Friday, 3 February 2017
(10.30 am)
HOUSEKEEPING
MR TROWER: My Lord, just before Mr Arden carries on, there is one housekeeping matter from yesterday.
Your Lordship asked us about whether it was a good idea for your Lordship to have a file of the cases of the Supreme Court. It sounds worse than it is, in the sense that there are two relatively slim bound volumes of cases, and I think we all do think it would be a good idea if your Lordship had them. We will put a sheet of paper at the front which identifies those paragraphs in each of the cases which deals with the contributory related issues, because there are of course, within the cases, sections dealing with currency conversion claims and the lacuna in relation to interest, which your Lordship doesn't need to be troubled with. We will prepare that and it will be available during the course of the day.
MR JUSTICE HILDYARD: Thank you very much. Thank you.
Submissions by MR ARDEN (continued)
MR JUSTICE HILDYARD: Yes, Mr Arden.
MR ARDEN: My Lord, I finished yesterday by taking your Lordship through at a bit of a gallop through Webb v Whiffin and the Brett and Morris cases.

MR JUSTICE HILDYARD: Yes.
MR ARDEN: Your Lordship indicated you may wish to come back on those this morning. My Lord, I am happy to go back to those cases if your Lordship would find it helpful.
MR JUSTICE HILDYARD: I have neglected to look at them again. I was puzzling, really, over this business of subordination and nil value, looking at the recent Lehman case. I still find it a little confusing.
I am also just puzzling as to whether your submission, you only look at contractual contingencies and not economic dependency, and you rely on that particular phrase in Lord Justice Lewison's judgment. I fully understand why you do so but, logically, one might expect it simply to be a matter of sequence. That is to say you look at the contingencies which emerge from the contractual terms and, having established, that you then work out whether there are any other impediments to recovery of the debt; that will include economic dependencies, as well.
I know what you are going to say, you are going to say: well, don't worry your head about that because the Court of Appeal have explained the result. It doesn't include that thought.
But I still find it hard to entirely reconcile myself to the actual process, or logic. I don't mean it

rudely, but I do. There we are.
MR ARDEN: Your Lordship has anticipated I would come back to your Lordship on that point, much as I did yesterday, which is to say that the Court of Appeal had to decide how subordination worked in this case. They have come out with the result that I repeatedly emphasised to your Lordship yesterday, which is to construe the agreement as being properly -- it is a contingent contractual -- or a contractual agreement, where liability is contingent. Then that carries with it all of the consequences I outlined yesterday, and makes it fundamentally different from the economic dependency that any creditor, contingent or otherwise, in any level is subject to the trickle down.
MR JUSTICE HILDYARD: Yes. I don't think there is much dispute between you as to whether ultimately it is contingent. It is the "one would expect a nil value", which -- I find it difficult to catch that bus.
MR ARDEN: Well, my Lord, your Lordship raised this yesterday.
MR JUSTICE HILDYARD: Mm-hm.
MR ARDEN: I certainly didn't disagree, and I may have come close to agreeing but there is a sort of functional aspect to this --
MR JUSTICE HILDYARD: Mm-hm.

MR ARDEN: -- which is that you have to do it that way in order to achieve subordination. That is the way you achieve subordination, without infringing the pari passu rule.
MR JUSTICE HILDYARD: Mr Justice David Richards might have thought that it wasn't so easy and therefore he adopted a rather different basis for subordination, which resulted in the same punch line.
MR ARDEN: Yes. It is the same result by a different means, but obviously the two means are fundamentally different.
MR JUSTICE HILDYARD: They are. One has been overruled by the Court of Appeal, I accept that.
MR ARDEN: My Lord, that's right.
MR JUSTICE HILDYARD: Yes.
MR ARDEN: My Lord, I should say --
MR JUSTICE HILDYARD: I was really just giving you an excuse as to why I hadn't read Morris.
MR ARDEN: My Lord, they are fascinating cases. I don't know how your Lordship managed to keep away from them.
I should say, on estimation, of course the issue 3 is premised on a nil value going in. In other words, your Lordship is not being asked to determine that is wrong, that the estimation process shouldn't work in that way.
My Lord, as I sort of explained to your Lordship

yesterday, just assume that that wasn't the case and so one went through a non-binary estimation: let's say the result of that was to attribute a 10 per cent value, you get to the same result that we are contending for. Of course, the reason you can't do that is because it wrecks subordination.

MR JUSTICE HILDYARD: Yes. I can see that ultimately this is sort of flapping about a point which may not actually affect the analysis. I can see that, but I am just explaining to you that I do find that difficult. In a way, it also goes in my own mind -- whether logically or not -- to the essential difference between you and Mr Trower, for example. You are a bucket man, he is a sluice man. You just look at the bucket and you have to be able to reconcile yourself, or persuade yourself, that there is something payable under the relevant bucket in order to justify the claim outwards. If there isn't, and there is a nil value, that is the end of the story. Mr Trower, on the other hand, being a sluice man, said, "No, no, you don't look at that, you look at the overall indebtedness. If there is an overall indebtedness, you have the outward claim and you then determine, at the end of the day, what the result should be". It is simply trying to create a logical universe in my own mind, and that is where sometimes the steps

have confused me, as you can tell.

MR ARDEN: My Lord, I think that is right.

But, my Lord, as far as overall indebtedness is concerned, this is the deficiency point. One still has to ask: well, what debts go into the debit side of the --

MR JUSTICE HILDYARD: Yes.

MR ARDEN: If there is a contingent debt, one has to say: well, what's it -- so you still get back to the -- once one is in the realm of contractual contingency, in a sense the bucket comes -- I am not sure I can pursue your Lordship's analogy properly.

MR JUSTICE HILDYARD: Yes.

MR ARDEN: But the contingency, the existence of contingent liabilities, and what you do with them, is a process you have to go through in order to determine the total amount of the deficiency. When you are asking what the totality of the debts are, you have to ask yourself where they are contingent, as I said, what amount is payable in respect of it.

MR JUSTICE HILDYARD: Yes. So now you have seen the level of my confusion, do you think we should go to Morris or not? I think read them and I will get a chance to interrogate you in reply, if necessary.

MR ARDEN: My Lord, I am happy for your Lordship to read

them. My Lord, they don't go to this particular point.

MR JUSTICE HILDYARD: No.

MR ARDEN: They go to the measurement of the liability --

MR JUSTICE HILDYARD: Yes.

MR ARDEN: -- under section 74.

MR JUSTICE HILDYARD: Yes.

MR ARDEN: To pick up, or to use Mr Justice Dixon's terms, the importance of establishing the claims on the fund, because it is by reference to those that your liability is measured under section 74.

Morris is a different case, as your Lordship knows, but you see the importance of going through that process, being emphasised in the judgment of the Lord Chancellor, the need to assess at the date of the call and the importance of not inflating the liability by reference to what he described as nominal amounts. Admittedly in the case of debts which existed at a particular date which have then been dealt with or discharged.

As I said, it is a different case but I think the principles and the approach which the Court of Appeal applied are useful for your Lordship and very much, I would submit, consistent with what we say about section 74.

MR JUSTICE HILDYARD: Shall we leave it, having made my

confession that I will read those two cases, and maybe the universe will become clear in exactly where they fit in it likewise and then I can plague you again if necessary?

MR ARDEN: My Lord, absolutely, I would be quite happy.

My Lord, I thought I had finished issue 3. I haven't quite. I have one more point which I can deal with briefly, in part because, subject to your Lordship, Mr Atherton and I have agreed a division of responsibility which hands this point over to him.

My Lord, the point is the one which we make, the conundrum we pose in paragraph 63 of our skeleton. This is the analysis that I think Mr Trower characterised as dense. I don't bridle at the use of that term. It is about right. My Lord, perhaps if your Lordship would just glance down 63, and then I will just make a few submissions on it.

(Pause)

MR JUSTICE HILDYARD: Yes.

MR ARDEN: Your Lordship, this is not a result for which we contend and it is not a result that arises on our analysis. This just won't happen. It is something which might happen on LBIE's analysis if you make a call, if you can make a call, in respect of the subordinated debt.

What it postulates is a situation where a call is made. There is a proof in LBHI2's estate. Sums are paid on account of that call. Those sums taken together with the other assets in LBIE's estate, mean that there are sufficient funds to pay all of the levels above us with a little bit over. The consequence of that is that the contingency is satisfied. We can then prove for the full amount of our claim and one then gets into the position of set-off, reversing the whole thing, so that the contingency is no longer satisfied and then it is, then it isn't, and so on and so forth.

Now, Mr Trower's answer to that was to take your Lordship to provisions in the subordinated debt agreement.

MR JUSTICE HILDYARD: 7(b).

MR ARDEN: 7(b), which precludes set-off. Now, the difficulty with that is in fact identified in Mr Trower's skeleton in part of his submissions made in relation to issue 9A. It is a contracting out difficulty.

As he rightly points out, at paragraph 26.9, you can't contract out of insolvency set-off, as NatWest v Halesowen. It is mandatory and self executing.

As I said, if your Lordship is content with this

course, Mr Atherton, who is going next, will expand on this a little bit. If that is right, you are left with the conundrum that we have identified which, as I have said, and I emphasise, is not a result that we contend for, because it just plainly undermines the whole point of the subordination agreement, and is not one which arises on our analysis.

Is your Lordship looking for 7(b)?

MR JUSTICE HILDYARD: I was going to wonder what you say 7(b) tackles.

MR ARDEN: Is it in T4/1? Yes, my Lord, T4/1.

MR JUSTICE HILDYARD: Which file is that; 4?

MR ARDEN: It is bundle 4. We are using the agreement at --

MR JUSTICE HILDYARD: Yes.

MR ARDEN: So it is page 6. 6 in the agreement, 12 in the bundle, the page.

MR JUSTICE HILDYARD: Yes.

MR ARDEN: My Lord, what it would cover, what it would preclude, is set-off or netting off out side of an insolvency.

MR JUSTICE HILDYARD: So 7(b), on your analysis, applies only outside insolvency, because otherwise it contradicts the scheme.

MR ARDEN: Exactly.

MR JUSTICE HILDYARD: Yes.

MR ARDEN: My Lord, I hope your Lordship doesn't mind if I leave that hanging there.

MR JUSTICE HILDYARD: No.

MR ARDEN: Sure as I am --

MR JUSTICE HILDYARD: Boyle's law is going to take --

MR ARDEN: Yes.

My Lord, that is then issue 3. Now, the only other issue that I am going to deal with is issue 7.

MR JUSTICE HILDYARD: Yes.

MR ARDEN: We deal with that from paragraph 69 to 80 of our skeleton.

My Lord, can I just preface that by making one point. If your Lordship would just go back to paragraph 43 of our skeleton.

MR JUSTICE HILDYARD: Yes.

MR ARDEN: My Lord, issue 7 recites the shareholdings and then asks the court to deal with the issues in the light of those shareholdings.

As your Lordship knows, there are different classes. We have ordinary and preference shares. An issue may arise, but doesn't arise for your Lordship and doesn't make a material difference to the hypothesis on which you have to deal with the issues in 7. An issue arises, or may arise, as to whether or not, when one is looking at ultimate adjustment and responsibility for debts and

liabilities, one should treat the preference shareholders and the ordinary shareholders differently because they have different rights to the surplus.

As your Lordship probably knows, I think you have looked at this in 3.2(c), the preference shareholders, here, have a right to the return of their capital, but no right to participate in the surplus. Only the ordinary shareholders have a right to participate in surplus. So if one bases responsibility by reference to rights to participate in surplus, then it would be allocated amongst ordinary shareholders but not preference shareholders.

My Lord, the reason it doesn't make a difference here is because of the numbers. What matters for the issues in issue 7 is the disparity between what LBHI2 holds and what LBL holds. LBL holds one share, we hold the rest. If the adjustment is done by reference to the nominal value of all shares, then the proportions are in the region of 13 billion to 1. If one does it by reference to ordinary shares, one gets down to the sort of measly figure of 6.2 billion or so to 1.

Whichever one it is, in terms of the disparity, the disparity is massive, so one can deal with the issues in issue 7 on either basis without it making a difference. My Lord, nor does it make a difference to what we say

about the need for an adjustment, because whichever way you look at it, when one came to the ultimate adjustment, where it is done by reference to share capital, it is what we could expect to come in from LBL is de minimis on either basis.

My Lord, I referred your Lordship to it because we raised the point which was raised in argument, I think by Mr Justice David Richards in waterfall 1. As he said, it doesn't really matter. We have picked up on that. I think, again, it doesn't matter, your Lordship can proceed on either basis.

So back to the issues in issue 7. We have dealt with them fairly briefly. Largely because we anticipated that in all of them, bar 7.5, on the position papers we would find ourselves aligned with LBIE. Indeed, that has turned out to be the case.

So if I can just go through the sub issues briefly: we agree with LBIE in its answer to and analysis of sub-paragraph 1 of issue 7, which is as to the nature of the liability under section 74.1. We agree with LBIE in its answer to issue 7.2 and 7.3, which deal with rights of contribution, indemnity and adjustment. We agree that it is all to be done through the statutory scheme, and by way of adjustment, not by way of contribution and indemnity. Therefore, set-off doesn't apply in the

context of adjustment.

We agree with LBIE on 7.4; whether the adjustment is affected by other claims. So the only sub issue of 7 with which we disagree with LBIE is in relation to the ability of a liquidator to call for less.

As I indicated, I think at the outset, having seen LBIE's submissions and heard what Mr Trower says about it, I suspect that the difference between us is maybe one of emphasis but certainly more apparent than real.

My Lord, what we say about that is in the skeleton. It is this: we submit that there is a discretion as to the way in which you make calls. You can make calls on one or more. You don't have to make calls on all contributories, you can make calls in differing amounts. We submit that is clear from both section 150, the use of the permissive "may" and also the rules themselves, which contemplate that there may be inequality of approach to different contributories.

But, my Lord, the reason that I think the difference between us is perhaps not as deep as it might be is that we would accept that the power to make a call, the discretion to make a call, has to be exercised in the light of the statutory purposes, which are set out in section 74 and then repeated in section 150 for the payment of creditors, the payment of expenses and

adjustment.

So the decision to make a call or not to make a call is one that has to be justified by reference to the achievement of those purposes. It is for that reason that in many cases, other than inability to pay, the personal circumstances of the contributory may well not be a relevant factor to take into account. If they cut across the statutory purposes, then the statutory purposes are likely to be preferred.

Now, we have postulated one possible scenario which would justify an inequality of call in our skeleton and it is essentially the same one that Mr Trower advanced as a possible set of circumstances where you might make different calls; that is where all statutory purposes can be achieved by making adequate calls. You might well get a case where an inequality of call will result in -- and so, for example, if you have solvent contributories and an imbalance in nominal value, you may, by making a larger call on the larger shareholder, be able to achieve not merely the satisfaction of the creditor's debts and liabilities and the payment of the expenses, but also by dint of doing that achieve adjustment at the same time; that clearly makes sense, because it prevents you from making two calls. It prevents an essentially simple winding up from becoming

more complicated than it needs to.

My Lord, beyond that we say in the skeleton -- and I think this must be right -- that everything will depend upon the particular circumstances. Beyond saying what I said fairly shortly, it is quite difficult for the court to give definitive guidance because it is all completely fact dependent. So, my Lord, that I think is all I wanted to say on 7.5.

My Lord, there then remains 8, the rule against double proof. Again, we agree with LBIE, and our analysis, I think, is essentially the same. That we deal with from 81 to 87 of our skeleton.

On issue 9, the preliminary issue, again, we agree with LBIE about contracting out.

The same applies to issue 10. On recharge, again we agree with LBIE in its answer and the analysis which leads to that answer to the issue posed by 10.

MR JUSTICE HILDYARD: Yes.

MR ARDEN: My Lord, on 12, the LBL issues, we have nothing to say because it doesn't concern us.

So, my Lord, on the disputed issues, that is our position and those are our submissions. Perhaps I can just check behind me, and then I will just come back to deal briefly with the agreed issues.

My Lord, those are my submissions on the disputed

issues.
I think on the agreed issues, essentially they are being left over and then, I think, with those and these issues, your Lordship is going to receive assistance on how they are impacted by the Supreme Court. I think they will be revisited in due course, but I don't think there is anything I need to say about those or about Mr Trower's approach at the moment. I think this is probably something we come back to.
So, my Lord, unless I can assist your Lordship, those are our submissions.
MR JUSTICE HILDYARD: Thank you very much.
Yes.
Submissions by MR ATHERTON
MR ATHERTON: My Lord, I am obliged.
MR JUSTICE HILDYARD: Mr Atherton.
MR ATHERTON: Could I just start off where Mr Arden left off in terms of what our position is in relation to the various issues.
As far as we are concerned, we understand that issues 2, 4, 5, 6 and 12 are agreed between the parties as a matter of principle.
I think issues 2 and 4, particularly the terms of the declarations, need to be agreed. They may also be subject to alteration in the light of any decision from

the Supreme Court.
As regards 5 and 6, and issue 12, which are the LBL issues, the administrators of LBH have agreed with LBL the terms of declarations that could be made, and for our part we don't think that they will be impacted by the determinations, pending judgments from the Supreme Court.
As regards those same issues, 5 and 6, I understand that the declarations have been agreed as between all of the parties, but there is an issue potentially between LBL and LBIE as regards the terms of the declaration in relation to 12. As far as we are concerned, we have accepted the modification to the declaration as proposed by LBL.
MS TOUBE: My Lord, I hesitate to rise but I should just say that issue 12 has been agreed by everybody, including LBIE. LBIE had different wording, originally, but everybody has adopted ours.
MR TROWER: That's right.
MR ATHERTON: That is helpful.
MR JUSTICE HILDYARD: So issue 12, subject to it being appropriate to make a declaration in respect of it at all and it being your present view that the Supreme Court's reference is not really going to affected --
MR ATHERTON: That's right.

