

OPUS2

Lendy & Saving Stream Security Holding Ltd

Day 4

July 1, 2021

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1 Thursday, 1 July 2021
 2 (10.58 am)
 3 THE CLERK OF THE COURT: This is in the matter of Lendy Ltd
 4 and Saving Stream Security Holdings Limited, case number
 5 CR–2019–BHM–000443 and 444.
 6 Can I remind parties that they should be in a
 7 private, quiet area if possible so that you are not
 8 overheard and can hear. Whilst this hearing is being
 9 recorded by HMCTS, you must not make any personal or
 10 private recordings or publish any part of this hearing.
 11 It is a criminal offence to do so.
 12 Thank you.
 13 HIS HONOUR JUDGE RAWLINGS: Unlike every other day, I'm not
 14 aware of any preliminary points we need to deal with.
 15 Is there anything?
 16 MS TOUBE: No, my Lord we are straight on to issue 10 now.
 17 HIS HONOUR JUDGE RAWLINGS: Okay, fine.
 18 Submissions on Issue 10 by MS TOUBE
 19 MS TOUBE: Issue 10 is a question which the administrators
 20 ask with their SSSHL hat on. So they ask administrators
 21 of that company.
 22 And your Lordship will know that this is an
 23 issue that arises in relation to the Model 2 Debenture.
 24 So we need to start by taking that document up. It's at
 25 bundle C, tab 10. Now I should say there were both

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1 debentures and then there were legal mortgages. Nothing
 2 turns on the terms of the mortgages so we only need to
 3 look at the debenture.
 4 And we start with clause 14 of the debenture at 173,
 5 and that provided for the security agent, that's SSSHL,
 6 to hold its rights, and you'll see at the bottom of
 7 14.1.1:
 8 " ... upon trust to pay and apply the same for the
 9 benefit of the Beneficiaries in accordance with their
 10 respective entitlements under the Finance Documents
 11 subject to and in accordance with the terms thereof."
 12 So the first question is who are the beneficiaries,
 13 and we see that from page 153, and the beneficiaries are
 14 the lenders, SSSHL, and then Saving Stream, that's
 15 Lendy, a receiver and delegate. We don't need to worry
 16 about those words.
 17 And then we ask what are the finance documents,
 18 that's at 154, and you'll see that those include the
 19 loan agreement.
 20 Going back in the document to page 182, we see
 21 clause 21 which relates to the application of proceeds,
 22 and that's where the issue in particular that we're
 23 looking for arises.
 24 So all monies received by SSSHL, pursuant to this
 25 deed:

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1 "... after the security constituted by this deed has
 2 become enforceable, shall [we can ignore the brackets]
 3 ... be applied in the following order of priority ..."
 4 Now the first is all costs, charges and expenses
 5 incurred by or on behalf of the beneficiaries, the
 6 security agent etc under and in connection with this
 7 deed and of all the remuneration due to any receiver.
 8 You can ignore that.
 9 So the first point is, it is clear that what comes
 10 out first are all costs, charges and expenses incurred
 11 by or on behalf of Lendy and the Model 2 investors
 12 relevantly but also SSSHL.
 13 Now those will include the costs of enforcement,
 14 which in this case involves all sorts of things in
 15 relation to enforcing the security against the
 16 borrowers. So that may be quite a large chunk of costs
 17 which come out first.
 18 Then we get to 21.1.2:
 19 "... in or towards payment of or provision for the
 20 Secured Liabilities in any order and manner that the
 21 Security Agent determines ..."
 22 And "Secured Liabilities" is defined at 156:
 23 "All present and future monies, obligations and
 24 liabilities of the Borrower to the Beneficiaries ..."
 25 So again to Lendy and to Model 2 Investors:

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1 "... whether actual or contingent and whether owed
 2 jointly or severally, as principal or surety or in any
 3 other capacity together with all interest (including
 4 without limitation, default interest) accruing in
 5 respect of those monies, obligations or liabilities
 6 pursuant to any Finance Document ..."
 7 Finance document, again including the loan
 8 agreement.
 9 So the question that arises in this issue is when
 10 clause 21.1.2 says that SSSHL can pay or provide for the
 11 secured liabilities in any order or manner that the
 12 security agent determines, how should that discretion be
 13 exercised? And in essence what we say is SSSHL is in
 14 administration. In administration when it has
 15 liabilities which are owed to different people.
 16 Different creditors. It should pay them *pari passu*.
 17 HIS HONOUR JUDGE RAWLINGS: Yes.
 18 MS TOUBE: So, it shouldn't prioritise the Model 2 Investors
 19 over those creditors in its general estate.
 20 HIS HONOUR JUDGE RAWLINGS: Yes, but none of these are
 21 creditors in its estate, they're in the estate of Lendy,
 22 if --
 23 MS TOUBE: No, that's correct, but Lendy is one of its
 24 creditors as well.
 25 HIS HONOUR JUDGE RAWLINGS: SSSHL's creditors?

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1 MS TOUBE: Yes. Yes.
 2 HIS HONOUR JUDGE RAWLINGS: For what?
 3 MS TOUBE: Well, for the costs apart from anything else, but
 4 also for the inter—company liabilities. And it, as
 5 a company that's in administration which is holding
 6 these monies for its beneficiaries, which are Lendy and
 7 the Model 2 Investors, the Model 2 Investors are also
 8 not its creditors in any real sense.
 9 HIS HONOUR JUDGE RAWLINGS: No, they're not, no. In respect
 10 of the money that it is exercising a discretion over,
 11 and obviously it isn't exercising discretion any more,
 12 I am, the actual monies it is exercising a discretion
 13 over, none of those would go to SSSHL's creditors as
 14 (inaudible). That's the whole point of having
 15 a security trustee, because it is deciding how monies
 16 that don't belong to it, and in respect of which it owes
 17 no liability, should be distributed.
 18 MS TOUBE: Yes, that's correct.
 19 The first question we get is: how does the court
 20 have jurisdiction to determine this question?
 21 It's common ground, I should say, that the court
 22 does have that ability to determine the question.
 23 The Model 2 Investors say that Lendy, or SSSHL, is
 24 surrendering its discretion to the court. That's not in
 25 fact quite the right analysis. In fact, the question

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1 being asked by SSSHL's administrators is not, "Please
 2 can you exercise my discretion?", but, "Can the
 3 discretion be exercised as a matter of general legal
 4 principle in any way other than the way in which we
 5 suggest, and if so, what should those principles be?"
 6 So it's not strictly a surrender of discretion.
 7 Now, that doesn't hugely matter to your Lordship,
 8 because the question we're asking is the same question,
 9 which is: what are the principles by which that
 10 discretion should be exercised?
 11 HIS HONOUR JUDGE RAWLINGS: So you're characterising it as,
 12 plain and simple, an application by administrators for
 13 directions as to how they exercise the SSSHL discretion,
 14 rather than the surrendering of the SSSHL discretion as
 15 trustee to the court. It's not a trustee asking the
 16 court to exercise the discretion; it's the
 17 administrators asking how it should exercise the
 18 discretion.
 19 MS TOUBE: Yes, it's asking what are the legal principles we
 20 should apply when we are exercising our discretion.
 21 HIS HONOUR JUDGE RAWLINGS: Okay. All right.
 22 MS TOUBE: But as I say, it doesn't matter because the real
 23 question is, what are those principles?
 24 So the first point we make is that the discretion
 25 which is being exercised by the administrators must be

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1 exercised honestly and in good faith. And in this
 2 respect, we rely on the Braganza case which we refer to
 3 in paragraph 152 of our skeleton. And it will be worth
 4 just turning that up. It's in authorities bundle 2,
 5 tab 32, page 882 and we start at paragraph 18. Can
 6 I just invite your Lordship to read paragraphs 18–20.
 7 HIS HONOUR JUDGE RAWLINGS: Yes, okay. It probably goes
 8 nowhere, but this talks about a clear conflict of
 9 interest, and I understand within the context of the
 10 Braganza contract where that clear contract of interest
 11 is, but in the case of SSSHL, there wouldn't be
 12 a conflict of interest or shouldn't be because that's
 13 the whole point in putting SSSHL there. I'm not sure it
 14 goes anywhere.
 15 MS TOUBE: I think the point is the conflict of interest is
 16 both Lendy on the one hand, and the Model 2 Investors on
 17 the other hand, want to be paid first.
 18 HIS HONOUR JUDGE RAWLINGS: Yes.
 19 MS TOUBE: In fact what Lendy says is you should pay us
 20 equally at the same time but the Model 2 Investors say,
 21 no, no, you should pay me first.
 22 So there is a conflict of interest between the two
 23 of them. SSSHL is saying: well, which one of them
 24 should I pay?
 25 HIS HONOUR JUDGE RAWLINGS: All right, well, I think I'll

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1 answer that. I think the conflict of interest there
 2 referred to is about the conflict that one party to
 3 a contract has in making the decision in that it may be
 4 in its interests to exercise it in one way or another.
 5 But actually having thought about it, because SSSHL is
 6 at least a sister company of Lendy, there is at least
 7 the appearance of a conflict of interest there in
 8 wanting to prefer Lendy potentially as a sister company
 9 owned by the same parent. I probably answered my own
 10 question, but carry on.
 11 MS TOUBE: Yes, I don't think that we're strictly in
 12 Braganza case where the trustee — where SSSHL itself
 13 cares which of these gets it. The conflict is between
 14 the beneficiaries in this case.
 15 HIS HONOUR JUDGE RAWLINGS: Yes.
 16 MS TOUBE: The position, of course, for the underlying
 17 creditors of Lendy is going to be much more — of much
 18 more interest.
 19 But the point I was really getting to is in
 20 paragraph 20, was the quotation from the Abu Dhabi case,
 21 so that when that discretion is being exercised, it has
 22 to be exercised honestly and in good faith:
 23 "' ... but, having regard to the provisions of the
 24 contract by which it is conferred, it must not be
 25 exercised arbitrarily, capriciously or unreasonably.'"

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1 So the point is the discretion isn't at large; it's
2 got to be exercised in a way which is honestly and in
3 good faith.

4 Then we say, well, SSSHL is of course in
5 administration, and they have a statutory duty to treat
6 their own creditors fairly. And it would naturally be
7 the case in an administration that creditors should be
8 treated *pari passu*, but we also draw attention to the
9 general *pro rata* principle in the underlying documents.
10 So as between Lendy and — as between the lenders and
11 others.

12 So I should say paragraph 12.7, which we draw
13 attention to in 152.3, as we point out, does not deal
14 with the allocation of the recoveries between the Model
15 2 Investors and trustees/transferees in Lendy, but it
16 does talk about the concept of proportionate share.
17 I don't think I need to take you to 12.7, because we set
18 it out in that paragraph.

19 HIS HONOUR JUDGE RAWLINGS: Okay.

20 MS TOUBE: Then, we say well, what are the arguments that
21 are made to say that, in fact, the Model 2 Investors
22 should be paid out first? And all of those arguments
23 really depend on extraneous bits of correspondence which
24 I'm sure my learned friend will take you through. I'll
25 take you through some of them now. And it's the

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1 question of what Lendy was saying to the Model 2
2 Investors, and what Lendy was saying to the FCA.

3 And we start in paragraph 154 by dealing with the
4 most troublesome of these documents *vis-a-vis* the FCA,
5 which is the document which is dated 16 March 2018. And
6 again, I don't think I need to take you to it because we
7 set it out in detail, but you'll see that what Lendy was
8 telling the FCA was that all capital payments received
9 would be apportioned to ensure investors received full
10 repayment for settling any interest or costs payable to
11 or paid out by Lendy.

12 HIS HONOUR JUDGE RAWLINGS: Yes.

13 MS TOUBE: And as we point out in our paragraph 155,
14 although it is no doubt the case that Lendy was telling
15 the FCA this, it appears not to have told the investors
16 this. We make that point in paragraph 156. So again,
17 I think it is fair to say that Lendy's dealings with the
18 FCA were not accurate, candid or any of those other
19 things. But that doesn't tell you how SSSHL should
20 exercise its discretion.

21 And of course we know from the amended Model 2
22 Terms, as your Lordship knows, that there was
23 a waterfall which came in under clause 13, and I will
24 come back to what happened around this, but we should
25 start with looking at this.

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1 So we look at tab 15 and page 296. And your
2 Lordship will see that under that waterfall, Lendy,
3 acting as agent on behalf of each lender and SSSHL,
4 shall enforce payment of the debt and enforce the
5 security against the borrower. And lenders don't have
6 rights to enforce the security directly except via Lendy
7 or SSSHL.

8 And then we get 13.3:

9 "In the event of a shortfall in the amounts
10 available for repayment of the Loan, the available ..."
11 [VC poor connection; visual/audio freeze]

12 HIS HONOUR JUDGE RAWLINGS: Sorry, Ms Toube, you just froze
13 for a few moments there, so I didn't hear what you said
14 after referring to 13.3.

15 MS TOUBE: I was just — actually just reading it out. So
16 I haven't said anything more than what is in there.

17 HIS HONOUR JUDGE RAWLINGS: Okay, that's fine.

18 MS TOUBE: Just drawing attention to the fact that the
19 accrued interest fee or commission under the loan
20 agreement comes out before the principal under the
21 waterfall. That's what the terms say. And no matter
22 what Lendy was saying to (inaudible) or indeed
23 (inaudible) in other documents, this is what its lender
24 terms actually said.

25 The other point just to make, before we look at

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1 these documents, the FCA e-mail to which my learned
2 friend just referred in paragraph 154 of our skeleton is
3 (inaudible) March 2018 obviously is at a relatively late
4 date.

5 HIS HONOUR JUDGE RAWLINGS: Ms Toube, unfortunately we are
6 missing some of what you're saying, unfortunately. Can
7 I just suggest that sometimes it does fix it if you
8 leave and join again, I'm sorry to say but sometimes
9 that does —

10 (Off the record discussion re VC connection)

11 (Pause)

12 MS TOUBE: Can you hear me better?

13 HIS HONOUR JUDGE RAWLINGS: Yes.

14 MS TOUBE: So what we have here is a shortfall in this
15 trust, and the question is how we should be applying the
16 shortfall in the trust. So it's an insolvent trust run
17 by administrators of an insolvent company, and the
18 question is how we should distribute, and I was just
19 taking your Lordship through the principles, and I think
20 we were just looking at, if you heard me, I hope,
21 clause 13 of the amended model terms.

22 HIS HONOUR JUDGE RAWLINGS: I think you had read out 13.3,
23 and that's about as far as we got. We heard.

24 MS TOUBE: And I was just making one point in relation to
25 the FCA e-mail, which was the FCA e-mail of 16 March,

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1 and what is said is that this is effectively governing
 2 in some way or evidence in some way of how these items
 3 should be distributed, and I said to your Lordship that
 4 this had not been, as far as we know, circulated to the
 5 investors. And also, it post-dated most of the loans
 6 that we were talking about, and I was about to show you
 7 Mr Powell's position, for instance.

8 And if we look at his witness statement in bundle B,
 9 tab 4, at paragraph 46. If I can just invite your
 10 Lordship to read the beginning of that paragraph. And
 11 here Mr Powell is explaining why he was reducing his
 12 investments. But you'll see from the very beginning of
 13 that paragraph that he started doing that in early 2018.
 14 So prior to this date of the FCA e-mail.

15 So then we say, well, how does all of this work in
 16 terms of a chronology of the other documents that were
 17 out there? And we deal with this in paragraph 157 of
 18 our skeleton. And first of all, we draw attention to
 19 the first overdue loans default policy. I don't need to
 20 take you to that because there is nothing in there
 21 at all about the order in which things should be paid
 22 out.

23 Then we get the second overdue loan default policy.
 24 Again, there is nothing in there telling us in what
 25 order these should be paid out.

1 Then we get to the recovery and collections policy
 2 which we refer to in 157.3. That, I think, your
 3 Lordship saw yesterday but we should look at it again.
 4 It's in bundle E2, tab 111. And if your Lordship looks
 5 at page 489, you will see the priority of payments
 6 provision.

7 Now this document was effective from 13 April 2018.
 8 It was published on 27 March 2018. And it did say that
 9 the investors would be paid before Lendy. Now, the
 10 oddity of that is that as your Lordship knows, it was
 11 inconsistent with the terms of the amended Model 2
 12 Loans. The investment terms.

13 And we know that Mr Powell picked this up. And we
 14 know this from again bundle E2, tab 114, page 499, and
 15 we see that Mr Powell says: well, can you explain the
 16 discrepancy between clause 13.3 and the terms and
 17 conditions and the priority of payments in that
 18 document? And the response to that comes from Lendy,
 19 over the page at 500, saying: yes, we acknowledge there
 20 is a mismatch between the two of them and the terms and
 21 conditions will be amended.

22 So if that is where it had stopped, that would have
 23 been clear. But in fact the amended Model 2 Terms were
 24 not amended, and so Mr Powell e-mailed again and we see
 25 that at page 504, and he says:

1 "Just a reminder that the [terms and conditions] ...
 2 still haven't been corrected ..."

3 He then doesn't get a response to that, and he
 4 responds again, which we see at tab 121, and he says on
 5 13 September:

6 "Still wrong, and even worse, cut and paste into the
 7 Wealth terms as well. Are you really this incompetent
 8 that you can't correct an error in a legal document after
 9 5 months?"

10 He sends a further e-mail, still no response, on
 11 page 530 on 3 October, and he says:

12 "Seriously? A cut and paste of the previous answer
 13 from 5 months ago. Still not fixed. So completely
 14 incompetent at customer service and legals.

15 "So how do I escalate this to a complaint ..."

16 HIS HONOUR JUDGE RAWLINGS: Yes.

17 MS TOUBE: Then he gets a response to that which says:

18 "I have referred your inquiry to the legal team and
 19 I will get back to you as soon as I have an update, in
 20 the meantime, we thank you for your patience."

21 And that's it. It's common ground that the amended
 22 Model 2 Terms were not amended, and in fact what then
 23 what happens is that there is a second collections
 24 policy and this one is in bundle E3, tab 194. Now, this
 25 we don't have a date for, but it's some time

1 between April and August, 2018. I believe that the
 2 statement of agreed facts says it was probably
 3 post-August 2018, so it's quite late and it was uploaded
 4 to the website, although again we don't know exactly
 5 what date that was. And it makes it absolutely clear at
 6 966 under "Priority of payments":

7 "Payments received from a borrower or as a result of
 8 any enforcement ... will be applied as set out in
 9 Lendy's Lender terms and conditions."

10 So whatever Lendy was telling the FCA, its amended
 11 terms and conditions said that the priority was as set
 12 out there. And it had an amended recovering collections
 13 policy which said those terms governed. And despite
 14 Mr Powell's having picked up the point and Lendy saying,
 15 "Oh, yes, we have it wrong, we'll amend our terms and
 16 conditions", they didn't. In fact they expressly did
 17 the opposite, which is to say terms and conditions still
 18 applied.

19 HIS HONOUR JUDGE RAWLINGS: So as I understand it, nobody is
 20 suggesting that any of this has any contractual force,
 21 and nobody is basing a claim on representation. I know
 22 that Mr Gledhill places some reliance on it and he'll
 23 come to it. But your position, as I understand it,
 24 Ms Toube, is that this is really not pertinent to the
 25 question of how the discretion should be exercised.

1 MS TOUBE: Yes. The reason I'm dealing with these points is
 2 to deal with what is said by my learned friend, which is
 3 it should be dealt with differently because these
 4 documents say something different. And what I'm saying
 5 is, well, the documents are a mess, to put it mildly,
 6 but they certainly end up with a position which says the
 7 opposite of what the Model 2 Investors would like it to
 8 say.
 9 HIS HONOUR JUDGE RAWLINGS: Okay. So in principle,
 10 Mr Gledhill may say, but if I put it in potentially
 11 clear terms, I think he is saying: look, Lendy is
 12 a beneficiary of this trust and there is conduct here on
 13 the part of which is unethical or contrary to what it
 14 promised to the FCA and all the rest of it, and that
 15 conduct of a beneficiary can be relevant to the exercise
 16 of the discretion here.
 17 Is it your case that conduct of a beneficiary can't
 18 be relevant to the exercise of discretion?
 19 MS TOUBE: Yes, that is our case.
 20 HIS HONOUR JUDGE RAWLINGS: All right. Thank you.
 21 MS TOUBE: So when we're looking at what the trustee should
 22 do, a trustee of an insolvent trust, the trustee itself
 23 in administration, it should divide the shortfall pari
 24 passu and our point is really as simple as that.
 25 HIS HONOUR JUDGE RAWLINGS: I think it's probably also your

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1 case that in the widest sense, fairness doesn't, or
 2 perhaps it does. I think perhaps you say that pari
 3 passu is the only fair way in which it can be
 4 distributed, is that right?
 5 MS TOUBE: Yes. We say it's fair, it's appropriate, it is
 6 the governing principle where you have an insolvent
 7 entity and here we have an insolvent trust.
 8 HIS HONOUR JUDGE RAWLINGS: Do you?
 9 MS TOUBE: Well, there are shortfalls. So the trust does
 10 not have provision --
 11 HIS HONOUR JUDGE RAWLINGS: Well, perhaps. I suppose that
 12 the trust might also be in a sense limited recourse, in
 13 the sense that it has a chunk of money and it's just
 14 doling it out as appropriate. I'm not entirely sure
 15 that the trust can be said to be insolvent. I know it's
 16 short of what it would like to have in order to ensure
 17 that everybody got everything to which they are
 18 entitled. But is it insolvent?
 19 MS TOUBE: Well, there are certainly shortfalls as against
 20 the realisation of the security, and to that extent,
 21 there is not sufficient within the trust to make payment
 22 to all the beneficiaries in full.
 23 HIS HONOUR JUDGE RAWLINGS: For what they'd like to receive,
 24 yes.
 25 MS TOUBE: Well, for even what they're entitled to receive,

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1 ultimately.
 2 And so the point about Lendy's conduct is that as
 3 between beneficiaries, there might be claims which can
 4 be made -- and I have said this before, there might be
 5 claims which can be made by the Model 2 Lenders against
 6 Lendy in Lendy's administration for misrepresentation or
 7 for whatever else, but Lendy itself is now in an
 8 insolvency, and so Lendy, of course, for all intents and
 9 purposes, is Lendy's unsecured creditors. So the effect
 10 of what is said by the Model 2 Investors is that because
 11 of misrepresentations which it says were made to it --
 12 HIS HONOUR JUDGE RAWLINGS: Or to somebody.
 13 MS TOUBE: -- or to somebody, to some or more of the Model 2
 14 Investors -- Lendy's other creditors should be denied
 15 a recovery into Lendy's estate. So HMRC, as your
 16 Lordship has seen, is a creditor. The Model 1
 17 Investors. Indeed, Model 2 Investors for their own
 18 shortfalls. So there will be all sorts of creditors in
 19 Lendy's estate. So punishing Lendy in the way in which
 20 the Model 2 Investors would no doubt wish to do, no
 21 longer, once Lendy is insolvent, has the effect that
 22 they would like it to have.
 23 HIS HONOUR JUDGE RAWLINGS: Yes, but that sort of comes back
 24 to your submission or position that the conduct of the
 25 beneficiaries is not relevant to the exercise of the

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1 discretion.
 2 MS TOUBE: Yes. So my point is, the conduct of the
 3 beneficiaries is not relevant to the exercise of the
 4 discretion, and even if it were, in circumstances where
 5 Lendy is insolvent, the conduct of Lendy pre-insolvency
 6 is cannot be used post-insolvency for the exercise of
 7 discretion where it would penalise Lendy's creditors.
 8 HIS HONOUR JUDGE RAWLINGS: Okay.
 9 MS TOUBE: And the same point would run in relation to
 10 questions of: oh, is it fair? Well, whatever might have
 11 been the position prior to Lendy's insolvency, after
 12 Lendy's insolvency, where Lendy's assets are held on the
 13 statutory trust for its creditors as a whole, it would
 14 be unfair, should that be a question that's of any
 15 relevance, to penalise Lendy.
 16 HIS HONOUR JUDGE RAWLINGS: One of the points Mr Gledhill
 17 says is you need to look at the main purpose of the
 18 trust. And the main purpose of the trust is to ensure
 19 the Model 2 Investors get paid. Therefore the exercise
 20 of discretion, as I understand it, should give effect to
 21 that main purpose of the trust and ensure that Model 2
 22 Investors get paid so far as possible. What about that?
 23 MS TOUBE: Well, in relation to that, it is true that
 24 a purpose of the trust was for Model 2 Investors to be
 25 paid. But it was also a purpose of the trust for Lendy

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1 to be paid in relation to its costs and interest. And
 2 we know that partly from the naming of Lendy as
 3 a beneficiary, and from the waterfall, which we've seen
 4 in the Model 2 Loans.
 5 HIS HONOUR JUDGE RAWLINGS: Yes.
 6 MS TOUBE: And generally from the provisions of the Model 2
 7 loan itself, the underlying loan which was capital
 8 interest fees, etc. So the main purpose of the trust is
 9 to distribute the proceeds of realising the security in
 10 accordance with the waterfall. And then the question
 11 is: well, what is that waterfall, in circumstances where
 12 we are now where we are factually.
 13 HIS HONOUR JUDGE RAWLINGS: So the purpose of the trust is
 14 important, but the purpose of the trust is to distribute
 15 to the beneficiaries, with no particular priority being
 16 given to the Model 2 Investors.
 17 MS TOUBE: Yes.
 18 HIS HONOUR JUDGE RAWLINGS: Okay.
 19 MS TOUBE: So, my Lord, those are my submissions in relation
 20 to issue 10.
 21 HIS HONOUR JUDGE RAWLINGS: Yes, all right, thank you.
 22 Mr Gledhill?
 23 Submissions to Issue 10 by MR GLEDHILL
 24 MR GLEDHILL: My Lord, can I start by clearing two short
 25 points out of the way. The first is one point, the

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1 suggestion is made by my learned friend that the trust
 2 is insolvent. The trust is not insolvent. The trust is
 3 there to provide a fund to discharge various liabilities
 4 owed to Lendy and to the lenders by third parties by the
 5 borrowers. The trust has insufficient monies to
 6 discharge those funds in full. It does not entail that
 7 the trust is insolvent. It merely entails that the
 8 trustees are going to have to take a discretionary
 9 exercise of power to decide who gets paid what out of
 10 the available pot.
 11 The second point. At one point in her submissions,
 12 at an earlier point in her submissions, my learned
 13 friend suggested that the trust secures monies generally
 14 owed by Lendy, by SSSH to Lendy, and that is incorrect.
 15 Your Lordship expressed some unease at that proposition.
 16 The answer to it is apparent if you turn up the
 17 debenture in the C bundle at tab 10, and remind yourself
 18 of what the trust secures.
 19 It's a provision that Ms Toubé in fact showed you at
 20 the bottom of C173:
 21 "Security Trust
 22 "14.1.1. The Security Agent shall hold and
 23 administer all the rights benefits and interests
 24 constituted in its favour by or pursuant to this
 25 Debenture ..."

