Neutral Citation Number: [2021] EWHC 2285 (Ch).

Before

HHJ BRIAN RAWLINGS

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- **CR-2019-BHM-000443 and CR-2019-BHM-000444**

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS IN BIRMINGHAM
INSOLVENCY AND COMPANIES LIST (ChD)

IN THE MATTER OF LENDY LTD (IN ADMINISTRATION)
IN THE MATTER OF SAVING STREAM SECURITY HOLDING LIMITED (IN ADMINISTRATION)
AND IN THE MATTER OF THE INSOLVENCY ACT 1986
B E T W E E N :

(1) Damian Webb, Phillip Rodney Sykes and Mark John Wilson
(as joint administrators of Lendy Ltd (in administration))
(2) Damian Webb, Phillip Rodney Sykes and Mark John Wilson
(as joint administrators of Saving Stream Security Holding Limited (in administration))

Applicants

---and---

(1) Lisa Taylor
(as a representative respondent on behalf of the Model 2 Investors and Model 2 Transferees)
(2) Christine Mary Laverty, Helen Julia Dale and Patrick O'Sullivan
(as joint conflict administrators of Saving Stream Security Holding Limited (in administration))

Respondents

Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

Hearing dates 28 June -2 July 2021

Handed down on 12 August 2021

Adv Felicity Toube QC and Ryan Perkins, instructed by Shoosmiths LLP, for the Applicants

Adv Andreas Gledhill QC and Carmine Conte, instructed by gunnercooke LLP, for the First Respondent

The Second Respondents not participating in the hearing

BACKGROUND

1. On 9 October 2012, Lendy Ltd ("Lendy") was incorporated with Tim Alastair Gordon ("Mr Gordon") as its sole director and shareholder. Liam Brooke ("Mr Brooke") was appointed as the second director of Lendy on 12 January 2013 and thereafter became a shareholder.

2. Lendy initially provided finance to purchase luxury boats, but in November 2013, the directors decided to launch an electronic peer to peer ("Peer to Peer") lending platform under the name "Saving Stream" to fund the purchase of real property. The platform was hosted on the domain www.lendy.co.uk, formerly www.savingstream.co.uk ("the Lendy Platform"). Mr Gordon developed the IT to host the Peer to Peer lending on the Lendy Platform. Mr Brooke's background was in financial services. The Lendy Platform connected people who wished to borrow money with investors who wanted to lend money.

3. In February 2014, Lendy obtained FCA interim permission to enter into regulated consumer credit agreements, to exercise the rights of a lender under consumer credit agreements and to operate a Peer to Peer lending platform.

4. Peer to Peer lending operated on the Lendy Platform as follows:
   (a) potential lenders signed up to the Lendy Platform, indicating their willingness to lend;
   (b) borrowers who wished to borrow applied for a loan and Lendy would carry out certain checks upon the potential borrower, the purpose of the loan and security offered and if the potential borrower/lending/security passed those checks, the proposed loan was uploaded to the Lendy Platform as a loan offered to potential lenders who had already signed up to the Lendy Platform;
   (c) potential lenders selected which loan, available on the Lendy Platform, they wished to participate in and how much they wished to contribute to that loan;

(d) when, in aggregate, the amount that potential lenders were prepared to provide to fund a particular loan equalled the total amount of the loan which was required, by the borrower, the money was collected from what were now the relevant lenders and the loan advanced to the relevant borrower;

(e) when the loan was repaid, the repayment was distributed to the lenders who had funded the advance of that loan.

THE MODEL 1 STRUCTURE

5. The loan model used by Lendy for Peer to Peer lending initially provided for Lendy to contract as principal both with the borrower who received the loan and with the lenders who funded it ("Model 1"). Under Model 1 therefore, the lenders (who I will refer to as "Model 1 Investors") would lend money to Lendy and Lendy would loan the money to the borrowers (who I will refer to as "Model 1 Borrowers" and the loan as "the Model 1 Borrower Loan"). In this structure, there was not intended to be any contractual relationship between the Model 1 Investors who funded the loan and the Model 1 Borrower who received the Model 1 Borrower Loan.

6. Security for Model 1 Borrower Loans was taken in the name of Lendy.

7. In March 2014, Lendy advanced the first Model 1 Borrower Loan.

8. Lendy created a secondary market in mid-2014, which allowed Model 1 Investors to sell to other Model 1 Investors their part of the Model 1 Borrower Loan before it was repaid. I will refer to Model 1 Investors who purchased parts of Model 1 Borrower Loans originally advanced by others as "Model 1 Transferees", in order to distinguish them from the Model 1 Investors who originally participated in the relevant Model 1 Borrower Loan. Lendy facilitated on the Lendy Platform the sale, by Model 1 Investors, and purchase, by Model 1 Transferees, of parts of Model 1 Borrower Loans already advanced, but not yet repaid in full (it also enabled Model 1 Transferees to sell on the part or parts of loans that they had acquired (I will also refer to the purchasers of loan parts from Model 1 Transferees as "Model 1 Transferees").

THE MODEL 2 STRUCTURE

9. In 2015, Lendy instructed its solicitors to draft a revised suite of loan and security documentation to change the structure of lending on the Lendy Platform so that Lendy would

act as agent for the individuals who provided money to fund loans to borrowers and those individuals, rather than Lendy, contracted as principals with the borrower ("Model 2").

10. Under Model 2, Lendy signed the loan agreement with the borrower ("Model 2 Borrower Loan" and "Model 2 Borrowers"), as agent, on behalf of the lenders ("Model 2 Investors"). The Model 2 Borrower Loan documentation stated that Lendy was acting as agent on the behalf of a group of investors (who were identified in Lendy's own books and records but were not disclosed in the loan documentation to the Model 2 Borrowers).

11. The Model 2 Borrower Loans were secured by debentures and guarantees granted by the Model 2 Borrowers to Saving Stream Security Holdings Limited ("SSSHL" and "Model 2 Security"). SSSHL was incorporated on 17 August 2015 and acted as security trustee on behalf of Model 2 Investors and Lendy. Messrs Gordon and Brooke were appointed as the only two directors of SSSHL and they each held one of its two issued shares.

12. The parties have agreed that, for the purpose of these proceedings, Lendy should be taken to have operated the Model 1 structure from March 2014 until 31 September 2015 and the Model 2 structure from 1 October 2015 onwards.

13. The first Model 2 Borrower Loan was completed with the relevant Model 2 Borrower on 27 October 2015. Thereafter, all loans were Model 2 Borrower Loans. No attempt was made to change existing Model 1 Borrower Loans to Model 2 Borrower Loans, although there were situations where (i) Model 1 Borrower Loans were extended on Model 2 Borrower Terms or (ii) further advances were made on Model 2 Borrower Terms.

14. Whilst SSSHL was the security trustee for Model 2 Security, Lendy was still the entity which carried out all the administrative work in liaising with Model 2 Borrowers, putting the loan and security documentation in place, updating the Lendy Platform, recovering Model 2 Borrower Loans and enforcing Model 2 Security. The Model 2 Investor Terms (as amended) provide in clause 8.1.3 that Model 2 Investors *"irrevocably and unconditionally, authorise Lendy to instruct* [SSSHL] *in relation to the Finance Documents, including without limitation the security documents and their enforcement."*

15. Lendy continued to operate a secondary market under the Model 2 structure, which allowed Model 2 Investors to sell their part of a Model 2 Borrower Loan, before it was repaid. I will refer to those who purchased parts of Model 2 Borrower Loans on the secondary market as "Model 2 Transferees".

LENDY PROVISION RESERVE LIMITED

16. On 20 January 2015, Lendy Provision Reserve Limited ("LPR") was incorporated. LPR was advertised on the Lendy Platform as holding a fund designed to compensate Model 1 Investors/Model 1 Transferees in the event that the amount realised from the Model 1 Borrower Loan that they had invested in was insufficient to repay them in full ("Investor Shortfall"). The stated intention was for LPR to always hold a sum of money equivalent to 2% of the total value of the Lendy loan book at any time. The Lendy Platform confirmed that the fund was paid out to Model 1 Investors/Model 1 Transferees on a discretionary basis and did not guarantee that there would be no loss to Model 1 Investors/Model 1 Transferees. Lendy first informed the Model 1 Investors of LPR in an email dated 23 January 2015. Following the switch to the Model 2 structure, in September 2015, LPR was represented as providing compensation for Model 2 Investors for Investor Shortfalls on a similar basis.

17. The FCA expressed the view, in a letter dated 1 June 2017, that the information given on the Lendy Platform about LPR was misleading in that it appeared to suggest that 2% of the total value of the Lendy loan book would be sufficient to compensate any Investor/Transferee if there was an Investor Shortfall, but that was not necessarily the case.