MR JUSTICE HILDYARD: -- is agreed on the basis of the wording proposed by LBL.
MR ATHERTON: Correct.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: As far as regards issue 8, we have effectively adopted, as set out in our position paper, the position of LBIE. I think the only outlier by way of a change is LBL in relation to that issue.
Issues 7.1 to 7.4, we effectively agree with LBIE. Again, as far as LBH is concerned there is no issue there, and we would hope, insofar as appropriate, to agree declarations in due course, even if in escrow, if you like.
As regards issues 9A and 10, the LBH administrators don't take a position.
On that basis, my Lord, and as you will have seen from our outline submissions, the only issues that I propose to deal with are issues 1, 3 and 7.5. I was proposing to deal with those in this way, with your Lordship's permission: I was going to deal with issue 3 first, essentially because it follows directly on from Mr Arden and it is certainly fresh in everyone's mind.
I was then going to deal with issue 7.5, because that relates, or there are issues which are relevant to issue 7.5 and issue 3; then I was going to deal with

issue 1, which will then hopefully lead in with Mr Marshall, who I understand will be starting with issue 1. That is why I have adopted this particular order.
My Lord, Mr Trower, in relation to issue 3, started his submissions by indicating that the position adopted, essentially, on this side of the court, by LBH, LBL and LBHI2 was a consequence of a misunderstanding of the waterfall and a misinterpretation of Lord Justice Lewison's reasoning in the Court of Appeal.
What is sauce for the goose is sauce for the gander, in the sense that I would suggest that the position adopted by LBIE is consequential upon a misunderstanding of the waterfall, a mischaracterisation of what is meant by contingent, a misunderstanding/a misinterpretation of Lord Justice Lewison, a non-application of the mandatory regime for estimating contingent liabilities, which in turn results in a misapplication of the call provisions in section 74 and section 150.
Just pausing there, I should have pointed out that, I am very grateful to Mr Arden for his submissions, which I adopt wholeheartedly and in whole. Hopefully I won't repeat what he said, but my submissions are, essentially, perhaps a change in emphasis or additions to what he says. But, for example, the point about

mischaracterisation of the meaning of contingency, or contingent, follows on directly from Mr Arden and your Lordship's discussion about dependency. We will come on to that momentarily.

Without wanting to demean the seriousness of the process that we are involved in, we have had some colourful allusions during the course of submissions, which have served their purpose.

MR JUSTICE HILDYARD: Do you mean buckets or sluices?

MR ATHERTON: I was going to say free flowing streams, buckets. We have also learned that Mr Arden and Mr Trower dine together and contemplate leaving without paying the bill together and in some cases when they can't pay the bill, it appears that they have an inveterate gambling problem. I am going to join in if you don't mind. I hope your Lordship will see where I am going, and the first line of this is not true. I have very hairy legs. Or rather, let me do it the other way around. Chimpanzees have very hairy legs. I have very hairy legs, therefore I am a chimpanzee. I hope your Lordship will bear witness that I am not. But if one applies effectively that type of Socratic syllogism -- is how Mr Trower seeks to justify the position he has embarked upon. If I could give you two syllogisms which I say exposes his analysis for being

flawed -- and I do mean that with the greatest of respect, and he knows I mean that with the greatest of respect.

First of all, we embark on the first analysis. Payment of the sub-debt is contingent upon payment of all liabilities higher up the waterfall. Payment of all liabilities in the waterfall are dependent upon payment of all liabilities higher up the waterfall, therefore all liabilities in the waterfall are contingent.

We say one only has to go through that process to expose the fact that the characterisation of contingency by reference to dependency is fundamentally flawed. The mere fact, as I think Mr Arden submitted, that when one is in the waterfall -- and using Mr Trower's illusion -- if the bucket isn't full, the water doesn't spill down in to the next bucket. All that means is it is not contingent on the filling up of the immediately prior bucket, it just means that the assets available in the estate of the company are insufficient to pay the liability. What is important about the waterfall liabilities is they are all there and all determined. They are actual liabilities. So, for example, upon the winding up, statutory interest is payable. That is a crystallised liability. It may be, in the circumstances, unable to make that payment. When one

goes down the waterfall, it may be that one can't pay sufficient for preferential creditors, whatever it might be. But that doesn't render the payments lower down the waterfall in any way contingent.

The second syllogism, which I think is the way Mr Trower actually puts his case, is as follows: the payment of liabilities in the waterfall are contingent upon payments being made higher up the waterfall, but you value all of the payments in the waterfall, both prior and successive, in full. The sub-debt is also contingent upon payments being made higher up the waterfall and therefore you must value that in full.

Again, we say that reasoning simply can't pertain in this case. The reason being -- and building upon what I have already submitted, my Lord -- all the liabilities in the waterfall are already determined, actual liabilities for the purposes of this analysis. We will come back and elaborate upon it in a moment. Therefore they have to be paid. They are not contingent. They are actual liabilities. The sub-debt is a properly so-called contingent liability. It is conditional upon payment of prior ranking claims, which include all of the liabilities from 1 to 7, but ranking before any obligations in relation to shareholders.

I suppose, one might say: so far so good. But,

again, it comes back to the fact that one is dealing, in 1 to 7, with actual liabilities. The reason why this is important is because -- as Mr Arden said today and yesterday -- when one is concerned in dealing with the call in a liquidation, one is concerned with dealing with actual liabilities.

Now, it may be that those liabilities can't be definitively determined, but they can be estimated. On the basis of that estimation, a call can be made. Mr Trower, I think, has made that submission. That is plain on the face of section 74.

The issue here, and what has sort of permitted Mr Trower to make the submission in the way that he has made it, is because he has conflated contingency and dependency and he has been allowed -- if I can put it this way -- to exercise that slight of hand because the contingency to which the sub-debt is subject, just so happens to mirror the waterfall; that is why Mr Trower was able to say, "The waterfall payments are contingent on the payments being made higher up the level", because that is the actual contingency by way of contract that applies to the sub-debt obligation.

I hope your Lordship sees that the waterfall claims, as you debated with Mr Arden, aren't contingent, they are merely dependent.

What are they dependent upon? Simply the ability to pay.

The sub-debt is not subject to that in terms of the way the waterfall operates. It is actually a pre-condition, contractually, that those prior ranking claims are in fact paid in full. So although there is a synergy between the two, they are fundamentally very different, in terms of how they are to be dealt with.

Now, applying Mr Trower's analysis further, and for which he relies upon the statement in the Court of Appeal of Lord Justice Briggs and Lord Justice Lewison. He says the situation is this: well, because contributories, particularly an unlimited company, are obliged to pay all the waterfall, from 1 to 7, then they are automatically obliged to pay anything in between, and that is why I can make a call. But one has to analyse, at each stage, in circumstances about how that obligation does arise.

So if I could give your Lordship an example: if we are looking at unsecured provable claims, at level five of the waterfall, within that one would have a series of provable debts. They will be plainly provable debts which are ascertained and determined and definitive in their value. They don't produce a problem. One would have prospective claims. Still dependency, as your

Lordship discussed yesterday, and you raised the question with Mr Arden about whether or not you would have issues of estimation with dependencies and the answer is: in the context of a prospective debt you would, because when you are making a distribution, you value it if that distribution is in advance in time from when the liability would otherwise be paid, you discount it.

Similarly, if one has contingent liabilities, at level 5 in the bucket, they have to be valued for the purposes of set-off and distribution if there is to be set-off, in any event, for the purposes of distribution. Mr Arden used the example of the valuation of the indemnities in the Danka case. Another very simple example would be in the context of an insurance company or a reinsurance company, where you have home insurance in relation to fire. One can determine, along the continuum, if it runs for 12 months, there has been no fire after 11 months and actually being able to work out what the chances are of the fire actually happening in the last month, and that would give you the value in respect of that contingent claim.

Leaving aside the circumstances we are in at the moment, if the liquidators or the administrator had a situation of assessing what the liabilities of

a company were, they would have to go through that process in relation to the level 5 waterfall liabilities. Estimating, or determining what those values were. It wouldn't necessarily be a situation where they would be definitive in relation to, certainly contingent liabilities. But in order to make a call on contributories they would have had to estimate those values in order to infer an appropriate exercise of the ability to make a call, and that would bring it within section 74.

I have not been able to think of an example, but if for example you had in bucket 5, what has been referred to in the context of this particular contingency, a binary contingency, let's say of 100, the liability would be 100. If it was similar in this context, the binary nature, it may be appropriate to make that value nil. You couldn't put it in as 100, because there is no liability at that stage or at any level in the waterfall. The position must be the same whether the company is solvent or insolvent. In a solvent context if one was subject to a contingent liability, until a contingency falls in nothing is due or payable. That is subject to one point: that must be the position in the context of an insolvency. Until the contingency falls in, nothing is due or payable. Therefore, if you

made a call against a contributory, the contributory would be entitled to say, "Well, I am simply not liable for that because that contingency hasn't occurred in the insolvency of the company". On that basis, we say that the analysis breaks down. As your Lordship already has, and if your Lordship goes back to the transcript where Mr Trower is dealing with his analysis, it is largely all predicated on the equiparation between contingent liability as regards the outbound claim and the inbound claim as regards LBHI2; the equiparation of that contingency with the dependency issues in terms of when the waterfall comes into play and the ability of those liabilities, which are actual liabilities, to be paid.

That is why it is not sufficient simply to say, "Well, because contributories are liable to pay liabilities from 1 through to 7, therefore they must be liable on that basis to make contributions", one has to, at each level, at least estimate what those liabilities are in order that you can put forward a genuine and proper call.

Now, we say that, therefore, deals with the misunderstanding of the waterfall, which Mr Arden also dealt with yesterday, the mischaracterisation of contingency. The third element, then, which we say is the flaw in the analysis is the misinterpretation of

Mr Justice Lewison.
Now, the first point, and if your Lordship were to ask me the question that you have asked Mr Arden this morning, I would give your Lordship the same answer: it doesn't really matter because Lord Justice Lewison has said the value is nil.
But Mr Trower's assertion is: well, when Lord Justice Lewison made that observation, at paragraph 41 of the judgment, he was talking about ranking; where in the waterfall? That is why it was given a nil value.
Now, hopefully your Lordship can see now why that can't be right. Lord Justice Lewison wasn't dealing with ranking when he valued it at nil, because you don't value it at nil. Statutory interest will have its full value at the end of the waterfall, whether or not it is capable of being paid from that waterfall. It may remain unpaid, but it has that fixed value. So the value at nil that Lord Justice Lewison is applying can't be by reference to ranking. And --
MR JUSTICE HILDYARD: Lord Justice Lewison, subject to Mr Trower correcting me, appears to say, expressly, it is nothing to do with ranking.
MR ATHERTON: No, I agree. I was going to take your Lordship to paragraph 41, but your Lordship has seen it

because the mood music in the new regime is to try to cram as much into provable liabilities as opposed to non-provable to ensure that they can properly be dealt with in the process of liquidation and winding up and that is why he is led, I think, to the determination that it must be nil.
Now, that is my supposition. But I think that is the only way one can analyse it, in terms of why you get there. The question may be -- with your Lordship's permission I will come back to it.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: It may have to be, in certain circumstances, that it can't be nil. I will come back that in a moment, if I might.
The other aspect, and it is probably easier if -- rather than me paraphrasing, if your Lordship has the transcript from day 1 to hand. I am not sure we have a designated bundle for it.
MR JUSTICE HILDYARD: No. I have, yes.
MR ATHERTON: Thank you.
MR JUSTICE HILDYARD: I am not sure it has been designated, but I have a bundle.
MR ATHERTON: It is page 82. I will just start there because it is the break after lunch.
MR JUSTICE HILDYARD: Yes.

time and time again.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: We agree. In its terms it is plain that he is talking about contingency when he is dealing with nil value. He comes back to it in paragraphs 62 and 63 of his judgment, where he does say that one of the reasons why it is nil value is because of the aspect of subordination. I think the issue simply is the nature of the contingency is such and its context, it is creating a subordination, is that the value of that contingency has to be nil and there is no real two ways about it.
MR JUSTICE HILDYARD: Why do you say that?
It is what you would expect. I know you say that the Court of Appeal says it and therefore that is what I now expect. Why does the contingency, stripping out any issue of dependency, why does it lead to nil?
MR ATHERTON: Well, the answer to that is given, I think, by Lord Justice Lewison in paragraph 63; because he is tying it to subordination. He has concluded that these debts are provable. Unlike Mr Justice David Richards, who achieved the same result from a different route.
MR JUSTICE HILDYARD: Therefore subordination worked, yes.
MR ATHERTON: Mr Justice Lewison came to the conclusion that they must be provable, as did Lord Justice Briggs,

MR ATHERTON: If your Lordship could just, to yourself, read into it. The important bit comes, really, at the start of Mr Trower's submission at line 23, on page 83. Taking you through to line 22, on page 84. Actually, my Lord, if you could read to page 85 to line 22.
MR JUSTICE HILDYARD: 83 to 85?
MR ATHERTON: Yes, please.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: Down to line 22.
(Pause)
MR JUSTICE HILDYARD: Yes, I have come to line 5, on 86.
MR ATHERTON: That is more than I asked your Lordship to do, but I am very grateful for the extra effort.
It took me some time to unpick this, because I am a bit slower than Mr Trower. But what I think it basically comes down to, he says that the payment on the waterfall, when you get to the level of non-provable debts and statutory interest, is quite illuminating as regards his analysis because you are not trammelled by any issues of set-off, and you simply have to pay them. So what he says is -- and we can go back to 84 my Lord, please, at line 6:
"You cannot set-off the account in LBIE's administration, that is the very nature of it."
That doesn't present a problem. So they have no

value in the insolvency, if looked at through Lord Justice Lewison's perspective.

Now, pausing there, that is not, with respect, what Lord Justice Lewison was saying because that is Mr Trower saying, "Lord Justice Lewison is talking about ranking".

It simply can't be right, because the non-provable liabilities in the administration in this case, subject to the Supreme Court, and in any liquidation, will have a definitive value. You can't value them at nil. They have a value.

Similarly, statutory interest is determined as an actual liability upon the winding up of the company under section 189. It will have a definitive value, so you don't value them at nil. You have to give them their actual value because they are crystallised liabilities within the winding up. Lord Justice Lewison wouldn't have valued them at nil, he would have valued them at the full value because Lord Justice Lewison is valuing the nil liability because it is contingent and the circumstances and nature of that contingency. So he is not valuing it by reference to its ranking.

So we say, again, that, if you like, is the distillation of Mr Trower's analysis; how he uses, we say, a misinterpretation of Lord Justice Lewison to

putatively support that analysis.

Now, it is convenient, I think, if you go to 85, as you have read that, just for me to make this point: I was trying to work out, rightly or wrongly, why the administrators of LBIE might be taking this position.

Now, on one level it may simply be, as Mr Arden says, and as was alluded to by the Blakeley Ordinance case, to swell the assets in the estate of LBIE for the benefit of its creditor constituency. What it is actually doing is importing the contributory principle into administration, because what is essentially happening is Mr Trower is saying, "No, there is no set-off here". So you value the out going claim in full which means, in theory, LBHI2 have to pay it and only after that payment is it possible for them to take or participate in any distributions from LBIE. We say that that is, at the moment certainly, impermissible, because the courts thus far have found that the contributory principle doesn't apply in administration.

Now, whether or not it is the same aspect of the same issue, either that or they are trying to create a situation whereby set-off, for whatever reason or on whatever basis, hasn't taken place in the administration, then move into liquidation where the contributory principle does apply. So there is no

prospect of set-off, insofar as it hasn't already occurred in relation to the liabilities owed by LBIE to LBHI2 and the sub-debt claim back from LBHI2.

Now, that may just be musings on my part, but I was just trying to work out what was the purpose or the motivation to create the situation that we say is being created.

The next point in the analysis deals with the non-application of the mandatory requirements of the insolvency regime. This goes to two points. First of all, your Lordship may recall, earlier on in my submissions, I was suggesting that the position in relation to the contingent liability, where the company was solvent, is that there is no liability due or payable because the contingency hasn't fallen in. The same position obtains in the insolvency because it must be the same.

Now, the slight difference there is it does in fact, as a matter of insolvency principle, become due, even though the contingency hasn't happened. It becomes due because that is what we are told happens, by rule 2.81 and 2.85, dealing with estimation and set-off. So it becomes due at that point in time, but it is still not payable. It becomes due because it has to be estimated and there is, therefore, we say, an obligation on the

administrators to estimate the liability.

It may be that the estimate is nil. They have estimated the incoming claim at nil, as per Lord Justice Lewison, they are adopting that. Then they say, "Nevertheless, the out going claim must be given full value".