22

1 Pick it up three lines from the bottom:
 2 " ... and apply the same for the benefit of the
 3 Beneficiaries in accordance with their respective
 4 entitlements under the Finance Documents ..."
 5 And we saw the definition of "Finance Documents" at
 6 C154. "Finance Documents" means the loan agreement and
 7 the security agreement and all the agreements entered
 8 into between Saving Stream and the borrower.
 9 So it is simply incorrect to say that this trust is
 10 in Lendy's favour in its capacity as a creditor of
 11 SSSH. It is in its favour as a creditor of the
 12 underlying borrowers.
 13 My Lord, I'm going to start my more general
 14 submissions on this topic by taking a little time going
 15 through the aspects of the factual background which we
 16 suggest to be particularly relevant.
 17 Your Lordship knows from the evidence that Lendy
 18 launched its online platform in February 2014, and that
 19 in the period between 2014 and the second half of 2015,
 20 it operated under the Model 1 structure. Webb 2,
 21 paragraphs 29–31, bundle reference B, tab 1, page 7,
 22 don't need to take you to it, tells us that
 23 in March 2015, Lendy commissioned Grant Thornton to
 24 prepare a regulatory report, and that report identified,
 25 among other things, a concern that because lenders were

23

1 lending to Lendy under Model 1, and Lendy was then
 2 lending to borrowers as principal, Lendy's arrangements
 3 were not truly those of a peer-to-peer lender.
 4 And that appears to have been what precipitated the
 5 shift to Model 2 later in the year, and the evidence in
 6 the bundle tells you that Lendy announced the change
 7 from Model 1 to Model 2 in an e-mail to investors of
 8 21 September 2015. That's bundle E1, tab 9, page 81.
 9 Down to that point, when Lendy took security for
 10 loans, reflecting the fact that it was the principal
 11 vis-a-vis the borrower, it took the security in its own
 12 name. It was the chargee. And just for your note,
 13 there is a relevant debenture in the bundle at file C,
 14 tab 2, page 16.
 15 HIS HONOUR JUDGE RAWLINGS: Yes.
 16 MR GLEDHILL: But as part of the shift to the Model 2
 17 arrangement, SSSH was set up and Webb 2, paragraph 34,
 18 tells us that SSSH was incorporated on 17 August 2015.
 19 So very roughly a month before the shift to Model 2 was
 20 announced to investors on 21 September 2015.
 21 The evidence tells us that SSSH's two shareholders
 22 were the two founders of the business, Mr Brooke and
 23 Mr Gordon. So far as the evidence goes, SSSH had no
 24 separate employees, and no separate business other than
 25 to act as the security trustee vehicle. And your

24

1 Lordship saw yesterday afternoon, I took you to
2 clause 8.1.3 in the Model 2 investor terms, both in the
3 original and the amended, which shows that SSSHL,
4 unsurprisingly, took its orders from Lendy.
5 In our skeleton argument, we made the point to your
6 Lordship that even after Model 2 was introduced to
7 create a true peer-to-peer relationship, Lendy could
8 have continued to take security for the lender's loans
9 from borrowers and declared itself to be a trustee of
10 that security.

11 So that begs the question: why was it necessary to
12 put SSSHL into the structure? And my Lord finds the
13 answer to that question, if you now take out bundle E3,
14 and turn up tab 179, you can see the heading, "New P2P
15 Trust Structure". This is the announcement I mentioned
16 a moment ago. It is an exhibit to Mr Powell's witness
17 statement, paragraph 39, and this is the announcement
18 that dates from September 2015. And by and beneath
19 the second hole punch, you can see the material passage
20 under the heading in capitals, "New Structure":

21 "When you invested in a loan, we kept detailed
22 records of this, but an administrator may consider it a
23 pari passu risk ... in the event of Lendy 'Ltds (highly
24 unlikely) bankruptcy."

25 Just note the words there, "Lendy Ltd's (highly

25

1 unlikely) bankruptcy".

2 "One bad loan, could in theory undermine the rest.
3 "When we become a Pure P2P platform, you lend to the
4 borrower via Lendy Ltd and a 'nominee company' called
5 Saving Stream Security Holding Ltd, holds the security
6 on your behalf. The purpose of the nominee company is to
7 manage the investment on behalf of all the Lenders so
8 that the borrower only has to deal with a single entity
9 rather than '1000s of individuals ...

10 "This mitigates bankruptcy risk and the contagion of
11 one bad loan will not affect the others."

12 Now, I emphasised in the first paragraph the
13 reference to Lendy Limited's what was called "highly
14 unlikely" bankruptcy, and so when you read in the third
15 paragraph that the point of SSSHL is to mitigate
16 bankruptcy risk, what this document is telling you is
17 that the purpose of the interposition of SSSHL in the
18 structure is quite specifically to protect Model 2
19 Lenders from the risks presented by Lendy's own
20 bankruptcy.

21 And it's also relevant for your Lordship's purposes
22 to note the way in which SSSHL's position is described
23 in two lines in that second paragraph. It is described
24 as a nominee. A bare trustee. So investors are being
25 told that SSSHL is a bare trustee for them of the

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1 security in respect of their loans to the underlying
2 borrowers.

3 But as your Lordship knows, and not for the only
4 time, Lendy did something rather different to what it
5 told the investors it was going to do. Because having
6 told investors that SSSHL would simply be a bare
7 trustee, it then put in place the debenture that your
8 Lordship has seen which provided for its own claims to
9 be secured, and which also conferred on SSSHL
10 a discretion as to the order of payment.

11 And if you create a trust and give the trustee
12 a discretion, you have of course not created a bare
13 trust or a relation of nomineehip. A bare trustee does
14 not have any discretion; he or she simply holds the
15 legal title to the asset to the order(?) of the
16 principal.

17 Your Lordship knows that in the period after Model 2
18 was introduced in September 2015, Model 2 arrangements
19 were governed by the original Model 2 Terms down
20 to March 2018, when the amended Model 2 Terms came out.

21 The evidence tells us that towards the end of the
22 original Model 2 period, some of the loans started to go
23 into default.

24 HIS HONOUR JUDGE RAWLINGS: Which is your Model 2 vehicle?
25 You mean before the new Model 2 Terms are brought in.

27

1 MR GLEDHILL: Yes. Forgive me, the original terms are in
2 effect between September 2015 and March 2018, and the
3 point I'm making to your Lordship is that towards the
4 end of that original Model 2 period, some of the loans
5 started to go into default, and the consequence of that
6 was before the lender terms were amended, Lendy started
7 to give investors assurances about how they could expect
8 Lendy to act in the event of a shortfall situation.

9 And the clearest of those is the one that your
10 Lordship finds if you put away bundle E3 for the moment
11 and turn now instead to bundle E2. And it's at tab 103.
12 Page 414. This is another document exhibited by
13 Mr Powell. It's referred to in paragraph 91 of his
14 witness statement. And it dates from 23 February 2018,
15 so it's still during the currency of the original Model
16 2 Terms. And over the page at page E415, you see at the
17 top of page E415:

18 "We have never taken the support of our investors
19 for granted, nor shall we ever. You are our number one
20 concern and protecting your interests and hard-earned
21 capital is our top priority. Unfortunately, on the rare
22 occasion when a property does not reach its expected
23 sale price it can potentially cause harm to our
24 reputation, which in turn can damage our own balance
25 sheet and profitability.

28

1 "Our job is to be the champion of our investors and
 2 protect your interests . And it is for that reason that
 3 we take any potential losses very seriously . Where we
 4 might be faced with a recovery shortfall , we will pursue
 5 every avenue available to us to recover investors '
 6 capital in full , along with interest accrued and any
 7 bonuses owed."
 8 HIS HONOUR JUDGE RAWLINGS: Yes.
 9 MR GLEDHILL: And just while we're there, you might as well
 10 note the last two lines on the page under the heading,
 11 "Final":
 12 "A firm's approach to recovery will have a huge
 13 bearing on the health of a loan and we have long
 14 understood the importance of this."
 15 So this is reassuring investors under the original
 16 Model 2 Terms that Lendy's top priority in the event of
 17 a shortfall situation is to protect their interests and
 18 their hard-earned capital. So far so good. But as your
 19 Lordship knows, then in March 2018, the amended terms
 20 come out. And if you turn on within the E2 bundle to
 21 tab 107, you will find the track change version that
 22 I took you to earlier that shows the main differences
 23 between the original and the amended terms.
 24 HIS HONOUR JUDGE RAWLINGS: Which bundle are we in?
 25 MR GLEDHILL: Still in E2, tab 107. And within that tab, if

29

1 you turn on to page 450, you can see the key difference,
 2 what's changing in these Model 2 Terms as regards
 3 shortfall situations is the new provision you see at
 4 13.3. I'll just read that:
 5 "In the event of a shortfall in the amounts
 6 available for repayment of the Loan, the available
 7 proceeds will be paid [note these words] in the order
 8 set out in the Loan Agreement, as follows: first,
 9 payment of any unpaid fees, costs and expenses of the
 10 Agent under the Finance Documents; second, payment of
 11 any accrued interest, fee or commission due but unpaid
 12 under the Loan Agreement; third, payment of any
 13 principal ... fourth, payment of any other sum ... under
 14 the Finance Documents. However, Lendy may, and Saving
 15 Stream Security Holding may, vary this order in their
 16 discretion."
 17 It's worth noticing in passing that even the terms
 18 of clause 13.3 were a misrepresentation of the correct
 19 position. Those words that I emphasised when I read it
 20 out to you, "the available proceeds will be paid in the
 21 order set out in the Loan Agreement"; the loan agreement
 22 doesn't say anything about priority. Nor in fact does
 23 the debenture.
 24 What this was purporting to do was to suggest that
 25 actually there had been continuity all along, and that

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1 this wasn't changing anything; it was simply reflecting
 2 what was in the loan agreements and the debenture. And
 3 that was untrue.
 4 HIS HONOUR JUDGE RAWLINGS: I suppose in a sense it wasn't
 5 changing anything because it wasn't Lendy's discretion
 6 to decide how things were paid in the event of
 7 a shortfall; it was SSSHL's discretion.
 8 MR GLEDHILL: Yes, nominally, the same people.
 9 HIS HONOUR JUDGE RAWLINGS: I know in a sense the respect in
 10 which you want to rely on it, but is this not in
 11 effect — let's ignore for the moment that Lendy was
 12 probably telling SSSHL what to do — is this not rather
 13 irrelevant, given that it was SSSHL's discretion as to
 14 the order in which things were paid, and Lendy was
 15 suggesting that it wasn't or wouldn't be?
 16 MR GLEDHILL: It is irrelevant as a matter of legal analysis
 17 to the question which your Lordship has to decide. It
 18 is a point of some importance, for the reasons I'm
 19 coming on to, in understanding what happened thereafter.
 20 HIS HONOUR JUDGE RAWLINGS: Yes.
 21 MR GLEDHILL: Just while we're on this document, I did just
 22 want to show you clause 12.7, which is the one over the
 23 page. Back over the page at 449. There was some
 24 reliance placed on this in my learned friend's skeleton
 25 argument. If you look at 7 in the middle of the page,

31

1 just above the first hole punch, it's talking about the
 2 shortfall situation. And it says:
 3 "If that is the case ..."
 4 Do you see those words:
 5 "... then the lenders shall only be entitled to
 6 recover their proportionate share of such available
 7 proceeds."
 8 And the suggestion was originally made in my learned
 9 friend's argument that that was a flag for the fact that
 10 lenders would have to share *pari passu* with Lendy under
 11 the SSSHL trust. And we made the point in our skeleton
 12 argument, it simply does not say that. What it is
 13 telling the reader is that if there are 100 investors in
 14 a given loan, they share rateably according to their
 15 participations in the loan. It's saying absolutely
 16 nothing about Lendy's entitlement to share under the
 17 SSSHL trust. I just mention that in passing. My
 18 learned friend didn't place any great weight on that in
 19 the context of her submissions.
 20 So that was the change, the key change, clause 13.3
 21 made in March 2018. How did the investors react to
 22 that?
 23 And there is some quite important evidence about
 24 that in Mr Powell's witness statement, which I'd like to
 25 take you back to in the B bundle at tab 4.

32

1 HIS HONOUR JUDGE RAWLINGS: I'll make a point which probably
 2 again goes nowhere — probably tired of making points
 3 that go nowhere. If clause 13.3 can be taken to say all
 4 sorts of useful things that are irrelevant, apart from
 5 the final sentence, which says:
 6 "However, Lendy may, and Saving Stream Security
 7 Holding may, vary this order in their discretion."
 8 That's not true either. Only Saving Stream Security
 9 Holdings could. Does it, in a fine analysis, actually
 10 contradict what Lendy was — necessarily contradict what
 11 Lendy was saying to the FCA, because it might be saying:
 12 oh yes, well of course we'll always exercise our
 13 discretion, even though we haven't got one, in favour of
 14 preferring the position of the M2 lenders, as we told
 15 the FCA.
 16 MR GLEDHILL: That's exactly what they do tell the FCA, and
 17 then they surreptitiously renege on it. And just so
 18 your Lordship knows where I am going, a suggestion is
 19 made to your Lordship that the representations made by
 20 Lendy are relevant to the discretionary exercise which
 21 is going to be conducted under this test (?) and we
 22 suggest that that is plainly wrong. It is a highly
 23 relevant consideration. I'll come back to that later
 24 on.
 25 But I'm going to come on to the exchange with the

33

1 FCA in a moment. I just wanted to start it off just by
 2 showing you what the immediate reaction was on the part
 3 of the lenders, and there is some relevant evidence of
 4 that in Mr Powell's witness statement, back at bundle B,
 5 tab 4, and we can pick it up at page 115.
 6 At the bottom of page 115, your Lordship sees
 7 there's a heading, (iii), "The Amended Model 2 Terms".
 8 If you turn over the page, you can see by the second
 9 hole punch, there's a paragraph starting:
 10 "75.3. Clause 24.1 ..."
 11 Could I just invite you to read that section. So
 12 starting on B115 and finishing at B116 before you get to
 13 paragraph 75.3.
 14 HIS HONOUR JUDGE RAWLINGS: Yes.
 15 MR GLEDHILL: So the hearing bundle, for obvious reasons,
 16 break under its own weight, doesn't purport to account
 17 for each and every communication Lendy sent to its
 18 investors. But Mr Powell's evidence is that it was his
 19 impression, in the last sentence of 75.2, that Model 2
 20 Investors would recover their capital before Lendy would
 21 recover any amounts due to it, and he wasn't
 22 cross-examined about that. And that is, at the very
 23 least, consistent with the e-mail I showed your Lordship
 24 a moment ago, dating from February 2018.
 25 If you keep Mr Powell's statement open and we dip

34

1 back into the second of the E bundles, E2, tab 110. If
 2 your Lordship has that, it's a document headed "Investor
 3 Round—up". It's an exhibit to paragraph 76 of Mr Powell
 4 and he tells us it dates from 16 March 2018. And the
 5 key bit is a few pages on at E484 — 483, in fact, you
 6 can start. You'll see right at the bottom of 483,
 7 there's a heading, "New Rules". So this is the e-mail
 8 that announces the change to the Model 2 rules. And you
 9 can see what it says on page 484. It starts at the top:
 10 "Below is a quick summary of what's new."
 11 "The refreshed [terms and conditions] ... published
 12 on March 5th 2018 reflect recent changes we have been
 13 making ..."
 14 Next paragraph:
 15 "It also included reference to the addition of
 16 a voting feature ..."
 17 That's the provision I showed your Lordship
 18 yesterday, clause 16. Then it says this:
 19 "The other main addition is a clarification and
 20 strengthening of Clause 13.3 which relates to investor
 21 protection in the event of a distressed sale of an
 22 investment asset.
 23 "It is important that you familiarise yourself with
 24 the new set of [terms and conditions] ... in their
 25 entirety."

35

1 Next paragraph:
 2 "If for any reason you 'dont agree to our new terms
 3 and would rather close your account than opt out of
 4 specific new features, you can do so by selling your
 5 loan parts and contacting Support who will advise on
 6 closing your account."
 7 Two points to make about that. The first, the
 8 suggestion by Lendy that the new clause 13.3 represents
 9 a "strengthening of investor protection" is bluntly
 10 devious. What Lendy has in fact just done is to
 11 introduce a provision which tells investors that Lendy's
 12 own dues are not only in competition with the investors
 13 but will in fact rank ahead of amounts owed to
 14 investors.
 15 Secondly, if my Lord looks back to what Mr Powell
 16 says about this, there is some useful evidence back in
 17 the B bundle, tab 4, page 116.
 18 You see at the foot of page B116, if you have that,
 19 that he is dealing at paragraph 76 with the document
 20 that you've got open.
 21 If you turn over to B117, you can see that he makes
 22 some comments about that suggestion, that if investors
 23 don't like it, they can get out. Can I leave you to
 24 read paragraph 76.2 to yourself.
 25 HIS HONOUR JUDGE RAWLINGS: Okay.

36

1 MR GLEDHILL: So far as the evidence goes, clause 13.3 of
 2 the amended Model 2 Terms is the first occasion on which
 3 Lendy flags to Model 2 Investors that their interests
 4 and its own interests may be in conflict in a recovery
 5 situation. It does that by sending them a copy of the
 6 Model 2 Terms under cover of an e-mail that gives
 7 a thoroughly misleading account of the effect of that
 8 change, and it tells them that if they don't like it,
 9 they can opt out, at a point by which that was
 10 practically very difficult to do.

11 Two things happened after the publication of the
 12 Model 2 Terms.

13 First, was an intervention by the Financial Conduct
 14 Authority which we referred to at paragraph 52 of our
 15 skeleton argument.

16 I want to take you through that now in a little more
 17 detail by reference to the contemporaneous documents.

18 Just to set the scene from this, your Lordship knows,
 19 I've already told you this, that interim authorisation
 20 for Lendy was given by the FCA in February 2014. And we
 21 know that it applied for full authorisation on
 22 30 March 2016. And for your Lordship's note, the dates
 23 are in Webb 2, paragraphs 16 and 48.

24 HIS HONOUR JUDGE RAWLINGS: When did you say it applied for
 25 full registration?

37

1 MR GLEDHILL: They got interim authorisation February 2014
 2 and they applied for full authorisation on
 3 30 March 2016.

4 HIS HONOUR JUDGE RAWLINGS: Is it easy to say what the
 5 difference between interim and full is and why you'd
 6 want full?

7 MR GLEDHILL: Not — it's not something that we've
 8 specifically applied our minds to. There are
 9 differences, but I'm afraid I haven't specifically
 10 checked back with the statutory framework and we'd need
 11 to do that to give a proper answer.

12 HIS HONOUR JUDGE RAWLINGS: It's fair to assume there is
 13 some benefit in obtaining full registration.

14 MR GLEDHILL: Absolutely. Your Lordship is already alive to
 15 the point that the process for Lendy of obtaining full
 16 authorisation was a pretty extended process, and as at
 17 the date Lendy published its amended Model 2 Terms
 18 in March 2018, so close on two years after the date it
 19 applied for full authorisation in March 2016, Lendy
 20 still did not have full FCA authorisation. And Webb 2,
 21 paragraph 61 tells us that it did eventually get it on
 22 11 July 2018. So it took about two and a half years.

23 Why the delay? Well, the document suggests that the
 24 delay was referable to the FCA having considerable
 25 reservations during the course of that two-and-a-half

38

1 year period about various aspects of Lendy's business.
 2 We don't have time to get into that topic at any level
 3 of detail, but I do just want to show you a couple of
 4 the relevant letters to give you the flavour. Both of
 5 them are back in file E1, so you can put away E2 for the
 6 moment.

7 In bundle E1 the first one is a letter you'll find
 8 at tab 44. It dates from 12 August 2016, so this is
 9 roughly six months after Lendy has applied for full
 10 authorisation. And you can see — I'm not going to read
 11 this extensively at all, but I'll just dip into a few
 12 passages to give you the flavour, on the first page:

13 "What are we writing to you about?"

14 "We have concerns about the following advertisements
 15 (which are subject to our rules on communicating with
 16 clients, including financial promotions) ..."

17 Then it references various things on the website.

18 Then there is a subheading by the second hole punch:

19 "Why are we writing to you?"

20 "We have some concerns that these advertisements do
 21 not comply with our rules and guidance in the Conduct of
 22 Business Sourcebook ... We consider that your
 23 advertisements may not meet our requirements to be fair,
 24 clear and not misleading ..."

25 If you look at the penultimate line of the page, you

39

1 can see the reference to COBS 4.2.1 which was the
 2 provision I mentioned to your Lordship yesterday in the
 3 context of this debate.

4 Just over the page, perhaps one point to draw out
 5 from this at E161, one of the things that is
 6 particularly concerning the Authority is that at that
 7 point Lendy is trading and calling itself Saving Stream
 8 which the Authority believes runs the risk that
 9 investors will believe that peer-to-peer lending
 10 products are something analogous to a bank account. And
 11 you see in the middle of the page, paragraph 4:

12 "We consider that the use of the trading name
 13 'saving stream' is misleading for the reasons set out
 14 above."

15 That dates from about six months after the
 16 application for full authorisation.

17 If you now turn on to tab 79, we now have a letter
 18 from the Authority dated 1 June 2017, so we have moved
 19 on about ten months in time from the letter you have
 20 just seen. And as your Lordship will see from this, the
 21 FCA is still considering Lendy's authorisation
 22 application and sets out a large number of reservations
 23 including, again, about whether Lendy's promotional
 24 materials are misleading.

25 It's a long letter, I'm not going to go to it in any

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1 detail at all, but you can see that if you dip into page
 2 E267, and just glance at the bottom paragraph under the
 3 heading, "The Lendy website and financial promotions":
 4 "The FCA has considered the new Lendy website and in
 5 our view, it lacks balance."
 6 And it goes on.
 7 So this letter, the letter we're looking at now,
 8 pre-dates the amendment of Lendy's lender terms and
 9 conditions in March 2018 by approximately six months.
 10 And by the time Lendy put out those terms and
 11 conditions, it had been having a difficult time with the
 12 regulator for an extended period in its bid to gain full
 13 authorisation. And that is the context of a very
 14 important exchange between Lendy and the regulator, for
 15 which we have to go back to bundle E2. We pick it up in
 16 there tab 108 to begin with. You can see in the middle
 17 of the page, it's an e-mail from Robert Cooper at the
 18 FCA to Paul Coles. Paul Coles is head of regulatory
 19 compliance at Lendy, dated 6 March 2018, and so this is
 20 very close in point of time to the publication of the
 21 amended Model 2 Terms. I'll just read some extracts
 22 from it:
 23 "Dear Mr Coles
 24 "I refer to previous correspondence regarding Lendy
 25 Ltd's Part 4A application. To confirm, Authorisations

41

1 are still in the process of preparing our formal 'Minded
 2 To Refuse' letter and this will be issued in due
 3 course."
 4 And that's important. So at this point, getting on
 5 for two years into the process of considering the
 6 application for authorisation, the Authority is
 7 indicating to Lendy that as things stand, it is minded
 8 to refuse that application. And the letter goes on, the
 9 e-mail goes on:
 10 "However, it has come to light that Lendy has
 11 amended the published lender's Terms and Conditions on
 12 its website on 5 March 2018. On initial consideration of
 13 these, it appears that these are an amended version of
 14 the terms and conditions submitted to the FCA and dated
 15 23 June 2017 ..."
 16 And then skip down to the last two lines of the
 17 page:
 18 "Based on our initial review of latest terms and
 19 conditions, we note two substantive changes compared to
 20 the previously published version ..."
 21 Over the page you can see what those are. The first
 22 one is section 16 about opinion of lenders. That's the
 23 provision I showed you yesterday. But what really
 24 matters is the next point, starting:
 25 "The firm has introduced substantial changes ..."

42

1 "The firm has introduced substantial changes to
 2 clause 13 ..."
 3 And it then quotes the provision. And then it says:
 4 "Please respond to the following questions by [close
 5 of business] 8 March ..."
 6 I'm going to read you 2 and 6:
 7 "2. How has the firm communicated the change in
 8 terms and conditions to its lenders prior to the
 9 publication on 5 March ... Please provide screenshots or
 10 correspondence to support this ...
 11 "6. Please explain whether the 'order of
 12 preference' referred to in clause 13.3 existed prior to
 13 5 March 2018. If so, where this was previously
 14 documented within Lendy's loan documentations, terms or
 15 internal policies, and how was this clearly communicated
 16 to investors?"
 17 And then your Lordship sees the follow up exchanges
 18 to that if we now go on to the next tab, tab 109 and we
 19 need to read it backwards. They are in reverse order.
 20 So we start at page E481, please. E-mail from
 21 Mr Cooper -- sorry, an e-mail from Mr Coles to
 22 Mr Cooper, dated, if you look back at the bottom of the
 23 previous page, it's from 9 March, and back on E481:
 24 "Good morning Robert."
 25 We will skip the first paragraph. In relation to

43

1 the second paragraph, he says this:
 2 "The changes to the payment waterfall ('order of
 3 preference' clause (13.3)) were non-material
 4 clarifications to ensure that investors' interests are
 5 completely clear and transparent in the event of a
 6 formal or distressed asset disposal, against which a
 7 first or second charge is held. Our legal team have
 8 confirmed that these minor changes cause no practical or
 9 legal detriment to investment, indeed the complete
 10 opposite."
 11 Indeed the complete opposite. Then turn back to
 12 page 479. FCA's response. This is Mr Cooper on
 13 13 March 2018. Reading it from the paragraph in the
 14 middle of the page, he says this:
 15 "Our concern here is that, until 5 March 2018, it
 16 appears lenders were not previously provided with an
 17 explanation as to the 'order of preference' and to all
 18 intents, this is new information. We also note Lendy
 19 also does not provide any information about its 'unpaid
 20 fees, costs and expenses' that would enable lenders to
 21 establish the likely cost when an asset sale leads to a
 22 shortfall.
 23 "If this 'order of preference' was always in place,
 24 we consider this to be material information that lenders
 25 should have been provided with prior to them making a

44

1 decision to invest. This is information that would help
 2 an lender formulate a view as to the likely risks of
 3 losing their investment (COBS 14.3.2R(1))."
 4 And then there is the crucial reply to that, which
 5 your Lordship finds if you now turn back to E475, and
 6 the reply is the document that starts at the second hole
 7 punch. Just so your Lordship understands, what's
 8 happened is that Mr Coles has e-mailed back to Mr Cooper
 9 his original e-mail with mark-up, and one suspects that
 10 in the original, it may have shown in colour but it
 11 doesn't on this, but I can tell your Lordship what is
 12 Mr Cooper's e-mail and what is Mr Coles' e-mail.
 13 So if you look at the last paragraph on this page,
 14 you can see "our concern here is that". That's what
 15 I have just read to you from Mr Cooper. And turning
 16 over the page, the quote from Mr Cooper stops at
 17 the second line with the words "order of preference".
 18 And then what you see there, running between the words
 19 "all capital payments" in the chunk that runs out
 20 slightly skewed out to the left, all of that is
 21 Mr Coles' reply, Lendy's reply. So it finishes just
 22 before the paragraph you get to in the middle of page
 23 starting with the words "if this 'order of preference'".
 24 Could I just invite you to read that extract through
 25 to yourself, just to save my reading voice, and then

45

1 I'll make some points about it.
 2 HIS HONOUR JUDGE RAWLINGS: Yes.
 3 MR GLEDHILL: You see it then goes on, after the extract you
 4 have just finished, to quote again Mr Cooper's e-mail
 5 back to him:
 6 "If this 'order of preference' was always in place,
 7 we consider this to be material information ..."
 8 If you just cast your eye about eight lines down in
 9 that paragraph, you should see a sentence starting:
 10 "As per my previous e-mail ..."
 11 Now, that is Mr Coles replying to that point. So
 12 the FCA has asked, "Was this ever flagged to the
 13 investors before?"
 14 And Mr Coles says:
 15 "As per my previous e-mail we freely acknowledge
 16 that prior notification wasn't provided on this
 17 occasion."
 18 So there are three points to make about this reply
 19 by Mr Coles to the Authority. The first is that the
 20 sentence I have just read out accepts that investors
 21 were not told about the priority of waterfall in
 22 clause 13.3 before the Model 2 Terms were amended and
 23 sent out. By which time, as I have already explained to
 24 your Lordship, by reference to Mr Powell's evidence,
 25 they were effectively locked in.

