1	Wednesday, 8 February 2017	1	during my submissions.
2	(10.30 am)	2	Thirdly, Chartbrook, and this was the point I did
3	Closing submissions by MR ATHERTON	3	make to your Lordship but I didn't the reference, which
4	MR JUSTICE HILDYARD: Yes.	4	relates to our argument about the use of the word
5	MR ATHERTON: Your Lordship does not need to look to	5	"solvent" and "solvency" in clause 5. The two
6	horrified. Yes, it is me.	6	references there are to the speech of Lord Hoffmann at
7	MR JUSTICE HILDYARD: I think I just have a horrified face.	7	paragraph 17, rather than 16 as referred to in
8	MR ATHERTON: I am grateful for that indication.	8	the transcript. Then a paragraph from Lord Walker along
9	I think it falls to me to go first by way of reply.	9	the same lines over the page at page 4, at paragraph 94
10	I hope your Lordship has received something in writing	10	of the report of Chartbrook.
11	this morning.	11	Then at (v), again I think I made these points in
12	MR JUSTICE HILDYARD: Yes, I have. I would not pass a test	12	opening, but they are really to support the submissions
13	on it. I have flicked through it.	13	that Mr Marshall was making as regards the question of
14	MR ATHERTON: It is really intended for your Lordship's	14	interpretation of the contract; namely that one does
15	reference after today. I propose to through it quite	15	have to have regard to the regulatory regime in which
16	quickly because I indicated to Mr Trower and my learned	16	this contract sits. That was accepted by Mr Justice
17	friends that I will try and only take 45 minutes, but	17	David Richards at first instance.
18	everything I need is either in this document or cross	18	Secondly, there was no consideration by anyone
19	referred to in the materials that are referred to. So	19	within the Lehman group as to how any of this would
20	I will only try to highlight what I consider to be	20	operate in an insolvency, and the reference there is
21	the more important points.	21	given to the judgments of Mr Justice David Richards.
22	I accept that it is not necessarily restricted to	22	Thirdly, a submission I did make and which
23	a reply. It is for these reasons. First of all,	23	Mr Marshall made, which is that there is no particular
24	I indicated to your Lordship that I would give your	24	thought given to the fact that LBIE was an unlimited
25	Lordship some cross references which I didn't give you,	25	company, and I think it is fair to say there was also an
	Page 1		Page 3
	1 age 1		1 age 3
1	so they are in there.	1	assumption that everyone proceeded on; that LBIE was
2	Secondly, it's an attempt to deal with areas where	2	just like any other company, essentially limited
3	your Lordship has maintained a concern about	3	in terms of its incorporation.
4	a particular issue throughout everyone else's	4	Then at paragraph 10 onwards under the heading
5	submissions; and insofar as I am able to assist, I have	5	"Relevance of the contributories' insolvencies",
6	sought to do so.	6	essentially we rehearse there the nature of the
7	Thirdly, the points made relate to a point which	7	contingencies which all the relevant claims are subject
8	I believe Mr Trower will be making, relying on	8	to, and essentially for the purpose of dealing with
9	Mr Justice Vinelott's decision in	9	the case referred to at (v) on page 5, which is referred
10	the Maxwell Communications case. So that is hopefully	10	to in our outline submissions in writing but which I did
11	a fair explanation of the documents. By way of	11	not develop in the course of my oral submissions in
12	introduction at the beginning of the document, we set	12	opening to your Lordship. Therefore, I just wanted to
13	out how we see the three issues on which we have been	13	bring it back into some form of focus for your
14	making substantive submissions inter-relate, but I think	14	Lordship's consideration.
15	I can leave that. I do not need to elaborate upon that	15	The point we get at there is this: it is one thing
16	any further.	16	to say, well, we can return LBIE to solvency in
17	Then if we could go to page 3, my Lord, this deals	17	the context of clause 5 by reference to the claim of
18	with issue 1. We refer to where these matters were	18	a liquidator for a call against its members. We have
19	dealt with by way of oral submission in the course of	19	dealt with that already as why that is not within
20	the opening I made. Then in relation to contractual	20	clause 5. But equally, it is not possible to say that
21	interpretation, I have given your Lordship the specific	21	it is possible to bring LBIE back into solvency for
22	references to the paragraphs in the authorities which	22	the purposes of clause 5 by reference to the claim of
23	I am most concerned with, so Rainy Sky, Arnold v	23	the administrators through proof in respect of the
24	Britton which for some reason, no doubt by reference	24	putative call by a liquidator.
25	to Rugby School, I continued to call Arnold v Brown	25	The reason for that is first for the same reason
	Page 2		Page 4
	1 age 2		i age T

1	that we give in relation to liquidator, it is simply	1	essentially affirm
2	outside the scope of the provision. Secondly, because	2	Chancellor Mor
3	plainly the claim of the administrators in respect of	3	case. Again for
4	a putative call under section 74 in liquidation is	4	point at paragra
5	contingent. And assuming for these purposes that that	5	submissions.
6	claim or its fruits may constitute an asset, we say	6	We say that i
7	certainly at this stage in the proceedings it is	7	was seeking to i
8	a contingent asset; and in those circumstances,	8	administrators a
9	a contingent asset is not ordinarily used as part of the	9	the provisions of
10	calculation of whether or not a company is solvent or	10	simply does not
11	insolvent. It is simply irrelevant.	11	Then my Lor
12	I will not take you to the report, but I will	12	bottom of page
13	explain the circumstances of Rococo because they are to	13	clarify the posit
14	some extent revealing	14	me upon during
15	MR JUSTICE HILDYARD: This is Rococo?	15	questions to Mr
16	MR ATHERTON: Yes, my Lord, and the reference to	16	We say that v
17	the authorities bundle is set out in the submissions.	17	the regime by re
18	Essentially, if you go over the page to page 6, you will	18	exclusively that
19	see it is Lord Justice Lewison, where he essentially	19	Act, principally
20	says that a contingent asset is not something which is	20	can garner that
21	taken into account in determining whether or not	21	Richards at para
22	a company is solvent in the context of an insolvency	22	the citation of the
23	type claim.	23	We say the sa
24	In that case, what was happening was a liquidator	24	is tab 49A of th
25	had brought claims for preferences that had allegedly	25	does not matter
	Page 5		
1	been procured by the directors of the company, and of	1	on unpaid capi
2	course for those purposes, the preferences were	2	company or an
_	The state of the s	1 -	

rms and concurs with the reasoning of orris at first instance in the Eurosail or your Lordship's note, we deal with this aph 34 of our written outline

is a good illustration of why, if one rely upon the contingent claim of the as causing LBIE to fall within of clause 5 of the sub-debt agreement, it ot operate in that way.

rd, issue 3 we begin dealing with at the e 6. Here again, it's just an attempt to tion which I think your Lordship quizzed g my opening and you have also addressed in r Arden.

when a company goes into liquidation, reference to which calls are made is t as provided for under the Insolvency y section 74 and section 150. We say one from the decision of Mr Justice David ragraphs 134 to 137 and 214 where there is the ex parte Branwhite case.

same is apparent in Re Pyle Works, which he bundle at those references. So it r whether you have existing unpaid calls

course for those purposes, the preferences were according to the liquidator given at a time when the company was insolvent. And that is the relevant time by reference to section 123 of the Insolvency Act 239 and 241.

Now in defence, the directors said, oh, but the liquidator has a claim for the recovery of an unlawful dividend, and if you take account of that unlawful dividend and put it in the balance sheet of the company as an asset, it means that the company was not insolvent at the time it gave the preferences, and therefore the statutory requirements to bring such claim are not met and as a consequence, the liquidator should

What the Court of Appeal held was by reference to the Chancellor, Sir Andrew Morritt as he then was was that such a contingent asset cannot been taken into account for the purposes of determining or seeking to ascribe solvency to the company in that context.

And for your Lordship's note, the Eurosail case is also in the authorities bundle. That is at bundle 3, divider 88. For reference, if your Lordship could look at the headnote at some point, and also paragraphs 37 to 43 of Lord Walker's speech in that case. There, he

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ital, whether in respect of a limited company or an unlimited company, the regime for calls in respect of such liabilities is by reference to sections 74 and 150. And of course therefore, in particular by reference to the terms of those provisions, for the purposes for which calls can be made, namely to ensure that the assets of a company or the funds available to the company are sufficient to pay its debts, and such as are necessary by reference to the wording of section 150 of the Insolvency Act insofar as they are necessary to pay the liabilities of the company, expenses and any adjustments as between the members.

Your Lordship, I use the phrase in paragraph 14 that they are capped. Of course in a limited company, the liability of the contributes is capped at the amount of the capital, the nominal capital, which is unpaid. In the context of an unlimited company in liquidation -because it is only a liquidator that can make the calls against shareholders in an unlimited company -- their liability is capped by reference to the specific provisions and the terms of section 74 and section 150.

Then we develop that in paragraph 15. There --MR JUSTICE HILDYARD: I am so sorry, Mr Atherton. I understood you just now to have said that

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1	the liability of members of an unlimited company is	1	the shareholders.
2	capped prior to insolvency by any amounts outstanding,	2	MR ATHERTON: I think it may be that the labelling of
3	any nominal amounts on their shares.	3	whatever this at this stage inchoate right is is perhaps
4	MR ATHERTON: Yes, because one could have unpaid capital in	4	if not misleading, then unnecessary.
5	the context of an unlimited company. So outside	5	One only needs to go as far as, we say, Mr Justice
6	a liquidation, that capital could be called by	6	David Richards went, and that it creates an asset which
7	a director. However, assuming all the capital is paid	7	is available to the liquidator for the purposes of
8	up in an unlimited context, calls can only be made by	8	discharging the liabilities in the winding-up and any
9	the shareholders by a liquidator in a liquidation.	9	subsequent adjustment. When I say liabilities,
10	We say the parameters in respect of which	10	I include the winding-up costs.
11	the liquidator can make calls is determined by	11	So there isn't any issue or obscurity in that
12	the specific terms of section 74 to ensure it has	12	regard. It creates, as we say in a subsequent
13	sufficient assets to pay its liabilities and,	13	paragraph, a fund, or the putative right will create
14	section 150 insofar as it is necessary to allow	14	a fund which will effectively operate as an accretion to
15	the payment of the liabilities, the cost of winding-up	15	the statutory fund available to creditors against which
16	and the adjustments.	16	they can prove and through which the liquidator will
17	So we say that is the regime that is applicable.	17	discharge the liabilities, expenses in the winding-up
18	We say by reference to the cases in paragraph 50, which	18	and any adjustment necessary for the shareholders.
19	again was a point made to your Lordship in opening, but	19	MR JUSTICE HILDYARD: I quite understand the point. I think
20	this gives the specific cross-references. You can	20	you are emphasising that you would not yourself, if
21	see	21	there is a choice in the matter, go along with
22	MR JUSTICE HILDYARD: On that footing, an unlimited company	22	Lord Justice Briggs' analysis.
23	prior to any insolvency is really very much like	23	MR ATHERTON: Correct, yes.
24	a limited company?	24	MR JUSTICE HILDYARD: You would prefer to rest with what
25	MR ATHERTON: Yes, yes, correct.	25	Mr Justice David Richards actually said and
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	Page 9		Page 11
1	MR JUSTICE HILDYARD: It is so odd, isn't it, because an	1	Lord Justice Lewison's possibly different emphasis.
2	unlimited company can reduce its capital in any way it	2	MR ATHERTON: With the concurrence of Lord
3	wants. Why is that? Why are there differences in this	3	Justice Moore-Bick.
4	way?	4	MR JUSTICE HILDYARD: Who agreed with everybody. Yes.
5	MR ATHERTON: I am not sure I can answer that, my Lord, to	5	MR ATHERTON: So that your Lordship knows where we are
6	be perfectly honest. Of course, the protection for	6	coming from, our interpretation of clause 5 of the
7	creditors arises from the ability of a liquidator to	7	sub-debt agreement does not, by reference strictly to
8	make calls against members up to the amount necessary to	8	that interpretation whether or not the right of
9	ensure, insofar as possible and the means of the	9	a liquidator is an asset to make a call and the fruits
10	contributees is available, to allow for the payment of	10	of that call is an asset of the company is arguably
11	those liabilities, the winding up expenses and any	11	irrelevant.
12	adjustments.	12	MR JUSTICE HILDYARD: I understand because you say
13	We say that is borne out by the citation of the	13	insolvency in effect, putting it very broadly, means
14	authorities in paragraph 15. For example, the Contract	14	pre-liquidation solvency.
15	Corporation which was a limited company	15	MR ATHERTON: Indeed, indeed.
16	MR JUSTICE HILDYARD: One of the reasons I ask the question	16	MR JUSTICE HILDYARD: I understand that. By way of question
17	is looking at it possibly in excessively economic terms,	17	for all of you, I blinked but no more at the cases to
18	you might expect assets to mean those rights and	18	the Supreme Court yesterday and I noticed that in
19	properties which creditors can look to for their	19	Mr Miles' submission in his case, there was quite
20	satisfaction if necessary at the end of the day.	20	a detailed treatment as to the nature of the section 74
21	MR ATHERTON: Yes.	21	right, where he made broadly the same point as you and
22	MR JUSTICE HILDYARD: And one might expect therefore, given	22	naturally Mr Arden, whose role he was then undertaking
23	an unlimited company can reduce its capital, that they	23	as I understand it, as you are making now.
24	are really being invited to deal with the company on	24	Now is that a matter for direct decision in
25	the footing that capital includes the calls against	25	the Supreme Court, or is it a matter one cannot
	Page 10		Page 12
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1	necessarily tell because they may or may not reach their
2	decision without it?
3	MR ATHERTON: I think the answer is the latter. I think for
4	present purposes and again, of course, if your
5	Lordship is delaying judgment until such time as we see
6	what the Supreme Court say, I am entitled to say that
7	the Court of Appeal have found that the right of
8	a liquidator, either the right itself or the fruits of
9	that right, is not an asset of the company.
10	For present purposes that matters, because we say
11	you take it in two stages. First, our interpretation of
12	clause 5 is independent of that issue, but secondly, if
13	one has to analyse that position because it is not an
14	asset of the company, that serves to buttress
15	the submission we make on interpretation.
16	Then at paragraph 16, we cite Re Pyle Works and
17	Re Mayfair Property. We say by reference to
18	the references could I just correct a reference to
19	Mayfair Property in the bundle so your Lordship has
20	the correct reference? It is authorities bundle 2,
21	tab 52A, not 49A. Over the page.
22	MR JUSTICE HILDYARD: Yes, thank you.
23	MR ATHERTON: The significance of those cases is that in
24	relation to Re Pyle, that was the decision which
25	Lord Justice Lewison was relying upon for his
	Page 13

Paragraph 17 is a slightly different point.

There is -- and I think I have to accept, if I can rely on elements of uncertainty in my favour in the Court of Appeal -- I have to accept that the Court of Appeal found, as did Mr Justice David Richards, that by reference to section 80 of the Insolvency Act, the contingent claim that the administrators have been found to be able to bring in respect of a future call by a liquidator is a claim in respect of which the company must be characterised as a creditor. The reason for that is, as was explained by Mr Justice David Richards, I think at paragraphs -- it is not in there in error: 141 to 143, but you have the references to where the Court of Appeal deal with it -- on the basis that otherwise it might be not possible for a proof to be placed within the insolvency of a contributory.

We say, well, that is fair enough insofar as it goes. However, that characterisation of the company as a creditor for that particular purpose or for that rationalisation is not determinative of whether or not the corresponding claim or fruits of a claim are an asset of the company. That aspect is really a construct deriving from section 80 in order to plug the gap which Mr Justice David Richards said needs to be plugged in order to ensure that any call could be made in

conclusion. We say that the analysis in Mayfair Property company -- again, I will not take your Lordship to it, but you will see from those references that what is essentially held there is that any right to call for or to make a call and the proceeds of the call in respect of an unlimited company is not an asset of the company.

It is neither capital nor an asset because it can't be charged, it can't be used as an accretion to the general assets of the company for the company's purposes. And Mayfair Property was an interesting case because it was where there had been some glitches in relation to the 1862 Act, I think. So what was allowed was that when an unlimited company re-registered as a limited company, you could reproduce the protection for creditors by stipulating that certain capital, unpaid or otherwise, could only be realised by a liquidator for the purpose of liquidation and the payment of creditors. So essentially reproducing the unlimited status at least in that regard to that aspect of the uncalled or unlimited capital of the company.

The court was perfectly plain there, saying it can't be charged, and all the hallmarks of an asset of the company were absent in relation to that type of arrangement. So we deal with that in paragraph 16.

Page 15

the insolvency of the contributories where there was one so that the right or the ability to recover not be lost.

The identification of a creditor it does not automatically follow, we say, that the corresponding claim is an asset. The characterisation of the creditor is merely the vehicle which allows the officeholder to ensure that the company and its creditors do not lose out insofar as its contributories are in an insolvency.

And the nature of the claim or the fruits of that claim is as Mr Justice David Richards described. Of course he said, yes, the company must be a creditor. He does not then say the claim which is to be brought or its fruit are an asset. He simply says it is an asset available to a liquidator.

So in my submission, Mr Justice David Richards was not troubled by the potential gap or lacuna between finding a creditor and necessitating a determination of a claim which the creditor has of being an actual asset of that creditor. It really was a means to an end, in my submission.

MR JUSTICE HILDYARD: Would you see a difference -- take the case of another right available only to a liquidator such as you instance in your initial submissions, I think. For example, a claim for preference or wrongful trading, whatever it was. Would that be

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4 (Pages 13 to 16)