18. Whilst there was approximately 2% of the value of the Lendy loan book in the LPR bank account at all times, this money was not ring fenced or held on trust for a particular purpose. When the LPR account fell below the requisite 2%, Lendy's operational account was used to "top up" the LPR account. Prior to the appointment of the applicants as Administrators of Lendy, and SSSHL ("the Applicants"), the LPR was used to compensate Investors/Transferees on 6 loans where there was an Investor Shortfall.

19. On 7 September 2018, a charge was registered against LPR to secure a £1m working capital facility provided by Metro Bank to Lendy but guaranteed by LPR. On appointment of Administrators to LPR on 24 May 2019, the balance on the LPR bank account was £1,531,995 which was distributed to Metro Bank pursuant to its charge.

THE GROWTH AND SUBSEQUENT DECLINE OF LENDY

20. As at December 2015, the Lendy loan book had reached circa £70m and investments made on the Lendy Platform were running at approximately £10m a month.

21. Lendy applied for a full FCA licence in March 2016. As part of the application process the FCA met with Mr Brooke and other senior employees of Lendy in June/July 2016 to ascertain how the Lendy Platform worked.

22. Lendy Group Limited ("LGL") was incorporated on 11 November 2016 with Mr Brooke and Mr Gordon as LGL's only directors and shareholders. On 3 January 2017, Mr Brooke and Mr Gordon each transferred their shares in SSSHL to LGL and on 1 March 2017 Mr Brooke and Mr Gordon transferred their shares in Lendy to LGL.

23. In June 2017, Lendy's loan book peaked at £228m and monthly investments from investors averaged £14m per month.

24. Mr Gordon resigned as a director of LGL, SSSHL and Lendy and transferred his shares in LGL to Mr Brooke on 26 July 2018 (although it appears that Mr Gordon had little to do, in any event, with the day-to-day operations of Lendy after initially developing the IT for the Lendy Platform).

25. On 11 July 2018, the FCA granted Lendy full authorisation as an approved Peer to Peer lending platform.

26. The last Model 2 Borrower Loan was advanced on 18 September 2018. After that, Lendy entered into no new loans and only raised funds on the Lendy Platform to fund further tranches of existing loans.

27. On 12 November 2018, the FCA agreed a VREQ (Voluntary Requirements) with Lendy, pursuant to section 55L(5)(a) of the Financial Services and Markets Act 2000, imposing a voluntary restriction on payments with increased reporting requirements to the FCA. The VREQ required all payments in the ordinary course of business over £5,000 (whether as a single transaction or as a combination of related transactions) and any payments not in the ordinary course of business to be authorised by the FCA before payment was made.

28. The FCA had concerns about the extent of Lendy's compliance with the VREQ and carried out a short-notice audit at Lendy's offices on 9 and 10 April 2019. The FCA discovered that Lendy had made approximately 50 ordinary course of business payments of over £5,000 totalling almost £1,000,000 in the period 8 November 2018 to 29 March 2019, which were not authorised by, or notified to, the FCA.

29. On 15 January 2019, the FCA put Lendy on a supervision watchlist requiring weekly reports to be made to it. On 16 April 2019, the FCA required Lendy: not to dispose of, deal with or diminish the value of any of its assets; and not in any way to release client money without, in either case, the prior written consent of the FCA. As a result, every payment Lendy made had to be approved by the FCA. These restrictions were reported in the media and became public knowledge. As a result, many Investors became nervous and started demanding to be repaid.

30. On 22 May 2019, the FCA contacted Lendy and SSSHL to notify them that they intended to wind up Lendy and SSSHL on just and equitable grounds. Hearing of the FCA's petition was listed for 28 May 2019.

31. On 24 May 2019, Damian Webb ("Mr Webb"), Phillip Rodney Sykes and Mark John Wilson, all of RSM Restructuring Advisory LLP of 25 Farrington Street, London, were appointed Joint Administrators of both Lendy and SSSHL ("the Applicants").

32. On 26 July 2019, Christine Mary Laverty, Helen Julia Dale and Trevor Patrick O'Sullivan, all of Grant Thornton UK LLP, 30 Finsbury Square, London were appointed as additional Administrators of SSSHL ("the Conflict Administrators"). Mr Webb explains that there were two reasons for appointing the Conflict Administrators: (a) to act on behalf of SSSHL in relation to any conflict issues that may arise in connection with the appointments of RSM Restructuring Advisory LLP members (before 24 May 2019) as administrators over Model 2 Loan Borrowers or fixed charge receivers over their assets; and (b) to provide an independent oversight in relation to the charging structure and priority where Lendy is proposing to deduct costs and charges from the Model 2 Borrower Loan recoveries being made by SSSHL under the security it holds on behalf of Model 2 Investors and agree what represents a fair recharge as between the parties.

APPLICATION FOR DIRECTIONS

33. On 10 July 2020, the Applicants, as Administrators of Lendy and SSSHL, issued an application for directions under paragraph 63 of Schedule B1 to the Insolvency Act 1986 with a view to resolving certain questions regarding the rights and liabilities of the Model 1 and Model 2 Investors as against Lendy and SSSHL, as well as other issues in their administrations ("Directions Application"). The Directions Application had attached to it a suggested list of the issues that the Applicants asked the Court to determine ("List of Issues").

34. The Respondents to the Directions Application were named as:
    (a) Lisa Taylor ("Ms Taylor"), who is a Model 2 Investor. Ms Taylor was joined by the Applicants with the intention that she would argue on the determination of the List of Issues in the manner that best suited the interests of the Model 2 Investors and Model 2 Transferees (with the intention that the Applicants would make the contrary argument); and
    (b) the Conflict Administrators, who it was not intended would take an active part in the Directions Application (and in the event, who have not played an active role in the Directions Application), were joined so that they would be bound by the result of the Directions Application.

35. On 17 July 2020, HHJ Barker QC gave directions for the fixing of a Case Management Conference ("CMC") at which directions would be given in relation to the Directions Application. That CMC was listed for 23 September 2020.

36. LGL, acting by its sole director, Mr Brooke, applied to be joined as a respondent to the Directions Application, shortly before the CMC on 23 September 2020. LGL's argument was that it should be joined as a respondent to the Directions Application because there was no party before the Court which was in a position to argue for the interests of unsecured creditors of Lendy (of which LGL said it was one), or for the interests of LGL as sole shareholder interested in any surplus produced in the administration of Lendy (LGL arguing that a substantial surplus was likely).

37. The FCA wrote a letter to the Applicants on 18 September 2020 ("the FCA Letter") indicating that it believed that certain additional issues should be included in the List of Issues to be determined by the Court on the Directions Application. The additional issues that the FCA suggested should be included in the List of Issues included: (a) whether terms that Lendy may wish to rely upon against Model 2 Investors were: (i) incorporated into Lendy's contract with the relevant Investors; or (ii) 'unfair terms' under Part 2 of the Consumer Rights Act 2015; and (b) whether Lendy would breach its fiduciary duties to Model 2 Investors by charging Model 2 Borrowers default interest for its own account.

38. At the CMC taking place on 23 September 2020 before HHJ Barker QC, in addition to the Applicants and Ms Taylor, the FCA and LGL were each represented. HHJ Barker made an order which:
    (a) appointed Ms Taylor as representative respondent for the Model 2 Investors and Model 2 Transferees;

(b) adjourned the application made by LGL to be joined as a respondent to the Directions Application, giving directions for the filing and service of evidence on that issue;

(c) directed that the List of Issues attached to his order would provisionally form the subject matter of the Directions Application, with liberty to the parties to propose amendments to that provisional List of Issues;

(d) required the Applicants to confirm whether the additional issues identified in the FCA Letter, should be included in the List of Issues to be determined by the Court;

(e) directed that the FCA should set out in writing its response to any points made by the Applicants about the additional issues set out in the FCA Letter and confirm whether the FCA wished to be joined as a respondent to the Directions Application; and

(f) gave directions for the trial of the Directions Application.

39. At the adjourned CMC on 23 October 2020 which came before me, I:

(a) noted that the FCA did not wish to be joined as a respondent to the Directions Application;

(b) added to the List of Issues, a new issue, namely, whether Lendy:

"As regards its contractual liability under the relevant loan agreement with the Model 1 Investors, is liable to Model 1 Investors only to the extent that Lendy is repaid by the borrower under, or makes recoveries in respect of, a relevant loan agreement between it and the borrower";

(c) directed the Applicants to write to the unsecured creditors of Lendy to invite them to consider whether they wished to be joined to the Directions Application in order to argue that the answer to the question set out in paragraph 39(b) above should be "yes";

(d) directed that Ms Taylor should write to the Applicants to confirm if she was willing to argue that the answer to the question set out in paragraph 39(b) above should be "yes"; and

(e) adjourned LGL's application to be joined as a respondent to the Directions Application to 21 December 2020.