46

1 The second point. The higher of the two extracts
 2 from Mr Coles' e-mail that I have just read to your
 3 Lordship, or asked your Lordship to read, is the
 4 clearest possible representation to the Regulator that
 5 in any shortfall case, Lendy would prioritise the monies
 6 owed to investors above the monies owed to Lendy itself.
 7 Your Lordship sees what Mr Coles says. He describes it
 8 as a "key foundation stone of the business".
 9 The third point. We know that Lendy finally got its
 10 FCA authorisation four months after the date of this
 11 exchange. There is nothing anywhere in the bundles to
 12 suggest that at any point in that four-month period,
 13 Mr Coles or anyone else at Lendy told the Financial
 14 Conduct Authority that Lendy had had a change of heart
 15 on what the FCA plainly regarded as a fundamental point.
 16 HIS HONOUR JUDGE RAWLINGS: I suppose a rhetorical question,
 17 which is if this assurance was given to the FCA as to
 18 how Lendy intended to do things in practice, why didn't
 19 the FCA come back and say: well, that's good then,
 20 you'll be changing clause 13.3 because it says the
 21 opposite.
 22 MR GLEDHILL: Well, the evidence doesn't give you a clear
 23 answer to that. Because the paper trail in relation to
 24 this is very incomplete. But we know what Lendy did to
 25 give effect to this undertaking, and that is the point

47

1 that I'm coming on to immediately next. Lendy did do
 2 something to honour the undertaking that Mr Coles gave
 3 to the FCA.
 4 The point that I was making to your Lordship, that
 5 in circumstances where the FCA plainly regarded this as
 6 a highly material point, and gave full authorisation
 7 four months later, your Lordship has to assume that the
 8 assurances given in this e-mail were fundamental to the
 9 Authority's decision to grant that authorisation to
 10 Lendy, and indeed perhaps to permit Lendy to continue in
 11 business at all.
 12 HIS HONOUR JUDGE RAWLINGS: Now, we are running up to 12.26.
 13 So that will be around almost an hour and a half we have
 14 been going in this morning's session. What is going to
 15 be a good point for a break?
 16 MR GLEDHILL: Well, I was — so your Lordship knows,
 17 I probably have about another 30 to 45 minutes and we
 18 started a little bit late and I was very grateful to
 19 your Lordship for that. It gave me a slightly more
 20 civilised start time this morning than I might otherwise
 21 have had. It is very much up to your Lordship; we could
 22 either take a short break now for the transcriber or we
 23 could rise for a short adjournment as an early lunch
 24 break and then come back and knock this point off when
 25 we come back. It's entirely a matter for you.

48

1 HIS HONOUR JUDGE RAWLINGS: To get to the end of what you
 2 want to say, it's about half an hour, is it?
 3 MR GLEDHILL: Yes. I think I might get to the end of it
 4 before 1 o'clock. It might be a little after 1 o'clock.
 5 HIS HONOUR JUDGE RAWLINGS: Let's take a break until 12.35,
 6 and then if you -- we run over as necessary to
 7 accommodate your submissions. I know that Ms Toube will
 8 want to come back again. If Ms Toube thinks she's going
 9 to be 10 or 15 minutes, depending on how I'm feeling
 10 about it, maybe 20 minutes, then it may be that we will
 11 do it and finish off at that stage. Otherwise we'll
 12 adjourn until after lunch. So we'll see where we get
 13 to, and Ms Toube can let me know how long she is likely
 14 to be. We may get it all wrapped up before taking a
 15 late lunch, or we will come back after lunch. But
 16 anyway, if we come back at 12.35, 25 to 1, please.
 17 Thank you.

18 (12.28 pm)

19 (A short break)

20 (12.35 pm)

21 MR GLEDHILL: Before the break I showed your Lordship the
 22 e-mail exchange between Lendy and the Authority. Before
 23 I show you my next document, I just wanted to remind you
 24 of something in the administrator's skeleton argument
 25 that relates to this. It is at page 51 of their

49

1 skeleton.
 2 And they set out -- in the middle of that page, they
 3 set out a chunk from that e-mail. At 155, they say this
 4 e-mail is not an aid to construction. Of course we are
 5 not suggesting anything of the sort. I will come back
 6 to what we are saying about this in a moment.
 7 Then at 156.1, they say this:
 8 "There is no suggestion that the email from Mr Coles
 9 was disseminated to Model 2 Investors."
 10 Formally, of course, that is correct, but in a
 11 pretty empty formal sense, because substantively it is
 12 very wrong indeed by reference to the document that your
 13 Lordship sees, if you turn on within bundle E2 now, to
 14 the document you find at tab 112.
 15 E, 112 is a document exhibited to Mr Powell's
 16 paragraph 77. He tells us this dates from
 17 13 April 2018, so this is pretty much exactly a month
 18 after the exchanges with the Financial Conduct Authority
 19 that you have been looking at. And your Lordship asked
 20 a moment ago, what did Lendy do to give effect to the
 21 assurances Mr Coles gave to the Authority. The answer
 22 is this. Turning on to the second page, E493,
 23 "Collections and recoveries", middle of the page, "the
 24 new policy".
 25 HIS HONOUR JUDGE RAWLINGS: I should have written it down,

50

1 you gave me a date when this was sent according to
 2 Mr Powell.
 3 MR GLEDHILL: The date was 13 April 2018.
 4 HIS HONOUR JUDGE RAWLINGS: Thank you. Yes.
 5 MR GLEDHILL: Paragraph 77 of his witness statement. Middle
 6 of page 493, by the first hole punch, "Collections and
 7 recoveries -- the new policy":
 8 "This new policy outlines to borrowers what we
 9 expect of them and aims to give our investors comfort
 10 about the robust procedures Lendy has in place to
 11 protect them in the case of the borrower's default."
 12 Skip the next paragraph.
 13 "The policy outlines ..."
 14 Fourth bullet point:
 15 "Priority of payments to investors.
 16 "You can read the new Collections and Recoveries
 17 policy here."
 18 And the link document you get to is the one you see
 19 if you turn back to tab 111. It started off on
 20 page 487. Let's start it off on page 486, because this
 21 is a document that the administrators have found, and so
 22 you can see if you look at the subject, "[Collection and
 23 recovery] policy -- new", so this is a new policy,
 24 dating from 27 March, so very roughly a fortnight after
 25 the exchange of e-mails with the conduct authority that

51

1 I've just shown you, and then announced to the investors
 2 about three weeks later.
 3 The first page is E487, "Collections & Recoveries
 4 policy":
 5 "The purpose of this policy is to set out the action
 6 Lendy takes to encourage borrowers to repay ... also
 7 serves to set out the action Lendy takes when a borrower
 8 [is] unable to repay ..."
 9 And the critical passage of course is the one that
 10 Ms Toube has already shown you at E489. On the
 11 right-hand column, "Priority of payments":
 12 "Unless Lendy is receiving a payment from a borrower
 13 in connection with an extension, the funds forwarded ...
 14 shall be put to the amounts owing with the following
 15 priority :
 16 "1. Capital ...
 17 "2. Interest ...
 18 "3. Bonus accrual
 19 "Lendy will only take any portion of interest or
 20 fees owing to them once all of the above have been
 21 satisfied ."
 22 Now, the terms of the first recovery policy, so just
 23 pausing there. The answer to your Lordship's question:
 24 what did Lendy do pursuant to that exchange with the
 25 Financial Conduct Authority to assure it that its -- the

52

1 Authority's concerns had been addressed?
 2 The straight answer is the bundles do not
 3 conclusively tell us; but the overwhelming inference
 4 from the timing of this document is that this was
 5 Lendy's response to the problem identified by the
 6 Authority. It is what set the Authority's mind at rest.
 7 But its terms were, of course, inconsistent with
 8 clause 13.3 of the amended Model 2 Terms. And your
 9 Lordship has seen that Mr Powell picked up on that. And
 10 I'm just going to take you back quickly again through
 11 the relevant exchange, just making one or two comments
 12 in addition to the comments that my learned friend made.
 13 The first document is at 114, E499, so just so your
 14 Lordship has it clear in your mind, 13 April is the date
 15 that the first collection and recoveries policy is sent
 16 out to the investors. And this is a message from
 17 Mr Powell of 30 April. So 17 days later he has picked
 18 up on the discrepancy, and he says:
 19 "Could you explain the discrepancy between
 20 clause 13.3 in the [terms and conditions] ..."
 21 And the recoveries policy. And he sets it out. And
 22 then you go on in tab 114, in the same tab to page 500.
 23 And your Lordship has already seen this with Ms Toubé.
 24 A reply — interestingly, it takes them a little bit
 25 over a week to answer that simple question, and they say

53

1 there by the second hole punch:
 2 "The order of payments in the event of a shortfall
 3 will be as per the Collections & Recoveries policy.
 4 "We will be updating the [terms and conditions] ...
 5 so that they correspond with the Collections &
 6 Recoveries policy."
 7 And then page 504, Ms Toubé showed you this e-mail,
 8 an e-mail now from 1 August. So just to be clear, it's
 9 now been three months. So Lendy has committed to
 10 Mr Powell that the amended terms will be re-amended to
 11 bring them into line with the collection and recovery
 12 policy, and here is Mr Powell three months later saying:
 13 what's happening? And nothing has happened in that time
 14 with, of course, one important exception. In that
 15 three-month period, on 11 July 2018, Lendy has now got
 16 its FCA authorisation.
 17 And following that, two things now happen. The
 18 first is Lendy simply ignores further e-mails from
 19 Mr Powell on this subject. Again, I'll take you through
 20 them quickly through again. They're at tab 121. The
 21 first one is at E528 on 13 September. So this is
 22 five months after they have committed to amending the
 23 terms to bring them into line with the recovery policy.
 24 And then the other one that you see at E530, again, by
 25 the second hole punch, Mr Powell now on 3 October:

54

1 "Seriously? A cut and paste of the previous answer
 2 from 5 months ago."
 3 And then above that the support team by the first
 4 hole punch:
 5 "I have referred your enquiry to the legal team and
 6 I will get back to you as soon as I have an update ..."
 7 Nothing thereafter. It's pretty remarkable, we
 8 suggest, that Lendy should have simply fobbed off
 9 Mr Powell in this way, given the categorical assurance
 10 they gave to him in May 2018 and the categorical assurance
 11 that they gave to the FCA in March 2018. But what is
 12 simply astonishing is what they then did next. And that
 13 is in the third of the E bundles, E3, tab 194. And that
 14 of course is the second recovery policy. And your
 15 Lordship has seen the material passage; it's at
 16 bundle page E966.
 17 HIS HONOUR JUDGE RAWLINGS: Remind me when this is issued.
 18 MR GLEDHILL: I'm going to give you the answer to that in
 19 just a moment. E966 first of all. That's the relevant
 20 bit. "Priority of payments". What was there before
 21 deleted and amended to read:
 22 "Payments ... from a borrower or as a result of any
 23 enforcement action will be applied as set out in Lendy's
 24 Lender terms and conditions."
 25 Flat contradiction of the assurance begin to

55

1 Mr Powell. Completely inconsistent with the assurances
 2 given to the Financial Conduct Authority in March. The
 3 answer to the question: when does this document date
 4 from? I can show your Lordship. I have mentioned this
 5 a couple of times in the course of submissions already
 6 but your Lordship should just see it. It's in the A
 7 bundle. Tab 4 in that is the statement of agreed facts.
 8 And within that, so file A, tab 4, if you turn up
 9 page 45. Sorry, I am still getting there myself. You
 10 see a paragraph midway between the two hole punches:
 11 "Despite the statement the Lendy Legal Team
 12 made ..."
 13 If you read that and the continuation paragraph (b)
 14 over the page.
 15 HIS HONOUR JUDGE RAWLINGS: Yes.
 16 MR GLEDHILL: So we don't know the date, but on
 17 28 August 2018, Lendy is still telling Ms Taylor that
 18 loans in recovery are going to result in a recovery of
 19 capital first. And your Lordship will note that in the
 20 e-mail exchanges between Mr Powell and Lendy that I have
 21 just showed you, there is no whisper in that of
 22 a suggestion that, in fact, the first recovery policy
 23 has been withdrawn, those e-mails at the end date
 24 from September and October.
 25 So it looks as if this second recovery policy comes

56

1 very late in the chronology.
 2 HIS HONOUR JUDGE RAWLINGS: Are you taking the fact that
 3 they told Ms Taylor on 28 August 2018 as some indication
 4 that it was after that date?
 5 MR GLEDHILL: Yes, because they tell her, looking at the top
 6 of page A46:
 7 "This loan is currently in recovery and therefore
 8 our collections and recovery team will recover capital
 9 firstly ."
 10 Which would be inconsistent with the terms of
 11 the second recovery policy.
 12 HIS HONOUR JUDGE RAWLINGS: It would, but I don't think any
 13 of us can be confident that --
 14 MR GLEDHILL: That is fair comment, but what is extremely
 15 surprising is that if the second recovery policy
 16 predated the exchanges between Mr Powell and Lendy that
 17 your Lordship has just seen from September
 18 and October 2018, they would not have mentioned the
 19 existence of that policy in those exchanges.
 20 So, I have three short points to make about
 21 the second recovery policy and its significance . The
 22 first is there is no evidence anywhere to suggest Lendy
 23 told the Financial Conduct Authority that it was now
 24 proposing to do something completely contrary to the
 25 assurances that it gave in March 2018 that it was

1 prioritising lenders in a shortfall case.
 2 The second point to make is that whereas, as your
 3 Lordship has seen, the first recovery policy was
 4 announced to lenders with a fanfare in an e-mail
 5 in April 2018 in the e-mail I showed you, the second
 6 recovery policy was smuggled in through the back door
 7 without telling anybody about it, and if your Lordship
 8 will get that out, I can take you to it if you like, but
 9 it 's paragraph 79.6 in Mr Powell's witness statement, at
 10 B, tab 4, page 119, where he says investors were never
 11 told about it.
 12 HIS HONOUR JUDGE RAWLINGS: Do we know it was on the site
 13 at all?
 14 MR GLEDHILL: Well, there's an interesting side issue about
 15 that, because Mr Powell makes the point that if you go
 16 to the 13 April announcement, as it was up on the
 17 website, at some point somebody has changed the link so
 18 that it takes you -- instead of taking you to the first
 19 recovery policy , it takes you to the second recovery
 20 policy . So the straight answer to your question is that
 21 at some point somebody changed the link in the 13 April
 22 investor announcement, so that anyone who clicked on it
 23 was taken to the second recovery policy.
 24 We don't know who did that and we don't know when
 25 they did it and we don't know why they might have done

1 that. Rather than simply more candidly putting out
 2 another announcement saying there is a new policy.
 3 The third point I just wanted to make by reference
 4 to the second recovery policy is this . It looks
 5 strongly on the evidence that it
 6 post--dates September/October 2018. Your Lordship knows,
 7 I've made this point a number of times, Webb 2,
 8 paragraph 80 tells us that Lendy wrote its last loan on
 9 18 September 2018. So it looks as if the second
 10 recovery policy post--dates the point at which Lendy
 11 ceased bringing new lenders in.
 12 That concludes what I was going to say to your
 13 Lordship about the fact. And I'm now going to outline
 14 quickly what I say are the applicable legal principles
 15 before making some succinct submissions about what it is
 16 we say your Lordship should decide under this limb of
 17 the application.
 18 HIS HONOUR JUDGE RAWLINGS: Yes.
 19 MR GLEDHILL: If I can take you back to our skeleton
 20 argument. Paragraph 47 on page 40, please. My Lord has
 21 read this. We crystallised from the text that when
 22 a trustee is faced with a discretionary exercise of
 23 power, and is uncertain about whether or not to exercise
 24 it in a particular way, they can generally do one of two
 25 things. They can either take the decision and go to the

1 court and seek the court's approval. That's the
 2 possibility we refer to in 47.1. And if that is what is
 3 done, then the court's function is a limited one. It's
 4 effectively limited to reviewing whether or not the
 5 primary decision--maker, the trustee, has exercised its
 6 discretion in a way that is within the limits of
 7 rationality and honesty.
 8 Alternatively, a trustee can seek to surrender its
 9 discretion to the court and say to the court, take the
 10 decision for me. And where that is what happens, as you
 11 can see in the extract from Lewin we set out in the
 12 middle of paragraph 47.2, the court will act as
 13 a reasonable trustee could be expected to act having
 14 regard to all the material circumstances.
 15 So in that situation, it is exercising an original
 16 discretion and on a review jurisdiction .
 17 And we make the important point at paragraph 47.3
 18 that the trustee typically surrenders the discretion to
 19 the court, where the trustee is a company in
 20 liquidation , and the trustee may itself be one of the
 21 objects in respect of which the power is exercisable.
 22 And the reason for that is discussed in a case called
 23 Thrells. I'm not going to show your Lordship that in
 24 any great level of detail , but I do just want to remind
 25 your Lordship of the key passage in it . It 's in your

1 authorities bundle, tab 12. Thrells v Lomas, a decision
2 of Sir Donald Nicholls that dates from 1992. We don't
3 need to trouble too much with the facts.

4 If you turn on to page 286, the simple point here is
5 that there is a pension scheme that is in surplus and
6 the trustees have a discretion what to do with it. They
7 can kick the surplus back to the company that is now
8 insolvent. The company is itself the trustee. Or they
9 can apply it among the other objects of the pension
10 fund.

11 Just looking at D, you'll see that the liquidator
12 was represented by Nicholas Warren as he then was, later
13 Mr Justice Warren and the material passages run between
14 letters F and H. Can I ask you to read those two
15 paragraphs to yourselves:

16 "Before me is an application ..."

17 And the next one:

18 "In these circumstances ..."

19 HIS HONOUR JUDGE RAWLINGS: Okay, yes.

20 MR GLEDHILL: The simple point to collect from that, at 459,
21 H, is Sir Donald's comment that the liquidator is
22 confronted with an impossible conflict of duties. And
23 your Lordship will bear in mind that where the insolvent
24 company, of which the liquidator is the office holder is
25 one of the objects potentially of a discretionary power,

61

1 there are, at the very least, two compelling reasons why
2 the position is one of impossible conflict. The first
3 is that the liquidator in his capacity as such owes
4 duties to unsecured creditors which conflicts with his
5 duty to have regard to the interests of the other
6 beneficiaries of the trust. Wearing his liquidator hat,
7 he has to favour the unsecureds. Wearing his trustee
8 hat, he cannot possibly lean towards the unsecureds
9 because that is not the power conferred upon him by the
10 trust.

11 And the second and not immaterial consideration is
12 that the office holder will also have a claim against
13 the insolvent estate for his own fees.

14 And your Lordship will remember earlier this week
15 that my learned friend's instructing solicitors
16 circulated an estimated outcome statement giving you
17 a few figures. And that statement, we may go back to it
18 in a moment, showed that the administration costs,
19 including remuneration and expenses to date, total
20 a little over £6.5 million for two years.

21 So there is no possible basis upon which the
22 administrators in this case, in their capacity as SSSHL
23 administrators, being also the administrators of Lendy,
24 could possibly take a decision about who the proper
25 distributed beneficiaries under the power constituted by

62

1 the debenture should be.

2 HIS HONOUR JUDGE RAWLINGS: I suspect you're going to come
3 to it. Ms Toube puts it slightly differently in that
4 she suggests that, okay, we have a conflict but what
5 we're asking you to do is to direct us what to do rather
6 than surrendering our discretion to the court.

7 MR GLEDHILL: Well, I'd say it's a distinction without a
8 difference. You can go to the court and say: tell us
9 what to do; tell us what to do in our capacity as
10 administrators and we will cause the trustee to do that.
11 That is effectively one and the same as saying we are
12 surrendering our discretion to the court.

13 It may be a distinction without a difference, but
14 what absolutely cannot happen is that the administrators
15 cannot say to your Lordship: determine the relevant
16 principles, decide whether the Model 2 lenders are
17 correct in the analysis that they are suggesting of how
18 the discretion should be exercised, and then we will
19 treat that merely as an illuminating explanation of the
20 principles and go away and exercise our discretion.

21 MS TOUBE: My Lord, just in case it helps cut through this
22 point, we absolutely aren't saying that. We are asking
23 your Lordship to give us a direction as to how to
24 exercise our discretion and we will do it.

25 HIS HONOUR JUDGE RAWLINGS: In that respect, the principles

63

1 that I should apply are no different than if the
2 discretion was surrendered to the court. Okay.

3 MR GLEDHILL: We are happy then. We are both on the same
4 page. As I say, if there is a distinction at all, it's
5 a distinction without a difference. I think we are both
6 saying to your Lordship that effectively you put
7 yourself in the position as the trustee, and where one
8 characterises it as the court taking a decision as a
9 trustee or the court telling the administrator what to
10 do is a distinction without any practical significance,
11 so we can move on from that.

12 So I have already shown your Lordship what the
13 approach is by reference to paragraph 47.2 in our
14 skeleton. You don't need to go back to it, but just
15 quoting it back to you:

16 "... [the court] ... will act as a reasonable
17 trustee could be expected to act having regard to all
18 the material circumstances ..."

19 I'm now coming on to a slightly different point.
20 I notice the time. Entirely up to your Lordship. If
21 you want me to keep going, I can keep going, or if
22 you want me to break, I can break.

23 HIS HONOUR JUDGE RAWLINGS: How much longer are you likely
24 to be?

25 MR GLEDHILL: In total, so I am going to be about 25,

64

1 20 minutes or so.
 2 HIS HONOUR JUDGE RAWLINGS: Ms Toubé still has to come back
 3 to provide her reply, so we are going to have to come
 4 back this afternoon anyway. If that's a convenient
 5 point, we may as well break at that point. I am
 6 assuming that the two hours that we have after lunch are
 7 more than adequate to deal with anything you want to say
 8 and Ms Toubé wants to say. Let's come back at
 9 2 o'clock, please.

10 (1.00 pm)

11 (The short adjournment)

12 (2.00 pm)

13 HIS HONOUR JUDGE RAWLINGS: Good afternoon. Sound good?

14 MR GLEDHILL: Sound is very good.

15 HIS HONOUR JUDGE RAWLINGS: Mr Gledhill, carry on.

16 MR GLEDHILL: I had finished dealing with the facts. We'd
 17 established the parameters of the exercise which your
 18 Lordship is being asked to conduct, and then the
 19 starting point for discussion when it comes on to the
 20 question of what should the court do and what are the
 21 principles is just to take you back quickly, if I may,
 22 to the relevant provision in the debenture, C10,
 23 page 182.

24 21.1 says that the monies received by the security
 25 agent will be applied in the following order of

65

1 priority :
 2 "21.1.2 in or towards payment of or provision for
 3 the Secured Liabilities in any order and manner that the
 4 Security Agent determines ..."

5 So the first point to make is, the trustee under
 6 that has an unqualified discretion. And it's important
 7 just to notice the words "in any order", so the
 8 proposition that we are advancing to your Lordship is
 9 not that Lendy be disentitled from participating.
 10 Couldn't do that. The trust says otherwise. But what
 11 we are saying is that the claims of the Model 2
 12 Investors would be discharged in full before a penny
 13 goes to Lendy under clause 21.1.2.

14 And it's important to make a point to your Lordship,
 15 which is possibly obvious, but can do with spelling out
 16 in any event. Each of these trusts is a separate trust
 17 in respect of separate loans and separate security. So
 18 if there is only quite a moderate shortfall to the class
 19 of Model 2 Investors in respect of any given loan, and
 20 that obviously may depend significantly on the answers
 21 that your Lordship gets to under issues 5 and 8, then on
 22 the distribution model that we're proposing, what
 23 happens is that the Model 2 Investors come out first and
 24 then Lendy gets the rest.

25 We are not saying that there should only be any

66

1 distribution to Lendy at all once all of the claims of
 2 Model 2 Investors are fulfilled. We couldn't say that
 3 because each of those debentures constitutes a separate
 4 trust. Quite an important point. Maybe obvious, as
 5 I say, but it's worth making.

6 So far as that is concerned, what are the
 7 principles? The administrator's skeleton argument has
 8 taken your Lordship to the very well-known House of
 9 Lords' decision in *Braganza* and Lady Hale's well-known
 10 remarks in that about the duty of good faith in
 11 contract. And that has nothing to do with the
 12 issue before your Lordship.

13 *Braganza* is concerned with a situation where there
 14 is a contract, bipartite or multipartite, where one of
 15 the parties has a discretion conferred upon them, which
 16 can adversely impact the rights of the other party and
 17 impact its own rights. And what *Braganza* tells you is
 18 that the courts are more ready now than they used to be
 19 to imply terms to the effect that that discretion has to
 20 be exercised rationally and reasonably, has to be
 21 exercised in a particular way, and has to come to
 22 a conclusion which is within certain parameters.

23 And that case isn't of any assistance to your
 24 Lordship because what your Lordship is concerned with is
 25 an express trust. And the person exercising the

67

1 discretion here is the trustee who, of its very nature,
 2 cannot have any beneficial interest in the subject
 3 matter, and the obligations which that trustee owes are
 4 obligations in equity and not of law.

5 And in fact *Braganza* doesn't help your Lordship
 6 because the points that are made in *Braganza* are all
 7 parts of the trustee's duty in any event.

8 Now, it is a question that frequently arises in
 9 a trust context where a trustee is given a discretionary
 10 power to disburse a fund amongst a defined class of
 11 beneficiaries. As to the circumstances in which and the
 12 principles by reference to which the trustee can say:
 13 well, the objects are A, B, C, D and E, those are the
 14 people among whom I can distribute it, can I give it all
 15 to A, can I give it to A and B or do I have to give it
 16 to A, B, C, D and E equally, or how does it work, what
 17 are the principles?

18 And the answer to that question is adequately
 19 addressed in three materials which we have put into your
 20 Lordship's bundle. The first is a short extract
 21 from Lewin, and my Lord finds that at tab 63 in the
 22 authorities' bundle.