Just dealing with this point, Mr Trower also said in his submissions, and it was an interesting word: it is a distraction to consider the outbound claim and the inbound claim as mirror images of themselves.

In my submission he is right, it is a distraction, because it distracts from the flaw in the arguments as presented by LBIE in order to get from where they start to where they want to finish. The reality is that the sub-debt contribution claim from LBIE against LBHI2 is entirely parasitic upon the sub-debt claim from LBHI2 into LBIE. It is highly false to draw a distinction between the two.

Now, in the context of estimation you heard from Mr Arden, where he said, "Well, in relation to issue 2, the principal position would be another value, because if one was looking at contingencies, the different contingencies as against the contingencies to which the outbound claim is subject, and the contingencies to which the inbound claim was subject, then in theory

because the inbound claim was subject to less contingency than the outbound claim, it would be different a different and higher value. Therefore, in theory, you would have a net balance in terms of any set-off". I am not suggesting we need to go through the exercise, but just for the purposes of articulation that means that there would be a net balance in favour of LBHI2.

The reality is that set-off has already occurred in this administration. It must have done because it is mandatory. It is self executing.

The intervention of the human agency, by which I mean the insolvency practitioner, is to give tangibility to that automatic, self-estimating set-off by providing an estimate for the net balance that arises from the two cross claims.

Now, prior to that the estimate may be: well, I can't put it in the set-off account because my estimate of the two claims is nil.

Well, so be it. Then it is nil. There isn't, therefore, in relation to the sub-debt contribution claim, anything which could form the basis of a legitimate call by a liquidator, or could form the basis of a legitimate contingent proof by an administrator in this case.

Now, we say that follows. Your Lordship is familiar with Stein v Blake. That is what Stein v Blake says. It is self executing, it is mandatory, it occurs automatically. We also say it is apparent from the relevant rules. My Lord, if it is convenient, could I just take you to those. I know they have been referred to, and Mr Arden refers to them, but I think it pays just to look at them. You can find those in bundle 5 of the authorities bundle, at tab 157. Yes, at 157 is rule 2.81. So sub-rule 1 makes it:

"Mandatory for the administrator to estimate the value of any debt which by reason of it being subject to any contingency [so this case] or any other reason does not bear a certain value."

So where you have an unascertained or unliquidated claim at level 5 in the waterfall, one is obliged to estimate it. You may revise it in the context of or by reference to the hindsight principle. And:

"Where the value of the debt is estimated in this rule the amount provable in the administration in the case of that debt is that of the estimate for the time being."

As Mr Arden said yesterday, correctly, the value which you would take is the value at the date of proof which would incorporate, insofar as relevant to the

estimation of the contingency, an element of hindsight by reference to the date of administration or rather the date when the administration became a distributing administration.

Now, my Lord, if we could go to 2.85, which deals with the set-off provisions. Rule 1 says it applies when it has become a distributing administration. Sub-rule 2 deals mutuality. Then if we go over the page, sub-rule 3:

"An account shall be taken at the date of the notice of what is due from each party to the other in respect of the mutual dealings and the sums due from one party shall be set-off against the sums due from the other."

If you read it with sub-rule 4:

"A sum shall be regarded as being due to or from the company for the purposes of paragraph 3 whether it is payable at present or in the future ... (b) the obligation by virtue of which it is payable is certain or contingent, or its amount is fixed or liquidated."

So that shows what I meant when I said, "It won't be due or payable in a solvent context but it may become due in the context of an insolvency", because the purpose is to deem it due for the purpose of estimation under 2.81, then insofar as the potential for a set-off as a consequence of mutual dealings, then for the

purposes of that set-off.

So, as I say, this process has already happened. What we don't have is the human intervention of the estimate. Either it is not set-offable because they are both nil, that takes care of itself. Or you can set it off.

We say it doesn't really matter in a way, because if, as Mr Trower submits, the contingency is, if you like, binary, it is all or nothing, then it doesn't really matter because the two sides of the equation will always balance. Even if you were adopting an analysis of contingency on the basis of a continuum, it becoming less or greater as you go along that horizontal continuum, you get to the situation where it will always be the same value. So one may then ask the question: why is this creating a difficulty?

It is only creating a difficulty because we say LBIE are adopting the wrong analysis as regards the waterfall, the nature of the contingency and the failure to apply the set-off provisions or the estimation provisions that they are required to apply in the course of the administration.

Again, I come back to the point I made earlier. Let's assume that you were just assessing what your provable, unsecured liabilities were at level 5, for the

purposes of knowing that the likelihood was that the assets of the company in winding up would not be sufficient to pay them. Before you make your call, you have to estimate what those liabilities are. You don't have to ascertain them, but they do require estimation in order to give a three-dimensional element and a justifiable element to the call against the contributories.

Now, Mr Trower and LBIE in their position paper sought to justify their analysis in relation to why they can give full value to the outbound claim by indicating, by reference to the contract company case in the 19th century, that was an example of where there were plainly future liabilities and, therefore, prior to ascertainment of the liabilities, and prior to the ascertainment of the assets that would be available to the liquidator in the winding up, the liquidator was at liberty to put in a call to shareholders in respect of their unpaid share liability. We say that is a very different situation. That is where one is dealing with actual liabilities. They may be prospective in some cases. They may have already crystallised, but you are estimating what the liabilities are and the liquidators have come to the conclusion that it is necessary to make a call, and the call is upheld by the court.

But what one had in that case is -- and I don't think I need to take you back to it, but if your Lordship goes to, we say, that case and -- I have lost my reference, but I will come back to it.

There are three cases which deal with this issue, but if you look at the rehearsal of the evidence, the liquidators have actually gone to the effort of estimating the liabilities that support, or in support of, the call that they wish to make. The court says it is entirely justifiable.

What is not justifiable is, as in the Blakeley Ordinance, one cannot put in a call for liabilities which do not exist, or which haven't been estimated. You cannot put a call in -- and this is I think the Barnard's Bank (?) case -- you cannot put a call in where it is obvious that the assets will be sufficient to pay the liabilities. All we have here is a situation where there is no estimate of the incoming claim, or rather the incoming claim is estimated at nil, but there is arguably no corresponding estimate applied on any reasoned basis to the outgoing claim.

Now, your Lordship might think: well, because these two claims are parasitic, in fact either we say the position is the inbound claim has been valued or estimated at nil, and that must dictate the value of the

parasitic outbound claim. Either that, or if the administrators are given the value to the outbound claim of, say, 1.3 billion, then that, suffice it to say, is the estimate that they are giving to the inbound claim, because the two -- it is binary. They can't have, on this analysis, different values.

Now, the way out of the conundrum is to apply Lord Justice Lewison's analysis, and it may be no more than analysis of cutting the Gordian knot, and no more sophisticated than that. But in terms of, "I have a contingency", the context of that contingency is it relates to subordination. I don't want to upset the subordination because of the regulatory context that it applies in and, therefore, the nature of the right or the nature of the liability can only be valued at nil, until such time that the contingency has fallen in.

MR JUSTICE HILDYARD: Going back to the actual section, section 70 --

MR ATHERTON: 74.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: Yes, my Lord.

MR JUSTICE HILDYARD: We will have a break soon.

MR ATHERTON: I beg your pardon, yes.

MR JUSTICE HILDYARD: Which I have in 132 of the same volume 5.

MR ATHERTON: Yes.

MR JUSTICE HILDYARD: The thing is, to me it rather depends whether you are using the spectacles of limited companies or unlimited companies. Take the case first of a limited company:

"When a company is wound up every present, last member liable to contribute ...(Reading to the words)... payments of its debts and liabilities and the expenses."

Now, in the context of a limited company, we know that liability is actually capped --

MR ATHERTON: Correct.

MR JUSTICE HILDYARD: -- by the nominal amount of the share. But if you have a company where some of the share capital is paid in full and some not, it seems odd, doesn't it, that you pre-estimate in order to determine whether you should make a call? You should really make a call, shouldn't you, on their unsatisfied contractual liability to pay up to the nominal amount?

MR ATHERTON: Well, the anterior question, my Lord, is whether or not one needs to. If there are sufficient assets within the estate of the company, one doesn't need to make the call.

MR JUSTICE HILDYARD: Well, is that right? Or from the point of view of ensuring that the capital account, as it were, is made good, because you -- I can't remember

what the accounting treatment of an unpaid share is. I would have thought that was just an asset of the company.
MR ATHERTON: Well, I would say it is part of the capital.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: We will come to this in relation to issue 1. But I think --
MR JUSTICE HILDYARD: So it would really be a distribution to those shareholders if you didn't call it in, surely, in effect?
MR ATHERTON: Perhaps if we go to tab 143, my Lord. I am not sure we have looked at section 150 in any detail. This is where the ascertainment issue comes in:
"The court may at any time after making a winding up order, and either before or after it has ascertained the sufficiency of a company's assets, make calls on all or any of the contributories for the time being to the extent of their liability for payment of any money which the court considers necessary to satisfy the company's debts and liabilities."
Now, I read "ascertainment" as being definitive. But it is plain that the exercise of the power to make the call is linked to the necessity to satisfy the company's debts and liabilities.
MR JUSTICE HILDYARD: And for the adjustment of the right to

the contributories amongst themselves.
MR ATHERTON: Yes, of course. At the initial stage, one has to estimate what the liabilities are and then see if a necessary adjustment is made.
If the situation is that the liabilities are relatively small and the company's assets are relatively large, then it may be that you don't need a call.
The reality is, of course, if you are in liquidation then the assets are likely to be insufficient to meet the liabilities in which case, in all likelihood, you would need to make a call. This is why I think the old cases show that the liquidators come to court with estimates and evidence to indicate why the assets are insufficient and what the levels of liabilities are, in order that the court or the jurisdiction can be exercised.
MR JUSTICE HILDYARD: I really ought to know the answer to this, but I just don't, I am afraid.
Take the case of the limited company. Some of the shareholders are paid in full to the nominal amount of their shares, some have not. Let us take the first example, where the assets prove sufficient for the payments of it is liabilities.
MR ATHERTON: Yes.
MR JUSTICE HILDYARD: Normally, as I understand it, any

distribution of surplus will then be according to the stated nominal amount.
MR ATHERTON: Correct.
MR JUSTICE HILDYARD: But some of them will have paid the nominal amount and some not.
MR ATHERTON: That's right. I am sorry.
That is when you have the adjustment. You make the call against those who have not paid, in order that those who have paid do not take the entirety of the burden.
MR JUSTICE HILDYARD: If that is so, why didn't you do it first off? Because you are going to have do that in any event, either because there is a deficiency or because there would be a surplus and there is a need for an adjustment.
MR ATHERTON: But it may also depend on the amount of the call.
MR JUSTICE HILDYARD: Well, no. Well, they may, subject to the conditions of the limitation, but assume it is the usual limitation, capped at nominal value. Why do you have to make any pre-estimate? You are going to have to call that in, one way or the other.
MR ATHERTON: Because I think the situation is this: you do estimate the assets and liabilities, and that will dictate what level of call you may need to make against

those who have not paid the entirety of the shares. Because it may not be necessary to make a call against --
MR JUSTICE HILDYARD: I think that is my point: why? One way or the other, if there is a deficiency you are going to have to get them to pay up, insofar as they have not paid the nominal capital. If there is a surplus you are going to have to do it, in order that some shareholders shouldn't get a benefit denied others. One way or another, you are going to have to call up to the nominal. You know that, you don't need any estimate at all.
MR ATHERTON: In order to come to the conclusion that you need to call up all the unpaid elements from all the shareholders, then you will have had to undertake an estimate of the liabilities and the assets.
MR JUSTICE HILDYARD: Why? That is my point.
MR ATHERTON: Because there may be a situation where you estimate the liabilities and the assets and it only requires a certain level of contribution from those who have not paid, and then they will pay pari passu and make that contribution.
Now, if it turns out that there is still an element of unpaid -- and when you are doing that you may take into account any adjustment that you think is

appropriate to deal with shareholders. If at that point in time they are still insufficient, you can make another call. That was common ground as accepted by Lord Justice Briggs, that a liquidator can make more than one call, and the same would be true in the context of an unlimited company. But you estimate the balance sheet at what you think you will need. It may be an over estimate, it may be an under estimate. But that, I think, in my submission is the process and is indicated as being the appropriate course by reference to section 150.

MR JUSTICE HILDYARD: So you read 74 -- and this may be common ground for all I know. But when it says:

"When is company is wound up every present and past member is liable to contribute to its assets to any amount sufficient for the payment of its debts and liabilities."

You say that means its debts and liabilities as estimated from time to time and after the application of mandatory set-off.

MR ATHERTON: Yes. Yes, I do.

MR JUSTICE HILDYARD: So --

MR ATHERTON: I would go as far as to say that I don't think that is novel, in my submission.

MR JUSTICE HILDYARD: No, I just want to make clear that

that is what it means?

MR ATHERTON: Yes, because one is dealing with sufficiency. One is not simply saying: you owe all your money on the unpaid element of the capital, I want it all in.

To use a phrase that Mr Trower is fond of: it is a bit more nuanced than that.

I think that is borne out when one reads 74 with section 150.

MR JUSTICE HILDYARD: So I must rid myself of the notion -- which is in fact not a notion supported by any of you, so I ought to rid myself of it -- but there is a distinction between the obligation of any shareholder to pay up any amount uncalled on his share, up to the nominal value, and any other exposure to that contributory, under the provisions of section 74. It is all one unitary obligation.

MR ATHERTON: Yes. Yes, but it doesn't stop you coming back if there is more to be paid.

MR JUSTICE HILDYARD: Well, that is a question of estimation --

MR ATHERTON: Yes, exactly.

MR JUSTICE HILDYARD: -- and hindsight.

MR ATHERTON: Exactly.

MR JUSTICE HILDYARD: Yes, yes. Sorry, it is probably a very (inaudible) point. I think I have become

confused in my mind.

MR ATHERTON: You have certainly confused me, my Lord.

MR JUSTICE HILDYARD: Good. All right. Five, ten minutes.

MR ATHERTON: I am obliged.

(11.58 am)

(A short break)

(12.09pm)

MR ATHERTON: I am obliged, my Lord.

I wonder whether it may help just on what the issue we are dealing with if we went to tab 147, in bundle 5. This is section 154, which deals with the adjustment of rights between contributories. That may also indicate that one would, for example, make a call in relation to liabilities and then immediately before, if there were any surplus, one with then consider what the adjustment might be and, insofar as necessary, make a call in respect of adjustment, or indeed a potentially further call.

Now, the point, the bombshell that your Lordship left court on is the question: what is the limitation?

In unpaid capital cases the limitation is the element that is unpaid.

Now, your Lordship said, in the course of Mr Trower's submissions, if your Lordship has the transcript from day 1 again -- and I am sorry to jump

around. I apologise.

MR JUSTICE HILDYARD: Hold on. Yes.

MR ATHERTON: If your Lordship could go to page 74, and perhaps in fairness your Lordship should just read -- because I have highlighted the previous passages. If your Lordship starts at page 72, just if it helps the context, from line 23. This is Mr Trower to your Lordship, and then continue reading to page 74, line 6. Or maybe 8.

(Pause)

MR JUSTICE HILDYARD: Where down to?

MR ATHERTON: Page 74, probably line 9, my Lord. I think that draws it to a conclusion.

MR JUSTICE HILDYARD: Yes, okay.

(Pause)

Yes.

MR ATHERTON: I think that is the point that your Lordship was getting at. You have the obvious cap in the context of a limited company but, potentially, no cap in the context of an unlimited company.

MR JUSTICE HILDYARD: Mm-hm.

MR ATHERTON: The answer to that, in my submission, is that it is capped by reference to section 74 and section 150. You make the call against those members in an unlimited company in an amount which is, by reference to

section 74, sufficient for the payment of the company's debts or liabilities and then, by reference to section 150, by reference to what the court considers necessary to satisfy the company's debts and liabilities. So there is an inherent statutory cap and that again, in my submission, undermines the analysis that the outbound claim from LBIE to LBHI2 is full value, because you simply cannot say that that is a liability of the company. The value must be nil, we say.

The point I was going to make in support of that is -- and this is a point that Mr Arden made yesterday -- the ability to make calls, or the jurisdiction to make calls, it must be limited to the specified purposes of section 74 and section 150. Anything outwith that would be a wrongful exercise of the jurisdiction, or would be beyond the jurisdiction as prescribed by the two sections. Now, that, I think, was supported by Mr Arden's reference to the case of King v Tate.

MR JUSTICE HILDYARD: Just one moment.

MR ATHERTON: Of course.

MR JUSTICE HILDYARD: King v Tate was the one where effectively the contributories had a bit of a windfall --

MR ATHERTON: That's right.

MR JUSTICE HILDYARD: -- at the expense of the creditors.

MR ATHERTON: That's right. But the point was that you couldn't make a proof for a call for any more than was actually represented to the liabilities.

MR JUSTICE HILDYARD: Correct me if I am wrong, but what you are explaining to me is: once the insolvency process has begun, all liabilities are in accordance with an estimate. Their reality is no longer.

MR ATHERTON: That's right. Well, either they bear their value, where there is --

MR JUSTICE HILDYARD: Sorry?

