Lonscale only had £12,000 in the bank [p. 4709], on 6 October 2008 there was a fourth round of funding. RE1 and RE2 each

subscribed for £25,000 of notes [p. 4711] and AT1 subscribed for £50,000 of Lonscale notes [p. 4712]. On 11 December 2008, there was a final round of funding in that calendar year, by which RE1 and RE2 each subscribed £250,000 for class C notes [p. 4758] and AT1 subscribed for £500,000 of Lonscale notes [p. 4760].

144. Mr Addison attended a board meeting of the ICC on 11 July 2008, also attended by Messrs Meader and Radford. The minutes of that meeting [p. 714], which lasted 45 minutes, indicate that Mr Addison tabled an Investment Managers Report, from which it was shown that the Cells were continuing to deliver robust returns, despite the general downturn due to rising inflation and the credit crunch. Mr Addison also explained that the UK funds, which were the major investors in the Cells, were raising on average £3-5 million each week. This meant that the Cells were halfway towards the amount of £1 billion authorised by the GFSC and the board agreed that, when the Cells were nearer that limit, the GFSC should be contacted with a view to seeking an increase of the limit. The next board meeting of the ICC took place on 2 October 2008. The minutes [p. 752] show that it lasted 30 minutes, during which Mr Addison reported that the funds were performing well. The board discussed the current state of the markets and the effect on the funds, with Mr Addison commenting that IPOs would not be feasible in the near future. Mr Addison also advised that there had been heightened press interest in the funds due to their performance, which was why the accounts should urgently be concluded and lodged with the CISX. Mr Meader advised that the final draft of the accounts would be circulated and signed by two of the directors. At various meetings between 31 October and 21 November 2008, the latter relating to RE2 [p. 768], the boards of the Cells met to review the audited financial statements from the date of incorporation to 31 March 2008 and resolved that Messrs Meader and Radford be authorised to sign them and that the financial statements be published on the CISX.

145. By August 2008, a document in relation to the Club Easy Group entitled "Business Plan for Growth" [p. 4631] was in circulation and the directors of Lonscale were invited by Mr Jeffs to support it [p. 4655]. This was the culmination of efforts in the preceding months to come up with a plan of action. Consideration was being given to re-structuring so that there would be a property holding company and an operational company. It envisaged reaching a break even position in 2012/13, but this was dependant on significant further investment. On 21 August 2008, Mr King was also indicating to Mr Farrell and Mr Barkman the way in which the Group could perform in the near term:

> "*Clearly this requires huge input from Arch and Foundations otherwise I can't see that Clubeasy will ever show a profit with its current level of gearing. That said the refinancing exercise may require additional capital in the coming months of up to £7m.*
>
> *In order for the management to even have a shot at making inroads, Arch/Foundations have to give a commitment to Clubeasy to provide the necessary capital investment [say £50m equity over the next 2-3 years], via whatever means are available to each party.*"

2009 and the end of the ICC's Arch-related regime

146. Following a similar pattern to 2008, there was a further subscription for notes by RE1 and RE2 on 5 January 2009, this time for £250,000 each [p. 4773], which enabled AT1 to subscribe for £500,000 of Lonscale notes [p. 4775].

147. On 21 January 2009, Gordon Featherstone, who had been brought in to work within the Club Easy Group as a replacement finance director in 2008, was querying with Mr Jeffs the need for some documentary evidence for the two £3 million amounts paid to Arch and Foundations [p. 4833]. He pointed out that he had shown these simply as "restructuring costs". Then on 27

January 2009, Tom Moore of Kingston Smith LLP, in the context of preparing to audit Lonscale, asked Mr Featherstone for some support of the two £3 million fees paid on the acquisition because he needed "*to understand the commercial rationale behind them*", which Mr Featherstone forwarded to Mr Jeffs because "*Only you guys can help here*" [p. 4834]. When this reached Mr Farrell later the same day, he suggested asking Mr Addison because he had gone through it with BDO [p. 4837]. Mr Addison replied by repeating most of what he had written to BDO in November 2007 as set out previously [p. 4840]. He omitted any reference to there being no formal appointment letter and that Arch had acted on behalf of AT1 under the terms of its investment management agreement with that Cell. This response was then provided to Mr Jeffs who sent it on to Mr Featherstone [p. 4845]. On 29 January 2009, Mr Jeffs similarly asked for something from the Foundations side to share with the auditors, to which Mr Montague replied that he needed some information to understand the request [p. 4850]. Subsequently, an invoice dated 9 March 2009 to Lonscale was forthcoming from FCL and was raised "*in respect of the capital appreciation arising in the sale of the Clubeasy group*" [p. 4977].

148. Mr Addison attended a board meeting of the ICC on 30 January 2009, with Mr Meader tendering his apologies. The minutes of that meeting [p. 790] record that the board members discussed the negative comments made by certain press reporters, and felt that these incorrect perceptions could best be dealt with by the release of more timely and detailed information to the markets. Mr Addison advised that over the next period the Funds were expected to carry out share buybacks. Mr Radford reported on the successful visit to Bordeaux by Capita and that they were working on producing interim accounts for the Cells so that they could be filed with the CISX. The board discussed valuation policies in the Scheme Particulars, which had been looked at by Mr Addison and the effect of the new Companies (Guernsey) Law, 2008 and whether to pursue authorisation rather than just registration of the funds.

149. Mr Jeffs circulated a draft letter of comfort dated 30 January 2009, which was to be provided by AT1 to Lonscale Limited as part of the audit process, which reached Mr Addison no later than 10 February 2009, along with Mr King's observations on it [p. 4888]. On 16 February 2009, Mr Jeffs sent an e-mail to Mr Addison asking for the letter, which had been approved by the Investment Committee, to be signed and sent to him at the earliest opportunity [p. 4892]. A signed letter was sent, but by Arch rather than AT1, and so with minor modifications, dated 16 February 2009 [p. 4896]. That letter was provided to Kingston Smith LLP and reads:

> "*We refer to your request that we, (Arch Treasury IC Limited) provide you with this letter of comfort in respect of the provision of support to you and your subsidiaries (listed above) to assist you with continuing provision of working capital.*
>
> *We confirm that we will continue to provide working capital funding for a period of at least 12 months from the date of approval of the accounts of Lonscale Limited and its subsidiaries. We also confirm that the balance due to Arch Treasury IC Limited for Lonscale Limited at 31 July 2008 is £23,900,000. However no amounts are repayable within 12 months of approval of the accounts.*
>
> *We have been informed that Lonscale and its subsidiaries have budgeted for additional loans of £3,000,000 from Arch Treasury IC Limited and its shareholders for the period to 31 July 2009 and we confirm that we have budgeted to provide this amount as working capital funding.*
>
> *We undertake to inform you immediately in writing in the event that circumstances change in a manner such that it would or might no longer be open to us to continue to assist in your fundraising.*

For and on behalf of Arch Financial Products LLP acting as duly appointed Investment Manager for Arch Treasury IC Limited".

Arch later provided a letter signed by Mr King to the directors of AT1 dated 3 March 2009 [p. 4925], which set out the position as follows:

"*As your appointed Investment Manager we have considered the request from the auditors to Lonscale Limited and can confirm that, after due consideration by Arch's Investment Committee, currently it is our intention to continue to provide working capital to Lonscale Limited and its subsidiaries as per the attached draft letter. It is our recommendation that the requested letter of support be provided.*

I can confirm that the Arch Investment Committee considered the issue and approved such action at the meeting held on 16th February 2009."

150. In early 2009, as ACD of the OEICs, Capita undertook an investigation because of poor liquidity within the OEICs. Accordingly, on 12 March 2009, Mr Farrell sent a letter to the Chief Executive Officer of Capita Financial Group in which he recommended that consideration be given to suspending trading in the Funds of the OEICs [p. 4974]. It is apparent from the letter that it resulted from earlier correspondence and a meeting held on 10 March 2009. The reason Mr Farrell gave for this recommendation was that liquidity was a problem and there was a very strong risk that redemption requests would exceed the liquidity available to meet those requests. On the same day, Michael Derks of Arch was forwarding to the directors of the ICC and Cells his comments on the option of suspending trading in the Cells [p. 4978].

151. On 16 March 2009, Mr King provided Mr Featherstone with a summary of the position that he considered was a more accurate one for the benefit of Kingston Smith LLP [p. 4988]:

"*The funding of Lonscale for the purchase of Clubeasy was always intended to be structured in such away [sic] that part of it would be capital and part loans. There has been some confusion regarding Loan Notes which was caused, in part, by poor drafting internally within Arch. In addition there was an implication that Lonscale had itself issued Loan Notes to support the monies that it received from Arch which was incorrect. All of this is now being corrected.*

We believe that in the draft Lonscale Balance Sheet that we currently have should be adjusted by reducing the 'Creditors Falling Due After More than One Year' by £8m and increasing the 'Capital and Reserves' by £8m.

The original funding to Lonscale from Arch Treasury, plus interest to 30 July 2008, of £23.9m was made up as follows

- *£2.9m of funding via 6.5% Senior Loan Notes; and*
- *£13m of funding via 12 Mezzanine Loan Notes; and*
- *£8m capital.*

The £8m of capital should be seen as a subscription for share yet to be issued at that time: as the paperwork was not done at that time we are now putting this in place.

As Arch Treasury did not have the resources to provide all of this, it needed to be able to break up transactions, and there was a requirement to add some equity component to a

mezzanine loan note, Arch Treasury issued the following Loan Notes to investors (i.e. various Arch managed funds):-

- *"Lonscale A Notes" – £2.9m of senior loan notes paying a 6.5% coupon (with no equity share) – so these are effectively identical to the Senior Notes issued to AT by Lonscale.*

- *"Lonscale B Notes" - £13m mezzanine notes paying a 12% coupon, plus 25% share of any equity upside – so these are effectively the Mezzanine Notes issued to AT by Lonscale with the addition of the synthetic equity; and*

- *"Lonscale C Notes" – effectively synthetic equity of £8m that included 100% of Lonscale equity, but only 75% of the equity performance upside – there is no Lonscale equivalent to these.*"

The steps envisaged were undertaken on 30 March 2009. AT1 exercised its call option under notes issued to the Cells, with the Cell in question waiving the notice period usually required [eg, p. 4991] and AT1 as noteholder in respect of the Lonscale notes transferred them to the Cells [eg, p. 4992]. As a result, Lonscale assumed AT1's obligations in relation to the Cells, with equity warrants in Lonscale being provided to the Cells holding class B notes and the interests of the Cells holding class C notes being converted into shares in Lonscale (see para. 177, Cause and para. 153, Les Defenses).

152. There was a board meeting of ICC held on 18 March 2009, but on this occasion Mr Addison attended by telephone rather than in person. The minutes of that meeting [p. 803] record that Mr Addison reiterated to his fellow directors what had happened in respect of suspending the UK Funds due to liquidity issues and they discussed the consequences. Mr Radford, in particular, felt it was important to provide Capita with information, noting that, as the majority shareholder, Capita could convene an EGM to remove the board of directors and place the Funds into liquidation. The minutes include:

> "*Mr Radford suggested the possibility of providing Capita with a seat on the Board and Mr Meader asked if Mr Addison thought this would be beneficial.*
>
> *Mr Addison advised that he would take on board the suggestion to keep Capita informed and would relay the conversation to his colleagues and to the lawyers concerned.*"

There was also discussion about the contact that Mr Radford had had with the GFSC and the CISX. Mr Addison also informed his fellow directors that the division of income and capital shares in AT1 was proving cumbersome and asked if it were possible to "collapse" the structure back to what had originally been envisaged, and this was agreed. Mr Addison further advised that Arch would no longer be charging investment management fees on cross holdings and that it was considering refunding some of those previously charged. There was a further short board meeting of the ICC on 2 April 2009, at which the audited financial statements for the period ended 31 March 2008 were approved [p. 807]. There was a board meeting of AT1 on 20 May 2009 at which it was agreed to convert the Cell's capital shares to income shares [p. 846].

153. AT1 subsequently provided a letter of comfort directly to the directors of Lonscale dated 24 March 2009, again to be provided to Kingston Smith LLP, which was signed by Mr Addison as a director of AT1 and by Mr King on behalf of Arch [p. 5009], the material parts of which read:

> "*We confirm that we will continue to provide working capital funding for a period of at least 12 months from the date of approval of the accounts of Lonscale Limited. We have*

received the budgets for the year to 31 July 2009 which show additional loans of £3,000,000 from Arch Treasury IC Limited and we confirm that we have budgeted to provide this amount as additional working capital funding.

The Clubeasy "group" was purchased by Lonscale Limited following the issue, at par, of 8,000,000 ordinary shares of £1 each, giving a total number of 8,000,001 £1 ordinary shares, and issue of senior ("A" class Loan Notes: £2,900,000.00) and mezzanine ("B" class Loan Notes £13,000,000.00) loan notes totalling £15,900,000 to Arch Treasury IC Limited during the period to 31st July 2008. We confirm that these amounts are not due for repayment within 12 months of approval of the Lonscale Limited consolidated financial statements. …

Arch Treasury IC Limited has appointed Arch Financial Products LLP as Investment Manager and has given them full discretionary rights to invest and we, Arch Treasury IC Limited, confirm that we will not rescind or amend those rights and instructions as affects Lonscale Limited for 12 months from the date of approval of the Lonscale accounts.

We, Arch Financial Products LLP, as Investment Manager and with full discretionary rights confirm that we have taken this letter into account in planning our investment activities on behalf of Arch Treasury IC Limited and will comply with the terms of this undertaking."

154. At a meeting of the board of directors of Lonscale held on 25 March 2009, the oversight of omitting to allot 8 million ordinary £1 shares to AT1 was rectified [p. 5014]. That rectification took effect from the date of completion of the SPAs (29 October 2007). By an agreement dated 30 March 2009, *inter alia* RE1 and RE2 acquired tranches of the shares in Lonscale that had previously been allotted to AT1 [p. 5026]. The final tranche of those shares was acquired from AT1 by Grange Nominees Limited. The consideration for each share was 96.56p.

155. The consolidated financial statements for Lonscale for the year ended 31 March 2009 [p. 5046] include the explanation that:

> "*On 29 October 2007 the Group acquired 100% of the issued capital of Clubeasy Group plc, Clubeasy Property (UK) Limited and Hayes Limited for £20,276,985 inclusive of costs of acquisition. During the year additional costs of £20,901 were incurred in relation to those acquisitions, increasing the consideration paid inclusive of costs of acquisition to £20,297,886.*"

Mr Farrell resigned as a director of Lonscale on 9 April 2009. Messrs King and Jeffs were appointed as directors on the same day.

156. On 12 May 2009, Mr King informed the directors of the ICC and Cells by e-mail [p. 5148] that Arch's Investment Committee had approved on 14 April 2009 ongoing support for Lonscale, with amounts to be paid in April, May and July. He added that "*Without these payments, the investment could be seriously compromised as the company is in turnaround stage but is forecast to be self sufficient shortly.*" Messrs Meader and Radford duly approved the transaction on 15 May 2009 and informed the GFSC [p. 5157], with Bordeaux receiving confirmation by return that the GFSC was content for the transaction to proceed [p. 5165]. (There was by then a requirement imposed by the GFSC that no business could be conducted by the Cells without first seeking its approval.) As a result, RE1 and RE2 each subscribed for £240,000 of Lonscale class A notes on 19 May 2009 [p. 5187]. Subsequently, RE1 and RE2 each subscribed for £490,000 Lonscale

class A notes on 23 June 2009 [p. 5294], although the amount paid by each was £492,966.85 [p. 5293].

157. On 15 May 2009, Mr Addison sent an e-mail to Messrs Meader and Radford [p. 5155] informing them that Capita had decided not to become insiders, so they would not be able to see some documents, eg, the liquidity plan. This was followed on 18 May 2009 by a meeting between the directors of the ICC and the Cells with Capita [p. 841].

158. On 3 June 2009, a board meeting of the ICC was held, but the minutes show that Mr Addison abstained from that meeting "*to avoid any possible conflict of interest*" and a letter to that effect was tabled [p. 867]. The business discussed related to the acquisition by Arch International Group Holdings Limited ("AIGHL"), which had purchased all of Arch UK's share capital in March 2008, of certain of the Cells' shareholdings in that company by way of buyback. The other directors resolved to ratify the various agreements, even though the independent valuation of those shares resulted in a loss to the Cells. It was considered preferable to accept the amount offered, which was already in escrow, rather than risk further losses in future.

159. On 9 July 2009, Arch's Investment Committee approved a proposal that RE1 and RE2 should purchase further notes from Lonscale, totalling around £650,000 [p. 5365]. This further injection of funds was intended to deal with an issue that had arisen in respect of Hayes Limited and its lender, Lloyds. The transaction needed to be referred to the GFSC, which sought further clarification, which was provided by Mr King to the directors of the ICC and Cells on 27 July 2009 [p. 5379]. Mr King drew attention to the reputational consequences for the entire Club Easy Group and its brand name if the problems facing Hayes Limited meant the students had difficulties with their accommodation. Because the loan notes were issued by the top company, Lonscale, the security arose from the assets of the whole Group, and not just those held by Hayes Limited. In the end, RE1 and RE2 each subscribed for £300,000 of Lonscale class A notes on 14 August 2009.

160. The ICC held a board meeting on 17 July 2009. The minutes [p. 913] cover the audit position of the Cells, the delay in publication of net asset values at the CISX because of a review being undertaken of them by the GFSC and then turn to Mr Addison's update on Capita. This extended to advising Messrs Meader and Radford that Arch was considering transferring the investment management mandate to a new investment manager unconnected to Arch. On 27 July 2009, Mr Meader had forwarded to Mr Addison a draft announcement of suspension of the Guernsey funds, indicating that Bordeaux was being pressured to proceed on it, but Mr Addison's response [p. 5374] was that he could not agree to any suspension on the basis of the information to which he was privy. The pressure to which Mr Meader referred was being exerted by Capita to suspend the listings or de-list completely, resulting in discussions between Mr Radford and the CISX, as referred to in an e-mail from him to his fellow directors dated 8 July 2009 [p. 903]. On the evening of 27 July 2009, the ICC board of directors held a meeting, with Mr Addison attending by telephone [p. 925], at which the opposition of Mr Addison for the same reasons as he had set out was reiterated. However, Messrs Meader and Radford felt that it would be in the best interests of the shareholders of each Cell to suspend the listing of the shares on the CISX until an acceptable net asset value computation for each had been agreed, so the board resolved by a majority to suspend the listings temporarily.

161. In a document dated 21 August 2009, the FSA, which had been reviewing the position of the Arch Group since around the time of the suspension of the UK Funds, set out a synopsis of the legal and compliance issues identified [p. 5800]. At section 22 of the document, in respect of Lonscale/Club Easy, it referred to:

"– *Club Easy is the trade name for a group of UK and Isle of Man companies focused on the student accommodation sector. The student accommodation sector was seen as one that would weather the downturn in property well. This has proven to be the case, with rental growth of circa 10% achieved.*

– *It was acquired using an Isle of Man SPV, Lonscale Ltd in October 2007*

– *The transaction was originated and due diligenced by the principals of Foundations Capital, in combination with Cobbetts (Legal), Storeys (Valuation) and PKF (Forensics).*

– *As originator of the transaction and in consideration for them agreeing to give up the lion share of the transaction to the Arch syndicate, it was agreed that Foundations would be paid an origination fee based on the difference between the total amount paid for the Notes (syndication proceeds) and the acquisition price.*

– *Arch created a debt and equity investment syndicate via Arch Treasury in the form of A, B and C Notes, with Arch FP as arranger. Several funds participated. The syndication proceeds were £21M. Foundations agreed to share their origination fee 50/50 with Arch FP as Arranger i.e. £3M each.*

– *At the time of acquisition, the completion balance sheet value was circa £33.3M and the acquisition price circa £17M, thus the acquisition was believed to be extremely good value. Upon deal finalisation (completed by Foundations), the acquisition price dropped further to £13.2M plus a contingent amount of £1.8M, making £15M. Thus the funds made a substantial gain at inception.*

– *Further, the £1.8M amount was contested by Arch and subsequently did not need to be paid, providing additional value to the investor syndicate.*"

162. At a board meeting of the ICC held on 7 September 2009, a proposal from Spearpoint setting out the basis on which it could be appointed as the replacement investment manager was tabled and considered. The minutes of that meeting [p. 968] indicate that Mr Radford considered that Arch's position had become untenable and that Mr Meader noted that two alternative proposals, neither of which was satisfactory, had been put to the board informally. Accordingly, provided that others, such as Capita, the GFSC and the FSA supported Spearpoint's appointment, it appeared to be a good option. Arch was duly replaced as investment manager to each of the Cells by Spearpoint pursuant to a transfer and implementation agreement dated 25 September 2009 [p. 5929]. It was signed on behalf of Arch by Mr Addison and Mr Farrell and on behalf of Spearpoint by Mr Davey and another. Mr Davey explains that the first task of Spearpoint was to acquire information about the underlying assets of the Cells and the approach it took as to classify each as "urgent", "dead – waste of time" or "other", and that Lonscale, along with one other asset, was given an "urgent" classification (para. 17 of his witness statement).

163. At a board meeting of the ICC held on 1 October 2009 [p. 1078], which Mr Addison attended by telephone, the directors discussed the outstanding audited accounts and net asset value publications. They resolved to notify the CISX that the accounts would not be published earlier than 31 October 2009 or later than 30 November 2009 and that no net asset valuation would be made available until the accounts were published. They gave as the reason for the delay "*the need to be extremely cautious in valuing underlying assets in very difficult market conditions*".

164. During the afternoon of 5 October 2009, Mr Davey spoke with Mr Scott on the telephone because Mr Davey was gathering a list of potential non-executive directors for consideration of appointment to an independent board for the ICC and so also the Cells. Mr Davey explained to Mr Scott that the FSA, GFSC and Capita were of the view that there should be an orderly wind down of the ICC and the Cells. Mr Scott met with representatives of Capita on 9 November 2009.

165. As part of the transfer process from Arch to Spearpoint, in his e-mail dated 12 October 2009 [p. 5959], Mr Davey made a suggestion for how to deal with historic fees payable to Arch, which was considered by the board of the ICC at a meeting on 16 October 2009. Mr Farrell had previously given Arch's perspective and support in a response sent *inter alia* to Mr Radford on 13 October 2009 [p. 5978]. The minutes of the ICC board meeting [p. 1089] record that Mr Addison tendered his apologies and the response sent to Mr Davey by Mr Radford on 19 October 2009, which broadly agreed with the principal suggestion made by Spearpoint but offered different terms [p. 1092], further explains that Mr Addison "*did not attend that meeting because of his potential conflict of interest*". This response led Spearpoint to send a letter dated 22 October 2009 to Arch proposing some amendments to the transfer and implementation agreement. At a board meeting of the ICC on 22 October 2009, it was agreed that the ICC and the Cells would accept the terms for the transfer from Arch to Spearpoint set out in a document emanating from Arch [p. 1096].

166. Mr Davey explains that he felt that there needed to be a knowledge transfer from those who had worked within Arch to Spearpoint, although he recognised that concern might be expressed that it was using Arch staff to resolve a situation that Arch had created (para, 12 of his witness statement). The methodology used was to create a new entity, Spearpoint (UK) Limited, which was not regulated, as the research base and source of information for Spearpoint, as investment manager to the Cells, to operate. Mr Davey identified Mr Smith and Richard Rhodes as persons who could assist Spearpoint and that Mr King and others had important knowledge, but that they were unlikely to be retained within the Spearpoint organisation for longer than necessary.