23 HIS HONOUR JUDGE RAWLINGS: Yes.

24 MR GLEDHILL: And the relevant extract is at page F1598. At
 25 the top of the page, paragraph 29–062, "Duty of trustees

68

1 ... to act impartially":
 2 "Trustees must act impartially, that is, they must
 3 hold an even hand among all the beneficiaries, except
 4 insofar as the settlement authorises them to
 5 discriminate."

6 And then you see the important commentary at 29–064
 7 between the two hole punches. Can I ask you to read
 8 that to yourself, please.

9 HIS HONOUR JUDGE RAWLINGS: Yes.

10 MR GLEDHILL: The point being made there is where you have
 11 a power whereby you say to a trustee, "Here is £100, you
 12 make a decision about how you want to distribute it as
 13 between A, B, C, D and E", it is inherent in the nature
 14 of that power that the trustee can decide to give £20 to
 15 each of them, £100 to one of them, £25 to four of them
 16 and nothing to one of them.

17 It's meaningless in that situation to say that the
 18 only rational way in which it can be exercised is by
 19 *pari passu* distribution. The essence of the power is
 20 that the power is given to the trustee to make
 21 a decision, and that that decision may connote
 22 ultimately an unequal outcome. In fact a *pari passu*
 23 distribution, unless there is good reason for it, may of
 24 itself be an abdication of that power.

25 And that is the point which you see Lewin making in

69

1 the second and third lines where he says:
 2 "The very discretion conferred is to prefer one over
 3 another; unfairness is not a ground of challenge."

4 And the authority for that and the second of the
 5 materials I wanted to take you to, which underpins that,
 6 is a decision of the Court of Appeal in a case called
 7 *Edge v Pensions Ombudsman*, tab 15 of the authorities
 8 bundle.

9 We summarise the factual background to this in our
 10 skeleton argument, so I'm not going to take you to the
 11 headnote. But in a nutshell, a situation had arisen
 12 under a pension scheme which enabled the trustees to
 13 confer additional advantages, and they had exercised
 14 that power to confer additional advantages on one class
 15 at the expense of another class. And the pension
 16 ombudsman received a complaint from a disappointed
 17 beneficiary, and he upheld that complaint on the basis
 18 that he said the trustees had a power to act in an
 19 even-handed way between the beneficiaries.

20 And there was an appeal to the first instance judge,
 21 Sir Richard Scott, which was successful. There was then
 22 a further appeal to the Court of Appeal, and the
 23 Court of Appeal upheld Sir Richard Scott. And I wanted
 24 to show you two things in this decision. The first is
 25 on page 626. Leading judgment is Lord Justice Chadwick

70

1 and we're in his judgment. On 626 you see just beneath
 2 the letter F, he starts talking about the need to
 3 consider the circumstances in which the surplus has
 4 arisen.

5 And the point I just wanted to bring out is, he sets
 6 out there a variety of the considerations which the
 7 trustees could reasonably have had regard to, but the
 8 key one to get out of it is the one you see between
 9 letters G and H, just off the bottom of the page:

10 "They must, for example, always have in mind the
 11 main purpose of the scheme ..."

12 So that is the benchmark.

13 And then what he goes on to say over the page is
 14 that once the trustees have had regard to the main
 15 purpose of the scheme, if they in their discretion
 16 arrive at a very unequal result, provided they haven't
 17 misconducted themselves on ordinary equitable
 18 principles, that decision stands.

19 And you will see between letters D and E,
 20 a paragraph starting in the middle of the page between
 21 the hole punches, where he addresses the submission
 22 advanced by the Pensions Ombudsman which was the basis
 23 for the decision, which was then the subject of the
 24 litigation, where he says this:

25 "Properly understood, the so-called duty to act

71

1 impartially — on which the ombudsman placed such
 2 reliance — is no more than the ordinary duty which the
 3 law imposes on a person who is entrusted with the
 4 exercise of a discretionary power: that he exercises the
 5 power for the purpose for which it is given, giving
 6 proper consideration to the matters which are relevant
 7 and excluding from consideration matters which are
 8 irrelevant. If pension fund trustees do that, they
 9 cannot be criticised if they reach a decision which
 10 appears to prefer the claims of one interest — whether
 11 that of employers, current employees or pensioners —
 12 over others. The preference will be the result of a
 13 proper exercise of the discretionary power."

14 And then if your Lordship turns back in the same
 15 volume in the authorities to tab 6, we provided you
 16 there with one of the war horses of equity
 17 jurisprudence, *McPhail v Dalton*, which was a decision
 18 about a fiduciary power to distribute a fund amongst
 19 a very large class of objects. And one of the points
 20 taken there was that it gave rise to difficulty because
 21 the class was defined in such a way that it was
 22 difficult to understand all of the individuals who might
 23 be within it, and a suggestion was made: well, how do
 24 the trustees exercise that power? Because isn't their
 25 *prima facie* duty to follow the maxim, equality is

72

1 equity, and distribute *pari passu*.
 2 If you turn on to page F176, you see what
 3 Lord Wilberforce said about that. Just after letter A,
 4 four lines down:
 5 "As a matter of reason, to hold that a principle of
 6 equal division applies to trusts such as the present is
 7 certainly paradoxical. Equal division is surely the
 8 last thing the settlor ever intended: equal division
 9 among all may, probably would, produce a result
 10 beneficial to none. Why suppose that the court would
 11 lend itself to a whimsical execution? And as regards
 12 authority, I do not find that the nature of the trust,
 13 and of the court's powers over trusts, calls for any
 14 such rigid rule. Equal division may be sensible and has
 15 been decreed, in cases of family trusts, for a limited
 16 class; here there is life in the maxim 'equality is
 17 equity,' but the cases provide numerous examples where
 18 this has not been so, and a different type of execution
 19 has been ordered, appropriate to the circumstances."
 20 So what this is telling your Lordship is in the
 21 situation — Edge was concerned with the situation where
 22 the trustee had taken the decision and had preferred
 23 certain beneficiaries over others, and that was subject
 24 to challenge. In this case the court is concerned with
 25 asking the question: how would it execute the power if

73

1 it stood in the place of the trustee, if the trustee had
 2 surrendered its discretion.
 3 And what Lord Wilberforce is saying here is well,
 4 you find cases of family trusts generally dating from
 5 the 19th century where the court isn't in any position
 6 to second-guess the settlor and to prefer one member
 7 over the other, and so errs towards the principle that
 8 equality is equity, but that is effectively purely
 9 a default rule.
 10 And we made the point to your Lordship in our
 11 skeleton argument the trustee here was constituted as
 12 SSSHL. There are some cases where the court is in
 13 difficulty in deciding what might be a fair method of
 14 distribution because it's simply not as close to the
 15 coalface of the facts as the trustee was, but we
 16 respectfully suggest to your Lordship that having read
 17 the evidence you have read and listened to four days of
 18 legal argument, you are as well placed as anyone, with
 19 respect, is ever likely to be.
 20 So those were the three materials that we say
 21 condition the approach that you should take to the
 22 exercise of the discretion, or in giving the
 23 administrators, as they would have it, directions as to
 24 how they should exercise their discretion.
 25 And we suggest that it is clear that you or they

74

1 have a free hand to apply the trusts — unequally the
 2 funds, unequally as between Lendy and the Model 2
 3 Lenders. And as your Lordship knows, we say you should
 4 exercise that discretion to exclude Lendy from
 5 participation, unless and until in respect of any given
 6 loan, the shortfall to the Model 2 Investors has been
 7 made good.

8 Now my learned friend places emphasis on the fact
 9 that Lendy is now insolvent. And I make the point to
 10 your Lordship that the beneficiaries of the trust are
 11 not the unsecured creditors of Lendy. But it's
 12 nevertheless worth just reminding ourselves who those
 13 unsecured creditors are.

14 Does your Lordship have to hand the estimated
 15 outcome statement which Shoosmiths circulated, I think
 16 on Monday evening?

17 HIS HONOUR JUDGE RAWLINGS: Probably not to hand, but I can
 18 go back and get it. You think it was Monday evening.

19 MR GLEDHILL: I think it was Monday evening. Someone can
 20 correct me if I'm wrong about that. It was an e-mail
 21 from Ms Doyle, and ... I have it. Would it be — it was
 22 an e-mail of —

23 HIS HONOUR JUDGE RAWLINGS: Estimated outcomes statement as
 24 at 23 May 2021, that?

25 MR GLEDHILL: Yes, that's the one. So who are the

75

1 creditors? Taking them in order of size, the largest
 2 class — leaving aside the Model 2 Investors, the
 3 largest class is the Model 1 Investors at 12.5 million,
 4 but that obviously depends on the answer that your
 5 Lordship gets to under issue 3.

6 HIS HONOUR JUDGE RAWLINGS: So in the event that they are on
 7 limited recourse, then they are zero.

8 MR GLEDHILL: I cannot say to your Lordship they will be
 9 zero, but they will certainly be much less than that.

10 It is just possible there might be some instances where
 11 Lendy received recoveries and didn't pass them on.

12 HIS HONOUR JUDGE RAWLINGS: Okay.

13 MR GLEDHILL: Then the next biggest creditor after them, and
 14 in fact the biggest if you knock out the M1 creditors,
 15 the Model 1 creditors, is the cost of the
 16 administration, and your Lordship sees that stated as at
 17 23 May 2021 at £6.5 million.

18 HIS HONOUR JUDGE RAWLINGS: That's going to come out first
 19 whatever happens.

20 MR GLEDHILL: Yes, from assets in the estate.

21 HIS HONOUR JUDGE RAWLINGS: The costs of the administration
 22 won't suffer as a result of my decision.

23 MR GLEDHILL: No, that seems to be correct because there are
 24 £21.1 million of asset realisations in the kitty. And
 25 the same would seem to hold good for the HMRC claims to

76

1 the extent that they are also administration expense
 2 claims.
 3 HIS HONOUR JUDGE RAWLINGS: (inaudible) 2 million that comes
 4 out.
 5 MR GLEDHILL: Yes. And then the unsecured creditors have
 6 1.3 — just under 1.4 million for trade creditors, and
 7 it won't escape your Lordship's attention in the line
 8 immediately beneath that 1.3 million figure that —
 9 either comprises or in addition to it, there is
 10 a £600,000 proof by LGL. That's the parent company.
 11 That's the vehicle for Mr Gordon and Mr Brooke, who the
 12 administrators are suing for fraud. As I understand it,
 13 that is in respect of loans allegedly made before
 14 administration. So they will be a significant
 15 beneficiary from any enhanced unsecured dividend that is
 16 payable with monies dispensed to Lendy under the trust.
 17 And then your Lordship sees there is also a figure
 18 for FCA remediation, £1 million. Just to help your
 19 Lordship, you can chase down the reference afterwards if
 20 it's necessary to do so, but basically what happened
 21 here was that there were various Model 2 Investors who
 22 were buying loan portions on the secondary market,
 23 despite the fact that the relevant loan was in trouble,
 24 it may even have gone into default by the time they
 25 bought in.

77

1 And one of the many criticisms that the FCA made is
 2 they ought to have been told, unsurprisingly, before
 3 buying loans at par value, that the loans were already
 4 distressed. So that £1 million figure there is in fact
 5 a figure for amounts that would otherwise be payable to
 6 Model 2 Investors as well.
 7 HIS HONOUR JUDGE RAWLINGS: Does that mean that the FCA has
 8 paid that and is seeking to get it back again?
 9 MR GLEDHILL: Not as far as I'm aware. I looked at the
 10 underlying paragraphs of Mr Webb's witness statement
 11 referred to in that note, paragraphs 65 through 67, and
 12 I didn't understand that to be saying that the FCA had
 13 paid and was then subrogated. And in fact as far as
 14 I know, it wouldn't do that. It's not like the
 15 financial services compensation scheme.
 16 HIS HONOUR JUDGE RAWLINGS: Shouldn't do, no.
 17 MR GLEDHILL: I think what it did was to impose
 18 a restitution order on Lendy, which Lendy evidently
 19 hadn't fulfilled by the time of administration.
 20 HIS HONOUR JUDGE RAWLINGS: But don't these same people, if
 21 they are the current transferees of the Model 2 loan,
 22 don't they benefit from having the money allocated as
 23 you urged me to do?
 24 MR GLEDHILL: That's exactly my point. That's exactly my
 25 point.

78

1 HIS HONOUR JUDGE RAWLINGS: Okay. Fine.
 2 MR GLEDHILL: So if you asked one of the notional
 3 beneficiaries of this compensation, "Would you like to
 4 have an unsecured claim for your compensation or would
 5 you like to have an enhanced payment under the security
 6 waterfall from the trustee?", the answer is obvious,
 7 it's going to be the latter.
 8 HIS HONOUR JUDGE RAWLINGS: So there may be a proportion
 9 there that would be secured. We don't know how much
 10 but — okay.
 11 MR GLEDHILL: Just in relation to the unsecured creditors,
 12 we don't get any breakdown of who else other than the
 13 parent companies in that £1.4 million odd. One point
 14 I did pick up, reading Mr Webb's witness statement, is
 15 that there are or there is reference in that to the fact
 16 that the former Finance Director of Lendy as at the date
 17 of that statement, July of last year, was pursuing
 18 unfair dismissal claims against Lendy, which obviously
 19 opens up the possibility that some other of these trade
 20 creditors are also Lendy insiders, if I can put it that
 21 way. We just don't know.
 22 So, my Lord, those are the principles and that's all
 23 I'm going to say about the background. And I am now
 24 going to make submissions to your Lordship about the
 25 reasons why we say that the discretion under this trust

79

1 should be exercised in the way in which I have proposed,
 2 and I make five points.
 3 The first and the most important consideration is
 4 that many of the Model 2 Investors are likely, like
 5 Mr Melton, to be retired and to be unable to replace
 6 capital losses that they have sustained. Some of them
 7 will be elderly. Many, like Mr Powell, who you will
 8 remember is a part-time sales assistant at HMV, are
 9 likely to be of limited means.
 10 Those persons are likely to have been hit hard by
 11 the losses to capital which they have sustained, and
 12 I respectfully suggest that a trustee should be doing
 13 its best to assist them.
 14 On the other side of the coin, your Lordship has no
 15 evidence suggesting that any particular hardship will be
 16 caused to unsecured creditors if you deny Lendy
 17 participation in the fund in the way that I have
 18 suggested.
 19 HIS HONOUR JUDGE RAWLINGS: Yes, although in the event that
 20 Model 1 investors do have those unsecured claims, then
 21 the profile of them is likely to be similar to the
 22 profile of the Model 2.
 23 MR GLEDHILL: I accept that. I accept that. It is a much
 24 smaller class, in the region of one-tenth, but I have to
 25 accept that the same points that I have just made might

80

1 apply to that residual class of M1 investors.
 2 The second point of the five is the one that I have
 3 just made to your Lordship by reference to the
 4 Shoosmiths' outcome statement, that a significant
 5 proportion of the unsecured debt appears to be owed to
 6 Lendy insiders. The reference in Mr Webb's witness
 7 statement to the unfair proceedings by Kieran O'Connor,
 8 the former Finance Director, was Webb 2, paragraph 431.
 9 £600,000 proof by LGL, the holding company.

10 And your Lordship bears in mind that even if the
 11 administrators succeed in fraud claims against Mr Brooke
 12 and Mr Gordon, those claims would not be eligible for
 13 set-off if LGL truly has debts in respect of
 14 pre-litigation funding, which had excluded — there
 15 would be a problem with mutuality, obviously.

16 And I suggest to your Lordship that it will be an
 17 unfortunate result which Model 2 Investors are likely to
 18 find unpalatable, if Lendy is allowed to rank *pari passu*
 19 with their claims under the trust, if the consequence of
 20 that will be to swell the dividend for distribution to
 21 creditors, including some of those who were involved in
 22 this saga before the balloon went up and it went into
 23 administration.

24 Third point, your Lordship, is one that we made in
 25 our skeleton argument. It is to be assumed that Lendy's

81

1 unsecured creditors freely ran a risk on Lendy's
 2 insolvency. Model 2 Lenders most emphatically did not
 3 run that risk. And I showed your Lordship earlier that
 4 when Model 2 was introduced, the investors were told
 5 that their security would be held in SSSHL and that the
 6 whole point of that quite specifically was to immunise
 7 them from the consequences of Lendy's bankruptcy.

8 When I took your Lordship to Lord Justice Chadwick's
 9 decision in *Edge*, I drew your attention to his comment
 10 that one begins by identifying the main purpose of the
 11 trust, what those who set it up were seeking to achieve.
 12 And I suggest that when your Lordship looks at the
 13 announcement that was originally made to the investors
 14 about the reason for putting security behind SSSHL, the
 15 answer to that is clear. It was to immunise the Model 2
 16 Lenders from the consequence of Lendy's insolvency.

17 They were told at the outset that SSSHL would hold
 18 the security on bare trust. No mention was made at that
 19 stage of Lendy having competing claims under it. No
 20 mention was made to them that the trustee had
 21 a discretion to pay Lendy either an advance or *pari*
 22 *passu* with their claims. And I suggest that that is an
 23 important point in the context of your overall
 24 discretionary exercise.

25 Fourth point. It will not have escaped your

82

1 Lordship's attention that in inviting you to direct
 2 a *pari passu* distribution to Lendy and the Model 2
 3 Investors, the administrators are effectively inviting
 4 either you to renege or inviting you to allow them to
 5 renege on the clear assurances which Lendy gave the
 6 Financial Conduct Authority in March 2018 that lenders
 7 would take priority. I do not in any way criticise the
 8 administrators for taking that position. It's
 9 a directions application and it is their obligation to
 10 give the court the benefit of adversarial argument on
 11 that point.

12 But we do question whether it could possibly be
 13 right for this court to go down that road. Lendy gave
 14 the Authority categorical assurances that lenders would
 15 come first. It said the same in the first recovery
 16 policy which they disseminated to the investor community
 17 in April 2018, and as far as the evidence goes, that was
 18 fundamental to their subsequently obtaining
 19 authorisation from the Authority in July 2018.

20 We respectfully suggest to your Lordship it could
 21 not be right to accede to the administrator's suggestion
 22 that you should resile from those assurances or allow
 23 Lendy to resile from the assurances it gave to the
 24 regulator as part of the price for continuing in
 25 business as a regulated entity at all. No trustee

83

1 should do that. Still less, with appropriate respect,
 2 should a court when asked to put itself into the shoes
 3 of a trustee.

4 Fifth point. We suggest to your Lordship, as well
 5 as that specific point, that Lendy's more general
 6 misconduct is also a factor of some relevance. My Lord
 7 has seen reference to it in some of the FCA
 8 correspondence, though you have not been taken by all
 9 means to the full volume of the material dealing with
 10 that point. Your Lordship has seen in particular the
 11 concern that the FCA expressed from time to time about
 12 whether Lendy was mis-selling, which resulted, among
 13 other things, in Lendy's forced change of name from the
 14 misleading Saving Stream name to Lendy. And in our
 15 skeleton argument, perhaps if your Lordship can take
 16 that out and turn up page 49.

17 In our skeleton argument on page 49, we made the
 18 point that even that, even when it made that concession,
 19 the way that it characterised it to its investor
 20 community was thoroughly misleading. Looking at
 21 page 49, paragraph 55.3, so Lendy's response to that
 22 first letter, that was the letter that I read to your
 23 Lordship about the Authority referring to the
 24 inappropriateness of using the word "Saving Stream" as
 25 the tag for this product:

84

1 "Lendy's response to that first letter was
2 particularly noteworthy. One of the FCA's principal
3 concerns at this point was that Lendy's use of the
4 'Saving Stream' trading name was misleading ..."

5 Then 55.4:

6 "Lendy replied on the 2 September 2016 deadline,
7 initially declining to comply with the FCA's direction
8 ... but an internal document dating from 1 December 2016
9 ... shows that by that date it was reluctantly bowing to
10 pressure from the regulator, in part, out of a concern
11 that if it did not, the 'FCA will almost certainly then,
12 over the next 3 months, look at every aspect of Lendy
13 Ltd's compliance with the regulator's rules ...'."

14 Your Lordship sees paragraph 55.5:

15 "Remarkably, however, when announcing this
16 rebranding to its existing lender base, Lendy made no
17 mention at all of the fact that it had resulted from a
18 threat of intervention by the FCA to correct the
19 misleading impression created by its previous trading
20 name. Instead, it sought to explain it away with bland
21 generalities that were, on any view, far from frank:
22 'following feedback from users we are integrating the
23 Saving Stream platform under the Lendy brand. This is
24 in order to simplify the brand and make accessing the
25 crowdfunding platform easier for all our clients'."

85

1 Thoroughly disingenuous. And I make the point to
2 your Lordship, in light of that point and many other
3 like it, that the wider public may find it very
4 difficult to understand why any portion of the trust
5 monies held by SSSHL should go to the Lendy estate,
6 given that Lendy was itself responsible for getting the
7 Model 2 Investors into this mess.

8 And for the reason that I have already given to your
9 Lordship, it is simply no answer to say that Lendy is
10 now insolvent. As I have explained, the whole point of
11 constituting SSSHL the trustee, rather than Lendy, as it
12 had been under Model 1, was specifically to immunise the
13 Model 2 Investors from the adverse consequences of
14 a potential Lendy insolvency.

15 My Lord, those are my submissions on that final
16 subject.

17 HIS HONOUR JUDGE RAWLINGS: Thank you. Ms Toubé, what do
18 you want to come back on?

19 Reply Submissions on Issue 10 by MS TOUBE

20 MS TOUBE: My Lord, as we saw from the points that my
21 learned friend ended with, much of his submissions are
22 based effectively on an assumption that one should
23 punish Lendy for its, to put it mildly, poor behaviour
24 for the representations which it made to the FCA and
25 possibly also to its investors. There is no doubt that

86

1 the Model 2 Investors, and no doubt also the Model 1
2 Investors, will feel quite strongly about issues such as
3 that. But contrary to what my learned friend says, it
4 does make all the difference that Lendy is now
5 insolvent.

6 This is not an issue which depends upon punishing
7 Lendy, punishing those who were its directors, or
8 dealing with misrepresentation claims which may be
9 brought in the future.

10 Lendy itself has unsecured creditors. It is the
11 statutory trustee, indeed, for those unsecured
12 creditors, holding them on the statutory trust.
13 I should correct one point. That 21.1 million includes
14 the asset realisations on the Model 2 Loans. So when it
15 says Lendy's administration, of course some of those are
16 the exact loans that we're talking about here, held
17 within SSSHL.

18 I have asked my instructing solicitors what is held
19 outside that, and the answer is about 4.5 million. So
20 there is not a large pot of money sitting there in
21 Lendy's estate outside these sums.

22 Now, of course, my learned friend is right that say
23 one has a loan of £100, one recovers £60 of it. The
24 Model 2 Investors may in some cases be asking for £55 of
25 it. So there may be a trickle down into the Lendy

87

1 estate of some small sums. But if the Model 2
2 Investors' argument is correct, the vast majority of the
3 sums held by SSSHL will go to the Model 2 Investors in
4 preference to the unsecured creditors, and indeed the
5 expense creditors in Lendy's estate.

6 And those include more than £5 million worth of
7 liabilities to HMRC, who cannot in any sense be called
8 insiders or people who ran the risk of non-recovery.

9 It also includes the Model 1 Investors who either
10 are not limited recourse for the reasons we've
11 explained, or will in any event potentially have
12 misrepresentation claims. So those Model 1 Investors
13 are not Lendy insiders who should be punished in the way
14 in which my learned friend suggests that that should be
15 the case.

16 So I'll come back to those points again at the end,
17 if I might. But I think it's important to bear that in
18 mind that no doubt it is true that the Model 2 Investors
19 wish all this money to go to them. They might even have
20 thought that they were entitled to have it all to go to
21 them. The question is, however, how should SSSHL
22 exercise its discretion?

23 HIS HONOUR JUDGE RAWLINGS: You say it makes all the
24 difference in the world, and obviously, why does it make
25 a difference at all? I think Mr Gledhill says, well,

88

1 hang on a minute, you should exercise your discretion in
 2 favour of the Model 2 Investors, because they are a much
 3 more sympathetic bunch than the other unsecured
 4 creditors of Lendy who will be getting the money if you
 5 don't do that.
 6 So he said that. Why should it make all the
 7 difference in the world that Lendy is insolvent as to
 8 how the discretion is exercised?
 9 MS TOUBE: Well, your Lordship knows my primary submission
 10 is that one shouldn't be having regard to these factors
 11 at all, because the main purpose of this trust was to
 12 pay the beneficiaries. The beneficiaries were the Model
 13 2 Investors and Lendy. If one has a shortfall,
 14 a general principle should be that you should treat them
 15 evenly handed, if there is nothing to suggest that you
 16 should treat them otherwise than evenly handed. There
 17 is nothing that suggests you should treat them otherwise
 18 than evenly handed; that's the answer.
 19 But the point I was dealing with there is my learned
 20 friend says: ah, well, the main purpose was in fact to
 21 pay the Model 2 Investors first. I don't accept that
 22 for a moment. And, because Lendy behaved so badly, when
 23 a trustee is exercising its discretion, it should
 24 exercise its discretion against Lendy. And I say, well,
 25 if that were right, which as your Lordship knows I say

89

1 it is not, it makes all the difference in the world that
 2 Lendy is insolvent, because when you say Lendy, you mean
 3 the insolvent estate of Lendy, which means you mean the
 4 unsecured creditors of Lendy.
 5 HIS HONOUR JUDGE RAWLINGS: That's true, but he then goes
 6 and has a look at the unsecured creditors of Lendy and
 7 says, well, actually some of them are associates, some
 8 of them were tied up in all the misrepresentations that
 9 they made. So you say they're unsecured creditors as if
 10 that is somehow — that they are somehow more
 11 meritorious than Lendy would be if it was a solvent
 12 trading company.
 13 But Mr Gledhill goes beyond that and says, look at
 14 the unsecured creditors, they include the holding
 15 company, they include a former financial director who
 16 are substantial creditors who will benefit, and who were
 17 tied up in the bad behaviour of Lendy.
 18 MS TOUBE: Well, I should say — we do dispute those claims.
 19 So these are the claims that, for example, that £600,000
 20 had been admitted for voting purposes. There are all
 21 sorts of counterclaims and cross-claims and disputes on
 22 quantum in relation to those claims.
 23 HIS HONOUR JUDGE RAWLINGS: Fine.
 24 MS TOUBE: So — and in any event, in the grand scheme of
 25 things, looking at what those unsecured — the insolvent

90

1 estate is, those are very small. The largest claims,
 2 apart from the costs, are HMRC and the Model 1s. So it
 3 cannot be right for a trustee to exercise its discretion
 4 to deny payment to an entire class of creditors because
 5 it is possible that a small proportion of those may be
 6 people involved in bad behaviour.
 7 HIS HONOUR JUDGE RAWLINGS: Okay.
 8 MS TOUBE: Because if and insofar as they were involved in
 9 bad behaviour, there are claims, as you know, that are
 10 being made against them. And of course there are the
 11 misrepresentation claims.
 12 So all of the factors which my learned friend relies
 13 on may well give rise to additional claims which the
 14 Model 2 Investors have. And my learned friend says, ah,
 15 well, they just give rise to personal claims that — we
 16 don't want them as much as we want the money. To which
 17 the answer is, of course you would rather have all of
 18 the money, but that is not an answer to the point. The
 19 real complaints that you have are against Lendy which
 20 entitle you to make claims for breach of statutory duty
 21 or misrepresentation etc. But they don't entitle you to
 22 take the entire element of the shortfall to pay
 23 yourselves off first.
 24 And SSSHL was not regulated by the FCA. SSSHL did
 25 not make any representations to the FCA. SSSHL did not

91

1 make any representations to the Model 2 Investors. The
 2 question is —
 3 HIS HONOUR JUDGE RAWLINGS: Why would that be relevant?
 4 It's just the trustee exercising the discretion.
 5 MS TOUBE: Yes.
 6 HIS HONOUR JUDGE RAWLINGS: So if at the moment (inaudible)
 7 under the microscope, it's the beneficiary's behaviour,
 8 if at all.
 9 MS TOUBE: Yes, the point I was making was, I suppose that
 10 I could conceive of an argument which could be made if
 11 Lendy were the trustee and also the beneficiary. But it
 12 is SSSHL, which is a different company with its own
 13 creditors.
 14 HIS HONOUR JUDGE RAWLINGS: All right.
 15 MS TOUBE: So it does boil down to the point which your
 16 Lordship put to me earlier which is: do you accept that
 17 the bad behaviour of one beneficiary is something that
 18 can and indeed, according to Mr Gledhill, should be
 19 relied upon to deny its estate any recovery at all until
 20 the Model 2 Investors have been paid off in full.
 21 And effectively what my learned friend says is, yes,
 22 you can take into account a selection of things which
 23 would entitle you to make a claim against that
 24 beneficiary to disentitle their insolvent estate to
 25 everything, and we say that's just not right.