different? It is at the point of insolvency, at the point of the point of the point of insolvency, at the point of the point of the point of the insolvency in the author of the company that a the centing of the insolvence in the point of the insolvence, and an administration, the point of the insolvence in the p	,			
MR ATHERTON. This, I think, is the interesting dichoturny. Once one is in the situation where the claim by a liquidator for a call can be recated as contingent in be logical corollary - their dequestion is if you the logical corollary - their dequestion is if you have a potential preference in a liquidation, then presumably that is a contingent claim which could be probably that the contingence that which could be probably they the directors. That analysis must apply, applying the analysis in the Court of Appeal. Where I think the analysis falls down of course is that the contingency is so remote or my be so remote that you would value that contringency at nil. I does not really have any life of its own. MR ATHERTON: Indeed, but I think that analysis must follow through. What implications that has for that type of claim, preference, undervalue, wrongful trading, in my substances. MR ATHERTON: Indeed, but I think that analysis must follow through. What implications that has for that type of claim, preference, undervalue, wrongful trading, in my substances in a color cartanly it is possible to reproduce, for example, an undervalue claims and page 17 Page 17 Page 17 Lordship's question in opening - definitely give a commentual commitment and an MR ATHERTON: That is right. But it is not, a liquidation. Page 17 Page 19 Lordship's question in opening - definitely give a commentual commitment to stand by MR ATHERTON. That is right. But it is only enforceable— MR ATHERTON That is right. But it is only enforceable— MR ATHERTON. That is right. But it is only enforceable— MR ATHERTON. That is right. But it is only enforceable— MR ATHERTON. That is right. And that childrence MR ATHERTON. That is a	1	different?	1	is at the point of insolvency, at the point of
3 Once one is in the situation where the claim by 4 a liquidator for a call can be treated as contingent in 5 an administration and also by directors—that was 6 the logical corollary—then the question is if you 6 have a potential preference in a liquidation, then 8 presumably that is a contingent claim which could be 9 brough by the directors 10 That analysis must apply, applying the analysis in 11 the Court of Appeal. Where I thins the analysis fails 12 down of course is that the contingency is so remote or 13 may be so remote that you would value that contingency 14 at mil. It does not really have any life of its own. 15 MR RUSTICE HILDYARD. That would depend upon 16 the circumstances. 17 MR ATHERTON: Indeed, but I think that analysis must follow 18 through. What implications that has for that type of 19 claim, preference, undervalue, symagiful trading in my 20 submission is not clear. Certainly it is possible to 21 expectace, for example, a undervalue claim and 22 appelsonce claim by reference to breaches of fiduciary 23 dury by the misfeasort director. 24 MR JUSTICE HILDYARD. One's instinct is that there is 25 a difference between a contractual commitment and an 26 a definitely give a contractual commitment and an 27 exposure. Shareholders in an unlimited company do 28 definitely give a contractual commitment and an 29 have a preference, undervolace claim in respect of 3 the company to the last furthing. 4 MR ATHERTON: That is right. But it is only enforceable— 3 MR ATHERTON. But equally you might be able to apply 3 the company to the last furthing. 4 MR ATHERTON: That is right. But it is notly enforceable— 4 MR ATHERTON: The set of the respect of a liquidator. 5 And a liquidator. 6 MR ATHERTON: The set of the or of the between the only bears who should eat in it the way, this issue, with respect to him. 6 The circumstances who operates in contract is a deferred 6 MR ATHERTON: The is right. But it is only enforceable— 6 MR ATHERTON: The set of the analysis to the robotate claim in respect of 7 where the onl				
a liquidator for a call can be treated as contingent in an administration and also by directors—that was 5 machemistration and also by directors—that was 5 misohemory rates at 281 and 285. They become due and therefore that is why you have to estimate their value, by the company by the site contribution of the question is if you 6 more provided by the site of the question is if you 6 percent and increased and therefore that is why you have to estimate their value, by the property of the court of Appeal. Where I think the analysis in 11 me Court of Appeal. Where I think the analysis falls 11 me Court of Appeal. Where I think the analysis falls 11 me Court of Appeal. Where I think the analysis falls 11 me Court of Appeal. Where I think the analysis falls 12 down of course is that the contingency is so remote or 13 may be so remote that you would value that contingency is so remote or 14 may 11 the down of course is that the contingency is so remote or 15 may be so remote that you would value that contingency at nell. It does not really have any life of its own. 14 Mc ATHERTON: I take on the soft fath type of 18 mrough. What implications that has for that type of 19 claim, preference, undervalue, wrongful trading, in my 19 calmy preference of the reaches of fiduciary 22 due to the mine of the inhouse claim and 22 apreference calmy reference to threades of fiduciary 23 due by the minesteament director. 21 me 19 me minesteament of the calmy and the first being an asset. We asy you 22 definitely give a contractual commitment of stand by 23 definitely give a contractual commitment to stand by 24 definitely give a contractual commitment to stand by 25 me company to the last farthing. 24 MR ATHERTON: That is much as only engaged to the company do 4 definitely give a contractual commitment to stan				
5 the logical corollary – them the question is if you 6 the logical corollary – them the question is if you 7 have a potential preference in a liquidation, then 8 presumbly that is a contingent claim which could be 8 brought by the directors. 10 That analysis must apply, applying the analysis in 11 the Corol of Appeal. Where I think the analysis falls 12 down of course is that the contingency is so remote or 13 may be so remote that you would value that contingency 14 at mil. It does not really have any life of its own. 15 MR AUSTICE HILDYARD and what we had contingency 15 may be so remote bat you would value that contingency 16 the circumstances. 17 MR ATHERTON: Indeed, but I think that analysis must follow through. What implications that has for that type of claim, preference, undervalue, vrought trading, in my 20 submission is not clear. Certainly it is possible to 21 reproduce, for example, an undervalue, claim and 22 apreference caliem by reference to braches of fiduciary 32 duty by the mistiseasal inference. 19 may 18 may 1			1	
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25 a submission I made to your Lordship in opening, which 25 indication of where Lord Justice Lewison got his nil				
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1	valuation from. The important point for issue 3 is	1	should have been paid, because they should not have been
2	this: if the sub-debt claim, the inbound claim, is to be	2	paid because the contingencies have not been met.
3	valid at nil, then by reference to the parameters of	3	Our alternative analysis is that you deal with that
4	section 74 and section 150 of the Insolvency Act,	4	on the logically anterior position. When you put your
5	the outbound claim must be nil. Because you cannot	5	proof in and LBHI2 work out what the dividends are, then
6	bring a claim simply for the purposes and we say this	6	you work out it will be sufficient to discharge prior
7	is essentially the consequence of what	7	ranking liabilities. You don't actually have to recover
8	the administrators are purporting to do here simply	8	any repayment of dividends because the analysis would
9	to swell the assets of the company beyond what is	9	result in the fact that there is a set-off of
10	necessary or sufficient to pay its liabilities.	10	the cross-claims, reducing them to a nil balance, and
11	MR JUSTICE HILDYARD: None of these are in the context of an	11	therefore the prior ranking claims can't be paid.
12	unlimited company.	12	Now we endorse the test put forward by LBHI2 and, as
13	MR ATHERTON: No, my Lord, they are all limited companies.	13	I say, accords with our analysis as to why the position
14	MR JUSTICE HILDYARD: One has the feeling of cart before	14	in relation to that put forward by LBIE simply cannot be
15	the horse to some extent or chicken and egg which	15	correct. The further point and this is where we get
16	is in order for the court to be satisfied in any given	16	into the question that your Lordship was about to
17	jurisdiction the subordination has worked, it has to say	17	posit in the context of subordination what happens
18	nil, because otherwise it has not worked.	18	when, as here, the issue of set-off raises its head?
19	MR ATHERTON: That brings me on to essentially if we can	19	Now I am assuming it is more than an assumption
20	pause on paragraph 23, I do not think Mr Trower is	20	because Mr Trower was kind enough to indicate to me why
21	making this point. We are now into the territory of	21	he was relying on Mr Justice Vinelott's decision is
22	Maxwell Communications, towards the bottom of page 10.	22	because I think LBIE are going to say that following on
23	Mr Justice Vinelott concluded in that case that the	23	from the Maxwell Communications case, one can have as
24	liabilities were not contingent.	24	a matter of English law subordination. We don't
25	First of all, we say the nature of the subordination	25	disagree with that but they will say that our reliance
	7. 24		D
	Page 21		Page 23
1	in this case is different so that reasoning wouldn't	1	upon the National Westminster Bank v Halesowen case goes
2	apply. In any event, we doubt very much whether or not,	2	too far.
3	with respect to Mr Justice Vinelott, that the analysis	3	Mr Justice Vinelott's analysis in Maxwell was: I am
4	is correct.	4	not bound by that case because the dicta,
5	In any event, what your Lordship has just been	5	notwithstanding it was the House of Lords, was that
6	alluding to brings us into the realms of paragraph 63 of	6	dicta. But more importantly, it was dealing with
7	LBHI2's written opening. Your Lordship will remember	7	the inability to contract out of the set-off provisions.
8	that this manifested itself as part of an iterative	8	What Mr Justice Vinelott was concerned with was
9	process, a test of the case theory of LBIE to the effect	9	the ability or otherwise to contract out of the
10	that the inbound claim could be valued at nil but that	10	provisions which required pari passu distributions to
11	had no consequence or effect on how one was to value	11	creditors and essentially came to the conclusion that
12	the outbound claim, the contribution claim, from LBIE to	12	Halesowen didn't deal with that and therefore he was
13	LBIH2.	13	free to say to read down in effect the pari passu
14	If you remember, the analysis in paragraph 63 was if	14	provisions to allow for subordination to take place.
15	you have a proof what I would refer to as an omnibus	15	In the course of his judgment, he noted that there
16	proof against LBHI2 ie one that took into account	16	was a substantive difference between the policy that
17	the amount that was necessary to clear prior ranking	17	might lie behind the mandatory nature of set-off and
18	liabilities and the balance of the amount which was	18	the policy behind pari passu, and there were very good
19	necessary to clear the subordinated debt, then if	19	reasons why you shouldn't be able to contract out of the
20	the consequence of that omnibus claim or omnibus proof	20	set-off provisions.
21	was that the dividend paid by LBHI2 was sufficient to	21	We are not into the pari passu incident here. We
22	pay prior ranking liabilities, then we say the correct	22	are into straightforward can you contract out of set-off
23	analysis put forward by LBHI2 is that there would then	23	because the justification of LBIE to say why
24	have to be because there would then be a set-off,	24	the analysis of the administrators of LBHI2 and
25	there would have to be a repayment of the dividends that	25	the administrators of LBH are wrong, because of
i		1	

1	the set-off provisions or the preclusion of set-off in	1	of whether or not the Halesowen rule, if I can put it
2	the sub-debt agreement. We say insofar as you have	2	that way, should be maintained was considered by
3	a subordination clause which brings you into conflict	3	the court committee in the 1980s and they concluded that
4	with the preclusion from the inability to preclude	4	the law should be changed by that they meant that
5	insolvency set-off, we say subordination has to yield.	5	statute should intervene to overturn the result of
6	It is as simple as that.	6	Halesowen. My submission is what that means is that
7	That we say makes perfect sense. It is entirely	7	Halesowen accurately reflects the law that you cannot
8	orthodox, not least because one creates or one can	8	contract out of mandatory set-off.
9	create subordination in a number of ways which does not	9	Your Lordship if you like may not find those
10	fall foul of or create any tension with set-off. So for	10	submissions terribly helpful in the sense of providing
11	example, you have as was explained in the extract	11	your Lordship with an exit route. But we say what this
12	from Fuller and to an extent from the extract in Derham	12	analysis does do is expose what the right answer. This
13	which we referred to one can have subordination	13	is why Lord Justice Lewison valued the claim,
14	through the operation of a trust where the proceeds of	14	the inbound claim, at nil. Because by doing so you
15	any proof by	15	avoid the tension or potential tension between
16	MR JUSTICE HILDYARD: This is a turnover?	16	the subordination provision and the desire to maintain
17	MR ATHERTON: Indeed. One has a turnover and then one might	17	that subordination and the inability to contract out of
18	have a turnover of trust arrangement. But the pure	18	set-off.
19	turnover may not solve the problem. The trust will	19	So by giving the claim a nil value, you are
20	because there is no mutuality in the set-off. Equally,	20	acknowledging as part of the contingency, if you like
21	you could have subordination created by an agreement not	21	wrapped up within that, the fact of subordination.
22	to exercise your right of proof, a waiver of proof.	22	We say that that analysis is also the basis upon which
23	I think this is an issue which may be up for grabs	23	either expressly, or perhaps more particularly but
24	in the Supreme Court	24	accurately, implicitly the Australian decisions came to
25	MR JUSTICE HILDYARD: That was a difference between	25	the same conclusion; that by giving a nil value, it must
	Page 25		Page 27
1	Mr Justice David Richards and the Court of Appeal,	1	be the position that you don't then create this tension
2	I think.	2	between subordination and set-off.
3	MR ATHERTON: That is right. The reason being that if you	3	MR JUSTICE HILDYARD: It is slightly reverse engineering
4	waive your right to prove because your claim is not	4	though, isn't it? You say, well, now what I have to do
5	provable, it is not susceptible to set-off. So one can	5	is get to nil. It looks like a contingency which is
6	see as a matter of reality there are ways to achieve	6	subject to all sorts of valuation issues. It would be
7	subordination.	7	far more neat if I did not enter into them and I said
8	My suggestion is not antithetical in the sentence	8	nil, then we can all go away happy. It is not
9	that I am doing down subordination completely. I am	9	, 8 , 113
10		1 2	particularly logically satisfactory.
	simply saying that where you have a situation as here,	10	particularly logically satisfactory. MR ATHERTON: I would like to think I was being slightly
11	simply saying that where you have a situation as here, where although there is a subordination clause and		MR ATHERTON: I would like to think I was being slightly
11 12		10	MR ATHERTON: I would like to think I was being slightly more sophisticated than that in this sense; that what
	where although there is a subordination clause and	10 11	MR ATHERTON: I would like to think I was being slightly
12	where although there is a subordination clause and the operation of set-off would compromise that	10 11 12	MR ATHERTON: I would like to think I was being slightly more sophisticated than that in this sense; that what your Lordship is doing is looking at the nature of the
12 13	where although there is a subordination clause and the operation of set-off would compromise that subordination, we say that is just the way it works.	10 11 12 13	MR ATHERTON: I would like to think I was being slightly more sophisticated than that in this sense; that what your Lordship is doing is looking at the nature of the contingency and that carries with it the fact that it is
12 13 14	where although there is a subordination clause and the operation of set-off would compromise that subordination, we say that is just the way it works. Set-off is mandatory and the particular provisions are	10 11 12 13 14	MR ATHERTON: I would like to think I was being slightly more sophisticated than that in this sense; that what your Lordship is doing is looking at the nature of the contingency and that carries with it the fact that it is subordinated. So you factor that into the determination
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1	regards giving it a nil value.	1	MR JUSTICE HILDYARD: Yes, that is very helpful.
2	In addition, the alleged binary nature of the	2	MR ARDEN: That observation applies in relation to
3	contingency also, we say, makes it plain as to how this	3	section A, which deals with issue 3. Section B, that is
4	should operate as a matter of reality. As I said in	4	our case on issue 3, 5 through to 8. Then LBIE's answer
5	opening, the administrators are required to take an	5	and our answer to the answer which is paragraph 9.
6	account.	6	So that is simply a summary and there is nothing new
7	If on any extrapolation it is binary, so it is	7	in that. My Lord, if I can leave aside section D for
8	either nil and nil in which case they don't fall into	8	the moment, the same applies to issue 7 which we deal
9	the set-off account because the contingency has not	9	with very shortly at paragraph 13. My Lord, again,
10	arisen or because it is binary, it is full and full,	10	there is nothing new there. It is simply a summary.
11	zero net balance and the thing is absolutely set-off.	11	MR JUSTICE HILDYARD: Yes.
12	Or even if we were wrong in determining that it was	12	MR ARDEN: My Lord, that leaves section D. We there deal
13	binary because of the parasitic nature of the debt, at	13	with essentially the same subject matter that
14	any level of a continuum or by any reference to	14	Mr Atherton has covered as part of the submissions that
15	a statistic, the debts will always cancel each other	15	he has just made. We thought we should deal with it
16	out.	16	because it was one of the points your Lordship raised on
17	That logical analysis and principled analysis we say	17	a number of occasions, principally in questions directed
18	conforms to what the reality is.	18	to Mr Atherton on the clause 5.2 point. But it is
19	MR JUSTICE HILDYARD: Do you mean the net value will always	19	a point which arises generally in particular in relation
20	be nil?	20	to issue 3.
21	MR ATHERTON: That's right, there is no net balance. So you	21	Your Lordship raised a point about the Supreme Court
22	either don't place it in the set-off account because	22	and the statements of case. My Lord, this point and
23	both claims are nil, or if you do, you can't put one in	23	the authorities that relate to the point, and in
24	and not the other in terms of giving an estimate.	24	particular Pyle Works and Mayfair Property are all
25	We say that is in effect what LBIE has done. They have	25	relevant to at least two of the issues that are before
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1	given the contribution claim a value of, let's say,	1	the Supreme Court. The first is as to the nature and
2	\$1.3 billion. That must equate and equiparate to	2	extent of the liability under section 74; how far does
3	the value of the inbound claim of \$1.3 billion.	3	it go and does it extend to statutory interest and then
4	We say that analysis is logical, principled and	4	on to unprovable liabilities.
5	therefore undermines what we say LBIE is trying to	5	The second is as to whether or not the LBIE
6	achieve, or the approach that LBIE has taken in relation	6	administrators can prove in respect of a contingent
7	to the inbound claim and the outbound claim.	7	liability under section 74. So if one looks and I am
8	MR JUSTICE HILDYARD: That is helpful, even if the lesson	8	not going to take your Lordship to all of the
9	might be to a draftsman: for goodness sake, exclude	9	references, but if one looks at the judgments in
10	the right of proof.	10	Waterfall I, you can see these two authorities I have
11	MR ATHERTON: We say if your Lordship came to that	11	just referred to being referred to in the context of
12	conclusion, it would be in no way heterodox or novel.	12	both of those issues. Then as I said, when one looks at
13	It is entirely an application of the relevant principle.	13	the statements of case in the Supreme Court, ours as
14	Slightly over, those are my submissions, my Lord.	14	well as LBHI1, you can see these authorities being dealt
15	MR JUSTICE HILDYARD: I am very grateful, thank you.	15	with. Therefore, the same points arise.
16	MR ARDEN: Your Lordship had a note in the form of a summary	16	In our submissions, my Lord, we have not sought to
17	from us this morning.	17	persuade your Lordship to take a different view to
18	MR JUSTICE HILDYARD: That is very helpful.	18	the view taken by the Court of Appeal on the issues that
19	Closing submissions by MR ARDEN	19	were before the Court of Appeal. But accepting that we
20	MR JUSTICE HILDYARD: The same applies, I am afraid. It was	20	are where we are with the Court of Appeal, there are
21	quite a quick read to see the lie of the land, but I am	21	points that can be made which are relevant to the issues
22	not able to tell you where the cities and rivers are.	22	before your Lordship on the nature and extent of
23	MR ARDEN: I am not going to speak too much of it because	23	section 74 liability. In other words, it is not all
24	most of it is not new. It constitutes a summary of	24	closed off, not all dealt with by the answers given by
25	the argument to date.	25	the Court of Appeal to the issues that were before it.
==			and Court of Appear to the issues that were before it.
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1	So, my Lord, with that background	1	These sorts of issues, the Supreme Court are unlikely to
2	MR JUSTICE HILDYARD: In the Supreme Court, is the analysis	2	touch upon the issues that are concerning your Lordship
3	of Lord Justice Briggs that the contribution call,	3	and the points your Lordship is raising on these issues.
4	whatever it extends to, is an asset of the company,	4	So for example, the nature and extent of the section 74
5	considered to be a point which has to be disposed of in	5	liability, and that seems almost inevitable the Supreme
6	order to assess the decision made in that context by	6	Court will have something to say about that which will
7	the Court of Appeal as a whole.	7	have a bearing on the issues before your Lordship.
8	MR ARDEN: My Lord, I can see how it might not need to be	8	So, my Lord, I respectfully endorse what Mr Atherton
9	dealt with. If one looks at Lord Justice Lewison's	9	has said on this question about the nature and extent of
10	judgment, he says it is not an asset of the company, but	10	the liability and how it arises in the context of unpaid
11	nevertheless the company is a creditor. In that	11	capital. In the note, we have drawn attention to or
12	respect, he agrees with Lord Justice Briggs.	12	made the point that Mr Atherton makes about the position
13	So in terms of provability, one can see the outcome	13	changing fundamentally upon liquidation. Your Lordship
14	might be that: it is not an asset but nevertheless it is	14	will see that at D under post-liquidation, and we have
15	a creditor of the company. But the nature of	15	referred to the same paragraphs in Waterfall I that my
16	the company's rights embrace: is it an asset or not.	16	learned friend has referred to.
17	I think for my part, with some diffidence because I was	17	We have given three examples of the way in which
18	not there, I can see that as part of the overall	18	things change in respect of unpaid capital. One of them
19	consideration of say that issue is it a creditor, is	19	is the same as my learned friend, the third, which is
20	there a provable debt it is difficult to see how one	20	that once the company is in liquidation and when you are
21	would deal with the second, is it a creditor, without	21	talking about calls under section 150 in respect of
22	dealing with the first, what is the nature	22	a section 74 liability, it is no longer an automatic
23	MR JUSTICE HILDYARD: That is as it rather strikes me.	23	call for the whole of the unpaid capital.
24	The Supreme Court has no need to finesse any of these	24	The liquidator may do that in an appropriate case, but
25	issues, it can deal with them and probably will. But	25	it does not do it, as it were, as a matter of right in
	•		, , ,
	Page 33		Page 35
1	there we are, that's that, we will have to await what	1	the way in which, for example, a company could do prior
2	they say. But it does suggest to me that it would be	2	to liquidation.
3	quite brave precedent to simply assume that	3	The liquidator has to justify the call by reference
4	Lord Justice Briggs' assessment was mere obiter, or not	4	to the debts and liabilities, and that is obviously
5	an integral part of his approach.	5	a point I have made on a number of occasions. We give
6	MR ARDEN: My Lord, I tend to agree. There is a sort of	6	as an example of that, just a single example, it is
7	starting point in both judgments: is it an asset or is	7	the Contract Corporation. I am not going to take your
8	it not, and the two Lords Justices take different views	8	Lordship to it, it is one of the cases that Mr Trower
9	about that. Then they proceed from a different starting	9	took your Lordship to in opening. But your Lordship may
10	point, but then on the creditor point to the same	10	remember it was a case of the nominal capital was
11	conclusion.	11	made up of shares of large amounts, I think £100 shares,
12	MR JUSTICE HILDYARD: The Supreme Court may say, look,	12	of which a very small amount had been paid prior to
13	the answer is what Mr Justice David Richards gave: you	13	liquidation I think about £10 or £20, but some small
14	can't prove it, end of story. Subordination works in	14	amount of the nominal capital.
15	that way. But they may not.	15	What one sees in that case is estimates being
16	Anyway, we shall see.	16	produced by the liquidator of the unpaid debts and
17	MP APDEN: I think it would be although one can skirt	17	liabilities and then the proper amount of the call,
18	MR ARDEN: I think it would be, although one can skirt		
	around this, one can try and navigate a course which	18	which is less than the unpaid capital, being justified
19	around this, one can try and navigate a course which enables your Lordship to come to a view on the issues	18 19	which is less than the unpaid capital, being justified by reference to those estimates.
19 20	around this, one can try and navigate a course which enables your Lordship to come to a view on the issues without it is fairly tricky, and I think	18 19 20	which is less than the unpaid capital, being justified by reference to those estimates. My Lord, that is the section 150 process being gone
19 20 21	around this, one can try and navigate a course which enables your Lordship to come to a view on the issues without it is fairly tricky, and I think MR JUSTICE HILDYARD: At first instance, you have to	18 19 20 21	which is less than the unpaid capital, being justified by reference to those estimates. My Lord, that is the section 150 process being gone through. What one sees in that case is the court not
19 20 21 22	around this, one can try and navigate a course which enables your Lordship to come to a view on the issues without it is fairly tricky, and I think MR JUSTICE HILDYARD: At first instance, you have to navigate. The Supreme Court, you can deal with what you	18 19 20 21 22	which is less than the unpaid capital, being justified by reference to those estimates. My Lord, that is the section 150 process being gone through. What one sees in that case is the court not disputing that that is the proper approach
19 20 21 22 23	around this, one can try and navigate a course which enables your Lordship to come to a view on the issues without it is fairly tricky, and I think MR JUSTICE HILDYARD: At first instance, you have to navigate. The Supreme Court, you can deal with what you want to deal with.	18 19 20 21 22 23	which is less than the unpaid capital, being justified by reference to those estimates. My Lord, that is the section 150 process being gone through. What one sees in that case is the court not disputing that that is the proper approach post-liquidation. It is more to do with the extent to
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1	MR JUSTICE HILDYARD: There may be unfairness between them	1	So far as unpaid capital is concerned, essentially
2	and the members who paid in full, because it is at that	2	I am in agreement with Mr Atherton, the position
3	stage that the unfairness arises.	3	changes. What was originally a contractual right is now
4	MR ARDEN: My Lord, that is right. You can just see that,	4	no longer a contractual right, there is substituted
5	that is one example, and my learned friend has given	5	the statutory regime.
6	many more in the written note he has taken your Lordship	6	My Lord, at E then we refer to Pyle Works and
7	through today; many more examples of that sort of	7	Mayfair Property. Both the cases, as your Lordship
8	process being gone through in the case of calls where	8	probably knows, deal with the issue as to whether or not
9	there is unpaid capital.	9	a company and to what extent a company can charge its
10	My Lord, we have added a couple of other examples of	10	uncalled capital, and to what extent that then is good
11	this. I do not think I need to take your Lordship to	11	in a winding-up. They are in our submission helpful to
12	the authorities, they are now in the bundle. Under D1,	12	your Lordship because in dealing with that question in
13	we have referred to the Welsh Flannel And Tweed case.	13	the case of companies with a nominal capital, they
14	I am not sure whether your Lordship	14	contrast that position where the outcome in the case
15	MR JUSTICE HILDYARD: I can't find the bundle, I'm sorry	15	of ordinary nominal capital is you can charge it they
16	MR ARDEN: It is page 6 of the note, D1, "Interest on unpaid	16	contrast that with the position, the liability of
17	calls", and then it is in the footnote.	17	members of an unlimited company.
18	If your Lordship wants to go to the case I am not	18	So in order to decide whether the company can charge
19	going to take you to it now it is 31A	19	or not, in the case of a company with a nominal capital,
20	MR JUSTICE HILDYARD: Is that 2/31A?	20	you have to consider the liabilities of the member and
21	MR ARDEN: It is 1/31A.	21	the rights of the company to determine first of all
22	MR JUSTICE HILDYARD: Thank you.	22	whether it is an asset and then whether it can be
23	MR ARDEN: That is just a case where the Vice Chancellor,	23	charged. But as I said, they then contrast the position
24	Sir Richard Malins name took the view that if a call is	24	with the liability of a member of the unlimited company,
25	made in a liquidation and not paid, as it was not in	25	whose only liability is to contribute in accordance with
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	Page 37		Page 39
1	that case for many years, you calculate interest not by	1	the statutory regime in the event of a winding-up.
2	reference to a rate of interest specified in	2	Now, my Lord, we have referred to the relevant
3	the articles, in that case it was 10 per cent, but by	3	paragraphs in the judgment exactly in Pyle Works. They
4	reference to the general rate which in that case was	4	are the same passages Mr Atherton refers to. They are
5	5 per cent.	5	the paragraphs set out in the judgment of
6	In that case, he declined to follow an earlier	6	Lord Justice Lewison in that section of his judgment
7	decision of his own which did it by reference to	7	where he deals with the issue as to whether or not in
8	the article. So you don't have regard to the articles	8	the case of an unlimited company, the liability is to be
9	for interest. Then there is Fowler v Broad's patent.	9	treated as an asset of the company or not.
10	My Lord, this is a case of again, the bundle	10	So far as Mayfair Property is concerned, again we
11	reference here is authorities bundle 2 and it is 47A.	11	have referred to the relevant paragraphs. This is
12	Again, I think the summary we give is probably enough	12	a slightly different case. Pyle Works establishes that
13	for your Lordship this morning; that where uncalled	13	the company can charge its unpaid capital. In Mayfair
14	capital has been charged and the company goes into	14	Property, the court had to consider the same question
15	liquidation, the charge is good see Pyle Works but	15	but in relation to capital which under the 1879
16	you enforce through sections 74 and 150. You enforce it	16	Companies Act had been set aside for the purposes or to
17	by asking the court to direct or order the liquidator to	17	be made available for the purposes of satisfying
18	make the call. You can't do it in an ordinary chargees	18	the claims of creditors in a liquidation.
19	or mortgagees action.	19	My Lord, there a different view was taken in
20	So, my Lord, I am not sure whether that adds to	20	relation to that sort of capital. But again, your
21	the sum of knowledge, but it may not add much	20 21	Lordship will find there a consideration of the
22	MR JUSTICE HILDYARD: Welsh Flannel may be more interesting	21 22	liability of the members of an unlimited company. As
23	because it goes to the right rather than the person in	23	I said, and as Mr Atherton says, it is essentially that
24	charge of the company.	24	the liability is simply to contribute pursuant to
25	MR ARDEN: My Lord, that is right. My Lord, that is all.	25	the statutory scheme, to contribute to the fund that
23	THE THE LIST. MY LOTA, MAC IS TIGHT. MY LOTA, MAC IS AII.	23	the statutory scheme, to contribute to the fund that
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1	the scheme envisages to the extent necessary if I can	1	those in?
2	then add the King v Tait reference to the extent	2	MR JUSTICE HILDYARD: There was another case on contract
3	necessary to meet the proper claims against that fund	3	which was heard yesterday in the Supreme Court for one
4	and with the liability being assessed by reference to	4	day as to whether you looked at the words first.
5	those claims.	5	MR TROWER: Yes. What a surprising proposition.
6	MR JUSTICE HILDYARD: Where? Oh, I see. I have	6	MR JUSTICE HILDYARD: Yes. Who knows.
7	the references in Mr Atherton's	7	(11.45 am)
8	MR ARDEN: 44A and 52A.	8	(A short break)
9	MR JUSTICE HILDYARD: I think Lord Justice Lindley may have	9	(11.55 am)
10	been the last person who really understood all of this,	10	MR ARDEN: My Lord, just two short points but more in
11	because he wrote the book both on partnership and on	11	the nature of reference or something like it than
12	limited companies, and the crossover was partly because	12	substantive points.
13	you couldn't have more than ten members in	13	My Lord, in the context of the Mayfair Property
14	a partnership. So I expect he really may have been able	14	case, I referred to the 1879 Companies Act. That is not
15	to explain all of this.	15	in the bundles. It is a very short Act and the relevant
16	MR ARDEN: I have not taken your Lordship to them. I am	16	provisions are set out in the report, along with
17	happy to go through those cases if your Lordship would	17	the legislative background. Your Lordship will see from
18	find it helpful, but they are probably they are	18	the judgments that it was in fact a legislative response
19	leading judgments on this, the difference that I am just	19	to the collapse of the Glasgow bank, which your Lordship
20	explaining to your Lordship.	20	has seen some cases arising out of that collapse.
21	MR JUSTICE HILDYARD: On the status of the capital	21	So a response to that, and the ruin that it caused
22	MR ARDEN: Exactly. And they are worth reading together	22	in the Central Belt and essentially, amongst other
23	because Lord Justice Lindley, then as Master of the	23	things, allowed unlimited companies to re-register as
24	Rolls anticipates in Pyle Works the issue in Mayfair	24	limited, creating at the same time a portion of their
25	Property and takes the opportunity in Mayfair Property	25	capital, which was to be simply devoted to the purposes
	D 44		D 42
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1	then essentially to go back and re-analyse, but in	1	of winding-up.
2	the context of a slightly different capital, the issues	2	So it is all there, but if your Lordship needs
3	that he addresses in Pyle Works.	3	the Act, then we can supply it and put it into
4	My Lord, can I leave those there? I am happy to go	4	the bundles at some point, if that would help your
5	through them if your Lordship would find it helpful.	5	Lordship's understanding of Mayfair Property. The other
6	MR JUSTICE HILDYARD: No, I will read them.	6	thing I wanted to mention to your Lordship was this. In
7	MR ARDEN: In our submission, they are important for your	7	Pyle Works, Lord Justice Lindley refers to Webb v
8	Lordship.	8	Whiffen and to the judgment of Lord Cairns in that case,
9	That may be a convenient moment for	9	and says he thinks that supports his approach.
10	the transcribers. I am probably about done, but subject	10	Just for the reference, I think the passage he is
11	to just checking behind me. Perhaps I can do that over	11	referring to is at page 734 of the report. It is
12	the course of the next five minutes.	12	the whole of the passage which takes up nearly all of
13	MR TROWER: Before your Lordship rises for the short break,	13	the page, and it is a passage in which Lord Cairns deals
14	there is a note that has been circulated amongst	14	with the pre-1862 position. So he deals with
15	the parties about the issues in the Supreme Court and	15	the liability of partners and then the liability under
16	how they impact on today's, which we will hand in. Can	16	the precursors to the 1862 Act, and then just starts,
17	I stress, it has been prepared by the LBIE	17	"But by the Act of 1862 that state of things is entirely
18	administrators. It has been commented on by people, but	18	swept away", and then he deals with the liability to
19	it is not strictly speaking an agreed note.	19	contribute to a common fund. I think it is 734. We
20	MR JUSTICE HILDYARD: Would you like to defer it until it is	20	have not noted it there, but I think that is the passage
21	an agreed note?	21	which is being referred to.
22	MR TROWER: I think it is in a sufficient form for your	22	MR JUSTICE HILDYARD: Thank you.
22	Lordship to see it. There is a short counternote from	23	MR ARDEN: My Lord, those are our submissions, I think more
23	LBL drawing your Lordship's attention to some other	24	in reply to your Lordship than in reply to Mr Marshall.
24		1	
	points in relation to the Supreme Court. Can I hand	25	If there are any matters on which I can assist your