167. In a document dated November 2009, Spearpoint provided an analysis of Lonscale and set out the potential courses of action [p. 6021]. Spearpoint had explored selling Lonscale to a third party but dismissed that option because of low indications on price. (Mr Davey also referred to Arch having undertaken a similar exercise in the summer of 2009 and the potential buyers of Lonscale being approached by Spearpoint being those with which Arch had made enquiries earlier in the year. At that time, the marketplace was such that there were plenty of situations where buyers for property were being sought because of the global financial crash, so anyone with liquidity was looking for a bargain.) Spearpoint considered fixing the business but regarded that as being its Plan B. Accordingly, Spearpoint considered the best course of action to be "*for the Cells … to agree a sale to a party related to the minority shareholder*". Spearpoint recognised that the structure of the deal was far from perfect but regarded the party related to the minority shareholder as the natural buyer because of knowing the business, already having a representative on the board of directors and being motivated to buy it and fix it. The deal would be structured in such a way that there would be some cash immediately and some deferred, as well as the right for ownership to revert to the Cells in the event of default on the deferred consideration, plus the retention of an entitlement to share in any windfall gains and property appreciation. Spearpoint regarded this outcome as "*a reasonable exit value*", with fair protection to the Cells.

168. At a board meeting of the ICC held on 19 November 2009, which Mr Addison attended by telephone, a proposal to appoint Andrew Duquemin, Hugh Aldous and Mr Scott to the board was considered and agreed, subject to receiving GFSC approval and on the basis that the appointments

would not take effect until the ICC was in a position to announce them to the CISX [p. 1127]. The GFSC confirmed its approval of those board appointments on 9 December 2009.

169. On 20 November 2009, in an internal e-mail within Arch [p.6099], Mr King commented that "*the position at Lonscale is pretty hopeless due to the burden of debt, little change being made to systems to enable the garnering of portfolio management contracts for the OpCo, no progress in actually bringing any contracts to the fore, complications with getting banks to bend etc*". He regarded the realisation value as being zero, which is what he proposed should be given as the September valuation, recognising that the August value had been zero for equity and that debt had been given a "*£4m haircut*", but he recommended that there be "*a complete write-down of the outstanding loan notes to zero*". This recommendation was put into effect a few days later [p. 6109]. Mr Davey had been forewarned about the possibility of "*back-dating a lowering of NAV value on the student accommodation portfolio*" in an e-mail from Mr King on 4 November 2009 [p. 6023]. As Mr Davey noted, this course of action would have an impact on Spearpoint because the fees of the investment manager are in part calculated on the basis of the value of the assets being managed, which he described, during questioning, as "*a minor irritation in the context of everything else*". However, he said that this was not the motivation for disposing of Lonscale as quickly as possible.

170. Mr Addison attended a board meeting of the ICC on 27 November 2009 [p. 1151], at which the directors resolved that, despite the concerns raised by Spearpoint and Capita plc, the temporary suspension of the listing of the Cells on the CISX should be lifted once the net asset valuation computations had been agreed.

171. Spearpoint became the new investment manager of AT1 under an agreement dated 30 November 2009 [p. 6164]. The terms of this agreement were different from those of the IMA between Arch and AT1.

172. By a letter dated 3 December 2009 sent to Messrs Meader and Radford, Mr Addison tendered his resignation as a director of the ICC and Cells [p. 1155]:

> "*As agreed, following the appointment of Spearpoint Limited as investment manager, please accept this as my resignation as a director of Arch Guernsey ICC Ltd and its cells following the appointment of additional directors at the board meeting of 10 December 2009. I have enjoyed working with you immensely and hope that our paths will cross again in the future.*"

173. Mr Addison attended a board meeting of the ICC by telephone on 4 December 2009, at which publication of the net asset values at 31 March 2009 and at 30 September 2009 were agreed to be published on the CISX, along with a letter to be sent to shareholders of the Cells on 7 December 2009 [p. 1164]. This letter, signed by Mr Radford, explained to shareholders the role being undertaken by Spearpoint and the fact that certain Arch staff had been employed by Spearpoint to provide continuity. It announced the appointment as directors of Messrs Duquemin, Aldous and Scott and the resignation of Mr Addison. It further explained that Arch had agreed to give up its entitlement to certain accrued management fees and that Spearpoint would be paid an implementation fee.

174. Mr King prepared a memorandum dated 3 December 2009 [p. 6173] containing his proposals for the restructuring of Lonscale, which Mr Davey had requested from him because Mr Davey knew that Mr King was a director of Lonscale and so had been intimately involved in the Cells' investment for some time. This was the first occasion on which Mr Davey had been fully briefed

about Lonscale. Mr Davey forwarded the memorandum on 9 December 2009 to Messrs Meader, Radford, Aldous, Duquemin and Scott [p. 6187]. In his memorandum, Mr King explained that:

> "*Clubeasy was acquired as a turnaround project, and had a running loss of approximately £5m per year when purchased. The implementation of significant change was delayed due to missing the first pricing point at purchase [referring to the long lead times when changing the terms on which the student accommodation was let], which meant that the hugely loss making run-rate continued for some time building up the need for Lonscale to borrow to fund operating losses. This only put more burden on the consolidated company.*
>
> *Since then, some progress has been made in increasing revenues (particularly via above market rental increases), and reduction in costs (mainly focused utility provision costs in an all-inclusive product Clubeasy offering), however the company, even on an operating level excluding all debt to the funds, is still running at a loss. This requires either the equity owners or lenders to support the company to keep it going.*"

175. On 10 December 2009, there was a further board meeting of the ICC. As the minutes show [p. 1226], Mr Addison attended by telephone. Because the audited financial statements ended 31 March 2009 were not available to sign, the resignation of Mr Addison did not take effect. Similarly, the appointments of Messrs Aldous, Duquemin and Scott were deferred, although they were present and invited to stay for the remainder of the meeting. Mr Davey was also present. Some of the discussion related to general transitional matters. However, in respect of Lonscale, the minutes record that:

> "*Mr Davey drew attention to his paper in the Board Pack and advised that there could be value in the investment but only if there were changes to controls and management. It was noted that the investment had been included in the NAVs at nil and that further funding was required. It was noted that historically student accommodation has been profitable. The partner in the investment had been given two weeks to consider proposals for restructure.*
>
> *The investment was bought as a turnaround but the projections had not been achieved. The operational management of the business was discussed. It was noted that further progress would be made once the partner had considered their options.*"

176. The paper to which this minute refers had been prepared by Mr King, being one of those who had moved from Arch to Spearpoint, and was addressed to the Guernsey Investment Committee [p. 6188]. According to Mr Scott, it was from this paper that the new directors learnt how the interests of the Cells were structured, with RE1 and RE2 holding equity and debt and the other four Cells holding debt through the mezzanine loan notes. They also understood that the latest valuation of the Cells' interests was zero and that Mr King took the view that "*from the forecasts provided by management, it is clear that Clubeasy cannot even breakeven under the current set-up*". He also noted that "*an outright sale for cash would probably produce a zero value outcome for the funds (= current NAV)*" and made a number of proposals as "*corrective projects*" for consideration.

177. Mr Davey's preferred option for Lonscale (paragraphs 45 and 46 of his witness statement) was to see if the minority shareholder, effectively being Mr Barkman and Mr Montague, would be prepared to make an offer to buy out the Cells. He formed the impression that they believed that the property market would "roar back", which was the main reason they were keen to acquire the whole of Lonscale. He reminded them that to date it had been the Cells putting additional monies

into Lonscale and that their "free ride" was over. Either they needed to take over Lonscale at a reasonable price or the Cells would take Lonscale over, thereby extinguishing their minority interest. The negotiations over price continued until such time as Mr Davey believed they would go no higher and to push further would result in them losing interest.

178. On 20 December 2009, Mr Davey sent an e-mail to Messrs Scott, Aldous, Duquemin, Meader and Radford about Lonscale [p. 6236], attaching a draft MOU for a sale to the minority equity owner. He indicated that there was some urgency because the buyer wished to complete before the end of the year. He explained the respective ownership and how it was treated in the owners' net asset values. He drew attention to the possibility that Lonscale would be re-acquired on default, but, in that event, then being owned 100% rather than the existing 75.5% stake, adding that the risk was that the new owners could make the overall business worse in the time it would be under their control. Mr Davey commented further on 29 December 2009, following a meeting he had with Mr Montague and Mr Barkman, on the revised terms then under consideration, and he forwarded these comments to Messrs Aldous, Duquemin and Scott on 30 December 2009, accompanied by a copy of a revised valuation that had been provided to him by Mr Smith [p. 6238]. Mr Duquemin had concerns, which he set out in an e-mail to Messrs Aldous and Scott on 31 December 2009 [p. 6267] that he did not understand fully why Lonscale as an asset had been written off completely when there appeared to be a clear margin or property assets above bank debt. He also wished to have some independent view on the value of the assets. He had been told by Bob Locker, with whom he had worked previously, that a detailed look could prove expensive, and so Mr Locker had volunteered to have a look at the properties with his team with a view to giving an informal view. Mr Duquemin believed that might assist and had been authorised by Mr Davey to forward the information provided to Mr Locker.

2010, including the Disposal Agreement

179. Mr Locker provided his initial thoughts to Mr Duquemin on 5 January 2010 [p. 6295] and briefly also on 8 January 2010 [p. 6307], with Mr Duquemin summarising these, as also discussed with Mr Locker, in an e-mail to Mr Davey on 12 January 2010 [p. 6308]. Mr Duquemin relayed that through sampling the portfolio, Mr Locker's team had identified a number of properties where the valuation attributed by Storeys appeared to be higher than the vacant possession valuation ought to be. This was confirmed by Mr Locker's subsequent informal written comments sent by him to Mr Duquemin on 20 January 2010 and relayed by Mr Duquemin to Messrs Aldous, Scott and Davey the same day [p. 6409]. Mr Locker indicated that his team had found some property valuations to be consistent with those in the Storeys' valuation, but had found others where there was a marked difference in values. He explained the different approaches that could be taken to valuing this type of portfolio and concluded that he was "*very sceptical of the total valuation without an explanation for the substantial percentage differences between the comparables*".

180. At the suggestion of Capita, Mr Davey had also shared the paper on Lonscale with Martin Bolland, the incoming chairman of Capita plc, who provided his input on 3 January 2010, which Mr Davey forwarded to Mr Duquemin the following day [p. 6280]. Mr Bolland hoped that Lonscale was one of the lower quality assets with which Mr Davey had become involved. He had discussed it with someone who has experience of the student accommodation sector, who was not particularly enthused by the predominance of houses in multiple occupation as against purpose built units. Mr Bolland doubted whether there was any meaningful value in the run-off period and floated the option of handing the assets back to the banks. As Mr Davey explains, Spearpoint did not find that an attractive option because it was not prepared to walk away and give up on realising value from Lonscale (para. 37 of his witness statement). At this time, Mr Davey was also seeking a view from John Reynolds at Capita on why Lonscale had been written down to zero, which he also forwarded to Mr Duquemin [p. 6285].

181. Early on 15 January 2010, Mr Davey provided to the directors of the ICC and Cells a sale and purchase memorandum of understanding ("the MoU") for which he sought agreement to sign [p. 6309]. Mr Davey envisaged there being a conference call at 4 pm that day to discuss this. A few hours later, Mr Davey offered the following explanation in a second e-mail [p. 6350]:

> "*I forgot to say when I sent the MOU on Lonscale that this is probably our most tricky decision. Although the auditors have written the holding down to nil we believe that there is potential value in the business. We also have a plan to fix it. This would involve putting in a specialist to renegotiate debt, a cost reduction program and changes to the student offering at the next pricing point. Without doubt there is a high level of execution risk associated with this (particularly around the banks) and it is a 2-3 year job. Further cash would also have to be committed which we estimate to be in the region of £2-4m over the next two years. If this was successful we would hope to realise more value although the precise timing and amount would be uncertain and dependent upon a recovery in the property market.*
>
> *We do not believe that the buyers are high quality buyers. They are, without doubt the only likely buyer in the current position, and highly motivated. If they do not fix this business then it will have very negative consequences for their overall business. Part payment in ARCH shares and deferred consideration make this a very scrappy deal. We are concerned that a default is possible. We have, therefore, put in place a mechanism to monitor progress closely and simplify the process of stepping in. If they do default we believe that we will have received at least £1.3m of value (on signing of MOU and completion) together with any deferred consideration paid. We will also be in a better position as we will own 100% of the business and believe that they are likely to have done some hard work for us in cutting costs and putting some additional cash into the business itself.*
>
> *All in all a scrappy deal but one where the risk to the funds is reduced and £10.6m would represent a reasonable exit in our view.*"

182. The meeting of the board of the ICC took place at 5.20 pm on 15 January 2010. The minutes [p. 6357] show that Mr Meader and Mr Radford gave their apologies. Indeed, Mr Radford had sent an e-mail just a few minutes earlier [p. 6353] in which he confirmed that he had read the MoU and supported the proposals. Mr Scott and Mr Aldous attended by telephone, so Mr Duquemin was the only director physically present. The minutes reflect the points that Mr Davey reiterated and also Mr Duquemin's information as a result of the informal view expressed by Mr Locker, which Mr Davey pointed out was reinforced by a recent letter received from one of the bank lenders, which also called into question the values given to the properties by Storeys. After further discussion, the board resolved to approve the signing of the MoU. Mr Davey indicated that he expected a final agreement to be signed in the following fortnight. Mr Scott explains (at para. 100 of his witness statement):

> "*What we knew at this time therefore was that (i) the financial information we had on Clubeasy was not entirely robust and/or reliable and, despite the rather dismal picture that it painted of the financial situation, was still likely to be over optimistic, (ii) Clubeasy was haemorrhaging cash, (iii) the proposed sale represented the only available option for the Cells to exit from this investment in a way that realised any immediate value for the Cells; it was an out of favour asset and there were very few potential buyers, and (iv) all other options required the Cells to remain in the investment and commit additional funds on an on-going basis into the black hole of Lonscale. Taking all*

of that information into account, we could only regard the investment in Lonscale as a dismal and failing investment."

183. Extraordinary General Meetings ("EGMs") of the Cells took place on 28 January 2010. The various notices of those meetings were sent out on 4 January 2010. The meetings were held sequentially. By way of example, the notice in respect of RE [p. 1340] includes a letter from the five directors recommending shareholders to vote in favour of the proposals to be put to the meeting. The first ordinary resolution being put related to an amendment to the investment objective of the Cell, so that it would read:

> "*The Investment Manager will manage the Company's portfolio with a view to realising its assets within the shortest period of time consistent with achieving a reasonable realisation price for such assets and with the intention of disposing of all such assets within 5 years. Realisations will be managed, as far as possible, with a view to ensuring regular and consistent distributions of proceeds to Shareholders.*"

The special resolution to be put involved a name change to the name of the Cell in which these proceedings were commenced. This was proposed to underline that Arch had no further involvement in the management of the Cell. The various resolutions were approved at the EGMs. By a written special resolution of the ICC on 29 January 2010 [p. 1418], the name of the ICC was changed to SPL Guernsey ICC Limited.

184. On 19 January 2010, Mr Davey informed the five directors that the MoU on Lonscale had been signed [p. 6360]. Mr Barkman had signed on behalf of the Buyer, and Mr Davey on behalf of the six Cells selling. The terms were broadly those previously discussed. Initial consideration was due from the Buyer of £200,000 worth of shares in various Cells of the ICC on execution of the MoU, the balance of the Buyer's shares in those Cells, which are shown in Appendix 1 as having a value a little above £1 million when using the net asset values of 30 September 2009, being "payable" on completion, plus £200,000 in cash. Deferred consideration of a little over £9.3 million in total would be payable in tranches monthly until January 2012. There were some other elements of the overall consideration due from the Buyer, in return for which the selling Cells agreed to write-off the debts due to them under the various Lonscale Notes of approximately £23.2 million, plus some other elements of consideration.

185. Having signed off the audited financial statements for the year ended 31 March 2009, Messrs Meader and Radford resigned as directors of the ICC and so also the Cells on 28 January 2010. It had been intended that all the former directors would resign at the same time, to achieve what Mr Scott describes as "*a clean handover*", but there had been a delay in approving the financial statements for some other cells, so Messrs Meader and Radford had remained on the board until those financial statements were finally signed off, and Mr Scott does not know why Mr Addison's resignation was agreed at the end of 2009.

186. A replacement amended MoU was subsequently signed on 15 February 2010 and forwarded to Messrs Aldous, Duquemin and Scott by Mr Davey the following day [p. 6416]. He explained that the changes were mainly for technical reasons and further clarified for Mr Scott's benefit [p. 6461], that these were to permit the Buyer to "*squeeze the deal*" into their fund. He added "*we remain desperate to sell*". One change was that the identity of the Buyer had changed to Lonscale Guernsey Limited SPV.

187. Ernst & Young LLP replaced Moore Stephens as auditors to the ICC and the Cells with effect from 4 March 2010.

188. At a board meeting of the ICC on 10 March 2010, as recorded in the minutes [p. 6471], Spearpoint reported that the shares, worth approximately £150,000, had been received in respect of the sale of Lonscale and that completion was expected a few days later. There was a plan in place in the event the Buyer failed to complete. Mr Davey continued to keep Messrs Aldous, Duquemin and Scott informed during that month of progress towards finalising the sale of Lonscale. The formal Acquisition Agreement (but adopting the term used by the parties being referred to as "the Disposal Agreement") was executed on 26 March 2010 [p. 6556]. As Mr Davey had explained, the terms of the deal had evolved slightly from what had previously been discussed with the board of directors, so as to accommodate matters to suit the Buyer, Lonscale Holdings Limited, a Guernsey-registered company, but the substance was essentially the same. The Sellers were PF2, PF3, PF4, PF5, RE1 and RE2. There was a condition that the Buyer be registered as the holder of 1,960,000 shares in Lonscale within ten days. That number reflected the balance of the shares in Lonscale above those held by RE1 and RE2 then owned by Foundations Capital Program plc. Just over 1.5 million shares in various SPL cells were to be transferred to the Buyer by it taking on the debts owed by Lonscale under the various multi-class Notes and payment of the cash consideration. The cash consideration was apportioned between PF2, PF3, PF4, PF5, RE1 and RE2 as 21.593%, 16.057%, 21.593%, 12.735%, 41.011% and 14.011% respectively. Payment of the balance of the cash consideration of £9,316,587.72 was to be paid in accordance with the instalment plan set out, although if early repayment of £200,000 was made on or before 10 June 2010, the amount would reduce by £600,000. The deferred consideration was secured against the shares in Lonscale. (These terms were subsequently amended in July 2010 [p. 6825] so that the early repayment was put back to 10 September 2010 and the amount reducing by only £400,000. The payment due on 10 July 2010 was also reduced by £200,000 in consideration of payment of a little over £500 in amendment fees. Mr Davey reported that the money due in September was paid on time, which meant £475,000 had been received [p. 6845].) In questioning, Mr Davey summarised the position as it being "*a scrappy deal in scrappy circumstances with a scrappy buyer*", adding that those were the circumstances that Spearpoint and the Cells had inherited.

189. Mr Scott estimates that about two-thirds of the time of the new board of directors of the ICC and the Cells during the first quarter of 2010 was spent trying to save some of the other cells, known as the Africa Cells, although those efforts were eventually unsuccessful. The three of them spent their time on problems that required their immediate attention in order to offer the opportunity to optimise a medium-term solution for as many investments as possible. In the Report and Consolidated Financial Statements of PF2 for the year ended 31 March 2010 [p. 6625], which was finalised by the end of September 2010, the position in respect of Lonscale was summarised as follows:

> "*In March 2010, the Fund sold its stake in Lonscale as part of an exit from the business by all of the Cells of SPL Guernsey. The Fund's interest in Lonscale had been valued at zero prior to the sale because of the high levels of bank debt against the properties owned by Lonscale and the consistent operating losses generated by the business. The business was sold for £10.4m to the then minority Shareholder of Lonscale in a deal featuring part up-front and part deferred consideration. The deferred consideration is conditional and is payable over a two year period following the date of the sale. The position is valued at zero in the accounts because of the conditional nature of the deferred consideration, however as at the date of writing this report (6 September 2010) the Fund has received £0.3m of upfront and deferred consideration. If the Fund is paid in full, we expect to receive £2.2m over two years in total consideration for the same.*"

190. In an e-mail on 15 April 2010 [p. 6759], Mr Davey put to Messrs Aldous, Duquemin and Scott a proposal that the Cells lend Lonscale £200,000 over a six-week period at 5% per annum to meet a cash flow gap that had been known about for some time and which should have occurred once the transaction had completed, and so be something for Lonscale to manage, but which had, due to the delay in executing the Disposal Agreement, instead arisen during the completion process. Those funds were needed as part of the restructuring over debt with Lloyds Bank, with which Spearpoint was assisting. Mr Davey pointed out that this effectively amounted to returning the cash element of what had been received under the Disposal Agreement and he assessed the prospects of default on this loan as being highly unlikely and that the loan would enhance the prospects of the Cells receiving the deferred consideration that was due to commence in June 2010. Lonscale would get an influx of cash in May from student payments due at that point. Mr Davey's investment proposal noted that Mr King continued to be a director of Lonscale, but that it was a term of the sale that he resign that position upon completion, which was envisaged to be within the following week. Mr Scott confirms (para. 113 of his witness statement) that the board of directors agreed this short-term loan, which was duly repaid by 13 May 2010.

191. The resignation of Bordeaux as Administrator was accepted by the board of directors on 20 April 2010 and took effect two months later. With effect from 1 August 2010, Elysium Fund Management Limited ("Elysium") was appointed as the new Administrator. Mr Duquemin, as the chairman and principal shareholder of Elysium, did not participate in the process of identifying a new Administrator. Christopher Harris was appointed as a director of the ICC and the Cells with effect from 1 August 2010. This appointment arose from Mr Duquemin's stated intention to resign as a director following the appointment of Elysium. His resignation took effect from 1 October 2010, following the release of the 31 March 2010 results the day before.

192. On 29 November 2010, Elysium informed the board of the ICC and the Cells that it had uncovered documentary evidence that Arch had arranged for what Mr Scott describes as "*a secret commission*" (para. 128 of his witness statement) to be made in 2007 in connection with the Lonscale transaction. When questioned about this terminology, Mr Scott acknowledged that there had been documentation prepared subsequently that meant it was not secret or hidden, but that the material had not been unearthed for the benefit of the new directors until this time, which is why he referred to it as previously having been secret.

2011 onwards

193. By early 2011, Lonscale Holdings Limited was struggling to meet the instalments of the deferred consideration under the amended Disposal Agreement. By way of example, as recorded in the minutes of the ICC board of directors meeting on 21 March 2011 [p. 6881], Spearpoint had chosen to permit reduced payments of £265,000 per month to enable Lonscale to keep on side with their banks, which was regarded as preferable in the longer term because it preserved the possibility of the deferred consideration being paid in due course. However, the instalments were changed again pursuant to a Variation Agreement relating to the Acquisition Agreement (ie, an amendment to the Disposal Agreement) that was executed on 15 April 2011 [p. 6913].