92

1 And so in that regard the cases upon which my
2 learned friend relies, which are cases where it entitles
3 a trustee to make a decision about what to do, for
4 example in the Edge case there was no shortfall there
5 was a surplus which it was distributing, it was entitled
6 to take a decision about where to put that surplus.
7 Whereas here you've got a shortfall in a trust where the
8 main purpose was said to be to pay the beneficiaries
9 without determining which one of them one should pay.

10 HIS HONOUR JUDGE RAWLINGS: Yes.

11 MS TOUBE: And so that I think really deals with almost all
12 the points I wanted to make.

13 I'm just looking at the basis on which my learned
14 friend said that discretion should be exercised in
15 favour of the Model 2 Investors. The first point was
16 the Model 2 Investors are, or at least some of them are,
17 disadvantaged. And we accept, we absolutely accept that
18 people like Mr and Mrs Melton in particular have lost
19 their life savings. And it is absolutely the case that
20 both Model 1 and Model 2 Investors, who are not going to
21 be able to recover in full from this company, will be
22 disadvantaged. Some of them may lose their life
23 savings. Other people like Ms Taylor being more
24 sophisticated with less loss. But that is not a basis
25 on which SSSHL should exercise its discretion.

93

1 HIS HONOUR JUDGE RAWLINGS: Well, nor even a factor you say.

2 MS TOUBE: Nor even a factor.

3 HIS HONOUR JUDGE RAWLINGS: Okay.

4 MS TOUBE: But if it were a factor it isn't a factor that
5 points only in one direction, if I can put it that way.

6 I have already dealt with his second point which is
7 some of the unsecured debt is for Lendy insiders,
8 because of course the answer is: but most of them
9 weren't.

10 And the third point was unsecured creditors ran the
11 risk, whereas he says Model 2 Investors did not, they
12 thought they were going to be paid out in full. And the
13 answer to that, apart from all the documents which your
14 Lordship has already seen, warning the Model 2 Investors
15 of the risks. It certainly can't be said for example
16 HMRC chose to run the risk of not being paid.

17 The fourth point he made was that the administrator
18 should not be allowed to renege on Lendy's
19 representations. But the administrators are the SSSHL
20 administrators and they are not infected by Lendy's
21 representations.

22 HIS HONOUR JUDGE RAWLINGS: Yes, I think the point was --
23 yes. Right, I suppose in the wider sense he is saying
24 that the party who made the representations should not
25 be favoured with a proportion of the default interest

94

1 which would be contrary to the representations they
2 made. Perhaps "renege" isn't entirely the right word,
3 but I get the general point that he was making, which is
4 that it seems that providing Lendy with some proportion
5 of the default interest would be something that they had
6 represented that they would not have.

7 MS TOUBE: Yes. So the first point is, it depends what
8 answer you give in relation to default interest.

9 HIS HONOUR JUDGE RAWLINGS: Yes.

10 MS TOUBE: The second point is -- so if my learned friend is
11 right, Lendy is not getting any default interest. If
12 Lendy does get default interest that's because the
13 contract provided on its proper construction for Lendy
14 to get its default interest. And Lendy, whatever Lendy
15 said to the FCA, that is what the contract provided for.

16 HIS HONOUR JUDGE RAWLINGS: Yes.

17 MS TOUBE: There may be claims, as I have said before,
18 against Lendy for breach of statutory duty or for
19 misrepresentation, but given that Lendy means the
20 unsecured creditors of Lendy they cannot be infected by
21 Lendy's misrepresentations.

22 So in that context it makes all the difference in
23 the world that Lendy is insolvent, if this is a relevant
24 factor at all, which we say it's not.

25 And the same point is made in relation to Lendy's

95

1 misconduct. And again my learned friend says there,
2 well that the Model 2 Investors and the market would
3 think this was a terrible thing to happen if
4 a discretion were exercised in this way, and even more
5 so by the court. And the answer is, well holding that
6 over the court's head cannot be appropriate in these
7 circumstances where this is not about rewarding the
8 lendeer, this is about the proper exercise of discretion
9 to two classes of beneficiaries where one of them,
10 Lendy's unsecured creditors, are no more, if I can put
11 it this way, "the bad guys" than the Model 2 Investors.
12 HMRC, the Model 1 Investors, the administrators for
13 their costs, these are not people who are infected by
14 what Lendy did prior to administration.

15 So my Lord I think that deals with all the points
16 that my learned friend made that I hadn't already dealt
17 with in opening.

18 HIS HONOUR JUDGE RAWLINGS: Yes. All right. Thank you. Is
19 there anything else?

20 MS TOUBE: No, my Lord, nothing more from me.

21 HIS HONOUR JUDGE RAWLINGS: All right. At this point in the
22 proceedings I normally try to give some indication of
23 when I might hand down judgment. I hope it will come as
24 no surprise that I'm not going to do anything other than
25 reserve judgment, rather than sculling forth with my

96

1 answers now.
 2 It is possible that I may be able to send out
 3 a draft of the judgment in about six weeks' time. That
 4 is possible. If it's not then, then it's more likely to
 5 be 12 weeks' time because of commitments I have there.
 6 In terms of distributing the draft judgment,
 7 Mr Gledhill and Ms Toube or other counsel, are you away?
 8 Because I normally would just send it to counsel and
 9 then provide for them to disseminate it. Once it's
 10 available I would intend to send it out, but if either
 11 of you are away for periods then it may be best for you
 12 to provide those details so that I know who I might send
 13 it to in the alternative. Obviously you both have
 14 juniors that I could send it to.
 15 Do you know whether there are any dates -- sorry for
 16 the difficult question -- when both you and your juniors
 17 are away? If there are and you are unable to answer
 18 that immediately, if you just e-mail my clerk to say
 19 actually this is when I am away, this is when my junior
 20 is away, and I can get some indication of who it would
 21 be best to send the draft judgment to, once it's
 22 available.
 23 As I say, I'm probably not really going to be able
 24 to produce it until at least the beginning of August,
 25 but if not then, then more like the end of September or

97

1 beginning of October. So if you could send to my
 2 clerk's e-mail address details of when you and your
 3 juniors are away so that I know the best person to send
 4 the draft judgment to when it's available. And I am
 5 only looking for when you are away in August
 6 and September really.
 7 MS TOUBE: My Lord, I can certainly give that to you,
 8 although I can say that even if I'm away I will have
 9 access to my e-mails so I can circulate it then in any
 10 event.
 11 MR GLEDHILL: The same will go for me and Mr Conte. In
 12 practical terms if your Lordship sends the draft to
 13 Ms Toube and Mr Perkins and to me and Mr Conte it will
 14 get to where it needs to get to. Even if we are away we
 15 will be on e-mail.
 16 HIS HONOUR JUDGE RAWLINGS: Then don't worry about it.
 17 Provided you have that confidence I shall send it to all
 18 four of you and then I trust that it will get to the
 19 right place. And obviously the instructions as to what
 20 to do and to come back as usual with comments etc will
 21 come out with the draft judgment.
 22 All right, if there is nothing else we can end at
 23 that point, one hour and six minutes ahead of schedule
 24 I think.
 25 MS TOUBE: Thank you very much, my Lord.

98

1 MR GLEDHILL: I'm grateful to your Lordship. Thank you.
 2 (2.55 pm)
 3 (The hearing concluded)

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8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

99

1 INDEX

2 PAGE

3 Submissions on Issue 10 by MS TOUBE1

4 Submissions to Issue 10 by21

MR GLEDHILL

5

6 Reply Submissions on Issue 10 by MS86

7 TOUBE

8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

100

101

A	81:11 89:24 91:10,19 92:23 95:18	appears (6) 10:15 24:4 42:13 44:16 72:10 81:5	avenue (1) 29:5	better (1) 12:12	cases (7) 73:15,17 74:4,12 87:24 93:1,2	column (1) 52:11
a46 (1) 57:6	agent (9) 2:5 3:6,21 4:12	applicable (1) 59:14	aware (2) 1:14 78:9	between (29) 7:22 8:13	cast (1) 46:8	come (27) 3:17 10:24 16:23 29:20 33:23,25 42:10 47:19 48:24,25 49:8,15,16 50:5 63:2 65:2,3,8 66:23 67:21 76:18 83:15 86:18 88:16 96:23 98:20,21
abdication (1) 69:24	11:3 22:22 30:10 65:25 66:4	application (10) 2:21 6:12 40:16 22 41:25 42:6,8 59:17 61:16 83:9	away (13) 28:10 39:5 63:20 85:20 97:7,11,17,19,20 98:3,5,8,14	9:10,10,14 14:16,20 16:1 19:3 23:8,19 28:2 29:23 38:5 41:14 45:18 49:22 53:19 56:10,20 57:16 61:13 69:7,13 70:19 71:8,19,20 75:2	caused (1) 80:16	commentary (1) 69:6
ability (1) 5:22	ago (5) 15:13 25:16 34:24 50:20 55:2	applied (11) 3:3 16:8,18 37:21,24 38:2,8,19 39:9 55:23 65:25		biggest (2) 76:13,14	ceased (1) 59:11	coming (3) 3:11 9:20 14:18 19:23 56:25 65:19 77:3
able (3) 93:21 97:2,23	agree (1) 36:2	applies (1) 73:6	B	bid (1) 41:12	century (1) 74:5	comfort (1) 51:9
above (5) 32:1 40:14 47:6 52:20 55:3	agreed (2) 16:2 56:7	apply (7) 2:8 6:20 23:2 61:9 64:1 75:1 81:1	b (11) 13:8 23:21 32:25 34:4 36:17 56:13 58:10 68:13,15,16 69:13	biggest (2) 76:13,14	certain (2) 67:22 73:23	coming (3) 3:11 9:20 14:18 19:23 56:25 65:19 77:3
absolutely (7) 16:5 32:15 38:14 63:14,22 93:17,19	agreement (9) 2:19 4:8 11:20 23:6,7 30:8,12,21,21	approach (3) 29:12 64:13 74:21	b115 (1) 34:12	bipartite (1) 67:14	chadwick (1) 70:25	confronted (1) 61:22
abu (1) 8:20	agreements (2) 23:7 31:2	applying (1) 12:15	b116 (2) 34:12 36:18	bit (4) 35:5 48:18 53:24 55:20	chadwicks (1) 82:8	confrontation (1) 51:9
accede (1) 83:21	ah (2) 89:20 91:14	apportioned (1) 10:9	b117 (1) 36:21	bits (1) 9:23	challenge (2) 70:3 73:24	confronting (1) 64:19
accept (7) 80:23,23,25 89:21 92:16 93:17,17	ahead (2) 36:13 98:23	approval (1) 60:1	back (46) 2:20 10:24 15:19 19:23 31:23 32:25 33:23 34:4 35:1 36:15,16 38:10 39:5 41:15 43:22,23 44:11 45:8 46:5 47:19 48:24,25 49:8,15,16 50:5 51:19 53:10 55:6 58:6 59:19 61:7 62:17 64:14,15 65:2,4,8,21 72:14 75:18 78:8 86:18 88:16 98:20	blatant (1) 85:20	champion (1) 29:1	confronting (1) 64:19
accepts (1) 46:20	aid (1) 50:4	approximately (1) 41:9	back (46) 2:20 10:24 15:19 19:23 31:23 32:25 33:23 34:4 35:1 36:15,16 38:10 39:5 41:15 43:22,23 44:11 45:8 46:5 47:19 48:24,25 49:8,15,16 50:5 51:19 53:10 55:6 58:6 59:19 61:7 62:17 64:14,15 65:2,4,8,21 72:14 75:18 78:8 86:18 88:16 98:20	blatantly (1) 92:15	change (9) 24:6 29:21 32:20,20 35:8 37:8 43:7 47:14 84:13	confronting (1) 64:19
access (1) 98:9	aims (1) 51:9	april (10) 14:7 16:1 50:17 51:3 53:14,17 58:5,16,21 83:17	background (3) 23:15 70:9 79:23	boil (1) 92:15	characterised (1) 84:19	confronting (1) 64:19
accessing (1) 85:24	alive (1) 38:14	arbitrarily (1) 8:25	backwards (1) 43:19	bonuses (1) 52:18	characterises (1) 64:8	confronting (1) 64:19
accommodate (1) 49:7	allegedly (1) 77:13	area (1) 1:7	bad (7) 26:2,11 90:17 91:6,9 92:17 96:11	bonus (1) 52:18	characterising (1) 6:11	confronting (1) 64:19
accordance (4) 2:9,11 21:10 23:3	allocated (1) 78:22	arent (1) 63:22	badly (1) 89:22	bonuses (1) 29:7	charge (1) 44:7	confronting (1) 64:19
according (3) 32:14 51:1 92:18	allocation (1) 9:14	argument (17) 25:5 31:25 32:9,12 37:15 49:24 59:20 67:7 70:10 74:11,18 81:25 83:10 84:15,17 88:2 92:10	balance (2) 28:24 41:5	borrower (10) 3:24 11:5 16:7 23:8 24:11 26:4,8 52:7,12 55:22	charged (2) 58:17,21	confronting (1) 64:19
account (6) 34:16 36:3,6 37:7 40:10 92:22	allow (2) 83:4,22	around (2) 10:24 48:13	balloon (1) 81:22	breakdown (1) 79:12	changes (6) 35:12 42:19,25 43:1 44:2,8	confronting (1) 64:19
accrual (1) 52:18	allowed (2) 81:18 94:18	arrangement (1) 24:17	bank (1) 40:10	bring (3) 54:11,23 71:5	changing (4) 30:2 31:1,5 47:20	confronting (1) 64:19
accrued (3) 11:19 29:6 30:11	almost (3) 48:13 85:11 93:11	arrangements (2) 24:2 27:18	bankruptcy (7) 25:24 26:1,10,14,16,20 82:7	bracket (1) 85:9	characterised (1) 84:19	confronting (1) 64:19
accruing (1) 4:4	along (2) 29:6 30:25	arrive (1) 71:16	bare (6) 26:24,25 27:6,12,13 82:18	brackets (1) 3:2	characterises (1) 64:8	confronting (1) 64:19
accurate (1) 10:18	already (12) 37:19 38:14 46:23 52:10 53:23 56:5 64:12 78:3 86:8 94:6,14 96:16	aside (1) 76:2	base (1) 85:16	braganza (8) 7:2,10 8:12 67:9,13,17 68:5,6 75:15	charge (1) 44:7	confronting (1) 64:19
achieve (1) 82:11	also (24) 3:12 5:4,7 9:8 13:5 17:25 18:12 20:25 26:21 27:9 35:15 44:18,19 52:6 62:12,23 77:1,17 79:20 84:6 86:25 87:1 88:9 92:11	ask (5) 1:20,20 2:17 61:14 69:7	based (2) 42:18 86:22	breach (2) 91:20 95:18	chargee (1) 24:12	confronting (1) 64:19
acknowledge (2) 14:19 46:15	alternatively (1) 60:8	asked (8) 6:1 46:12 47:3 50:19 65:18 79:2 84:2 87:18	basically (1) 77:20	break (10) 34:16 48:15,22,24 49:5,19,21 64:22,22 65:5 96:7	charges (2) 3:4,10	confronting (1) 64:19
acting (1) 11:3	although (4) 10:14 16:4 80:19 98:8	asking (8) 6:8,15,17,19 63:5,22 73:25 87:24	basing (1) 16:21	breakdown (1) 79:12	chase (1) 77:19	confronting (1) 64:19
action (3) 52:5,7 55:23	always (4) 33:12 44:23 46:6 71:10	aspect (1) 85:12	basis (5) 62:21 70:17 71:22 93:13,24	bring (3) 54:11,23 71:5	checked (1) 38:10	confronting (1) 64:19
actual (2) 4:1 5:12	amend (1) 16:15	aspects (2) 23:15 39:1	base (1) 85:16	bringing (1) 59:11	chase (1) 77:19	confronting (1) 64:19
actually (7) 8:5 11:15,24 30:25 33:9 90:7 97:19	amended (25) 10:21 12:21 14:11,21,23,24 15:21,22 16:10,12 25:3 27:20 28:6 29:19,23 34:7 37:2 38:17 41:21 42:11,13 46:22 53:8 54:10 55:21	asset (6) 27:15 35:22 44:6,21 76:24 87:14	based (2) 42:18 86:22	brooke (3) 24:22 77:11 81:11	checkbox (1) 38:10	confronting (1) 64:19
addition (4) 35:15,19 53:12 77:9	amendment (1) 41:8	assets (2) 20:12 76:20	basically (1) 77:20	brought (2) 27:25 87:9	choked (1) 38:10	confronting (1) 64:19
additional (3) 70:13,14 91:13	among (6) 23:25 61:9 68:14 69:3 73:9 84:12	assist (1) 80:13	basing (1) 16:21	bullet (1) 51:14	chose (1) 94:16	confronting (1) 64:19
address (1) 98:2	amongst (2) 68:10 72:18	assistance (1) 67:23	bear (2) 61:23 88:17	bunch (1) 89:3	chronology (2) 13:16 57:1	confronting (1) 64:19
addressed (2) 53:1 68:19	amounts (6) 11:9 30:5 34:21 36:13 52:14 78:5	assistant (1) 80:8	bearing (1) 29:13	bundle (29) 1:25 7:4 13:8 14:4,14 15:24 22:17 23:21 24:6,8,13 25:13 28:10,11 29:20,24 32:25 34:4,15 36:17 39:7 41:15 50:13 55:16 56:7 61:1 68:20,22 70:8	chunk (4) 3:16 18:13 45:19 50:3	confronting (1) 64:19
addresses (1) 71:21	analogue (1) 40:10	associates (1) 90:7	bearing (1) 29:13	burst (1) 85:9	circulate (1) 98:9	confronting (1) 64:19
adequate (1) 65:7	analysis (4) 5:25 31:16 33:9 63:17	assume (2) 38:12 48:7	bears (1) 81:10	brackets (1) 3:2	circulated (3) 13:4 62:16 75:15	confronting (1) 64:19
adequately (1) 68:18	announced (4) 24:6,20 52:1 58:4	assumed (1) 81:25	become (2) 3:2 26:3	braganza (8) 7:2,10 8:12 67:9,13,17 68:5,6 75:15	circumstances (10) 20:4 21:11 48:5 60:14 61:18 64:18 68:11 71:3 73:19 96:7	confronting (1) 64:19
adjoin (1) 49:12	announcement (6) 25:15,17 58:16,22 59:2 82:13	assuming (1) 65:6	before (25) 11:20,25 14:9 19:4 24:19 27:25 28:6 34:12,20 45:22 46:13,22 49:4,14,21,22 55:20 59:15 61:16 66:12 67:12 77:13 78:2 81:22 95:17	breach (2) 91:20 95:18	civilised (1) 48:20	confronting (1) 64:19
adjournment (2) 48:23 65:11	announces (1) 35:8	assurance (4) 47:17 55:9,10,25	begin (2) 41:16 55:25	break (10) 34:16 48:15,22,24 49:5,19,21 64:22,22 65:5 96:7	claims (27) 19:3,5 27:8 66:11 67:1 72:10 76:25 77:2 79:18 80:20 81:11,12,19 82:19,22 87:8 88:12 90:18,19,22 91:9,11,13,15,20 95:17	confronting (1) 64:19
administer (1) 22:23	announcing (1) 85:15	assurances (9) 28:7 48:8 50:21 56:1 57:25 83:5,14,22,23	beginning (4) 13:10,12 97:24 98:1	breakdown (1) 79:12	clarified (1) 35:19	confronting (1) 64:19
administration (16) 4:14,14 5:5 9:5,7 17:23 19:6 62:18 76:16,21 77:1,14 78:19 81:23 87:15 96:14	another (6) 8:4 28:12 48:17 59:2 70:3,15	assurance (4) 47:17 55:9,10,25	begins (1) 82:10	bring (3) 54:11,23 71:5	clarifications (1) 44:4	confronting (1) 64:19
administrator (3) 25:22 64:9 94:17	answer (28) 8:1 15:12 22:16 25:13 38:11 47:23 50:21 52:23 53:2,5 55:1,18 56:3 58:20 68:18 76:4 79:6 82:15 86:9 87:19 89:18 91:17,18 94:8,13 95:8 96:5 97:17	assure (1) 52:25	begs (1) 25:11	brings (1) 59:11	class (12) 66:18 68:10 70:14,15 72:19,21 73:16 76:2,3 80:24 81:1 91:4	confronting (1) 64:19
administrators (24) 1:19,20 6:1,12,17,25 12:17 49:24 51:21 62:22,23,23 63:10,14 67:7 74:23 77:12 81:11 83:3,8,21 94:19,20 96:12	answered (1) 8:9	astonishing (1) 55:12	behalf (5) 3:5,11 11:3 26:6,7 behaved (1) 89:22	brooke (3) 24:22 77:11 81:11	classes (1) 96:9	confronting (1) 64:19
advance (1) 82:21	answers (2) 66:20 97:1	attention (7) 9:8,13 11:18 13:18 77:7 82:9 83:1	behaviour (6) 86:23 90:17 91:6,9 92:7,17	brought (2) 27:25 87:9	clause (24) 2:4,21 4:10 10:23 12:21 14:16 25:2 30:18 31:22 32:20 33:3 34:10 35:18,20 36:8 37:1 43:2,12 44:3 46:22 47:20 53:8,20 66:13	confronting (1) 64:19
advanced (1) 71:22	anybody (1) 58:7	authorisation (17) 37:19,21 38:1,2,16,19,20 39:10 40:16,21 41:13 42:6 47:10 48:6,9 54:16 83:19	being (12) 1:8 6:1,25 8:21 21:15 26:24 62:23 65:18 69:10 91:10 93:23 94:16	bullet (1) 51:14	clear (14) 3:9 7:8,10 14:23 16:5 17:11 39:24 44:5 47:22 53:14 54:8 74:25 82:15 83:5	confronting (1) 64:19
advancing (1) 66:8	anyone (3) 47:13 58:22 74:18	authorisations (1) 41:25	begin (2) 41:16 55:25	bunch (1) 89:3	clear (14) 3:9 7:8,10 14:23 16:5 17:11 39:24 44:5 47:22 53:14 54:8 74:25 82:15 83:5	confronting (1) 64:19
advantages (2) 70:13,14	anything (10) 1:15 5:3 11:16 30:22 31:1,5 50:5 65:7 96:19,24	authorities (5) 7:4 61:1 68:22 70:7 72:15 73:12 75:10 79:3 89:12,12 93:8 96:9	beginning (4) 13:10,12 97:24 98:1	bundle (29) 1:25 7:4 13:8 14:4,14 15:24 22:17 23:21 24:6,8,13 25:13 28:10,11 29:20,24 32:25 34:4,15 36:17 39:7 41:15 50:13 55:16 56:7 61:1 68:20,22 70:8	clear (14) 3:9 7:8,10 14:23 16:5 17:11 39:24 44:5 47:22 53:14 54:8 74:25 82:15 83:5	confronting (1) 64:19
adversarial (1) 83:10	anyway (2) 49:16 65:4	authority (21) 37:14 40:6,8,18 42:6 46:19 47:14 49:22 50:18,21 51:25 52:25 53:6 56:2 57:23 70:4 73:12 83:6,14,19 84:23	begins (1) 82:10	burst (1) 85:9	clear (14) 3:9 7:8,10 14:23 16:5 17:11 39:24 44:5 47:22 53:14 54:8 74:25 82:15 83:5	confronting (1) 64:19
adverse (1) 86:13	anywhere (3) 7:14 47:11 57:22	authorities (5) 7:4 61:1 68:22 70:7 72:15 73:12 75:10 79:3 89:12,12 93:8 96:9	begs (1) 25:11	bracket (1) 85:9	clear (14) 3:9 7:8,10 14:23 16:5 17:11 39:24 44:5 47:22 53:14 54:8 74:25 82:15 83:5	confronting (1) 64:19
adversely (1) 67:16	apart (4) 5:3 33:4 91:2 94:13	available (11) 11:10,10 22:10 29:5 30:6,6,20 32:6 97:10,22 98:4	behalf (5) 3:5,11 11:3 26:6,7 behaved (1) 89:22	brackets (1) 3:2	clear (14) 3:9 7:8,10 14:23 16:5 17:11 39:24 44:5 47:22 53:14 54:8 74:25 82:15 83:5	confronting (1) 64:19
advertisements (3) 39:14,20,23	appeal (5) 70:6,20,22,22,23		behaviour (6) 86:23 90:17 91:6,9 92:7,17	bracket (1) 85:9	clear (14) 3:9 7:8,10 14:23 16:5 17:11 39	

consequences (2) 82:7 86:13
 consider (6) 25:22 39:22
 40:12 44:24 46:7 71:3
 considerable (1) 38:24
 consideration (6) 33:23
 42:12 62:11 72:6,7 80:3
 considerations (1) 71:6
 considered (1) 41:4
 considering (2) 40:21 42:5
 consistent (1) 34:23
 constituted (4) 3:1 22:24
 62:25 74:11
 constitutes (1) 67:3
 constitution (1) 86:11
 construction (2) 50:4 95:13
 contacting (1) 36:5
 contagion (1) 26:10
 conte (2) 98:11,13
 contemporaneous (1) 37:17
 context (7) 7:9 32:19 40:3
 41:13 68:9 82:23 95:22
 contingent (1) 4:1
 continuation (1) 56:13
 continue (1) 48:10
 continued (1) 25:8
 continuing (1) 83:24
 continuity (1) 30:25
 contract (8) 7:10,10 8:3,24
 67:11,14 95:13,15
 contractual (1) 16:20
 contradict (2) 33:10,10
 contradiction (1) 55:25
 contrary (4) 17:13 57:24
 87:3 95:1
 convenient (1) 65:4
 cooper (7) 41:17 43:21,22
 44:12 45:8,15,16
 coopers (2) 45:12 46:4
 copy (1) 37:5
 correct (11) 4:23 5:18 15:8
 30:18 50:10 63:17 75:20
 76:23 85:18 87:13 88:2
 corrected (1) 15:2
 correspond (1) 54:5
 correspondence (4) 9:23
 41:24 43:10 84:8
 cost (2) 44:21 76:15
 costs (13) 3:4,10,13,16 5:3
 10:10 21:1 30:9 44:20
 62:18 76:21 91:2 96:13
 couldn't (2) 66:10 67:2
 counsel (2) 97:7,8
 counterclaims (1) 90:21
 couple (2) 39:3 56:5
 course (20) 8:16 9:4 10:21
 19:8 27:12 33:12 38:25
 42:3 50:4,10 52:9 53:7
 54:14 55:14 56:5 87:15,22
 91:10,17 94:8
 courts (5) 60:1,3 67:18
 73:13 96:6
 cover (1) 37:6
 cr2019bhm000443 (1) 1:5
 create (2) 25:7 27:11
 created (2) 27:12 85:19
 creditor (4) 19:16 23:10,11
 76:13
 creditors (43)
 4:16,19,21,24,25 5:8,13
 8:17 9:6,7 19:9,14,18
 20:7,13 62:4 75:11,13
 76:1,14,15 77:5,6 79:11,20
 80:16 81:21 82:1 87:10,12
 88:4,5 89:4 90:4,6,9,14,16
 91:4 92:13 94:10 95:20
 96:10
 criminal (1) 1:11
 critical (1) 52:9
 criticise (1) 83:7
 criticised (1) 72:9
 criticisms (1) 78:1
 crossclaims (1) 90:21
 crossexamined (1) 34:22
 crowdfunding (1) 85:25
 crucial (1) 45:4
 crystallised (1) 59:21

currency (1) 28:15
 current (2) 72:11 78:21
 currently (1) 57:7
 customer (1) 15:14
 cut (4) 15:6,12 55:1 63:21