MR ATHERTON: They bear their value, in terms of liability where there is no issue.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: Or contingent --

MR JUSTICE HILDYARD: If there is any reduction because of the exigencies of there being a deficiency --

MR ATHERTON: That's right.

MR JUSTICE HILDYARD: -- liability means estimate liability.

MR ATHERTON: Correct. Of course, with the benefit of hindsight, you are not precluded from making further calls or further estimations because one can take into account the hindsight principle.

MR JUSTICE HILDYARD: So the guarantee -- taking the question I asked Mr Trower -- is not of the actual liability but the estimated liability in the insolvency accounts?

MR ATHERTON: Correct. Correct.

MR JUSTICE HILDYARD: As estimated from time to time.

MR ATHERTON: Yes, indeed. Indeed, as set out in rule 2.85 of the Insolvency Rules.

MR JUSTICE HILDYARD: There is no difference in quality between the contractual obligation of shareholders to pay up on their shares in a limited company, and the uncapped, subject to statutory cap, liability of shareholders in unlimited companies.

MR ATHERTON: In my submission, yes. So there is that element of symbiosis. But, of course, the potential for liability is obviously at large in principle in the unlimited context, subject to the liabilities expenses of the winding up.

My Lord, just for your Lordship's note, if I could just pause there and go back to a particular issue, we spoke about dependencies, you spoke about dependencies with Mr Trower --

MR JUSTICE HILDYARD: I am so sorry.

MR ATHERTON: No, of course.

MR JUSTICE HILDYARD: It just shows my ignorance. In

a limited company, the reason why I think I rebel against the notion in any context the shareholders may not be as a matter of automaticity, as it were, called up to the nominal value is because otherwise they will in effect have achieved the issue of shares at a discount. So I have always imagined -- wrongly it seems -- that as to the nominal amount, they had to cough up in any event.

MR ATHERTON: The reality is, my Lord, they will always be required because otherwise you are probably in a solvent liquidation. So the reality is that the --

MR JUSTICE HILDYARD: That is what I am getting at. Whatever the situation. In a solvent situation, it is going to be unfair if they get a return at nominal having not paid it.

MR ATHERTON: No, but then before you distribute the surplus, by reference to section 154, there is an adjustment.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: To ensure that those who have paid in full are not bearing the burden.

MR JUSTICE HILDYARD: This is a notional adjustment.

MR ATHERTON: Well, it may have to be an actual adjustment that comes in to ensure the full surplus, or those who haven't paid -- it may be a bit like the rule in

Cherry v Boltby, where you make a contribution and then you share out in the distribution.
MR JUSTICE HILDYARD: Yes. That is another facet of my surprise that you have to estimate before you call in a limited company, but there we are. That is the rule, is it?
MR ATHERTON: Well, in my submission that is what the principle, or the regime required or set out in the Act, by 74, section 150. As your Lordship is intimating, the reality may be very different.
In the old cases, of course, one had very large unpaid capital. That was just what happened. Then, I think the position was in 1865, when there was in the UK and Europe a form of depression or recession, that is when all of these companies started to collapse and all these liabilities for unpaid capital were being called in; that led to a change whereby you had your £1 share and you paid your £1, so there was a difference in --
MR JUSTICE HILDYARD: You are still allowed to issue shares unpaid, aren't you, in a private company? In a public company it has to be 25 per cent paid at the very at least.
MR ATHERTON: That's right, yes.
MR JUSTICE HILDYARD: And it has to be paid in cash, or cash equivalent. I thought those were sort of maintenance of

capital and the whole thing was cohesive, in the sense that as to that element of the exposure of a contributory they would never, in any circumstance, be allowed ultimately not to pay up.
MR ATHERTON: I don't think I am disagreeing with your Lordship. I think the process of call and adjustment, whether in an insolvent liquidation or a solvent liquidation. Which is the purpose of this, of these contributory rules -- if I can use it in a non-technical sense -- as provided for by the Act, are there to ensure that the losses in the company are borne equitably as between the membership. That is the objective, the goal.
MR JUSTICE HILDYARD: Anyway, it may not matter because you say we are dealing with an unlimited company in an unlimited context. The guarantee, the exposure of the contributory, the unlimited contributory is in respect of the estimated liabilities of the company from time to time, after the application of mandatory set-off.
MR ATHERTON: Yes, my Lord.
MR JUSTICE HILDYARD: That is that.
MR ATHERTON: Yes. I don't personally, or in my submission that is not heterodox or antithetical.
MR JUSTICE HILDYARD: No. In a sense, that is a sort of simple way through from your point of view. You accept

the nil valuation on the one side, you say it can't be more than that on the other side, and there we are.
MR ATHERTON: That's right. That's right. But before I leave this issue, if your Lordship has concluded interrogating me on that.
MR JUSTICE HILDYARD: No, I am sorry.
MR ATHERTON: All I was going to say to your Lordship is you were discussing dependencies with Mr Arden yesterday, and with me -- excuse me.
I am sorry, my Lord, Lord Justice Briggs, at paragraph 164 and 198, makes the point that in relation to currency conversion, they are not contingent liabilities. They are full blown actual liabilities, crystallised liabilities, of the company. At paragraph 198, he essentially makes the same point about statutory interest. So they are the points I was making, they are crystallised, actual liability of the company from the outset, so they are not contingent and they are not, in relation to the currency conversion claims and statutory interest, they are already crystallised. They may have to be subject to calculation, but they are not contingent.
MR JUSTICE HILDYARD: So on the findings of the Court of Appeal, the unlimited shareholders are liable for that, are they?

MR ATHERTON: Yes.
MR JUSTICE HILDYARD: In full?
MR ATHERTON: Yes. Correct.
What Mr Trower says is that we are seeking to hide behind the trickle down. If it doesn't trickle down, we are not liable. That is plainly not correct, because where the liabilities are in the waterfall, they are liabilities and a call can be made. Absolutely. The reason Mr Trower's articulation of what our position must be is flawed is because it derives from the mischaracterisation of the contingency in the context of the waterfall.
I did say to your Lordship that there may be a circumstance where one has to bite the bullet in a case like this. I am just trying to provide a sort of logical conclusion as to where one might go in this case.
Now, your Lordship was taken by Mr Arden, yesterday, to Danka case. That provides an illustration, in the sense that if you have a contingency, which may or may not fall in -- and that was the contingency on an indemnity, so it is much more straightforward, I accept that -- it is not appropriate for the office holder to simply sit there and wait to see whether the contingency falls in, because that would really just

prolong the process. The whole point about estimation, the point about set-off, within the pari passu principle, is to draw a conclusion to the process and allow the distribution to take place as quickly, efficiently and as fairly as possible.

Now, your Lordship may recall Lord Justice Patten said, "Well, waiting for the contingency to fall in is not estimation, and you are not obliged to keep a fund open against which proofs can be made in relation to contingency, you have to bite the bullet". That is that. Apply that reasoning -- which must be right, and I don't think anyone would dissent from that -- to this case. In my submission the way in which the administrators could crystallise this issue is by placing an estimate on the inbound and the outbound claims. Either at nil, so there is not actually anything set-off, but that is the issue, that deals with it, because either there doesn't seem to be any prospect of the contingency falling in or if it does fall in, it won't fall in for several years. Remember in the context here, that these issues are sought to be determined in order to allow a release of funds which have been locked into the process for several years now, not least because of the complexity of the competing interests. So it might be that they either say nil, or

in order to, as I said, cut the Gordian knot, simply place a value on it. It may be a notional value. I don't know, but what that points towards is the, if you like, commonsense approach is that adopted by Lord Justice Lewison in taking a nil value rather than putting some value on it, which may or may not compromise the subordination and therefore give LBHI2 a benefit which, by reference to its subordinated status, allows it to participate in a way which was never intended.

MR JUSTICE HILDYARD: At the risk of being a dog with a bone, when Lord Justice Lewison says, "One would expect", is he saying that as a matter of law it is nil or is it a matter of his practical experience or anticipation that it is nil? And are you saying: that may be right, it may be wrong; it would depend on the liquidator?

MR ATHERTON: I don't think that one is concerned with it as a matter of law. I think one is concerned with it as a matter of estimate, in the circumstances.

MR JUSTICE HILDYARD: So it would be consistent with what Lord Justice Lewison says to adopt, broadly, the following: I mustn't take into account the economic factors as such.

MR ATHERTON: Yes.

MR JUSTICE HILDYARD: The contingency is wrapped up in the solvency issue.

I don't agree with Lord Justice Lewison that it is nil, I am going to say it is ten or whatever it is.

MR ATHERTON: But your Lordship doesn't actually have to make that.

MR JUSTICE HILDYARD: I know, but I am trying to work out whether it is all wrapped up in the contingency or as a matter of law, or it is merely a process of estimation.

MR ATHERTON: I am not a statistician, but it may be that an actuary or a statistician could place a value on the contingency. With all of the relevant information, what are the prospects of all prior ranking claims being paid?

My Lord, would it be convenient for me to move on to a different topic?

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: I was now going to just deal, briefly, with the paragraph 63 issue of Mr Arden's --

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: -- skeleton argument.

Now, I think the way Mr Arden dealt with it, if I might say so, sort of deals with it. The simple fact of the matter is that set-off, as a matter of English

insolvency law, heritage and policy, is considered to be, when dealing with mutual claims, the best way of manifesting the pari passu principle. So set-off is an element of pari passu, not anti-deprivation and therefore, on the basis of the discourse that you had with Mr Trower, it is not capable of being abrogated. That is clear from the NatWest Bank v Halesowen case, which I am sure your Lordship is familiar with. Does your Lordship want me to take you to the authority?

MR JUSTICE HILDYARD: Perhaps you had better, just in case.

MR ATHERTON: Yes, of course.

MR JUSTICE HILDYARD: I mean, it was mentioned by Mr Arden.

MR ATHERTON: Yes. I don't think it is controversial in terms of actually establishing the principle.

MR JUSTICE HILDYARD: No.

MR ATHERTON: It is in bundle 2, at tab 61. I don't think one needs to go to the headnote, but what I would ask your Lordship to go to is page 802 and the speech of Lord Dillon. The analysis starts at just below E, the paragraph beginning:

"In the Court of Appeal ..."

Just so your Lordship gets the whole process, if your Lordship wouldn't mind reading through to 805, just above E.

MR JUSTICE HILDYARD: Okay.

MR ATHERTON: I think that will deal with that particular issue.

(Pause)

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: I am obliged. For your Lordship's note, Lord Simon of Glaisdale concurred, at page 808F through to 809B, as did Lord Kilbrandon, at 823 to 824. There was a dissent from Lord Cross of Chelsea at 818A to B.

My Lord, the same principle, by reference to the Halesowen case, was applied in the MS Fashions case in the Court of Appeal. Again, for your Lordship's note, that is bundle 2, tab 68 and it is Lord Justice Dillon at page 446. That establishes the principle.

Your Lordship went to clause 7B this morning with Mr Arden, and we therefore say it is put in terms by LBIE in response to the iterative process that Mr Arden is embarking upon in paragraph 63 by saying that is not what we or LBH suggest is the position, but it is testing what would happen if LBIE's postulated position was correct. We, when we read, or when we were considering LBIE's position, came up with essentially the same analysis, albeit that we say the analysis would arise earlier, because of course the contingency, which the payment of the sub-debt is subject to, is not, as suggested by Lord Justice Lewison, the payment of prior

ranking liabilities. It is the ability of LBIE to pay prior ranking liabilities.

It is a difference not of substance. Rather than, as Mr Arden says, there would have to be a repayment of dividends, we would say that when you put in your proof and you work out what the dividends are, you will work out if the dividend is such from LBHI2 that you would become able to pay the prior ranking liabilities, the consequence of that would be there would then be a set-off in terms of the two claims. You would be able to work it out, and there wouldn't be any payment anyway because of the set-off that arises by reference to the two cross claims as between LBIE and LBHI2. Therefore rendering LBIE back in to the position that it is not in fact able to satisfy the prior ranking liabilities. But other than that small divergence, we agree with the analysis.

Your Lordship may find in the correspondence bundle -- and I am not suggesting we go to it now -- for your Lordship's note: this point was first raised by LBIE by letter to Mr Arden's instructing solicitors, Dentons, on 27 January 2017. That is in the correspondence bundle, at divider 10. Then, the response, which for LBH's part we endorse, is by letter from Dentons of 30 January 2017, in the same bundle, at

divider 12. It is couched in terms, by LBIE, that LBHI2 is seeking to set-off. That is not the position. The position is that set-off would arise automatically and on a mandated basis by reference to rule 2.85. So the attempt to preclude that mandatory process by reference to a contractual term, as set out in the sub-debt agreement, as we say four square in opposition to what the House of Lords held in the Halesowen case.

My Lord, I have finished, I think, on issue 3. I was then just going to go and deal with issue 7.5, if I might. I am obliged.

I think I can take this, hopefully, slightly quicker, but I think it is important to remind oneself of what the issue is because, in my submission, LBH is the only party that has actually answered the question that is posed.

The issue is whether the LBHI administrators should be directed to assert less than 100 per cent of the contribution claim against LBL and/or LBHI2 and, if so, by how much the contribution claim should be reduced as against LBL and/or LBHI2 and what factors should the court take into account in reaching its decision.

The first point I make is that the question is posed and directed towards the position in administration, not in liquidation. We say that the answer to the question

follows on from the submission that I have made and that Mr Arden has made -- I am jumping ahead slightly, but in direct answer to the question -- should be that the LBIE administrators should be directed that they are not to make a contribution call against either LBL or LBHI2. We say that is the corollary of the position as postulated by LBH, LBHI2 and I think LBL.

Now, the logically anterior question is whether or not the court has the jurisdiction to direct the administrators to do anything. We say that is tolerably clear and, again, I don't think it is necessary for me to take your Lordship to any of the authorities on this because I don't think it is controversial.

First, it is quite plain that an administrator is an officer of the court and, therefore, subject to the supervisory jurisdiction of the court; that is made clear in the Atlantic Computer case, just for your Lordship, at page 529. That is at bundle 2 of the authorities, divider 67.

Now, there is a further aspect to the supervision of the court in respect of an administrator. That is paragraph 74 of schedule B1, which I am not sure is in the bundle. That allows relief to be granted where -- does your Lordship have it? That is great. I am grateful for that.

Your Lordship will find it in Sealy & Milman, at page 653, if you are in the same edition. So where the administrator is acting, or has acted so as to unfairly harm the interests.

Just for the transcript writer that is F-A-I-R-L-Y, not F-U-R-L-Y. It's just my accent, everyone writes it down, they think I am saying "fur" when I mean "fair".

That is a further aspect of the ability of the court to grant relief in relation to an administrator, specifically.

The third aspect is as was applied by Mr Justice David Richards in another of the Lehmans related case, which is Lomas v Burlington Loan Management, which your Lordship will find at bundle 4, divider 101. There is an exposition of a principle, at paragraphs 174 to 183.

That is quite an interesting case, where, amongst others, certain creditors, including currency conversion creditors, had entered into settlement agreements. On one construction of those agreements, it would appear or it was suggested that the currency conversion creditors had waived their claims. Mr Justice David Richards found that in fact on the proper construction of the agreements that didn't happen, but if that was the proper construction, he would have precluded the

administrators from relying on their strict legal rights by reference to that construction, such that they wouldn't be entitled to say that the claims had been waived.

MR JUSTICE HILDYARD: This was on ex parte James grounds, was it?

MR ATHERTON: That's right, yes.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: It comes down, in that context, to the office holder having to be more honourable than the most honourable person, if I can put it that way. There is a much higher threshold of conduct.

It wasn't suggested in the case -- just as it isn't suggested here -- that the administrators in that case were doing anything wrong. It was simply a question of: if that construction had obtained, then the judge would have precluded the reliance on that construction by the office holder, even though it was strictly in accordance with the legal rights, if that had been the interpretation.

It is right therefore, we say, that in this context, where we are in administration, arguably, the ability of the court to control the conduct of the administrator is wider than it might be in relation to a liquidator.

The reason I say that is because in a liquidation

one is dealing strictly with the ability of the liquidator to make calls under section 74 and section 150. Your Lordship heard from Mr Trower about the use of the word "may". I think we accept, it is not a discretion which is boundless, but it does give the court the ability to exercise some discretion as to the amount of the call, and the timing of the call. It may even allow you to make unequal calls. I think that Mr Arden accepted that this morning. It may be that in the exercise of any power over the administrators, in any given case, the court would exercise its supervisory jurisdiction by reference to the proscriptions or the ambit inherent within section 74 and section 150. The reason why this has resonance in this case is because of the position which has been adopted by the administrators of LBIE as regards the valuation of the outbound claim into the administration of LBHI2.

We say either it is wrong, for the reasons that I have sought to develop this morning, in which case the reality is: if your Lordship found that it was wrong, then it wouldn't be pursued by the administrators. I have no doubts about that. But, in theory, your Lordship could direct that they were not to make any contribution claim as against LBHI2 or LBL, either because it wasn't within or for the purposes of

section 74 or anything like a notional equivalent, or because arguably, notwithstanding that they were correct -- and your Lordship doesn't have to make this determination -- it could be considered to be unfair as regards the contributories. Bringing into either ex parte James and/or the --

MR JUSTICE HILDYARD: Ex parte James isn't a sort of general palm tree, is it?