194. As Mr Davey pointed out to Mr Aldous in an e-mail on 26 April 2011 [p. 6924]:

> "*As discussed Lonscale is short of cash. I believe that this is a cashflow issue only but cannot prove it to a professional standard. They have an urgent need. ie Wed. Given the timeframe, and their weak financial position, I cannot prove to the cells that they will get their money back to the standard required. I am, however, prepared to take a personal punt myself and lend them the money. So this email is about disclosure to the board and my own compliance officer who is copied in on this e-mail. I will receive a 5k fee for*

lending 100k. Can you confirm that you are happy with this? Please call if you would like to discuss."

Mr Aldous responded the same day that he could not see any conflict causing the board to have a problem with Mr Davey's plan [p. 6926], and the compliance officer, Jackie Sholl, had no issues either because it was a personal loan from Mr Davey [p. 6928].

195. On 7 July 2011, Mr Davey informed Messrs Aldous, Harris and Scott that Lloyds Bank, which owned about a quarter of the total debt of the Club Easy Group had taken steps against Hayes Limited by putting it into administration [p. 6937]. This was further discussed at a meeting of the ICC's board of directors on 11 July 2011, the minutes of which [p. 6940] refer to Hayes Limited being placed into liquidation, with Mr Davey raising the possibility that the ICC might be interested in purchasing properties owned by Hayes Limited at a discount depending on the prices at which Lloyds wanted to sell. Mr Davey recognised that Lonscale needed some breathing space in relation to the instalments schedule for the deferred consideration under the amended Disposal Agreement and informed the directors of this view by e-mail on 18 July 2011. In this e-mail [p. 6946], Mr Davey mentioned that Lonscale was seeking a loan of £45,000 to meet demands of suppliers and, for similar reasoning to the position in April 2011, he could not make a case for the Cells to advance such a loan, but he was willing to lend Lonscale that amount personally until the Group got its rent roll in September. He sought the board's approval to him making that loan.

196. Mr Addison has signed a note made of a telephone conversation with Mr Radford, also involving Mr Farrell, at 14.55 on 15 August 2011 [p. 6957], which reads:

> "*Peter called from his mobile to follow up on an email request from RA to confirm certain details with respect to an investment by the ICC in Lonscale and subsequent correspondence from the new ICC directors.*
>
> *He confirmed that we had discussed Lonscale with him and the fact that Arch would be taking a fee from the transaction but would check his notes when he is back in the office, to see if he had anything officially recorded.*"

197. On 15 August 2011, Mr Davey sent another e-mail to Mr Aldous on the subject of him making a further personal loan to Lonscale [p. 6958]:

> "*Lonscale needs to borrow £43k until the end of the month. I have already lent them £45k. I will probably do this in expectation of getting back the full sum at the end of the month plus interest. They promise me that if they can get through Aug into Sept they will be in a position to have brought on board new investors into the Lonscale holding company which will allow them to make an offer to buy out the Cells in full. I have no way of proving this so I cannot justify the Cells taking the risk. From a personal perspective I am happy to help them one last time as the payoff to the Cells will be good if they can bring in new investors allowing them to make an offer to buy us out. there [sic] is obviously a conflict but given the position of the Cells this is a conflict in the Cells favour. Any objections to me making the loan?*"

The same day, Mr Aldous indicted he had no objection [p. 6960].

198. There was a similar e-mail communication from Mr Davey on 14 October 2011 [p. 6970] to the board of the ICC, following a meeting he had had with Mr Barkman. This time the loan request was for £140,000 for just under one week and, although Mr Davey had indicated previously that he had made his last loan, he mentioned what he described as a "carrot" in inviting board permission, which related to the possibility of Lonscale making a discounted offer of £3 million,

plus the outstanding payment from June of that year in satisfaction of the balance of the deferred consideration then still due. Mr Davey explained that the loan would be "*for a £7k return on the £140k lent*", which he regarded as "*quite cheap for this sort of risk money*". The response from Mr Aldous was that he had not minded Mr Davey "bridging" Lonscale in the past and had no objection because he had "*been completely and utterly transparent about it*" [p. 6973]. In principle, Mr Aldous was also content with the concept of a discounted early payment. Mr Scott was also content with Mr Davey's proposal to lend money to Lonscale, recognising that, although risky, Mr Davey could decide what to do with his own money. Mr Scott was also content with the proposed discounted early repayment because "*getting cash out now might look like a very good deal looking back later*". Mr Davey's response was that he might have taken those comments as reason to ask "*for a higher return as from an investment perspective it is an opportunity to gouge but didn't want it to look too egregious based on the connection*" [p. 6977].

199. At a meeting of the board of the ICC on 7 November 2011, as set out in the minutes [p. 7001], Mr Davey advised that he had been re-paid the money that he had lent to Lonscale in his personal capacity. He reported that Lonscale had still not paid any of the deferred consideration due from June 2011 onwards. The increase in tuition fees had resulted in there being fewer students requiring accommodation. There were ongoing discussions with Lonscale about an exit strategy. On 14 November 2011, Mr Davey sent an e-mail to the directors updating them about ongoing discussions with Mr Barkman [p. 7008], explaining that he was content with the instalments schedule being delayed because money had been poured into Lonscale to put it into a better position to survive, which had the benefit of improving the collateral held by the Cells. At that time, further consideration of accepting partial early repayment was dependent upon the instalment that had been due in June 2011 being paid. Mr Scott's position was that he was sceptical about the financial outlook for the following two years for this asset and so considered it might be a good time to disentangle the Cells from Lonscale altogether if possible, even at a discount (para. 142 of his witness statement).

200. By the summer of 2012, no further instalments of the deferred consideration had been paid by Lonscale Holdings Limited. The board of the ICC considered a proposal at its meeting on 16 July 2012 to acquire a small portfolio of properties that had been mortgaged with the Yorkshire Building Society ("the Yorkshire portfolio"), thereby enabling a restructuring of the deferred consideration. The minutes of that meeting [p. 7062] record that the board resolved to make such a recommendation to a new SPV, KCSB Properties Limited, to acquire the Yorkshire portfolio and noted the cash requirements of the various Cells to provide funding by way of loan notes. The aggregate amount was £940,000. The Yorkshire portfolio had a value of almost £2.5 million. The amount of deferred consideration being forgiven was, therefore, a little over £1.5 million of what was, by then, approaching £7 million in outstanding deferred consideration and accrued interest. The balance of the deferred consideration of a little over £5.25 million, together with interest that would become payable, was to be repaid in a further 28 instalments running from September 2012 to December 2014. A Deed of Amendment and Restatement of the Acquisition Agreement (ie, a further amendment to the Disposal Agreement) was then prepared but was not executed because Foundations Program plc was by then under the control of what Mr Scott describes as a receiver and so the revised repayment schedule never formally came into effect.

201. In November 2012, Spearpoint was renamed Brooks Macdonald Asset Management (International) Limited. It remained the investment manager of the Cells until the end of 2014. For 2015, Elysium undertook that function and since 1 January 2016 the Cells have been self-managed.

202. Les Defences of the Second to Fourth Defendants were tabled on 23 November 2012. In response to para. 172 of the Cause ("*The Lonscale Investing Cells did not authorise either of these payments ("the Lonscale Disputed Payments")*", para. 200 of their pleading states:

> "*(1) It is admitted that no authorisation for these payments was given on behalf of the Lonscale Investing Cells by Mr Radford or Mr Meader, neither of whom knew of the alleged payments, nor were on notice of them.*
>
> *(2) Nor was Mr Radford, Mr Meader, or Bordeaux on notice, at the time Bordeaux made the transfers required for the investment in the Lonscale Notes, that Arch was raising a larger sum by way of the Lonscale Notes than the amount for which AT1 had agreed to acquire Lonscale Limited.*
>
> *(3) Paragraph 19(5) above is repeated as to the nature of Arch's and Mr Addison's obligations in respect of conflicts of interest and any fees received by Arch as a result of transactions effected on behalf of the Cells. The said fees were not disclosed to the Boards of the Lonscale Investing Cells, whether before or after the investments were made.*
>
> *(4) Save as set out above, paragraph 172 is not admitted.*"

Paragraph 19(5) of those Defences reads:

> "*In the event that a conflict arose between Arch's own interest and that of the Cells, Arch had a contractual duty to fairly resolve such conflict, which duty inter alia required as part of such fair resolution full and proper disclosure to the Directors of the nature and extent of that interest and of what had been done to manage the conflict fairly. Moreover, Mr Addison also owed a duty as a Director to fully disclose to the other Directors the nature and extent of any material interest he had in any transaction, which included (by virtue of his position in Arch), disclosure of the nature and extent of Arch's interest in the same.*"

Further, at para. 209, the issue of the knowledge of Messrs Meader and Radford of the details of the acquisition of Lonscale is re-visited:

> "*(2) At all materials times Mr Meader and Mr Radford had no knowledge or, and were not on notice of, the Lonscale Disputed Payments.*
>
> *(3) As set out above at paragraphs 5(3) [referring to Article 35 of the Articles of Association of each Cell] and 19(5), each Director had a duty to disclose the nature and extent of any material interest he had in a transaction or arrangement with a Cell to the other Directors. As such, Mr Meader and Mr Radford were entitled to assume that Mr Addison would fully make any disclosure of any interest (including through Arch) he had in the transaction. For the avoidance of doubt, if (which is not admitted), Mr Addison was aware of the alleged Lonscale Disputed Payments, Mr Addison was obliged to disclose that payment to Mr Meader and Mr Radford so they could consider whether this conflict had been or could be appropriately managed, and if so how.*"

203. During 2013, Lonscale Holdings Limited informed the directors of the ICC and the Cells that there was a re-financing underway, which was expected to complete in October of that year. Accordingly, it agreed to pay £5,000 each week on a Friday. Mr Scott confirms that the last payment received was £15,000 on 11 October 2013 (para. 164 of his witness statement). Despite

Lonscale Holdings Limited being in default of the terms for paying the deferred consideration at various times, as Mr Davey explains, the Cells did not take Lonscale back, as they were entitled to opt to do under the terms of the amended Disposal Agreement, because it was not economically viable for them to do so.

204. On 4 November 2014, Lonscale Holdings Limited was ordered by this Court to be compulsorily wound up [p. 7447]. The Cells did not submit any proof of debt to the liquidators because, as Mr Scott puts it, "*there was zero prospect of any recovery*" (para. 162 of his witness statement).

205. On 19 December 2014, judgment was entered in the High Court in favour of the Cells jointly and severally against Arch and Mr Farrell in the amounts specified in the order, including pre-judgment interest, together with costs on the indemnity basis [p. 7449]. Those amounts (including pre-judgment interest) were £3,454,865.02, £2,568,958.15, £3,454,865.02, £2,037,440.46, £6,421,020.54 and £6,421,020.54 in favour of PF2, PF3, PF4, PF5, RE1 and RE2 respectively. Mr Scott confirms that the amounts payable to the Cells under this order remain unpaid.

206. On 19 January 2015, the Upper Tribunal, Tax and Chancery Chamber (Financial Services) published its decision. This was a reference by Arch, Mr Farrell and Mr Addison of the Notices issued by the FSA (now known as the Financial Conduct Authority) on 14 September 2012. In respect of Mr Addison, the Upper Tribunal determined to impose a financial penalty of £200,000 on him for failure to comply with Statements of Principle 1 and 7 pursuant to section 66(3)(a) of the Financial Services and Markets Act 2000, to withdraw his approval to carry out controlled functions pursuant to section 63 of that Act and to make an order, pursuant to section 56 of that Act, prohibiting him from performing any function in relation to any regulated activities carried on by any authorised or exempt persons, or exempt professional firm, on the ground that he is not a fit and proper person.

207. On 13 July 2015, Lonscale Limited was struck off the Register of Company in the Isle of Man and dissolved [p. 7452].

208. The Court has set out these facts in considerable detail and, so far as possible, chronologically, in order to provide as full an analysis as possible of what took place over these years. The Court is of the view that they paint a picture of a level of involvement from Mr Addison that goes further than the position he sought to portray, through downplaying his involvement and seeking to deflect attention away from himself.

Experts' opinions

209. Ultimately, the positon of the parties' experts on the issues they were asked to address resulted in more agreement than disagreement than may have been envisaged on reading their respective initial reports. The Jurats consider that this earlier divergence of opinion arose, at least in part, from Mr Tyrtania not being provided with the Plaintiffs' witness statements at that stage. The Jurats further note that Mr Tyrtania had been instructed as an expert in the Upper Tribunal proceedings on behalf of Arch, Mr Farrell and Mr Addison. Whilst his previous involvement in these matters is not a reason to treat his evidence as anything other than independent expert opinion, the Jurats note that his initial report dated 8 September 2016 analyses some of the issues by reference to Arch rather than being focused on Mr Addison's position as a director of the ICC and of the Cells. Elements where Mr Tyrtania had strayed outside the areas where he was able to offer an opinion had been removed from his initial report as a result of rulings made at the pre-trial review. Consequently, the internal numbering between his two reports was not always entirely consistent, but has been addressed by the Deputy Bailiff when directing the Jurats. The

Deputy Bailiff further reminded the Jurats that leave had been given to the parties to adduce this expert evidence to assist on the question of loss and not in respect of other matters, eg, breach of duty.

210. Having met on 27 January 2017, the two experts produced a helpful note of their discussion [item B23 in the trial bundle]. The Jurats recognise that these areas of agreement and disagreement provide the best starting point for their consideration of the experts' evidence.

211. In respect of ascertaining a fair value of the Club Easy Group at the time of the Group's acquisition by Lonscale in 2007 and when the Cells disposed of their interest in Lonscale in 2010, Mr Tyrtania and Mr Moore agree that the value cannot be determined by reference to its asset value alone. Mr Tyrtania remains of the view that he has not been provided with sufficient information to determine the value of the Group at the time of Lonscale's acquisition of it, whereas Mr Moore believes the Group had nil value at that time. Both experts agree that a turn around of the Group required more than simply debt restructuring. Mr Tyrtania believes that acquiring the Group may have been a reasonable proposition if it were possible to turn the business around. He is aware that Arch was considering various ways to do this, but is unable to say how far Arch had progressed with its plans. At the time of disposal of the Cells' interest in Lonscale, Mr Moore believes that the fair value of those interests was zero. Both experts agree that Spearpoint did well in obtaining the price achieved on the disposal of the Cells' investment in Lonscale. Mr Tyrtania adds that he cannot rule out the possibility that Spearpoint could have achieved a higher value through holding the investment in Lonscale for five years before disposing of it, although he cannot quantify what value could have been achieved in those circumstances. Both experts agree that the sale by the Cells of their interest in Lonscale can be described as a "*distressed sale*", with Mr Moore not regarding it as a "*fire sale*". The experts agree that the losses suffered by the Cells on their investments in Lonscale can properly be calculated on the basis of the schedule of monies paid out and monies received. Neither expert was able to identify a good proxy for the investment made in Lonscale nor to determine what return could have been expected from any hypothetical alternative investment. They further agree that it is likely that the credit crunch had some effect on the attitude of the lending banks to the Club Easy Group. They also agree that the student property sector was seen as a more resilient sector at the time of the credit crunch, with the consequence that the valuation of student accommodation may not have been hit as much as other property sub-sectors.

212. Mr Moore summarised his conclusion on the fair market value of the Club Easy Group at the time of its acquisition by Lonscale by stating that regard ought to have been had to its profit and loss account rather than concentrating on its net assets. The Group was seen as continually loss-making and required regular capital injections to keep it operational, which is why he would have valued it at nil at that time. For it to have value, a detailed recovery plan needed to be in place to generate sufficient cash flow to service and repay its indebtedness. Mr Moore queried Mr Tyrtania's initial valuation of the Group of £29.2 million based on its property portfolio, and in Mr Tyrtania's response, he acknowledges that Mr Moore had presented a well-reasoned theory for calculating the fair market value at both acquisition and disposal. Mr Tyrtania had no argument with Mr Moore's conclusion that Mr Tyrtania had reached a valuation at £29.2 million that was too high. Because the Group continued to be loss-making after its acquisition by Lonscale, and had required some £6 million by way of cash injection, Mr Moore took the view that it had properly been valued at nil prior to its disposal. Further, he took the view that the Cells could not reasonably have obtained more in return for their investment either through retaining it until a later date or disposing of it differently.

213. Having regard to the due diligence undertaken in 2007, Mr Moore is of the view that the PKF report should have sounded warning bells that the acquisition of the Group would be a risky

transaction warranting further investigation. In his opinion, in order to determine properly the value of the Group as an ongoing business, which was the basis on which it was being acquired, he would have looked at the current assets and liabilities, proposed future levels of assets and liabilities after allowing for the injection of new capital and reconstructed loan amounts, and models of future earnings and profitability, with a view to identifying the date on which the Group would become profitable. In the light of Mr Tyrtania's response to Mr Moore's report, the Jurats find that Mr Tyrtania also aligns himself to that methodology, although Mr Tyrtania questions whether the Club Easy Group was acquired as a going concern, preferring to view it as being a turnaround opportunity in respect of a distressed asset.

214. Mr Moore took the view that it was a sensible decision to sell Lonscale at the time that Spearpoint took over as investment manager and, further, that the option of selling to the minority shareholder was likely to give the most realistic prospect of the best reasonably achievable return. Having taken the view on valuation that he did, Mr Moore concluded that any price agreed above zero would be a positive outcome for the Cells. In relation to the option of retaining the investment in Lonscale for longer, Mr Moore commented that changes to valuations in property markets happen relatively slowly, meaning that any recovery from the fall in valuation in 2009 may have taken several years. Overall, he took the view that the sale was conducted reasonably and in a manner most likely to achieve the most favourable price possible. In his response, Mr Tyrtania found himself in broad agreement with Mr Moore's response to the questions he was asked to deal with, albeit that Mr Tyrtania notes that Mr Moore does not appear to have commented on any possible effect of the revised investment strategy of the new board of the Cells once Spearpoint had been appointed.

215. Although both experts made some attempt to consider what the Cells might have achieved had they invested in some other student accommodation business, rather than the Club Easy Group, they ended up agreeing that they could not properly offer any opinion on this issue. In those circumstances, aside from noting that there has been agreement that the student property sector has been more resilient than other property sectors, the Jurats can derive no further assistance from those sections of the experts' reports.

216. To the extent that the expert evidence differed, the Jurats find themselves more inclined to accept the evidence of Mr Moore than that of Mr Tyrtania.

Further directions – Breach of duty

217. The Deputy Bailiff summarised the elements that the Plaintiffs needed to prove as being the existence of a duty, breach of that duty and a causative link to the loss (or losses) that arise from that breach. If Mr Addison wishes to avoid the consequences of the losses that are so found, he needs to show that the Plaintiffs have failed to mitigate their losses. If there remains some damages that would otherwise be payable by Mr Addison to the Plaintiffs, Mr Addison further advances that he enjoys an indemnity under the Articles of Association of the Cells or, as an alternative, that the Court should relieve him from his liability pursuant to section 522 of the Companies (Guernsey) Law, 2008. The Deputy Bailiff pointed out that if the Jurats did not find that there had been a breach of any duty as pleaded, that would end the Plaintiffs' claim. Similarly, if there was no causative link from a breach to some loss, that would also result in the Plaintiffs' claims being dismissed.

218. The duties themselves, as set out in para. 10 of the Amended Cause, had been admitted by Mr Addison to exist. In respect of the duty at sub-para. (d) ("*not to act in the affairs of the Company and Cells where there was a conflict between the duties owed to the Company and Cells and other duties and interests of the Directors (or any of them), unless any such conflicting duties or*

interest has been properly disclosed by the Director concerned to the other Directors"), Mr Addison relies, however, on Article 35 of each Cell's Articles of Association and/or on the general disclosure of his conflict of interest in the Scheme Particulars and/or his disclosure at Board Meetings of the Cells. Accordingly, the Deputy Bailiff was able to direct the Jurats that Mr Addison did not challenge the existence of the duty relating to conflicts of interest but that he argues that no breach can be found by reason of what he suggests he was required to do to discharge this duty.

219. The Deputy Bailiff referred to Article 35 of the Articles of Association of each Cell, relating to directors' interests, as something to which the Jurats may well wish to pay particular regard, because it was relied upon by Mr Addison. It provides:

> "*35.1 Subject to the provisions of the Law, and provided that he has disclosed to the other Directors the nature and extent of any material interest of his, a Director notwithstanding his office:-*
>
> *35.1.1 may be a party to, or otherwise interested in, any transaction or arrangement with the Cell, or in which the Cell is otherwise interested;*
>
> *35.1.2 may act by himself or through his firm in a professional capacity for the Cell (otherwise than as Auditor) and he or his firm shall be entitled to remuneration for professional services as if he were not a Director;*
>
> *35.1.3 may be a Director or other officer of, or employed by, or a party to any transaction or arrangement with, a shareholder of or otherwise directly or indirectly interested in, any body corporate promoted by the Cell, or with which the Cell has entered into any transaction, arrangement or agreement or in which the Cell is otherwise interested; and*
>
> *35.1.4 shall not by reason of his office, be accountable to the Cell for any benefit which he derives from any such office or employment or from any such transaction or arrangement or from any interest in any such body corporate and no such transaction shall be liable to be avoided on the ground of any such interest or benefit.*
>
> *35.2 For the purposes of this Article:-*
>
> *35.2.1 a general notice given to the Directors that a Director is to be regarded as having an interest of the nature and extent specified in the notice in any transaction or arrangement in which a specified person or class of persons is interested shall be deemed to be disclosure that the Director has an interest in any such transaction of the nature and extent so specified; and*
>
> *35.2.2 an interest of which a Director has no knowledge and of which it is unreasonable to expect him to have knowledge shall not be treated as an interest of his.*"

The operation of Article 35 is, therefore, dependent on there being disclosure of the interest in question. That disclosure can be achieved by a general notice given to the other directors. Accordingly, the Jurats could consider whether any general notice covered the conflict of interest relating to the fee payable to Arch in respect of the acquisition of Lonscale and so the Club Easy

Group by any of the Cells and also focus on the way in which Mr Addison says he informed Mr Meader, and so by association Mr Radford, of the fee.

220. Guernsey's companies' legislation is not as extensive as the UK Companies Act 2006. One example of the differences between the two enactments is that the general duties of directors specified in Chapter 2 of Part 10 of the 2006 Act have not been replicated in the 2008 Law. By way of example, section 175(1) of the 2006 Act provides that "*A director of a company must avoid a situation in which he has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company.*" The other subsections of section 175 explain that this applies in particular to the exploitation of any property, information or opportunity, and that the duty is not infringed if the matter has been authorised by the directors, which may be given where the matter is proposed to and authorised by the directors. By way of further example, section 174 of the 2006 Act provides that *"A director of a company must exercise reasonable care, skill and diligence*", which means "*the care skill and diligence that would be exercised by a reasonably diligent person with (a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company, and (b) the general knowledge, skill and experience that the director has.*"

221. Section 162 of the 2008 Law, which appears to be drawn from Chapter 3 of Part 10 of the 2006 Act, rather than from anything found in Chapter 2, including, as it does, elements taken from sections 182 and 185 of the 2006 Act, so far as they are material, is the Guernsey provision requiring disclosures of interest. (The Deputy Bailiff explained to the Jurats that the Incorporated Cell Companies Ordinance, 2006, as amended, had been repealed and replaced by the 2008 Law, with effect from 1 July 2008. Part XXVIII of the 2008 Law now deals with incorporated cell companies.) Section 162 provides that:

> "*(1) A director of a company must, immediately after becoming aware of the fact that he is interested in a transaction or proposed transaction with the company, disclose to the board of directors –*
>
> *(a) if the monetary value of the director's interest is quantifiable, the nature and monetary value of that interest, or*
>
> *(b) if the monetary value of the director's interest is not quantifiable, the nature and extent of that interest.*
>
> *(2) Subsection (1) does not apply if –*
>
> *(a) the transaction or proposed transaction is between the director and the company, and*
>
> *(b) the transaction or proposed transaction is or is to be entered into in the ordinary course of the company's business and on usual terms and conditions.*
>
> *(3) A general disclosure to the board to the effect that a director has an interest (as director, officer, employee, member or otherwise) in a party and is to be regarded as interested in any transaction which may after the date of the disclosure be entered into with that party is sufficient disclosure of interest in relation to that transaction.*"

222. It is, however, common ground between the parties that, in the absence of any express provision or settled jurisprudence in Guernsey law, regard can properly be had to English law for guidance.