40. At the hearing on 21 December 2020, I:

(a) dismissed LGLs application to be joined as a respondent to the Directions Application;

(b) appended to my order the List of Issues to be determined by the Court pursuant to the Directions Application which included the additional issues that the FCA Letter suggested should be included in the List of Issues;

(c) directed that Ms Taylor should argue that the answer to the question set out in paragraph 39(b) above should be "yes"; and

(d) extended the deadlines for compliance with the directions set out in HHJ Barker's Order of 23 September 2020.

41. A pre-trial review was fixed for 7 June 2021. On application by the Applicants (supported by Ms Taylor), I dispensed with the pre-trial review hearing and made an order which provided for the List of Issues to be reduced from 16 issues to 10 issues (the Applicants having confirmed that 6 of the existing 16 issues had either been agreed between them and Ms Taylor, or the parties had agreed that they should be decided at a later date).

THE EVIDENCE

42. The substantive evidence which has been filed and served for the purposes of the Directions Application consists of:
    (a) the second, third and fifth witness statements of Mr Webb dated 9 July 2020, 16 September 2020, and 17 May 2021;
    (b) a witness statement of Norman Melton ("Mr Melton") dated 20 April 2020. Mr Melton made his first investment on the Lendy Platform in early 2016 and all of his investments were therefore in Model 2 Borrower Loans. His witness statement was filed on behalf of Ms Taylor;
    (c) a witness statement of Michael Powell ("Mr Powell") dated 21 April 2021. Mr Powell made his first investment on the Lendy Platform on 18 June 2014 and he is or was both a Model 1 Investor and a Model 2 Investor. Mr Powell also began engaging with the P2P Independent Forum in June 2014 ("the P2P Forum"). The P2P Forum is a forum in which private investors discuss Peer to Peer lending platforms (such as that operated by Lendy). Mr Powell commented upon the Lendy Platform in the P2P Forum and communicated with Lendy concerning the Lendy Platform. Mr Powell's witness statement was filed on behalf of Ms Taylor;
    (d) Lendy standard documentation relating to both the Model 1 structure and the Model 2 structure; and
    (e) a bundle of miscellaneous documents produced by the Applicants and Ms Taylor, including relevant correspondence.

REPRESENTATION AND CROSS-EXAMINATION OF WITNESSES

43. Before me the Applicants were represented by Ms Toube QC and Mr Perkins and the First Respondent, Ms Taylor by Mr Gledhill QC and Mr Conte. I am grateful to all of them for their clear and comprehensive submissions and also for the efforts they have made to agree matters wherever possible.

44. Mr Gledhill elected not to cross-examine Mr Webb upon his witness statements. Ms Toube carried out short cross examinations of Mr Powell and Mr Melton on the first day of the trial.

LIST OF ISSUES

45. The List of Issues (now reduced to 10) to be determined by me are as follows (headings are added for each group of issues for clarity):

MODEL 1 BORROWER LOANS AND MODEL 1 INVESTOR TERMS

(1) Do the Model 1 Investors (in their capacity as such) have any claim other than an unsecured provable claim against Lendy?

(2) Do the proceeds of security of a Model 1 Borrower Loan form part of Lendy's general estate?

(3) As regards its contractual liability to Model 1 Investors pursuant to the Model 1 Investor Terms, is Lendy liable to each Model 1 Investor only to the extent that Lendy is repaid by a Model 1 Borrower under, or makes recoveries in respect of, the relevant Model 1 Borrower Loan which that Model 1 Investor has funded? ***In any event, are the provable claims of the Model 1 Investors limited or capped by reference to the amounts repaid to or recovered by Lendy in respect of the Model 1 Borrower Loans which those Model 1 Investors have funded?*** (the wording in italics and bold was added when an amendment to Issue 3 was agreed between counsel shortly before trial)

(4) If the answer to the question in issue (3) is 'yes', should the Model 1 Investors' contractual claims be valued in an amount equal to the gross proceeds received by Lendy for the relevant Model 1 Borrower Loan or the net proceeds of that Model 1 Borrower Loan (taking into account the costs of realisation)?

MODEL 2 BORROWER LOANS AND MODEL 2 INVESTOR TERMS

INTERPRETATION, INCORPORATION AND CONSUMER RIGHTS

(5) On a proper construction of clause 6.3 of the Model 2 Borrower Loan, is the Model 2 Borrower required to pay the default interest to (i) the relevant Model 2 Investors and/or Model 2 Transferees, (ii) to Lendy (as principal) or (iii) in any other manner?

(6) Were any of the relevant clauses in the Model 2 Investor Terms not properly incorporated into the contract between Lendy and Model 2 Investors (on the basis that they were onerous or unusual or otherwise)?

(7) Do any of the relevant clauses in the Model 2 Investor Terms constitute 'unfair terms' under Part 2 of the Consumer Rights Act 2015?

FIDUCIARY DUTIES, PROPRIETARY RIGHTS AND FAIRNESS RULES

(8) Has Lendy breached any of its fiduciary duties regarding its charging fees and interest for its own account in connection with the Model 2 Borrower Loans? If so:

  (a) what is the appropriate form of relief for Model 2 Investors and/or the Model 2 Transferees;

  (b) is Lendy entitled to an equitable allowance to cover its costs as agent; and

  (c) if the answer to the question in issue (8)(a) is 'yes', how should that allowance be calculated in principle?

(9) Based upon the answers to the questions in issues (5)-(8), do the Model 2 Investors and/or the Model 2 Transferees have a legal or equitable proprietary interest in any of the following:

  (a) any default interest payable by a Model 2 Borrower to Lendy under a Model 2 Borrower Loan;

  (b) all standard interest payable by a Model 2 Borrower to Lendy under a Model 2 Borrower Loan; and

  (c) any of the fees payable by a Model 2 Borrower to Lendy pursuant to a Model 2 Borrower Loan?

DISTRIBUTION OF SECURITY PROCEEDS

(10) Should the Secured Liabilities (as defined in the relevant debenture) be discharged *pro rata* between Lendy on the one hand, and Model 2 Investors and/or Model 2 Transferees on the other hand, or in some other manner?

46. Ms Toube and Mr Gledhill agreed that it would be most convenient to deal with the issues in the order: 1-5, 8, 6-7 and 9-10 (in other words taking issue 8 out of order). This is because the

answers to issue 8 are, they both accepted, of central importance to issues 6-7 and 9-10, and the answers to those issues may depend on the answers to issue 8. I will deal with the issues in that order.

ISSUES (1) – (4): MODEL 1 BORROWER LOANS AND INVESTOR TERMS

MODEL 1 DOCUMENTS

47. Before addressing issues (1)-(4), all of which relate to the claims of Model 1 Investors, I will describe the documents produced by Lendy which govern the relationship between: (a) Lendy and the Model 1 Borrowers; and (b) Lendy and the Model 1 Investors. I will then set out what has been agreed between Ms Toube and Mr Gledhill about the nature of the contractual relationship between Lendy and Model 1 Borrowers and Lendy and Model 1 Investors and I will say why I accept what they have agreed between them.

48. There are four standard documents which apply to Lendy's contractual relationship with Model 1 Borrowers and Model 1 Investors ("Model 1 Standard Documents"):
    (a) a Loan agreement between the Model 1 Borrower and Lendy setting out the terms on which Lendy lent money to Model 1 Borrowers ("Model 1 Borrower Loan Agreement");
    (b) a Debenture between the Model 1 Borrower and Lendy providing security for the relevant Model 1 Borrower Loan ("Model 1 Debenture");
    (c) where relevant, a Guarantee to support a Model 1 Borrower's payment obligations under the Model 1 Borrower Loan Agreement to Lendy ("Model 1 Guarantee"); and
    (d) Terms and conditions between Lendy and Model 1 Investors setting out the terms on which Model 1 Investors lent money to Lendy, published on the Lendy Platform ("Model 1 Investor Terms").

49. Mr Webb says, in his Second Witness Statement, that Model 1 Investor Terms were uploaded to the Lendy Platform on 6 July 2017. He believes, based upon the Applicants' enquiries, that the only alteration carried out to the Model 1 Investor Terms after 6 July 2017 was that the definition of Lendy in the earlier version was "Saving Stream" whereas in the later version it was "Lendy". Mr Webb produces both versions as exhibits to his third witness statement dated 17 September 2020.

50. There were "back-to-back" loans from Lendy to Model 1 Borrowers pursuant to the Model 1 Borrower Loan Agreement and security was provided to Lendy for Model 1 Borrower Loans by the Model 1 Debenture and Model 1 Guarantee (hereinafter referred to together as the "Model 1 Security"). Mr Webb exhibits to his Second Witness statement copies of the Model 1 Borrower Loan Agreement, Model 1 Debenture and Model 1 Guarantee. He does not suggest that the terms of any of those documents ever altered, and it is agreed between counsel that they did not.