D

d (5) 61:11 68:13,16 69:13
 71:19
 dalton (1) 72:17
 damage (1) 28:24
 date (17) 12:4 13:14 15:25
 16:5 38:17,18 47:10 51:1,3
 53:14 56:3,16,23 57:4
 62:19 79:16 85:9
 dated (5) 10:5 40:18 41:19
 42:14 43:22
 dates (9) 25:18 28:14 35:4
 37:22 39:8 40:15 50:16
 61:2 97:15
 dating (4) 34:24 51:24 74:4
 85:8
 day (1) 1:13
 days (2) 53:17 74:17
 deadline (1) 85:6
 deal (6) 1:14 9:13 13:17 17:2
 26:8 65:7
 dealing (7) 10:3 17:1 36:19
 65:16 84:9 87:8 89:19
 dealings (1) 10:17
 deals (2) 93:11 96:15
 dealt (3) 17:3 94:6 96:16
 dear (1) 41:23
 debate (1) 40:3
 debenture (11) 1:23 2:3,4
 22:17,25 24:13 27:7 30:23
 31:2 63:1 65:22
 debentures (2) 2:1 67:3
 debt (3) 11:4 81:5 94:7
 debts (1) 81:13
 december (1) 85:8
 decide (6) 22:9 31:6,17
 59:16 63:16 69:14
 deciding (2) 5:15 74:13
 decision (23) 8:3 45:1 48:9
 59:25 60:10 61:1 62:24
 64:8 67:9 69:12,21,21
 70:6,24 71:18,23 72:9,17
 73:22 76:22 82:9 93:3,6
 decisionmaker (1) 60:5
 declared (1) 25:9
 declining (1) 85:7
 decreed (1) 73:15
 deed (3) 2:25 3:1,7
 default (14) 4:4 13:19,23
 27:23 28:5 51:11 74:9
 77:24 94:25
 95:5,8,11,12,14
 defined (3) 3:22 68:10 72:21
 definition (1) 23:5
 delay (2) 38:23,24
 delegate (1) 2:15
 deleted (1) 55:21
 denied (1) 19:14
 deny (3) 80:16 91:4 92:19
 dep'd (2) 9:23 66:20
 depending (1) 49:9
 depends (3) 76:4 87:6 95:7
 described (2) 26:22,23
 describes (1) 47:7
 despite (3) 16:13 56:11
 77:23
 detail (5) 10:7 37:17 39:3
 41:1 60:24
 detailed (1) 25:21
 details (2) 97:12 98:2
 determine (3) 5:20,22 63:15
 determines (3) 3:21 4:12
 66:4
 determining (1) 93:9
 detriment (1) 44:9
 devious (1) 36:10
 dhabi (1) 8:20
 didnt (6) 11:13 16:16 32:18
 47:18 76:11 78:12

difference (11) 30:1 38:5
 63:8,13 64:5 87:4 88:24,25
 89:7 90:1 95:22
 differences (2) 29:22 38:29
 different (8) 4:15,16 17:4
 27:4 64:1,19 73:18 92:12
 differently (2) 17:3 63:3
 difficult (5) 37:10 41:11
 72:22 86:4 97:16
 difficulty (2) 72:20 74:13
 dip (3) 34:25 39:11 41:1
 direct (2) 63:5 83:1
 direction (3) 63:23 85:7 94:5
 directions (3) 6:13 74:23
 83:9
 directly (1) 11:6
 director (3) 79:16 81:8 90:15
 directors (1) 87:7
 disadvantaged (2) 93:17,22
 disappointed (1) 70:16
 disburse (1) 68:10
 discharge (2) 22:3,6
 discharged (1) 66:12
 discrepancy (3) 14:16
 53:18,19
 discretion (68) 4:12
 5:10,11,12,24
 6:2,3,6,10,13,14,16,18,20,24
 8:21 9:1 10:20 16:25
 17:16,18 20:1,4,7,20
 27:10,12,14 30:16
 31:5,7,13 33:7,13
 60:6,9,16,18 61:6
 63:6,12,18,20,24 64:2 66:6
 67:15,19 68:1 70:2 71:15
 74:2,22,24 75:4 79:25
 82:21 88:22 89:1,8,23,24
 91:3 92:4 93:14,25 96:4,8
 98:2,8 33:20
 59:22 61:25 68:9 72:4,13
 82:24
 discriminate (1) 69:5
 discussed (1) 60:22
 discussion (2) 12:10 65:19
 disintitle (1) 92:24
 disintitiled (1) 66:9
 disingenuous (1) 86:1
 dismissal (1) 79:18
 dispensed (1) 77:16
 disposal (1) 44:6
 dispute (1) 90:18
 disputes (1) 90:21
 disseminate (1) 97:9
 disseminated (2) 50:9 83:16
 distinction (5) 63:7,13
 64:4,5,10
 distressed (3) 35:21 44:6
 78:4
 distribute (7) 12:18 21:9,14
 68:14 69:12 72:18 73:1
 distributed (4) 5:17 13:3
 18:4 62:25
 distributing (2) 93:5 97:6
 distribution (7) 66:22 67:1
 69:19,23 74:14 81:20 83:2
 divide (1) 17:23
 dividend (2) 77:15 81:20
 division (4) 73:6,7,8,14
 document (25) 1:24 2:20
 4:6,7 10:5 14:7,18 15:8
 26:16 28:12 31:21 35:2
 36:19 38:23 45:6 49:23
 50:12,14,15 51:18,21
 53:4,13 56:3 85:8
 documentations (1) 43:14
 documented (1) 43:14
 documents (16) 2:10,17 9:9
 10:4 11:23 12:1 13:16
 17:4,5 23:4,5,6 30:10,14
 37:17 94:13
 does (25) 5:19,22 9:13,16
 12:7,9 13:15 18:2,9 22:6
 27:13 28:22 30:22 32:12
 33:9 37:5 44:19 56:3 68:16
 75:14 78:7 87:4 88:24
 92:15 95:12

doesn't (10) 6:7,22 10:19
 15:3 18:1 30:22 34:16
 45:11 47:22 68:5
 doing (2) 13:13 80:12
 doling (1) 18:14
 donald (1) 61:2
 donalds (1) 61:21
 done (3) 36:10 58:25 60:3
 dont (31) 2:15 5:16 8:11
 9:17 10:6 11:5 13:19 15:25
 16:4 23:22 36:2,23 37:8
 39:2 56:16 57:12
 58:24,24,25 61:2 64:14
 78:20,22 79:9,12,21
 89:5,21 91:16,21 98:16
 door (1) 58:6
 doubt (5) 10:14 19:20 86:25
 87:1 88:18
 down (11) 24:9 27:19 42:16
 46:8 50:25 73:4 77:19
 83:13 87:25 92:15 96:23
 doyle (1) 75:21
 draft (6) 97:3,6,21
 98:4,12,21
 draw (4) 9:8,12 13:18 40:4
 drawing (1) 11:18
 drew (1) 82:9
 due (4) 3:7 30:11 34:21 42:2
 dues (1) 36:12
 during (2) 28:15 38:25
 duties (2) 61:22 62:4
 duty (10) 9:5 62:5 67:10
 68:7,25 71:25 72:2,25
 91:20 95:18

E

e (7) 35:1 50:15 55:13
 68:13,16 69:13 71:19
 e1 (3) 24:8 39:5,7
 e161 (1) 40:5
 e2 (9) 14:4,14 28:11
 29:20 25 35:1 39:5 41:15
 50:13
 e267 (1) 41:2
 e3 (4) 15:24 25:13 28:10
 55:13
 e415 (2) 28:16,17
 e475 (1) 45:5
 e481 (2) 43:20,23
 e484 (1) 35:5
 e487 (1) 52:3
 e489 (1) 52:10
 e493 (1) 50:22
 e499 (1) 53:13
 e528 (1) 54:21
 e530 (1) 54:24
 e966 (2) 55:16,19
 earlier (5) 22:12 29:22 62:14
 82:3 92:16
 early (2) 13:13 48:23
 easier (1) 85:25
 easy (1) 38:4
 edge (4) 70:7 73:21 82:9
 93:4
 effect (9) 19:9,21 20:20 28:2
 31:11 37:7 47:25 50:20
 67:19
 effective (1) 14:7
 effectively (9) 13:1 46:25
 60:4 63:11 64:6 74:8 83:3
 86:22 92:21
 eight (1) 46:8
 either (8) 33:8 48:22 59:25
 77:9 82:21 83:4 88:9 97:10
 elderly (1) 80:7
 element (1) 91:22
 eligible (1) 81:12
 else (6) 5:3 19:7 47:13 79:12
 96:19 98:22
 email (35) 12:1,25,25 13:14
 15:10 24:7 34:23 35:7 37:6
 41:17 42:9 43:20,21
 45:9,12,12 46:4,10,15 47:2
 48:8 49:22 50:3,4,8 54:7,8
 56:20 58:4,5 75:20,22
 97:18 98:2,15

emailed (2) 14:24 45:8
 emails (4) 51:25 54:18 56:23
 98:9
 emphasis (1) 75:8
 emphasised (2) 26:12 30:19
 emphatically (1) 82:2
 employees (2) 24:24 72:11
 employers (1) 72:11
 empty (1) 50:11
 enable (1) 44:20
 enabled (1) 70:12
 encourage (1) 52:6
 end (9) 17:6 27:21 28:4
 49:1,3 56:23 88:16 97:25
 98:22
 ended (1) 86:21
 enforce (3) 11:4,4,6
 enforceable (1) 3:2
 enforcement (3) 3:13 16:8
 55:23
 enforcing (1) 3:15
 enhanced (2) 77:15 79:5
 enquiry (1) 55:5
 ensure (5) 10:9 18:16
 20:18,21 44:4
 entail (1) 22:6
 entails (1) 22:7
 entered (1) 23:7
 entire (2) 91:4,22
 entirety (4) 18:14 48:25
 64:20 95:2
 entirety (1) 35:25
 entitle (3) 91:20,21 92:23
 entitled (5) 18:18,25 32:5
 88:20 93:5
 entitlement (1) 32:16
 entitlements (2) 2:10 23:4
 entitles (1) 93:2
 entity (3) 18:7 26:8 83:25
 entrusted (1) 72:3
 equal (4) 73:6,7,8,14
 equality (3) 72:25 73:16 74:8
 equally (2) 7:20 68:16
 equitable (1) 71:17
 equity (5) 68:4 72:16
 73:1,17 74:8
 error (1) 15:8
 errs (1) 74:7
 escalate (1) 15:15
 escape (1) 77:7
 escaped (1) 82:25
 essence (2) 4:13 69:19
 establish (1) 44:21
 established (1) 65:17
 estate (15) 4:19,21,21
 19:15,19 62:13 76:20 86:5
 87:21 88:1,5 90:3 91:1
 92:19,24
 estimated (3) 62:16 75:14,23
 etc (4) 3:6 21:8 91:21 98:20
 even (17) 15:6 18:25 20:4
 25:6 30:17 33:13 69:3
 77:24 81:10 84:18,18
 88:19 94:1,2 96:4 98:8,14
 93:4
 evenhanded (1) 70:19
 evening (3) 75:16,18,19
 evenly (3) 89:15,16,18
 event (16) 11:9 25:23 28:8
 29:16 30:5 31:6 35:21 44:5
 54:2 66:16 68:7 76:6 80:19
 88:11 90:24 98:10
 eventually (1) 38:21
 ever (4) 28:19 46:12 73:8
 74:19
 every (4) 1:13 29:5 34:17
 85:12
 everybody (1) 18:17
 everything (2) 18:17 92:25
 evidence (18) 13:2 23:17
 24:5,21,23 27:21 32:23
 34:3,18 36:16 37:1 46:24
 47:22 52:22 59:5 74:17
 80:15 83:17
 evidently (1) 78:18
 exact (1) 87:16
 exactly (5) 16:4 33:16 50:17

78:24,24
 example (4) 71:10 90:19
 93:4 94:15
 examples (1) 73:17
 except (2) 11:6 69:3
 exception (1) 54:14
 exchange (7) 33:25 41:14
 47:11 49:22 51:25 52:24
 53:11
 exchanges (5) 43:17 50:18
 56:20 57:16,19
 exclude (1) 75:4
 excluded (1) 81:14
 excluding (1) 72:7
 execute (1) 73:25
 execution (2) 73:11,18
 excisable (1) 60:21
 exercise (33) 6:2,13,16,17
 8:4 10:20 17:15,18 19:25
 20:3,6,19 22:9 33:12,20
 59:22,23 63:20,24 65:17
 72:4,13,24 74:22,24 75:4
 82:24 88:22 89:1,24 91:3
 93:25 96:8
 exercised (20) 4:13 6:3,10,25
 7:1 8:21,22,25 9:2 16:25
 60:5 63:18 67:20,21 69:18
 70:13 80:1 89:8 93:14 96:4
 exercises (1) 72:4
 exercising (8) 5:10,11,12
 6:20 60:15 67:25 89:23
 92:4
 exhibit (2) 25:16 35:3
 exhibited (2) 28:12 50:15
 existed (1) 43:12
 existence (1) 57:19
 existing (1) 85:16
 expect (2) 28:7 51:9
 expected (3) 28:22 60:13
 64:17
 expense (3) 70:15 77:1 88:5
 expenses (5) 3:4,10 30:9
 44:20 62:19
 explain (4) 14:15 43:11
 53:19 85:20
 explained (3) 46:23 86:10
 88:11
 explaining (1) 13:11
 explanation (2) 44:17 63:19
 expression (1) 67:25
 expressed (2) 22:15 84:11
 expressly (1) 16:16
 extended (2) 38:16 41:12
 extension (1) 52:13
 extensively (1) 39:11
 extent (2) 18:20 77:1
 extract (5) 45:24 46:3 60:11
 68:20,24
 extracts (2) 41:21 47:1
 extraneous (1) 9:23
 extremely (1) 57:14
 eye (1) 46:8

F

f (2) 61:14 71:2
 f1598 (1) 68:24
 f176 (1) 73:2
 faced (2) 29:4 59:22
 facie (1) 72:25
 factor (6) 84:6 94:1,2,4,4
 95:24
 factors (2) 89:10 91:12
 factual (2) 23:15 70:9
 factually (1) 21:12
 fair (8) 10:17 18:3,5 20:10
 38:12 39:23 57:14 74:13
 fairly (1) 9:6
 fairness (1) 18:1
 faith (4) 7:1 8:22 9:3 67:10
 familiarise (1) 35:23
 family (2) 73:15 74:4
 fanfare (1) 58:4
 far (11) 12:23 13:4 20:22
 24:23 29:18 37:1 67:6
 78:9,13 83:17 85:21

favour (7) 22:24 23:10,11
 33:13 62:7 89:2 93:15
 favoured (1) 94:25
 fca (43) 10:2,4,8,15,18
 12:1,25,25 13:14 16:10
 17:14 33:11,15,16 34:1
 37:20 38:20,24 40:21
 41:4,18 42:14 46:12
 47:10,15,17,19 48:3,5
 54:16 55:11 77:18
 78:1,7,12 84:7,11 85:11,18
 86:24 91:24,25 95:15
 feacs (3) 44:12 85:2,7
 feature (1) 35:16
 features (1) 36:4
 february (5) 23:18 28:14
 34:24 37:20 38:1
 fee (2) 11:19 30:11
 feedback (1) 85:22
 feel (1) 87:2
 feeling (1) 49:9
 fees (5) 21:8 30:9 44:20
 52:20 62:13
 few (4) 11:13 35:5 39:11
 62:17
 fiduciary (1) 72:18
 fifth (1) 84:4
 figure (4) 77:8,17 78:4,5
 figures (1) 62:17
 file (3) 24:13 39:5 56:8
 final (3) 29:11 33:5 86:15
 finally (1) 47:9
 finance (11) 2:10,17 4:6,7
 23:4,5,6 30:10,14 79:16
 81:8
 financial (11) 37:13 39:16
 41:3 47:13 50:18 52:25
 56:2 57:23 78:15 83:6
 90:15
 find (7) 29:21 39:7 50:14
 73:12 74:4 81:18 86:3
 finds (4) 25:12 28:10 45:5
 68:21
 fine (5) 1:17 11:17 33:9 79:1
 90:23
 finish (1) 49:11
 finished (1) 46:4 65:16
 finishes (1) 45:21
 finishing (1) 34:12
 firm (3) 42:25 43:1,7
 firms (1) 29:12
 first (55) 2:12 3:4,9,10,17
 5:19 6:24 7:17,21 9:22
 13:18,19 21:25 26:12 30:8
 32:1 36:7 37:2,13 39:7,12
 42:21 43:25 44:7 46:19
 51:6 52:3,22 53:13,15
 54:18,21 55:3,19 56:19,22
 57:22 58:3,18 62:2 66:5,3
 68:20 70:20,24 76:18 80:3
 83:15,15 84:22 85:1 89:21
 91:23 93:15 95:7
 firstly (1) 57:9
 five (3) 54:22 80:2 81:2
 fix (1) 12:7
 fixed (1) 15:13
 flag (1) 32:9
 flagged (1) 46:12
 flags (1) 37:3
 flat (1) 55:25
 flavour (2) 39:4,12
 flavoured (1) 55:8
 follow (2) 43:17 72:25
 following (7) 3:3 39:14 43:4
 52:14 54:17 65:25 85:22
 follows (1) 30:8
 foot (1) 36:18
 force (1) 16:20
 forced (1) 84:13
 forgive (1) 28:1
 formal (3) 42:1 44:6 50:11
 formally (1) 50:10
 former (3) 79:16 81:8 90:15
 formulate (1) 45:2
 forth (1) 96:25
 fortnight (1) 51:24

forwarded (1) 52:13
 found (1) 51:21
 foundation (1) 47:8
 founders (1) 24:22
 four (6) 47:10 48:7 69:15
 73:4 74:17 98:18
 fourmonth (1) 47:12
 fourth (4) 30:13 51:14 82:25
 94:17
 framework (1) 38:10
 frank (1) 85:21
 fraud (2) 77:12 81:11
 free (1) 75:1
 freely (2) 46:15 82:1
 freeze (1) 11:11
 frequently (1) 68:8
 friends (3) 31:24 32:9 62:15
 froze (1) 11:12
 fulfilled (2) 67:2 78:19
 full (22) 10:9 18:22 22:6
 29:6 37:21,25
 38:2,5,6,13,15,19,20 39:9
 40:16 41:12 48:6 66:12
 84:9 92:20 93:21 94:12
 function (1) 60:3
 fund (6) 22:3 61:10 68:10
 72:8,18 80:17
 fundamental (3) 47:15 48:8
 83:18
 funding (1) 81:14
 funds (3) 22:6 52:13 75:2
 further (3) 15:10 54:18 70:22
 future (2) 3:23 87:9

going (35) 2:20 8:17 22:8
 23:13,14 27:5 33:18,21,25
 39:10 40:25 43:6 48:14,14
 49:8 53:10 55:18 56:18
 59:12,13 60:23 63:2
 64:21,21,25 65:3 70:10
 76:18 79:7,23,24 93:20
 94:12 96:24 97:23
 gone (1) 77:24
 good (14) 7:1 8:22 9:3 29:18
 43:24 47:19 48:15
 65:13,13,14 67:10 69:23
 75:7 76:25
 gordon (3) 24:23 77:11 81:12
 governed (2) 16:13 27:19
 governing (2) 13:1 18:6
 grand (1) 90:24
 grant (2) 23:23 48:9
 granted (1) 28:19
 grateful (2) 48:18 99:1
 great (2) 32:18 60:24
 ground (3) 5:21 15:21 70:3
 guidance (1) 39:21
 guys (1) 96:11

H

h (3) 61:14,21 71:9
 hadnt (2) 78:19 96:16
 hales (1) 67:9
 half (4) 23:19 38:22 48:13
 49:2
 hand (7) 7:16,17 69:3
 75:1,14,17 96:23
 handed (3) 89:15,16,18
 hang (1) 89:1
 happen (3) 54:17 63:14 96:3
 happened (6) 10:24 31:19
 37:11 45:8 54:13 77:20
 happening (1) 54:13
 happens (4) 15:23 60:10
 66:23 76:19
 happy (1) 64:3
 hard (1) 80:10
 hardearned (2) 28:20 29:18
 hardship (1) 80:15
 harm (1) 28:23
 hat (3) 1:20 62:6,8
 havent (5) 11:16 15:2 33:13
 38:9 71:16
 having (13) 5:14 8:5,23
 16:14 27:5 38:24 41:11
 60:13 64:17 74:16 78:22
 82:19 89:10
 head (2) 41:18 96:6
 headed (1) 35:2
 heading (6) 25:14,20 29:10
 34:7 35:7 41:3
 headnote (1) 70:11
 health (1) 29:13
 hear (3) 1:8 11:13 12:12
 heard (2) 12:20,23
 hearing (4) 1:8,10 34:15 99:3
 heart (1) 47:14
 held (7) 20:12 44:7 82:5
 86:5 87:16,18 88:3
 hell (1) 16:22
 help (3) 45:1 68:5 77:18
 helps (1) 63:21
 here (18) 12:14 13:11
 17:12,16 18:7 44:15 45:14
 51:17 54:12 61:4 68:1
 69:11 73:16 74:3,11 77:21
 87:16 93:7
 higher (1) 47:1
 highly (5) 25:23,25 26:13
 33:22 48:6
 hit (1) 80:10
 hmcts (1) 1:9
 hmrc (6) 19:15 76:25 88:7
 91:2 94:16 96:12
 hmv (1) 80:8
 hold (6) 2:6 22:22 69:3 73:5
 76:25 82:17
 holder (2) 61:24 62:12
 holding (8) 5:5 26:5 30:15
 33:7 81:9 87:12 90:14 96:5

holdings (2) 1:4 33:9
 holds (2) 26:5 27:14
 hole (12) 25:19 32:1 34:9
 39:18 45:6 51:6 54:1,25
 55:4 56:10 69:7 71:21
 honesty (3) 7:1 8:22 9:2
 honesty (1) 60:7
 honour (102) 1:13,17
 4:17,20,25 5:2,9 6:11,21
 7:7,18,25 8:15 9:19 10:12
 11:12,17 12:5,13,22 15:16
 16:19 17:9,20,25
 18:8,11,23 19:12,23
 20:8,16 21:5,13,18,21
 24:15 27:24 29:8,24
 31:4,9,20 33:1 34:14 36:25
 37:24 38:4,12 46:2 47:16
 48:2,12 49:1,5 50:25 51:4
 55:17 56:15 57:2,12 58:12
 59:18 61:19 63:2,25 64:23
 65:2,13,15 68:23 69:9
 75:17,23 76:6,12,18,21
 77:3 78:7,16,20 79:1,8
 80:19 86:17 88:23 90:5,23
 91:7 92:3,6,14 93:10
 94:1,3,22 95:9,16 96:18,21
 98:16
 hope (2) 12:20 96:23
 horses (1) 72:16
 hour (3) 48:13 49:2 98:23
 hours (1) 65:6
 house (1) 67:8
 however (5) 30:14 33:6
 42:10 85:15 88:21
 huge (1) 29:12
 hugely (1) 6:7