In *In re Med Vineyards Limited (in liquidation)* (unreported, 25 July 1995), the Court acknowledged that the root of an earlier Law from 1908 relating to companies was the Companies Act 1862, and further that the omission from the 1908 Law of certain provisions had not arisen from any "*conscious decision to exclude them*". In *Flightlease Holdings (Guernsey) Limited v Flightlease (Ireland) Limited* [2009-10] GLR 38, the Court pointed out (at para. 91) that:

> "*(1) the concept of a limited company was imported into Guernsey law from English law;*
>
> *(2) since its importation into Guernsey law in the 1880s, it has naturally been appropriate to look to English law to help in the solution of problems concerning companies which are not covered by Guernsey statutes or customary law*".

Although it is less apparent that where there are omissions in the 2008 Law they do not now result from there being a conscious decision taken not to include them in Guernsey's statutory regime relating to companies than would have been the case previously, the Deputy Bailiff has directed the Jurats about the law relating to directors' duties on the basis that the customary law in this Island reflects the approach that has developed elsewhere, including where those duties have been codified into statute.

223. The Deputy Bailiff first warned the Jurats about substituting for the decisions of the directors of the ICC and the Cells their own opinions as to the decisions taken. In doing so, he referred them to the passage from *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 821 (at page 832), to which Advocate Williams drew attention:

> "*Their Lordships accept that such a matter as the raising of finance is one of management, within the responsibility of the directors: they accept that it would be wrong for the court to substitute its opinion for that of the management, or indeed to question the correctness of the management's decision, on such a question, if bona fide arrived at. There is no appeal on merits from management decisions to courts of law: nor will courts of law assume to act as a kind of supervisory board over decisions within the powers of management honestly arrived at.*"

224. This level of caution about interfering with directors' decisions is further described in other cases which serve as a reminder that decisions taken in good faith should not be treated as breaching the director's fiduciary duty. For example, in *Iesini v Westrip Holdings Ltd* [2009] EWHC 2526 (Ch) Lewison J (as he then was) commented, in the context of decisions in accordance with the duty in section 172 of the 2006 Act to promote the success of the company involving whether to bring (or continue) a court claim, that "*The weighing of all these consideration is essentially a commercial decision, which the court is ill-equipped to take, except in a clear case.*" Similarly, in *Extrasure Travel Insurances Ltd v Scattergood* [2003] 1 BCLC 598, Jonathan Crow, sitting as a Deputy Judge of the High Court, summarised the position (at para. 97) as being that:

> "*… it is not sufficient for a company to prove that its directors took action which proved to be damaging to the company, unless it can also show that the directors did not honestly believe that the action was in the best interests of the company. The fact that the directors' belief was unreasonable does not put them in breach of their fiduciary duties, if that belief was honestly held.*"

A further passage to which Advocate Williams refers (albeit slightly expanded here) is from the judgment of Jonathan Parker J in *Regentcrest plc (in liquidation) v Cohen* [2001] 2 BCLC 80 (at para. 120):

"*The duty imposed on directors to act bona fide in the interests of the company is a subjective one (see Palmer's Company Law para. 8.508). The question is not whether, viewed objectively by the court, the particular act or omission which is challenged was in fact in the interests of the company; still less is the question whether the court, had it been in the position of the director at the relevant time, might have acted differently. Rather, the question is whether the director honestly believed that his act or omission was in the interests of the company. The issue is as to the director's state of mind. No doubt, where it is clear that the act or omission under challenge resulted in substantial detriment to the company, the director will have a harder task persuading the court that he honestly believed it to be in the company's interest; but that does not detract from the subjective nature of the test.*"

225. Although the Deputy Bailiff drew these principles together for the benefit of the Jurats so as to direct them to focus on what Mr Addison had decided on behalf of the Cells and their investment in Lonscale, and so the Club Easy Group, and to view this subjectively rather than objectively, he added that this line of authority might not be as helpful to their deliberations as Advocate Williams suggested it would be because the principal allegation against Mr Addison was that he had made no disclosure of the conflict of interest that existed in Arch being paid a substantial fee for its part in this acquisition. However, if the Jurats were to find that there had been some disclosure, the level of disclosure and the decision-making following thereafter would become more relevant as to whether Mr Addison had acted in the honest belief that it was in the best interests of the Cells to proceed as they did and invest in the Club Easy Group and provide funds for the payment of the fees to Arch and to the order of Mr Barkman. In relation to those questions, there were other issues more directly engaged concerning whether Mr Addison had exercised the care, skill and diligence reasonably expected of him as a director. The statement of that duty of care in section 174 of the 2006 Act reflects the position at common law (see, eg, Hoffmann LJ in *Re D'Jan of London Ltd* [1993] BCC 646, referring to the similarly worded section 214(4) of the Insolvency Act 1986 as being an accurate statement of the duty of care owed by a director at common law). The Deputy Bailiff made it clear to the Jurats that the position in Guernsey law is the same and that they could, therefore, regard the cases to which the Court had been referred as developments of those principles that could assist them in their deliberations.

226. In that regard, the Deputy Bailiff highlighted the approach that had been described by Jonathan Parker J in *Re Barings plc (No. 5)* [1999] 1 BCLC 433, a case to which both Advocates had referred. Albeit in the context of considering disqualification orders, this judgment explains (at page 484) that:

"*… the court will assess the competence or otherwise of the respondent in the context of and by reference to the role in the management of the company which was in fact assigned to him or which he in fact assumed, and by reference to his duties and responsibilities in that role. Thus the existence and extent of any particular duty will depend upon how the particular business is organised and upon what part in the management of that business the respondent could reasonably be expected to play (see Bishopsgate Investment Management Ltd (in liq) v Maxwell (No 2) [1993] BCLC 1282 at 1285 per Hoffmann LJ). For example, where the respondent was an executive director the court will assess his conduct by reference to his duties and responsibilities in that capacity.*"

The Deputy Bailiff, therefore, directed the Jurats that they may find it helpful to consider whether Mr Addison had any role distinct from that of the other directors of the ICC and the Cells and, in any event, to consider the part that he was reasonably expected to play in the management of the business of each of the Cells. In doing so, he also drew attention to the content of the paragraph

following that extract in the judgment: "*Thus, while the requisite standard of competence does not vary according to the nature of the company's business or to the respondent's role in the management of that business – and in that sense it may be said that there is a 'universal' standard – that standard must be applied to the facts of each particular case.*" In doing so, he stressed that the findings as to whether Mr Addison had or had not discharged his duties as a director to the standard required was a fact-specific determination for them to reach on the evidence they had heard and read rather than through any comparison with what might or might not have happened in any of the cases to which the Advocates had referred the Court. Further, the passage on which Advocate Richardson places particular store is slightly later in the judgment (at page 489) and summarises the general propositions in relation to the duties of directors that can be adopted as applicable to directors of Guernsey companies:

> "*(i) Directors have, both collectively and individually, a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business to enable them properly to discharge their duties as directors.*
>
> *(ii) Whilst directors are entitled (subject to the articles of association of the company) to delegate particular functions to those below them in the management chain, and to trust their competence and integrity to a reasonable extent, the exercise of the power of delegation does not absolve a director from the duty to supervise the discharge of the delegated functions.*
>
> *(iii) No rule of universal application can be formulated as to the duty referred to in (ii) above. The extent of the duty, and the question whether it has been discharged, must depend on the facts of each particular case, including the director's role in the management of the company.*"

227. The Deputy Bailiff directed the Jurats that the ability of a director to delegate exists as a matter of Guernsey law in the same way that it has been described elsewhere. The first statement on which Advocate Richardson relies comes from the judgment of Briggs J (as he then was) in *Lexi Holdings plc (in administration) v Luqman* [2007] EWHC 2652 (Ch) (at para. 219):

> "*… it is in my judgment now firmly established as a matter of law that no company director may simply leave the management of the company's affairs to his or her colleagues, or to other delegates, without committing a breach of duty. The reason for this is because, although the law permits and to an extent encourages delegation by directors of their functions, every act of delegation gives rise to a concomitant obligation to supervise the delegate. I have in mind in particular the analysis of Jonathan Parker J in re Barings plc and Others (No. 5) [1999] 1 BCLC 433 at 486 to 489, basing himself on the decision of the Court of Appeal in re Westmid Packing Services Ltd [1986] 2 BCLC 646, and on an earlier judgment of Sir Richard Scott VC in an earlier part of the Barings disqualification proceedings, cited at page 487F to H.*"

228. The second case from which Advocate Richardson seeks to draw principles in respect of circumstances giving rise to a conflict of interest is the New South Wales case, *Asic v Adler* [2002] NSWSC 171. In amongst the lengthy judgment of Santow J in that case, a series of summary propositions was set out in para. 372. The principles applicable to the duty of care and negligence, which had been enacted as section 180 of the Corporations Act 2001, were:

> "*(1) Directors owe a duty of care and skill at common law and in equity: Permanent Building Society (in liq) v Wheeler (1994) ACSR 109; Daniels t/as Deloitte Haskins & Sells v AWA Ltd (1995) 37 NSWLR 438.*

(2) However, the equitable duty to exercise reasonable care and skill is not properly classified as a fiduciary duty: Permanent Building Society (in liq) (supra) per Ipp J (at 158).

(3) The statutory duty of care and diligence, s180, is framed in similar terms to its predecessor s232(4). It has been said of the latter that the duties imposed upon directors by it are essentially the same as the duties of directors under the common law: Sheahan (as liquidator of South Australian Service Stations) (in liq) v Verco [2001] SASC 91; (2001) 37 ACSR 117 per Mullighan J (at 134); Daniels v Anderson (1995) 37 NSWLR 438 per Powell JA at 603; see also Lockhart J in Australian Innovation Ltd v Petrovsky (1996) 21 ACSR 218 at 222.

(4) In determining whether a director has exercised reasonable care and diligence one must ask what an ordinary person, with the knowledge and experience of the Defendant might be expected to have done in the circumstances if he or she was acting on their own behalf: Permanent Building Society v Wheeler (supra) per Ipp J (at 159); ASC v Gallagher (1993) 10 ACSR 43.

(5) However, under the implied term in a contract of employment of an executive director, the director (such as here Mr Williams and Mr Fodera) will be taken to have promised the company that he or she has the skills of a reasonably competent person in his or her category of appointment and that he or she will act with reasonable care, diligence and skill: Permanent Building Society v Wheeler at 287-8.

(6) Although the standard of reasonable care is generally said to be that of an ordinary prudent person (Re City Equitable Fire Insurance Co. Ltd [1925] Ch 407 per Romer J) there is some suggestion that directors of a professional trustee company owe a higher duty of care: Wilkinson v Feldworth Financial Services Pty Ltd (1998) 29 ACSR 642 at 693.

(7) In determining whether a director has breached the statutory standard of care and diligence (s180(1)), the court will have regard to the company's circumstances and the director's position and responsibilities within the company: see also Explanatory Memorandum to the CLERP Bill 1999 (para. 6.75).

(8) In accordance with these responsibilities directors are required to take reasonable steps to place themselves in a position to guide and monitor the management of the company: Daniels t/as Deloitte (supra) at 664. That is to say, (supra) at 666-67:

- *(a) a director should become familiar with the fundamentals of the business in which the corporation is engaged;*
- *(b) a director is under a continuing obligation to keep informed about the activities of the corporation;*
- *(c) directorial management requires a general monitoring of corporate affairs and policies, by way of regular attendance at board meetings; and*
- *(d) a director should maintain familiarity with the financial status of the corporation by a regular review of financial statements. Indeed, he or she will be unable to avoid liability for insolvent trading by claiming that*

they had never learned to read financial statements: Commonwealth Bank of Australia v Friedrich (1991) 5 ACSR 115 at 125.

(9) A director appointed to a company because of special expertise in an area of the company's business is not relieved of that duty to pay attention to the company's affairs which might reasonably be expected to attract inquiry, even outside that area of expertise: Re Property Force Consultants Pty Ltd (1995) 12 ACLC 1051 at 1061.

(10) At general law, a director is entitled to rely without verification on the judgment, information and advice of management and other officers appropriately so entrusted. However, reliance would be unreasonable where directors know, or by the exercise of ordinary care should have known, any facts that would deny reliance on others: Daniels t/as Deloitte at 665-6.

(11) Although reasonableness of the reliance or delegation must be determined in each case, the following may be important in determining reasonableness:

(a) the function that has been delegated is such that "it may properly be left to such officers": Re City Equitable Fire Insurance Co Ltd (supra) per Romer J.

(b) the extent to which the director is put on enquiry, or given the fact of a case, should have been put on inquiry: Re Property Force Consultants Pty Ltd (supra) per Derrington J at 1,060.

(c) the relationship between the director and delegate, must be such that the director honestly holds the belief that the delegate is trustworthy, competent and someone on who reliance can be placed. Knowledge that the delegate is dishonest or incompetent will make reliance unreasonable: Biala Pty Ltd v Mallina Holdings Ltd (1994) 15 ACSR 1 at 62.

(d) the risk involved in the transaction and the nature of the transaction: Permanent Building Society v Wheeler (1994) 14 ACSR 109 (although in this case the Chief Executive Officer in question also had a conflict of interest).

(e) The extent of steps taken by the director, for example, inquiries made or other circumstances engendering "trust";

(f) whether the position of the director is executive or non-executive: Permanent Building Society v Wheeler per Ipp J, though, in Daniels v Anderson (supra), the majority have moved away from this distinction.

(12) That general law explains what the Corporations Act now requires when referring (s190(2)) to "reasonable grounds" in codifying the directors' responsibilities for the actions of the delegate. Thus under s198D of the Corporations Act directors may delegate any of their powers to a committee of directors, a single director, an employee of the company or any other person (This delegation must be recorded in the company's minute book: see s251A). Moreover, the director will be responsible for the delegate's exercise of power if he or she did not believe on reasonable grounds and in good faith, after making proper inquiries if the circumstances indicate the need for it, that the delegate was reliable and competent in relation to the power delegated and would

exercise the power in conformity with the duties imposed on the directors of the company by the Corporations Act: s190(2).

(13) For the purposes of s180(1) and relevantly in the present case, failing to ensure that a company makes loans only in accordance with its authorised practices and failing to ensure that the company has a proper system of controls and audit in its business to avoid any defalcation by officers and employees may amount to breaches of the statutory duty of care and diligence: <u>*Cashflow Finance Pty Ltd v Westpac Banking Corp*</u> *[1999] NSWSC 671 per Einstein J.*

(14) Where there is a transaction involving the potential for conflict between interest and duty, as here arose, the duty of care and diligence falls to be exercised in a context requiring special vigilance, calling for scrupulous concern on the part of those officers who become aware of that transaction to ensure that any necessary corporate approvals are obtained and safeguards put in place. While the primary responsibility will fall on the director or officer proposing to enter into the transaction, this does not excuse other directors or officers who become aware of the transaction.

(15) In order for the safe-harbour "statutory business judgment rule" to be relied upon, the director must first have made a business judgment. Then that business judgment must satisfy the following requirements, namely made in good faith for a proper purpose; after the director has informed himself as to the subject matter of the judgment to the extent he reasonably believes to be appropriate; in circumstances where the director does not have a material personal interest in the subject matter of the judgment and rationally believes that the judgment is in the best interests of the corporation: s180(2). The directors' belief that his or her judgment is in the best interests of the corporation is a rational one unless the belief is one that no reasonable person in that position would hold: s180(2)."

229. The Deputy Bailiff directed the Jurats that, whilst these principles gave a flavour of what the position is in Guernsey where there is no statutory framework for directors' duties, not all of them were applicable to Mr Addison. In particular, it was common ground that Mr Addison was not an executive director of the ICC or any of the Cells. The Jurats might wish to consider whether Mr Addison had been appointed as a director as a result of any special expertise and, in any event, the role he was there to play. He highlighted that Advocate Richardson had placed particular emphasis on principle (14) and invited them to weigh carefully how far Article 5 of the Articles of Association of the Cells went in permitting Mr Addison to delegate matters to, eg, the investment manager, Arch. They might also consider whether Mr Addison had, as the Plaintiffs contend, effectively abrogated any responsibility arising from his position as a director of the Cells for supervising what Arch was doing. Subject to the caveat already mentioned, he reminded them of para. 453 in <u>*Asic v Adler*</u> (*supra*), the conclusion of Santow J on the application of section 180 of the Corporations Act, to which Advocate Richardson had drawn attention (again slightly expanded here):

"*As to s180 and the duty of care and diligence, Mr Williams was not entitled to rely on Mr Adler to make investments, which conformed with the law and were not detrimental to the interests of HIH, without at least making sure there were put in place proper safeguards including independent appraisal of the investments made by way of proper due diligence and by ensuring that before the arrangements were put in place, the terms of the mandate were approved by the Investment Committee, if not the Board. Mr Williams simply did not do this either when making the original commercial deal or by instructing Mr Howard. It is nothing to the point to say that he hoped that the investment*

would turn out profitably or he would not have made it. The fact of the matter was that Mr Williams did not ensure that the company complied with its own safeguards laid down for approval of such a mandate by its Investment Committee, nor did he put in place safeguards to avoid investments being made which were in breach of the law and which, directly or indirectly, advantaged Mr Adler, Adler Corporation and PEE and were not reasonable in the circumstances even if HIHC and PEE had been dealing at arm's length. Mr Williams' concern should have been heightened by the fact that he was dealing with a fellow director. That is enough, though one can add that Mr Adler, as should have been apparent, had an obvious inherent conflict of interest as a significant shareholder in HIH. That is quite apart from his early intention to on-sell investments to AEUT like dstore; the evidence of the extent of Mr Williams' knowledge about such investment is set out at para 515 below. Accordingly, I conclude that Mr Williams was in breach of s180 of the Corporations Act in failing to exercise the degree of care and diligence that a reasonable person would have exercised as a director in the circumstances and occupying the office held by Mr Williams. Mr Williams is not able to invoke the business judgment rule in the circumstances where he either failed to make a business judgment at all or to the extent that he did, failed to establish that he made it in good faith for a proper purpose, and in any event, where he had a material personal interest in the subject matter of the judgment and had failed to inform himself to the extent he could reasonably believe to be appropriate."

230. Although the document post-dates the events on which the Jurats were called upon to focus, the Deputy Bailiff directed them that the *Code of Practice – Company Directors*, published with effect from 1 August 2009 by the GFSC, could be regarded as a level of guidance, although expressly not purporting to state the law, of what was expected within Guernsey at that time, and arguably for some time beforehand, of such officers. The principles of particular relevance are:

"*Directors should:*

1. *Understand and act in accordance with their legal duties and the constitution of the company and seek advice on those when necessary.*

2. *Ensure that the board of directors has effective control of the company.*

3. *Treat the company as a separate legal entity from its shareholders, directors and others and avoid conflicts of interest with it or deal with them in accordance with the company's articles of association. …*

5. *Know the company's business and finances and have full and up to date information on them. …*

12. *Not attempt to avoid those responsibilities by purporting to contract out of them or assigning them to others.*

Guidance Note:

Principle 12 is not intended to prevent directors from delegating to the extent permitted by the applicable law, nor from benefiting from indemnities in a company's articles of association. However, directors must appreciate that delegation to others does not absolve them from ultimate responsibility for the company's affairs."

231. On the basis that the Plaintiffs had concentrated on the alleged non-disclosure by Mr Addison of the particular conflict of interest that arose, the Deputy Bailiff invited the Jurats to consider that issue first on the basis that it would most likely follow from a finding of non-disclosure that there had been a breach of duty because Mr Addison had accepted that he understood that the payment of the fee amounted to a conflict of interest, meaning that it was incumbent upon him to manage that conflict and ensure that it was resolved fairly. Mr Addison had also accepted that Arch had been found by Walker J in the action against it brought by the Cells in England and Wales to have breached clause 13 of the various IMAs. The Jurats were directed that they could have regard to what had been pleaded on behalf of Messrs Meader and Radford in their Defences, but that the Jurats had not had the benefit of hearing what either of them would have said in evidence because neither had been a witness. Accordingly, the pleaded case was indicative of what they were likely to advance, but the weight to be afforded to that intended stance was very much a matter for the Jurats' assessment. Further, to the extent that they found there had been some disclosure, the Jurats were invited to consider what Mr Addison knew at the time of speaking to Mr Meader in August 2007 and, as a result of that knowledge, to decide whether what was said amounted to proper disclosure and satisfied the level of care, skill and diligence that would reasonably have been expected of him.

Disclosure by Mr Addison

232. The Jurats find that it is more likely than not that the conversation Mr Addison describes having had with Mr Meader between 10 and 17 August 2007, but not on 14 August 2007, did not take place at all. Having reached that conclusion, they are satisfied that Mr Addison breached one of the duties he accepts he owed to the Cells (para. 10(d) of the Amended Cause). They reached this conclusion for the following reasons.

233. The Jurats have noted that Mr Addison's account of what took place has not remained the same over the years that he has been required to recall what happened. There have been various inconsistencies and his version of events appears to them to have evolved with the telling. They carefully considered whether the differences in the accounts given by Mr Addison could have resulted from, as he put it himself, him concentrating harder, or focusing more, and managing to recall more details by the time he gave his evidence at this trial, but they are not persuaded that that is what has happened.

234. Unsurprisingly, Mr Addison does not question what the documents show, but he seldom even offers any explanation of them. His comment at para. 82 of his first witness statement that he was unaware at the time of the exchanges in early August 2007 involving his colleagues at Arch referring to the ability to extract cash from the Lonscale transaction is not believed by the Jurats. Mr Addison explained the way that the personnel at Arch worked in an open-plan area in a single room. His response to a question from the Court on the fifth morning of the trial included describing that room as:

> "*… like a large sort of trading floor, with banks of desks. The investment managers would all sit together with each other, back to back almost, so that if they wanted to meet or talk they could sort of swivel their chairs around. From memory, I didn't sit with them, I sat a little further away, because I'm dealing with company finance, including salaries of staff and certain things that do need to be kept confidential from the sort of general day-to-day business.*"

Although Mr Addison was not located in really close proximity to colleagues like Mr King, the Jurats find it was inevitable that a transaction involving such a significant benefit to Arch would have been referred to in Mr Addison's hearing and his professed ignorance of these matters until

later in the month is not believable. During the afternoon of the third day of the trial, Mr Addison had acknowledged that he had "*been kept informed in an informal manner all the way through, but not in any detail*", but the Jurats regard this as a prime example of him downplaying the extent of his knowledge and involvement of the Lonscale transaction.