51. Ms Toube and Mr Gledhill agree that, in borrowing from Model 1 Investors, Lendy acted as principal and not as agent for the Model 1 Investors and that, in advancing loans to Model 1 borrowing, and taking Model 1 Security to secure repayment of the Model 1 borrowing, Lendy acted as principal and not as agent for the Model 1 Borrowers.

52. Having reviewed the Model 1 Standard Documents, I am satisfied that Ms Toube and Mr Gledhill are right to agree that Lendy contracted as principal in borrowing from Model 1 Investors and in lending to Model 1 Borrowers. The following terms of the Model 1 Standard Documents support that conclusion:
    (a) both the Model 1 Borrower Loan Agreement and the Model 1 Debenture identify Lendy as the lender to Model 1 Borrowers;
    (b) clause 2 of the Model 1 Borrower Loan Agreement describes the rights and obligations under that agreement as being rights and obligations of Lendy as lender;
    (c) clause 16.1 of the Model 1 Borrower Loan Agreement states that "the Lender [i.e. Lendy] may assign any of its rights under the Finance Documents";
    (d) under clause 3 of the Model 1 Debenture, security is granted by the Model 1 Borrower to Lendy;
    (e) clause 20.1 of the Model 1 Debenture provides that Lendy is entitled to receive the entire proceeds of the security provided by that debenture up to the value of: (i) the costs, charges and expenses incurred by or on behalf of Lendy (and any Receiver, Delegate, attorney or agent appointed by Lendy) under or in connection with the debenture, and of all remuneration due to any Receiver under or in connection with the debenture; and (ii) the Secured Liabilities (as defined in the debenture) which are owing to Lendy. The Secured Liabilities include all monies owing by the Model 1 Borrower to Lendy under the Model 1 Borrower Loan Agreement. Any remaining surplus is payable to the Model 1 Borrower. So the Model 1 Debenture secures money owed by the Model 1 Borrower to Lendy, not any money owed to Model 1 Investors;
    (f) the Model 1 Guarantee is a guarantee of the debt owed to Lendy under the Model 1 Borrower Loan Agreement; and

(g) clause 4.5 of the Model 1 Investor Terms states that *"by funding a loan, you are agreeing to enter into a loan agreement with Lendy."*

53. None of the Model 1 Standard Documents appear to me (and neither Ms Toube nor Mr Gledhill suggested that they did) to contain any wording that suggests that Lendy was acting as agent for: (a) Model 1 Investors in advancing funds contributed by them towards a Model 1 Borrower Loan to the relevant Model 1 Borrower; or (b) Model 1 Borrowers in collecting Model 1 Investors' money to fund the advance of the relevant Model 1 Borrower Loan.

ISSUE (1)

54. Issue (1) is - "*Do the Model 1 Investors (in their capacity as such) have any claim other than an unsecured provable claim against Lendy?*"

55. Ms Toube, for the Applicants, and Mr Gledhill, for Ms Taylor, agree that the answer to this issue is "no". Ms Toube who was to argue that the answer was "yes", if she sensibly could, accepts that no argument to that effect can properly be constructed. Counsel have nonetheless asked me to make a declaration to that effect.

56. In order to consider whether or not to make that declaration (or the opposite declaration), it is necessary for me to consider the evidence before me and to decide whether the answer to Issue 1 is "no", as agreed between Ms Toube and Mr Gledhill.

57. Each Model 1 Investor chose which Model 1 Borrower Loan they wished to participate in funding. They did so by indicating, on the Lendy Platform, that they wished to participate in funding a particular Model 1 Borrower Loan and how much they were willing to fund of it. It was only once sufficient money had been committed by Model 1 Investors to fund the particular Model 1 Borrower Loan that the Model 1 Borrower Loan was said to "go live" on the Lendy Platform, and Lendy would commit to funding the relevant Model 1 Borrower Loan.

58. Once the Model 1 Borrower Loan was advanced, Lendy treated the Model 1 Investors who contributed a part of the relevant Model 1 Borrower Loan as having the benefit of that part, for certain purposes, so that:
    (a) the Model 1 Investor could, using the Lendy Platform, transfer to a Model 1 Transferee their part of the relevant Model 1 Borrower Loan; and

(b) the amount that the Model 1 Investor/Transferee would receive and when they would receive it was determined, according to the Model 1 Investor Terms, by how the Model 1 Borrower Loan performed after it was advanced. In particular:
(i) clause 4(6) stated: *"The loan will remain in place until the borrower repays the loan. Upon which time the funds plus interest earned will be made available to you for withdrawal or reinvestment*"; and
(ii) if enforcement action was taken then, in accordance with clause 5(4), the proceeds of that enforcement action would be used first to repay the principal amount of the Model 1 Borrower Loan provided by the relevant Model 1 Investors, then fees due to Lendy and then interest due to the relevant Model 1 Investors.

59. The way in which Lendy presented the investment opportunity to Model 1 Investors and when and how much Model 1 Investors got back was therefore tied to the performance of the Model 1 Borrower Loan that they had chosen to participate in funding.

60. When Lendy changed from the Model 1 structure of lending to the Model 2 structure of lending, from around mid-2015, it uploaded an explanatory note onto the Lendy Platform to explain the change. The substance of that note was that Lendy was changing the structure of the lending, so that it would act as agent for both Model 2 Investors and Model 2 Borrowers in order to avoid any possibility of an Administrator of Lendy treating the proceeds of Model 2 Borrower loans as being available for *pari passu* distribution to all investors. The change from the Model 1 structure to the Model 2 structure was therefore presented as a means of ensuring that Model 2 Investors would have direct rights to recover their investment and any interest they were entitled to from the Model 2 Borrower Loan that they had chosen to fund. The mechanism chosen to achieve that certainty was to provide for the Model 2 Investors to contract directly with the Model 2 Borrowers and for Lendy to act as agent on behalf of both.

61. The fact that Lendy expressed concern in its note explaining the switch from the Model 1 structure to the Model 2 structure that an Administrator of Lendy might treat the proceeds of Model 1 Borrower Loans as available for *pari passu* distribution amongst Lendy's unsecured creditors does not mean that now the Applicants have been appointed as Administrators of Lendy, Model 1 Investors must be treated as unsecured creditors of Lendy (or that the proceeds of Model 1 Borrower Loans are in fact available for *pari passu* distribution amongst Lendy's unsecured creditors). In order to determine whether Model 1 Investors have any claim other than an unsecured claim against Lendy, it is necessary to consider whether there is any basis upon which the Model 1 Investors can be found to have any direct rights against the Model 1

Borrowers, whose loans they funded, or any interest in Model 1 Security pledged as security for the Model 1 Borrower Loans. The possibilities are:

(a) the Model 1 Investors who funded a particular Model 1 Borrower Loan to a Model 1 Borrower are legally and beneficially entitled, as against the Model 1 Borrower, to repayment of the loan and/or to enforce payment of the loan by having recourse to the Model 1 Security;

(b) Lendy has the legal right to require repayment of the Model 1 Borrower Loan by the Model 1 Borrower and/or to enforce payment of the loan by having recourse to the Model 1 Security, but they hold those rights, or some of them, on trust for the Model 1 Investors who funded the relevant Model 1 Borrower Loan; or

(c) the Model 1 Investors who funded a particular Model 1 Borrower Loan to a Model 1 Borrower hold some security either from Lendy or the Model 1 Borrower, for the payment of money to them.

62. The starting point is that Lendy acted as principal in: (a) borrowing money from Model 1 Investors; (b) advancing Model 1 Borrower Loans to Model 1 Borrowers; and (c) taking Model 1 Security from Model 1 Borrowers (see paragraphs 52-53 above) so the Model 1 Investor has a contract with Lendy and the Model 1 Borrower has a contract with Lendy. This rules out Model 1 Investors having any direct rights against Model 1 Borrowers or the Model 1 Security that Model 1 Borrowers provided to Lendy for Model 1 Borrower Loans.

63. The Model 1 Debenture grants security to Lendy, as lender, for the debt owed by the Model 1 Borrower to Lendy. Sums received by Lendy under the Model 1 Debenture are to be applied in accordance with a "waterfall" set out in clause 20.1 of the Debenture which does not mention any monies owed to Model 1 Investors. The Model 1 Guarantee guarantees payment of the debt owed by the Model 1 Borrower to Lendy. This rules out Model 1 Investors having any legal right to enforce Model 1 Security and further reinforces the conclusion that Lendy acted as principal in entering into Model 1 Borrower Loan Agreements.