1	Lordship, I would be happy to do so. But otherwise	1	point.
2	those are our submissions.	2	The third point is a point your Lordship put to my
3	MR JUSTICE HILDYARD: No, thank you very much.	3	learned friend Mr Marshall, which is that in any event
4	Closing submissions by MR TROWER	4	the cross-claim in the present case is not
5	MR TROWER: My Lord, I understand that Ms Toube has nothing	5	the straightforward indemnity in respect of liability
6	to say in reply, so it is me next. I will be relying on	6	with which Farstad was concerned. It is an obligation
7	rather more than Mr Atherton and Mr Arden have. Your	7	to contribute to an insufficiency which may in whole or
8	Lordship has not heard from me substantively since	8	in part be referable to the inbound claim, but it is not
9	the beginning, so I have quite a lot of issues to cover.	9	a straightforward indemnity for it.
10	But most of what I have to say relates to issue 1 and	10	Now we have not been able to find any case in which
11	issue 3. I have one or two points in reply on 7 and 9	11	there has not been the direct relationship between claim
12	but we will not take so long on those, I suspect.	12	and cross-claim, and the importance of the link is
13	My Lord, as far as issue 1 is concerned, there are	13	reemphasised in such cases as we have been able to find
14	three points as we see it made against us. There is	14	which deal with the concept of circuity of action
15	a circuity of action point, there is the sub-debt term	15	generally. We have put three cases in the bundle which
16	construction point, which is put as an express term or	16	are the best cases we could find on what circuity of
17	an implied term by Mr Marshall, and there is	17	action is all about. I think they have been inserted
18	the clause 5.2 point. Can I just reply on those in	18	into the back of bundle 5 of your Lordship's
19	order.	19	authorities.
20	Mr Marshall took you to Farstad, dealing first with	20	In bundle 5, there are three cases now.
21	circuity of action, and he took you to Carr v Stephen.	21	MR JUSTICE HILDYARD: They are new, are they?
22	The essence of LBL's submission is because LBIE has	22	MR TROWER: They are new. I am only putting them in for
23	a right to a section 74 contribution against LBHI2, that	23	three circumstances in which courts have given, or three
24	is a cross claim which gives rise to a defence to any	24	contexts in which courts have given crisp analyses of
25	claim under the sub-debt agreements. So he puts it	25	what it is that the defence of circuity of action is all
		23	what it is that the describe of chearty of design is the
	Page 45		Page 47
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1	forward as a defense of circuity of action	1	about
1	forward as a defence of circuity of action.	1	about.
2	Three points in response to that: 1, circuity of	2	The first one is the Luckenbach case. I am afraid
2 3	Three points in response to that: 1, circuity of action is a defence which has to be advanced and	2 3	The first one is the Luckenbach case. I am afraid I do not know how they have made it into your
2 3 4	Three points in response to that: 1, circuity of action is a defence which has to be advanced and pleaded. It is capable of being an answer to a claim if	2 3 4	The first one is the Luckenbach case. I am afraid I do not know how they have made it into your Lordship's bundle. I have them in the authorities
2 3 4 5	Three points in response to that: 1, circuity of action is a defence which has to be advanced and pleaded. It is capable of being an answer to a claim if brought, but there is no authority which characterises	2 3 4 5	The first one is the Luckenbach case. I am afraid I do not know how they have made it into your Lordship's bundle. I have them in the authorities bundle 5, right at the back. I am afraid they have only
2 3 4 5 6	Three points in response to that: 1, circuity of action is a defence which has to be advanced and pleaded. It is capable of being an answer to a claim if brought, but there is no authority which characterises it in any other way. It does not impair the liability	2 3 4 5 6	The first one is the Luckenbach case. I am afraid I do not know how they have made it into your Lordship's bundle. I have them in the authorities bundle 5, right at the back. I am afraid they have only just come in.
2 3 4 5 6 7	Three points in response to that: 1, circuity of action is a defence which has to be advanced and pleaded. It is capable of being an answer to a claim if brought, but there is no authority which characterises it in any other way. It does not impair the liability unless and until it is raised in proceedings and	2 3 4 5 6 7	The first one is the Luckenbach case. I am afraid I do not know how they have made it into your Lordship's bundle. I have them in the authorities bundle 5, right at the back. I am afraid they have only just come in. MR JUSTICE HILDYARD: Yes, that is fine. Owners of the
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1	which one normally finds circuity of action arising as	1	the pleading point, but only as a further thing.
2	an issue. It is paragraphs 37 to 40. (Pause).	2	MR TROWER: But the important point is that it is a defence
3	MR JUSTICE HILDYARD: Yes.	3	in the context of legal proceedings. It does not matter
4	MR TROWER: That chimes with the critical line in Ginty	4	whether you call it a pleading point or not. I do not
5	which was cited in the Post Office case that we looked	5	understand why my learned friend puts it that way but
6	at before in the judgment of Lord Justice Geoffrey Lane	6	the point is that it is a defence in that context and
7	at page 134 of the Post Office case.	7	there simply isn't room for it once the mandatory
8	"The plea of circuity of action is not usually found	8	set-off has taken effect.
9	in these days(Reading to the words) but is	9	MR JUSTICE HILDYARD: I understand your point. Your point
10	a valid plea."	10	is circuity of action as a defence is that, although
11	So there one has the concept of it being a pleaded	11	a substantive defence, its prerequisite is that the one
12	defence which arises in proceedings where set-off is not	12	should cancel the other?
13	relevant.	13	MR TROWER: Indeed and that is if you like the third way of
14	Then the last case is a case I shall call	14	looking at it. That comes through very strongly from
15	the Harding case, because I am completely in capable of	15	some of those cases, that it is a straightforward
16	pronouncing the first word in the title of the case.	16	indemnity over. My Lord, that was all I was going to
17	There are two parts in the judgments of	17	say on circuity of action. Can I then move on to
18	Lord Justice Scrutton and Lord Justice Sankey which your	18	the term agreement which was put variously as an express
19	Lordship may find helpful. Lord Justice Scrutton at	19	term and as an implied term?
20	page 384, and it is a paragraph beginning:	20	Now, it emerged during the course of Mr Marshall's
21	"The learned judge freed from this liability on	21	submissions that the express term was the word
22	a ground of not pleaded in a form stated by him of his	22	"repayment". That was the word that we were looking at
23	own suggestion."	23	to see what it meant. So what we understand
24	He then goes on and discusses what circuity of	24	the position to be is that he says that whenever
25	action is all about on page 385.	25	the word "repayment" is used, it should be read as
	Page 49	_	Page 51
1	There is a further description of circuity of action	1	"repayment out of own funds in the section 74.2(e)
2	in the judgment of Lord Justice Sankey at page 391.	2	sense".
3	The very last words on 390:	3	The first point in response is that where the word
4	"I now proceed to the consideration of circuity of	4	"repayment" is used and I think we do need to turn up
5	action which induced me to decide in favour of the	5	the note of that agreement where the word "repayment"
6	defendants."	6	is used in line 3 of paragraph 4 of the variable terms,
7	He makes the point that:	7	it is used to introduce the terms on which repayment is
8	"Since the Judicature Acts gave facilities for	8	to be made. That is what it is being used for. Page 5,
9	counterclaim and third party procedure, the doctrine of	9	tab 1, bundle 4.
10	circuity of action has neither been seen as necessary or	10	MR JUSTICE HILDYARD: Page, sorry?
11	as frequently resorted to as in former years."	11	MR TROWER: Page 5, tab 1.
12	And he then cites from Bullen & Leake and on down.	12	MR JUSTICE HILDYARD: Yes.
13	So what one gets from all of these cases is a strong	13	MR TROWER: The word "repayment" there is used:
14	focus on the emphasis of this is a defence to be pleaded	14	"The terms for repayment are "
15	in legal proceedings. That is what it is all about, its	15	So that is what clause 9 is doing; it is setting out
16	name slightly gives the game away. And our respectful	16	the terms. Then there are six repayment terms, each of
17	submission is that where in the present case you have	17	which is itself subject to the restrictions on repayment
18	the operation of a mandatory insolvency set-off, there	18	contained in clause 4.3of the standard terms and
19	is simply no room for the operation of the principle of	19	the subordination in clause 5 of the standard terms.
20	circuity of action.	20	We respectfully submit that it is difficult to see
21	MR JUSTICE HILDYARD: Having ordered that there should be no	21	how anything else which is properly to be characterised
22	pleadings, I am relieved to see that it is not really	22	as a term for repayment, which is what a limited
23	dealt with only as a pleading point. It is dealt with	23	recourse would be, can properly be construed into
24	as matter of substance although in point of fact,	24	the sub-debt agreement when it is structured in this
25	Lord Justice Sankey appears at the end to raise	25	way. That is the first point. The draftsman has put in
	Page 50		Page 52

the terms and effectively Mr Marshall is inviting a further term to be put into the words of this section by use of the word "repayment".

The second point is that the ambit of the repayment

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obligation is at the core of this agreement, that it is fundamental to this agreement and any restriction or limitation on the extent of the obligation, whether derived from a limitation in the source from which a repayment is to be made or otherwise, is something which can't be read into the word "repayment".

We respectfully submit, because there is simply no other indication on the face of the agreement that the source of the repayment was a relevant factor for the parties in describing the obligation to repay.

In particular -- and it is obvious, but it is worth restating -- there isn't anything on the face of the agreement which identifies, refers to or relates in any way to section 74.2(e), or the words used in section 74.2(e) by which all of this is said to have been inspired.

Now, as we understand it, one of LBL's submissions is that it is not surprising not to find express references to a limitation in recourse in the sub-debt agreement because nobody was thinking about unlimited companies when the standard terms were drafted.

that is self-evident from the face of the agreement itself as being something which was contemplated.

Mr Marshall also submitted to your Lordship that
the EC directive didn't contemplate unlimited companies.
Again, my Lord, we don't accept that submission. The EC
directive is entirely neutral on the legal
characteristics of persons capable of being regulated
entities. My Lord will not find that surprising, given
the different characteristics which artificial entities

the different characteristics which artificial entities have under different European jurisdictions, as my Lord knows.

We can give your Lordship more particulars if necessary. I appreciate that the material is not in evidence, but we are responding to something which is asserted, and we can easily put it in evidence if it is necessary. But to give your Lordship a few examples: in Ireland, the concept of unlimited liability companies is well known. There are at least three credit institutions and nine other authorised firms listed on the Central Bank's register of authorised firms which are unlimited companies. The three credit institutions are Wells Fargo, AIB Mortgage Bank and Bank of Ireland Mortage Bank.

A French equivalent is an SNC and there is at least one regulated bank which is an SNC, Banque Edel.

