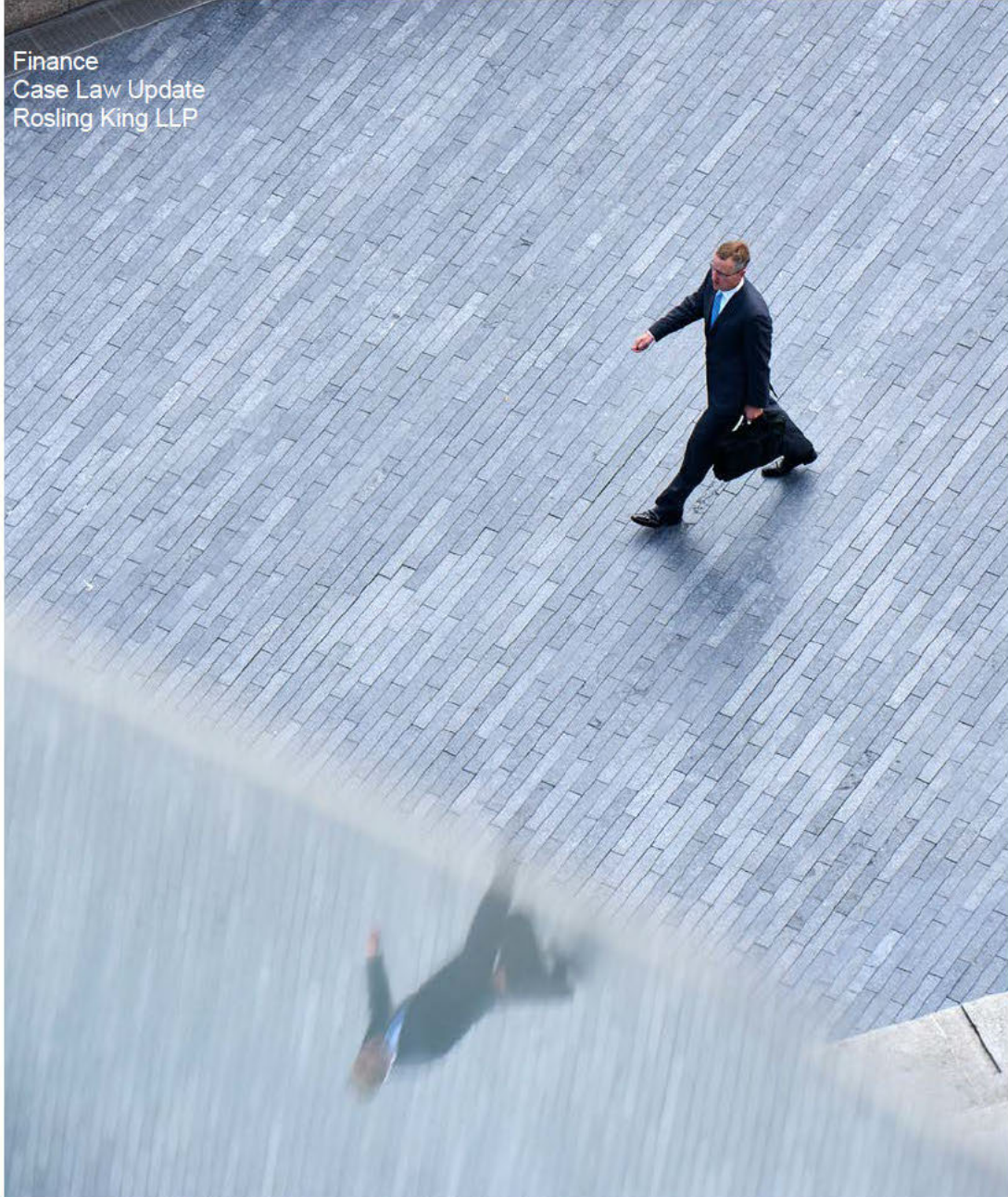


Finance
Case Law Update
Rosling King LLP



Introduction

It seems in the past few years, there has been an increasing number of claims being brought by sponsors/borrowers in relation to their secured lender's enforcement/restructuring action. These claims can include "underselling" claims i.e. that the secured asset was undersold to the detriment of the borrower (e.g. *Davey v Money* – in respect of which see our article [here](#)) and economic torts such as unlawful means conspiracy i.e. that in some way the lender and/or relevant appointed insolvency practitioner act unlawfully with others to cause the borrower/shareholders damage. In the recent case of *Standish (and 8 others) v The Royal Bank of Scotland, SIG Number 2 Ltd (formerly West Register Number 2 Ltd)* [2018] EWHC 1829 (Ch), the High Court was tasked with deciding whether such an unlawful conspiracy claim in respect of the restructuring imposed on behalf of the bank, NatWest, had reasonable grounds of success or should be struck out.