64. As for whether Lendy held on trust (for the Model 1 Investors who funded the relevant Model 1 Borrower Loan) the rights it was granted under the Model 1 Loan Agreement and Model 1 Security it is necessary for Lendy to have made an express declaration of trust or that Lendy otherwise had the necessary intention to hold the benefit of those agreements (or some of them) on trust for the Model 1 Investors.

65. I have not seen, nor have I had brought to my attention, any document that could be regarded as an express declaration by Lendy that it held the rights that it was granted under the Model 1 Loan Agreements, or Model 1 Security, on trust for any Model 1 Investor (or anyone else).

66. The Model 1 Investor Terms and the note placed on the Lendy Platform to explain why Lendy was changing from the Model 1 structure to the Model 2 structure show that Lendy intended that Model 1 Investors who contributed towards a particular Model 1 Borrower Loan should have the timing and value of the return on their investment determined by what Lendy received from the Model 1 Borrower Loan that they funded. That does not however, in my judgment, mean that Lendy intended to hold the benefit of the Model 1 Borrower Loan Agreements and Model 1 Security on trust for the Model 1 Investors who funded the relevant loan and I find that Lendy did not have that intention for the following reasons:

    (a) as I have already noted, there is no express declaration of trust; had Lendy truly intended to hold the benefit of Model 1 Borrower Loans/Model 1 Security on trust for Model 1 Investors, then given the substantial amounts of money involved, I would expect there to be such an express declaration of trust;

    (b) not only is there no express declaration of trust, but there is nothing in the Model 1 Investor Terms which refers to anything being held on trust (or wording to that effect) for Model 1 Investors, nor do the Model 1 Investor Terms do anything other than describe the timing and value of the return to Model 1 Investors being determined by payments received and recoveries made from the relevant Model 1 Borrower Loans/Model 1 Security;

    (c) describing the Model 1 Investors' recoveries and their timing by reference to the amount recovered from and timing of recoveries from the Model 1 Borrowers/Model 1 Security is very different from treating the Model 1 Investors who participate in a particular Model 1 Borrower Loan as beneficial owners of a proportion of those recoveries;

    (d) any purported trust created by the Model 1 Investor Terms over security held under a Model 1 Debenture would, in any event, be unenforceable under Section 53 (1) (b) of the Law of Property Act 1925 because the asset that Model 1 Borrower Loans were secured upon was land and the Model 1 Investor Terms are not signed for or on behalf of Lendy as is required by Section 53 (1) (b) in order to create a security interest in land;

    (e) any purported trust would have the purpose of securing payment by Lendy to Model 1 Investors and as such would be a sub-mortgage in favour of Model 1 Investors of the Model 1 Debenture granted by the Model 1 Borrower to Lendy. Such a sub-mortgage would be void as against the Administrators of Lendy pursuant to Section 859h of the Companies Act 2006 (because it has not been registered, in the Register of Charges of Lendy, at Companies House); and

(f) not only was money received from a particular Model 1 Borrower or from the realisation of particular Model 1 Security not kept in a separate bank account from monies received from other Model 1 Borrowers/Model 1 Security, such receipts and realisations were paid into Lendy's trading account and used, by Lendy, together with other receipts to fund Lendy's trading and pay Model 1 Investors money due to them. Treating Model 1 Borrower receipts and Model 1 Security receipts in that way is inconsistent with the existence of a trust.

67. I accept that clause 5.2 of the Model 1 Investor Terms sets out the procedure for selling secured assets at an auction and provides that the net proceeds of sale would be used to *"settle amounts due"* which, in accordance with clause 5.2.4, includes the *"principal amount of the loan which was funded by, and is repayable to the Investors (allocated in proportion to the loan amounts funded)"*; and *"interest due to the Investors (allocated in proportion to the loan amounts funded)"*. However:
    (a) there is no evidence before me that any assets were ever sold at auction pursuant to clause 5.2.4 which the Model 1 Investors might claim a proprietary interest in;
    (b) the wording of the clause does not suggest that Model 1 Investors are to have any proprietary interest in the proceeds of an auction sale, but rather that Lendy will have an obligation to apply any proceeds of an auction sale in the manner set out in clause 5.2; and
    (c) again, if clause 5.2 did create a proprietary interest for Model 1 Investors, such a proprietary interest would amount to a sub-mortgage and would be void as against the Administrators of Lendy pursuant to Section 859h of the Companies Act 2006 (because it has not been registered, in the Register of Charges of Lendy, at Companies House).

ISSUE (2)

68. Issue (2) is - *"Do the proceeds of security of a Model 1 Borrower Loan form part of Lendy's general estate?"*

69. Mr Toube, for the Applicants, and Mr Gledhill, for the First Respondent, also agree that the answer is issue 2 is "yes" (Ms Toube having concluded that she is unable to construct an argument that the answer should be "no"). I have, however, again been asked to make a declaration to that effect and I will do so for the reasons that follow.

70. It is not suggested that anyone other than either: (a) Lendy; or (b) Model 1 Investors have any interest in the proceeds of the realisation of Model 1 Security.

71. As already noted, Lendy acted as principal in: (a) advancing Model 1 Borrower Loans to Model 1 Borrowers; and (b) taking Model 1 Security from Model 1 Borrowers. Having determined, in answer to Issue (1), that the Model 1 Investors only have unsecured claims against Lendy for the monies that they advanced to Lendy to fund particular Model 1 Borrower Loans (not rights in monies repaid by Model 1 Borrowers or received by Lendy from the realisation of Model 1 Security) it follows that the proceeds of Model 1 Security (for all the reasons I have given in answering Issue (1)), form part of Lendy's general estate.

ISSUE (3)

72. Issue (3) splits into two parts**:**
    (a) as regards its contractual liability to Model 1 Investors pursuant to the Model 1 Investor Terms, is Lendy liable to each Model 1 Investor only to the extent that Lendy is repaid by a Model 1 Borrower under, or makes recoveries in respect of, the relevant Model 1 Borrower Loan which that Model 1 Investor has funded?; and
    (b) in any event, are the provable claims of the Model 1 Investors limited or capped by reference to the amounts repaid to or recovered by Lendy in respect of the Model 1 Borrower Loans which those Model 1 Investors have funded?

73. Here there is disagreement between Ms Toube and Mr Gledhill about the answer to issue 3. Ms Toube, on behalf of the Applicants, says that the answer to (a) and (b) is "No" and Mr Gledhill, on behalf of Ms Taylor, says that the answer to both (a) and (b) is "Yes".

THE PARTIES POSITIONS IN SUMMARY

MS TAYLOR

74. Mr Gledhill for Ms Taylor says:

(a) it is possible to have a contract, pursuant to which a lender is to be paid from a designated fund and for the borrower's liability is to be limited to the value of that designated fund ("Limited Recourse");

(b) whether the loan is Limited Recourse or not depends upon an objective reading of the terms of the contract. In this case:

(i) the whole tenor of the Model 1 Investor Terms is to the effect that investors were investing in loans that Lendy had already written and the Lendy Platform contained key information about each of the loans so that Model 1 Investors could choose which to invest in. If in fact Lendy was obliged to repay the Model 1 Investors in full, regardless of how the loan that they chose performed, any information on the Lendy Platform about individual Model 1 Borrower Loans would have been at least superfluous if not misleading;

(ii) clause 4.6 of the Model 1 Investor Terms provided that Model 1 Investors would only be repaid once the Model 1 Borrower repaid the Model 1 Borrower Loan made to them by Lendy, which indicates that both the amount and the timing of the payment to Model 1 Investors depended on what was repaid and when under the Model 1 Borrower Loan;

(iii) Lendy: disclaimed any responsibility for the price achieved on the sale of property provided as security for the loan at auction (clause 2.3); guaranteed that Model 1 Borrower Loans would be legally enforceable (clause 4.4) and that the secured assets were not stolen or fake (clause 5.4.5); and set out a mechanism for paying Model 1 Investors the value of assets placed in auction which did not reach their reserve price (clause 4.5.3). No purpose would be served by any of these clauses unless Model 1 Investors only had Limited Recourse to repayments and realisations made in relation to the Model 1 Borrower Loan that they chose to invest in; and

(iv) clause 12.3 makes it clear that Lendy's liability to Model 1 Borrowers is limited to the amount recovered under the Model 1 Borrower Loan that they funded;

(c) the existence of the LPR (from January 2015) to compensate Model 1 Investors if there was a shortfall on recovery of the Model 1 Borrower Loan that they had part funded is inconsistent with Model 1 Borrowers not having only Limited Recourse to the proceeds of the Model 1 Borrower Loan that they part funded;

(d) Mr Gledhill draws my attention to Regulation 7 of the Unfair Terms in Consumer Contracts Regulations 1999 ("Regulation 7") which provides that in the case of consumer contracts if there is any doubt about the meaning of a written term, the interpretation most favourable to the consumer is to prevail (in this case, that is the meaning most favourable to Model 1 Investors). Mr Gledhill says however that here the meaning is clear and that is that Model 1 Investors have Limited Recourse to the proceeds of the Model 1 Borrower

Loan that they part fund, so Regulation 7 does not affect the conclusion that Model 1 Investors have Limited Recourse; and

(e) Mr Gledhill finally deals with a point raised by Ms Toube (see paragraph 75(f) below). Mr Gledhill says Ms Toube is wrong to submit that, even if Model 1 Investors have Limited Recourse outside of administration, inside administration Model 1 Investors can prove for any shortfall between the capital and interest which is owing to them by Lendy and the amount recovered from the Model 1 Borrower/Model 1 Security applicable to the Model 1 Borrower Loan they participated in ("Model 1 Shortfall"). Mr Gledhill says that Ms Toube's submission is wrong because, although he accepts that Model 1 Investors can submit proofs of debt for the full amount owed to them for capital and interest, when the Administrators come to admit the proofs for dividend purposes, they must admit them at the value of the relevant Model 1 Investor's part of the amount recovered under the relevant Model 1 Borrower Loan.