I

id (2) 32:24 63:7
 identified (2) 23:24 53:5
 identifying (1) 82:10
 ignore (3) 3:2,8 31:11
 ignores (1) 54:18
 iii (1) 34:7
 ill (10) 7:25 9:24 30:4
 33:1,23 39:11 41:21 46:1
 54:19 88:16
 illuminating (1) 63:19
 im (31) 1:13 7:13 9:24 12:8
 17:1,4 18:14 23:13 28:3
 31:18 33:25 38:9 39:10
 40:25 43:6 48:1 49:9 53:10
 55:18 59:13 60:23 64:19
 70:10 75:20 78:9 79:23
 93:13 96:24 97:23 98:8
 99:1
 immaterial (1) 62:11
 immediate (1) 34:2
 immediately (3) 48:1 77:8
 97:18
 immunise (3) 82:6,15 86:12
 impact (2) 67:16,17
 impartially (3) 69:1,2 72:1
 imply (1) 67:19
 importance (2) 29:14 31:18
 important (14) 21:14 32:23
 35:23 41:14 42:4 54:14
 60:17 66:6,14 67:4 69:6
 80:3 82:23 88:17
 impose (1) 78:17
 imposes (1) 72:3
 impossible (2) 61:22 62:2
 impression (2) 34:19 85:19
 inappropriateness (1) 84:24
 inaudible (6) 5:14 11:22,23
 12:3 77:3 92:6
 include (5) 2:18 3:13 88:6
 90:14,15
 included (1) 35:15
 includes (2) 87:13 88:9
 including (6) 4:3,7 39:16
 40:23 62:19 81:21
 incompetent (2) 15:7,14
 incomplete (1) 47:24
 inconsistent (4) 14:11 53:7
 56:1 57:10

incorporated (1) 24:18
 incorrect (2) 22:14 23:9
 incurred (2) 3:5,10
 index (1) 100:1
 indicating (1) 42:7
 indication (3) 57:3 96:22
 97:20
 individuals (2) 26:9 72:22
 infected (3) 94:20 95:20
 96:13
 inference (1) 53:3
 information (5) 44:18,19,24
 45:1 46:7
 inherent (1) 69:13
 initial (2) 42:12,18
 initially (1) 85:7
 inquiry (1) 15:18
 insiders (5) 79:20 81:6
 88:8,13 94:7
 insofar (2) 69:4 91:8
 insolvency (6) 19:8 20:11,12
 82:2,16 86:14
 insolvent (24) 12:16,17
 17:22 18:6,7,15,18 19:21
 20:5 22:2,7 61:8,23
 62:13 75:9 86:10 87:5 89:7
 90:2,3,25 92:24 95:23
 instance (2) 13:7 70:20
 instances (1) 76:10
 instead (3) 28:11 58:18
 85:20
 instructing (2) 62:15 87:18
 instructions (1) 98:19
 insufficient (1) 22:5
 integrating (1) 85:22
 intend (1) 97:10
 intended (2) 47:18 73:8
 intents (2) 19:8 44:18
 intercompany (1) 5:4
 interest (26) 4:3,4
 7:9,10,12,15,22 8:1,7,18
 10:10 11:19 21:1,8 29:6
 30:11 52:17,19 68:2 72:10
 94:25 95:5,8,11,12,14
 interesting (1) 58:14
 interestingly (1) 53:24
 interests (9) 8:4 22:23 28:20
 29:2,17 37:3,4 44:4 62:5
 interim (3) 37:19 38:1,5
 internal (2) 43:15 85:8
 interposition (1) 26:17
 intervention (2) 37:13 85:18
 into (20) 15:6 19:15 23:8
 25:12 27:23 28:5 35:1
 39:2,11 41:1 42:5 54:11,23
 68:19 77:24 81:22 84:2
 86:7 87:25 92:22
 introduce (1) 36:11
 introduced (5) 25:6 27:18
 42:25 43:1 82:4
 invest (1) 45:1
 invested (1) 25:21
 investment (5) 14:12 26:7
 35:22 44:9 45:3
 investments (1) 13:12
 investor (7) 25:2 35:2,20
 36:9 58:22 83:16 84:19
 investors (97) 3:11,25 4:18
 5:7,7,23 7:16,20 9:15,21
 10:2,9,15 13:5 14:9 17:7
 19:10,14,17,17,20
 20:19,22,24 21:16 24:7,20
 26:24 27:5,6 28:7,18
 29:1,5,15 32:13,21
 34:18,20 36:11,12,14,22
 37:3 40:9 43:16 44:4
 46:13,20 47:6 50:9 51:9,15
 52:1 53:16 58:10
 66:12,19,23 67:2 75:6
 76:2,3 77:21 78:6 80:4,20
 81:1,17 82:4,13 83:3
 86:7,13,25 87:1,2,24
 88:2,3,9,12,18 89:2,13,21
 91:14 92:1,20 93:15,16,20
 94:11,14 96:2,11,12
 invite (4) 7:6 13:9 34:11

45:24
 inviting (3) 83:1,3,4
 involved (3) 81:21 91:6,8
 involves (1) 3:14
 irrelevant (4) 31:13,16 33:4
 72:8
 isnt (7) 5:11 9:1 67:23 72:24
 74:5 94:4 95:2
 issued (2) 42:2 55:17
 issues (2) 66:21 87:2
 items (1) 13:2
 its (120) 1:24 2:6 4:19,21,23
 5:6,8,21,24 6:6,15,16,19
 7:4 8:4 9:1,25 10:20 11:23
 12:16 14:4 15:21,25
 16:3,10 17:25 18:5,5,13,15
 20:13 21:1 22:19,24
 23:10,11,18 24:11 25:4
 26:21 27:8 28:11,13,15,22
 30:17 32:1,15 34:16,17
 35:2,3 37:4 38:7,12,17
 40:25 41:12,17 42:12
 43:8,23 44:19 47:9 48:25
 49:2 52:25 53:7 54:8,16
 55:7,15 56:6 57:21 58:9
 59:8 60:3,5,8,25 63:7 64:4
 66:6,14 67:5,17 68:1 69:17
 74:2,14 75:11 77:20 78:14
 79:7 80:13 83:8 84:19
 85:16,19 86:23,25 87:7
 88:17,22 89:23,24 91:3
 92:4,7,12,19 93:25
 95:13,14,24 97:4,4,9,21
 98:4
 itself (14) 8:12 17:22 19:7
 21:7 25:9 40:7 47:6 60:20
 61:8 69:24 73:11 84:2 86:6
 87:10
 ive (3) 37:19 52:1 59:7

J

job (1) 29:1
 join (1) 12:8
 jointly (1) 4:2
 judge (102) 1:13,17
 4:17,20,25 5:2,9 6:11,21
 7:7,18,25 8:15 9:19 10:12
 11:12,17 12:5,13,22 15:16
 16:19 17:9,20,25
 18:8,11,23 19:12,23
 20:8,16 21:5,13,18,21
 24:15 27:24 29:8,24
 31:4,9,20 33:1 34:14 36:25
 37:24 38:4,12 46:2 47:16
 48:12 49:1,5 50:25 51:4
 55:17 56:15 57:2,12 58:12
 59:18 61:19 63:2,25 64:23
 65:2,13,15 68:23 69:9
 70:20 75:17,23
 76:6,12,18,21 77:3
 78:7,16,20 79:1,8 80:19
 86:17 88:23 90:5,23 91:7
 92:3,6,14 93:10 94:1,3,22
 95:9,16 96:18,21 98:16
 judgment (9) 70:25 71:1
 96:23,25 97:3,6,21 98:4,21
 july (5) 1:1 38:22 54:15
 79:17 83:19
 june (2) 40:18 42:15
 junior (1) 97:19
 juniors (3) 97:14,16 98:3
 jurisdiction (2) 5:20 60:16
 jurisprudence (1) 72:17

K

keep (3) 34:25 64:21,21
 kept (1) 25:21
 key (6) 30:1 32:20 35:5 47:8
 60:25 71:8
 kick (1) 61:7
 kieran (1) 81:7
 kitty (1) 76:24
 knock (2) 48:24 76:14
 know (27) 1:22 10:21 13:4
 14:13,14 16:4,21 18:15

21:2 31:9 37:21 47:9,24
 49:7,13 56:16
 58:12,24,24,25 78:14
 79:9,21 91:9 97:12,15 98:3
 knows (13) 10:22 14:10
 23:17 27:3,17 29:19 33:18
 37:18 48:16 59:6 75:3
 89:9,25

L

lacks (1) 41:5
 lady (1) 67:9
 large (5) 3:16 9:1 40:22
 72:19 87:20
 largest (3) 76:1,3 91:1
 last (7) 29:10 34:19 42:16
 45:13 59:8 73:8 79:17
 late (5) 12:3 16:3 48:18
 49:15 57:1
 later (7) 24:5 33:23 48:7
 52:2 53:17 54:12 61:12
 latest (1) 42:18
 latter (1) 79:7
 launched (1) 23:18
 leading (1) 70:25
 leads (1) 44:21
 lean (1) 62:8
 learned (24) 9:24 12:1 17:2
 22:1,12 31:24 32:8,18
 53:12 62:15 75:8 86:21
 87:3,22 88:14 89:19
 91:12,14 92:21 93:2,13
 95:10 96:1,16
 least (6) 8:6,6 34:23 62:1
 93:16 97:24
 leave (2) 12:8 36:23
 leaving (1) 76:2
 left (1) 45:20
 legal (13) 2:1 6:3,19 15:8,18
 27:15 31:16 44:7,9 55:5
 56:11 59:14 74:18
 legals (1) 15:14
 lend (2) 26:3 73:11
 lendee (1) 96:8
 lender (9) 11:3,23 16:9 24:3
 28:6 41:8 45:2 55:24 85:16
 lenders (28) 2:14 9:10 11:5
 19:5 22:4 23:25 25:8
 26:7,19 32:5,10 33:14 34:3
 42:11,22 43:8 44:16,20,24
 58:1,4 59:11 63:16 75:3
 82:2,16 83:6,14
 lending (3) 24:1,2 40:9
 lendy (181) 1:3 2:15 3:11,25
 4:21,23 5:6,23 7:16,19
 8:6,8,17 9:10,15
 10:1,7,11,14 11:2,6,22
 14:9,18 16:10,14 17:11
 19:6,7,8,19,21
 20:5,5,15,25 21:2
 22:4,14,14 23:17,23
 24:1,1,6,9 25:4,7,23,25
 26:4,13 27:4 28:6,8 30:14
 31:11,14 32:10
 33:6,10,11,20 34:17,20
 36:8,10 37:3,20
 38:15,17,19 39:9 40:7
 41:3,4,10,14,19,24 42:7,10
 44:18 47:5,6,9,13,14,18,24
 48:1,10,10 49:22 50:20
 51:10 52:6,7,12,19,24
 54:9,15,18 55:8
 56:11,17,20 57:16,22
 59:8,10 62:23 66:9,13,24
 67:1 75:2,4,9,11 76:11
 77:16 78:18,18
 79:16,18,20 80:16 81:6,18
 84:12,21 83:2,5,13,23
 84:12,14 85:6,12,16,23
 86:5,6,9,11,14,23
 87:4,7,10,25 88:13
 89:4,7,13,22,24
 90:2,2,3,4,6,11,17 91:19
 92:11 94:7
 95:4,11,12,13,14,14,18,19,20,23
 96:14

lendys (44) 10:17 16:9
 19:2,6,9,14,15,19
 20:7,11,12,12 23:10 24:2
 26:19 29:16 31:5 32:16
 36:11 39:1 40:21,23 41:8
 43:14 45:21 53:5 55:23
 81:25 82:1,7,16 84:5,13,21
 85:1,3 87:15,21 88:5
 94:18,20 95:21,25 96:10
 less (3) 76:9 84:1 93:24
 let (1) 49:13
 lets (4) 31:11 49:5 51:20
 65:8
 letter (13) 39:7 40:17,19,25
 41:7,7 42:2,8 71:2 73:3
 84:22,22 85:1
 letters (4) 39:4 61:14
 71:9,19
 level (2) 39:2 60:24
 lewin (3) 60:11 68:21 69:25
 lgl (3) 77:10 81:9,13
 liabilities (10) 3:20,22,24
 4:5,11,15 5:4 22:3 66:3
 88:7
 liability (1) 5:17
 life (3) 73:16 93:19,22
 light (2) 42:10 86:2
 like (17) 17:7 18:16,23 19:22
 32:24 36:23 37:8 58:8
 78:14 79:3,5 80:4,7 86:3
 93:18,23 97:25
 likely (11) 44:21 45:2 49:13
 64:23 74:19 80:4,9,10,21
 81:17 97:4
 limb (1) 59:16
 limitation (1) 4:4
 limited (8) 1:4 18:12 60:3,4
 73:15 76:7 80:9 88:10
 limiteds (1) 26:13
 limits (1) 60:6
 line (5) 39:25 45:17 54:11,23
 77:7
 lines (7) 23:1 26:23 29:10
 42:16 46:8 70:1 73:4
 link (3) 51:18 58:17,21
 liquidation (1) 60:20
 liquidator (5) 61:11,21,24
 62:3,6
 listened (1) 74:17
 litigation (1) 71:24
 little (6) 23:14 37:16 48:18
 49:4 53:24 62:20
 loan (30) 2:19 4:7 11:10,19
 13:23 21:7,7 23:6 25:21
 26:2,11 29:13
 30:6,8,12,21,21 31:2
 32:14,15 36:5 43:14 57:7
 59:8 66:19 75:6 77:22,23
 78:21 87:23
 loans (16) 13:5,19 14:12
 21:4 24:10 25:8 27:1,22
 28:4 56:18 66:17 77:13
 78:3,3 87:14,16
 locked (1) 46:25
 lomas (1) 61:1
 long (3) 29:13 40:25 49:13
 longer (2) 19:21 64:23
 look (15) 2:3 11:1,25 13:8
 14:3 17:11 20:17 31:25
 39:25 43:22 45:13 51:22
 85:12 90:6,13
 looked (1) 78:9
 looking (12) 2:23 10:25
 12:20 17:21 41:7 50:19
 57:5 61:11 84:20 90:25
 93:13 98:5
 looks (6) 14:4 36:15 56:25
 59:4,9 82:12
 lords (1) 67:9
 lordship (115) 1:22 6:7 7:6
 10:22 11:2 12:19 13:3,10
 14:3,4,10 19:16 22:15
 23:17 25:1,6 27:3,8,1

45:5,7,11 46:24 47:3,3,7
 48:4,7,16,19,21 49:21
 50:13,19 53:9,14,23 55:15
 56:4,6,19 57:17 58:3,7
 59:6,13,16 60:23,25 61:23
 62:14 63:15,23 64:6,12,20
 65:18 66:8,14,21
 67:8,12,24,24 68:5 72:14
 73:20 74:10,16 75:3,10,14
 76:5,8,16 77:17,19 79:24
 80:14 81:3,10,16,24
 82:3,8,12 83:20
 84:4,10,15,23 85:14 86:2,9
 89:9,25 92:16 94:14 98:12
 99:1
lordships (6) 26:21 37:22
 52:23 68:20 77:7 83:1
lose (1) 93:22
losing (1) 45:3
loss (1) 93:24
losses (3) 29:3 80:6,11
lost (1) 93:18
ltd (3) 1:3 26:4,5
ltds (4) 25:23,25 41:25 85:13
lunch (5) 48:23 49:12,15,15
 65:6

M

m1 (2) 76:14 81:1
m2 (1) 33:14
main (12) 20:17,18,21 21:8
 29:22 35:19 71:11,14
 82:10 89:11,20 93:8
majority (1) 88:2
makes (6) 16:5 36:21 58:15
 88:23 90:9 95:22
making (13) 8:3 12:24 28:3
 33:2 35:13 44:25 48:4
 53:11 59:15 67:5 69:25
 92:9 95:3
manage (1) 26:7
manner (3) 3:20 4:11 66:3
many (4) 78:1 80:4,7 86:2
march (20) 10:5 12:3,25
 14:8 23:23 27:20 28:2
 29:19 32:21 35:4,12 37:22
 38:3,18,19 41:9,19 42:12
 43:5,9,13,23 44:13,15
 51:24 55:11 56:2 57:25
 83:6
market (2) 77:22 96:2
markup (1) 45:9
material (9) 25:19 44:24
 46:7 48:6 55:15 60:14
 61:13 64:18 84:9
materials (4) 40:24 68:19
 70:5 74:20
matter (9) 1:3 6:3,7,22
 11:21 31:16 48:25 68:3
 73:5
matters (3) 42:24 72:6,7
maxim (2) 72:25 73:16
maybe (2) 49:10 67:4
mcphail (1) 72:17
mean (4) 27:25 78:7 90:2,3
meaningless (1) 69:17
means (5) 23:6 80:9 84:9
 90:3 95:19
meantime (1) 15:20
meet (1) 39:23
melton (2) 80:5 93:18
member (1) 74:6
mention (4) 32:17 82:18,20
 85:17
mentioned (4) 25:15 40:2
 56:4 57:18
merely (2) 22:7 63:19
meritorious (1) 90:11
mess (2) 17:5 86:7
message (1) 53:16
method (1) 74:13
microscope (1) 92:7
middle (10) 31:25 40:11
 41:16 44:14 45:22 50:2,23
 51:5 60:12 71:20
midway (1) 56:10

might (19) 18:12 19:3,4
 20:10 29:4,9 33:11 48:20
 49:3,4 58:25 72:22 74:13
 76:10 80:25 88:17,19
 96:23 97:12
mildly (2) 17:5 86:23
million (13) 62:20 76:3,17,24
 77:3,6,8,18 78:4 79:13
 87:13,19 88:6
mind (6) 53:6,14 61:23
 71:10 81:10 88:18
mind ed (2) 42:1,7
minds (1) 38:8
minor (1) 44:8
minute (1) 89:1
minutes (5) 48:17 49:9,10
 65:1 98:23
misconduct (2) 84:6 96:1
misconducted (1) 71:17
misleading (8) 37:7 39:24
 40:13,24 84:14,20 85:4,19
mismatch (1) 14:20
misrepresentation (7) 19:6
 30:18 87:8 88:12 91:11,21
 95:19
misrepresentations (3) 19:11
 90:8 95:21
misselling (1) 84:12
missing (1) 12:6
mitigate (1) 26:15
mitigates (1) 26:10
model (113) 1:23 3:11,25
 4:18 5:7,23 7:16,20
 9:14,21 10:1,21 12:21
 14:11,23 15:22 17:7
 19:5,10,13,16,17,20
 20:19,21,24 21:4,6,16
 23:20 24:1,5,7,7,16,19
 25:2,6 26:18
 27:17,18,19,20,22,24,25
 28:4,15 29:16 30:2 34:7,19
 35:8 37:2,3,6,12 38:17
 41:21 46:22 50:9 53:8
 63:16 66:11,19,22,23 67:2
 75:2,6 76:2,3,15 77:21
 78:6,21 80:4,20,22 81:17
 82:2,4,15 83:2 86:7,12,13
 87:1,1,14,24
 88:1,3,9,12,18 89:2,12,21
 91:2,14 92:1,20
 93:15,16,20,20 94:11,14
 96:2,11,12
moderate (1) 66:18
moment (12) 25:16 28:10
 31:11 34:1,24 39:6 50:6,20
 55:19 62:18 89:22 92:6
moments (1) 11:13
monday (3) 75:16,18,19
money (8) 5:10 18:13 78:22
 87:20 88:19 89:4 91:16,18
monies (13) 2:24 3:23 4:5
 5:6,12,15 22:5,13 47:5,6
 65:24 77:16 86:5
month (2) 24:19 50:17
months (13) 15:9,13 39:9
 40:15,19 41:9 47:10 48:7
 54:9,12,22 55:2 85:12
more (22) 5:11 8:17,18
 11:16 19:13 23:13 37:16
 48:19 59:1 65:7 67:18 72:2
 84:5 88:6 89:3 90:10 93:23
 96:4,10,20 97:4,25
morning (2) 43:24 48:20
mornings (1) 48:14
mortgages (2) 2:1,2
most (5) 10:4 13:5 80:3 82:2
 94:8
move (1) 64:11
moved (1) 40:18
ms (77) 1:16,18,19 4:18,23
 5:1,3,18 6:19,22 7:15,19
 8:11,16 9:20 10:13
 11:12,15,18 12:5,12,14,24
 15:17 16:24 17:1,19,21
 18:5,9,19,25 19:13
 20:9,23 21:6,17,19 22:19

49:7,8,13 52:10 53:23 54:7
 56:17 57:3 63:3,21 65:2,8
 75:21 86:17,19,20 89:9
 90:18,24 91:8 92:5,9,15
 93:11,23 94:2,4 95:7,10,17
 96:20 97:7 98:7,13,25
 100:3,5
much (13) 8:17,17 48:21
 50:17 61:3 64:23 76:9 79:9
 80:23 86:21 89:2 91:16
 98:25
multipartite (1) 67:14
must (6) 1:9 6:25 8:24
 69:2,2 71:10
mutuality (1) 81:15
myself (1) 56:9

N

name (6) 24:12 40:12
 84:13,14 85:4,20
naming (1) 21:2
naturally (1) 9:6
nature (3) 68:1 69:13 73:12
necessarily (1) 33:10
necessary (3) 25:11 49:6
 77:20
need (14) 1:14,24 2:2,15
 9:17 10:6 13:19 20:17
 23:22 38:10 43:19 61:3
 64:14 71:2
needs (1) 98:14
never (2) 28:18 58:10
nevertheless (1) 75:12
next (11) 35:14 36:1 42:24
 43:18 48:1 49:23 51:12
 55:12 61:17 76:13 85:12
nicholas (1) 61:12
nicholls (1) 61:2
nobody (2) 16:19,21
nominal (1) 31:8
nominee (3) 26:4,6,24
nomineeship (1) 27:13
none (3) 4:20 5:13 73:10
nonmaterial (1) 44:3
nonrecovery (1) 88:8
nor (4) 28:19 30:22 94:1,2
normally (2) 96:22 97:8
note (10) 24:12 25:25 26:22
 29:10 30:7 37:22 42:19
 44:18 56:19 78:11
noteworthy (1) 85:2
nothing (13) 2:1 13:20,24
 32:16 47:11 54:13 55:7
 67:11 69:16 89:15,17
 96:20 98:22
notice (2) 64:20 66:7
noticing (1) 30:17
notification (1) 46:16
notional (1) 79:2
nowhere (3) 7:8 33:2,3
number (4) 1:4 28:19 40:22
 59:7
numerous (1) 73:17
nutshell (1) 70:11

O

objects (5) 60:21 61:9,25
 68:13 72:19
obligation (1) 83:9
obligations (4) 3:23 4:5
 68:3,4
obtaining (3) 38:13,15 83:18
obvious (4) 34:15 66:15 67:4
 79:6
obviously (9) 5:11 12:3
 66:20 76:4 79:18 81:15
 88:24 97:13 98:19
occasion (3) 28:22 37:2
 46:17
oclock (3) 49:4,4 65:9
occonor (1) 81:7
october (5) 15:11 54:25
 56:24 57:18 98:1
odd (1) 79:13
oddiy (1) 14:10

offence (1) 1:11
office (2) 61:24 62:12
oh (3) 16:15 20:10 33:12
okay (17) 1:17 6:21 7:7 9:19
 11:17 17:9 20:8 21:18
 36:25 61:19 63:4 64:2
 76:12 79:1,10 91:7 94:3
ombudsman (4) 70:7,16
 71:22 72:1
once (6) 19:21 52:20 67:1
 71:14 97:9,21
onenth (1) 80:24
online (1) 23:18
open (2) 34:25 36:20
opening (1) 96:17
opens (1) 79:19
operated (1) 23:20
opinion (1) 42:22
opposite (5) 16:17 17:7
 44:10,11 47:21
opt (2) 36:3 37:9
order (28) 3:3,20 4:11
 13:21,25 18:16 27:10,15
 30:7,15,21 31:14 33:7
 43:11,19 44:2,17,23
 45:17,23 46:6 54:2 65:25
 66:3,7 76:1 78:18 85:24
ordered (1) 73:19
orders (1) 25:4
ordinary (2) 71:17 72:2
original (11) 25:3 27:19,22
 28:1,4,15 29:15,23 45:9,10
 60:15
originally (2) 32:8 82:13
others (4) 9:11 26:11 72:12
 73:23
otherwise (6) 48:20 49:11
 66:10 78:5 89:16,17
ought (1) 78:2
ourselves (1) 75:12
outcome (4) 62:16 69:22
 75:15 81:4
outcomes (1) 75:23
outline (1) 59:13
outlines (2) 51:8,13
outset (1) 82:17
outside (2) 87:19,21
over (24) 4:19 5:10,13 14:19
 28:16 31:22,23 34:8 36:21
 40:4 42:21 45:16 49:6
 53:25 56:14 62:20 70:2
 71:13 72:12 73:13,23 74:7
 85:12 96:6
overall (1) 82:23
overdue (2) 13:19,23
overheard (1) 1:8
overwhelming (1) 53:3
owed (9) 4:1,15 22:4,14 29:7
 36:13 47:6,6 81:5
owes (3) 5:16 62:3 68:3
owing (2) 52:14,20
own (13) 8:9 9:6 19:17 24:11
 26:19 27:8 28:24 34:16
 36:12 37:4 62:13 67:17
 92:12
owned (1) 8:9

P

p2p (2) 25:14 26:3
pages (1) 35:5
paid (20) 7:17 9:22 10:11
 13:21,25 14:9 20:19,22,25
 21:1 22:9 30:7,20 31:6,14
 78:8,13 92:20 94:12,16
paper (1) 47:23
par (1) 78:3
paradoxical (1) 73:7
paragraph (52) 7:3,5 8:20
 9:12,18 10:3,13,16 12:2
 13:9,10,13,17 24:17 25:17
 26:12,15,23 28:13 34:9,13
 35:3,14 36:1,19,24 37:14
 38:21 40:11 41:2 43:25
 44:1,13 45:13,22 46:9
 50:16 51:5,12 56:10,13
 58:9 59:8,20 60:12,17