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I think this is part of some argument about the inappropriate use of the standard form agreement as well. In support of this, Mr Marshall submitted that the use of this form by an unlimited company was perhaps unique. He also said that unlimited companies were not standard borrowers, it was an unusual type of borrower. It was an unusual beast in the modern day world. He said once "such a rare thing", a very rare thing.

I am afraid we simply do not accept that. There is no evidence to this effect. In fact, as may not be that surprising when one considers the US tax reasons that caused LBIE to registered as unlimited: Merrill Lynch, Morgan Stanley, Goldman Sachs, and Credit Suisse all operate in the UK as banks through regulated unlimited companies. Goldman Sachs International has even appeared in Waterfall II as a respondent, your Lordship will recall.

It is also of some significance on this point that the sub-debt agreement itself contemplates that the borrower may be a partnership. If you look at clause 8 of the standard terms, it expressly contains reference to the borrower being a partnership and what happens in those circumstances. So unlimited liability with no limitation on the source from which the liability is to be discharged is therefore something

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We also understand there are examples of private banks
in Germany which are formed as KGs, which are a form of
limited partnership in which some members have limited
liability and some of whose members have unlimited
liability.
So it is simply not right to say that

So it is simply not right to say that the regulations pursuant to which these subordinated debt agreements were put in place with the INPRU reference in relation to capital advocacy at the beginning of them are subordinated debt agreements which were put in place against the background of an EC directive which didn't contemplate unlimited liability.

Finally on this area, my Lord, and it is a slightly different point, you asked me whether it was still the case that unlimited liability companies take the benefit of not having to file accounts. I said it was, and that is right for most unlimited liability companies, section 448 of the Companies Act. There is however a specific exception for unlimited liability companies carrying on businesses as banks and for their shareholders, which shows where those unlimited liability companies under section 448 do have to file accounts.

Now that shows two things. The first is that so far as banks which unlimited liability companies are

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1	concerned, one can't say they have taken that particular	1	qualification. There was a member of LBI, which is not
2	benefit of unlimited liability because they plainly	2	a member of the UK group, but was actually a regulated
3	haven't, and that was the context in which my Lord asked	3	entity, and it appears at the very top of the tree.
4	me the question. But I think what I am entitled to	4	I should stress, there are and were a few other
5	submit is that the companies legislation itself had in	5	regulated entities within the Lehman's group doing
6	mind the very fact that banking institutions may be	6	specific regulated activities which don't appear within
7	trading as unlimited companies.	7	the structure that people were considering at the time
8	We can all go and look at the accounts of CJ Hoare &	8	the emails were entered into.
9	Co are one of the best known unlimited liability	9	The reason that the concept of a regulated group was
10	companies which operates as a bank.	10	used at all we submit the obvious reason is that
11	MR JUSTICE HILDYARD: Mr Atherton said the differences	11	looking at the position of LBIE itself, it may have been
12	between limited and unlimited liability companies only	12	necessary to consider how others within the group
13	came into play in the event of insolvency but the	13	structure who were providing regulatory capital, in
14	agreement did not contemplate or insolvency was not	14	particular LBHI2, fitted into LBIE's regulatory
15	something in the minds of parties to it.	15	position. It is not more complicated than that.
16	MR TROWER: That may well be right. Your Lordship has what	16	That is made clear, we suggest, when one if
17	Mr Justice David Richards said on that subject, and it	17	we can just turn up for a moment the bundle of emails so
18	would be surprising if the parties were thinking in	18	that one can see what one gets out of them. We have two
19	a focused way in relation to insolvency in that sense.	19	groups of material. There are the emails behind tabs 1
20	MR JUSTICE HILDYARD: But my point is that on Mr Atherton's	20	to 4, which are tax emails or tax materials. They are
21	view of things which I would not hold him to but	21	backwards and forwards
22	on his view of things, the agreement cannot be any	22	MR JUSTICE HILDYARD: Which files?
23	different for a limited or unlimited	23	MR TROWER: I am so sorry. Bundle 5.
24	MR TROWER: Yes, my Lord, that must be right.	24	MR JUSTICE HILDYARD: These were our 11.30 to 12 o'clock
25	My Lord, the second aspect that I wanted to reply on	25	canter.
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1	in relation to express and implied terms is	1	MR TROWER: Yes, indeed they were. I am tempted to go at
2	the regulatory context and the emails in bundle 5 that	2	a gallop, but I need to go a little slower than that to
3	your Lordship was taken to.	3	make the point.
4	MR JUSTICE HILDYARD: Yes.	4	1 to 4 are materials between the Lehman group and
5	MR TROWER: As we understand the submission, it seemed to be	5	the Inspector of Taxes, which aren't really to the point
6	that at the time of the subordinated debt agreements,	6	so far as the regulatory aspect is concerned. They are
7	there was something called the LBUK regulated group,	7	simply talking about the purpose for the structuring
8	which means there was a concern to protect the interests	8	which is being put in place.
9	of the creditors of all members of the Lehman group,	9	Once you go to the ones where there is communication
10	including the creditors of LBL, is the way it was put by	10	with the FSA, they are all on LBIE paper. You get it
11	Mr Marshall. The core of the argument seemed to be that	11	from the bottom. And there is an obvious reason for
12	there was a regulatory need to protect the interests of	12	that: LBIE is the regulated entity. Perhaps
13	the creditors of those members to the same extent as	13	the clearest statement of what is going on can be seen
14	they were concerned to protect the interests of LBIE's	14	from the materials that are behind tab 5, which is 6
15	creditors. That seemed to be the thrust of the	15	October letter from LBIE to the FSA, which includes and
16	submission.	16	has behind it the application for change in controller.
17	We submit that the reason it is clear that	17	And you obviously get that on page 6. The target firm
18	the references to the group have nothing to do with	18	in respect of whom the controller is going to be changed
19	the protection of creditors of other members of the	19	is LBIE, as you would expect.
20	group is that as far as is relevant, none of them were	20	And the role if you go on to page 7,
21	regulated entities. In particular neither LBL nor LBHI2	21	the corporate controllers are LBHI1 and LBHI2, and that
22	were regulated	22	is the context in which they come in to the mix. Then
23	MR JUSTICE HILDYARD: I think you said LBIE was the only	23	if you go on to page 13, you have a pithy description of
24	one.	24	the rationale behind the acquisition in 5.3, focusing of
25	MR TROWER: Yes. The only thing there is this	25	course as you would expect on LBIE's position. Then
	D 50		D 20
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1	your Lordship sees a description of what is happening in	1	the position.
2	relation to the sub-debt in 5.5.	2	We were not quite sure we understood where that
3	Then if we go on to tabs 6 and 7, which was a notice	3	particular bit of the argument takes one I will come
4	of approval behind tab 6, change of control page 1	4	on to the broader point in a moment. But isn't any part
5	change of control of Lehman Brothers International	5	of our case that there is a separate item in the form of
6	Europe. So of course one would have expected that is	6	the section 74 claim against its members which can be
7	what one is focusing on as LBIE.	7	included within LBIE's regulatory capital. We don't say
8	Then tab 7, there is another letter from the FSA in	8	that. Of course the shares held by the members which
9	relation to group restructuring and change of control.	9	are paid up have generated payments and are subject to
10	And in the substantive paragraph the focus there is on	10	restrictions on their repayment, which render them
11	the sub-debt facilities provided to LBIE, if your	11	suitable to be counted as regulatory capital
12	Lordship would just read to the end of that. (Pause).	12	MR JUSTICE HILDYARD: This is a slightly different point.
13	"The firm" is, as my Lord knows, a technical term	13	This is on the schedules as to what the assets of the
14	used by regulators, which means the regulated entity,	14	company are taken to be, and he accepted that the equity
15	and that is LBIE. Just to make that point good, the way	15	was an asset but not that the call in respect of
16	"firm" is used in the FSA handbook is it is defined to	16	unlimited equity
17	mean "an authorised person":	17	MR TROWER: Yes. The short point on that, I do not contend
18	"An authorised person is a person who has permission	18	that a call under section 74, that statutory cause of
19	to carry on one or more regulated activities and a	19	action, is taken into account for regulatory capital
20	person is any person including(Reading to the	20	purposes. But the answer to that is sort of, so what?
21	words) and a partnership."	21	It does not affect the position one way or the other.
22	So it is clear that what is being dealt with here is	22	It does not have anything to do with the question of
23	regulation in relation to LBIE and LBIE alone. My Lord	23	whether a right of recourse by the borrower against the
24	was taken to tabs 8 to 11. It is difficult to see what	24	contributories is to be treated as an asset of the
25	help one gets from them because they are subsequent to	25	companies, which is the question we are looking at for
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,	the data of the end and in the data are consistent to the constitution of the constitu		
1	the date of the subordinated debts agreement in any	1	the purposes of determining the construction point which
2	event. I was not proposing to say much more about them.	2	Mr Marshall is raising.
3	I was not quite clear what it was that	3	So we do respectfully say that the mere fact that
4	MR JUSTICE HILDYARD: I think Mr Marshall said he was not	4	the call against the members happens to be available to
5	relying on them as any evidence of intention, but simply	5	a company which is an unlimited liability company in
6	as confirmation of what was then ie before	6	the event of an insufficiency is not taken into account
7	the contract was entered into the regulatory	7	for regulatory capital purposes simply does not tell
8	architecture. MR TROWER: As we say, the overall point we make is that	8	
9		1 0	your Lordship anything one way or the other on the
	**	9	question of construction which Mr Marshall invites your
10	the regulatory architecture simply required regulation	10	question of construction which Mr Marshall invites your Lordship to conclude in his favour.
11	the regulatory architecture simply required regulation of LBIE to the extent that there was other group	10 11	question of construction which Mr Marshall invites your Lordship to conclude in his favour. We simply do not understand why it is there should
11 12	the regulatory architecture simply required regulation of LBIE to the extent that there was other group involvement. It was in relation to the regulatory	10 11 12	question of construction which Mr Marshall invites your Lordship to conclude in his favour. We simply do not understand why it is there should be a limitation in the right of recourse against
11 12 13	the regulatory architecture simply required regulation of LBIE to the extent that there was other group involvement. It was in relation to the regulatory capital that was being provided from elsewhere within	10 11 12 13	question of construction which Mr Marshall invites your Lordship to conclude in his favour. We simply do not understand why it is there should be a limitation in the right of recourse against the members merely by reason of the fact that it is not
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1	assignability was concentrating on the factual matrix	1	have to look at the subordination provisions including
2	aspect of assignability, because he took your Lordship	2	within them 5.1(a), which is focusing on
3	to what Lord Hoffmann had to say in the investors	3	the circumstance in which insolvency might have
4	compensation scheme case about not taking into account	4	occurred.
5	assignability when you are thinking about the extent to	5	There is a definition, as one would expect, of
6	which you can look at factual matrix.	6	insolvency on page 7 of the subordinated debt agreement
7	Now that is as may be, that goes both ways.	7	and insolvency officer.
8	The real point in relation to assignability is that	8	MR JUSTICE HILDYARD: So when Mr Justice David Richards
9	the sub-debt agreement and the shares, even if they were	9	said, as he did in the judgment at first instance in
10	to go elsewhere within the Lehman group were capable of	10	Waterfall I:
11	being assigned. There is no restriction, save for the	11	"There is no evidence to suggest anyone(Reading
12	consent of the FSA in relation to the sub-debt agreement	12	to the words) any such consideration was given."
13	and for other members in relation to the shares on	13	What do you say about that? Was he simply talking
13		14	about LBIA as an unlimited
	assignments.	15	
15	So the point we make is that the agreements	16	MR TROWER: No. I think all he is saying there is that
16	contemplated that the lender under the sub-debt and		there were some well, what he is actually referring
17	a contributory of LBIE may well become different	17	to are a number of interviews that were carried out with
18	entities, albeit within the same group. It seems	18	various people by the office holders.
19	likely. That is, we respectfully suggest, a clean and	19	There is a question of: did anyone subjectively
20	comprehensive answer to the suggestion that somehow	20	think through how this would all work out in the event
21	the structure does not make sense. The structure does	21	of insolvency. And subjectively, that may be right.
22	not all contemplate that the inbound claim and	22	What that does not help your Lordship at all on is
23	the outbound claim are always going to be in the same	23	the question of construction of the agreement:
24	hands, and it is as simple as that.	24	the objective issues that have to be taken into account
25	MR JUSTICE HILDYARD: Tracking back again and again	25	for those purposes where it is plain as a pikestaff that
	Page 65		Page 67
	1 age 03		1 age 07
1	harping on, for which apologies: am I to take it that	1	the agreement was contemplating the consequences of
2	the context did not in the parties' minds include	2	insolvency. It is the very essence of the subordination
3	looking at the consequences on insolvency, as	3	apart from anything else. The only time you need it is
4	Mr Atherton suggests?	4	the insolvency.
5	For the purposes of the implied term, or	5	So I think it is difficult to put too much weight in
6	interpolation of the term, it may be that	6	terms of an argument based on what it is that is said by
7	the authorities rather suggest that you have to say	7	Mr Justice David Richards there. He was not looking at
8	it is a state of things which the parties did not	8	it in the context of a question of construction of
9	contemplate. Otherwise the court might think if you	9	the agreement, I think he was doing it in the context of
10	can't say that, they just decided to keep it out of	10	giving it some general background as to
11	account or made a mistake or some such, from which	11	the circumstances in which they came to be entered into.
12	the court should not save them.	12	It is no different when one steps back and thinks
13	So the driver on implication or interpolation is to	13	about it from any situation in which what appeared,
14	say this was a circumstance not envisaged at the time.	14	doubtless to everyone at the time, to be a well
15	The problem with that, if you have to rely on it, is	15	capitalised international bank based in
16	that you then knock out of the context this particular	16	the United States. People were not on the whole
17	consideration in terms of looking at how the agreement	17	thinking about the prospect of insolvency. Why would
18	is otherwise to be construed. What do you say I should	18	they be? This was 2006, not 2008.
19	do in that respect?	19	MR JUSTICE HILDYARD: This was a point which Mr Atherton
20	MR TROWER: My Lord, it is plain, we say, that the parties	20	raised and which I think he said was in support of
21	must have contemplated the insolvency context,	21	Mr Marshall at 5.9 in his note. And I freely admit that
22	objectively speaking, because of the terms of	22	I had not really spotted that in Mr Justice David
23	the sub-debt agreement itself.	23	Richards' judgment. I turned it up when I saw that,
24	You only have to look at the subordination	24	because it caused me surprise.
25	provisions and the way that they are drafted you only	25	MR TROWER: As is always the way when one picks up
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1	statements made by judges in cases	1	a informal insolvency and the other is not an informal
2	MR JUSTICE HILDYARD: Absolutely. I agree with what you are	2	insolvency. To that extent, if and insofar as
3	going to say there.	3	the argument is made against us that the parties simply
4	MR TROWER: one has to think about the context in which	4	did not contemplate insolvency at all and therefore you
5	it was said.	5	have to fill a gap, which includes the implication of
6	MR JUSTICE HILDYARD: Maybe I have overegged the point, but	6	the term which they wish to imply, if that is the point
7	I was trying to work out what relevance it had.	7	that is actually being made, we would respectfully
8	MR TROWER: On the construction point certainly, it really	8	submit that the express terms of the subordination make
9	does not have any relevance at all. How can it?	9	that an extremely difficult point to pursue.
10	MR JUSTICE HILDYARD: No.	10	MR JUSTICE HILDYARD: Well, in Aberdeen City Council, which
11	MR TROWER: The whole purpose of this agreement was to	11	I do not think is in the bundles, because I assume it is
12	provide for subordination in the event of an inability	12	summarised at some length in Arnold v Britton, there was
13	to pay the senior liabilities in full. So it	13	as I understand it, a discussion by I think Lord Clarke
14	contemplated circumstances of what would happen in	14	as to the difference between implication and the process
15	circumstances of financial distress.	15	of, as it were, benign construction or what they call
16	MR JUSTICE HILDYARD: But then that is generally true, as	16	"the internal context".
17	I have said and you tell me if I am wrong, and maybe	17	MR TROWER: Yes. There was a bit of a move away from
18	· · · · · · · · · · · · · · · · · · ·	18	•
18	Mr Atherton will shake his head vigorously it could have a bearing on implication or interpolation because	19	that — or not move away, but Marks & Spencer reformulated the approach in the sense that
	of the difficulties the court has in determining whether	20	**
20	<u> </u>		Lord Neuberger stressed that they are two slightly
21	there is a gap which it is reasonable and necessary and	21	different exercises. But yes, subject to that.
22	in accordance with the contract as a whole to plug, or	22	MR JUSTICE HILDYARD: If you are reliant, as Mr Marshall at
23	whether it is an error such that the court should not	23	any rate was as his fallback position, on implication
24	relieve the parties, or alternatively should assume that	24	and accepting the reaffirmation as some would see it of
25	they addressed it and decided not to do anything about	25	orthodoxy as to the conditions in which you can imply or
	Page 69		Page 71
	1 age 07		1 age / 1
1	it because they could not agree on it, it was too	1	interpolate a term, is it relevant for me to have in
1 2	it because they could not agree on it, it was too difficult, or whatever it is.	1 2	interpolate a term, is it relevant for me to have in mind that the parties would have been focused on
2	difficult, or whatever it is.	2	mind that the parties would have been focused on
2 3	difficult, or whatever it is. MR TROWER: Yes, yes. Well, we respectfully submit that it	2 3	mind that the parties would have been focused on insolvency and if they had wanted to deal with it in
2 3 4	difficult, or whatever it is. MR TROWER: Yes, yes. Well, we respectfully submit that it does not really help very much one way or the other that	2 3 4	mind that the parties would have been focused on insolvency and if they had wanted to deal with it in a way which it said was necessary, they would have done
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2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24	difficult, or whatever it is. MR TROWER: Yes, yes. Well, we respectfully submit that it does not really help very much one way or the other that subjectively speaking people were not focusing on the imminence or indeed the medium-term possibility that this might happen. Sort of, so what, is the way we would look at it. MR JUSTICE HILDYARD: But do you pray it in aid that they must have been thinking, or the objective observer would have thought that they were thinking in order to add any firepower against implication? MR TROWER: Well, the core of our argument in relation to implication is that the terms of the agreement are clearly set out sorry, not the terms of the agreement are clearly set out in a context in which the parties were considering two possibilities of the subordination condition being required to be fulfilled. The first is the possibility of an order being made for winding-up and the second is where there is no order made for a winding-up. So yes, I pray it in aid in that sense, that it was essential in order to understand the way the subordination worked that the parties were	2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24	mind that the parties would have been focused on insolvency and if they had wanted to deal with it in a way which it said was necessary, they would have done so? MR TROWER: Yes, my Lord, it is absolutely relevant. It must be. Of course, there may be circumstances, I would accept, where notwithstanding that, the business necessity test, the of course test would still be satisfied. But it is MR JUSTICE HILDYARD: You rely on it as another nail in the process of implication? MR TROWER: It really is not something which put it this way: the more the agreement actually expressly deals with something and contemplates something, the less straightforward it is for the court to imply a term that covers the same ground. MR JUSTICE HILDYARD: Because it would be doing this is what they, in a rightly ordered world as it has turned out to be, should have done, rather than this is what actually they did do, sub silentio, or that which anyone would say of course they must have left that out by mistake.

miles from that situation, given what this agreement was actually all about, which was about the ability to go obtain reproprient of the subordanced debt in the context of financial distress. MR LIGITE HILDYARD. So it may be as to I and 3 it is really about not implication but either reproprient, which may be so to I and 3 it is really about not implication but either reproprient, which may be so to I and 3 it is really about not implication but either reproprient, which may be so to I and 3 it is really about not implication but either reproprient, which may be so to I and 3 it is really about not implication but either reprograve, which is so solvency. MR TROWER. Yes, which I will come on to in a moment. I have one or two separate points to make. Before I get to 52, can I deal with one point that 1 is was are along against to by Mr Marshall in relation to 67 and 17? This is, is I understood the submission, he said 1 the dray are strong pointess to be fact that there is to be 14 they are arone pointess to be fact that there is to be 14 they are arone pointess to be fact that there is to be 14 focused on the word "in" as being the reason that you could see it was — can we put the proper 1 the contributiones. MR TROWER: If you go to clauses 67 and 78 on page 12 of the agreement of the arone is the solution of the arone in to for the first time the question of what is entire to the inclination grow. The same points to the source could red extend to 10 the contributiones. MR TROWER: So this is a representation by the borrower that it is upped, it is not applied at a marker of the company's new and the position this way; even an autism of the representation by the portion of what is the nature of the gibt. The arone is a proper than their proper to the facilitation pursuant to the contribute of the interest of the semination of a an all marked or properly in the above these provisions is that they are concerned with protecting of the sub-ordination by a surely for the sub-ordination by a surely for the sub-or	-			
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,	24	Lordship on the point that is made by Mr Marshall. It	24	will not arise unless and until you go into liquidation.
Page 74 Page 76	25	does not help.	25	MR TROWER: No, it will. The decision of the Court of
Page /4 Page /6		D 7.		D 7/
		Page /4		Page /6