THE APPLICANTS

75. Ms Toube says:

(a) she accepts that: (i) it is possible to enter into a loan contract which provides for the lender to have Limited Recourse: (ii) whether the loan contract is Limited Recourse or not depends upon the true construction of the loan contract; and (iii) Lendy was not obliged to pay the Model 1 Investor until the Model 1 Borrower paid Lendy;

(b) Lendy represented to Model 1 Investors (when changing from the Model 1 structure to the Model 2 structure) that if there was a Model 1 Shortfall following realisation of Model 1 Security then Lendy would be responsible for paying that shortfall to Model 1 Investors;

(c) Model 1 Investors did not have sole recourse to the proceeds of the Model 1 Borrower Loan that they had funded. This undermines the rationale for limiting Model 1 Investors to recoveries made under the relevant Model 1 Borrower Loan;

(d) the requirement under clauses 4.5 and 4.6 of the Model 1 Investor Terms, that the Model 1 Investors' loans must remain in place until the relevant Model 1 Borrower Loan was repaid, merely specified the time for repayment, not the extent of the repayment;

(e) the LPR, created to provide compensation at Lendy's discretion, if there was a Model 1 Shortfall, merely dictated the source from which Model 1 Investors would be repaid, it is neutral on the question of whether the Model 1 structure was Limited Recourse. In any event, the LPR was only created in January 2015 and cannot therefore be relevant to Model 1 Investors who invested in Model 1 Borrower Loans entered into before January 2015; and

(f) the position is in any event different in insolvency. In *Re-Arm Asset Backed Securities SA* [2014] BCC 252 (Ch), David Richards J (as he then was) made it clear that even if creditors are subject to Limited Recourse, they are entitled to submit proofs of debt for the full amount of the debt owed to them, without reference to the recoveries from the designated fund to which they have Limited Recourse. This is obviously right, Ms Toube says, otherwise Model 1 Investors would be subject to a double discount. First, they have no proprietary interest in the security which is provided for the relevant Model 1 Borrower Loan that they have funded, they therefore have to share that security *pari passu* with other creditors. Second, having been forced to share that security *pari passu* with other creditors, they would then be forced (if Mr Gledhill is right) to discount their *pari passu* claim to the amount actually recovered from the Model 1 Borrower Borrower/Security which they had part funded.

DISCUSSION AND CONCLUSION ON ISSUE 3

THE CONTRACTUAL LIABILITY OF LENDY

76. I note that the following is common ground between Ms Toube and Mr Gledhill:
    (a) a loan contract can provide for the lender to have Limited Recourse against the borrower; and
    (b) whether or not the loan contract between Lendy and the Model 1 Investors is a Limited Recourse loan contract depends upon an objective reading of the Model 1 Investor Terms.

Legal Principles of the Construction of Contracts

77. Mr Gledhill and Ms Toube agree that the leading authorities on the construction of contracts are the Supreme Court cases of: (a) *Arnold v Britton* [2015] AC 1619 (SC); and (b) *Wood v Capita Insurance Services Limited* [2017] AC 1173 (SC).

78. In *Arnold v Britton,* Lord Neuberger gave the following guidance on interpreting written contracts (where relevant):
    "15. *When interpreting a written contract, the court is concerned to identify the intention of the parties by reference to* "what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean…" *And it does so by focussing on the meaning of the relevant words… in*

their documentary, factual and commercial context. That meaning has to be assessed in the light of (i) the natural and ordinary meaning of the clause, (ii) any other relevant provisions…, (iii) the overall purpose of the clause… (iv) the facts and circumstances known or assumed by the parties at the time that the document was executed, and (v) commercial common sense, but (vi) disregarding subjective evidence of any party's intentions.

16. For present purposes, I think it is important to emphasise seven factors.

17. First, the reliance placed in some cases on commercial common sense and surrounding circumstances ….should not be invoked to undervalue the importance of the language of the provision which is to be construed. The exercise of interpreting a provision involves identifying what the parties meant through the eyes of a reasonable reader, and, save perhaps in a very unusual case, that meaning is most obviously to be gleaned from the language of the provision…

18. Secondly, when it comes to considering the centrally relevant words to be interpreted, I accept that the less clear they are, or, to put it another way, the worse their drafting, the more ready the court can properly be to depart from their natural meaning… However, that does not justify the court embarking on an exercise of searching for, let alone constructing, drafting infelicities in order to facilitate a departure from the natural meaning. If there is a specific error in the drafting, it may often have no relevance to the issue of interpretation which the court has to resolve.

19. The third point… is that commercial common sense is not to be invoked retrospectively. The mere fact that a contractual arrangement, if interpreted according to its natural language, has worked out badly, or even disastrously, for one of the parties is not a reason for departing from the natural language. Commercial common sense is only relevant to the extent of how matters would or could have been perceived by the parties, or by reasonable people in the position of the parties, as at the date that the contract was made….

20. Fourthly, while commercial common sense is a very important factor to take into account when interpreting a contract, a court should be very slow to reject the natural meaning of a provision as correct simply because it appears to be a very imprudent term for one of the parties to have agreed, even ignoring the benefit of wisdom of hindsight. The purpose of interpretation is to identify what the parties have agreed, not what the court thinks that they should have agreed…

21. The fifth point concerns the facts known to the parties. When interpreting a contractual provision, one can only take into account facts or circumstances which existed at the time that the contract was made, and which were known or reasonably available to both parties….

22. Sixthly, in some cases, an event subsequently occurs which was plainly not intended or contemplated by the parties, judging from the language of their contract. In such a case, if it is clear what the parties would have intended, the court will give effect to that intention…."

[The seventh point was only relevant to the specific clause in the contract before the Supreme Court].

79. In *Wood v Capita Insurance Services Limited,* Lord Hodge was concerned to point out that there was, in his view, no inconsistency between the Supreme Court decision in *Rainy Sky SA v Kookmin Bank* [2011] 1 WLR 2900 (SC) (which appeared to place greater emphasis on the factual background to the interpretation of the relevant contractual clauses than Lord Neuberger did in *Arnold v Britton)* and the judgment of Lord Neuberger in *Arnold v Britton*. Lord Hodge said:

"*13. Textualism and contextualism are not conflicting paradigms in a battle for exclusive occupation of the field of contractual interpretation. Rather, the lawyer and the judge, when interpreting any contract, can use them as tools to ascertain the objective meaning of the language which the parties have chosen to express their agreement. The extent to which each tool will assist the court in its task will vary according to the circumstances of the particular agreement or agreements. Some agreements may be successfully interpreted principally by textual analysis, for example because of their sophistication and complexity and because they have been negotiated and prepared with the assistance of skilled professionals. The correct interpretation of other contracts may be achieved by a greater emphasis on the factual matrix, for example because of their informality, brevity or the absence of skilled professional assistance. But negotiators of complex formal contracts may often not achieve a logical and coherent text because of, for example, the conflicting aims of the parties, failures of communication, differing drafting practices, or deadlines which require the parties to compromise in order to reach agreement. There may often therefore be provisions in a detailed professionally drawn contract which lack clarity and the lawyer or judge in interpreting such provisions may be particularly helped by considering the factual matrix and the purpose of similar provisions in contracts of the same type…*

14. On the approach to contractual interpretation, the Rainy Sky and Arnold cases were saying the same thing".

Construing the Model 1 Investor Terms

80. It is common ground that the Model 1 Investor Terms that were placed on the Lendy Platform constitute the contract between Lendy and the Model 1 Investors and it is these terms that I need to decide the meaning of.