64:13 68:25 71:20 81:8
 84:21 85:14
paragraphs (6) 7:6 23:21
 37:23 61:15 78:10,11
parameters (2) 65:17 67:22
parent (3) 8:9 77:10 79:13
pari (12) 4:16 9:8 17:23 18:2
 25:23 32:10 69:19,22 73:1
 81:18 82:21 83:2
part (7) 1:10 17:13 24:16
 34:2 41:25 83:24 85:10
participating (1) 66:9
participation (2) 75:5 80:17
participations (1) 32:15
particular (7) 2:22 21:15
 59:24 67:21 80:15 84:10
 93:18
particularly (3) 23:16 40:6
 85:2
parties (3) 1:6 22:4 67:15
party (1) 21:2
parts (2) 36:5 68:7
parttime (1) 80:8
party (3) 8:2 67:16 94:24
pass (1) 76:11
passage (4) 25:19 52:9 55:15
 60:25
passages (2) 39:12 61:13
passing (2) 30:17 32:17
passu (12) 4:16 9:8 17:24
 18:3 25:23 32:10 69:19,22
 73:1 81:18 82:22 83:2
paste (3) 15:6,12 55:1
patience (1) 15:20
paul (2) 41:18,18
pause (1) 12:11
pausing (1) 52:23
pay (12) 2:8 4:10,16
 7:19,21,24 82:21 89:12,21
 91:22 93:8,9
payable (3) 10:10 77:16 78:5
payment (13) 3:19 11:4
 18:21 27:10 30:9,10,12,13
 44:2 52:12 66:2 79:5 91:4
payments (11) 10:8 14:5,17
 16:6,7 45:19 51:15 52:11
 54:2 55:20,22
peertopeer (3) 24:3 25:7
 40:9
penalise (2) 20:7,15
penny (1) 66:12
pension (5) 61:5,9 70:12,15
 72:8
pensioners (1) 72:11
pensions (2) 70:7 71:22
penultimate (1) 39:25
people (9) 4:15 31:8 68:14
 78:20 88:8 91:6 93:18,23
 96:13
per (3) 46:10,15 54:3
perhaps (7) 18:2,2,11 40:4
 48:10 84:15 95:2
period (8) 23:19 27:17,22
 28:4 39:1 41:12 47:12
 54:15
periods (1) 97:11
perkins (1) 98:13
permit (1) 48:10
person (3) 67:25 72:3 98:3
personal (2) 1:9 91:15
persons (1) 80:10
pertinent (1) 16:24
pick (4) 23:1 34:5 41:15
 79:14
picked (4) 14:13 16:14
 53:9,17
place (7) 27:7 32:18 44:23
 46:6 51:10 74:1 98:19
placed (3) 31:24 72:1 74:18
places (2) 16:22 75:8
plain (1) 6:12
plainly (3) 33:22 47:15 48:5
platform (4) 23:18 26:3
 85:23,25
please (9) 6:1 43:4,9,11,20
 49:16 59:20 65:9 69:8

pm (5) 49:18,20 65:10,12
 99:2
points (18) 1:14 17:1 20:16
 21:25 33:2 36:7 46:1,18
 57:20 68:6 72:19 80:2,25
 86:20 88:16 93:12 94:5
 96:15
policies (1) 43:15
policy (37) 13:19,23 14:1
 15:24 16:13 50:24
 51:7,8,13,17,23,23
 52:4,5,22 53:15,21
 54:3,6,12,23 55:14
 56:22,25 57:11,15,19,21
 58:3,6,19,20,23 59:2,4,10
 83:16
poor (2) 11:11 86:23
portion (2) 52:19 86:4
portions (1) 77:22
position (13) 8:16 13:7
 16:23 17:6 19:24 20:11
 26:22 30:19 33:14 62:2
 64:7 74:5 83:8
possibility (2) 60:2 79:19
possible (8) 1:7 20:22 47:4
 62:21 76:10 91:5 97:2,4
possibly (5) 62:8,24 66:15
 83:12 86:25
postaugust (1) 16:3
postdated (1) 13:5
postdates (2) 59:6,10
postinsolvency (1) 20:6
pot (2) 22:10 87:20
potential (2) 29:3 86:14
potentially (5) 8:8 17:10
 28:23 61:25 88:11
powell (20) 13:11
 14:13,15,24 28:13 35:3
 36:15 51:2 53:9,17
 54:10,12,19,25 55:9
 56:1,20 57:16 58:15 80:7
powells (10) 13:7 16:14
 25:16 32:24 34:4,18,25
 46:24 50:15 58:9
power (20) 22:9 59:23 60:21
 61:25 62:9,25 68:10
 69:11,14,19,20,24
 70:14,18 72:4,5,13,18,24
 73:25
powers (1) 73:13
practical (3) 44:8 64:10
 98:12
practically (1) 37:10
practice (1) 47:18
precipitated (1) 24:4
predated (1) 57:16
predates (1) 41:8
prefer (4) 8:8 70:2 72:10
 74:6
preference (9) 43:12
 44:3,17,23 45:17,23 46:6
 72:12 88:4
preferred (1) 73:22
preferring (1) 33:14
preinsolvency (1) 20:5
preliminary (1) 1:14
prelitigation (1) 81:14
prepare (1) 23:24
preparing (1) 42:1
present (2) 3:23 73:6
presented (1) 26:19
pressure (1) 85:10
pretty (4) 38:16 50:11,17
 55:7
previous (7) 15:12 41:24
 43:23 46:10,15 55:1 85:19
previously (3) 42:20 43:13
 44:16
price (2) 28:23 83:24
prima (1) 72:25
primary (2) 60:5 89:9
principal (7) 4:2 11:20
 24:2,10 27:16 30:13 85:2
principle (7) 6:4 9:9 17:9
 18:6 73:5 74:7 89:14
principles (15) 6:5,9,19,23

12:19 59:14 63:16,20,25
 65:21 67:7 68:12,17 71:18
 79:22
prior (7) 13:14 20:11 43:8,12
 44:25 46:16 96:14
prioritise (2) 4:18 47:5
prioritising (1) 58:1
priority (16) 3:3 14:5,17
 16:6,11 21:15 28:21 29:16
 30:22 46:21 51:15
 52:11,15 55:20 66:1 83:7
private (2) 1:7,10
pro (1) 9:9
probably (11) 7:7 8:9 16:2
 17:25 31:12 33:1,2 48:17
 73:9 75:17 97:23
problem (2) 53:5 81:15
procedures (1) 51:10
proceedings (2) 81:7 96:22
proceeds (5) 2:21 21:9
 30:7,20 32:7
process (4) 38:15,16 42

putting (3) 7:13 59:1 82:14

Q

quantum (1) 90:22

question (33) 1:19 2:12 4:9

5:19,20,22,25 6:8,8,23

8:10 10:1 12:15,18 16:25

20:14 21:10 25:11,13

31:17 47:16 52:23 53:25

56:3 58:20 65:20 68:8,18

73:25 83:12 88:21 92:2

97:16

questions (2) 20:10 43:4

quick (1) 35:10

quickly (4) 53:10 54:20

59:14 65:21

quiet (1) 1:7

quite (9) 3:16 5:25 16:3

26:18 32:23 66:18 67:4

82:6 87:2

quotation (1) 8:20

quote (2) 45:16 46:4

quotes (1) 43:3

quoting (1) 64:15

R

ran (3) 82:1 88:8 94:10

rank (2) 36:13 81:18

rare (1) 28:21

rata (1) 9:9

rateably (1) 32:14

rather (10) 6:14 26:9 27:4

31:12 36:3 59:1 63:5 86:11

91:17 96:25

rational (1) 69:18

rationality (1) 60:7

rationality (1) 67:20

rawlings (101) 1:13,17

4:17,20,25 5:2,9 6:11,21

7:7,18,25 8:15 9:19 10:12

11:12,17 12:5,13,22 15:16

16:19 17:9,20,25

18:8,11,23 19:12,23

20:8,16 21:5,13,18,21

24:15 27:24 29:8,24

31:4,9,20 33:1 34:14 36:25

37:24 38:4,12 46:2 47:16

48:12 49:1 50:25 51:4

55:17 56:15 57:2,12 58:12

59:18 61:19 63:2,25 64:23

65:2,13,15 68:23 69:9

75:17,23 76:6,12,18,21

77:3 78:7,16,20 79:1,8

80:19 86:17 88:23 90:5,23

91:7 92:3,6,14 93:10

94:1,3,22 95:9,16 96:18,21

98:16

re (1) 12:10

reach (2) 28:22 72:9

react (1) 32:21

reaction (1) 34:2

read (26) 7:6 12:22 13:10

26:14 30:4,19 34:11 36:24

39:10 41:21 43:6,19

45:15,24 46:20 47:2,3

51:16 55:21 56:13 59:21

61:14 69:7 74:16,17 84:22

reader (1) 32:13

reading (4) 11:15 44:13

45:25 79:14

ready (1) 67:18

real (3) 5:8 6:22 91:19

realisation (1) 18:20

realisations (2) 76:24 87:14

realising (1) 21:9

really (9) 8:19 9:23 15:7

16:24 17:24 42:23 93:11

97:23 98:6

reamended (1) 54:10

reason (8) 17:1 29:2 36:2

60:22 69:23 73:5 82:14

86:8

reasonable (2) 60:13 64:16

reasonably (2) 67:20 71:7

reasons (6) 31:18 34:15

40:13 62:1 79:25 88:10

reassuring (1) 29:15

rebranding (1) 85:16

receive (1) 18:23,25

received (7) 2:24 10:8,9 16:7

65:24 70:16 76:11

receiver (2) 2:15 3:7

receiving (1) 52:12

recent (1) 35:12

record (1) 12:10

recorded (1) 1:9

recordings (1) 1:10

records (1) 25:22

recourse (3) 18:12 76:7

88:10

recover (6) 29:5 32:6

34:20,21 57:8 93:21

recoveries (10) 9:14 50:23

51:7,16 52:3 53:15,21

54:3,6 76:11

recovering (1) 16:12

recovers (1) 87:23

recovery (28) 14:1 19:15

29:4,12 37:4 51:23 52:22

54:11,23 55:14

56:18,18,22,25

57:7,8,11,15,21

58:3,6,19,19,23 59:4,10

83:15 92:19

reducing (1) 13:11

refer (4) 7:2 14:2 41:24 60:2

referable (1) 38:24

reference (15) 23:21 26:13

35:15 37:17 40:1 46:24

50:12 59:3 64:13 68:12

77:19 79:15 81:3,6 84:7

references (1) 39:17

referred (8) 8:8 12:2 15:18

28:13 37:14 43:12 55:5

78:11

referring (2) 11:14 84:23

reflect (1) 35:12

reflecting (2) 24:10 31:1

refreshed (1) 35:11

refuse (2) 42:2,8

regard (8) 8:23 60:14 62:5

64:17 71:7,14 89:10 93:1

regarded (2) 47:15 48:5

regarding (1) 41:24

regards (2) 30:2 73:11

region (1) 80:24

registration (2) 37:25 38:13

regulated (2) 83:25 91:24

regulator (5) 41:12,14 47:4

83:24 85:10

regulators (1) 85:13

regulatory (2) 23:24 41:18

relates (3) 2:21 35:20 49:25

relation (14) 1:23 3:15 12:24

20:9,23 21:1,19 27:13

43:25 47:23 79:11 90:22

95:8,25

relationship (1) 25:7

relatively (1) 12:3

relevance (2) 20:15 84:6

relevant (20) 17:15,18 19:25

20:3 23:16 24:13 26:21

33:20,23 34:3 39:4 53:11

55:19 63:15 65:22 68:24

72:6 77:23 92:3 95:23

relevantly (1) 3:12

reliance (3) 16:22 31:24 72:2

relied (1) 92:19

relies (2) 91:12 93:2

reluctantly (1) 85:9

rely (2) 7:2 31:10

remarkable (1) 55:7

remarkably (1) 85:15

remarks (1) 67:10

remediation (1) 77:18

remember (2) 62:14 80:8

remind (5) 1:6 22:17 49:23

55:17 60:24

reminder (1) 15:1

reminding (1) 75:12

remuneration (2) 3:7 62:19

renege (5) 33:17 83:4,5

94:18 95:2

repay (2) 52:6,8

repayment (3) 10:10 11:10

30:6

replace (1) 80:5

replied (1) 85:6

reply (9) 45:4,6,21,21 46:18

53:24 65:3 86:19 100:5

replying (1) 46:11

report (2) 23:24,24

representation (2) 16:21

47:4

representations (8) 33:19

86:24 91:25 92:1

94:19,21,24 95:1

represented (2) 61:12 95:6

represents (1) 36:8

reputation (1) 28:24

requirements (1) 39:23

reservations (2) 38:25 40:22

reserve (1) 96:25

residual (1) 81:1

resile (2) 83:22,23

respect (15) 4:5 5:9,16 7:2

27:1 31:9 60:21 63:25

66:17,19 74:19 75:5 77:13

81:13 84:1

respectfully (3) 74:16 80:12

83:20

respective (2) 2:10 23:3

respond (1) 43:4

responds (1) 15:4

response (8) 14:18

15:3,10,17 44:12 53:5

84:21 85:1

responsible (1) 86:6

rest (4) 17:14 26:2 53:6

66:24

restitution (1) 78:18

result (8) 16:7 55:22 56:18

71:16 72:12 73:9 76:22

81:17

resulted (2) 84:12 85:17

retired (1) 80:5

reverse (1) 43:19

review (2) 42:18 60:16

reviewing (1) 60:4

rewarding (1) 96:7

rhetorical (1) 47:16

richard (2) 70:21,23

righthand (1) 52:11

rights (5) 2:6 11:6 22:23

67:16,17

rigid (1) 73:14

rise (4) 48:23 72:20 91:13,15

risk (9) 25:23 26:10,16 40:8

82:1,3 88:8 94:11,16

risks (3) 26:19 45:2 94:15

road (1) 83:13

robert (2) 41:17 43:24

robust (1) 51:10

roughly (3) 24:19 39:9 51:24

roundup (1) 35:3

rules (5) 35:7,8 39:15,21

85:13

run (6

33:8,16 35:17 42:4,22
 45:14 47:19 55:19 60:1
 65:4 75:25 76:18 77:10,11
 78:24,24 79:22 89:18 90:5
 92:25 95:12
themselves (1) 71:17
theory (1) 26:2
thereafter (2) 31:19 55:7
therefore (2) 20:19 57:7
thereof (1) 2:11
theres (4) 34:7,9 35:7 58:14
theyd (1) 18:23
theyre (5) 4:21 5:9 18:25
 54:20 90:9
thing (2) 73:8 96:3
thinks (1) 49:8
third (9) 22:4 26:14 30:12
 47:9 55:13 59:3 70:1 81:24
 94:10
thornton (1) 23:23
thoroughly (3) 37:7 84:20
 86:1
though (2) 33:13 84:8
thought (3) 8:5 88:20 94:12
threat (1) 85:18
three (8) 23:1 46:18 52:2
 54:9,12 57:20 68:19 74:20
threemonth (1) 54:15
thrells (2) 60:23 61:1
through (12) 9:24,25 12:19
 23:15 37:16 45:24 53:10
 54:19,20 58:6 63:21 78:11
thursday (1) 1:1
tied (2) 90:8,17
time (19) 7:20 15:25 23:14
 27:4 39:2 40:19
 41:10,11,20 46:23 48:20
 54:13 64:20 77:24 78:19
 84:11,11 97:3,5
times (2) 56:5 59:7
timing (1) 53:4
tired (1) 33:2
title (1) 27:15
together (1) 4:3
told (14) 10:15 26:25 27:5,6
 33:14 37:19 46:21 47:13
 57:3,23 58:11 78:2 82:4,17
too (1) 61:3
took (7) 24:9,11 25:1,4
 29:22 38:22 82:8
topic (2) 23:14 39:2
total (2) 62:19 64:25
toube (73) 1:16,18,19
 4:18,23 5:1,3,18 6:19,22
 7:15,19 8:11,16 9:20 10:13
 11:12,15,18 12:5,12,14,24
 15:17 16:24 17:1,19,21
 18:5,9,19,25 19:13
 20:2,9,23 21:6,17,19 22:19
 49:7,8,13 52:10 53:23 54:7
 63:3,21 65:2,8 86:17,19,20
 89:9 90:18,24 91:8
 92:5,9,15 93:11 94:2,4
 95:7,10,17 96:20 97:7
 98:7,13,25 100:3,6
towards (6) 3:19 27:21 28:3
 62:8 66:2 74:7
track (1) 29:21
trade (2) 77:6 79:19
trading (5) 40:7,12 85:4,19
 90:12
trail (1) 47:23
transcriber (1) 48:22
transferees (1) 78:21
transparent (1) 44:5
treat (5) 9:5 63:19
 89:14,16,17
treated (1) 9:8
trickle (1) 87:25
trouble (2) 61:3 77:23
troublesome (1) 10:4
true (5) 20:23 25:7 33:8
 88:18 90:5
truly (2) 24:3 81:13
trust (53) 2:8 12:15,16,16
 17:12,22 18:7,9,12,15,21

20:13,18,18,21,24,25
 21:8,13,14
 22:1,2,2,5,7,13,18,21 23:9
 25:15 27:11,13 32:11,17
 62:6,10 66:10,16 67:4,25
 68:9 73:12 75:10 77:16
 79:25 81:19 82:11,18 86:4
 87:12 89:11 93:7 98:18
trustee (52) 5:15 6:15,15
 8:12 17:21,22,22 24:25
 25:9 26:24,25 27:7,11,13
 59:22 60:5,8,13,18,19,20
 61:8 62:7 63:10 64:7,9,17
 66:5 68:1,3,9,12
 69:11,14,20 73:22
 74:1,1,11,15 79:6 80:12
 82:20 83:25 84:3 86:11
 87:11 89:23 91:3 92:4,11
 93:3
trustees (11) 22:8 61:6
 68:7,25 69:2 70:12,18
 71:7,14 72:8,24
trustees transferees (1) 9:15
trusts (6) 66:16 73:6,13,15
 74:4 75:1
try (1) 96:22
turn (17) 22:16 25:14
 28:11,24 29:20 30:1 34:8
 36:21 40:17 44:11 45:5
 50:13 51:19 56:8 61:4 73:2
 84:16
turning (3) 7:4 45:15 50:22
turns (2) 2:2 72:14
twoandahalf (1) 38:25
type (1) 73:18
typically (1) 60:18

U

ultimately (2) 19:1 69:22
unable (3) 52:8 80:5 97:17
uncertain (1) 59:23
underlying (6) 8:16 9:9 21:7
 23:12 27:1 78:10
undermine (1) 26:2
underpins (1) 70:5
understand (8) 7:9 16:19,23
 20:20 72:22 77:12 78:12
 86:4
understanding (1) 31:19
understands (1) 45:7
understood (2) 29:14 71:25
undertaking (2) 47:25 48:2
unease (1) 22:15
unequal (2) 69:22 71:16
unequally (2) 75:1,2
unethical (1) 17:13
unfair (3) 20:14 79:18 81:7
unfairness (1) 70:3
unfortunate (1) 81:17
unfortunately (3) 12:5,6
 28:21
unless (3) 52:12 69:23 75:5
unlikely (1) 1:13
unlikely (3) 25:24 26:1,14
unpaid (3) 30:9,11 44:19
unpalatable (1) 81:18
unqualified (1) 66:6
unreasonably (1) 8:25
unsecured (25) 19:9 62:4
 75:11,13 77:5,15 79:4,11
 80:16,20 81:5 82:1
 87:10,11 88:4 89:3
 90:4,6,9,14,25 94:7,10
 95:20 96:10
unsecureds (2) 62:7,8
unsurprisingly (2) 25:4 78:2
until (6) 44:15 49:5,12 75:5
 92:19 97:24
untrue (1) 31:3
update (2) 15:19 55:6
updating (1) 54:4
upheld (2) 70:17,23
uploaded (1) 16:3
upon (7) 2:8 62:9,21 67:15
 87:6 92:19 93:1
urged (1) 78:23

used (2) 20:6 67:18
useful (2) 33:4 36:16
users (1) 85:22
using (1) 84:24
usual (1) 98:20

V

v (3) 61:1 70:7 72:17
value (1) 78:3
variety (1) 71:6
various (4) 22:3 39:1,17
 77:21
vary (2) 30:15 33:7
vast (1) 88:2
vc (2) 11:11 12:10
vehicle (3) 24:25 27:24 77:11
version (3) 29:21 42:13,20
via (2) 11:6 26:4
visavis (2) 10:4 24:11
visualaudio (1) 11:11
voice (1) 45:25
visavis (2) 10:4 24:11
visualaudio (1) 11:11
voice (1) 45:25
volume (2) 72:15 84:9
voting (2) 35:16 90:20

W

wanting (1) 8:8
wants (1) 65:8
war (1) 72:16
warning (1) 94:14
warren (2) 61:12,13
wasnt (6) 31:1,4,5,15 34:21
 46:16
waterfall (9) 10:23 11:2,21
 21:3,10,11 44:2 46:21 79:6
way (26) 6:4,4 8:4 9:2 13:2,2
 18:3 19:19 21:25 26:22
 55:9 59:24 60:6 67:21
 69:18 70:19 72:21 79:21
 80:1,17 83:7 84:19 88:13
 94:5 96:4,11
wealth (1) 15:7
wearing (2) 62:6,7
webb (6) 23:20 24:17 37:23
 38:20 59:7 81:8
webbs (3) 78:10 79:14 81:6
website (6) 16:4 39:17
 41:3,4 42:12 58:17
wed (2) 38:10 65:16
week (2) 53:25 62:14
weeks (3) 52:2 97:3,5
weight (2) 32:18 34:16
wellknown (2) 67:8,9
went (2) 81:22,22
werent (1) 94:9
weve (3) 21:3 38:7 88:10
whatever (5) 16:10 19:7
 20:10 76:19 95:14
whats (4) 30:2 35:10 45:7
 54:13
whereas (3) 58:2 93:7 94:11
whereby (1) 69:11
whilst (1) 1:8
whimsical (1) 73:11
whisper (1) 56:21
whole (5) 5:14 7:13 20:13
 82:6 86:10
whom (1) 68:14
wider (2) 86:3 94:23
widest (1) 18:1
wilberforce (2) 73:3 74:3
wish (2) 19:20 88:19
withdrawn (1) 56:23
witness (10) 13:8 25:16
 28:14 32:24 34:4 51:5 58:9
 78:10 79:14 81:6
wont (2) 76:22 77:7
work (2) 13:15 68:16
world (4) 88:24 89:7 90:1
 95:23
worry (2) 2:15 98:16
worse (1) 15:6
worth (5) 7:3 30:17 67:5
 75:12 88:6
wouldnt (3) 7:11 31:15 78:14
wrapped (1) 49:14

writing (2) 39:13,19
written (1) 50:25
wrong (5) 15:6 16:15 33:22
 50:12 75:20
wrote (1) 59:8

Y

year (3) 24:5 39:1 79:17
years (4) 38:18,22 42:5 62:20
yesterday (5) 14:3 25:1
 35:18 40:2 42:23
youd (1) 38:5
youll (8) 2:6,18 10:7 13:12
 35:6 39:7 47:20 61:11
youre (3) 6:11 12:6 63:2
yourself (6) 22:17 35:23
 36:24 45:25 64:7 69:8
yourselves (2) 61:15 91:23
youve (2) 36:20 93:7

Z

zero (2) 76:7,9

I

1 (25) 1:1 19:16 23:20,21
 24:1,7 40:18 49:4,4,16
 52:16 54:8 76:3,15 77:18
 78:4 80:20 85:8 86:12 87:1
 88:9,12 93:20 96:12 100:3
10 (12) 1:16,18,19,25
 21:20,23 22:17 49:9 86:19
 100:3,4,5
100 (5) 32:13 65:10 69:11,15
 87:23
1000s (1) 26:9
103 (1) 28:11
105 (1) 1:2
107 (2) 29:21,25
108 (1) 41:16
109 (1) 43:18
11 (2) 38:22 54:15
110 (1) 35:1
111 (2) 14:4 51:19
112 (2) 50:14,15
114 (3) 14:14 53:13,22
115 (2) 34:5,6
116 (1) 36:17
119 (1) 58:10
12 (3) 39:8 61:1 97:5
121 (2) 15:4 54:20
1226 (1) 48:12
1228 (1) 49:18
1235 (3) 49:5,16,20
125 (1) 76:3
127 (3) 9:12,17 31:22
13 (14) 10:23 12:21 14:7
 15:5 43:2 44:13 50:17 51:3
 53:14 54:21 58:16,21
 77:6,8
133 (17) 11:8,14 12:22 14:16
 30:4,18 32:20 33:3 35:20
 36:8 37:1 43:12 44:3 46:22
 47:20 53:8,20
14 (3) 2:4 77:6 79:13
1411 (2) 2:7 22:22
1432r1 (1) 45:3
15 (3) 11:1 49:9 70:7
152 (1) 7:3
1523 (1) 9:13
153 (1) 2:13
154 (3) 2:18 10:3 12:2
155 (2) 10:13 50:3
156 (2) 3:22 10:16
1561 (1) 50:7
157 (1) 13:17
1573 (1) 14:2
16 (7) 10:5 12:25 24:14
 35:4,18 37:23 42:22
17 (2) 24:18 53:17
173 (1) 2:4
179 (1) 25:14
18 (2) 7:5 59:9
182 (2) 2:20 65:23
1820 (1) 7:6

194 (2) 15:24 55:13
1992 (1) 61:2
19th (1) 74:5
1s (1) 91:2

2

2 (111) 1:23 3:11,25 4:18
 5:7,7,23 7:4,16,20 9:15,21
 10:1,21 14:11,23 15:22
 17:7 19:5,10,13,17,20
 20:19,21,24 21:4,6,16
 23:20 24:5,7,14,16,17,19
 25:2,6 26:18
 27:17,18,19,20,22,24,25
 28:4,16 29:16 30:2 34:7,19
 35:8 37:2,3,6,12,23
 38:17,20 41:21 43:6,7
 46:22 50:9 52:17 53:8 59:7
 63:16 65:9 66:11,19,23
 67:2 75:2,6 76:2 77:3,21
 78:6,21 80:4,22 81:8,17
 82:2,4,15 83:2 85:6
 86:7,13 87:1,14,24
 88:1,3,18 89:2,13,21 91:14
 92:1,20 93:15,16,20
 94:11,14 96:2,11
20 (4) 8:20 49:10 65:1 69:14
200 (1) 65:12
2014 (4) 23:18,19 37:20 38:1
2015 (8) 23:19,23 24:8,18,20
 25:18 27:18 28:2
2016 (6) 37:22 38:3,19 39:8
 85:6,8
2017 (2) 40:18 42:15
2018 (38) 10:5 12:3 13:13
 14:7,8 16:1,3 27:20
 28:2,14 29:19 32:21 34:24
 35:4,12 38:18,22 41:9,19
 42:12 43:13 44:13,15
 50:17 51:3 54:15 55:10,11
 56:17 57:3,18,25 58:5
 59:6,9 83:6,17,19
2021 (3) 1:1 75:24 76:17
21 (4) 2:21 24:8,20 100:4
211 (3) 65:24 76:24 87:13
2112 (4) 3:18 4:10 66:2,13
23 (4) 28:14 42:15 75:24
 76:17
241 (1) 34:10
25 (3) 49:16 64:25 69:15
255 (1) 99:2
27 (2) 14:8 51:24
28 (2) 56:17 57:3
286 (1) 61:4
29062 (1) 68:25
29064 (1) 69:6
2931 (1) 23:21
296 (1) 11:1

3

3 (5) 15:11 52:18 54:25 76:5
 85:12
30 (4) 37:22 38:3 48:17
 53:17
32 (1) 7:5
34 (1) 24:17
39 (1) 25:17

4

4 (8) 13:9 32:25 34:5 36:17
 40:11 56:7,8 58:10
40 (1) 59:20
414 (1) 28:12
421 (1) 40:1
431 (1) 81:8
44 (1) 39:8
444 (1) 1:5
449 (1) 31:23
45 (3) 48:17 56:9 87:19
450 (1) 30:1
459 (1) 61:20
46 (1) 13:9
47 (1) 59:20
471 (1) 60:2

472 (2) 60:12 64:13
473 (1) 60:17
479 (1) 44:12
48 (1) 37:23
483 (2) 35:5,6
484 (1) 35:9
486 (1) 51:20
487 (1) 51:20
489 (1) 14:5
49 (3) 84:16,17,21
493 (1) 51:6
499 (1) 14:14
4a (1) 41:25

5

5 (9) 15:9,13 42:12 43:9,13
 44:15 55:2 66:21 88:6
500 (2) 14:19 53:22
504 (2) 14:25 54:7
51 (1) 49:25
52 (1) 37:14
530 (1) 15:11
55 (1) 87:24
553 (1) 84:21
554 (1) 85:6
555 (1) 85:14
5th (1) 35:12

6

6 (4) 41:19 43:6,11 72:15
60 (1) 87:23
600000 (3) 77:10 81:9 90:19
61 (1) 38:21
626 (2) 70:25 71:1
63 (1) 68:21
65 (3) 62:20 76:17 78:11
67 (1) 78:11

7

7 (2) 23:21 31:25
752 (1) 34:19
753 (2) 34:10,13
76 (2) 35:3 36:19
762 (1) 36:24
77 (2) 50:16 51:5
79 (1) 40:17
796 (1) 58:9

8

8 (2) 43:5 66:21
80 (1) 59:8
81 (1) 24:8
813 (1) 25:2
86 (1) 100:5
882 (1) 7:5

9

9 (2) 24:8 43:23
91 (1) 28:13
966 (1) 16:6