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1	Appeal was that we presently have a right to prove in	1	the statutory right under section 74 once the company
2	the insolvencies of our contributories insofar as they	2	went into liquidation was part of the company's capital.
3	have become distributing.	3	And we do submit that on any view, it is an asset of
4	Now there is an issue because Mr Arden's clients are	4	the company's, whoever the person is who is entitled to
5	not yet in distributing administration	5	realise it
6	MR JUSTICE HILDYARD: I understand what you are getting at.	6	MR JUSTICE HILDYARD: Where would you place it in
7	And because of the rule that you must assess or estimate	7	the accounts?
8	the proof at the time, it converts the prospect into an	8	MR TROWER: The accounts?
9	estimatable actuality.	9	MR JUSTICE HILDYARD: Not capital.
10	MR TROWER: Indeed. We accept that the officeholder in	10	MR TROWER: It would certainly not be capital, no.
11	the insolvency of our contributories will have to	11	MR JUSTICE HILDYARD: What would it be?
12	estimate the value of our claim because it is not	12	MR TROWER: It would be a debt, insofar as it was possible
13	a straight call. There is an issue as to whether any	13	to give it a value. It would be a receivable from
14	discount should be given for the fact that we are not	14	the moment in time at which the right to prove arose.
15	yet in liquidation. That is a question, but that is not	15	And properly prepared accounts would have to identify
16	for your Lordship today.	16	what was the appropriate figure to give it for
17	But we do say it is very difficult to see why that	17	the purposes when one knew what the likely recovery was
18	is not an asset in the form of a legal right to prove.	18	going to be.
19	That is what the company has at the moment: a legal	19	MR JUSTICE HILDYARD: So in an unlimited company, you would
20	right to prove. Why is that not an asset?	20	always have a balanced account, would you?
21	The third stage is let's assume that we were to go	21	MR TROWER: Well, no, because well, we are dealing with
22	into liquidation. Our rights in those circumstances to	22	a rather special context here because we are dealing
23	make a call under section 74 are also an asset of the	23	with a context in which the right we are here concerned
24	company's even before the call is made. That was the	24	with is a right to prove in the insolvency of our
25	point on which there was potential disagreement between	25	contributories. That is what I am focusing on, so it is
	Page 77	-	Page 79
1	Lord Justice Briggs and Lord Justice Lewison.	1	quite difficult to
2	We say it is a chose of action in the form of	2	MR JUSTICE HILDYARD: It is a fiendish thing to value for
3	a debt that is what section 80 says it is based	3	the purposes
4	upon on the contract of membership, although it moves	4	MR TROWER: Of course, and it may well be that anybody who
5	through to have the attributes of the statutory right	5	is required to put it into their accounts would give it
6	under section 74 and section 80. It remains our on	6	no value because they could not do so safely.
7	this core point, we do submit that	7	I perfectly accept that. But that is not really
8	Lord Justice Lewison's doubts on this point are	8	the question for my Lord for present purposes;
9	misplaced, and they were doubts but they were not	9	the question is characterising the right.
10	characterised as he didn't positively disagree. And	10	MR JUSTICE HILDYARD: Yes.
11	the view of Mr Justice David Richards and the view of	11	MR TROWER: One point we do make, the last stage when one is
12	Lord Justice Briggs are to be preferred.	12	looking at the nature of the various assets that arise
13	MR JUSTICE HILDYARD: You equate those, do you?	13	here: it was common ground as we understood it amongst
14	MR TROWER: I do. On this particular point, we say	14	the judges in the Court of Appeal that once the proceeds
15	Mr Justice David Richards did go as far as	15	of the proof or the call are received, they are an asset
16	Lord Justice Briggs.	16	of the company's. There didn't seem to be any doubt
17	It is of some relevance when looking at what	17	about that.
18	Lord Justice Lewison said, some relevance, that what he	18	MR JUSTICE HILDYARD: How could there be?
19	was looking at and the cases he was looking at were not	19	MR TROWER: Quite, which is not a bad starting point for
20	concerned with the question of whether or not the right	20	saying that the cause of action by which they had got
21	to call under section 74 was an asset of the company's,	21	in
22	but with whether the statutory right was to be treated	22	MR JUSTICE HILDYARD: The same would apply if you recovered
23	as part of the company's capital.	23	in a misfeasance claim. Once you got it in, it would
24	If one looks at those cases, that is what they were	24	definitely be. But what do you say in a misfeasance
	all leaking at the question of whether or not	25	claim or some statutory claim would be an asset which is
25	all looking at: the question of whether or not		<u>,</u>
25	Page 78	20	Page 80

1	to be put in as a receivable in the company's account?	1	MR JUSTICE HILDYARD: Yes, that is it.
2	MR TROWER: You have to identify what it is you are talking	2	MR TROWER: The case we were shown this morning, yes.
3	about. I quite accept there are some causes of	3	MR JUSTICE HILDYARD: Yes. is that a good moment?
4	action there are issues, and this is actually one of	4	MR TROWER: I have not quite finished on 5.2, but it will
5	the points that I think was raised before the Supreme	5	take me a few more minutes to do so, and then I was
6	Court there are issues about how one characterises	6	going to go on to issue 3.
7	the claims that are made, for example, by a liquidator	7	MR JUSTICE HILDYARD: Very good.
8	for preference and for	8	(1.05 pm)
9	MR JUSTICE HILDYARD: There is some statutory claim.	9	(The short adjournment)
10	MR TROWER: Some statutory claims, where the cause of action	10	(2.00 pm)
11	under the statute, the liability only ever arises at	11	MR JUSTICE HILDYARD: Good afternoon.
12	the moment in time at which the court grants the relief,	12	MR TROWER: My Lord, two more points on 5.2 before I move
13	pursuant to a claim brought under the statute by	13	on.
14	the officeholder.	14	The first point relates to a slightly different but
15	They are conceptually very different from	15	linked aspect of the interrelationship between this
16	circumstances in which what you have is a claim, which	16	argument on what the Court of Appeal actually concluded
17	is	17	in Waterfall I.
18	MR JUSTICE HILDYARD: Where you are revealing the result	18	All of the members of the Court of Appeal considered
19	rather than imposing it after	19	that it was wrong to characterise the argument that
20	MR TROWER: Indeed. The liability is there already, we know	20	statutory interest could be funded from a call or
21	that, under section 74 and section 80. We know it goes	21	a realisation of the members' liability to contribute
22	back to the contractor membership. What is happening	22	under section 74 is boot straps. They said that
23	under the statute is that the mechanism for bringing	23	argument was wrong. They agreed that statutory interest
24	the money in is by way of call actually by the court,	24	could be funded from a call.
25	although delegated to the liquidator.	25	The reason they all reached that conclusion was that
23	antiough delegated to the riquidator.	23	The reason they air reached that conclusion was that
	Page 81		Page 83
1	MR JUSTICE HILDYARD: This is still linked to	1	statutory interest ranked before members and as an
2	your antecedent right point.	2	adjustment call could be made to protect members'
2 3	your antecedent right point. MR TROWER: Indeed.	2 3	adjustment call could be made to protect members' rights, it made no sense that a call could not also be
2 3 4	your antecedent right point. MR TROWER: Indeed. MR JUSTICE HILDYARD: It is an existing right under	2 3 4	adjustment call could be made to protect members' rights, it made no sense that a call could not also be made to fund statutory interest. They also agreed that
2 3 4 5	your antecedent right point. MR TROWER: Indeed. MR JUSTICE HILDYARD: It is an existing right under the terms of the subscription.	2 3 4 5	adjustment call could be made to protect members' rights, it made no sense that a call could not also be made to fund statutory interest. They also agreed that sub-debt ranked between statutory interest and members.
2 3 4 5 6	your antecedent right point. MR TROWER: Indeed. MR JUSTICE HILDYARD: It is an existing right under the terms of the subscription. MR TROWER: Yes.	2 3 4 5 6	adjustment call could be made to protect members' rights, it made no sense that a call could not also be made to fund statutory interest. They also agreed that sub-debt ranked between statutory interest and members. That is why they put it.
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2 3 4 5 6 7 8	your antecedent right point. MR TROWER: Indeed. MR JUSTICE HILDYARD: It is an existing right under the terms of the subscription. MR TROWER: Yes. MR JUSTICE HILDYARD: Yes. MR TROWER: The root of all these points obviously goes to	2 3 4 5 6 7 8	adjustment call could be made to protect members' rights, it made no sense that a call could not also be made to fund statutory interest. They also agreed that sub-debt ranked between statutory interest and members. That is why they put it. So we do respectfully suggest, given that this is the case and they all agreed that the sub-debt ranked
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1	made to contributories in order to pay those prior	1	relation to paragraph 63 of Mr Arden's skeleton
2	liabilities, which is the logical consequence of	2	argument, which we have spent a little bit of time on.
3	Mr Atherton's position.	3	But I was going to come to in a moment, if I may, when
4	We say that makes no commercial sense, all the more	4	I have been through the various steps in the argument
5	if one assumes that is the sub-debt holder and the	5	that have been put against us.
6	contributory are separate people which, as I have made	6	What is contended as we understand it is that and
7	submissions to your Lordship already, is within	7	on issue 3 we are dealing with value the amounts to
8	the contemplation of the clause.	8	be included in the section 74 claim in respect of the
9	My Lord, that is all I was going to say further on	9	sub-debt is the amount estimated as the provable debt in
10	5.2. The only other point that sort of linked	10	accordance with rule 2.81. That is the way it is put
11	although it leads into issue 3, which is the next one	11	against us.
12	I am going to deal with is that in his paper this	12	What is said therefore is that the same estimation
13	morning, much was made by Mr Atherton of the fact that	13	process applies to both sides of the account. You have
14	LBHI2 is not yet in distributing administration.	14	to look at the estimation, take it in one side and out
15	Therefore, the asset in the form of the claim against	15	it goes the other side. The way Mr Atherton put it in
16	the contributories is, he says, contingent.	16	his submission was the reason for that is that
17	That rather misses the point because the whole	17	the sub-debt contribution claim is entirely and
18	purpose of the Waterfall application and one can see	18	I think he used the word "parasitic" on the sub-debt
19	this in the formulation of issue 3 is to assess	19	claim itself and it was false to draw a distinction
20	whether there would be a claim in a distributing	20	between them.
21	insolvency of LBHI2. That is the purpose of it. We are	21	The idea of estimation in this context is that
22	looking at it in that hypothetical context. We are not	22	unless you estimate under rule 2.81 as we understood it,
23	looking at it in the context of both of the	23	you cannot work out what the extent of the debts and
24	contributories actually being within a distributing	24	liabilities are for section 74 purposes. That was as
25	process at the moment. The reason it is necessary is so	25	we understood it the way the point is put.
	Page 85		Page 87
1	that the parties can assess what their position will be.	1	Our case is that we submit it is not the correct
2	One day of course, there will have to be	2	approach. We need for this purpose I am afraid to go
3	a distribution. LBHI2 is sitting on a slug of money, it	3	back again to what Lord Justice Lewison said in those
4	needs to know how it is going to distribute it.	4	critical passages in his judgment, paragraph 41 in
5	The whole purpose of these applications is to bring	5	particular, in bundle 1 behind tab 9.
6	the parties closer together in understanding of what	6	The critical question here is to identify what
		7	Lord Justice Lewison means, we suggest, when he
7	their legal rights and remedies are.		. 55
8	As I say, issue 3 does proceed on the basis that we	8	describes the subordinated debt as a contingent debt,
9	are proving in a distributing process for the	9	and more particularly what is the nature of
10	contributory, which we will come on to. My Lord, I was	10	the contingency.
11	going to move on to issue 3 next. I was going take my	11	If you go back to the language of paragraph 38,
12	Lord through a summary by way of response to what has	12	further back, he describes clause 5 of the sub-debt
13	been said against us as to the way we say it works.	13	agreement as:
14	We have prepared, and I hope it is helpful and	14	"Giving rise to a contingent right to payment
15	I will go through it after I have made some points.	15	contingent on the satisfaction of the relevant
16	We have prepared a table which explains what we say	16	condition."
17	happens on the basis of varying possibilities as to	17	Now what that means, we submit, is that the nature
18	the position of the contributories. The reason we have	18	of the contingency is having enough money to pay
19	done it is twofold, really. First of all, for my part	19	the liability and still be solvent. That means it is
20	I find it helpful sometimes to see in the form of	20	necessary to have enough money to pay the liabilities
21	figures what one says the consequences of a particular	21	higher in the Waterfall. Having enough money to pay is,
22	argument are. And secondly, it is designed to try and	22	as your Lordship put it in I think some of the
23	assist on how it is that we say in various hypothetical	23	discussion, is the essence of dependency. That is
24	situations the result works through, with particular	24	the distinction, if you like, between dependency and
25	reference at the end to the point that has been made in	25	a conventional contingency.
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So if one wants to think of it in the language of dependence and contingency, it can properly be said that contingency in this case is nothing to do with usual contingency of whether or not an extraneous event will or might occur. It is all about whether or not the stage is reached within the insolvency at which payment can be made.

Against that background, we submit the point that Lord Justice Lewison was making in the third sentence of paragraph 41, which is the point we have spent a little bit of time on, is that the contingent characteristics of the debt arise not because that is the way it is characterised by the statutory code but because that is what the sub-debt agreement provides for. That is what he means.

Put another way, its positions in the rankings in insolvency is as an unsecured provable debt, but the agreement amounts to an enforceable and effective means of subordinating the debt to a lower level in the Waterfall. That is what he is talking about. We suggest that one can also see this is what he must have meant from the opening sentence of paragraph 41, the very first one:

"I do not consider that it matters whether or not a proof is lodged. What matters is the subject matter 1 provable nor payable at all until such time as a surplus 2 arises. Sub-debt is provable but not to any extent that may impair the subordination. 3

> So you have a very similar analogous situation, we suggest, between the subordinated debt and the way one needs to think about it and statutory interest.

Now, Waterfall I established that notwithstanding the fact that statutory interest was not payable because there was no surplus, it was still a liability in respect of which a contribution could be sought from the contributories. That was the essence of one of the holdings.

What this shows is that where the characteristics or features of the liability include a contingency in the form of an ability to pay, the valuation consequences of that contingency do not fall to be taken into account in quantifying the outbound section 74 claim, otherwise you could not have had a situation in which in statutory interest it was possible to have a call to recover.

So that is the essence of the way we say my Lord can most helpfully approach this question. The analogy with statutory interest is a good one, it is an apt one. It helps explain the approach that Lord Justice Lewison took in paragraph 41 and gives it sensible meaning in

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of the proof."

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He was therefore quite conscious of the fact that while proof was permitted in principle, and indeed that was the whole purpose of it, it was only permitted to the extent that it did not impair the subordination.

We suggest the position of statutory interest provides a helpful analogy here. Because like the subordinated debt, the statutory right to payment of interest only arises where a sufficiency condition is satisfied. In the case of interest, it is if and when a surplus is established. That is the way it was put by Mr Justice Richards in the Waterfall IIA judgment.

Your Lordship may recall -- and I am not sure whether we put it in the bundles -- but when your Lordship was hearing the withholding tax case, you had to consider the nature of statutory interest, and you adopted what Mr Justice Richards had said in Waterfall IIA. It is as and when the surplus is established, that is the concept which underpins it.

In the case of the subordinated debt, one has a very similar concept. One has a case of insolvency as defined within the subordinated debt. In both cases, the liability is not one which is given value before the time the condition is satisfied. What I mean by that is inbound value. Statutory interest is neither

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1 the context of the nature of the valuation process which 2 was going on, which is very far removed from

the estimation process under rule 2.81.

4 Now, my Lord --

MR JUSTICE HILDYARD: You say Lord Justice Lewison was

6 simply saying that the contingency is not referable to

7 the ordinary statutory scheme, but arises from

8 the specific terms of the subordination agreement?

9 MR TROWER: Yes. He is recognising that what gives it its

10 characteristics is the subordination agreement, not an

11 insolvency ranking with it derived from the insolvency

scheme.