MR ATHERTON: It is often used like that, I accept, but I am trying to --

MR JUSTICE HILDYARD: But, I mean, in Mr Justice David Richards case, there was basically a case of estoppel.

MR ATHERTON: Yes.

MR JUSTICE HILDYARD: The question was if the court should give effect to estoppel by, in the particular context, invoking the ex parte James rule.

MR ATHERTON: Yes.

MR JUSTICE HILDYARD: But that is not a sort of general wand of what I think might be fair or practical, or anything else. I mean, it has to have some legal or equitable footing, hasn't it?

MR ATHERTON: Well, Mr Justice David Richards puts it on the ground of unfairness and says that is a recognised concept in English law and it is essentially the same,

because he said he would have applied paragraph 74.
MR JUSTICE HILDYARD: But he had the benefit of the fact that it fitted neatly, didn't it, in to the general concept of estoppel?
MR ATHERTON: I think that is probably fair in the circumstances of the case. I don't disagree with your Lordship that it is often a refuge for --
MR JUSTICE HILDYARD: It has to have limits is the point about ex parte James.
MR ATHERTON: Yes, of course.
MR JUSTICE HILDYARD: Or it does descend into arbitrariness.
MR ATHERTON: I quite agree. For these purposes, I am simply seeking to submit that when the court has jurisdiction to direct the administrators as to their conduct, it is either, insofar as they are different, by reference to the court's supervisory jurisdiction, generally over its officers, or it has tangibility by reference to paragraph 74 in the context of an administration under schedule B1, or by reference to ex parte James. So your Lordship has those tools, if you like.
MR JUSTICE HILDYARD: But in no way must I depart from the statutory scheme, must I, unless there is some legal or equitable footing for doing so?
MR ATHERTON: Correct, I agree. I agree with that.

It may be that if one were to consider it appropriate to control the conduct of administrators in any given case, in the context of calls being made or contingent proofs being made by reference to what a liquidator could do in a liquidation, then one might apply the ambits of section 74 or section 150, but I would submit that that may not necessarily be the case.
In this case, we say the circumstances are such that either the contribution claim made by the administrators does not fall within section -- or if they were a liquidator would fall within section 74 and section 150. Therefore, your Lordship could direct them not to make this call or --
MR JUSTICE HILDYARD: Mustn't you win on the law, or not at all, on this point?
MR ATHERTON: I think the answer to that is -- and your Lordship doesn't have to make the determination -- but as a matter of principle if what the administrators were seeking to do was strictly within the conduct which was entirely consistent with the strict legal rights, if there was a basis for challenging under paragraph 74 schedule B1, and if the relevant criteria in ex parte James was satisfied, then your Lordship could use those tools to control that conduct.

MR JUSTICE HILDYARD: If.
MR ATHERTON: Yes, of course.
MR JUSTICE HILDYARD: What is the factor in the hypothesis which you have to deal with, which is whatever reason you have not satisfied me on the law that I can say, "Well, hang the law, I think it is fairer that I should do something else"?
MR ATHERTON: I am not going to convince you, I don't think, that I have an answer to that question. One suggestion might be the fact that what we say is occurring here is the impermissible intervention or injection of the contributory rule into the administration. Or an attempt --
MR JUSTICE HILDYARD: But if that is the effect of the law, that is the effect of law.
But, anyway, I can think about it. You can probably tell that when one feels that ex parte James is being used as an outrider to specifically identified points of law equity, I think I might be very anxious about it.
MR ATHERTON: I accept that. Obviously, as I have said to your Lordship, I am not asking your Lordship to exercise the jurisdiction.
MR JUSTICE HILDYARD: No.
MR ATHERTON: I am simply saying that they are the tools that allow you to control an administrator, and that is

what the question posits.
MR JUSTICE HILDYARD: It shows how a court in an administration can give teeth, for example, to an equity or an estoppel.
MR ATHERTON: Indeed. Indeed.
MR JUSTICE HILDYARD: Without it having to be asserted by a separate action, or anything else. It just takes a view an estoppel exists, I am going to direct the administrators to abide by it.
MR ATHERTON: That's right.
MR JUSTICE HILDYARD: There is no more than that?
MR ATHERTON: I think that is probably right, yes.
In direct answer to the question, your Lordship could direct the administrators not to make the contribution claim they are seeking to make, but that would be on the basis that it would be wrong as a matter of law, on the basis that has been put forward by myself and Mr Arden. In which case, the reality is that your Lordship wouldn't have to make the direction --
MR JUSTICE HILDYARD: That's right.
MR ATHERTON: -- because the administrators would not operate on that.
MR JUSTICE HILDYARD: I think it is law or nought, really, unless you have some particular estoppel or other legal or equitable right.

MR ATHERTON: Very well, I am content to accept that.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: It is just after 10 to, I was going to move on to issue 1, but it would be convenient to me if we started just before 2 o'clock if that is convenient to everybody else?
MR JUSTICE HILDYARD: Does that suit everyone? Five to two?
MR ATHERTON: I am obliged.
(12.52pm)
(The luncheon adjournment)
(2.00pm)
MR TROWER: My Lord, there is a new file that has an appeared on your desk. That is the cases.
MR JUSTICE HILDYARD: Thank you very much.
MR ATHERTON: I don't know about you, my Lord, but I am now regretting turning to contractual construction on a Friday afternoon, but there we are. That was my fault.
MR JUSTICE HILDYARD: I am sure you will enliven it.
MR ATHERTON: What your Lordship will need from the outset is volume 4, divider 1, which is the agreement. It does seem an age ago, although it was only earlier this morning, that Mr Trower was addressing you on this point. My Lord, I think we can go to page 10 of the bundle, which is the subordination provision.

Our basic proposition here is that by reference to the specific wording of the clause, particularly the use of the word "it" and "solvent", which we say has been used to convey a particular notion, the consequence of this clause, on a fair interpretation, is that insofar as LBIE, in order to pay prior ranking claims, those ranking in priority to the subordinated liability, insofar as it has to have regard to or recourse to a call by a liquidator, or the contingent claim of an administrator to the same effect as against its members, it can never be solvent for the purposes of this clause.

Now, we say the consequence of that is essentially, therefore, notwithstanding if as a consequence of that call LBIE is capable of being able to discharge its prior ranking liabilities, the subordinated debt never becomes payable.

Now, Mr Trower in his skeleton argument, and to an extent in his oral submissions, immediately jumped in and says, "That interpretation creates or is contrary to business commonsense, commercial commonsense", for two reasons: (1) it means, as I have just submitted it means, the sub-debt is never payable, that is contrary to business and commercial commonsense, and (2) because the prior consequence is you cannot apply any call in

repayment of prior ranking liability.

In relation to that second point, that is not what was submitted and that is not what we say is the consequence of our interpretation. If the call is made and assets are acquired, and I use that in the loosest sense, funds are required as a consequence, then they may very well be used to pay prior ranking liabilities and they may or may not be sufficient in order to discharge them. If they are not, the sub-debt is not payable. That is how the clause is intended to operate.

However, if they are, notwithstanding that those liabilities have been paid, within the meaning of the clause the sub-debt isn't payable.

We say that Mr Trower's application or utilisation immediately of business commonsense, commercial commonsense, he was a bit ruder than that in his skeleton, I think he was suggesting we were being absurd, but that is neither here nor there. In doing it that way he has come in too early, if I can put it that way, by the application of business commonsense in the course of the iterative process which is the construction of the agreement, and also gives too high a profile and too much emphasis to business commonsense, or commercial commonsense. To some extent, we say that, in any event, the notion of whether or not my

construction of the agreement is a matter of business commonsense or not is ameliorated. Its relevance is substantially reduced given the regulatory context in which this agreement sits. I don't think there is any dissension that it does sit in a regulatory context, and that I think was accepted by Mr Justice David Richards at first instance, where he said it was appropriate to consider it in its regulatory context. Insofar as there is any absurdity in the context of the way this agreement is said to work on our analysis, it is the progeny of LBIE's treatment of the outbound sub-debt contribution claim in relation to issue 3. That is what creates the difficulty, we submit. It is not a consequence of the construction that we place upon it.

We also question in our position paper, and in our skeleton argument, the extent to which this issue actually had any resonance in this particular case. The answer is it does have resonance because of the way LBIE answer the question in relation to issue 3.

Now, we say that the starting point for any contractual construction are the words themselves. One criticism that Mr Trower makes is that he says that we are trying to restrict the meaning of the clause. We would counter that by saying what Mr Trower is seeking to do is inject into the clause something that is not

there. So if we go to the clause, we say, on its face it is plain what the meaning is intended to convey. The borrower being solvent, pausing there, it is in inverted commas. The use of the word "solvent" we say is deliberate in order to convey a particular notion. Essentially, the company can pay its liabilities. It can pay its liabilities. It is in inverted commas because it is not a pure solvency test as per, for example, section 123 of the Insolvency Act, because you take out of account subordinated liabilities, obligations which are not payable or capable of being established in any insolvency of the borrower and excluding liabilities as defined. That is why its in inverted commas.

So:

"The borrower being solvent at the time of and immediately after the payment by the borrower and accordingly no such amount which would otherwise fall due for payment should be payable except to the extent the borrow could make such a payment and still be solvent."

So the word is used again. Sub-clause 2:

"For the purposes of sub-paragraph 1B, the borrower shall be solvent if it is able to pay its liabilities other than subordinated liabilities in full,

disregarding the liabilities set out in A and B."

We say that is perfectly plain, on its face, which means LBIE must be able, from essentially its own funds, not by recourse to its membership, be able to discharge the liabilities. So you are not looking at the ability of LBIE, or a liquidator, to make a call on its shareholders.

Now, Mr Trower said, "This clause does in the deal with the source from which the liabilities of the company are to be paid". We say that is not correct. The source is LBIE. That is the source of the funding. We say that there is nothing novel or contrary to any notions of commonsense, business or otherwise, in that construction. Indeed, we indicate, or we submit, that it is entirely consistent, for example, with the terms of section 74 and section 150.

I am sorry, but perhaps, just to make that point, or illustrate it rather more clearly, if we could go to bundle 5, tab 132. Section 74.1:

"When a company is wound up every present and past member is liable to contribute to its assets to any amount sufficient for payment of its debts and liabilities."

So what that clause envisages is not the fact, for example, that the call is an asset, but it is a source

by which one can contribute to the assets. Then if you go to --

MR JUSTICE HILDYARD: I don't follow that. Why is not the chose in action as much an asset as any other asset?

MR ATHERTON: I am sorry, my Lord, could you repeat that please? I am sorry.

MR JUSTICE HILDYARD: Why is not the chose in action, conferred by section 74, just as much an asset as any other chose in action?

MR ATHERTON: There may be a difference in whether it is unpaid capital or an unlimited company, in our submission. If it is unpaid capital, there is a chose in action. There is a debt already there. Section 80 says:

"The liability is created upon the accession to membership and can be enforced as a debt."

Now, that gets you into another question which is addressed in the Court of Appeal. I will take you to it, the Court of Appeal. The fact that section 80 creates, in effect, the notion of a debt. It is a statutory construct, in my submission. Therefore, one doesn't have to hunt around for a creditor.

MR JUSTICE HILDYARD: Why do you say its a statutory construct? I mean, the source of it is the fact that the liability has not been limited. The pledge given by

each shareholder in an unlimited company operates in contract and is enforceable by statute. But the source is a promise, "I will stand by, to the last farthing, the operations of this company. I promise. And in return for that I get a share in your company". Why is that not a chose in action?

MR ATHERTON: I am not doubting that it is.

MR JUSTICE HILDYARD: But then it includes that, doesn't it? Its assets include that asset.

MR ATHERTON: First of all, we say that, in the context of this clause, it can't have been contemplated that what it would include is the ability of a liquidator to make a call and have recourse to its members. That can't be what was intended by this. Therefore it can similarly not have been intended that the funds which are available by reference to the clause to make the company solvent, one could have regard or would ever have contemplated the notion that an administrator would be able to bring a contingent proof or claim in respect of the call.

I accept what your Lordship says, but then one gets into the issue and we try and separate it out. In our submission, the construction of the clause, one doesn't have to ascertain whether or not something is an asset or not. But we say when one understands what is or

isn't an asset, and whether or not these calls are an asset of the company, that serves to bolster our construction.
MR JUSTICE HILDYARD: Just so that I know that I am on the right page, your point is this, isn't it: this particular promise is in effect, "I promise if called upon by a liquidator in an insolvency to pay"?
MR ATHERTON: Yes. All we are saying is, here, a call can be made in respect of the prior ranking liabilities. If those prior ranking liabilities are paid through that call, if that results in them all being paid off, it doesn't result, for the purposes of the provision, insolvency such as then brings into play --
MR JUSTICE HILDYARD: Well, that is the consequence.
MR ATHERTON: That's right.
MR JUSTICE HILDYARD: I am just trying to get into the "it" point.
I mean, this resonates with me for this reason: that I have always in my mind drawn a distinction between the contractual promise to pay up shares and the contractual exposure which can only be brought home by a liquidator in certain contexts. But you were, I think, dissuading me from that before the short adjournment. You were wanting to see them as unitary.
MR ATHERTON: I don't resile from that position. It

possibly being slightly more equivocal than I was submitting, but I don't think what I was submitting was incorrect.
MR JUSTICE HILDYARD: The amount unpaid on an issued share is absolutely, undoubtedly an asset of the company.
MR ATHERTON: Agreed.
MR JUSTICE HILDYARD: It is simply a deferred payment of that which is already due by all the other shareholders and, if it weren't, it would be a reduction in its capital.
MR ATHERTON: I accept that.
MR JUSTICE HILDYARD: It is absolutely plain.
MR ATHERTON: I don't dissent from that.
MR JUSTICE HILDYARD: So it is a slightly different quality to the exposure which a liquidator can enforce.
MR ATHERTON: Indeed. Exactly right. Exactly.
MR JUSTICE HILDYARD: But you say as to both -- I am sorry to harp back.
MR ATHERTON: No, no, of course not.
MR JUSTICE HILDYARD: But you say as to both that you cannot enforce either, except after estimation and the application of mandatory set-off. I thought that was an important part of your point before the short adjournment.
MR ATHERTON: It is. I think it is brought out in, I think,

Webb v Whiffin, where you had a huge unpaid capital element. I think it was £100 unpaid -- ordinary shares of £100, £10 were paid.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: What the court was applying there was the then equivalent of section 74. The call was not for the £90, it was for, I think, £30 because that was the basis of the estimate which the liquidators had put in, in order to justify the call before the court. So the court was applying the section 74 process within the context of the winding up.
Now, it may be, for example, if a call has been made on unpaid capital pre-liquidation, that just has to be paid to the liquidator.
MR JUSTICE HILDYARD: So liquidation diminishes, does, it or could diminish, the contractual promise to pay the nominal value?
MR ATHERTON: Well, I think the way I would answer that question is by again referring to the process that was begun through by Webb v Whiffin.
On your Lordship's analysis, with respect, what the liquidator could or should have done is said, "I want the £90". They didn't do that, because it may have been that prior to that the company could have called in under the Articles before that, but by applying the

section 74 process, the statutory process, they were making an estimate, putting on a value, in order to justify the call that was being made. That was less than the full amount --
MR JUSTICE HILDYARD: Was it in the House of Lords?
MR ATHERTON: Webb v Whiffin was, yes. It was. There wasn't any query about -- I don't think any of their Lordships --
MR JUSTICE HILDYARD: They are very different. Who am I to say, the House of Lords decided, but they are different, very different.
MR ATHERTON: I agree, I will be relying on the difference when I come to look and what Lord Justice Briggs says in Waterfall I in the Court of Appeal. My learned friend, Mr Trower, sought to put it in the course of his submissions, which I now can't find. If your Lordship just bears with me. Yes, if your Lordship has the transcript for day 1.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: Please. If your Lordship looks at page 55, line 11, through to 56, line 24, please.
(Pause)
MR JUSTICE HILDYARD: Well, Mr Trower says they are all assets of the company, both the exposure and the commitment are assets of the company.

MR ATHERTON: Well --
MR JUSTICE HILDYARD: You say the exposure is -- query -- not, because it only arises and is enforceable in the event of a liquidation by a liquidator.
MR ATHERTON: That's right. I am sorry, my Lord.
MR JUSTICE HILDYARD: You therefore say it is not part of its assets. Of "its", the corporation's, assets.
MR ATHERTON: That's right. So if I was tracking Mr Trower's submission, where he says, in line 8, on page 56, "it" , what he actually means is: such entitlements, including such funds as may be generated by a liquidator through the specific means of making a call against its members.
That is what he means. We say that meaning can't possibly be incorporated without doing violence to the terms of that provision in the contract.
MR JUSTICE HILDYARD: You are going to show me, are you -- or do I have this wrong too? -- that Lord Justice Briggs draws the same distinction? Because I thought Lord Justice Briggs said it was all assets?
MR ATHERTON: Well --
MR JUSTICE HILDYARD: Or have I misunderstood that?
MR ATHERTON: That is what Lord Justice Briggs does say.
MR JUSTICE HILDYARD: Right.
MR ATHERTON: We say he is wrong to have said that, and

Lord Justice Lewison says that in an unlimited company calls, the ability to call, the proceeds of a call, are not assets of the company.
MR JUSTICE HILDYARD: They are not assets, unless they relate to that part of the call as reflects the outstanding amount on the promise to pay the nominal amount.
MR ATHERTON: Lord Justice Lewison's observations were made specifically in relation to unlimited companies.
MR JUSTICE HILDYARD: I see. I am sorry.
MR ATHERTON: We will come to it, because if I might respectfully say so, your Lordship made the same comment when Mr Trower was making submissions and, with respect, you had it the wrong way round.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: Lord Justice Lewison says in an unlimited company there can't be assets.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: It may just be a nomenclature issue that we don't have to deal with, but it might be more accurate. I know all the judges talk about assets. It may be the accretion to the funds available, whether it is unpaid capital or whether by contribution in an unlimited context, are actually capital rather than strictly so-called assets, insofar as there is a difference.