235. In relation to his claimed disclosure of the fee, the version of events given by Mr Addison in his first witness statement begins with para. 62:

> "*I did not, therefore, initially know the size of the fee that would be paid to Arch FP. I did, however, assume in connection with market practice that it would be a sizeable fee based upon the value that could be saved on the purchase price of the Club Easy Group as a result of Arch FP's and Lee Barkman's work. Once it became apparent to me that this fee would be paid upon completion of a transaction in which the Cells were to participate, I immediately relayed the extent of my understanding of the issue to Neal Meader.*"

He continues (at para. 64.1):

> "*Whilst I cannot recall the precise date, I believe that Robin Farrell told me at some point between the 10 and 17 August 2007 that the Cells may invest in the Club Easy Group acquisition. When I found out that Arch FP's intention was that certain of the Cells would invest in a transaction in which Arch FP was due to receive a fee, I immediately called Mr Meader to obtain his in-principle agreement to the Lonscale Transaction and the payment to Arch FP. At that stage I did not know the amount of any fee payable to Arch FP in relation to the Lonscale Transaction. I understood after enquiries that this was also true at that time for Robin Farrell and Arch FP.*"

After referring to the practice that had developed between him and Messrs Meader and Radford of his reporting certain matters at board meetings but otherwise there being little discussion about investments, Mr Addison adds (at para. 64.4):

> "*I recall that Neal Meader was completely unfazed by the prospect of the Cells entering into a transaction that would generate a fee (of such a size that it was worthy of being discussed in this way) for Arch FP and seemed entirely comfortable, almost to the point of being disinterested, with the idea that the Cells' investment would result in a payment to Arch FP. Neal Meader confirmed to me that he had no objection to the investment proceeding due to the fact that Arch FP would receive the referenced fee. I recall that Mr Meader thanked me for flagging this with him and said words to the effect that fees of this type were 'paid all of the time' and that is [sic] was 'only right' that Arch FP was compensated for the work it had undertaken in relation to the deal.*"

236. Mr Addison further refers (in para. 65) to him having been told some years later by Mr Radford that Mr Radford had been aware of the fee payable to Arch arising from the Lonscale transaction:

> "*Neal Meader was at all times my principal contact in respect of matters relevant to the Lonscale Investing Cells. I was confident that he relayed matters that we discussed to his business partner, Peter Radford as one would normally expect within a business. The extent of Peter Radford's comfort with the Lonscale Transaction proceeding in circumstances where Arch FP was due to obtain a substantial fee was confirmed to me during a conversation that I had with him in August 2011. I clearly recall Peter Radford telling me that he had been aware of the fact that Arch FP stood to benefit from a significant fee in relation to the Lonscale Transaction and him giving me the firm*

impression that he had been entirely comfortable with it. Robin Farrell and I subsequently had a telephone conversation with Peter Radford on 15 August 2011 in which he further confirmed to Robin Farrell that he had known about the fee Arch FP was to derive from the Lonscale Transaction."

237. By way of further explanation, when he was cross-examined by Advocate Richardson on the morning of the fifth day of the trial, Mr Addison explained that the telephone conversation with Mr Meader could not have taken place on 14 August 2007 because that had been his brother's birthday and he had identified 10 August 2007 as being about the time when Mr Farrell had returned from holiday. (17 August 2007 appears to have been chosen because that is when the SPAs were executed.) He also explained that "*the words that Mr Meader said to me gave me enough comfort that he was perfectly happy for that sort of transaction to go through on that basis*" and later said the response from Mr Meader was "*"No, Robert, that's fine, this is the normal course of business", or words to that effect*". Mr Addison proceeded to explain that in the High Court "*other things came out, where I've said in my statement "no objection", and then I'm being criticised by Justice Walker for saying that I said it was fine. So bearing that in mind, this is my attempt to actually put those various things in my witness statement so that I wouldn't suffer the same criticism that I had for someone which I just see as just, you know, normal everyday wording.*" Mr Addison also accepted that para. 64.4 of his first witness statement was a new construct of events, but explained that it had been included because he was trying to assist this Court and "*not get criticised for these very things that have been pointed out to me now.*"

238. Turning to the file note dated 15 August 2011 [p. 6957] and para. 65 of his first witness statement, Mr Addison explained, referring here to Mr Radford, that "*this 15 August 2011 file note and conversation was just to confirm that he'd said that to us in the past*", although Mr Addison could not recall when Mr Radford had volunteered this information and whether it had been to Arch or to him and Mr Farrell. He agreed that the file note refers to two conversations, the more recent of which was in August 2011, during which Mr Radford had referred to an earlier conversation from which "*he knew about the Lonscale transaction and the fees*". In relation to Mr Addison's evidence about this document, the Jurats have formed the view that Mr Addison has no independent recollection of the conversations. He was reliant on reading the file note and then construing what had been recorded in it. Bearing in mind the significance for him of being believed that there had been disclosure to Mr Meader (and so to Mr Radford) of the fee payable to Arch associated with the Lonscale transaction, the Jurats find it extremely surprising that Mr Addison could not recall, without the assistance of the documents, the sequence of events surrounding his purported disclosure. They regard this as supporting their conclusion that Mr Addison has made up the telephone conversation he says he had with Mr Meader and that Mr Radford had subsequently confirmed that he was aware of these matters.

239. Previously, Mr Addison had not provided as much detail about the conversation with Mr Meader. Indeed, what he set out in para. 21 of his witness statement dated 8 March 2013 in the proceedings against Arch in England and Wales was quite brief:

> "*Because of the Cells' planned investment in a deal which involved a fee being paid to AFP, I telephoned Neal Meader and asked him whether the non-AFP ICC directors would object to the Cells' involvement in an investment in which it had already been agreed that AFP would be paid a fee. Neal Meader stated that he had no objection.*"

Arch's pleaded case had asserted in para. 129(2) that "*The payments made to Arch in respect of the transactions were disclosed and/or were consented to by the relevant Cells: (a) The payments were disclosed to the directors of the ICC and the relevant Cells*". Arch's response to a request for further information about para. 129(2)(a), in respect of which Mr Farrell had signed the

statement of truth on 20 July 2012, referred to the working practice of formal and informal discussions between Mr Farrell and Mr Addison and the Cell directors, Mr Radford and Mr Meader, before adding:

> "*The best particulars that Arch can provide at the present time is that disclosure was made in August 2007 in the course of a telephone conversation between Mr Addison and Mr Radford. At the time of the telephone conversation the precise size of the fee was not known however the structure and approximate figures were discussed.*"

(The Jurats note that Mr Addison seeks to explain away this reference to Mr Radford as a slip made by Mr Farrell, but do not regard that explanation as entirely satisfactory.) During the opening of Arch's case before Walker J, the disclosure made was dealt with by Mr Addison after lunch on the second day. He referred to disclosure "*of the potential fee to Mr Meader … of the arrangements that Arch had with Foundations Capital at the time, although they subsequently changed to Mr Barkman. … the size of the fee was not known at the time so an accurate figure could not be given, but he was told it would be substantial. … Mr Meader had no objections. He said it was fine and standard for a financial services firm such as Arch to be engaged in such matters. It is of regret that we haven't managed to document it at the time but his relaxed response gave us a lot of comfort and is probably the reason why we didn't.*"

240. In the judgment delivered by Walker J, these matters were addressed as follows:

> "*145. I have no doubt that when the main defence was being prepared, and the responses to the request for further information were being formulated, great care would have been taken in relation to what was said about disclosure and consent. First, if the cells had consented to the payment extracted by Arch FP, then this would go a long way towards providing a complete defence to the Lonscale Arch claim. It is clear that as at 20 July 2012 neither Mr Farrell nor Mr Addison had given instructions to Arch FP's lawyers that any director of the cells, whether Mr Meader or otherwise, had said in August 2007 that there was no objection to the payment envisaged to be received by Arch FP, let alone that it "was fine". I am sure that if instructions had been given that either of these things had occurred then they would have featured in the main defence or in the further information. By the stage that Mr Addison's witness statement was verified on 8 March 2013, Arch FP's lawyers had been instructed that in August 2007 Mr Meader had stated that he had no objection to the payment – but not that it "was fine". …*
>
> *147. It is difficult to understand how on this topic the instructions which Arch FP gave to its lawyers on 8 March 2013 when Mr Addison's witness statement was signed could have been so very different from the instructions given to those same lawyers in 2012. The changes are, to say the least, surprising. In addition to those surprising changes, at the stage of oral openings Mr Addison came up with the five additions listed above. It is astonishing that there could be such a dramatic change as would be involved if those additions were correct. When Mr Addison gave evidence he added for good measure that:*
>
> > *I said the fee would be a seven figure fee, but I didn't know any more than that.*
> > *…*
>
> *149. Nevertheless I cannot rule out the possibility that either or both of Mr Meader and Mr Radford were told informally prior to 17 August 2007 or prior to 29 October 2007 that some of the cells would be investing in the acquisition, and that Arch FP would*

be receiving a "fee". It is not suggested that they were told that the "fee" would come in large part from funds invested by the cells. I am sure they were not told this."

241. The Jurats recognise that Mr Addison has chosen to latch on to what Walker J stated in para. 149 as a means of underpinning why he still claims to have had the conversation with Mr Meader. However, this comment does not really assist him. Having considered all the evidence, the Jurats find that it is more likely the case that no disclosure was made. Such a finding leaves open the possibility that there was in fact some contact during this period, but on the civil standard of proof, they are persuaded that this did not happen. The law operates a binary system: either something is found to have taken place or, if there is no such finding, it did not. The findings made recognise that there is still a possibility that some contact took place, but the outcome is that there was none in the manner asserted by Mr Addison. Accordingly, the Jurats have independently formed their own views, which reflect the findings made by Walker J, that Mr Addison has made up the alleged conversation with Mr Meader. He has continued to seek to bolster his evidence by adding further detail. Mr Addison understood full well from the outset the importance of the disclosure issue and must have asked himself what he could remember about the conversation. Indeed, the Jurats appreciate that before this Court Mr Addison has admitted, when commenting on how Walker J had described the position he found, that "*All conflicts are serious and need to be addressed, I'm not impugning that, but not "as serious as could be imagined"*. The Jurats believe that this purported disclosure must have been an important live issue when Arch was instructing its lawyers in 2012 when these events would have been fresher in Mr Addison's memory and that the evolution of the version of events on which Walker J commented adversely has been continued by Mr Addison since and merits similar comment. The Jurats simply do not believe him when he says that the added detail since 2012 onwards is a consequence of him finding his recall improved the more he thinks about it. Instead, the Jurats find the developing versions as being surprising, astonishing and lacking credibility. In their view, the surrounding circumstances in July and August 2007, and from certain events later, support that conclusion rather than detract from it.

242. Mr Addison attended the meeting on 25 July 2007 with Mr Farrell and Mr Barkman at which the Club Easy Group project was first mentioned. The Jurats do not find Mr Addison's explanation that at that time Arch was to be involved only with the purchase negotiations and the structuring of the deal believable. The handwritten note of Mr Farrell indicates that the issues that must have been discussed by them to have led to such note-taking more likely than not included discussion of the amount that was available for them to extract from the transaction. The reference to "*£5M Upfront*" in relation to FHL, in which Arch UK had an interest, leads the Jurats to infer that the role to be undertaken by Arch-related entities was always envisaged to be greater than assisting with negotiations and structuring. They further infer that Mr Farrell's level of interest from the outset was in the Cells investing in the project and that Mr Addison was aware of this.

243. By early August 2007, others within Arch were engaged in considering the project. Mr King, in particular, referred to the element of "*what we can take out of it*", which the Jurats find must be a reference to Arch as well rather than solely to Mr Barkman's side of the transaction. Further, on 3 August 2007, Mr Farrell wanted AT1 funded with £8 million, so that it was "*physically in situ*", from which the Jurats infer that there was an intention that the Cells would be doing more than providing arm's length services relating to the transaction for which Arch would be paid. In cross-examination on the morning of the fourth day of the trial, Mr Addison agreed that on its face this showed that the Cells were going to invest in the transaction. Other exchanges at that time refer to Arch "*partnering*", and Mr Farrell made reference to Mr Barkman being authorised to negotiate up to a figure, which implies that Arch had already assumed a position in which it was exercising a high level of control over what was happening within the negotiations. Mr

Barkman also mentioned that it was "*no longer FHL deal*", from which the Jurats infer that, most likely from the outset, it was a real possibility that FHL, the joint venture between FCL and Arch UK, would be used as the entity involved in the Club Easy Group acquisition. This also resonates with the way Mr Blythe later wrote just before completion [p. 3494] that when the sale to Lonscale was first mooted, the Arch Group were the prospective purchasers.

244. The Jurats accept that the precise details of who would put what amount of money into the transaction was evolving quite quickly over the few weeks between the meeting on 25 July 2007 and the execution of the SPAs on 17 August 2007, but they do not accept that Mr Addison remained in ignorance of these matters as he first claimed was the case until some point between 10 and 17 August 2007, which is what precipitated the telephone call to Mr Meader that he says he made. Indeed, during that cross-examination, Mr Addison accepted that he knew from July 2007 that Arch was to be paid a fee and that by 3 August 2007 the amount of that fee had crystallised at £3 million (in cross-examination on the afternoon of the fourth day of the trial he said "*it looked like it would be 3 million, based on those assumptions at that first meeting with Mr Farrell, and nothing changed with those figures substantially to change that 3 million*"), but he maintained that he only knew about this "*a little later than that*" and reverted to what he had put in his first witness statement about it being no earlier than 10 August 2007. Whilst the Jurats accept that some of the e-mails at around this time do not show Mr Addison as one of the recipients, Mr Addison acknowledged that he had been one of those receiving Mr King's e-mail on 7 August 2007 [p. 2414] in which reference was made at "*at least £3m upside*" and a "*50/50 income split of this up-front bump-up with Foundations*". The combination of these factors leads the Jurats to find that Mr Addison was sufficiently well-informed of what was happening that he knew the basis on which a fee to Arch was to become payable and its amount by early August 2007 and certainly before the period beginning with 10 August 2007 to which Mr Addison has referred.

245. This conclusion becomes even clearer when the e-mail Mr Addison sent following his meeting with Barclays Wealth in the Isle of Man [p. 2420] is considered. The Jurats find that Mr Addison must have had sufficient information about the transaction and what role the Cells were likely to play to understand the significance of there being no appetite within Barclays Wealth to lend the amount of £9 million on which Mr Barkman had been relying. It was not this likely funding shortfall that led to the Cells becoming investors in the Club Easy Group acquisition, as Mr Addison has claimed, but rather than the shortfall would jeopardise the transaction unless the Cells took a larger stake in the transaction. It follows, therefore, that Mr Addison already knew enough about the details of the plan for the Club Easy Group acquisition to be able to relay straightaway that there might be a problem. Accordingly, the Jurats reject Mr Addison's explanation that he made contact with Mr Meader within the week-long timeframe he has advanced as a result of Mr Farrell telling him at that time that it was possible the Cells would be investing. There was clearly more than a possibility of that happening some days earlier and all that was changing was the amount that would have to be invested in order to secure the significant fee that had been identified as payable.

246. A further factor leading the Jurats to conclude that the alleged conversation with Mr Meader did not take place stems from the meeting Mr Addison and Mr Farrell had with Mr Symington of Methuen Consulting on 23 August 2007. The close proximity of this meeting to the time at which Mr Addison says that he telephoned Mr Meader and the issues discussed at it and recorded in the file note that Mr Addison signed [p. 2879], highlighting the importance of documenting reasons and establishing "*a clear paper trail*" strongly suggest that, within Arch and for Mr Addison, it was a topic that was at the forefront of minds at the time. If there had been a telephone conversation, possibly as recently as the preceding week, but in any event within the

fortnight prior to this meeting with Mr Symington, the Jurats think that Mr Addison would have realised the importance of recording it. Mr Addison's explanation that this was advice given to Arch and so not for him as a director of the ICC and the Cells is, in their view, a poor attempt by him to avoid the obvious implication flowing from there being no record of the alleged telephone conversation. If Mr Addison had recognised that contacting Mr Meader was required because there was a conflict of interest to manage, this timely reminder of the importance of documenting such events would inevitably have resulted in something being recorded.

247. The Jurats have also had regard to the way Mr Addison had informed Mr Meader about a potential conflict on 22 June 2007. In his e-mail [p. 2163], Mr Addison apologised for not having informed his fellow directors before the transaction relating to his pension took place. However, the fact that he addressed his mind to the conflict that had arisen and sent an e-mail, and then refers only to there being a telephone conversation with Mr Meader only some seven or eight weeks later leads the Jurats to the conclusion that the absence of anything capable of being printed, such as another e-mail, supports their view that this did not happen. Similarly, at a board meeting on 26 March 2008, Mr Addison sought prior approval to make an investment through his SIPP into one of the incorporated cells and he abstained from attending a meeting on 3 June 2009 to avoid any possible conflict of interest. These further examples of when Mr Addison recognised that a conflict existed and took steps to have his conflict recognised and recorded lend further support to the conclusion that he made no disclosure to Mr Meader or Mr Radford about the fees payable in respect of the Club Easy Group acquisition.

248. The final answer that Mr Addison gave in cross-examination (on the morning of the fifth day of the trial) was:

> "*I've already explained my regrets to the court for not having documented it and, if I'd gone back, I would have disclosed an awful lot more, but I think at the time, and now, that I carried out my duties as best I could.*"

Mr Addison's expressed regret at not having recorded anything has no bearing on the issue of whether he made any disclosure to Mr Meader because his explanation is not believed. Instead, the Jurats believe that the reason for there being no document, however brief, recording the conversation Mr Addison says he had is because no such conversation took place.

249. In the circumstances, the primary finding of the Jurats is that the Plaintiffs have satisfied them that Mr Addison made no disclosure to Mr Meader, or to Mr Radford, in August 2007 in a situation where there was an acknowledged conflict of interest arising. This means that Mr Addison has not complied with Article 35 of the Articles of Association of each Cell unless there has been a sufficient general disclosure notice. The Jurats do not find that the general disclosure that Mr Addison was a partner in Arch can satisfy this requirement in respect of a fee of £3 million payable to it upon completion of the Club Easy Group acquisition. There is a clear difference between Arch earning the fees to which it becomes entitled pursuant to the IMAs, which the Jurats regard as being the purpose of the general disclosure made, including in the various Scheme Particulars, and an exceptional fee being paid as is the case here. They do not think that the general disclosure point, as pleaded, was being strenuously advanced on behalf of Mr Addison but, to the extent that it was, they reject it. On the issue of disclosure of a conflict of interest, they find that the Plaintiffs have proved that element of their case.

Other breaches of duty

250. Although it is not strictly necessary for them to consider the position if they are wrong to conclude that there was no disclosure, the Jurats were invited by the Deputy Bailiff to proceed to

consider the adequacy of what Mr Addison claims to have said to Mr Meader and his overall conduct as a director of the Cells during the time that the Club Easy Group acquisition was underway. In doing so, the Jurats have formed the impression that Mr Addison probably did not recognise at the time he was appointed as a director of the ICC and subsequently of each Cell as it was incorporated that this meant that he had particular responsibilities attaching to those offices. To an extent, this is borne out from what Walker J found in respect of Arch's role as the investment manager. By extension from the approach that Arch has been found to have taken, Mr Addison more likely than not viewed his role as director as a link between Arch and Bordeaux, almost on an operational level rather than as requiring any oversight from him independent from his position at Arch.

251. Paragraph 60 of Mr Addison's first witness statement is an example of how he appears to have misunderstood his role. The conflicts alleged against him were not solely directed at him obtaining some personal benefit from the transaction. His suggestion that Arch might forgo receiving the fee that he acknowledges he knew had been negotiated to be paid to it is simply not borne out by any evidence showing that it was ever contemplated that Arch would not wish to extract what Mr Farrell and others clearly envisaged to be the "*meat on the bones*" available as a windfall payment to it. In any event, the way Mr Addison describes this issue in para. 79.3 of his first witness statement ("*The Lonscale Investing Cells would not have been in any better position if they had prevented Arch FP from receiving the Disputed Payments as the whole £6million would still have been payable to Lee Barkman*") equally demonstrates that the Cells were paying significantly more than strictly required because any of Arch's forgone fee would have been retained by Mr Barkman or someone on his behalf. Without proper consideration of the terms of the transaction, the tranche of the purchase price allocated to fee payments was not going to be something that the Cells required to be used to support the amount invested in purchasing the Club Easy Group, which it was apparent was needed from the outset. Mr Addison acknowledges as much at para. 72.4(i) of his first witness statement: "*the Lonscale Transaction would be a medium-term turnaround project that would require additional capital over time, but would be capable of giving substantial returns to investors.*" The Jurats find that Mr Addison did not approach the Club Easy Group acquisition from the perspective of his role as a director of the Cells making the investments they did.

252. Article 35 of the Articles of Association of each Cell requires a director to disclose to the other directors "*the nature and extent of any material interest of his*". Accordingly, the Jurats recognise that Mr Addison had an obligation, at its very lowest, to share with his fellow directors what he knew amounted to such a conflict of interest. As already mentioned, the Jurats find that Mr Addison knew by early August 2007 more about the Club Easy Group transaction and the amount that Arch would be paid than he says he mentioned to Mr Meader. He appears to have acknowledged this by some of the frankness in his final answer in cross-examination, to which reference has already been made. Further, as and when Mr Addison learnt more about the transaction, assuming for a moment that his state of knowledge improved over time, he had a continuing obligation to share that improved knowledge with his fellow directors in order to comply with Article 35. A single telephone conversation with Mr Meader in which none of the details about the fee payable was disclosed does not, in the Jurats' view, suffice.

253. Fees of £6 million in respect of an acquisition of the Club Easy Group for around £16½ million, as the price envisaged appeared to be at that time, represents over 36% of that acquisition price. Despite Mr Addison's attempt to describe this as a fee within a range that is usual in the commercial climate in which they were operating, the Jurats are not persuaded that what was being done here by Arch or by Mr Barkman and the Foundations vehicle can be viewed in any way as warranting such a disproportionately high return for them. Instead, they view this as

being exactly the type of extraction to which others, such as Mr Farrell, referred at this time. In other words, the amount of the fee, and how it would be taken, had nothing to do with the work that Mr Addison says Arch agreed to undertake in return for a fee, in the sense of being commensurate with what was required.

254. In any event, whether or not the fees payable to Arch and to the order of Mr Barkman fell within the range operating in the financial services sector in those times, Mr Addison acknowledges that Arch found itself in, and by extension his position as a partner in Arch led to, a situation where there was a serious conflict of interest that required managing. Given the Jurats' finding that Mr Addison knew more of the details than even the most expansive version of his conversation with Mr Meader actually covered, it follows that they also find that Mr Addison failed to disclose the extent of that material interest. In order to satisfy his obligation to disclose, Mr Addison needed to relay as much detail as he knew in order to enable Messrs Meader and Radford to consider whether the conflict that arose could be resolved fairly. Even if the amount of the fee payable were unknown down to the last pound, it was incumbent on Mr Addison to provide information of the approximate quantum of the fee. In that respect, commenting that "*it would be a seven figure fee*" is not as helpful as stating that the fee would be in the region of £3 million. Further, explaining that the fee was half of the total fees payable in relation to the acquisition, and that out of the other half Arch would be receiving a further benefit arising from the agreement given by Mr Barkman to redeem the preference shares in FHL, which is an aspect of the transaction in respect of which the Jurats find that Mr Addison was heavily involved, is the level of disclosure that Mr Addison should have been undertaking as and when he came to that knowledge. (The Jurats have noted the speed at which Mr Addison sought to effect the redemption of those preference shares once completion of the Club Easy Group had occurred, from which they draw the inference that he was well-informed about this aspect of the overall transaction, yet never mentioned it to his fellow directors despite the additional benefit that would accrue to Arch UK as a result.) By 10 August 2007, the Jurats find that Mr Addison had sufficient knowledge of this level of detail that even if they take Mr Addison's case at its highest, the disclosure he says he made at some point in the week that followed is viewed by them as inadequate.