81. Taking into account the principles set out in *Arnold v Britton* and *Wood v Capita Insurance Services Ltd* to which I just referred, the approach that I intend to take to determine whether the Model 1 Investor Terms on their true construction, restrict Model 1 Investors to Limited Recourse

(that is, to their proportion of the proceeds of the Model 1 Borrower Loan which they partially funded) is as follows:

(a) the meaning of the words has to be assessed in the light of: - the natural and ordinary meaning of the clause any other relevant provisions; the overall purpose of the clause; the facts and circumstances known or assumed by the parties at the time that the document was executed; and commercial common sense; but disregarding subjective evidence of any party's intentions;

(b) I will first determine whether the wording of the relevant Model 1 Investor Terms, objectively viewed when read in the context of the Model 1 Investor Terms as a whole and having regard to their purpose, leads me to conclude that the Model 1 Investors have limited or unlimited recourse to Lendy;

(c) I will consider whether commercial common sense suggests that the objective and natural reading of the words which I have settled on, when read in context and having regard to the purpose of the relevant clauses, would produce a result which the parties cannot have intended because that meaning would not make commercial sense; however, in doing so I will be wary of imposing a different meaning to the meaning which I consider the words naturally bear, or treating what I consider it would have been sensible for the parties to have agreed as "commercial common sense"; and

(d) if the intention is not clear, then I may have regard to the factual circumstances in which the Model 1 Investor Terms were produced and placed on the Lendy Platform, so far as available to me. I accept that the guidance given in *Wood v Britton* is that the proper time to consider the factual background is when the relevant contract was entered into. Model 1 Borrower Loan Agreements were entered into on numerous dates between March 2014 and October 2015. However, the standard terms remained the same and, in my judgment, the appropriate time for considering the relevant factual background (if I need to consider it) is February/March 2014 because:

(i) the Model 1 Investor Terms were produced against the factual background as it then existed and not in the context of the factual background when each Model 1 Borrower Loan was entered into (in so far as it may have been any different); and

(ii) I simply do not have sufficient detailed and reliable evidence of the factual background to enable me to determine what, if any, relevant changes occurred to the background between February/March 2014 and October 2015 (when the Model 2 structure was introduced).

82. Regulation 7 provides that, if there is uncertainty as to the construction of a term in a consumer contract, then it must be interpreted in the manner most favourable to the consumer. Mr Gledhill accepts that Model 1 Investors acted as consumers and Regulation 7 is therefore engaged, but he says that the meaning of the Model 1 Investor Terms is sufficiently certain to mean that

Regulation 7 plays no part in their interpretation. If contrary to Mr Gledhill's submission, I find that the relevant meaning of the Model 1 Investor Terms is uncertain, I will consider the application of Regulation 7.

The Meaning of the Words

83. The clauses of the Model 1 Investor Terms to which I have been referred by Mr Gledhill and Ms Toube, and which I consider to be relevant to the Issue 3, are (in numerical order) as follows:
    (a) The introduction states: *"Lendy is an online crowd funded investment platform. Investment opportunities are made available through the Lendy Platform for investors to invest in loans made to borrowers who have satisfied Lendy Ltd that their security is creditworthy …."*. (This is not an operative clause but may be an aid to interpretation);
    (b) clause 1.1 states: *"Lendy is an online crowd funded investment platform for asset-backed secured loans. These terms and conditions regulate the relationship between Lendy and Lendy's Investors"*;
    (c) clause 1.2 states: *" Lendy permits investment (for a fixed return)* [in] *existing asset-backed secured loans already in place. These loans are secured against assets which are held in our possession for the duration of the loan"*;
    (d) clause 1.3 states: *"Should the borrower fail to repay the loan, the asset will be sold to recover the existing loan plus any interest owed"*;
    (e) clause 4.3 states: *"Existing Active Loans which Investors may fund are viewed in the Loans page. Information contained in the Loans page includes: the Loan Amount, the Security Value of the Asset, the Loan to Value Ratio (LTV), the description and a photo of the asset, a redacted valuation report where available, and a short description of the Borrower's requirements"*;
    (f) clause 4.4 states: *"Lendy guarantees the enforceability of all its existing Loan Agreements"*;
    (g) clause 4.5 states: *"By funding a loan you are agreeing to enter into a Loan Agreement with Lendy. Once you have invested in a loan, the funds cannot be removed for the duration of that loan"*;
    (h) clause 4.6 states *"The loan will remain in place until the borrower repays the loan, upon which time the funds plus interest earned will be made available to you for withdrawal or reinvestment"*;
    (i) clause 5.2 states *"If seven days have elapsed since the end of the Loan Term and we have had no response from the Borrower and the balance outstanding under the Loan Agreement has not been repaid, Lendy will, acting on behalf of the Investors, at its option,*

enforce the default procedures set out in the Loan Agreement" including: under 5.2.1 and 5.2.2, disposing of the asset at auction, and further:

(i) under 5.2.3, "*Lendy provides no guarantee or warranty that the Market Value of any Asset will be realised at auction*"; and

(ii) under 5.2.4, "*an additional administration fee of 5% of the loan value will be deducted from the net proceeds of sale of the Asset at auction .....Net proceeds of sale of Assets shall be used to settle amounts due in the following order: (1) principle amount of loan which was funded by, and is repayable to the Investors (allocated in proportion to the loan amounts funded); (2) fees due to Lendy in accordance with Lendy Ltd's Terms and Conditions; (3) interest due to the Investors (allocated in proportion to the loan amounts funded); and (4) the balance (if any) will be returned to the Borrower to their Nominated Account.*";

(j) clause 5.2.5 states: *"in the event that the asset turns out to be stolen or fake, Lendy will reimburse all invested funds to Investors"*;

(k) clause 12.3 provides that:

"Our liability to you on any basis whatsoever shall not exceed the total amount of revenue earned by Lendy in respect of transactions entered into by you through Lendy, save in relation to errors in the Market Value which can be shown, by reference to an appropriately qualified independent third party, were outside the Specific Tolerance at the time the valuation was made, in which case our liability to you shall not exceed the proportion of the principal amount of the loan which was funded by you.";

(l) clause 12.4 provides that: *"We shall not be liable for any loss or damage arising out of or in connection with:….fraud on the part of the Borrower …"*; and

(m) relevant defined terms are set out at clause 17 and include:

-*"'Assets' means property owned by the Borrower that is pledged by the Borrower and accepted by Lendy, at its sole discretion, as security for proposed loans" ;*

-*"'Borrower' means a member …who borrows money under a Loan Agreement";*

"Lendy Client Deposit Account' means any segregated bank account we maintain with Barclays Bank (or such other UK bank as we may choose from time to time) for the sole purpose of holding funds to which Lendy members are beneficially entitled in accordance with these terms and conditions and/or any loan agreement";

-*"'Invest' means the irrevocable commitment by an Investor to fund a loan, or loans, in whole or in part and the subsequent transfer of funds from the Investors Account to the Lendy Client Deposit Account and then allocation to a Loan…";*

-*"'Loan Agreement' means the form of credit agreement agreed by the Borrower";*

-*"'Loan Term' means the duration of the loan specified in the Loan Agreement";*

-*"'Market Value' means the price which we believe the Asset will sell for on the open market from time to time, as determined by the valuer acting on our behalf;*

-*"'Investor' means a Lendy Member who places money into their Client Deposit Account and subsequently against a loan";* and

- *"'Specific Tolerance' means the following specified percentages of the Market Value of the Asset at the time of valuation by or on behalf of Lendy: (1) Vehicles: 50%; (2) Boats 50%; and (3) Aircraft 50% or* [(4)] *such other percentages as Lendy may from time to time notify to you"* .