13 MR JUSTICE HILDYARD: Why is he wanting to make that point?

14 MR TROWER: His point here was that the debt was actually

provable. And the consequence of the debt being

16 provable in normal circumstances is that you would get

17 into a situation where you would go through

18 the estimation process. The issue as I think my learned

19 friend Mr Arden identified most clearly on the other

20 side was, well, the consequence of that would be

21 immediately to impair the subordination. Because if you

22 go through what one might characterise as a standard

23 estimation process, that is what you are bound to end up 24

25 Some of the cases my learned friend Mr Atherton put

1	in his note this morning in the context of subordination	1	sufficient funds to pay everything at levels 1 to 5,
2	agreements actually do talk about nil valuation, as	2	that is down to unsecureds, inclusive in the Waterfall,
3	my Lord will have seen. I do not know whether that is	3	and has done so with £100 cash left over. It has debts
4	where Lord Justice Lewison got it from, I do not think	4	and liabilities at the remaining levels of the Waterfall
5	if any of the material which Mr Atherton cited was	5	as follows. So we have statutory interest of £500,
6	actually cited to the Court of Appeal.	6	non-provable claims of £200 and sub-debt of £300.
7	MR ATHERTON: If it helps my learned friend, I think	7	Now because it has £100 cash in hand, it has
8	we refer to it in our notes. Mr Snowden made	8	a deficit of £900. Then you could perhaps read to
9	a submission based on Goode, the extract from Goode,	9	yourself the next three lines, which are the bases on
10	which talks about nil valuation.	10	which we proceed, which I think are relatively
11	MR TROWER: Yes, that must be where it was then. That is	11	uncontroversial.
12	where it comes from. But it does not come from	12	What we have done next is given two example,
13	a standard estimation process, we respectfully suggest.	13	example A and example B, and we have done it
14	So another way of thinking about this, which is	14	deliberately. Example A is obviously not the position
15	the way we put it in opening and we reiterated in reply	15	we have, but it is helpful to test. Because what it
16	by way of response to what has been said by my learned	16	does is it strips out the complication of set-off. So.
17	friends, is that what has happened under	17	"Although in admin the contributor is able to pay
18	the subordinated debt agreement is that the parties have	18	100p in the pound(Reading to the words) £900 is
19	agreed for the purposes of subordination to slot this	19	received."
20	liability in a different level of the statutory	20	And then it is easy, everything is satisfied in
21	rankings.	21	full.
22	Nothing, we suggest, that Lord Justice Lewison says	22	Possibility 2:
23	is inconsistent with that. It may be I think	23	"The contributory is able to pay 50p in the pound,
24	the very fact we have all spent a very long time	24	so you get £450 back from your £900 claim. The sums of
25	debating it indicates that it maybe was not expressed as	25	£400 and £50 are paid in accordance with the Waterfall
	Page 93		Page 95
1	clearly as we would have hoped. But that,	1	leaving a deficit comprising 150 in respect of the CCCs,
2	we respectfully suggest, is what he is driving at.	2	non-provables, and 300 in respect of the sub-debt.
3	It is noticeable I do not put a great deal of	3	The sub-debt does not become payable at all."
4	weight on this but it is noticeable that he does not	4	You then have:
5	use the concept of estimation anywhere in this. He	5	"The contributory is able to pay 90p in the pound
6	talks about value. He does not seem to have been	6	(Reading to the words) and £810 is received. Sums
7	thinking about going through a rule 2.81 process and	7	of £400 and £200 are paid in accordance with
8	coming up with a zero figure. So what was he thinking	8	the Waterfall. The prior ranking liabilities have
9	of doing? What he was thinking of doing, the way he was	9	therefore been satisfied in full. The sub-debt is
10	thinking about it, was what do I do with this inbound	10	payable. The sub-debt is partially repaid using the
11	claim? How do I think about it? What then happens to	11	balance remaining, £210."
12	the outbound claim? What I do with this inbound claim is I do not give	12	That is all relatively straightforward in the
13 14	What I do with this inbound claim is I do not give	13 14	absence of set-off. We then go over the page.
15	it any value because that is what the sub-debt tells me	15	LBIE's contributor is the holder of the sub-debt:
16	should happen. And that impacts not one jot, we say, by reference to the statutory interest analysis on what	16	"Although in administration the contributor is able to pay 100p,(Reading to the words) and set off
17	happens with the outbound claim.	17	against the aggregate amount of the deficiency."
18	I am going to deal with the Halesowen argument in	18	So you get effectively the sub-debt is satisfied in
19	a moment, but can I take your Lordship through	19	full by set-off and you get £600 into the estate, of
20	the illustrations, because I hope that helps to show you	20	which £400 goes in statutory interest and £200 goes on
21	how it is. I could leave you with a cold towel around	21	non-provables.
22	your head to do it yourself, but I think it is probably	22	The reason the set-off is permitted in full there,
23	easier to do it together, if you are happy to do that	23	and this is where we start to move into the Halesowen
24	way.	24	point and the paragraph 63point is because it does not
25	We start with some simple assumptions. LBIE has	25	interfere with the subordination in any way.
i .	- ·	1	
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1	The second point is:	1	creditors are valid. It is obvious when one thinks
2	"The contributory is able to pay 50 pence in	2	about it that set-off restriction clauses are required
3	the pound. A contribution claim is made and admitted in	3	in order to enforce such arrangements, because otherwise
4	the sum of £900 calculated(Reading to the words)	4	the subordination will very often not be effective.
5	sub-debt does not become payable."	5	The juridical basis for allowing both subordinated
6	So that is identical to the situation where you have	6	debt and set-off restriction clauses is that there is no
7	different ones.	7	reason why a creditor can't waive his right to take
8	Then the final example is one where one gets into	8	the benefit of a mandatory route of this sort so long as
9	the potential for paragraph 63, slightly more obviously:	9	it does not adversely affect the position of other
10	"The contributory is able to pay 90 pence in	10	creditors, which is all explained by Mr Justice Vinelott
11	the pound. A contribution claim is made and admitted in	11	in MCC in authorities bundle 2 at tab 69A.
12	the net sum of 666 calculated on the basis that	12	Now as my Lord will know, this case was all about
13	the amount of the sub-debt which goes into the set-off	13	whether holders of certain subordinated loan stock could
14	account in LBIE's administration is £233 being	14	properly be excluded from a scheme on the basis they had
15	the maximum sum which can be taken into account for	15	no interest. To answer that question, it was necessary
16	the purposes of set-off which does not prevent LBIE from	16	to decide whether contractual subordination was
17	meeting its prior ranking liabilities in full.	17	effective in English law.
18	LBIE must have a net provable claim of 666 to ensure	18	What is critical for present purposes is that this
19	that the dividends payable to it equal 600 to enable	19	required an analysis, so far as Mr Justice Vinelott was
20	the prior ranking liabilities to be paid. The sums of	20	concerned, of both Halesowen and British Eagle. So he
21	£400 and £200 are paid in accordance with the Waterfall.	21	was looking at the mandatory nature of set-off and the
22	In effect by way of set-off, the contributory receives	22	mandatory nature of pari passu in order to reach his
23	£210"	23	conclusions.
24	Which is equivalent to the result for the lender	24	One gets that from the top of page 1407 between A
25	under example A3.	25	and B. He then embarks on pages 1408 and 1409 in
	D 07		D 00
	Page 97		Page 99
1	What that example shows is the way the set-off	1	a detailed description of what was going on in
1 2	What that example shows is the way the set-off works, we respectfully submit, in the context of the	1 2	a detailed description of what was going on in Halesowen. The bit that matters starts at 1411 between
2	works, we respectfully submit, in the context of the	2	Halesowen. The bit that matters starts at 1411 between
	works, we respectfully submit, in the context of the restriction on set-off which is provided for by clause 7	1	Halesowen. The bit that matters starts at 1411 between C and D, and it goes down to 1412 between B and C.
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	24	arrangements in the airlines?	24	incremental steps towards the stage at which you have
Page 102 Page 104	25	MR TROWER: Yes, I think there was. Yes, they were.	25	done so much that your participation has to be governed
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1	by the mandatory rule. But that is right, the starting	1	this fit in with the Court of Appeal's finding that it
2	point is of course you can't. If you simply don't	2	was provable?
3	prove, you can't be forced.	3	MR TROWER: It fits in well, the point here is what you
4	One of the arguments based on Stein v Blake was that	4	can prove it as, to what extent can you prove it. It
5	set-off is not about actually proving, set-off is about	5	goes into the set-off account at zero.
6	a situation in which you it treat the inbound claim as	6	MR JUSTICE HILDYARD: It is that last bit you are really
7	having been proved for the purpose of taking	7	relying on. It is not a "I do not want to participate"
8	the account. But that is a rather different point to	8	but, "I shall not participate at more than nothing",
9		9	
	the question of what it is that people are entitled to		except in a MR TROWER: "or more than such amount as I can
10	do in order to ensure first of all that they comply with	10	
11	the contractual obligation they have taken, and secondly	11	participate in without affecting the subordination".
12	that they don't offend one of the mandatory aspects or	12	MR JUSTICE HILDYARD: Right.
13	characteristics of the statutory rule.	13	MR TROWER: That is entirely consistent with the language of
14	Maybe it is not right to think of the statutory rule	14	7B and does not cut across policy, because the policy is
15	as having mandatory and non-mandatory aspects, but they	15	all about protecting the other participants within
16	don't offend the principle that they can enter into an	16	the estate.
17	agreement which has an effect of abrogating the	17	MR JUSTICE HILDYARD: Yes.
18	statutory rule because nobody else is prejudiced by it.	18	MR TROWER: My Lord, that really is issue 3 as we see it.
19	MR JUSTICE HILDYARD: A pre-existing agreement?	19	I have explained the series of steps which I say one
20	MR TROWER: Yes, absolutely.	20	goes through. We have given our answer to what at first
21	MR JUSTICE HILDYARD: Because it is too late by the time	21	blush was Mr Arden's powerful submission but which on
22	it has to be a commitment not to do anything such that	22	analysis proves, we submit, to be flawed.
23	it would be perverse to treat it as having been put	23	We respectfully suggest that the way we submit your
24	forward.	24	Lordship should think about the valuation is the correct
25	MR TROWER: Yes. That was one of the issues the House of	25	way of thinking about it and is entirely consistent with
	Dags 105		Page 107
	Page 105		Page 107
1	Lords in Halesowen was thinking about, whether it	1	both what Lord Justice Lewison said in the Court of
2	interfered with and that was ultimately the real	2	Appeal on proper analysis and the approach the Court of
3	mischief in Halesowen whether it interfered with	3	Appeal took generally to allowing a contribution claim
4	the administration of the estate if it was allowed to	4	in respect of all items in the Waterfall higher than
5	take place at a later stage. But you have this where	5	the members.
6	you have people's pre-existing rights, that	6	MR JUSTICE HILDYARD: I will not put this very well, but
7	consideration does not come into play in the same way.	7	the unease one feels with it is because it rather feels,
8	I was inviting your Lordship to look at 8.17 of what	8	certainly at first blush, to be conjuring something out
9	is said by Mr Fuller, if your Lordship would just read	9	of a deeming or curious sequence of things. I mean, you
10	that. It is the last bit that is interesting, on	10	conjure up the 1.2 billion upon the footing that the nil
11	valuation. (Pause).	11	valuation is necessary in order to perfect
12	MR JUSTICE HILDYARD: Yes.	12	the subordination agreed. But because your deemed
13	MR TROWER: So in summary, my Lord, we say and this	13	proof, if you like, flies free of any particular
14	really is on Mr Arden's much-cited paragraph 63 point	14	subordination, you get the full amount. It just sort of
15	the right way of thinking through what would happen is	15	feels uncomfortable, it feels a bit like magic.
16	what we have set out in example B, footnote (iii). That	16	MR TROWER: It is no different, we respectfully suggest
17	is what happens.	17	it is a bit like the bootstraps point actually, in
18	That is what the subordinated debt agreement	18	a way. It was a kind of what my Lord has just said
19	provides for and there is nothing in the principles,	19	was the kind of reason why people wondered about
20	which are now relatively well established in relation to	20	the bootstraps point as part of the argument. How can
21	subordinated debt agreements which cuts across that in	21	you create your surplus out of which the interest is
22	any way as a matter of public policy.	22	paid by a call? And it is similar: a call where
23	That in short, my Lord, is what has been described	23	the interest has no value at that stage, it is a sort of
24	The state of the s	24	similar point.
24	as the Halesowen point.		
25	as the ratesowen point. MR JUSTICE HILDYARD: I must think this through. How does	25	We accept we are generating the call off the back of
	MR JUSTICE HILDYARD: I must think this through. How does		We accept we are generating the call off the back of
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1	a liability, of course we do. But when one thinks about	1	I was going to go on. I will be able to deal with
2	it the other way round, which is what are	2	these issues much more shortly than 1 to 3, just to make
3	the liabilities in respect of which the unlimited	3	a few short submissions on 7 and 9 if my Lord is content
4	liability contributories have committed to contribute to	4	with that.
5	their last farthing, we suggest it becomes less	5	MR JUSTICE HILDYARD: Yes.
6	problematic, because it is at the end of the day	6	MR TROWER: So far as 7 is concerned, there is no doubt that
7	a liability which in certain circumstances is capable of	7	the dispute has narrowed considerably. The original
8	being discharged.	8	issue was whether
9	MR JUSTICE HILDYARD: They are thinking, God, this is unfair	9	MR JUSTICE HILDYARD: Do you accept Mr Arden's description
10	because they've put a nil value on the liability which	10	of the extent to which it has been confined?
11	has given rise to my crisis.	11	MR TROWER: My Lord, I regret to say I cannot remember
12	MR TROWER: And if I were to be solvent, it would not	12	exactly how he put it. As we understand it, the only
13	matter. The only reason this matters is because I'm	13	remaining issue because the question of rateability
14	MR JUSTICE HILDYARD: But that is the point sorry to chat	14	has gone in the sense that it is now accepted all round,
15	it through with you. The unlimited shareholder thinks	15	as we understand it, that there is prima facie liability
16	it will all be all right in the end, as long as there	16	across the board for everything by both members, which
17	isn't a shortfall.	17	was the first bit.
18	MR TROWER: That is right. The only reason there is	18	The second bit of it, which is linked to it, is
19	a problem for the unlimited liability shareholder is	19	whether or not the court can or should restrict
20	because he himself is insolvent. And the way your	20	the officeholder in making a call. We say that the test
21	Lordship might like to think about it is that there is	21	is actually very simple when it comes to it. It simply
22	no principled reason why his insolvency should reduce	22	boils down to what is in the interests of the estate.
23	amount for which he is ultimately reliable, which is	23	And if the estate there may be plenty of
24	what the result would otherwise be, which is actually	24	circumstances in which it is not in the interests of the
25	what would happen if my learned friends are correct.	25	estate to make a full call against each member.
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	Page 109		Page 111
1	MR II ISTICE HII DVARD. I am going to ask you a question which	1	The most obvious exemple is where you have small
1	MR JUSTICE HILDYARD: I am going to ask you a question which	1	The most obvious example is where you have small
2	will seem rather hair raising because I ought to know	2	holder and a large holder and the large holder is fully
2 3	will seem rather hair raising because I ought to know the answer, but is it disputed in the Supreme Court	2 3	holder and a large holder and the large holder is fully solvent, and indeed the small holder is too. It may
2 3 4	will seem rather hair raising because I ought to know the answer, but is it disputed in the Supreme Court whether these things are provable at all?	2 3 4	holder and a large holder and the large holder is fully solvent, and indeed the small holder is too. It may well be perfectly appropriate in those circumstances to
2 3 4 5	will seem rather hair raising because I ought to know the answer, but is it disputed in the Supreme Court whether these things are provable at all? MR TROWER: What, section 74 claims?	2 3 4 5	holder and a large holder and the large holder is fully solvent, and indeed the small holder is too. It may well be perfectly appropriate in those circumstances to make a call which reflects the size of their
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1	whatever dividend we are going to get paid out of each	1	on the part-paid shares. So you achieve equalisation
2	of these insolvencies and receive whatever dividend we	2	through the distribution of the surplus. Those are
3	are going to get. So there is not going to be an	3	the cases in paragraph 181.
4	adjustment call in a case where you have two heavily	4	The cases in paragraph 183 of our skeleton are
5	insolvent contributories.	5	the ones where a call was necessary because although
6	So that was that. My Lord, on the whether or not	6	enough had been realised in the liquidation to pay
7	you can call point and whether or not we ought to be	7	the creditors in full, the surplus was not sufficient to
8	directed not to call. I realise it went in a particular	8	equalise the positions of part-paid and fully-paid
9	direction, you did have a debate with Mr Atherton about	9	shareholders without making but in both instances you
10	ex parte James. We respectfully agree with the approach	10	will only get to the stage of the an adjustment call
11	your Lordship took.	11	where the debts, liabilities and expenses have been paid
12	Just for your note, in a not dissimilar context,	12	in full.
13	Lord Neuberger had quite a lot to say about ex parte	13	Finally, on the contribution bit, as we understand
14	James in Nortel in the Supreme Court. We need not turn	14	it, LBL's position is they accept that there is no right
15	it up; bundle 4, tab 97, paragraph 122 and following.	15	of contribution available as part of the adjustment
16	MR JUSTICE HILDYARD: Tab 97?	16	process. That is plainly right on the authorities but
17	MR TROWER: Paragraph 122 and following. He followed just	17	they say there is a right of contribution which arises
18	the approach your Lordship indicated in explaining why	18	extraneous to it and is capable of being asserted in
19	it was but in that case it was all about liabilities	19	the present case by LBL against LBHI2.
20	under financial support directives and contribution	20	Now, because of the adjustment we were rather
21	notices and contribution notices under pensions	21	unclear to be frank as to what the basis for that
22	legislation. He followed just your Lordship's approach.	22	entitlement to an extraneous contribution would be but
23	Once the court had decided whether it was a provable	23	the important point for present purposes is that one
24	debt, an expense or fell into a black hole, that was	24	theoretical concept we can see that an extraneous right
25	the end to it. The court could not under ex parte James	25	may be capable of being exercised if there is, as
	Page 113		Dags 115
	Page 115		
	0		Page 115
1	principles say the administration behaved in a	1	between members, it can't come into play we suggest
1 2		1 2	
	principles say the administration behaved in a		between members, it can't come into play we suggest
2	principles say the administration behaved in a particular manner simply because the court thought	2	between members, it can't come into play we suggest until after the debts, liabilities and expenses have
2 3	principles say the administration behaved in a particular manner simply because the court thought it was the right thing to do. It is all based on legal	2 3	between members, it can't come into play we suggest until after the debts, liabilities and expenses have been paid in full.
2 3 4	principles say the administration behaved in a particular manner simply because the court thought it was the right thing to do. It is all based on legal rights.	2 3 4	between members, it can't come into play we suggest until after the debts, liabilities and expenses have been paid in full. The reason for that is that any contribution which
2 3 4 5	principles say the administration behaved in a particular manner simply because the court thought it was the right thing to do. It is all based on legal rights. That was the first point I wanted to make about	2 3 4 5	between members, it can't come into play we suggest until after the debts, liabilities and expenses have been paid in full. The reason for that is that any contribution which is sought by the overpaying member against
2 3 4 5 6	principles say the administration behaved in a particular manner simply because the court thought it was the right thing to do. It is all based on legal rights. That was the first point I wanted to make about issue 7. The second point I wanted to make about	2 3 4 5 6	between members, it can't come into play we suggest until after the debts, liabilities and expenses have been paid in full. The reason for that is that any contribution which is sought by the overpaying member against the underpaying member before the debts, liabilities and
2 3 4 5 6 7	principles say the administration behaved in a particular manner simply because the court thought it was the right thing to do. It is all based on legal rights. That was the first point I wanted to make about issue 7. The second point I wanted to make about issue 7: your Lordship did have a debate about whether	2 3 4 5 6 7	between members, it can't come into play we suggest until after the debts, liabilities and expenses have been paid in full. The reason for that is that any contribution which is sought by the overpaying member against the underpaying member before the debts, liabilities and expenses have been paid in full will cut across the rule against double proof. It will compete with the primary
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2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20	principles say the administration behaved in a particular manner simply because the court thought it was the right thing to do. It is all based on legal rights. That was the first point I wanted to make about issue 7. The second point I wanted to make about issue 7: your Lordship did have a debate about whether or not there will always be a need for an adjustment call. We are probably not into the realm of adjustment calls in this case, for the reasons I have indicated. We did in our skeleton argument when we were considering the cases on adjustment calls respectfully suggest that that is not always the case because we included in paragraphs 181 and 183 two different categories of case in which there needed to be and I deliberately use this word equalisation between shareholders. Those referred to in paragraph 181 are where the equalisation process is between part-paid and fully-paid shareholders and is achievable out of the surplus realised in the liquidation. In other words,	2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20	between members, it can't come into play we suggest until after the debts, liabilities and expenses have been paid in full. The reason for that is that any contribution which is sought by the overpaying member against the underpaying member before the debts, liabilities and expenses have been paid in full will cut across the rule against double proof. It will compete with the primary claim which is available to the company against the underpaying member. Because you have a situation where the underpaying member is still liable to the company for the full amount of the deficiency in the debts, liabilities and expenses and along comes the other member seeking a contribution. Now, to the extent that those are the same, related in any way to the contract of membership, it is almost certain to be problematic with the rule against double proof. So if it is a completely extraneous entitlement to contribution. Well, it is a bit difficult to tell, but we had understood the argument to be raised that