255. In part, this aspect of the case shades into Mr Addison's performance of his other duties, such as his duty of care, skill and diligence, and the extent to which his performance of his functions as a director were capable of delegation. The Jurats recognise that the terms of the IMAs are such that each Cell had provided wide powers to Arch as investment manager. That is consistent with the wide terms of Article 5 of each Cell's Articles of Association. Clause 4(a) of each IMA afforded Arch "*complete discretion for the Company's account (and without prior reference to the Company) to buy, sell, retain, exchange or otherwise deal in investments and other assets*". However, having regard to the Deputy Bailiff's directions in respect of the ongoing need for oversight by the directors of a company, the Jurats do not regard "*complete discretion*" as amounting to a licence for a director of any of the Cells to abrogate entirely the responsibilities attaching to that office. In their view, the authority to take decisions is capable of being delegated but the responsibility to undertake adequate supervision cannot be avoided through such delegation. In any event, the IMAs themselves contain provisions that support this view, because clause 6, as an example, enabled the Cell to give instructions to Arch. In order to be in a position to consider whether it is appropriate to give any instruction of this nature, it follows that the directing minds of the Cell must have sufficient knowledge about what is happening. If the director with that knowledge does not share it with his fellow directors, this means that there has not been the exercise of the level of care, skill and diligence with regard to the affairs and management of the company concerned expected of that director. The Jurats are satisfied that Mr Addison fell short of what he was required to do in respect of the Club Easy Group acquisition by the Cells during August to October 2007.

256. The Jurats also regard it as a telling factor that, despite the size of the fees that were agreed to be paid, nothing appears to have been documented about the terms for payment of the fee or even who would be responsible for paying those fees. This goes further than the need to record how a conflict of interest was being managed, especially following the advice from Mr Symington, and relates more to the desirability of a proper arm's length commercial transaction being in written form. In the event, it became Lonscale that would pay the fee, as agreed by the board of directors, comprising Mr Farrell and Mr Barkman, who the Jurats note were both effectively the principal recipients of the benefit of those fees, as recorded in the minute on 16 August 2007, shortly after Lonscale had been incorporated and the day prior to the execution of the SPAs. At that time, they were described as "*an introduction commission … and appropriate structuring / arrangement fees to be invoiced in due course*". Subsequently, the invoice rendered to Lonscale referred to "*intermediary services*". The Jurats find that there is an inference they can draw from the fact that the fee element of the transaction was not being dealt with as openly and transparently as it could have been, that leads them to conclude that those involved were not keen to face any external scrutiny of this aspect. They prefer that conclusion over Mr Addison's suggestion, made on the morning of the fifth day of the trial, that if he had been engaging in any subterfuge in relation to the fees, rather than recording nothing, he, and one assumes, others, would have set about creating some form of paper trail that would sustain any level of scrutiny. The Jurats take the view that any paper trail so created would have led to questioning that would have shown there was no rationale for the fees being extracted from the Club Easy Group transaction. They have had regard to the reasons given when the Notes were issued by AT1 and Lonscale in relation to funding the transaction. The AT1 Notes refer to "*The net proceeds of the issue of the Notes will be used for the general corporate purposes of the Issuer*" and the Lonscale Notes refer to "*The net proceeds for the issue of the Notes will be used for the acquisition of property assets.*" If the reference to net proceeds deals with the proceeds after payment of the fees, this may be an accurate description, but other documentation relating to those fee payments, had such documentation existed at the time, may well have led to an unwelcome level of scrutiny as far as Arch was concerned.

257. To the extent that Advocate Williams sought to draw parallels between the way the Cells operated when Arch was the investment manager and Mr Addison a director and when Spearpoint became the investment manager and Mr Scott and others were directors placing reliance on how Spearpoint managed the investments, the Jurats do not find themselves comparing like with like. Their impression is that Mr Davey provided a considerable amount of detail to the directors of the ICC and the Cells, whereas the periodic updates given by Mr Addison to Messrs Meader and Radford were less comprehensive. Again, to the extent that there is any suggestion that Mr Davey seeking clearance to make personal loans to Lonscale reflects the way that Mr Addison set about disclosing to Messrs Meader and Radford his own and Arch's conflicts of interest, the Jurats reject this. The pattern was very much Mr Davey explaining why he could not put together a case for any of the Cells to make the loans required to keep Lonscale afloat. His actions in risking his own money were potentially for the benefit of the Cells because each time it staved off what became the eventual collapse of Lonscale, meaning that the possibility of more of the deferred consideration under the Disposal Agreement becoming payable made it attractive to the directors of the ICC and the Cells. Indeed, the Jurats take the view that the way Mr Davey sought to have the conflicts of interest managed puts Mr Addison's own effort in relation to the fees associated with the Club Easy Group acquisition in a very negative light.

258. It is apparent to the Jurats that Mr Addison was a key figure within Arch. They accept that Mr Farrell played an even more significant role, and had by far the largest beneficial interest in what Arch did, but as Arch's Chief Operations Officer, Chief Financial Officer and its compliance officer, and as a person who clearly had the confidence of Mr Farrell, the Jurats find that Mr

Addison's assertions that he knew less about the Lonscale transaction than the Plaintiffs suggest he did are founded more on the absence of a clear paper trail demonstrating that he was a copy recipient or participation in the e-mail traffic at this time than on the reality of what was taking place. In addition to the level of involvement already referred to before the week prior to the execution of the SPAs on 17 August 2007, Mr Addison accepted that he had reviewed each of the due diligence reports as they arrived. The Jurats have formed the impression that Mr Addison did not appreciate at the time that he should have been doing this as a director of the Cells as well as being interested in his capacity as a partner of Arch. It seems that Mr Addison has not questioned any of what was set out in those reports. The Jurats note that Mr Addison refers more than once in his evidence to him being aware that Mr Farrell had expressed an interest in the Cells becoming involved in the Lonscale transaction from the outset. There is, however, no suggestion that he ever enquired why this was so. Although he refers to there being "*significant potential for favourable returns for any relevant Cells*", as the link person between Arch and the ICC and the Cells, Mr Addison was best placed to make appropriate enquiries in his capacity as a director as to how the transaction would benefit the Cells concerned. The absence of such enquiries, when Mr Addison was aware that a very substantial amount of the investments to be made from the Cells would be used to pay the £6 million of fees, is a factor demonstrating that he was not complying with his duties as a director.

259. Whilst it is permissible for a director to place reliance on those the company engages to advise it, without considering the material from the perspective of the Cells and his position as a director of them, Mr Addison was failing to comply with the level of oversight that the Jurats find he should have been exercising. For example, rather than letting pass the valuation undertaken by Storeys of the property portfolio, and letting others query this, such as Mr Jeffs, Mr Addison had a responsibility to be more questioning than he was. The view that Mr Jeffs took was quite an extreme one, in that his valuation figure was some £13 million lower than the Storeys' valuation. The Jurats consider that the consequence of this is that Mr Addison should have realised the difficulties presented by the fees to be taken on completion from the funding being provided by the Cells. They regard this as being a further factor affecting the extent and nature of the conflict of interest that needed to be disclosed by him. Given the references in the Scheme Particulars to resolving conflicts in the "*best interests of investors*", the possibility of the valuation on which reliance had been placed being questionable should have led to some further investigation of the rationale of the fees element of the transaction. Indeed, the fact that Mr Jeffs was querying the valuation approach is precisely the type of information that Mr Addison should have been acting on as a director of the Cells, rather than regarding it as something only of relevance to the investment management team at Arch. It is an aspect of the ongoing obligation Mr Addison had of monitoring the business of the Cells and exercising an appropriate element of oversight (duty (g)). The Jurats find that Mr Addison's background in finance and structuring should have meant that he did not accept at face value an analysis of a loss-making business looking only at its net assets.

260. Mr Addison sought to explain the position as being that Arch itself was undertaking due diligence. On the fourth morning of the trial, one of his answers was that "*The key thing is that Arch undertook due diligence on the company itself and all the issues there to make sure we knew what we were buying*". Once again, the focus is on Arch rather than anything further expected by the directors of the Cells themselves. The Jurats are also conscious of the fact that the SPAs were executed before the due diligence had all been received and considered. It is clear that Mr Addison paid attention to the report from PKF, and the Jurats note that he was the person at Arch who signed the letter of engagement on 16 August 2007 [p. 2445]. The scope of what PKF were required to do was expressed to be "*limited*", as more particularly set out in Appendix 2 to that letter [p. 2519]. The letter stated that PKF's "*work and findings shall not in any way constitute*

recommendations regarding the completion of the proposed transaction". It was primarily an analysis of the financial information made available. They have also noted the speed at which Mr Addison reverted on receipt of the report from Cobbetts, which again suggests that he was prioritising his review of the documents relating to the acquisition of the Club Easy Group as and when they arrived. From all of these circumstances, including the approach to the due diligence being provided, Mr Addison was not adequately supervising what was involved in the Club Easy Group acquisition from his position as a director of the Cells and, even taking his case at its highest, he was failing to share with his fellow directors sufficient information that had come to his attention to enable them to form any view on the transaction either. Consequently, the Jurats find that he fell below the standard required of a director of each of the Cells involved.

261. During the period between execution of the SPAs and completion, Mr Addison, as a director of the Cells, was best placed to question the underlying basis for the acquisition of the Club Easy Group. He knew from the outset that fees were due to be taken in respect of the transaction. He knew early on that they had crystallised at £3 million for Arch and £3 million to the order of Mr Barkman. He knew that Arch would also gain some further indirect benefit as a result of redeeming the preference shares in FHL. The Jurats find that Mr Addison was sufficiently alive to some of his colleagues questioning the value of the Club Easy Group that the soundness of the acquisition should have become an issue for him or, if not for him, for his fellow directors of the Cells. Mr Addison became aware during this time that the extent of investment by the Cells increased because of the inability of Mr Barkman to fulfil his promises to obtain some of the funding required. He knew that there was a condition in the SPAs relating to the July 31 Net Asset Value (clause 3.1.7), which was not satisfied. There was, therefore, an opportunity between executing the SPAs and completion for Lonscale to choose not to purchase the Club Easy Group, probably as a result of the Cells declining to make the envisaged investments in Lonscale. Given the amount to be invested by the Cells and the significant portion of that investment to be taken as the fees previously identified as payable to Arch and to the order of Mr Barkman, the Jurats find it surprising that Mr Addison appears never to have drawn to Messrs Meader and Radford the position as it was evolving. Whether or not there was any disclosure in August 2007, the Jurats consider that someone in Mr Addison's position had the responsibility to do more than he did during this period to facilitate consideration of the transaction by the directors of the Cells themselves. The level of fees already committed to Arch and especially to Mr Barkman, given that the latter's participation in the process shifted so much making it questionable as to the rationale for paying him anything like £3 million, could have been re-visited but it appears to the Jurats that this was not done because Arch was on a path towards obtaining a huge fee and the transaction had to complete before it became payable. It looks now as though the motivation was not the benefit that might flow to the Cells but rather than size of the benefit payable to Arch and to Mr Barkman. The Jurats find that this was not in the best interests of the Cells (duty (a)) and that Mr Addison failed to exercise the care, skill and diligence that he should have done (duty (e)).

262. At para. 75 of his first witness statement, Mr Addison offers the following explanation:

> "*I understand that Neal Meader and Peter Radford were appointed as directors of the Company and Cells on the basis of their experience in acting as directors of Guernsey companies. At no stage do I consider that it was envisaged by any relevant party that they were required to perform an in-depth role in assessing the quality of the investments made by the Cells or the terms on which such investments were being acquired. The terms of the IMAs, the UK IMAs and the nature of Arch FP's relevant expertise all firmly indicate to me that such roles were clearly ones for Arch FP to perform. In those circumstances, I do not consider that Neal Meader or Peter Radford would have been in*

a position to, even if (which I do not accept) they had ever considered it necessary, to second guess or undertake any meaningful analysis of an investment opportunity. Arch FP was the designated professional advisor afforded with an extremely wide discretion in relation to the selection and management of investments and it was at all times considered that the Directors would defer to Arch FP on such matters and could rely upon it to properly fulfil its duties to the Lonscale Investing Cells."

The Jurats find it surprising that this explanation has been advanced even after Walker J had concluded that Arch had failed to comply with its duties under the IMAs. Having regard to the directions given to them, particularly the comprehensive principles set out in *Asic v Adler* (*supra*), they consider that, even allowing for a degree of reliance on and, as Mr Addison puts it, deference to Arch, the directors of the Cells, including Mr Addison, could not close their eyes to what was being done under that delegated authority. None of the directors of the Cells might have been in a position to descend into the minutiae of investments being made, but each would, the Jurats believe, have been able to supervise Arch at the high level that would have been involved if some consideration had been given to the basis on which Arch and others would be paid such a large fee associated with the making of an investment. The Jurats regard this as part of the inability of Mr Addison to understand in 2007 the role he was required to undertake as a director.

263. Mr Addison's other response to these issues has been to draw attention to the level of control that the OEICs had through their majority shareholdings in some of the Cells in the latter part of 2007. Mr Addison advances the case that this meant that if he had taken any steps to question the transaction, he would have been removed as a director of the ICC (and so of the Cells) by the OEICs and/or Arch. Although they note that Mr Radford alluded to this possibility at the board meeting held on 18 March 2009 [p. 803], the Jurats are not persuaded that this argument has any merit. In particular, they do not think that this affects the standard of care that Mr Addison as a director was required to meet. The competent director would do what was required of him or her even if it might lead to the shareholders exercising the power of removal. In the Jurats' minds, it is no answer to an allegation of not fulfilling the responsibilities of a director to argue that to have done so would have led to the director's removal.

264. Although the Jurats have first found that Mr Addison is in breach of his duty to disclose the conflict of interest that arose, looking at Mr Addison's performance as a director in the round, there are further examples of him breaching his duty to exercise the care, skill and diligence required of him, his duty to act bona fide in the best interests of each Cell and his duty to understand, monitor and oversee the management and business activities of each Cell. Accordingly, the Jurats find that those duties have been breached and turn next to consider the issue of causation.

Loss and causation

265. The quantum of the losses that are claimed by the Plaintiffs is not disputed by the Defendant. The calculations of those losses were agreed by the expert witnesses. Instead, Mr Addison's case has focused more on the issue of causation. There is, though, an argument that he advances that relates to the lower amount of loss claimed by the Plaintiffs in the alternative, comprising only the amount of the fees paid (ie, £6 million), being the extent of what they can recover if the only finding of breach relates to non-disclosure. Because the Jurats find that there were more breaches of duty by Mr Addison than solely relating to whether or not he disclosed to Mr Meader, as he claimed, this argument disappears. Accordingly, the starting point for the amount of loss caused by Mr Addison's breaches of duty is the full amount claimed by the Plaintiffs.

Directions

266. The directions of the Deputy Bailiff in respect of the issue of causation in this case start with the way the issue was put by Briggs J (as he then was) in *Lexi Holdings plc (in administration) v Luqman* [2008] EWHC 1639 (Ch) (at para. 28):

> "*The question whether a breach of duty constituted by total inactivity causes a particular loss raises issues of law, fact and hypothesis. The law serves to define the relevant duty, and the steps which that duty required these Defendants to take is ascertained by the application of those legal principles to the relevant background including, importantly, the particular knowledge, experience and skill which each of Monuza and Zaurian actually had. Thereafter, the court must construct a necessarily hypothetical edifice so as to ascertain what would probably have happened if the relevant duties had been performed, so as to ascertain whether in that event the losses actually suffered by Lexi would, probably, not have been suffered.*"

The "*hypothetical edifice*" approach has been endorsed in *Weavering Capital (UK) Ltd (in liquidation) v Dabhia* [2013] EWCA Civ 71, and, on the basis that he was satisfied that this approach is equally applicable in Guernsey law, the Deputy Bailiff invited the Jurats to consider what would have happened had Mr Addison complied with the duties they found he had breached.

267. In respect of the various bases on which Mr Addison has argued that the causative link has not been satisfied by the Plaintiffs, one was that the loss claimed by the Plaintiffs was not within the scope of duty owed by Mr Addison. The authority relied upon by Advocate Williams for this proposition is *Kuwait Airways Corporation v Iraqi Airways Co. (Nos 4 and 5)* [2002] 2 AC 883 and para. 71 of the speech of Lord Nicolls of Birkenhead. In directing the Jurats, the Deputy Bailiff found it helpful to start with para. 69:

> "*How, then, does one identify a plaintiff's "true loss" in cases of tort? This question has generated a vast amount of legal literature. I take as my starting point the commonly accepted approach that the extent of a defendant's liability for the plaintiff's loss calls for a twofold inquiry: whether the wrongful conduct causally contributed to the loss and, if it did, what is the extent of the loss for which the defendant ought to be held liable. The first of these inquiries, widely undertaken as a simple "but for" test, is predominantly a factual inquiry. The application of this test in cases of conversion is the matter now under consideration. I shall return to this in a moment.*"

In doing so, the Deputy Bailiff emphasised to the Jurats that if there were some reason other than Mr Addison's breach of duty that caused the losses the Plaintiffs have sustained, then it would mean that the Court would dismiss the Plaintiffs' action, which is also how Lord Nicholls explained the situation in para. 72, which will be reached shortly.

268. At para. 70 of this speech, the second element is dealt with:

> "*The second inquiry, although this is not always openly acknowledged by the courts, involves a value judgment ("ought to be held liable"). Written large, the second inquiry concerns the extent of the loss for which the defendant ought fairly or reasonably or justly to be held liable (the epithets are interchangeable). To adapt the language of Jane Stapleton in her article "Unpacking Causation" in Relating to Responsibility, ed Cane and Gardner (2001), p 168, the inquiry is whether the plaintiff's harm or loss should be within the scope of the defendant's liability, given the reasons why the law has recognised the cause of action in question. The law has to set a limit to the causally connected losses for which a defendant is to be held responsible. In the ordinary*

language of lawyers, losses outside the limit may bear one of several labels. They may be described as too remote because the wrongful conduct was not a substantial or proximate cause, or because the loss was the product of an intervening cause. The defendant's responsibility may be excluded because the plaintiff failed to mitigate his loss. Familiar principles, such as foreseeability, assist in promoting some consistency of general approach. These are guidelines, some more helpful than others, but they are never more than this."

His Lordship continued, in the paragraph to which Advocate Williams refers:

"*In most cases, how far the responsibility of the defendant ought fairly to extend evokes an immediate intuitive response. This is informed common sense by another name. Usually, there is no difficulty in selecting, from the sequence of events leading to the plaintiff's loss, the happening which should be regarded as the cause of the loss for the purpose of allocating responsibility. In other cases, when the outcome of the second inquiry is not obvious, it is of crucial importance to identify the purpose of the relevant cause of action and the nature and scope of the defendant's obligation in the particular circumstances. What was the ambit of the defendant's duty? In respect of what risks or damage does the law seek to afford protection by means of the particular tort? Recent decisions of this House have highlighted the point. When evaluating the extent of the losses for which a negligent valuer should be responsible the scope of the valuer's duty must first be identified: see Banque Bruxelles Lambert SA v Eagle Star Insurance Co Ltd [1997] AC 191. In Reeves v Comr of Police of the Metropolis [2000] 1 AC 360 the free, deliberate and informed act of a human being, there committing suicide, did not negative responsibility to his dependants when the defendant's duty was to guard against that very act.*"

Consequently, the Deputy Bailiff distinguished between the largely factual determination that the Jurats needed to make in respect of the first, "*but for*" element of the test and the evaluative determination required about whether the losses claimed could be regarded as being within the ambit of the duty Mr Addison owed to the Cells as a director.

269. Lord Nicholls further explained (at para. 72):

"*The need to have in mind the purpose of the relevant cause of action is not confined to the second, evaluative stage of the twofold inquiry. It may also arise at the earlier stage of the "but for" test, to which I now return. This guideline principle is concerned to identify and exclude losses lacking a causal connection with the wrongful conduct. Expressed in its simplest form, the principle poses the question whether the plaintiff would have suffered the loss without ("but for") the defendant's wrongdoing. If he would not, the wrongful conduct was a cause of the loss. If the loss would have arisen even without the defendant's wrongdoing, normally it does not give rise to legal liability. In Barnett v Chelsea and Kensington Hospital Management Committee [1969] 1 QB 428 the night watchman's death did not pass this test. He would have died from arsenic poisoning even if the hospital casualty department had treated him properly. Of course, even if the plaintiff's loss passes this exclusionary threshold test, it by no means follows that the defendant should be legally responsible for the loss.*"

The Deputy Bailiff felt that it was of assistance to the Jurats to give them directions based on this broad analysis of the principles relating to causation, adopting them as appropriate guidance in a case such as the present. It was a means by which to place into context the submissions of Advocate Williams that the losses flow from Arch's decision to invest in the acquisition of the

Club Easy Group rather than anything done by Mr Addison, where Arch has already been found to be liable for the losses that are also the subject of the present claim by the Cells.

270. Another way the position of Mr Addison has been put is that the Cells would have been in the same position if he had made the disclosure required to Messrs Meader and Radford. In this regard, Advocate Williams has referred to how Mummery LJ dealt with the position in an equitable compensation case (*Gwembe Valley Development Co Ltd (in receivership) v Koshy (No 3)* [2003] EWCA Civ 1048, at para. 147):

> "*... the court is not precluded by authority or by principle from considering what would have happened if the material facts had been disclosed. If the commission of the wrong has not caused loss to the company, why should the company be entitled to elect to recover compensation, as distinct from rescinding the transaction and stripping the director of the unauthorised profits made by him? There is no sufficient causal link between the non-disclosure of an interest by Mr Koshy and the loss suffered by GVDC, if it is probable that, even if he had made the required disclosure of his interest in the transaction, GVDC would nevertheless have entered into it. In our judgment, a director is not legally responsible for loss, which the company probably would have suffered, even if the director had complied with the fiduciary-dealing rules on disclosure of interests.*"

The Deputy Bailiff suggested to the Jurats that they could properly regard this as a particular example of the "*hypothetical edifice*" they should construct on the premise that Mr Addison had complied with his duty of disclosure and also his other duties as a director of the Cells. If the Cells would probably have suffered the losses they did suffer because the decision-making of the Cells would have been the same in any event, the Plaintiffs would not have established the sufficient causal link required to prove their case.

Discussion

271. The Jurats take the view that the key consideration for them is whether the Cells would have proceeded with their investments in Lonscale, and so facilitated the acquisition of the Club Easy Group pursuant to the modified SPAs, at all if the Defendant had fulfilled his duties to the Cells as their director. From their review of all the documents, it is clear that there was no proper consideration of this transaction by the directors of the Cells. The only way there could have been proper consideration was if Mr Addison had shared his knowledge about what the transaction entailed and, in particular, that a significant portion of the monies being invested would be paid to Arch and to the order of Mr Barkman as the £6 million of fees that had been agreed between them. Had there been the level of disclosure required, enabling a proper consideration of the pros and cons of the transaction, the Jurats are satisfied that the transaction itself would not have completed. Consequently, the Plaintiffs have proved to the satisfaction of the Jurats that Mr Addison's breaches of duty amount to a cause of the entirety of the losses sustained by the Plaintiffs. They reach that conclusion for the following reasons.