MR JUSTICE HILDYARD: Even an unlimited share has a nominal amount, doesn't it?
MR ATHERTON: Yes. But I don't think that makes any difference to our analysis, with respect, my Lord.
Would it help -- I am sure it won't, but I will try.
In bundle 1, my Lord, if you could go to tab 44, please. That is Birch v Cropper, the Bridgewater Canal case. Could your Lordship go to, please, page 543 of the speech of Lord MacNaghten, and I think it is about two-thirds of the way down, the line beginning:
"Every person who becomes ..."
MR JUSTICE HILDYARD: Hold on, sorry.
MR ATHERTON: I am sorry.
MR JUSTICE HILDYARD: No, no. Yes, we had a look at this, didn't we?
MR ATHERTON: Yes. Just go over the page, to the first line of 544. It is a limited company but the analysis must be stronger in the context of an unlimited company.
MR JUSTICE HILDYARD: So do I have it right? What the House of Lords is saying is liquidation works at change in the nature of the shareholders' liability. It becomes, after liquidation, in both contexts of a limited and unlimited company, a unitary obligation to pay up either with or without limitation, depending on what sort of company it is.

MR ATHERTON: That is my understanding of what the House of Lords say. Yes, my Lord.
MR JUSTICE HILDYARD: So there is an exchange. Before liquidation all you have is the promise to pay out to the nominal amount. It is contractually enforceable at the say-so of the directors and it is an asset to the company accordingly.
After liquidation, that element is swamped, goes, transmogrified into a unitary obligation enforceable only by the liquidator.
MR ATHERTON: That's right, correct. Within the ambit and context of section 74 and section 150.
MR JUSTICE HILDYARD: Yes, subject to --
MR ATHERTON: Absolutely. That is certainly my understanding and that is certainly my submission, my Lord.
Now, if, I think your Lordship can put that particular bundle away. I just wanted to go back to section 74, please. We are back in bundle 5, tab 132, and I just wanted to take your Lordship to, in 74, to E, which again we have been to before.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: In the third line:
"Policy or contract is restricted ... or whereby the funds of the company are alone made liable in respect of

the policy or contract."
So what the section there is drawing a distinction between, the funds of the company and the ability to call and the proceeds of the call. We say that is plainly designating, or having in contemplation that there is something different. We say the same is true, that chimes with the wording of section 150, which your Lordship will find at divider 143.
MR JUSTICE HILDYARD: I am not to try and work out whether there is any difference between funds and assets?
MR ATHERTON: For these purposes, I don't think it matters. What it's drawing a distinction between is the corpus available to the company, whether one calls them funds and assets, and the adjunct or the potential accretion to that fund or those assets represented by the ability to make an call and the proceeds of the call. In 2E it is drawing that distinction. Then, in my submission, we have the same delineation, in section 150, sub-section 1, where it says:
"The court may at the time, after making the winding up order, either before or after it has ascertained the sufficiency of the company's assets ... "
MR JUSTICE HILDYARD: I am so sorry, where are you looking now?
MR ATHERTON: I am so sorry, my Lord.

MR JUSTICE HILDYARD: It is my fault.
MR ATHERTON: Section 150, divider 143. The same bundle, it is divider 143.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: So if your Lordship has regard to section 101 ...
MR JUSTICE HILDYARD: So you say the reference in line 2 to "assets", means assets before called.
MR ATHERTON: Correct. So there is a delineation again between the sufficiency of the company's assets and the accretion or swelling of the fund by the making and honouring of a call.
We say that our construction of clause 5 chimes with that delineation, so there is plainly something different between, as your Lordship put it, the corpus of the company at that point in time, pre-liquidation, and then subsequently. We say this is borne out by how it was phrased by Mr Justice Lewison at first instance. Can I just park that for the moment, because I want to do the analysis of the Court of Appeal and where they came to on this as a separate topic, if that is convenient to your Lordship.
MR JUSTICE HILDYARD: Absolutely.
MR ATHERTON: I am grateful.
We also say that the clause, in the appropriate

context, actually does show you what the source is; that context is by reference to the relevant regulatory position that the company is in, and from which this contract derives. So, for example, if your Lordship could go to bundle 5. I had just put bundle 5 away, but it is bundle 5. I think your Lordship has that out already. Can we go to divider 172. These are the two extracts, at 171 and 172, but we will go to 172 first, from the FSA regulatory provisions. So if your Lordship has divider 172, you have INPRU 1063. And 1063.1, a calculation:
"A firm may take into account subordinated loan capital in its financial resources in accordance with tables 1062.2(a), (b) and (c), subject to 2 below."
I don't think the subject 2 is relevant for these purposes. I don't think it is relevant for my purposes. If we can then go backwards in the bundle, my Lord, to tab 171. This is INPRU 1062.2:
"The firm must calculate its financial resources in accordance with table 1062.2(a) below unless ... "
The "unless" in (a) and (b) don't really take us anywhere for these purposes.
Then, over the page, you will have what the company can take into account as regards its financial resources. We say this is, if you like, the detail of

the sources which are within clause 5. If your Lordship just looks down, you have the ordinary share capital, non-cumulative preference shares, share premium accounts, et cetera. Then, the first is initial capital, that is (a), and then the next box, investments own shares, intangible assets, that is (b). (a) minus (b) equals original owned funds. Then, you have further additions and subtractions. At the bottom of the column, you see, "Financial resources".
We say that is what is meant by solvency. That is the source of solvency for the purposes of clause 5.
What one does not see there are any items which relate to the ability of a liquidator to make a call. True it is, ordinary share capital, I accept, would include unpaid share capital in a limited company. That then brings us in to the next point. As was loomed large in the Court of Appeal, unlimited companies, nowadays, are a relatively rare occurrence. As Lord Justice Briggs said, quite vividly, and the charts which allow you to navigate the situation and the position in relation to unlimited companies are old.
Of course, no one anticipated -- and again this is borne out by what Mr Justice David Richards said at first instance -- or had regard to the status of LBIE as an unlimited company or, indeed, really had any notion

that it would ever become insolvent.
So, again, the context is relevant because what can never have been this contemplation in creating a relevant accretion to the assets or the funds available to the company for the purposes of dealing with creating solvency in clause 5, would be the ability of a liquidator to make calls against the membership.
Now, one can foresee that if it had been intended that one could look towards the membership in that way, but in the context of the agreement one might have, for example, representations from the membership as to the maintenance of their solvency. One doesn't have that. The representations, as regards the lender and the borrower -- the lender of course being LBHI2, which is the parent company -- there is no reference to that type of further support matrix, or further support network as regards the solvency of LBIE. One might have thought that that would be relevant if the regulator in the standard form contract was intending to have regard to the ability to make calls in an unlimited context against the company's membership. We say, that is all on a fair interpretation of clause 5, by reference to the improve documents at tab 171 and 172.
MR JUSTICE HILDYARD: I can see that isn't inconsistent with your case, but I am not sure it demonstrates it.

I mean, this is a list of admissible assets and a prescribed list of deductions to be made.
MR ATHERTON: Yes.
MR JUSTICE HILDYARD: Neither is complete.
MR ATHERTON: Well, it is complete for the purposes of --
MR JUSTICE HILDYARD: INPRU.
MR ATHERTON: Yes, and the regulatory context in which this company sits. One would have thought that, where one is dealing in this context that one is looking for a cushion of capital, would be, that that represents, the landscape which the company is inhabiting, and nothing beyond that.
MR JUSTICE HILDYARD: Well, I mean that is, with respect, sort of stating that INPRU and the statute walk hand in hand. What I am suggesting is that whilst this is entirely consistent with the statute, it is not demonstrative of its extent, nor it is a demonstrative of the extent of it. I suppose you would say, in the latter context, there is a much more exact correlation because the standardised form is prescribed by and is intended to implement the INPRU view of world.
MR ATHERTON: Absolutely. Your Lordship is right because it is illustrated by this point. We are looking at it for the purposes of the clause. Your Lordship's point about it albeit not referring to the statute, I am not

suggesting a call can't be made under section 74 and section 150, obviously it can. I am not suggesting, as I have previously submitted, that if funds are generated by such a call they cannot be applied to prior ranking liabilities. All I am saying is that by reference to this clause and the INPRU documentation, one cannot get to a situation where that means if all of the prior liabilities are paid, that constitutes solvency for the purposes of the provision.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: My Lord, your Lordship will be familiar with the authorities on contractual construction. So Rainy Sky --
MR JUSTICE HILDYARD: I saw there was another one coming up before the Supreme Court next month.
MR ATHERTON: Is there?
MR JUSTICE HILDYARD: As to whether one should look at the words first.
MR ATHERTON: We say you do, but it may be pending the determination of the Supreme Court, like so much in this case, my Lord.
MR JUSTICE HILDYARD: I may be wrong, but I did look at this and wondered whether we had been there before. The rule being that you must look at the words first and then swiftly move on.

MR ATHERTON: Well, I am trying to be as swift as I can, my Lord.
Your Lordship has the authorities, Arnold v Browne, Rainy Sky, also Chartbrook, because Chartbrook, at paragraph 16, says when a word is used in a specific context, and a specific word is used, prima facie it should carry with it that label and that meaning, and we say that is the importance of the word "solvent" and "solvency" here. It has a particular connotation and that connotation can't be the ability to create a "solvency position" as an accord by reference to the conduct or power of a liquidator, to put the company in that position. We say that simply doesn't make sense within the context of --
MR JUSTICE HILDYARD: I think there are authorities that say there are slightly different approaches, where you have actually defined terms.
I mean, the most honest description, possibly, with respect to everybody, is Bingham, where he says it is neither unswervingly literal nor unknowingly purposive, or whatever it is, ie it is a bit of a blend. The fact that you take into account the context gives a bit of a steer to having regard to the commercial realities of life, including the effects.
MR ATHERTON: Yes.

MR JUSTICE HILDYARD: Subject to what they next say, that seems broadly correct.

But if you have a defined term, and they have gone out of their way to say, "In this contract when I say 'this', I mean 'that'", you must probably give full and entire four wall context to that. That is broadly what you are saying, is it?

MR ATHERTON: Yes, but we say here solvency is defined because it is referred to in 5.1(b).

MR JUSTICE HILDYARD: It is definitely. It is in quotes the whole time.

MR ATHERTON: That's right. And then defined by reference to 2.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: I will take up a short amount of time, when I was debating a very similar question before one of your Lordship's former colleagues in chambers, Mr Jonathan Crow QC, when he was a judge. I was debating whether or not if one put in a definitions clause, Rumplestiltskin, whether or not it was bad because Rumplestiltskin didn't actually feature in the contract, but it was something else. Anyway. It was the same sort of issue.

MR JUSTICE HILDYARD: I am sure he followed you.

MR ATHERTON: He obviously didn't, like your Lordship.

We say, just by applying the usual tenets of construction that is where we get to. We say there is no ambiguity when one looks at that clause, in regulatory context there is no ambiguity.

The consequence of Arnold v Browne is really you only get into business commonsense, commercial commonsense when there is some sort of ambiguity. We say there isn't one, so one doesn't need to apply.

Let's say that there is, let's say that a commercial absurdity is asserted as a consequence of our interpretation, namely that the sub-debt is not payable, we say, "But look at it in the regulatory context, why is that so unusual? This is effectively capital". The reality is, we would say, that no one anticipated this loan, these loans, to ever be repaid. They are essentially sitting as capital. The only contemplation that anybody would have that they might be repaid would be in similar circumstances to a shareholder being entitled to a return of capital or the payment of a dividend. That contemplation or that anticipation is outside the notion of a company becoming insolvent and, therefore, through the insolvency process and the process of a liquidator making a call, being in some way able to repay the subordinated debt. So we say the regulatory context has a role to play and it cuts

down -- insofar as there is any commercial absurdity or situation where it doesn't accord with business commonsense, we say it doesn't matter in this case, or it is of less worth because of the regulatory context.

In response to dealing with Mr Marshall's arguments my learned friend also relied on the AIB case, also Mr Justice Andrew Smith's decision in the Swiss Marine case. Particularly in the latter, where what Mr Justice Andrew Smith said was where you are dealing with the standard form contracts, what you take aren't the usual meaning of the words, because they are open to a larger constituency than just the immediate parties, that is what one ought to do; that is consistent with what Lord Justice Millett says. We say that is the proper construction here. Just taking the usual meaning of the words. It can't include an accretion to the funds available by reference to a call by a liquidator against the membership in an unlimited context.

My Lord, I think that deals with that particular aspect of the interpretation. I would now like to say, and deal with the question of assets by reference to where we had come to in that context by reference to the first instance decision of Mr Justice David Richards and the Court of Appeal.

Now, we say on one level it doesn't really matter

whether these are assets or not, because on our interpretation, assets don't really matter. But if -- if -- we are right in our assertion that the ability to make a call by a liquidator and the fruits of that call are not an asset, we say even more so that we are correct on our analysis, because they simply don't feature, nor should they feature, in the accretion to create a solvency position for the purposes of the clause.

Now, Mr Trower submits that the notion that calls are not assets of the company, which is our submission, is wrong by reference to longstanding authority, and he cites Webb v Whiffin and General Works Company v Gill. We say there is a very simple answer to that: both of those cases did not involve unlimited companies and were concerned with unpaid share capital. We don't dissent from the notion that the ability to call for unpaid capital in respect of shares as a right or as a fructification of that right are properly so-called capital. Whether they are assets or not I don't think matters for these purposes. Maybe technically loose language, but they are certainly capital. Insofar as one is dealing with a limited company, one sees it in the INPRU documentation, that would be incorporated in the funds available for the financial resources. So

I don't think I need to take you, and descend into the detail of either Webb v Whiffin or the Gill case, the General Works Company case, we say they are distinguishable on that basis.

Where did this issue about assets come from in the Court of Appeal?

If your Lordship doesn't mind, if we can go to the Court of Appeal judgment. I think your Lordship has been dealing with it in the authorities bundle.

MR JUSTICE HILDYARD: Actually, I have been dealing with it in the core bundle.

MR ATHERTON: I am grateful.

MR JUSTICE HILDYARD: Tab 9.

MR ATHERTON: Thank you, my Lord, I am grateful for that.

(Pause)

Just for your Lordship's note, paragraphs 28 through to 32, Lord Justice Lewison refers to the improved documentation and the schedules that I took your Lordship to.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: Then if we could go to paragraph 113 and if your Lordship wouldn't mind, it is probably quicker if your Lordship reads from 113 to 120, inclusive, please. I can't recall now whether you have been taken to that before.

MR JUSTICE HILDYARD: This is Lord Justice Lewison?

MR ATHERTON: That's right. Yes, my Lord.

(Pause)

MR JUSTICE HILDYARD: Yes.

MR ARDEN: So Lord Justice Lewison, we say, is very clear that although the position may be different in relation to a limited company, he has grave doubts as to whether or not calls of this nature in an unlimited company do in fact represent an asset or an accretion to the assets of the company. He says, I am not citing it because I think the citation and the quotations from Pyle Works by Lord Justice Lewison is sufficient. He says that the Court of Appeal are bound by the interpretation of Webb v Whiffin in that case, in Pyle Works. The consequence of which is they are not assets. Now, that is Mr Justice Lewison.

If one goes ahead in the judgment, my Lord, to paragraphs 196 and 197.

MR JUSTICE HILDYARD: In the case of Sun v Wright, which is not subject to the control of the directors, it is quite difficult to see that that is an asset.

MR ATHERTON: Indeed. Indeed, which is in the context of a call in a liquidation against an unlimited membership.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: Yes. He goes on to say that when one is doing

the adjustment as between members, that informs the suggestion, or the notion, that those are not assets of the company where the recovery is made for the purposes of that adjustment as between the membership themselves.

MR JUSTICE HILDYARD: I suppose another way you could put it is that this is not a matter, unlike uncalled capital, which is legislated for, capable of being legislated for by the articles of association.

MR ATHERTON: Indeed. Indeed.

I was going to take your Lordship to paragraphs 196 and 197. This is the origin of the whole assets, if I can put it like this, controversy in the judgment of Lord Justice Briggs. 196 gives you the context of the argument he is dealing with, and then 197 is the relevant paragraph.

MR JUSTICE HILDYARD: How far should I go?

MR ATHERTON: Just to the end of paragraph 197, my Lord.

MR JUSTICE HILDYARD: Right, so Lord Justice Briggs and Mr Justice David Richards say that both the uncalled bit and the exposure bit are assets of the company.