You were taken in that context, by Mr Marshall to

Black's Case. He did it at pages 91 and 92 of Day 4, in

Page 116

all until the fully-paid shareholders had been repaid

Page 114

the equivalent of the amount that had not been paid up

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1	support of a submission as we understand it that	1	that.
2	the rule against double proof does not apply to protect	2	I think I should say this. We don't accept
3	the creditors of LBIE because it is an unlimited	3	although I think I do accept that your Lordship can't
4	company.	4	decide this point for today's purposes that there is
5	He said that the analysis was analogous to the fact	5	any genuine analogy between what he says his recharge
6	that set-off is permitted as between a section 74 call	6	agreement achieves as a matter of effect and the good
7	by an unlimited company and any independent dealing with	7	commercial grounds for entering into an agreement which
8	the relevant contributory because the contributories are	8	are considered in cases like Belmont in
9	liable anyway for the full amount of the liabilities and	9	the anti-deprivation context. So we don't accept that
10	it follows that the creditors of the unlimited company	10	there could ever be a good commercial reason for
11	are not prejudiced by the set-off. That is what	11	entering into a recharge arrangement that enabled him to
12	we understood the submission to be.	12	recharge his contributory's liabilities back to us.
13	Now, we submit that that analogy is not apposite and	13	But leave that to one side for a moment. What his
14	it is dealing with a rather different point. But it is	14	submission really failed to grapple with was the fact
15	inapplicable anyway where the contributories are	15	that the liability under section 74 is a statutory
16	insolvent because the rule against double proof is	16	liability in the form of a mandatory statutory rule and
17	always required where there are two proofs in the estate	17	we get all that from the Oregon case and all the rest of
18	of an insolvent debtor. In this instance it would be in	18	it which entitles a company as a statutory right to
19	LBHI2's estate. It matters not that there is unlimited	19	recover from the members their liability to contribute.
20	liability. What matters is whether or not the principal	20	And in the context of assets recovery as opposed to
21	creditor, which in this case is LBIE, has been paid in	21	assets distribution, it falls into the same category as
22	full.	22	the pari passu rule which is mandatory without regard to
23	So, we actually submit that Black's Case, your	23	commercial justification. So you have an similar
24	Lordship does not really get very much assistance from.	24	situation. The only circumstance in which it can be
25	It is dealing with a different point and it does not	25	contracted out of is by a creditor who agrees to
	2 445		7 440
	Page 117		Page 119
1	help anyway where the limited liability company is	1	subordinate himself to nobody else's prejudice
1 2	help anyway where the limited liability company is insolvent	1 2	subordinate himself to nobody else's prejudice. Perhaps one might say this, my Lord, in the same
2	insolvent.	2	Perhaps one might say this, my Lord, in the same
2 3	insolvent. MR JUSTICE HILDYARD: I am just trying to remember, is it	2 3	Perhaps one might say this, my Lord, in the same way and there is a symmetry to this that
2 3 4	insolvent. MR JUSTICE HILDYARD: I am just trying to remember, is it Paraguassu?	2 3 4	Perhaps one might say this, my Lord, in the same way and there is a symmetry to this that a creditor is able to contract out of the pari passu
2 3 4 5	insolvent. MR JUSTICE HILDYARD: I am just trying to remember, is it Paraguassu? MR TROWER: It is. That is all I have to say on issue 7.	2 3 4 5	Perhaps one might say this, my Lord, in the same way and there is a symmetry to this that a creditor is able to contract out of the pari passu rule where it does not affect anybody else, which we
2 3 4	insolvent. MR JUSTICE HILDYARD: I am just trying to remember, is it Paraguassu? MR TROWER: It is. That is all I have to say on issue 7. I have a little to say on issue 9. That is contracting	2 3 4 5 6	Perhaps one might say this, my Lord, in the same way and there is a symmetry to this that a creditor is able to contract out of the pari passu rule where it does not affect anybody else, which we know from the subordination cases, one can also see
2 3 4 5 6	insolvent. MR JUSTICE HILDYARD: I am just trying to remember, is it Paraguassu? MR TROWER: It is. That is all I have to say on issue 7. I have a little to say on issue 9. That is contracting out. It is the preliminary point for Waterfall IIB.	2 3 4 5 6 7	Perhaps one might say this, my Lord, in the same way and there is a symmetry to this that a creditor is able to contract out of the pari passu rule where it does not affect anybody else, which we know from the subordination cases, one can also see the same policy in play in relation to the operation of
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2 3 4 5 6 7 8	insolvent. MR JUSTICE HILDYARD: I am just trying to remember, is it Paraguassu? MR TROWER: It is. That is all I have to say on issue 7. I have a little to say on issue 9. That is contracting out. It is the preliminary point for Waterfall IIB. It is contracting out. It is actually a relatively short point that I have to make on this.	2 3 4 5 6 7 8 9	Perhaps one might say this, my Lord, in the same way and there is a symmetry to this that a creditor is able to contract out of the pari passu rule where it does not affect anybody else, which we know from the subordination cases, one can also see the same policy in play in relation to the operation of section 74.2(e) enabling a creditor to contract out of his entitlement to take the benefit of any call under
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1	of the people it is designed to protect?	1	company. You say it is a requisite characteristic of an
2	The answer to the present case is that there is	2	unlimited company which has issued nominal shares.
3	a statutory rule, it is designed to protect	3	MR TROWER: Yes, indeed. I understand the point you are
4	the creditors and if Mr Marshall is correct, they are	4	asking me.
5	prejudiced by his recharge agreement.	5	My Lord, that was all I was going to say subject to
6	The only other point I wanted to make in relation to	6	any other questions which I am very happy to try to deal
7	issue 9 is that he characterised the rule prohibiting	7	with on the main points on which I was going to reply.
8	the issue of shares at a discount as one that was linked	8	Your Lordship may want to have a discussion about
9	to the issue of the shares and the vires and authority	9	the other issues, where we should go from here, what if
10	of the directors at the time of issue. He took you to	10	anything we should do about the Supreme Court and so on.
11	Welton v Saffery again which we had looked at and some	11	But I did not have anything more substantive to say in
12	passages in the judgments that were expressed in those	12	reply, unless I can assist further on any particular
13	terms. What he basically said was that the cases were	13	point.
14	all about the fact that the directors did not have	14	MR JUSTICE HILDYARD: No. I am presently minded to think
15	authority to do what they did.	15	and we will have a bit of a break now I think I am
16	Now, our simple submission on that is that that is	16	almost certainly going to have to ask you back when
17	a limited submission that is only available on the	17	the oracle has spoken because I do not trust myself to
18	precise words that were used in that particular	18	remember everything with sufficient clarity and be
18	judgment. If you look at the way Lord Halsbury looked	19	brainy enough to go through it without your assistance,
		20	so I think it will be almost inevitable to have you
20	at the position in Oregon, that submission is not,	20	back.
21	respectfully suggest, maintained. He expresses himself		
22	much more broadly.	22	What is the position of Mr Marshall, just so I gauge
23	If we could just turn that up so that I can make	23	the afternoon's events? There have been some cases
24	good that submission, it is behind tab 47 of volume 2.	24	mentioned.
25	It is the passage at page 133: the paragraph "my Lords"	25	MR MARSHALL: There have been and in fact there are quite
	Page 121		Page 123
1	down to the end, which I think we have looked at		a few points which have not arisen previously too so
1	down to the end, which I think we have looked at	1 2	a few points which have not arisen previously too, so
2	already. Yes:	2	there will be a few areas I would like to address your
2	already. Yes: "My Lords, the whole structure of a limited	2 3	there will be a few areas I would like to address your Lordship on and hope to assist your Lordship on. That
2 3 4	already. Yes: "My Lords, the whole structure of a limited company"	2 3 4	there will be a few areas I would like to address your Lordship on and hope to assist your Lordship on. That is particularly on issue 1 and there are a couple of
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2 3 4 5 6	already. Yes: "My Lords, the whole structure of a limited company" (Pause). MR JUSTICE HILDYARD: How does the fact of it being an	2 3 4 5 6	there will be a few areas I would like to address your Lordship on and hope to assist your Lordship on. That is particularly on issue 1 and there are a couple of things that have come out on what you have just heard on issue 9 that I would like to briefly deal with.
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1	it formally and unless that was done, it could not	1	clearly not the case, as the Post Office case
2	properly be taken into account.	2	establishes. It could be a tortious claim as it was in
3	My Lord, that is in fact incorrect, as we know from	3	that case.
4	the Post Office case, because exactly that objection had	4	In fact, the authorities that Mr Trower has
5	been taken in that case and the Court of Appeal didn't	5	produced, several of them are cases where the claim
6	accept it. Your Lordship will see that from	6	coming in the other direction was in fact a claim for
7	the judgment of Lord Justice Geoffrey Lane at page 134	7	salvage or something similar to that, which seems to
8	letter H. It is in authorities bundle 2	8	have been some form of restitutionary claim. So it
9	MR JUSTICE HILDYARD: It was a defence of law unavailable?	9	certainly does not have to be a contractual right of
10	MR MARSHALL: If it arises from the facts, then it is	10	indemnity. It happens to have been that in Farstad but
11	available and that submission can be made on the basis	11	that is not the only way in which it can arise.
12	of it.	12	MR JUSTICE HILDYARD: You have to know that they cancel each
13	The second point was: if you have a set-off	13	other out, don't you?
14	available, particularly an insolvency set-off, there is	14	MR MARSHALL: Yes.
15	no room for circuity of action. My Lord, the short	15	MR JUSTICE HILDYARD: They must be of such a nature that one
16	answer to that is that you can only set-off if there is	16	is not of lesser value than the other and will be
17	a claim. There has to be a claim to be set-off. If	17	established to the same degree as the other and
18	there is no claim because there is a complete defence to	18	therefore will be a waste of time.
19	it, you don't get to set off.	19	MR MARSHALL: Ultimately, at the end of the day, you look at
20	So, there is a prior question: do you have a claim,	20	where you will end up at the end of the process. A lot
21	which is not really being addressed.	21	of these claims
22	The third point that was advanced	22	MR JUSTICE HILDYARD: You do that and say: I am going to
23	MR JUSTICE HILDYARD: It would give rather wide space for	23	deprive myself of mandatory set-off. I am just going to
24	circuity of action, wouldn't it?	24	see what happens.
25	MR MARSHALL: It really boils down to this: is it a defence	25	You are positing, aren't you, that in an insolvency
	Page 125		Page 127
1	or not? The in authorities from the earliest times	1	situation, mandatory set-off is subject to a prior and
2	and I showed your Lordship one of the very earliest	2	even more potent defence, as it were, which is circuity
3	it has always been treated as a defence, not	3	of action? And I say to you that you have to be
4	a counterclaim or cross-claim that is dealt with in that	4	absolutely sure, haven't you, on circuity of action that
5	way. It is correct to say that it has to be circuity in	5	what the claimant says gives rise to opposite and equal
6	the sense that the claim that comes back is for the same	6	claim of equal substance and therefore the court should
7	sum, for the same thing.	7	not waste its time. You say, no, I am not sure about
8	But, my Lord, we respectfully submit that that is	8	that, you might have to weigh them in the end and if
9	what this case is about. It is exactly the same thing	9	they are the same, same degree, same amount, then there
10	that is being claimed back for. It may be added to with	10	is circuity of action and it is a defence.
11	additional items but there is claim coming back to LBHI2	11	I am just saying why didn't the court just say: set
12	for the subordinated debt in the form of a call under	12	them off?
13	section 74. It might be a specific call under	13	MR MARSHALL: In these cases that we are concerned with and
14	section 74 just to deal with that but there might be	14	in some of the ones that we have looked at, you have
15	other items added in but that does not make any	15	a situation where a claim is being made in the Post
16	difference. The same sum is being sought.	16	Office case it is for the damage to the cable a claim
17	I show your Lordship by reference to one of the	17	could at a subsequent stage be made for in that case
18	authorities that Mr Trower has produced that that is	18	I think misrepresentation on Hedley Byrne lines. But
19	sufficient.	19	you don't wait for that claim to be made before you get
20	The third point was, I think, that one had to have	20	to the circuity. You look at what is going to be
21	a relationship between the claim that was going outbound	21	the ultimate position. If the claim is made, there
22	and inbound, on the quantum of it and source of it.	22	would inevitably be a right to compensation for the same
23	We say that is satisfied if and insofar as it is	23	amount and if that is ultimately going to be
24	suggested that there has to be an actual right of	24	the outcome, you do have circuity of action and
25	indemnity in some form of contractual sense. That is	25	therefore a defence to the claim.
	Page 126		Page 128

1	MR JUSTICE HILDYARD: I have a funny feeling that if that	1	the relevant vessel. That is why the circuity of action
2	was the common law, there would be an ugly rush for	2	defence did not get applied in that case.
3	set-off. But there we are.	3	Turning to the judgment of Lord Justice Sankey at
4	MR MARSHALL: The reason why set-off and counterclaims are	4	391, the first part of the judgment on that page makes
5	a more flexible method of dealing with the matter is	5	the point:
6	because there can be complications. There might be	6	"Since the Judicature Acts gave(Reading to the
7	a limitation of liability, as there was in one of the	7	words) circuity of action has neither been as
8	cases that we are concerned with which have just come	8	•
9	· ·	9	necessary nor as frequently resorted to as in former
	up, with results in the amounts not being saved.		years."
10	Or there may be a counterclaim or an attempt to	10	We would respectfully submit that the reason for
11	set-off what is an unliquidated damages claim. You	11	that is because of the flexibility which those defences
12	can't say it is going to be for the same amount, again	12	have that circuity of action does not have.
13	reflected in one of the cases. I think it is the Ocean	13	The interesting thing is that when there is then
14	v Harding case.	14	a reference to Bullen & Leake where there is
15	MR JUSTICE HILDYARD: Yes.	15	a quotation:
16	MR MARSHALL: Set-off and counterclaim are much more	16	"Wherever the rights of a litigant party(Reading
17	flexible whereas circuity of action is very much looking	17	to the words) same amount of damages which
18	at claiming back for precisely the same loss or the same	18	the plaintiff seeks to recover, the defendant may plead
19	amount, either by virtue of contract or some other form	19	the facts which constitute such right "
20	of recovery. So it is obviously a lot less flexible and	20	And then it emphasises the same point which we made
21	thereby presumably more rare than counterclaim and	21	previously, which is that it is a defence for
22	set-off is.	22	the purposes of avoiding circuity of action.
23	My Lord, can I just address the three authorities in	23	His Lordship then makes the point that the circuity
24	a little bit more detail? The Ocean v Harding decision,	24	of action defence, one of the aspects which make it less
25	which is a decision of the Court of Appeal I think	25	flexible is for example where you have an unliquidated
	Page 129		Page 131
	1 agc 12)		1 agc 131
1	reliance was placed on the judgments of	1	damages claim and they are not necessarily going to be
2	Lord Justice Sankey I think it was at page 391	2	identical or a mere cross-claim from liquidated damages
3	MR JUSTICE HILDYARD: Sorry?	3	on equitable grounds. You have to show it is the same
4	MR MARSHALL: I think it was at the back of the bundle of	4	sum that is going to be going around.
5	authorities at authorities bundle 5, my Lord. I am	5	So that is an example of where there is a more
6	afraid I do not have a flag number. I do not know	6	limited use for the circuity of action defence and where
7	exactly where it was put.	7	the set-off counterclaim doctrine has got more
8	MR JUSTICE HILDYARD: Yes.	8	flexibility.
9	MR MARSHALL: I think it was a passage from	9	His Lordship then concludes at the end of 391:
10	Lord Justice Sankey that was relied upon at page 391.	10	"In that particular case, neither of the pleas
11	Just so your Lordship can see how the matter was	11	•
11 12	Just so your Lordship can see how the matter was ultimately decided, the holding which is on page 372	11 12	relied upon to bring into operation the doctrine appeared on the pleadings(Reading to the words)
		l .	relied upon to bring into operation the doctrine
12	ultimately decided, the holding which is on page 372	12	relied upon to bring into operation the doctrine appeared on the pleadings(Reading to the words)
12 13	ultimately decided, the holding which is on page 372 makes it clear what was actually happening here was that	12 13	relied upon to bring into operation the doctrine appeared on the pleadings(Reading to the words) put forth for the first time before the Court of
12 13 14	ultimately decided, the holding which is on page 372 makes it clear what was actually happening here was that it was a three-party case. I think claimed by owners against people who had ended up purchasing under some	12 13 14	relied upon to bring into operation the doctrine appeared on the pleadings(Reading to the words) put forth for the first time before the Court of Appeal." And he concluded that it was not clear that
12 13 14 15	ultimately decided, the holding which is on page 372 makes it clear what was actually happening here was that it was a three-party case. I think claimed by owners	12 13 14 15	relied upon to bring into operation the doctrine appeared on the pleadings(Reading to the words) put forth for the first time before the Court of Appeal." And he concluded that it was not clear that the doctrine applied on the facts:
12 13 14 15 16	ultimately decided, the holding which is on page 372 makes it clear what was actually happening here was that it was a three-party case. I think claimed by owners against people who had ended up purchasing under some bills of lading and then they wished to claim over	12 13 14 15 16	relied upon to bring into operation the doctrine appeared on the pleadings(Reading to the words) put forth for the first time before the Court of Appeal." And he concluded that it was not clear that the doctrine applied on the facts: "It is doubtful that the(Reading to the
12 13 14 15 16 17	ultimately decided, the holding which is on page 372 makes it clear what was actually happening here was that it was a three-party case. I think claimed by owners against people who had ended up purchasing under some bills of lading and then they wished to claim over against their vendors who would then have a claim back	12 13 14 15 16 17 18	relied upon to bring into operation the doctrine appeared on the pleadings(Reading to the words) put forth for the first time before the Court of Appeal." And he concluded that it was not clear that the doctrine applied on the facts: "It is doubtful that the(Reading to the words) knowing the rights and position of other
12 13 14 15 16 17 18 19	ultimately decided, the holding which is on page 372 makes it clear what was actually happening here was that it was a three-party case. I think claimed by owners against people who had ended up purchasing under some bills of lading and then they wished to claim over against their vendors who would then have a claim back against the owners of the vessel. So it was a three-party affair and the difficulty	12 13 14 15 16 17 18 19	relied upon to bring into operation the doctrine appeared on the pleadings(Reading to the words) put forth for the first time before the Court of Appeal." And he concluded that it was not clear that the doctrine applied on the facts: "It is doubtful that the(Reading to the words) knowing the rights and position of other parties affected."
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12 13 14 15 16 17 18 19 20 21 22 23 24	ultimately decided, the holding which is on page 372 makes it clear what was actually happening here was that it was a three-party case. I think claimed by owners against people who had ended up purchasing under some bills of lading and then they wished to claim over against their vendors who would then have a claim back against the owners of the vessel. So it was a three-party affair and the difficulty was, as the holding makes it clear on page 372, that it was not possible to conclude that the same amount was going to go around the circle. In between the purchaser and the vendor in particular, it was not clear that amount recoverable between them was going to be the same	12 13 14 15 16 17 18 19 20 21 22 23 24	relied upon to bring into operation the doctrine appeared on the pleadings(Reading to the words) put forth for the first time before the Court of Appeal." And he concluded that it was not clear that the doctrine applied on the facts: "It is doubtful that the(Reading to the words) knowing the rights and position of other parties affected." So there was just uncertainty over whether or not they were going to end up dealing with the same sum going round and round and it was for that reason that they could not apply it in that case. My Lord, the two other cases: I think one of them

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you don't get an awful lot from that because all that seems to have happened in that case is, because of a limitation of liability applying to one of the owners of the vessels that had been in a collision, one could not say that the amounts that were being claimed by way of salvage were ultimately going to be recoverable from the owners of the vessel which was at fault. So consequently there was going to be a mismatch between the amounts that were being claimed on one side and amounts being claimed on the other. Your Lordship will see that that comes out of the second holding on page 197.

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There was also a further problem which was that there were two different departments of the Crown involved. Accordingly one could not say that the claim was going to be coming back as against the same party. That is what comes out of the third holding.

So it was decided really effectively on those two factors which were specific to the facts in that case. But your Lordship will see that in the course of the judgment of Lord Justice Somervell he refers at page 201 to a previous decision in the House of Lords called Katirastan(?) and in particular the speech of Lord Wright in that case. He says at the very end of page 201:

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"The argument under consideration was that if the colliding vessel was to blame in whole or in part, no salvage would be recovered by the owners of the salving vessel if both are in the same ownership. This is the emphatically negatived ...(Reading to the words)... of the defence."

He goes on to say:

"The question of avoiding circuity of action ...(Reading to the words)... as Lord Wright points out [and it is the speech from Katirastan]:

"The fact that ...(Reading to the words)... an item in the damage claim by the salved vessel against the vessel that is in whole or in part to blame for the collision."

So it rather indicates that you can potentially have it amongst other items but as long as it is one of the items that you are claiming for the same amount as is being claimed against you, that would be sufficient to invoke the circuity defence.

One sees actually towards the end of that paragraph where there are several quotations from Lord Wright's speech that there is a passage I think beginning about 7 lines up from the bottom of that paragraph, he said:

"If the other colliding vessel is solely to blame, the owner of the salved vessel ...(Reading to the

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1 words)... in any case, there may be questions of 2 limitations of liability which would mean that circuity 3 of action was not available as a defence."

But the observation is being made that if the circuity of action principle does apply, it means that the whole claim does become superfluous and would not be made, which is in line with the other authorities I took your Lordship to indicating that it is not merely a matter of counterclaim but it is something that disposes of the claim completely.

My Lord, the third authority which was Brumder, another decision of the Court of Appeal, I would respectfully submit, is of rather limited use because the court didn't actually analyse circuity of action as a doctrine in any detail and do not actually seem to have necessarily applied that defence. What they seem to have done is potentially used a different type of defence, derived from the case of Ginty v Belmont Building Supplies and another case called Kodak to the effect that if you are claiming, you can't claim where the claim arises out of your own wrongdoing, which is more akin to an ex turpi causa type of defence and your Lordship can see that in the passage from Lord Justice Beatson's judgment at paragraphs 37 through

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to 41. He calls this the Ginty, Boyle v Kodak defence.

I do submit your Lordship is not going to get a huge amount of assistance from Brumder. But the interesting point that Lord Justice Beatson makes at page 2797 at paragraph 51 is that he floats the idea just at letter D that there was also the possibility of a valid plea of circuity of action, and it is not clear whether it would be sufficiently dealt with by provisions for set-off and counterclaim in this situation. But he says it would not be inaccurate to describe the litigation as going round in a circle. So it is a rather tentative set of observations which don't give any detailed guidance on how the doctrine would apply.

It does seem that the matter was ultimately resolved on the basis of what the learned Lord Justice referred to as the Ginty, Boyle and Kodak defence as your Lordship will see from paragraphs 56 and 57, which resulted in the claim being dismissed.

MR JUSTICE HILDYARD: As you say, the actual decision appears to be based on what he describes in 48 as a common sense proposition of Lord Diplock's speech in Boyle:

"You are liable to (Inaudible) for my own wrongdoing is neither morals nor good law."