The Background

The claimants were the directors/shareholders of Bowlplex Ltd (the "**Company**"), which was (as the name suggests) a business that ran a number of bowling alleys. The Company had granted a debenture over its undertaking and legal charges over its properties in favour of National Westminster Bank plc ("**NatWest**") which had lent it monies. In 2009, the Company entered into a new facility agreement with NatWest but subsequently breached its financial covenants. What followed was a series of restructurings of the Company which was led by the Royal Bank of Scotland ("**RBS**") on behalf of NatWest.

The restructures led to the transfer of shares to West Register Number 2 Ltd ("**West Register**") (a subsidiary of RBS) which ultimately resulted in West Register allegedly holding 80% of the equity in the Company. The restructures also involved the appointment of an individual, Mr Sondhi, from West Register to observe the directors' actions at Company board meetings. Eventually, the shares in the Company were sold for £30 million resulting in a net return to shareholders of over £22 million.

The Claim

Following the sale of the Company, the directors/shareholders of the Company (as opposed to the Company itself) issued a claim on the basis that RBS and West Register had unlawfully conspired to maximise their own shareholding in the Company and minimise that of the existing shareholders. They also alleged the RBS had breached its duties of good faith and equitable duties to the shareholders and that Mr Sondhi had breached his fiduciary duties as shadow director of the Company. The shareholders sought to bring a claim on the basis that there was a breach of an implied overarching customer agreement between the Company and NatWest that governed their relationship. In response, RBS and West Register sought to strike out the claim on the basis it had no reasonable prospect of success.

The Issues raised and Decisions made

The test to strike out a claim is a demanding one and the Court had to consider several aspects of the claim and whether or not they would fail at trial.

1. The Customer Agreement and the duty of good faith

The shareholders sought to argue that there was an overarching customer agreement between NatWest and the Company into which there were implied terms for NatWest to act in good faith. They referred to the bank's policy to "Treat Customers Fairly" as pointing to the incorporation of this implied term. However, the Court gave this argument short shrift and held there was no "obvious reason why the court should conclude that there was an overarching agreement, without express terms, that came into being at some unspecified stage." The shareholders failed to particularise how a customer contract had been created and to show how the parties conduct would have been different if that contract had been in place. Furthermore, the Court could not see how the bank's internal "Treat Customers Fairly" principles could be implied into what was an unregulated loan.

The Court concluded the alleged customer agreement was a "completely artificial construct that is divorced from the commercial realities of the dealings between the parties". The Court was in no doubt that this element of the claim would fail.

2. Equitable Duties

The shareholders sought to rely upon the case of *Medforth v Blake* [2000] Ch 86 to demonstrate mortgagees owed duties of good faith and to act fairly, to a mortgagor even when it was not exercising powers under its security.

However, *Medforth* was distinguished by the Court on the basis that the case concerned whether a receiver of rent owed similar duties to that of the lender when managing the mortgagor's business to when selling a mortgaged property. The Court held it was "quite impossible" to extrapolate from *Medforth* "a wide ranging proposition" that will apply to a secured lender who has not exercised, or threatened to exercise, its security. Accordingly, it could not be applied to the present case as the shareholders' claim was focused on the restructuring of lending and wholly unrelated to the security. The shareholders were seeking to take the law regarding the equitable duties owed by a secured lender, which was nearly 19 years old, and extend it without any new case law or development in the intervening period. Furthermore, the shareholders had nothing to show that the conduct of NatWest/RBS has been unlawful which was a key element of bringing an unlawful means conspiracy claim.

3. Shadow directorship and fiduciary duties

The shareholders asserted that Mr Sodhi, who had been appointed by West Register, had acted beyond the intended role of an observer because the directors felt obliged to follow his instructions. However, Mr Sodhi's directions and instructions, which related to instructing KPMG in respect of a proposed Company Voluntary Arrangement and the engagement of a turnaround consultant, may have shown how Mr Sodhi was acting as a shadow director but the other directors did not actually rely on those directions. Instead,

the directors, who were fully aware of Mr Sodhi's conflict of interest, acted of their own will and were not overborne by Mr Sodhi.

Essentially, the Court held "the overall difficulty" for the directors/shareholders was that the directors themselves agreed to the restructuring of their own free will without having been directed by West Register to do so.

Ultimately, given its conclusions regarding the various grounds raised by the directors/shareholders, the Court struck out the claim.

Commentary

The case is an interesting example of the arguments that sponsors/borrowers may look to raise to bring claims against lenders and/or insolvency practitioners to challenge their actions in a distressed scenario. The advent of litigation funding and the development of case law in this area has fuelled such actions, but the successful strike out of the claim in this instance represents one of the tactical responses that can be used to defend such actions (interim applications for security for costs and early disclosure being some of the other options).

For further information, please contact [Alexander Pelopidas](#) or the Partner with whom you usually deal.