272. The Jurats note the description of the transaction offered by Mr Davey as being that Mr Hayes "*sold them a pup*". They also find persuasive the evidence of Mr Moore about the need for there to have been in place a proper business plan for the acquisition to be capable of being regarded as a turnaround project worth investing in. Whilst the absence of a proper business plan might have been countenanced by Arch, they consider it probable that it would not have been found acceptable had Messrs Meader and Radford been made aware of the situation. In their opinion, the benefits of the Club Easy Group acquisition would have started to unravel very quickly had Mr Addison deigned to explain to Mr Meader (or to Mr Radford) the basis for paying away £6 million of the Cells' invested monies and thereafter there being an informed discussion of what

was accepted by Mr Addison to be a serious conflict of interest that required managing. Indeed, the Jurats believe that it is likely that one of the reasons why there was no disclosure was that those within Arch, including Mr Addison, realised full well what the consequences would be and that the opportunity for Arch to receive such a large fee would soon disappear.

273. The Jurats have already commented on the scope of what Mr Addison was required to do as a director. It was not only to make the disclosure of the nature and extent of any material interest, but also to act as a competent director would for the benefit of each Cell's business. As part of the management of that conflict of interest, it was incumbent on Mr Addison to relay sufficient information to enable it to be resolved fairly. Part of that fair resolution process may have resulted in the recognition that the fee was being funded, at least in large part, from monies coming from the Cells and so may have led to there being no acceptable solution to manage the conflict that would have been regarded as satisfactory by Arch. If so, the transaction would not have completed. The Jurats have considered whether it was likely that the transaction would have still completed, but on different terms, and have concluded that the appetite of Mr Farrell and Mr Barkman, being the two persons whose decisions would have had the greatest influence, to complete would have disappeared if the fees to be taken were no longer available. The Jurats reject Mr Addison's contention that all they need to look at is whose decision it was to complete on the transaction because that approach overlooks the role that Mr Addison as a director had to exercise appropriate oversight of the business of each Cell. In their view, there is a distinction between Mr Addison's role not being to participate directly in investment decisions taken by Arch under the delegation afforded by the terms of the IMAs and supervising matters, including, in particular, anything out of the ordinary. Again, there is a difference between Arch earning the fees payable under those IMAs and Mr Addison realising that something exceptional is occurring, as was the case with the agreement to take fees out of the monies being invested by the Cells. The Jurats find that it was within the scope of Mr Addison's responsibilities as a director for him to supervise what was taking place and that the risk of the business of the Cells being conducted without the conflict of interest that arose being properly managed is the type of risk that the duties he has broken are intended to protect against.

274. The Jurats further reject Mr Addison's contention that the investment by the Cells and the payment of the fees would have happened regardless of Mr Addison's breaches of duty. (This was pleaded as a late addition to para. 158(3)(v) of Les Amended Defenses and Counterclaim.) Although it was theoretically possible for the directors of the ICC (and so the Cells) to have been removed by the shareholders, using Article 25 of the Articles of Association, the Jurats consider that the reality of the situation would have been otherwise. The possibility of removal would have resulted from some step being taken by the directors of the Cells, perhaps the issuing an instruction pursuant to clause 6 of the IMAs, thereby frustrating Arch's desire to obtain the fee associated with completing the Club Easy Group acquisition. In those circumstances, it seems fanciful to the Jurats that anyone would have been prepared to become a director of the ICC and so the Cells with a view to being compelled to accede to the transaction, which could have entailed having to revoke the instruction previously given. In respect of the position of the OEICs, and their holdings in the Cells, the Jurats find the suggestion from Mr Addison that they would have used their voting powers against the position adopted by the directors as equally fanciful and find that Advocate Richardson is correct to point out that this overlooks the position of Capita as the ACD. In the absence of any evidence that such a course of action was likely to be adopted by Capita, the submission that the directors could have been removed if they had been difficult about the transaction completing lacks substance. The fact that Mr Radford had previously alluded to the possibility does not make the likelihood any greater. It strikes the Jurats that this possibility is premised on a theoretical exercise of powers found in the constitutional documents where they are not persuaded that it would have happened in the manner Mr Addison

advances. It appears more likely that the taking of such a drastic step as removing the directors would have led to even greater scrutiny of the affairs of the ICC and the Cells at that time, rather than it only arising a little later. It is pure speculation on the part of Mr Addison that the transaction would still have taken place, with the consequence that the losses found to have been sustained would have been suffered in any event, and the Jurats are unpersuaded that this is a sound basis on which to find that the Plaintiffs have not proved causation. Accordingly, they do not accept that the same outcome for the Cells would have occurred had the duties of Mr Addison been complied with.

275. The Jurats are not persuaded that they can draw the inference that Mr Addison invites that Messrs Meader and Radford would have been content with the Club Easy Group acquisition had Mr Addison complied with his duties as a director and disclosed to them what he should have disclosed. (This was also pleaded as a late addition to para. 158(3)(v) of Les Amended Defenses and Counterclaim.) The Jurats recognise that they have not had the benefit of evidence from either Mr Meader or Mr Radford. What is put in their pleaded case has not been tested. The way it is put in para. 211 of Les Defences does amount to a denial that if they had been aware of the payment of the fees "*the effect of such knowledge would have been that the investment in Lonscale did not take place or was unwound*" (sub-para. (c)), but this is then elaborated upon as follows:

> "*(i) Mr Radford and/or Mr Meader would have required Arch to explain fully the basis for the alleged Lonscale Dispute [sic] Payments and Mr Radford and/or Mr Meader would have considered whether receipt by Arch of the the [sic] Lonscale Disputed Payments was commercially justified and whether the conflict of interest was fairly resolved.*
>
> *(ii) Mr Radford and Mr Meader are unable to say what explanation would have been provided by Arch, other than that it is to be inferred that Arch would have relied (at least) on the matters pleaded at paragraphs 108 to 132 of the Arch Defence and that they would then have sought further explanations and/or supporting evidence as to the basis on which Arch maintained that the conflict has been fairly resolved. Pending disclosure, Mr Radford and Mr Meader make no admissions as to what conclusion would have been reached.*
>
> *(iii) Depending on the content of the explanation provided by Arch, Mr Radford and/or Mr Meader would either, if satisfied, have permitted Arch to keep the commission or, if of the view that Arch had failed to resolve the conflict fairly, would have sought redress from Arch on the basis that (not by virtue of receiving a fee, which it was permitted to so, but by virtue of doing so in circumstances where a conflict had not been fairly resolved) Arch was in breach of its duty under the IMA.*
>
> *(iv) It is evident from the terms of the Arch Defence that Arch would not have agreed to repay the Disputed Lonscale Payments voluntarily. Had Mr Radford and Mr Meader caused the Cells to bring proceedings against Arch to recover the payments, the outcome would have been no different, in terms of recovery and costs, than can be expected from the claims the Cells have in fact brought against Arch. Nothing has been lost by virtue of the fact such claims were not made sooner.*"

The Jurats take the view that the position of Messrs Meader and Radford set out in this sub-paragraph, represents the position they needed to take before the proceedings before Walker J concluded, as well as before seeing disclosure in these proceedings. As such, it is an

understandable position for them to take at a time they were also defending the Plaintiff's action. In the light of the documents that have been adduced before the Court and the judgment of Walker J, the Jurats believe that the position of Messrs Meader and Radford would more likely than not have shifted away from there being a possibility that they would "*have permitted Arch to keep the commission*". Indeed, the Jurats take the view that Messrs Meader and Radford could well have indicated, as the Jurats find, that the conflict that fell to be disclosed would have been incapable of being resolved fairly and to the satisfaction of all parties. The Jurats will never know, though, because no party has called Mr Meader or Mr Radford as a witness. In respect of Mr Addison's contention that the act of paying away £20.2 million of the Cells' funds to AT1 shows that Messrs Meader and Radford were not prone to raise concerns about the activities of the Cells, the Jurats regard the payment away as an act of Bordeaux as administrator and not of Messrs Meader and Radford as directors of the Cells, and so do not find the absence of any enquiry or raising of concern as indicating that they would simply have rubber-stamped the transaction come what may. Further, the terms of the Notes made no reference to anything other than acquiring the property representing the investments. Accordingly, the Jurats are not persuaded that the Club Easy Group acquisition would still have proceeded to completion even if Messrs Meader and Radford had had disclosed to them all the information that Mr Addison should have disclosed.

276. In respect of the final two bases on which Mr Addison suggests that his breaches of duty were not causative of the losses of the Plaintiffs, the Jurats are similarly unpersuaded that these break the causal link. As previously mentioned, the experts agreed that they were unable to offer any opinion on the issue of what the outcome for the Cells would be had the monies invested in Lonscale been invested in some alternative investment. The Deputy Bailiff directed the Jurats that it is Mr Addison who bears the burden of demonstrating that the Cells would have suffered losses even if he had acted in accordance with his duties as a director of them (adopting the approach set out by Teare J in *Omak Maritime Ltd v Mamola Challenger Shipping Co.* [2010] EWHC 2026 (Comm), at para. 47, to which Advocate Richardson had referred). In the circumstances where the evidence on the issue was at best ambiguous, the Jurats are satisfied that Mr Addison has failed to discharge this burden. As regards the impact of the global credit crunch at around this time, the Jurats also find that Mr Addison has not discharged this burden. They have already indicated that where there was any dispute between the experts' evidence, they generally preferred that of Mr Moore. Mr Moore attributed the failure of the Club Easy Group to the poor cash flow it experienced and not to the global credit crunch. The experts agreed that the crunch will have had some effect on the attitude of the institutions lending money to the Group, yet there has been no evidence of the banks lending to the companies within the Group taking steps to call in a loan thereby precipitating the failure of the Group. Further, the experts agreed that the student property sector was one of the more resilient over this period. Using the financial statements of PF3 as an example, even Arch itself regarded the performance during the period ended 31 March 2008 as largely unaffected [eg, p. 4245]:

> "*For a Company of this nature, operating during the most intense credit crisis for a generation, this represents an exceptional return. Indeed, the consistency and the strength of the returns provide real justification for the strategy at a time when many equity, bond and credit investors suffered greatly through exposure to public markets. …*
>
> *The ongoing credit crunch/lending slowdown will continue to provide greater opportunities for strategic investors focused on stressed and distressed opportunities. The overhang of appetite for capital in the commercial trading and real estate markets is swelling demand for flexible short term financing and structured financing at high yields, as traditional bank lenders generally pull back from the table.*"

277. For all these reasons, the Jurats are satisfied that the Plaintiffs have established that the breaches of duty of Mr Addison were *prima facie* causative of the full losses pleaded by the Plaintiffs.

Mitigation

Directions

278. The next stage to which the Court turns is Mr Addison's contention that the Plaintiffs failed to mitigate their losses. The Deputy Bailiff reminded the Jurats first that para. 259 of Mr Addison's Defences raised the fee structure for Spearpoint after 30 November 2009 as being an incentive to maximise cash proceeds and that "*The sale by the relevant Cells of their interests in the Lonscale Notes and of the shares in Lonscale was at an undervalue*". He then directed them, by reference to the summary given in *McGregor on Damages* (19th ed., at para. 9-019):

> "*The onus of proof on the issue of mitigation is on the defendant. If he fails to show that the claimant ought reasonably to have taken certain mitigating steps, then the normal measure will apply.*"

He added that the test for the Jurats to apply is whether the Plaintiffs have acted reasonably and that the standard of reasonableness to apply is not high as a result of any defendant against whom an allegation of failing to mitigate is made already being found to be a wrongdoer. As it had been put in *Banco de Portugal v Waterlow* [1932] AC 452, albeit in the context of a breach of contract, but which he regarded as equally applicable to the breaches of director's duties in the present case:

> "*The law is satisfied if the party placed in a difficult situation by reason of the breach of a duty owed to him has acted reasonably in the adoption of remedial measures and he will not be held disentitled to recover the cost of such measures merely because the party in breach can suggest that other measures less burdensome to him might have been taken.*"

279. The Deputy Bailiff offered further guidance to the Jurats about one of the illustrations referred to in para. 9-082 of *McGregor on Damages* of what is not required of a plaintiff in mitigation, namely that a plaintiff need not risk his money too far. One case cited in support of this example is *Jewelowski v Propp* [1944] 1 KB 510, which involved a plaintiff who had been induced by fraudulent misrepresentation to advance £1,000 to a company on a debenture. When the company went into liquidation, the plaintiff's claim on his debenture resulted in him receiving £257 16s 2d. To meet claims against the company, the company's receiver sold its assets. They were bought by the plaintiff for £350. The plaintiff subsequently made a profit of £600 when he re-sold those assets and the question was whether that profit should be taken into account when assessing damages in his claim. Lewis J stated (at page 511):

> "*The duty of a person to minimize his damages is a proposition which is well-known, but the question is whether he must expend money to enable him to do so. For the plaintiff it is contended that for this purpose he must be looked on as an outsider and his profit is not to be taken into consideration just because he had the good fortune and business astuteness to make a good bargain. It is a question of some difficulty and one on which there does not appear to be any authority, but it seems to me that the argument for the plaintiff is right, so that a plaintiff who is claiming damages for fraudulent misrepresentations cannot be called on to spend money to enable him to minimize the damages. It seems to me that such a rule would be going far beyond the rule that a plaintiff must minimize his damages.*"

The Deputy Bailiff suggested to the Jurats that this might be a helpful comparison when it came to them considering Mr Addison's suggestion that the sale of Lonscale was premature.

Discussion

280. The Jurats reject Mr Addison's contention that Spearpoint did not properly investigate all options available to the Plaintiffs before proceeding to sell Lonscale. Although it was not part of Mr Addison's pleaded case, they also find that there is no substance in his suggestion that Spearpoint, and so the Plaintiffs, failed to undertake adequate due diligence at the time of agreeing to sell Lonscale. Instead, they prefer the evidence that was given by Mr Davey about what he caused Spearpoint to do once it began to review the various positions to which it came as the replacement investment manager for the ICC and the Cells, from which they are satisfied that there was an appropriate degree of consideration of the options and that Spearpoint was not improperly incentivised by the changed investment objective of the Plaintiffs. The Jurats note that the revised investment objective was not agreed until the EGMs that took place on 28 January 2010, although they appreciate that there had been prior discussion about it. However, the board meeting of the ICC at which it was resolved to sell Lonscale to the minority shareholders took place on 15 January 2010, which means that the revised investment objective was not at that stage formally in place and operating as any incentive to Spearpoint. In any event, as Mr Davey commented, selling Lonscale rather than retaining it and earning fees for managing that investment under the terms of the IMAs was not as financially attractive to Spearpoint, but it was felt to be the best outcome for the investors.

281. The Jurats accept that the timescale between Spearpoint taking over from Arch and the new directors of the ICC and the Cells taking up office and the decision to sell Lonscale makes it look as though this disposal of an asset was done hastily, but they also recognise that one of the key factors taken into account before making that decision was input from Mr King, who had been involved with Lonscale and the investment in the Club Easy Group from the start, and in particular his memorandum dated 3 December 2009. Thereafter, the Jurats are satisfied that the possibility of retaining Lonscale was considered, but that the choice was made not to do so because of the requirement for significant further investment. The Jurats are satisfied that the Plaintiffs were not required as a means of mitigating any losses to take such steps as would have been involved in retaining Lonscale at that stage and spending yet more money on it. The prospect of it being a successful turnaround project could properly be regarded as remote and they realise that eventually Lonscale failed, which rather proves that point. The Jurats further note that there were apparently no prospective third party purchasers lining up to offer any value for Lonscale, which was why the option of negotiating with Mr Barkman and Mr Montague as the minority shareholders was a sensible course of action to follow.

282. The Jurats also have regard to the acceptance by Mr Davey in his evidence that Spearpoint had not caused any formal review of the Lonscale investment to be commissioned, preferring instead to take some informal input on the issue of whether the latest Storeys' valuation could be relied upon and the conclusion reached on that basis that it had been prepared using an incorrect approach, which has now been confirmed by the evidence of the experts. The Jurats are satisfied that the absence of any more wide-ranging due diligence at this time does not impact on their overall conclusion that obtaining any value for Lonscale was a good outcome for the Cells. Accordingly, even though this aspect has not been pleaded, it makes no difference to their findings in relation to mitigation. Similarly, they note that the various occasions on which Mr Davey updated the board of directors of the ICC of how compliance with the Disposal Agreement was going, including when it was faltering, shows a sufficient level of oversight and monitoring (again in sharp distinction from that of Mr Addison when he was a director) to be regarded as the steps of a reasonable person trying to minimise its losses. Likewise, the complaint made that the

Plaintiffs did not seek to prove their outstanding debt in the liquidation of Lonscale Holdings Limited is not regarded by the Jurats as indicative of a failure to mitigate the Plaintiffs' losses. This is another aspect that has not been particularised in the pleaded case and, in any event, the Jurats are prepared to accept the evidence of Mr Scott that this would have been a pointless exercise on the basis that there was no value in that company.

283. During cross-examination, Mr Scott indicated that, on the occasions when Mr Davey made personal loans to Lonscale, Mr Scott would probably have been prepared to take the risk of lending money from the Cells, had that option been advanced. However, because Mr Davey proceeded in the way he did, this did not arise. To the extent that this is advanced as an example of a small way in which the Cells could have mitigated their losses by reaping the profit that otherwise went to Mr Davey personally, which is a further aspect that goes beyond the pleaded case, the Court does not regard this as being an area where the losses could have been reduced. Spearpoint, as investment manager, was unable in the time required to present a professionally reasoned case. Accordingly, the Cells did not actually get the opportunity to determine whether there was merit in taking the level of risk involved. Accordingly, as an opportunity to mitigate it is too theoretical to be of assistance to Mr Addison. Further, this is a further example of where Mr Addison would have expected the Cells to be expending money to reduce their potential losses and so, in the light of the Deputy Bailiff's directions, goes further than can be expected of a reasonable person seeking to minimise the loss.

284. When considering whether the eventual sale of the Cells' interests in Lonscale to Lonscale Holdings Limited was, as Mr Addison asserts, at an undervalue, the Jurats have paid particular regard to:

(a) the auditor's opinion, which was put into effect when Arch was still the investment manager, that the value of Lonscale was zero;
(b) the evidence of the experts, who agreed that the Disposal Agreement, and the proceeds generated thereby, represented a very good result for the Cells;
(c) the evidence of Mr Scott, effectively as spokesman for the boards of directors of the Plaintiffs, that the board had agreed with the position outlined by Mr Davey and confirmed now by the experts; and
(d) what was actually received by the Cells prior to the eventual collapse of Lonscale, noting that Mr Davey had said in his evidence that he viewed it as a low probability that the Cells would receive all of the deferred consideration that had been agreed.

They have further noted that Mr Addison has not advanced any evidence as to what he says the value of Lonscale was or could have been if, as he says should have been the case, it had been retained for longer. Without Mr Addison putting forward any positive case as to the effect that he claims the Plaintiffs' failure to mitigate has produced, the Jurats find themselves to be placed in a difficult position, although their conclusion that the eventual outcome was a good one and certainly within the range of what could reasonably be expected in the circumstances means that the absence of such a case becomes less relevant.

285. The Jurats have, therefore, started from the premise that the value of Lonscale was zero. Consequently, any step that resulted in something being obtained in return for selling the Cells' interests in Lonscale amounts to a means of the Plaintiffs mitigating their losses, which would otherwise have been even larger. In the situation at the end of 2009 and the beginning of 2010, the Jurats are satisfied that it was a reasonable step for the Plaintiffs to take, through Spearpoint, to explore selling to whatever vehicle Messrs Barkman and Montague eventually identified as the purchaser. They accept Mr Davey's evidence that he took steps to negotiate as robustly as he could to improve the potential returns to the Cells. They further accept that the terms of the

Disposal Agreement concluded with Lonscale Holdings Limited included elements that left open options for the Cells to assume control of Lonscale, if appropriate, and to derive some benefit in the event that Lonscale was turned into a success. There has been no evidence of any better possible outcome being available. Accordingly, the Jurats do not find that Mr Addison has persuaded them that the Plaintiffs failed to mitigate their losses.

Indemnity

286. The indemnity on which Mr Addison relies is found in Article 49.1 of the Articles of Association of each Cell (and in similar form in Article 37. 1 of the Articles of Association of the ICC). In closing Mr Addison's case, Advocate Williams acknowledged that the indemnity exists only "*to the extent that due care and diligence has been exercised*". (This is also a requirement pursuant to section 10 of the Protection of Investors (Bailiwick of Guernsey) Law, 1987, as amended, because otherwise the provision exempting the person from liability would be void.) Given the findings of the Jurats that Mr Addison did not comply with his duty to exercise the care, skill and diligence required of him as a director of the Cells and the ICC, it follows that he is unable to place reliance on the indemnity in those Articles to avoid the liability that otherwise attaches to him.

287. To the extent that Advocate Williams sought to argue that the indemnity exists in respect of breaches such as the duty to act *bona fide* in the best interests of the company and to give disclosure in respect of a conflict, the Deputy Bailiff directed the Jurats that Advocate Williams was correct to point out that section 157 of the Companies (Guernsey) Law, 2008 is not engaged. Subsection (1) of that section provides that:

> "*Any provision that purports to exempt a director of a company (to any extent) from any liability that would otherwise attach to him in connection with any negligence, default, breach of duty or breach of trust in relation to the company is void.*"

However, that section only came into force on 1 July 2008 (by virtue of the Companies (Guernsey) Law, 2008 (Commencement) Ordinance, 2008). Further, regulation 10 of the Companies (Transitional Provisions) Regulations, 2008, dealing with an exemption from liability or indemnity provided before the commencement of the 2008 Law, keeps available such an exemption from liability or indemnity until 1 January 2010. As decided in *Perpetual Media Capital Limited v Enevoldsen* [2014] GLR 57 (at para. 35), "*there is a presumption, albeit rebuttable, that directors take up office on the terms of the company's articles*". In the absence of any suggestion that such a presumption had been rebutted, the Jurats were invited to conclude that when Mr Addison became a director of the ICC and of each of the Cells as they were incorporated, all of which took place before 1 July 2008, he did so with the benefit of the indemnity in the respective Articles of Association. Further, because his tenure as a director ended in 2009, before the end of the transitional period, he would not lose the protection of these indemnities under section 157 of the 2008 Law.

288. The Deputy Bailiff directed the Jurats that as a matter of construction and in accordance with principle, even if they were considering the loss flowing from a breach of the duty relating to disclosure of a conflict of interest or to act *bona fide* in the best interests of a company, there could still be a finding that a breach of duty arose in circumstances where due care and diligence, as required by the Article in question, had not been exercised. Whether it had or not was a question of fact for them to determine. The principle involved is whether the beneficiary of an indemnity should be indemnified against liability for his own negligence, as expressed in *Canada Steamship Lines Ltd v The King* [1952] AC 192 and confirmed in *Smith v South Wales Switchgear Ltd* [1978] 1 WLR 165 (where Viscount Dilhorne regarded it as "*even more*

inherently improbable that one party should agree to discharge the liability of the other party for acts for which he is responsible", adding "*that the imposition by the proferens on the other party of liability to indemnify him against the consequences of his own negligence must be imposed by very clear words*" (page 168)).