MR ATHERTON: Well, there in lies the issue, because Lord Justice Briggs says that is what Mr Justice David Richards says as paragraph 165. That is what LBIE say, Mr Justice David Richards said --

MR JUSTICE HILDYARD: I see.

MR ATHERTON: -- in paragraph 75.4 of their skeleton argument. If we go to paragraph 165 of Mr Justice David Richards' decision, in divider 8. Does your Lordship have that?

MR JUSTICE HILDYARD: Yes. He is looking at it post-liquidation.

MR ATHERTON: That's right, but so is Lord Justice Briggs.

MR JUSTICE HILDYARD: I suppose you say the magic is in the assets available to a liquidator?

MR ATHERTON: Correct, yes. What Mr Justice David Richards does not say is that they are assets of the company. They are assets available to the liquidator. So I am not sure how I can put this. But, in my respectful submission, Lord Justice Briggs misdirects himself or assumes something in the words that Mr Justice David Richards uses which is not correct.

An example would be assets available to a liquidator for the purpose of discharging liabilities in the winding up would include things like the proceeds of a preference claim. The proceeds of an under value claim. A contribution to the assets from a misfeasance directive for wrongful trading. So conceptually it is very different.

Now, if you don't mind, if we could just go back to Lord Justice Briggs' judgment, where we left it, at 197.

If your Lordship just had regard to the beginning of the last sentence:

"As will later appear, I agree with the judge that the right to make calls, et cetera, is an asset of the company."

So we need to see if there is any additional reasoning which can be brought to bear in Lord Justice Briggs' judgment.

Now, as far as I can ascertain, I think what Lord Justice Briggs is referring to is paragraphs 210 to 212.

MR JUSTICE HILDYARD: Shall I read those?

MR ATHERTON: Yes please. I am sorry, my Lord. Yes, please.

(Pause)

MR JUSTICE HILDYARD: Yes, so you don't agree with 212?

MR ATHERTON: No, because what is the source of that assertion by, respectfully, by the Lord --

MR JUSTICE HILDYARD: Well, I can see the force of it. He just says if there is someone who owes, there must be an asset. That is all he is saying, really. That may not be right.

MR ATHERTON: Well, my interpretation is he is saying it is undoubtedly an asset, (1) by reference to his reference to Mr Justice David Richards, which in my submission was

exposed as fallacious, if I can put it that way, 2) he is relying on Webb v Whiffin as saying, "That is the situation", but that is plainly not the situation in Webb v Whiffin, where one is dealing with a limited company.

Again, if one is in the situation where one is relying on assets available to a liquidator, we say that palpably is not the same as the assets of the company. True it is, as I said, it will be an accretion to the funds available to discharge the liabilities in the liquidation. That doesn't of itself make those funds assets of the company, in that sense. They are brought into a single composite fund for the purposes of distribution.

MR JUSTICE HILDYARD: It is a very particular species of rights. I mean, normally, think is it Ayerst that says there is no change in ownership, and if there is no change in ownership, if you had it after liquidation, presumably you had it before; do you see what I mean?

But your answer to that is to say: well, no, this is a very particular right which, as regards the bit which extends beyond the call, the call on the limited --

MR ATHERTON: Yes.

MR JUSTICE HILDYARD: -- on the nominal capital, and rather like, as you say, other insolvency processes not

available beforehand. It is just of a different nature.

MR ATHERTON: Correct. The source is different. It is all part of the composition of that liquidation fund.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: But the origin is very different, we say.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: If your Lordship could just bear with me for one moment.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: My Lord, just in way of summary, therefore, we say that, on our construction of clause 5, it doesn't matter whether the accretion to the fund is an asset or not. We say it is just not within the clause. But we say that that construction is buttressed by the fact that these aren't assets and, therefore, they are well out with the contemplation of the regulator and the parties in the context where these are not negotiated contracts. My Lord --

MR JUSTICE HILDYARD: At the second level of your argument, can I just ask you this --

MR ATHERTON: Yes.

MR JUSTICE HILDYARD: -- what is the status of Lord Justice Briggs' analysis in terms of precedent?

MR ATHERTON: None.

MR JUSTICE HILDYARD: It is just an argument? It is just

a theory, is it?

MR ATHERTON: I think it is probably obiter.

MR JUSTICE HILDYARD: It isn't obiter to him, because he thought it was an essential dissolver of the boot straps argument.

MR ATHERTON: Well, the answer is it doesn't form part of the ratio of the case.

MR JUSTICE HILDYARD: It does for him.

MR ATHERTON: But in the context of what Lord Justice Lewison said, and the concurrence of Lord Justice Moore-Bick --

MR JUSTICE HILDYARD: He disagreed with everybody, you mean.

MR ATHERTON: But it is still two against one as to whether or not these form an asset of the company.

MR JUSTICE HILDYARD: Right.

MR ATHERTON: But, in any event, what I hope to have shown, in my submission I have shown, is that the analysis applied by Lord Justice Briggs is not appropriate. It is wrong, because he is putting too much weight on Webb v Whiffin, which is a different type of case.

MR JUSTICE HILDYARD: Yes.

MR ATHERTON: And he is affording a meaning to the words of Mr Justice David Richards, which they simply don't bear.

MR JUSTICE HILDYARD: So it is open to me to disagree?

MR ATHERTON: Yes, my Lord, very much so.

MR JUSTICE HILDYARD: Right.
MR ATHERTON: I am sorry, can I just ask for your Lordship's indulgence once more?
Just to reinforce that last point, my Lord, could your Lordship just go back to Lord Justice Briggs' judgment?
MR JUSTICE HILDYARD: Mm-hm.
MR ATHERTON: At 212.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: When one breaks it down, although it uses quite strident terms, it is actually not quite as conclusive as one might imagine:
"Furthermore, even though not conclusive on this issue, I consider that the undoubted fact that the fruits of a call constituted cash to the company point strongly to the conclusion of the liability of the company prior to making the call itself is an asset to the company."
So he is a little equivocal with respect to his own reasoning.
MR JUSTICE HILDYARD: He is not particularly equivocal in the last sentence.
MR ATHERTON: Well, then that is slightly more strident than the opening sentence of the paragraph.
MR JUSTICE HILDYARD: Yes. He gathers force.

MR ATHERTON: Yes.
MR JUSTICE HILDYARD: The eye of the hurricane.
MR ATHERTON: Indeed, my Lord. Your Lordship has my submissions anyway.
MR JUSTICE HILDYARD: Yes.
MR ATHERTON: They are my submissions. I was 15 minutes longer than I thought I would be.
MR JUSTICE HILDYARD: I am very grateful to you.
Is it your go?
MR MARSHALL: I believe so, my Lord.
MR JUSTICE HILDYARD: Do you want to gather yourself and have a break now?
MR MARSHALL: This might be a convenient moment for the transcribers. I understand that Ms Toube would prefer if we could rise at 4 o'clock today. I think she needs to be home before it is dark. If your Lordship would find that convenient, I am very happy to do so. I hope that would be the case with other parties.
MR JUSTICE HILDYARD: Certainly, we are well ahead of schedule and I would have to rise at 4.15 pm.
MR MARSHALL: Yes.
MR JUSTICE HILDYARD: So everything points towards 4 o'clock.
(3.02pm)
(A short break)

(3.10pm)
Submissions by MR MARSHALL
MR JUSTICE HILDYARD: Yes, Mr Marshall.
MR MARSHALL: My Lord, if I may I am going to start with issue 1 and follow on from where, to some extent, Mr Atherton left off.
My Lord, we submit that there is no obligation to contribute under section 74 of the 1986 Act in respect of the subordinated debt for essentially two reasons. Even if, contrary to our primary case, LBL is indeed a shareholder and all of our contentions for the part B trial are unsuccessful. The first of those is that LBIE has a complete defence to the subordinate debt claim under the doctrine of circuity of action. That is applying principles in a recent Supreme Court decision, the case of Farstad; since it has no liability for such a debt, it can make no quarrel in connection with it.
The second way we put the matter is that properly construed and if that argument is incorrect, properly construed the subordinated debt agreements only permitted recourse to the assets of LBIE, and not those of its members, so that the exception which arises under section 74.2(e) applies in this case.
My Lord, if I can begin, then, which the circuity of action point, which in a way it is somewhat odd that

I am addressing rather than Mr Trower, because one would have naturally thought, since it is a possible line that he could have taken as a defence to a claim against his client, it would be for him to take. But there we are, we nevertheless raise it.
We submit that it is a very well established principle, certainly going back to at least the early part of the 19th century, that where there is circuity of action, it is not merely a counterclaim, or a right giving rise to a potential set-off, but a complete defence to the claim such that the claim cannot be maintained. Using the old language, used in the days when the court dealt with actions of assumpsit and so on, there would be a non-suit. We can see that from one of the early cases, a decision of Lord Justice Tenterden back in 1829. This is the case of Carr v Stephens, which I think has been added to you Lordship's bundle. I think it is in authorities bundle volume 1 with a new tab 4A, which I hope your Lordship will find has already been included.
The facts are a little complex, and take a little bit of time, when you read the report, to get to grips with. If I can try and summarise it for your Lordship.
What seems to have happened is that there was a receiver appointed in respect of the rental derived

from an estate in which a married lady had an interest; she was entitled to the rental that the receiver happened to gather in.

What also appears to have happened is that a solicitor, who was in fact the claimant, was owed some money by the husband of the lady concerned. The husband issued a bill of exchange, which was accepted by the receiver and which was drawn in favour of the solicitor who was the plaintiff. The question arose as to payment under that bill of exchange. The receiver had obtained an indemnity, an indemnity in case if he made payment and there was then subsequent complaint, the payment was being made from funds to which the husband was not entitled, that he should be able to be indemnified by the solicitor against any such claim. It seems to have become evident that the lady would not have permitted, did not permit, the money to be paid over.

So the matter first came before Lord Tenterden who thought: well, you still have to pay and you will just have to claim back under the indemnity.

But then he seems to have revised his view on the matter. Your Lordship will see the revised view at the bottom of page 282 of the English reports, beside the number 760, the last paragraph on the page:

"Upon further consideration, I think I was wrong in

deciding that the plaintiff might recover on the bill and that the defendant must resort to the indemnity. That would only lead to a circuity of action. It appears that before the bill became due Mr and Mrs H ordered the defendant not to pay it with the money in his hands and to which they were entitled. He was bound to comply with that order and if he afterwards was compelled to pay the plaintiff, he would be liable to pay the amount to Mr and Mrs H over again and entitled to sue on the indemnity. In order to avoid that circuity of action, I am of the opinion that we ought to hold that the present action is not maintainable and the consequence is that the rule for entering a non-suit must be made absolute."

So your Lordship there sees the way it is dealt with is, it is a defence, the action cannot be brought. It is non-maintainable, non-suit entered.

Now, your Lordship, that is one of the older authorities your Lordship sees with the doctrine being recognised early days.

It has had, as I indicated earlier, more recent recognition and application in the case of Farstad in the Supreme Court, which your Lordship will find in bundle of authorities volume 3, at tab 81.

It is principally concerned with an oil rig supply

vessel and questions of contribution in relation to a fire that occurred on the vessel. Under the charterparty for the vessel, there was a provision for an indemnity for the charterer. Your Lordship will see that referred to on the first page of the report, page 87, in the second paragraph. It is clause 33.5 of the charterparty, which provided:

"The owner shall defend, indemnify and hold harmless the charterer, its affiliates and customers from and against any and all claims."

That included where the loss or damage was caused or contributed to by the negligence of the charterer, its affiliates, or customers.

Your Lordship sees, on the third paragraph of that page, there is then a summary of the background events. The oil rig supply vessel was damaged by fire. It was owned by the pursuer Farstad Supply, the owner, and was under charter to Asco, and Asco had engaged Enviroco, who were the defender, to clean out some of the tanks on board the vessel. On Asco's instructions the master started up the engines and, at the same time, an employee of Enviroco inadvertently opened a valve which released oil into the engine room, near hot machinery, and that resulted in the fire. The owner sued Enviroco for damages and negligence, and they

averred that if they were liable to the owner, then they were entitled to a contribution from Asco under statute. It was agreed that if Enviroco was entitled to such a contribution, Asco would at the least be entitled to an indemnity from the owner under clause 33.5 of the charterparty.

Your Lordship starts to see, therefore, the circuity issue arising.

As your Lordship will see, it was held, in fact, that the question that arose under the statute is whether if Asco had been sued by the owner, it would have been liable to the owner. The answer to that question was the same as it would have been if the owner had sued both Enviroco and Asco and the case had fallen within section 3.1 of the relevant statute; that depended on whether Asco would have had a defence under the charterparty for the owner's claim to damages.

They concluded that any liability of Asco to the owner in negligence or based on its negligence was in fact excluded by clause 33.5. So the primary finding was that in fact the clause that contained the indemnity was also in fact an exclusion clause, which excluded liability.

They did go on to say that even if it wasn't -- and this is the observation: if clause 33.5 was not

an exclusion clause but a narrow indemnity clause, Asco would not have sued, have been liable to the owner because it would have had a defence of circuity of action, or -- and because this was a Scottish case -- the equivalent Scottish doctrine, (Latin).

My Lord, the first judgment was that given by Lord Clarke, and begins at page 89, with which Lord Phillips agreed.

The issue we are interested in, I think, is dealt with at page 95, beginning at paragraph 29. Where your Lordship will see, at paragraph 29, that the primary finding was that clause 33.5 excluded liability.

Then, at paragraph 30, there was the observation that the conclusion that Asco would have had such a defence makes the remaining question, which formed part of the argument, irrelevant. That question was whether, if clause 33.5 was not an exclusion clause but only an indemnity clause, the position would be different.

The argument accepted by the majority in the inner house was that in such a case the owner would have been entitled to judgment against Asco because clause 33.5 did not afford a defence but would have been liable to indemnify Asco against the liability under the clause. It is said in those circumstances if the action had been

brought by the owner against both Enviroco and Asco as contemplated by the relevant Act, it would have been entitled to a joint several decree against both.

Your Lordship will see in paragraph 31 Lord Clarke agreed with Lord Mance that that argument couldn't be accepted. The charterparty was governed by English law and such a claim by the owner would be met by the defence of circuity of action and judgment would be given not for the owner but for Asco, there would thus be no order of the court that Asco pay compensation to the owner.

So it is not a question of counterclaims or anything of that nature. It is a straight defence and if it works you have no claim. That was a question of English law. Although it was a Scottish case, every other aspect of it was Scottish, this particular point was an English law point.

He goes on a little further to consider what would be the position under Scottish law and your Lordship sees that being dealt with in paragraph 32. In essence, his Lordship concluded that there is a very similar doctrine with a Latin tag associated with it, which applies under Scottish law.

Then, at paragraph 33, he concludes:

"That principle would apply here if contrary to the

view expressed above, clause 33.5 was no more than a narrow indemnity clause, even if Asco was in principle liable to the owner, it would be entitled to be immediately indemnified by the owner. It would be bound to repay the amount of the liability. In these circumstances it would, as Lord Dunedin put it, be useless to give judgment against the owner for Asco."

Accordingly, if Asco had been sued no such judgment would have been given for damages against it. It therefore was protected against the possibility of a judgment being given against it.

My Lord, just to complete the materials: Lord Hope whose judgment or speech begins at page 98 of the report, he dealt with the matter at paragraph 44, on page 100.

He agreed with Lord Clarke, as to it being, in fact, an exclusion clause case, but goes on to conclude that he would have reached the same conclusion if on the proper construction of the charterparty, the clause was to be regarded as providing Asco with an indemnity. He makes the further point that the defence of the circuity of action wasn't in so many words known to Scottish law but the underlying principle certainly is, although it was overlooked by the majority of the inner house. He then goes on to say, at the end, in the last two

sentences:

"Asco's right to an indemnity from the owner for the losses claimed for would be sufficient to defeat the owners' claim upon the application of this principle. The result is that for the purposes of the relevant section, Asco would have been found not liable to it in respect of the loss and damages on which the action against Enviroco is founded."

So it is a complete defence, no liability.

My Lord, Lord Roger, I don't think dealt with that particular topic we are interested in, but Lord Mance did, whose speech begins at page 102.

MR JUSTICE HILDYARD: Lord Roger may have done in 48.

MR MARSHALL: Well, he was in complete agreement, in fact, which Lord Clarke and Lord Mance, at 45.

MR JUSTICE HILDYARD: He seems to indicate, although it doesn't exist this Scottish law, there is nothing in Scottish law against it, therefore it does exist.

MR MARSHALL: Yes. Lord Mance deals with it more specifically at page 104, in paragraph 59. He concludes, there:

"The language operates as a series of indemnities against third party exposure ... this is both what the heading of clause 33 and what common commercial sense would bring one to expect ... it is unnecessary to

consider the position on unreal hypothesis that clause 33.5 operates as a pure indemnity."

Then, he goes on to say:

"The consequence of this hypothesis would seem to me as a matter of English law, as the law governing charterparty rather than Scots law, but under both English and Scots law the action would clearly fail whether for circuity of action in English terminology or pursuant to the equivalent Scots law doctrine."

So that is the more recent and highest authority.

MR JUSTICE HILDYARD: The judge was governed by the law of Scotland, was it?

MR MARSHALL: Sorry, my Lord, the charterparty?

MR JUSTICE HILDYARD: Yes.