MR MARSHALL: Exactly, it is paragraph 30 where he quotes

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34 (Pages 133 to 136)

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1	it.	1	the particular features of an unlimited company at all,
2	I am not sure they take matters very much further	2	it would just have been totally alien, and I think that
3	and certainly, we would submit, do not result in any	3	would be a tough ask.
4	change in the approach from the authorities I showed	4	MR MARSHALL: The second thing we draw upon is the fact that
5	your Lordship in the course of our submissions.	5	when one looks at both the actual FSA handbook and what
6	My Lord, the points that were raised on the issues	6	they set down as a form of capital, and when one gets to
7	of construction, just a number of new points raised	7	the actual correspondence with the FSA and indeed
8	there	8	with the Revenue, telling the Revenue what is being
9	MR JUSTICE HILDYARD: For example, looking at the accounts,	9	going on with the FSA, because that's what the Revenue
10	you say it would be actively wrong in these	10	correspondence is there for there is no mention at
11	circumstances, do you, for the liquidators concerned to	11	all about the possibility that capital coming
12	enter into the set-off account a set-off arrangement?	12	potentially from the shareholding companies.
13	MR MARSHALL: We would, given that they have this right to	13	MR JUSTICE HILDYARD: I am sure you are right that limited
14	claim over under section 74 to cover the liability	14	company is the template and the unlimited company is to
15	precisely this liability, and this is the liability they	15	some extent the surprise. But it is not unheard of and
16	are wanting to claim over for.	16	it must be simply worked through as to its consequences,
17	On the construction issues, it was suggested that we	17	I think. Everything is quite unusual, after all, in
18	were wrong in submitting to your Lordship that a limited	18	the circumstances of a 8 billion surplus. So there we
19	liability company was rather unique or special and does	19	are.
20	not seem to have been in contemplation when the FSA was	20	MR MARSHALL: Indeed. Well, it perhaps becomes of
21	regulating in this area at the relevant time.	21	particular relevance when one considers what has been
22	A number of things were given to your Lordship by	22	described in our submissions as the Aberdeen City
23	way of example by which various other entities	23	Council approach or point arising out of that.
24	Goldman Sachs was mentioned and a number of other	24	MR JUSTICE HILDYARD: Is there anything you rely on in
25	financial institutions as ones that might be using	25	Aberdeen City which is not repeated in
20	manota mottations as ones and imgin or using	20	The state of the s
	Page 137		Page 139
1	unlimited liability companies. As to when that might	1	MR MARSHALL: Arnold v Britton. Not that we relied on. We
2	be; whether that's happening today or in 2006, I have no	2	have a copy of it if your Lordship would like it.
3	idea. But there is certainly no material before	3	MR JUSTICE HILDYARD: I had better have it. I remember
4	your Lordship to come to a view about that.	4	the discussion in broad terms that Lord Clarke has as to
5	What we do have and what I was basing my submission	5	the difference between implication and reading into
6	on was the observation made by Lord Justice Briggs,	6	the words what you want to find there.
7	which I rather thought was not terribly controversial.	7	MR MARSHALL: I will hand that up to your Lordship. I have
8	It is in the judgment of the Court of Appeal in	8	a copy here.
9	Waterfall I in volume 1 of the trial bundles at tab 9,	9	What we got from Arnold v Britton, contrary to what
10	paragraph 167, where he describes an unlimited liability	10	Mr Trower submitted, is that in fact Lord Neuberger
11	company as being, for the last 100 years at least, an	11	didn't question our Aberdeen City Council at all. In
12	extremely rare species and talks about navigating in	12	fact, he affirmed the approach taken in Aberdeen City
13	waters which are rather uncharted or very old indeed as	13	Council as being an appropriate approach, as did
14	a result. We respectfully submit that is an accurate	14	Lord Hodge in the passage I took your Lordship to
15	description of the situation.	15	previously. So there is absolutely nothing in Arnold v
16	MR JUSTICE HILDYARD: I think it is and it isn't.	16	Britton which calls into question at all what is said in
17	The problem is neither have you particular evidence, nor	17	that case.
18	could you. There are examples around of a number of	18	MR JUSTICE HILDYARD: I think it is only whether it is
19	unlimited companies which may have become more	19	properly characterised as implication or constructive
20	fashionable in light of particular fiscal rules, and	20	interpretation of existing words.
21	they may have become more popular given the terrible	21	MR MARSHALL: And if your Lordship looks at the sixth point
22	calamity of 2008. It is just, you know, an	22	of Lord Neuberger, it would appear quite clear that he
23	imponderable.	23	is treating it as part of interpretation of express
24	You would have to go so far as to say, wouldn't you,	24	terms, not implication. So we do not accept there is
25	that they really wouldn't have cottoned on to	25	any conflict of any kind between those two authorities.
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1	On the question of what the FSA also had in mind, we	1	legitimately bear, you were construing. But it may not
2	of course had referred to the EC materials.	2	matter ultimately.
3	Your Lordship has been told, well, it is possible that	3	MR MARSHALL: Yes. At the end of the day, we submit that if
4	various entities in Europe may have some sort of	4	we have to, we rely on Aberdeen City Council as an
5	unlimited liability. But your Lordship has been given	5	approach your Lordship could adopt in this case.
6	the EC directives, and again they don't reflect	6	MR JUSTICE HILDYARD: Yes. Does your argument rely on or is
7	the possibility of companies of this kind with	7	it prejudiced according to whether it is to be thought
8	the possibility of calls upon shareholders.	8	that the context of insolvency with unlimited companies
9	There are other provisions referring to different	9	was or was not within the contemplation of the parties,
10	types of entity altogether, where there may be	10	not subject to be
11	the possibility of various forms of capital other than	11	MR MARSHALL: That would be a support for bringing in
12	paid up capital. But in the corporate context, there is	12	Aberdeen City Council as an approach.
13	no indication of anything like that. And in terms of	13	MR JUSTICE HILDYARD: If it was not?
14	partnership, I think Mr Trower referred to that as being	14	MR MARSHALL: If it was not.
15	a type of business arrangement that was covered by both	15	MR JUSTICE HILDYARD: If it was, wouldn't the inference be
16	the EC directors and the FSA regulations.	16	that they'd had a look at it and been unable to agree?
17	When one looks at what the FSA require in terms of	17	MR MARSHALL: If they had it in contemplation, we would
18	details of capital, when you look at partnership, it is	18	submit that would mean there would be support for taking
19	the partnership capital account that they are concerned	19	the express term approach to interpretation and looking
20	with, not the possibility of calls being made on	20	at the other contextual circumstances more closely in
21	partners thereafter.	21	order to determine whether or not it could really have
22	A number of points were made about the documents	22	been intended that they were going to have recourse to
23	MR JUSTICE HILDYARD: Can I take you back to Aberdeen? This	23	the shareholders to meet the subordinated debt, if that
24	is a slightly pedantic point, I fear. But if you go to	24	was in their mind. We would then say the materials
25	Arnold v Britton at page 29 in Lord Carnwath, which was	25	we have in bundle 5 become all the more important in
	Page 141		Page 143
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1	a dissenting speech	1	those circumstances.
2	MR MARSHALL: Would your Lordship allow me to	2	Regarding the bundle 5 materials, I think Mr Trower
3	MR JUSTICE HILDYARD: It is volume 4, 100 at page 29. Lord	3	submitted to your Lordship that items 1 to 4 of the
4	Carnwath thought that what Lord Clarke had been doing	4	bundle were all correspondence with the Revenue. That
5	was implying a term. Do you see that just above J?	5	is not correct. Item 1 is in fact correspondence with
6	MR MARSHALL: Yes.	6	the FSA, and it makes the points I had been making
7	MR JUSTICE HILDYARD: And I think the discussion about	7	before. I am sorry that in the transcript I did not
8	Aberdeen is where does one stop and the other begin?	8	complete the three points on the
9	I think some people see implication and some people see	9	MR JUSTICE HILDYARD: Had I counted wrong?
10	interpretation, which is one of the reasons why you get	10	MR MARSHALL: I was actually making this a number of times
11	this sort of tension which Marks & Spencers is meant to	11	during the course of the day, but the three points were
12	resolve. But maybe it is not as straightforward as all	12	that the structure would not be changing very easily
13	that. I do not know.	13	because it was a very carefully constructed one, and
14	MR MARSHALL: Certainly Lord Neuberger at paragraph 22 is	14	therefore there would not be assignments or changes of
15	dealing with it as part of the interpretation of express	15	shareholder. It was intended to be a reasonably
16	terms as one of his six points.	16	permanent arrangement and one of the letters that was
17	MR JUSTICE HILDYARD: They vary sometimes as to the way they	17	sent to the Revenue made that point.
18	look at it.	18	The second was that the group was being regulated as
19	MR MARSHALL: And Lord Hodge certainly seems to be looking	19	a group and there was an intention to protect
20	at it as a matter of textual analysis.	20	the creditors of the group.
21	MR JUSTICE HILDYARD: I think that is why maybe Lord Bingham	21	Then the third point was that when one looked at
22	used to use the word "interpolation". If you actually	22	the various charts and structure charts and descriptions
23	had to insert new words into the clause, you were	23	of participants involved, your Lordship could see that
24	interpolating. If you were inferring from the existing	24	there was not any consideration given or reference to
25	words some meaning which you thought the contract could	25	the possibility of calls upon the shareholders, and
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25	Page 142		Page 144

reflected in all of the other documents in this bundle. indeed LBL was not even referred to. 1 2 2 I am just reminded by Ms den Besten that in the That was the third point which I am afraid I did not 3 3 letter we were looking at in tab 7 that where they refer complete before the short adjournment on page 45. But 4 your Lordship will see that that was made in other 4 to LBIE, they do so as a defined term in that passage. 5 places. For example, I went through I think the three 5 MR JUSTICE HILDYARD: I have enough contracts to interpret points in the course of pages 28 to 30 of the same 6 without interpreting very closely ... 6 7 MR MARSHALL: Your Lordship has our submissions on that. We 7 transcript where it is made there. 8 8 submit it was the group being considered and there were The only other point I wanted to make regarding 9 9 the materials in the trial bundle 5 is that the later good reasons for that, because you don't want to have 10 materials in -- I think it is tabs 8 through to 11 are 10 creditors of certain group companies which are providing services ultimately for the benefit of the trading 11 designed to show your Lordship what the FSA was 11 12 addressing before November 2006 and how they were 12 company being prejudiced by virtue of claims over 13 13 addressing it. It was not for any other purpose, and against another member company. Your Lordship obviously 14 that is its significance. 14 has our point about that from our earlier submissions. 15 Insofar as one has regard to the letter of the FSA 15 My Lord, I think the only other matter on issue 1 was the suggestion that clauses 6F and 7F were simply 16 which is in tab 7, where they give their consent to 16 repayment of the subordinated loans as they were then in 17 concerned with circumvention of the subordination 17 18 18 provisions of the subordinated loan agreement. place and their substitution by the LBHI2 subordinated 19 debt, Mr Trower suggested that the word "the firm" has 19 We respectfully submit that can't be the right 20 20 to be treated as a reference to LBIE. If your Lordship interpretation. If they had simply been concerned about 21 has that in bundle 5, tab 7, this is on the last line of 21 the possibility of some substituted creditor or 22 22 subrogation rights, they simply could have provided that the third paragraph: 23 23 "We respectfully submit in the context of the other any arrangement that provided for a suretyship, security 24 correspondence that has been ongoing with the FSA and 24 or anything of that nature were not to include any right 25 25 of subrogation. That would have been possible for them the other materials that your Lordship has in Page 145 Page 147 the subsequent tabs, that has to be a reference to 1 1 to do and that is not what they did. 2 the UK group. And in particular, why one would have 2 They simply prevented any possibility of any form of 3 a reference to UK capital structure in relation to LBIE 3 recourse to anyone else in relation to the debt, and 4 would be a bit of a mystery because it was a UK company. 4 we submit that is entirely consistent with the approach 5 The UK capital structure is a UK capital structure for 5 to the construction we adopt, which was that it was to 6 Lehman Brothers as a group and that is consistent with 6 be LBIE's own assets without recourse to its other 7 the way in which FSA had been approaching regulation in 7 shareholders or other members of the group in order to 8 the correspondence about this particular matter all 8 meet the debt. 9 9 the way through." My Lord, on the remaining issues which concern LBL 10 MR JUSTICE HILDYARD: The FSA focuses on LBIE as 10 particularly, the only others I wanted to say something 11 the regulated entity, doesn't it? 11 briefly regarding were issue 7. 12 MR MARSHALL: It is the regulated entity --12 It was suggested that it was not clear there would 13 MR JUSTICE HILDYARD: They would be concerned to see claims 13 be independent rights to be pursued between LBL and 14 coming in. It may have a general paternal concern of 14 other parties. Well, that is exactly what we do say is 15 the group, but its focus is on LBIE. 15 the case. We do have independent rights, quite separate 16 MR MARSHALL: If your Lordship has the same bundle, if I go 16 from just rights to contribution as a result of 17 back to the first document with the FSA which led up to 17 the extent of our shareholding and the amount that may 18 this, which is at tab 1, talking about the UK 18 be called under section 74 based simply on the size of 19 restructuring, the very thing that is being referred to 19 shareholding. 20 in that passage. It is in the pre-penultimate 20 We have quite separate independent legal rights, for 21 paragraph: 21 example, potentially a right to indemnity as agent or as 22 "The final form of restructure would not lead to an 22 nominee in terms of the shareholdings that we held for 23 overall reduction of capital at the group or a reduction 23 others, and of course we also rely upon a contractual 24 in the quality of the capital available to the group." 24 entitlement under the recharge agreement. So these are 25 That is the concern of the FSA, we submit, and it is 25 independent claims which we wish to pursue and it may Page 148 Page 146

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1	not be possible to have well, it won't be possible,	1	just like in a different context, the rule in Trevor v
2	we submit, to have those as part of an adjustment	2	Whitworth is judge-made. It wasn't statutorily enacted
3	process.	3	for a very long time but no less effective for it, it is
4	They would be dealt with as an independent claim as	4	judge-invented. But rather like your implication of
5	part of the proving process and the other insolvencies.	5	terms, it was thought to be implicit, as it were, in
6	They don't simply disappear as a result of	6	the architecture. But pari passu is very much there for
7	the adjustment provisions in section 74.	7	all to see, isn't it?
8	MR JUSTICE HILDYARD: I do not think it is suggested they	8	MR MARSHALL: It's been treated as having a certain effect,
9	do? But they just think it is res inter alios acta, in	9	and that was done British Eagle. Prior to that, there
10	effect.	10	was probably some uncertainty about the position. But
11			
12	MR MARSHALL: Issue 9, to conclude, the suggestion is	11	they are both judge-made in the sense that has been
13	we aren't concerned with the anti-deprivation principle	12	developed in the authorities.
	but rather with the pari passu principle. The way that		Lastly, the suggestion was made that we referred to
14	is suggested is I think it is put this way because	14	Welton v Saffery and we made points about the fact that
15	we are dealing with a statutory liability under	15	the focus of that case was upon ultra vires and it was
16	section 74 rather than an asset that has been removed	16	said that was a rather narrow way to look at the case
17	from the grasp of LBIE, or at least its solvency	17	and we ought to look at other cases, and so on.
18	officeholder as a result of the recharge arrangement.	18	We went to that case because in my learned friend's
19	This really boils down, to an extent, to a semantic	19	skeleton argument at paragraph 279, that is the case.
20	type of argument. If they are right in their	20	It is just that case relied upon for the proposition
21	contention, and as I understand it is their contention,	21	that the purpose of the agreement in our case
22	that Lord Justice Briggs' description is correct and	22	the recharge agreement does not matter. That was
23	the right to make a call is an asset of the company,	23	the authorities said to support that, and that was
24	then the effect of the recharge agreement which preceded	24	derived from the passage at pages 304 to 305 which
25	the membership of LBL has the effect incidentally of	25	I took your Lordship to.
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	1 450 117		1 490 101
1	depriving LBIE of the asset so far as it concerns a	1	So that is why I addressed it. When you look at
2	claim against LBL. That is the effect.	2	those passages, they are all about the reason purpose
3	If one adopts an alternative analysis, that of	3	did not matter is because there was no authority because
4	Lord Justice Lewison, it deprives LBIE of a right of	4	it was ultra vires.
5	recourse. That is its effect. That being so, it is in	5	Can I just check if there was anything else?
6	our submission something which naturally falls within	6	MR JUSTICE HILDYARD: Yes.
7	the anti-deprivation doctrine rather than the pari passu	7	MR MARSHALL: Those are our submissions. I hope that was
8	doctrine.	8	within time. If there is anything else I can assist
9	Insofar as it is suggested that section 74, because	9	your Lordship with?
10	it is a statutory provision and the effect of the	10	MR JUSTICE HILDYARD: Thank you very much, Mr Marshall.
11	agreement is that you come out of it. But that is	11	Mr Trower, you have some sweeping up to do.
12	something that distinguishes it because it is	12	MR TROWER: No replies to replies from me.
13	a statutory provision from the anti-deprivation rule	13	MR JUSTICE HILDYARD: Well, you will all get another go when
14	which is said to be a judge-made rule. We don't really	14	the Supreme Court answers.
15	understand that suggestion, because in Lord Collins'	15	Final submissions by MR TROWER
16	judgment in Belmont, what you have is a general	16	MR TROWER: My Lord, I think I need to sweep up on anything
17	principle stated that you can't contract out of the	17	your Lordship needs help on and how it is that we see
18	insolvency legislation and then these two things are	18	the shape of what is going forward, particularly in
19	said to be sub-rules of that general principle. So	19	the light of the Supreme Court and the agreed issues.
20	it is not a question of one involving a statutory	20	As far as the agreed issues are concerned, we have
21	provision or not, they are both treated as involving	21	put in the materials, we have not spent a lot of time
22	the insolvency legislation and the effect of their	22	addressing them. We hope my Lord sees what the ambit of
23	application.	23	them is and why they are likely to have been agreed.
24	MR JUSTICE HILDYARD: They are both under the umbrella of	24	My Lord, can I just say this about them? It may
25	the insolvency and they are both the consequences. But	25	make a difference we are all here seeking directions
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1	as office holders. I think so long as my Lord directs	1	work together towards finding a day once we know when
2	the office holders to proceed in accordance with	2	the Supreme Court's judgments are available and you have
3	the conclusions my Lord reaches, that would be	3	had sufficient time to really see how they impact.
4	sufficient for everyone, rather than a full declaration	4	Of course, if it is delayed in a way which begins to
5	of rights if my Lord is still concerned with that. It	5	impact at all on the part B trial, I think we will just
6	may slightly depend upon the issue as to where my Lord	6	have to touch base again.
7	was on it. The important point is that everybody should	7	MR TROWER: I can quite see that if we are waiting for
8	actually be directed to act in a particular manner so	8	longer than we all hoped, we may have to come back and
9	everybody is then bound by it.	9	have a short hearing to explain the position and get
10	That is all I was going to say in relation to	10	your Lordship's direction.
11	the agreed issues in addition to what we have already	11	MR JUSTICE HILDYARD: Yes. Basically, just so that you
12	put in writing. As we have indicated, the second and	12	should know, presently from 8 May until the end of
13	fourth issues which are agreed are also issues on which	13	the summer term in July, I will be engaged on the RBS
14	the decision of the Supreme Court made there.	14	trial. There is therefore a little bit of time I have
15	It may be that because the agreement has been	15	in March, if the Supreme Court answers quite soon. And
16	reached on the basis of the decision of the Court of	16	in June and July, I have one or two free days because
17	Appeal, so we may have to revisit the exact formulation	17	I am only sitting Monday to Thursday by and large, so
18	of the agreement if the Supreme Court says something	18	Fridays might be available. That is just to give you
19	different in relation to any of the issues. But subject	19	a sort of foresight of what my own difficulties are.
20	to that, I was not going to say anything further in	20	MR TROWER: Yes, that is extremely helpful.
21	relation to that.	21	MR JUSTICE HILDYARD: I think Mr Bayfield may know that he
22	So far as the Supreme Court is concerned, we will	22	has Friday 30 June on another Lehman matter.
23	obviously notify your Lordship as soon as we get wind	23	MR TROWER: Yes. Your Lordship did indicate there may be
24	that their Lordships are about to say something and	24	a day in September.
25	produce their judgments. We will then obviously give	25	MR JUSTICE HILDYARD: Yes, I am hopelessly vague about it.
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1	your Lordship the judgment as soon as it is available.	1	I do apologise. If I can engineer it, it will either be
2	It may be premature until we see it to know exactly how	2	taking out Friday 22nd, which in fact coincides with
3	we should take matters forward, but what I am sure	3	your own, in which case there is no additional problem,
4	we can all do is consult together when we see	4	or Friday 29th. As soon as I know, I will let you know.
5	the judgment as to what we think the best course is. We	5	MR TROWER: That is very helpful.
6	are all at the end of the day representing office	6	MR JUSTICE HILDYARD: It is only likely to be one day,
7	holders and I am sure we will be able to find an	7	possibly one and a half, depending upon travel
8	appropriate way forward.	8	arrangements. That is the lie of it and I will let you
9	My Lord, subject to that, I do not think I had	9	know as soon as I can.
10	anything further to sweep up. But I am very happy to	10	On the agreed issues, I think I just need to
11	answer any further questions of a general or specific	11	figure I may very well have further questions on the
12	nature your Lordship may have, or try to.	12	agreed issues if, because I have not had as much of your
13	MR JUSTICE HILDYARD: Well, I have interrupted quite a lot	13	time on those as on the others, I am not really
14	and don't want to ask any more specific questions.	14	sufficiently up to speed on them.
15	I may have some more questions as I read through the	15	So I do not know what the formula is, but we will
16	transcripts and try and get it more orderly.	16	adjourn this until we have heard from the Supreme Court
17	As I indicated, I think it is inevitable we will	17	and then reconvene unless everyone is of the view,
18	have to meet again, and I would certainly as	18	including me, that it would be unnecessary, which
19	presently I stand, I very much welcome that to see what	19	I think is pretty unlikely.
20	will by then be a slightly different jigsaw. I want to	20	MR TROWER: That is indeed the case. Before your Lordship
21	see where the pieces fit in and I do not want to trust	21	rises, could I just say this: it has come to our
22	myself to squeeze them into the wrong slot.	22	attention that your Lordship's clerk is retiring and on
23	So we will have to do that. My own timetable is	23	behalf the Bar, can I say how much we have gained from
24	tricky. But as I presently see it, I doubt we would	24	the service he has provided to your Lordship over
25	need more than a day. So we will simply have to I think	25	the course of the Lehman matters and we very much hope
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1	that he has a long and happy retirement.	
2	MR JUSTICE HILDYARD: That is very nice, and I would concur	
3	and join in with that. Richard has been brilliant.	
4	Thank you very much indeed all of you. Thank you	
5	all also for your very great assistance and very	
6	efficient submissions.	
7	(4.20 pm)	
8	(The hearing was adjourned to a date to be fixed)	
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