289. Bearing in mind the Jurats' primary finding that the alleged conversation Mr Addison says he had with Mr Meader in August 2007 did not take place, the Jurats are satisfied that this aspect of non-disclosure by him falls under the heading of him not exercising the care and diligence that was required of him. They fail to understand the distinction that Advocate Williams appeared to be drawing between the various duties as pleaded and reach the conclusion that Mr Addison simply did not exercise "*due care and diligence*" in respect of his failings as a director in relation to the Club Easy Group acquisition, with the consequence that he cannot benefit from the indemnities in the Articles of Association.

Statutory relief from liability

290. The final element of Mr Addison's defence to the Plaintiffs' claim is that he should benefit from the operation of section 522(1) of the Companies (Guernsey) Law, 2008. This subsection provides (so far as relevant to Mr Addison):

> "*If in proceedings for negligence, default, breach of duty or breach of trust against –*
>
> *(a) an officer of a company …*
>
> *it appears to the Court that the officer … is or may be liable but that –*
>
> *(i) he acted honestly and reasonably, and*
>
> *(ii) having regard to all the circumstances of the case (including those connected with his appointment) he ought fairly to be excused,*
>
> *the Court may relieve him, either wholly or in part, from his liability on such terms and conditions as it thinks fit.*"

The Court understands that there are no previous decisions in Guernsey relating to the operation of this provision, although in the ***Perpetual Media*** case (*supra*), the Court of Appeal commented (at para. 49) that it gives "*a cushion for or comfort to directors*", being "*discretionary relief granted by the Court and tailored, if granted, to the circumstances of the individual case*". Accordingly, the Deputy Bailiff's directions to the Jurats were influenced by the approach taken pursuant to the equivalent provision in the Companies Act 2006, section 1157(1) (and its predecessor, section 727 of the Companies Act 1985).

Directions

291. The Deputy Bailiff first identified that there were three elements to the subsection that needed to be demonstrated before the Court could consider exercising what amounts to a discretionary form of relief. They are that Mr Addison, as a director, had acted honestly, reasonably and that he ought fairly to be excused. The Jurats were reminded that there had been no suggestion that Mr Addison had not acted honestly, which meant that the principal issues were whether he had acted reasonably and whether he ought fairly to be excused from some or all of the damages for which he would otherwise be found liable. The burden of proving this falls on Mr Addison, as explained through referring to how it had been put by Hoffmann J in ***Re Kirbys Coaches Ltd*** [1991] BCLC 414 (at page 415):

"*It is clear that a defaulting director ... who relies upon that section does have to make a positive case. It may be that honesty would be assumed in his favour in the absence of evidence to the contrary, but it is for him to show that he acted reasonably and ought fairly to be excused.*"

292. The Deputy Bailiff next directed the Jurats to have regard to the way that reliance on this provision had been put by Advocate Williams on behalf of Mr Addison in closing his case:

> "*This is plainly an appropriate case in which to grant relief:*
>
> *(i) There is no suggestion that Mr Addison acted otherwise than honestly.*
>
> *(ii) He was a non-executive director of the Company and its Cells, and in the discharge of his duties he relied upon third parties – both independent experts, such as PKF, Storeys and Cobbetts, and investment managers within his own firm – as he was fully entitled to do.*
>
> *(iii) Indeed, his conduct in that regard was no different from that of Mr Scott and his co-directors, particularly in his reliance upon Mr King and Mr Smith, both of whom were heavily involved in the acquisition of the Club Easy Group.*
>
> *(iv) As discussed below, Arch FP controlled the Company and at least five of the Cells at both the board level and the shareholder level. As a result, and as Mr Scott acknowledged during his evidence, Arch FP could have forced through the payment of its disputed fee on some basis.*"

Accordingly, when considering the reasonableness of what Mr Addison did as a non-executive director, the Jurats were invited to consider the way in which he relied on third parties, and in doing so to draw any warranted comparisons with the positions of the directors of the ICC and Cells after Mr Addison had resigned and been replaced, and whether his reaction was reasonable because of the ability of Arch to force through the payment of the fees that had been agreed for it and to Mr Barkman's order.

293. The Jurats were directed to apply an objective test to this element of the section. That direction is based on the way it was put in *Coleman Taymar Limited v Oakes* [2002] 2 BCLC 749 (at para. 85):

> "*Section 727 requires an 'essentially subjective approach' (see Re Produce Marketing Consortium Ltd [1989] BCLC 513 at 518, [1989] 1 WLR 745 at 750 per Knox J). In my view this subjective approach must be limited to the 'honesty' element of 'honestly and reasonably'. I do not see how the reasonableness requirement can be a subjective requirement. Any reasonableness test must by its very nature be objective.*"

Before leaving that case, the Deputy Bailiff considered it helpful to the Jurats to refer to the paragraph immediately following as well:

> "*It does not follow that merely because a director has acted (subjectively) honestly and (objectively) reasonably the court is bound to excuse him. Proof that a director has acted honestly and reasonably are pre-conditions of the court's jurisdiction. Once the conditions are fulfilled, the court must consider whether in all the circumstances the director ought fairly to be excused, and if so may (not must) relieve him either absolutely or partly on the terms the court thinks fit (see National Trustees Co of Australasia Ltd v General Finance Co of Australasia Ltd [1905] AC 373 at 381 (PC)).*"

294. In part as a means of drawing a distinction between this form of relief and that afforded by an indemnity provision, the Deputy Bailiff referred the Jurats to the brief explanation offered by Hoffmann LJ in *Re D'Jan of London Ltd* (*supra*, at page 649):

> "*It may seem odd that a person found to have been guilty of negligence, which involves failing to take reasonable care, can ever satisfy a court that he acted reasonably. Nevertheless, the section clearly contemplates that he may do so and it follows that conduct may be reasonable for the purposes of sec. 727 despite amounting to lack of reasonable care at common law.*"

This was explained in more detail by Evans-Lombe J in *Barings plc (in liquidation) v Coopers & Lybrand (a firm)* [2003] EWHC 1319 (Ch) by reference to what had been stated previously in respect of a similarly-worded provision in Australia in *Maelor Jones v Heywood-Smith* (1989) 54 SASR 285 (at page 294, quoted at para. 1130 of the *Barings* case):

> "*Whilst it may be that, in a particular situation, the very circumstances which give rise to a finding of negligence may be so pervasive and compelling as also to demand a conclusion that a person had acted unreasonably for the purposes of the exculpatory section, nevertheless that section is to be taken to directing its attention to a much wider area of concern – both in point of scope and time frame …*"

which then led Olssen J in that Australian case to conclude:

> "*… the court ... ought not to shrink from giving effect to its sense of fairness and justice. It should not hesitate, in a proper case, to relieve a person from what, having regard to particular facts and circumstances – particularly where the person concerned has acted honourably, fairly, in good faith, and in a common sense manner as judged by the standards of others of a similar professional background – from what might otherwise be seen to be a harsh and oppressive consequence of the strict application of the law, if applied in the absence of the considerations identified in the section.*"

As a result of his review of the approach that should be taken, Evans-Lombe J concluded, in the context of section 727 of the 1985 Act:

> "*They may have acted reasonably for the purposes of the section even though I have found them to have acted negligently, if they acted in good faith and their negligence was technical or minor in character, and not "pervasive and compelling". Nor am I limited to consideration of the nature of D&T's fault, but may take into account wider considerations, such as in D'Jan the economic reality that the defendant and his wife owned the entire company. Similar considerations weighed with the court in Re Duomatic [1969] 2 Ch 365.*"

295. In respect of the approach to take to section 522(1) of the 2008 Law, the Deputy Bailiff treated all of these principles as sound guidance, leading him to direct the Jurats that they should not regard any finding that there had been what might be regarded as negligence on the part of Mr Addison as somehow precluding him from benefiting from this statutory relief because it was clear from the wording of the provision that the legislature had expressly made this available in cases of negligence and breach of duty. However, the more pervasive and compelling the Jurats were to find Mr Addison's breaches, the less likely it was that they could properly find he had acted reasonably. Similarly, the further away from a finding that his breach or breaches had been technical or minor in character, the less likely it would be that they could find he acted reasonably. When considering whether Mr Addison had acted reasonably, the Jurats might find it

helpful to refer to the various words used by Olssen J, and consider whether Mr Addison had acted honourably, whether he had acted fairly, whether he had shown common sense, as judged objectively. Because there had been no allegation of bad faith against Mr Addison, the Deputy Bailiff directed the Jurats that they did not need to consider if he had acted other than in good faith.

296. By way of further explanation of the reference therein to *Re Duomatic* [1969] 2 Ch 365, the Deputy Bailiff pointed out that Buckley J had indicated that a director is regarded as having acted reasonably if he has acted in a way in which a man of affairs with reasonable care and circumspection could reasonably be expected to act in such a case. In that case, failing to seek legal advice had been found to be acting unreasonably. In relation to that, the economic reality of the ownership of the company, which was an aspect Advocate Williams had highlighted, was best covered by referring the Jurats to what Hoffmann LJ had stated in *Re D'Jan of London Ltd* (*supra*), where Mr D'Jan owned 99% of the company's shares and his wife owned the other 1% (at page 649):

> "*It may be reasonable to take a risk in relation to your own money which would be unreasonable in relation to someone else's. And although for the purposes of the law of negligence the company is a separate entity to which Mr D'Jan owes a duty of care which cannot vary according to the number of shares he owns, I think that the economic realities of the case can be taken into account in exercising the discretion under sec. 727. His breach of duty in failing to read the form before signing was not gross. It was the kind of thing which could happen to any busy man, although, as I have said, this is not enough to excuse it. But I think that it is also relevant that in 1986, with the company solvent and indeed prosperous, the only persons whose interests he was foreseeably putting at risk by not reading the form were himself and his wife. Mr D'Jan certainly acted honestly. For the purposes of sec. 727 I think he acted reasonably and I think he ought fairly to be excused for some, though not all, of the liability which he would otherwise have incurred. Mr D'Jan has proved as an unsecured creditor in the sum of £102,913. He has been paid an interim dividend of 40p in the pound and the liquidator has paid a further dividend of 20p but withheld payment to Mr D'Jan pending the resolution of these proceedings. In my view, having been responsible for the additional shortfall in respect of unsecured creditors, I do not think that he should be allowed any further participation in competition with ordinary trade creditors. On the other hand, I do not think it would be fair to ask him to return what he has received or make a further contribution out of his own pocket to the company's assets. I therefore declare that Mr D'Jan is liable to compensate the company for the loss caused by his breach of duty in an amount not exceeding any unpaid dividends to which he would otherwise be entitled as an unsecured creditor*."

297. A further factor on which the Deputy Bailiff gave the Jurats direction relates to the issue of whether Mr Addison's knowledge of his responsibilities as a director of the ICC and of the Cells could be regarded as relevant. He cautioned against placing too much reliance on how this issue had been addressed in the examples he would mention, reminding the Jurats that the question was particularly fact-sensitive and for them to determine on the evidence they had heard and read, but raised the point because it had been a feature in a number of relief from liability cases to which the Court had been referred. The first was *Queensway Systems Ltd (in liquidation) v Walker* [2006] EWHC 2496 (Ch), in which the liquidators of the company were seeking repayment from two directors of the company, who were also its sole shareholders, of monies that had been paid to them or for their benefit and so in breach of section 330 of the Companies Act 1985. At para. 69, the court stated that counsel for the Second Defendant had urged the submission:

"*... that Mrs Walker acted reasonably and in all the circumstances ought fairly to be excused because she was not in any position of knowledge such as should have compelled her to do anything but be acquiescent to the payments which occurred; she did nothing wrong; and in particular did not do anything to damage or defeat the interests of creditors. On the findings which I have made I do not consider that Mrs Walker acted reasonably for the purposes of s 727(1). It may be that by referring to Mrs Walker's position of knowledge it was intended to submit that Mrs Walker acted reasonably and ought fairly to be excused because her allowing the payments to occur was attributable to ignorance of her duties as a director and/or ignorance that such payments could involve a contravention of s 330 Companies Act 1985 or a misapplication of company funds. I would not accept any such submission.*"

In *Re DKG Contractors Ltd* [1990] BCC 903, which was a wrongful trading case involving misfeasance under which monies had been paid to one of the directors of a small company that had succeeded to the previous trading business of the principal, a Mr Gibbons, the court decided (at page 912) that neither of the directors:

"*... had any knowledge of company law or of the concept of limited liability. Mrs Gibbons did not know to what extent she might be liable for the company's debts. I do not think that they deliberately traded in the manner in which they did to avoid personal liability. However, I do not think that they acted reasonably. Before trading in the manner in which they did, they ought to have sought some advice at least, and I think it is significant that the the [sic] only offer of advice which was made to them was not taken up. Mr Parker said that he offered to show Mrs Gibbons what books were required for company trading. Mr and Mrs Gibbons, however, chose to trade in a way in which Mr Gibbons has had the lion's share of the company's money, and the outside creditors have been left unpaid. For the same reason, I do not think that they ought to be excused and I do not propose to apply sec. 727 of the Companies Act.*"

298. Some further general guidance on this issue was given in *Lexi Holdings plc (in administration) v Luqman* [2007] EWHC 2652 (Ch), where the conclusion, shortly after referring (at para. 219) to the "*concomitant obligation to supervise the delegate*", to which reference has previously been made, was (at para. 224):

"*In the present case, Monuza has sought to justify her complete inactivity upon the basis not only of her trust in her brother Shaid, but also on the basis that Shaid was apparently monitored in his activities by three other directors, all of whom, unlike her, were experienced professionals. In my judgment, while such reliance may reasonably greatly reduce the obligations of a non-professional non-executive director to appraise herself of the affairs of a company, and to supervise her colleagues, it cannot reduce them to vanishing point, so as to justify complete inactivity. In my judgment the defence that complete inactivity was a sufficient discharge of her fiduciary and common law duties fails the reality test. That conclusion also disposes of Monuza's attempt to rely on s.727. Complete inactivity as a director is by definition unreasonable.*"

In *Bishopsgate Investment Management Ltd v Maxwell* [1993] BCC 120, although the relief from liability provision had not been invoked, Hoffmann LJ explained why he regarded that decision as having been the correct one (at page 140):

"*If a director chooses to participate in the management of the company and exercises powers on its behalf, he owes a duty to act bona fide in the interests of the company. He must exercise the power solely for the purpose for which it was conferred. To exercise*

the power for another purpose is a breach of his fiduciary duty. It is no answer that he was under no duty to act in the first place. Nor can Mr Maxwell be excused on the ground that he blindly followed the lead of his brother Kevin. If one signature was sufficient, the articles would have said so. The company was entitled to have two officers independently decide that it was proper to sign the transfer. Mr Maxwell was in breach of his fiduciary duty because he gave away the company's assets for no consideration to a private family company of which he was a director. This was a prima facie use of his powers as a director for an improper purpose ... It seems to me that the cause of action is constituted not by failure to make enquiries but simply by the improper transfer of the shares to Robert Maxwell Group plc. Even if Mr Maxwell had made enquiries and received reassuring answers from other directions whom he was reasonably entitled to trust, he would not have escaped liability for a transfer which was in fact for a purpose outside the powers entrusted to the board. He may or may not have been entitled to relief under sec. 727 of the Companies Act 1985 but since in fact he made no inquiry, no reliance has – in my view rightly – been placed on this section."

Accordingly, in considering whether or not Mr Addison had acted reasonably, the Jurats would have to weigh what he had or had not done at the relevant time in the light of the role he was undertaking as a director, who was effectively an appointee on behalf of Arch.

299. The final aspect relating to reasonableness of Mr Addison's action was in respect of his contention that he was entitled to rely upon third parties. Referring to the way Nelson J had dealt with this in *Bairstow v Queens Moat Houses plc* [2000] 1 BCLC 549, which was a case in which directors were *prima facie* liable to repay dividends that had been unlawfully paid because the company had not had sufficient distributable reserves and, in respect of one year, the accounts did not show a true and fair view, the Deputy Bailiff noted the way in which the extent to which there can be reliance very much depends on the circumstances (at page 572):

> "*I am prepared to accept that an honest and reasonable director may in fact overlook his obligation under the 1985 Act by placing too much reliance upon his auditors, even though he should not have done.*
>
> *I am satisfied by the claimants on the balance of probabilities that they were neither dishonest nor unreasonable in being unaware that there were insufficient reserves available in the parent company to pay the dividends on the basis of the 1990 accounts, and that this rendered them unlawful under the 1985 Act. In all the circumstances it would be appropriate to give them relief and hence not order the repayment of the dividends which were unlawful by reason of there being insufficient reserves on the face of the 1990 accounts.*
>
> *The situation is somewhat different however in relation to the payment of dividends under the 1991 accounts when there were insufficient reserves, as the claimants knew that the 1991 accounts overstated the real profit very substantially, and must have appreciated that this was relevant to the dividend level being maintained. They must have turned their minds to whether or not the dividends could still be paid and what level they should be recommended, even if they did not consider the provisions of the 1985 Act. In any event if they did not consider what dividends should be paid, their conduct cannot have been reasonable given that they knew that there were seriously reduced profits, breach of the banking covenants, and rising debt and hence ought to have known that these circumstances questioned whether an ordinary dividend should be payable at all.*

> *I am not satisfied in these circumstances that the claimants are entitled to relief in relation to the payment of ordinary dividends on the basis of the 1991 accounts when there were insufficient reserves.*"

300. The Deputy Bailiff explained to the Jurats that Mr Addison was principally advancing that he should be relieved from liability, whether in whole or in part, because he had acted reasonably in all the circumstances. He pointed out that if the Jurats concluded that Mr Addison had not acted reasonably, that would end his reliance on section 522 of the 2008 Law. That is the approach that had been taken in *Coleman Taymar Limited v Oakes* (*supra*), which had involved the defendant not disclosing some secret negotiations with the company's landlords to take over the premises from which the company operated whilst also negotiating on behalf of the company to surrender its lease to its landlord. Whether Mr Addison had acted reasonably was a factual determination for them, taking into account the various elements to which he had referred. However, if they concluded that he had acted reasonably, they would then proceed to consider whether he ought fairly to be excused and, if so, whether to exercise the Court's discretion to grant any relief. There was a degree of overlap in relation to those matters.

301. The Jurats were reminded by the Deputy Bailiff that little had been said by either Advocate on this element. In some respects, Advocate Williams, on behalf of Mr Addison, was inviting the Jurats to conclude that if they found that Mr Addison had indeed acted reasonably, then it should follow that his position was such that he deserved to be relieved from liability. Implicit in that was that he should be relieved from the whole of the liability he would otherwise face. The Deputy Bailiff directed the Jurats that this was not automatic and would potentially involve them in a separate stage of consideration. In *Queensway Systems Ltd (in liquidation) v Walker* (*supra*), there was a brief comment on this further element (at para. 70):

> "*In any event I do not consider that Mrs Walker ought fairly to be excused under the subsection when the effect of doing so would operate to the prejudice of the Company's creditors, in that I would be relieving Mrs Walker from a liability to repay money to the Company at their expense.*"

The Deputy Bailiff, by reference to what had been pointed out in *Maelor Jones v Heywood-Smith* (*supra*), directed the Jurats that when assessing fairness their considerations could go beyond just what had been done or omitted to be done and should, so far as relevant, involve full consideration of all the consequences of affording Mr Addison the relief he sought.

Discussion

302. The Jurats first recognise, in the light of the Deputy Bailiff's directions, that Mr Addison is to be regarded as having acted honestly and in good faith. Neither of these aspects of his conduct has been challenged. However, they do not find that he has acted reasonably and, for that reason, he cannot benefit from the relief provided by section 522 of the 2008 Law. Their reasons for reaching that conclusion are as follows.

303. Although the Jurats have remarked that they consider that Mr Addison appears to have been out of his depth, they note the level of involvement that he had in setting up the structure at the outset. He was assertive enough not to want assistance from Carey Olsen in respect of the IMAs. The implication is that he should not be regarded as being anything like a novice in relation to corporate matters, but rather than he was able to understand the responsibilities he was undertaking as a director of the ICC and of the Cells. His failings cannot be excused on the basis of lack of knowledge of these types of matter.

304. The findings made by the Jurats demonstrate clearly that the breaches of duty for which Mr Addison is liable cannot be regarded as technical or minor in character. Indeed, Mr Addison himself acknowledged that all conflicts of interest are serious and need to be addressed. On the basis of the Jurats' primary finding that Mr Addison made no disclosure of the conflict of interest involving Arch taking a substantial fee for whatever part it was playing in the acquisition of the Club Easy Group, this was clearly something more than a mere technicality. It was a major breach of duty, with what turned out to be far-reaching consequences.

305. The Jurats have taken account of the fact that Mr Addison has been subjected to very severe regulatory sanctions. As a result, he has lost his ability to be employed within the regulated financial services sector. They have also borne in mind that Mr Farrell was more than likely the dominant person within Arch and that both he and Arch itself have already had judgment entered against them for the full amount claimed by the Cells in the present action. However, to the extent that Mr Addison was in any way subordinated to Mr Farrell, they do not find that this excuses him for the poor way in which he performed his duties as a director of the ICC and the Cells. His offices as director necessarily involved an element of independence from Arch. The absence of the types of enquiry the Jurats find he should have been making and, most particularly, his non-disclosure of the pertinent details of the extraordinary fees being extracted on completion of the Club Easy Group transaction lead the Jurats to the simple conclusion that Mr Addison did not act reasonably, as required in order to be entitled to relief from liability. Even if the Jurats are wrong to reach that conclusion, for similar reasons they would not be minded to grant Mr Addison any relief in any event on the basis that it would not be fair to the Cells, and to the investors in those Cells, to do so. The breaches found stretch over a period of time from first becoming aware of the potential for investment in the Club Easy Group through to final completion around three months later. There were various points at which Mr Addison could have done something to try to resolve the position as it was developing, but he did nothing. This is not a case where there was a single point in time where there was a lapse below the standards required of him and, having regard to the full history of what took place at that time, the Jurats have no hesitation in concluding that this is not a case where section 522 of the 2008 Law assists.

Conclusion

306. For the reasons given, the Court is satisfied that the Plaintiffs have proved that Mr Addison is liable for breaches of his duties as a director for the full amount of the losses claimed. The Plaintiffs have succeeded in establishing that there was no disclosure by Mr Addison to Mr Meader, as he claimed there had been, of any conflict arising from the proposed investments by the Cells in the Club Easy Group through what became Lonscale. In any event, the Plaintiffs have satisfied the Court that Mr Addison fell short in fulfilling his duties as a director to act in the best interests of the Cells, to exercise the care, skill and diligence expected of him and to understand, monitor and oversee the management and business activities of the Cells. Those breaches caused the losses incurred, and Mr Addison has not been able to persuade the Court that the causal link is broken. Mr Addison has also failed to discharge the burden he has in respect of mitigation and his claim to benefit from an indemnity is rejected because he did not exercise due care and diligence and his alternative claim to entitlement to enjoy relief from liability pursuant to section 522(1) of the 2008 Law is rejected because he did not act reasonably.

307. Counsel are invited to agree the terms of the order to be made against Mr Addison and, in particular, how to deal with any pre-judgment interest. The Court will now hear any further submissions on this issue and any further applications ancillary to this judgment.