MR MARSHALL: The charterparty was governed by English law, that is why Lord Mance thought it was probably an English law point rather than a Scottish law point.

MR JUSTICE HILDYARD: Right. But the case was fought in Scotland?

MR MARSHALL: It was fought in Scotland.

MR JUSTICE HILDYARD: Lord Mance thinks it is a matter of substance under the contract, rather than a matter of procedure.

MR MARSHALL: We would submit it is a matter of substance because it provides you with a complete defence to the

claim.

My Lord, we would submit one can see from those cases therefore that it is an instance of a defence. What is required is a right of indemnification or recourse in respect of the same claim, or amount, as against the party suing.

Here we have a claim for the recovery of the subordinated debt against LBIE by LBHI2, and we submit it precisely falls within the same principle, in the context we are concerned with for issue number 1, which is a claim in respect of the subordinated debt, which may only be pursued through the insolvency process. Indeed, that is what the subordinated debt agreement envisaged that it would only be pursued in the insolvency context.

In that context, there would then be the claim over against LBHI2 by LBIE because of the shareholding under section 74, for exactly the same thing. If that is the scenario we are concerned with, we have complete circuity. If that is so, there is no claim under the sub-debt that can be maintained, applying these principles.

MR JUSTICE HILDYARD: Does that apply even if there is a mismatch between the value, or estimate of one and the estimate of another?

MR MARSHALL: Well, even if there was a mismatch, whatever the claim is that is going to be made, under section 74, is certainly going to defeat that portion of the claim that is being made by LBHI2. It is LBIE's case that the claim, under section 74, is in fact exceeding by a very large margin whatever is coming in the other direction. So as long as that is the case, then they have a complete defence.

My Lord, it is submitted, really, in answer to this that there are two points that are raised at the moment.

The first point is: oh well, this isn't applicable because it is really a case of set-off, and solvency set-off arrangements come into play.

The second point, that was put forward rather more tentatively, is that in some way this interfered with the contributory rule. With respect, we don't accept that either of those can possibly be an answer, because the first set-off requires there to be two maintainable claims, which you are giving rise to debts or some other quantified amount that you can pursue, but here you don't have that. You don't get to that stage. There is no claim that can be maintained. There is a complete defence to it.

My learned friend wanted to rely upon a passage in the Post Office v Hampshire County Council case for the

proposition that it is really better considered within the ambit of set-off rather than something else.

Unfortunately, the passage that your Lordship was taken to is just the start of the analysis and doesn't complete the analysis, when one looks at that case. Could I take your Lordship to it? It is authorities 2, tab 64. It repays a little bit more study in our submission, than perhaps was given to it by Mr Trower. This was a case all to do with telephone cables, the Post Office underground telephone cables.

As your Lordship sees from the headnote, what had happened was the road had become flooded and someone from the local authority had arranged for some work to be carried out draining the water off the road. Before they did the work, they had asked the employees of the Post Office to indicate where the telephone cable was positioned. Unfortunately, they seem to have been informed wrongly, and plunged a crowbar into the wrong part of the relevant area, causing problems. Then the question arose: well, among other things, what happens when there is liability on the part of the council under statute, under the relevant statutory provision, covering this sort of thing?

Which I think was a provision of the Telegraph Act. But there is a claim going in the other direction for

precisely the same loss, from the council against the Post Office, for the wrong information they were given about where they were meant to be putting the crowbar.

Your Lordship will see that this was addressed in Lord Justice Geoffrey Lane's judgment after the passage which my learned friend took your Lordship to, which is on page 134. Your Lordship was taken, I think, to the passage referring to Ginty v Belmont Building Supplies.

MR JUSTICE HILDYARD: Yes.

MR MARSHALL: Letters D to G. But then your Lordship needs to go on a little bit further, to the foot of the page, letter H, where Lord Justice Geoffrey Lane then says:

"What is said here is this ..."

There was, first of all, an objection that the matter wasn't pleaded, and as far as that was concerned Mr Denning, who was for the council, his reply was:

"The facts we rely on are sufficiently pleaded. All we are saying is that insofar as the Post Office has suffered this damage, this expense, the reason for incurring this expense is their own fault and as the amendment to the particulars of claim made clear."

So they consequently submitted that every ground that was necessary for the foundation of the application of this doctrine of circuity of action is present, and his Lordship agreed with him. He then went on to say:

"In this case, it seems to me there was a total circuity of action on the basis of the proper findings of the judge. Consequently, the council succeeds on that issue."

So that meant defence to claim, end of case.

There was then, though, a further alternative point, which is then dealt with in the next part of the judgment:

"But once again the matter does not stop there, because yesterday evening ...(reading to the words)... and counterclaim based on the position in Hedley Byrne."

That was based on the negligence of the Post Office employee in advising as to where to carry out the repairs on the road.

His Lordship observes that they didn't have to get into the morass of Hedley Byrne and succeeding cases because of a concession, but he then goes on to say, as your Lordship sees in the last two sentences:

"But that is a long stop as far as the council is concerned. The council should, in my judgment, succeed on the circuity of action point, even though they have failed on the meaning of section 8."

So they didn't actually, in the end, have to rely on a counterclaim, at all. They just relied on a defence. The amendment wasn't in fact necessary. It was a sort

of long stop that was there.

My Lord, Lord Justice Ormrod, who gave a concurring judgment deals with the matter at page 136. Just beside letter G, where he made this point:

"The only remaining question then is whether, strictly speaking, this is a matter of counterclaim or whether it can be relied upon as a defence. I accept without hesitation Mr Denning's submissions that on the authorities this is a classic example of the circuity of action situation and that consequently a defendant to a claim under section 8 can rely by way of defence on facts which indicate that, had he brought a counterclaim, he would have been entitled in law to recover from the Post Office as damages for negligence the sums claimed against him by the Post Office, and consequently I accept the argument of Mr Denning and the short and effective submission that Hampshire County council is not only a valid counterclaim but a valid defence to the claim in this case."

Lord Justice Orr then agreed with Lord Justice Lane and Lord Justice Ormrod.

So, my Lord, that is how it was dealt with there, and I would submit to your Lordship that that is entirely in line with both the oldest authorities and the most recent from the Supreme Court.

We aren't dealing with counter claims, cross claims, set-offs, we are simply dealing with a defence to the claim.

My Lord, the second area, which was the contributory rule I think, is something that was described by Mr Justice David Richards, as he then was, in the Waterfall I proceedings, which I think your Lordship has in trial bundle 1, at tab 8. I think he describes it at page 47, paragraph 179.

MR JUSTICE HILDYARD: Paragraph 79, did you say?

MR MARSHALL: Paragraph 179, my Lord.

MR JUSTICE HILDYARD: I am so sorry.

MR MARSHALL: He describes it by reference to a series of cases in the 19th century, beginning with Overend Gurney Grissel's case, which established the principle that a person could recover nothing as a creditor of a company until he had discharged all of his liabilities as a contributory. He then referred to the classic statement of the principle given by Mr Justice Buckley in West Coast Goldfields, an early 20th century case:

"The person liable as contributory must discharge himself in that character before he can set-up that as a creditor he is entitled to receive anything and a fortiori, as it seems to me, before he can set-up as a contributory he is entitled to receive anything."

You will notice that that was upheld by the Court of Appeal. Later on, in the course of this quite lengthy section of his judgment, he then ultimately concludes that the contributory rule doesn't apply in the context of administration, which is also the conclusion of the Court of Appeal. Your Lordship will find that judgment in the next tab, tab 9. The relevant passages, I think, are at paragraph 132, on page 37, where Lord Justice Lewison agrees with Lord Justice Briggs on the matter, and Lord Justice Briggs deals with it, at 233 to 245.

Your Lordship will see the conclusion at 245 is that he agreed with the judge on that particular point.

Now, apart from the fact that it doesn't apply in the context of an administration anyway, it is also quite difficult to understand how this has any relevance to this issue at all, because it, LBHI2, has no claim. There is nothing you are preventing by virtue of the contributory rule. There just isn't a claim, so you just don't have to deal with it. There is no question of postponing anything by virtue of the contributory rule doctrine. There is just nothing to postpone.

So my Lord, we just don't see that as really having any relevance at all to the topic that your Lordship has to deal with.

So my Lord, it is quite a short point but, in our submission, it is a clear and straightforward answer to the issue that we have to deal with. If there is no proper claim in relation to the sub-debt, there is no possible basis for then claiming against either ourselves or anyone else under section 74.

If we are incorrect in the circuity of action approach, we would nevertheless submit to your Lordship that on the proper construction of the subordinated debt agreement this is a case where recourse was to be had to the funds of LBIE alone, in the sense that those words are used in section 74.2(e) of the Act. Your Lordship will recall the wording. I think the provision is in bundle 5, I think at several different places. I had it at 133. Your Lordship might have been marking it up from 132, but the reference in the provision is as to the funds of the company are alone made liable in respect of the policy, or contract.

MR JUSTICE HILDYARD: Where are you looking, I am sorry?

MR MARSHALL: I am looking at bundle 5, tab 133 where we have section 74, and sub-section 2(e). There were two alternatives, you can either have the liability of the individual members and the policy and contract restricted or where the funds of the company are made liable to the policy or contract. The wording is

following from some of the early cases that your Lordship saw under some of the 19th century statutes, where they tend to use that formulation. And my Lord, we submit that that interpretation applies where ever one sees provisions for repayment such as appear in the variable terms, and if your Lordship has the subordinated debt agreement, it is in volume 4 at tab 1 and if one goes to clause 9, for example, in the variable terms on page 5 the third line on clause 9, "the terms for repayment are..." where one sees reference to repayment we respectfully submit one then has to interpret what does repayment mean in this context? It means repayment by the borrower, obviously, we would submit, but also repayment by the borrower from their own funds. And similarly when one looks at the standard terms, for example where there is a definition of "advance" on page 7, and your Lordship will see reference to repayment.

MR JUSTICE HILDYARD: I am sorry, I was pondering your from their own funds point.

MR MARSHALL: Yes. I am using that language because it is the language of section 74.2(e) itself.

MR JUSTICE HILDYARD: Doesn't that sort of beg the question, I mean 74.2(e), as you confirmed, was a long utilised clause but we still have to decide whether it applies in

the context, or whether it only applied where there was an express clause to that effect in, for example, life assurance contracts.

MR MARSHALL: Well, what we say the provisions of 74.2(e) is all about is creating an exception --

MR JUSTICE HILDYARD: Where have we been looking at section 74? For some reason --

MR MARSHALL: It is bundle 5 of the authorities, my Lord, at either tab 132 or 133.

MR JUSTICE HILDYARD: Is that the only place we have been looking at it?

MR MARSHALL: I think so. There is 132 which has the pre 2009 version, and then there is the 133 which is the one from 2009 to present.

MR JUSTICE HILDYARD: Yes.

MR MARSHALL: But for present purposes I don't think it matters, because the provision is the same. This is an exception to sub-section 1. So it is creating a situation where there will not be liability on the part of members, or past members, to contribute to the assets. And you do it by a policy of insurance. Historically a lot of the cases were to do with life policies. Or other contracts, where the liability of individual member is restricted, or funds of the company alone are made liable in respect of the policy. Or

contract.
MR JUSTICE HILDYARD: Yes. That is so, but why does that help you with clause 9?
MR MARSHALL: What we submit clause 9 means when it refers to repayment. One has to interpret this agreement as to what it means by repayment. And we say it should be interpreted, properly interpreted, having regard to all of the rules, current rules of interpretation as meaning repayment from the funds of LBIE alone. And therefore falls within section 74.2(e).
MR JUSTICE HILDYARD: What are the particular things, and I am so sorry to be slow, but which you say ensure that repayment is only to be from the funds alone?
MR MARSHALL: A number of things, we rely upon.
MR JUSTICE HILDYARD: You are going to come to that?
MR MARSHALL: I am going to come through a full list of things that point that way.
MR JUSTICE HILDYARD: Yes.
MR MARSHALL: We submit it is internally consistent in the sense that if you look at other provisions of the contract, to make it work coherently that is how you should interpret it. I will also be relying upon the background, or context in which this agreement was made, and we submit that is relevant, even though one is dealing with, in part, a standard form agreement but in

part a non-standard form agreement, in the sense that there are variable terms which are made individually. But of course an important part of the variable term is identifying who the borrower is. The nature of the borrower is part of the variable term. And the context in this instance is a borrower which is an unlimited company, which is a fairly special one, and one has to then consider the particular background to that and the dealings with the regulator in that connection. But there are a number of factors which I am going to come to.
MR JUSTICE HILDYARD: I misunderstood you Mr Marshall, I am so sorry. I thought you were telling me within the phrase or word repayment is the self-contained answer, whereas you are going to show me all sorts of factors which you rely on as vesting in that single word the meaning that it is repayment out of the funds of the company alone?
MR MARSHALL: Yes. No doubt there is more than one way to interpret it, actually, but there are certainly two interpretations being advanced. One interpretation is repayment means repayment from the funds of LBIE and repayment from any funds it might be able to collect under section 74.
MR JUSTICE HILDYARD: That is one argument.

MR MARSHALL: That is one argument.
MR JUSTICE HILDYARD: And Mr Atherton has waxed lyrical on that this afternoon. But I had misunderstood; this was an opening rather than a closing submission.
MR MARSHALL: Oh, absolutely. I was asked by Mr Trower, or the gauntlet was thrown down, well, pick the term that has to be interpreted.
MR JUSTICE HILDYARD: And the term is the word "repayment".
MR MARSHALL: And the term is repayment, yes. In fact it is "repayment" and there are also instances where one finds the word "payment" being used as well. And we would submit that also is to be interpreted in that way. I think there are examples of that in clause 5, for example.
MR JUSTICE HILDYARD: And you are alerting me to the fact that these are variable terms because you are alerting me to the fact that part of your argument will be that the specific nature of the borrower is to be taken into account in this particular context.
MR MARSHALL: Absolutely. That is a variable factor.
MR JUSTICE HILDYARD: Right.
MR MARSHALL: That is not standard form. In fact in this instance it is a very unusual factor. Perhaps unique, in fact.
MR JUSTICE HILDYARD: I see. Yes.

MR MARSHALL: Now, the first answer from Mr Trower is well, if you look at all of the old cases, Re: Athenaeum up until the latter part of the 19th century, I think the latest he gets up to is about 1880. You get a much clearer statement, if you are going to rely on section 74.2(e). You get it all spelt out in bold terms but the problem with that my Lord is all of those authorities predate the modern approach to the interpretation of contracts, which we are informed by Lord Neuberger in Arnold v Britton has undergone to some extent a revolution over the last 45 years and we are no longer in a situation where we have to find things spelt out literally in that way. Rather, the approach is the one which was advocated by Lord Hoffmann in Investors Compensation Scheme and which has remained the position throughout all of the Supreme Court and Privy Council cases that have followed it; that when you are interpreting it is the meaning which the relevant contract or instrument would convey to a reasonable person having all of the background knowledge which would be reasonably available to the audience to whom the instrument or contract is addressed. And my Lord, that has been repeated a number of times, including in the most recent Supreme Court decision in Arnold v Britton. Adopting that approach, one has

regard to not only the internal context of the document in terms of trying to make sure that the various provisions in it work coherently together, but where appropriate to relevant contextual matters. And in this context we are talking about regulatory background, principally.
MR JUSTICE HILDYARD: But two points there. You have to find a provision.
MR MARSHALL: Yes.
MR JUSTICE HILDYARD: And you say you have found the provision.
MR MARSHALL: Yes.
MR JUSTICE HILDYARD: And the provision is repayment.
MR MARSHALL: Yes.
MR JUSTICE HILDYARD: And the other is notwithstanding the sea change in attitude to the approach of English law to contractual interpretation, if it is, you have to take into account in interpretation the fact that in the past for many, many years, as is part of the context, you only got away with this if it was clear.
MR MARSHALL: Yes, but my answer to your Lordship is --
MR JUSTICE HILDYARD: It is all part of the context, isn't it?
MR MARSHALL: Yes. I suppose my answer to that last point, my Lord, is in the old authorities they happen to have

express provisions. It wasn't said in the old authorities because you are seeking to come out of what was the equivalent of section 74.1 you have to do so in very clear terms. That isn't spelt out.
MR JUSTICE HILDYARD: No, one of the factors that a draftsman would take into account, being a learned man, is blimey, it has always been made express in the past, or words to like effect depending on the draftsman.
MR MARSHALL: Yes. No doubt in the old days they were very conscious of the wider circumstances in which liability would arise. But all I am submitting to your Lordship is no one has ever said if you want to use section 74.2(e) you have to do it in very clear and express terms, no one has ever said that, it just so happens that the older authorities did do it in much more express terms.
MR JUSTICE HILDYARD: Yes.
MR MARSHALL: But that doesn't mean that that sort of inhibits your Lordship in any way in adopting the correct modern approach to interpretation which is to be applied on this authority to this agreement, and that is where we would submit you start.
My Lord, I am very conscious of the fact it is now 3.59, so before I start going off into the various

factors, that might be a convenient moment to call a halt.
MR JUSTICE HILDYARD: Yes, indeed. Well, thank you. 10.30 on Monday, then. Have a very good weekend.
(3.59 pm)
(the hearing adjourned until 10.30 am on Monday 6 February 2017)