84. I am satisfied that an objective reading of the clauses of the Model 1 Investor Terms, to which I refer in paragraph 83(a)-(l), having regard to the purpose of those terms, clearly shows that it is intended that Model 1 Investors should be limited in what they receive from Lendy to their proportionate part of total recoveries from the Model 1 Borrower Loan that they participated in, where this is less than the aggregate of the capital and interest to which they would otherwise be entitled. I have come to this conclusion for the following reasons:

(a) in my judgment, the operative clause which determines Lendy's liability to Model 1 Investors is clause 12.3. In common with many other clauses of the Model 1 Investor Terms, clause 12.3 is badly drafted, but it seems to me that the clause does make it clear that, (save where a Model 1 Borrower Loan has been advanced but the value of the Asset taken as security for that loan does not meet the Loan to Value criteria) Lendy's liability to Model 1 Investors is limited by clause 12.3 to what Lendy receives from the Model 1 Borrower Loan that the Model 1 Investor has chosen to invest in. The ordinary meaning of the words *"Our liability to you on any basis whatsoever shall not exceed the total amount of revenue earned by Lendy in respect of transactions entered into by you through Lendy…."* can in my judgment only bear that meaning;

(b) the remaining relevant terms of the Model 1 Investor Terms are consistent with my interpretation of the intention of clause 12.3:

(i) the introduction to the Model 1 Investor Terms refers to Model 1 Investors making an investment through the Lendy Platform in loans made to borrowers. This language is inconsistent with the Model 1 Investors merely making a loan to Lendy with the return to the Model 1 Investors being unaffected by the performance of the underlying Model 1 Borrower Loan which the Model 1 Investor chooses to participate in;

(ii) similarly the reference in clauses 1.1 and 1.2 to Lendy being *"a crowd funded investment platform for asset-backed secured loans"* and *"Lendy permits investment (for a fixed return) in existing asset backed secured loans already in*

place" suggests that what the Model 1 Investors are investing in is the asset-backed secured loans they choose to invest in, not merely making a loan to Lendy;

(iii) Lendy specifically accepts liability for: - security values being outside the "Specific Tolerances" (clause 12.3); - Model 1 Borrower Loans being unenforceable (clause 4.4); and - the secured asset being stolen or fake (clause 5.4.5). There is no reason for Lendy to accept liability for these specific matters, if Lendy is liable to each Model 1 Investor for the full value of the loan made by the investor to Lendy in any event;

(iv) Lendy also excludes liability for: - the price achieved on the sale of security at auction (clause 5.2.3); and - loss or damage arising from any fraud by the Model 1 Borrower (clause 12.4.4). Again, no purpose would be served by excluding Lendy's liability for these matters, if Lendy is liable to the Model 1 Borrower for the whole of the principal and interest due to the Model 1 Investor in any event;

(v) clause 5.2.4 sets out the order in which the net proceeds of sale of assets, held by Lendy as security for Model 1 Borrower Loans, which are sold at auction will be applied, as between Lendy and Model 1 Investors. If Lendy is liable to pay Model 1 Investors all of the principal and interest due to them, regardless of how much is realised at auction, for assets upon which Model 1 Borrower Loans are secured, then no purpose is served by clause 5.2.4 setting out the order of priority (as between Model 1 Investors and Lendy) for distribution of the net proceeds of sale of an asset sold at auction which was provided as security for a Model 1 Borrower Loan;

(vi) clause 5.3 provides a mechanism for crediting to Model 1 Investors the value of assets provided as security for Model 1 Borrower loans which Lendy seeks to realise by sale at auction but which do not meet their reserve price. There would be no need for such a clause if Model 1 Investors could look to Lendy to discharge principal and interest owed to them in full, regardless of whether an asset taken as security for a Model 1 Borrower Loan, when placed in an auction, meets its reserve price or not;

(vii) clause 4.3 sets out the information that will be provided on the Lendy Platform in relation to each Model 1 Borrower Loan. If the Model 1 Investors must be paid in full by Lendy regardless of the performance of the underlying Model 1 Borrower Loan which they chose to part fund it is unlikely that the Model 1 Investors would want or need so much information about the loan they were choosing to part fund, because their getting paid would depend upon the financial position of Lendy, rather than the performance of any particular loan; and

(viii) Ms Toube says that clause 4.6, which provides that Model 1 Investors Loans to Lendy must remain in place until the Model 1 Borrower Loan to which they relate

has been repaid, simply specifies when, rather than how much Model 1 Investors will be paid. I accept that clause 4.6 might be interpreted that way but in my view read in the context of the other clauses to which I have already referred, it is consistent with both the timing and amount of the repayment to the Model 1 Investor being determined by the timing and amount of the repayment of the Model 1 Borrower Loan in which the Model 1 Investor chose to invest; and

(c) Lendy presented itself and the Lendy Platform as carrying on the business of Peer to Peer lending, that is lending by the Model 1 Investors to the Model 1 Borrowers. Whilst the Model 1 structure did not involve pure Peer to Peer lending (because Lendy acted as principal in borrowing from Model 1 Investors and in lending to Model 1 Borrowers) making the return of Model 1 Investors dependent upon the performance of the underlying Model 1 Borrower Loan that they chose to participate in, is consistent with Lendy facilitating Peer to Peer lending, which Lendy presented itself to Model 1 Investors to be doing

Commercial Common Sense

85. If, as I have found the position to be, the underlying purpose of the Lendy Platform was to facilitate Peer to Peer lending by Model 1 Investors to Model 1 Borrowers, then restricting the Model 1 Investors' recovery to the amount realised from the Model 1 Borrower Loan makes commercial sense and Lendy paying the Model 1 Investors regardless of the performance of the underlying Model 1 Borrower Loan makes less commercial common sense. On the other hand, Lendy may have only chosen to go some way towards creating a pure Peer to Peer lending platform and to have decided to accept a liability to pay the Model 1 Investors in full, regardless of the performance of the underlying Model 1 Borrower Loan that they chose to invest in.

86. So, in my judgment, a recourse to commercial common sense does not assist in determining whether the Model 1 Investors only have Limited Recourse. Limited Recourse is at least consistent with my objective reading of the meaning of the Model 1 Investor Terms and does not therefore result in my having to reconsider whether that objective reading can have been what the parties intended.

Relevant Factual Background

87. Having come to the conclusion that the meaning of the Model 1 Investor Terms is clear, my task of construing the intention of the Model 1 Investor Terms is complete. It is neither necessary nor consistent with the guidance that I have outlined above for me to go further, and to have regard to

the relevant factual background in which the Model 1 Investor Terms were placed on the Lendy Platform in February/March 2014. For completeness however, I will say that, in my judgment, the relevant factual matrix in February/March 2014 supports my conclusion as to the meaning of the Model 1 Investor Terms. In particular:

(a) whilst the Model 1 structure did provide for Model 1 Investors to lend to Lendy and for Lendy to lend to Model 1 Borrowers, Lendy held itself out as a Peer to Peer lending platform. The whole purpose of a Peer to Peer lending platform is that it introduces people willing to lend to people who wish to borrow. The lender is not meant to be the platform operator (Lendy), but rather the individuals who choose to fund the particular loan;

(b) my construction is consistent with Model 1 Investors making a choice, as they did, as to which Model 1 Borrower Loans to invest in and how much to invest in that loan; and

(c) Ms Toube relies upon the explanatory note sent to investors explaining the change from the Model 1 structure to the Model 2 structure as consistent with her case that Lendy was liable to pay Model 1 Investors in full regardless of the performance of the underlying Model 1 Borrower Loan that they chose to participate in. Under the heading "Old Structure" the note says *"Lendy was responsible for covering all repayments and shortfalls as it was both the borrower and the lender."* There are three points to be made about this note:

(i) it purported to represent Lendy's view of the effect of the Model 1 Investor Terms. Lendy's subjective view, as a party to the Model 1 Investor Terms, of their meaning is not a permissible aid to the construction of the Model 1 Investor Terms;

(ii) the note was circulated long after the Model 1 Investor Terms were placed on the Lendy Platform and the view expressed in the explanatory note may or may not have been Lendy's view at that time; Lendy's view is therefore not only an impermissible aid to interpretation, but it was also not a view expressed at what I consider to be the relevant time for considering the factual background (when the Model 1 Investor Terms were placed on the Lendy Platform, in March 2014); and

(iii) in my view, the note, when read as a whole, suggests that Lendy was unsure of whether it was liable to discharge a Model 1 Shortfall. The first page of the note under the heading *"New Structure"* says *"When you invested in a loan, we kept detailed records of this, but an administrator <u>may</u> consider it a pari passu risk … In the event of Lendy Ltd's (highly unlikely) bankruptcy. One bad loan, could in theory, undermine the rest."* (Emphasis added.) This does not suggest that Lendy was sure that it would be liable to make up any shortfall (because one bad loan would only undermine the rest if Lendy was liable to discharge a Model 1 Shortfall), but rather that it considered that it was possible that it may be.

88. Ms Toube suggested that the LPR merely identified a source from which Model 1 Investors might be paid. However, it is clear to me that the whole purpose of the LPR was to provide comfort to Model 1 Investors that, if there was a Model 1 Shortfall in recovery from the Model 1 Borrower Loan in which they had participated, there was a source from which they could be compensated for the effect of that shortfall upon them. They would only need compensation if the effect of a Model 1 Shortfall was that there would be a shortfall in payment of capital and interest to the relevant Model 1 Investors. Nonetheless, the LPR was only introduced in January 2015 and it was therefore not part of the factual matrix at the time that the Model 1 Investor Terms were placed on the Lendy Platform (February/March 2014), and as I have decided that that was the appropriate date at which to consider the factual background, I do not consider that the existence of the LPR is a matter that could have influenced my construction of the Model 1 Investor Terms had it been necessary for me to have regard to the factual background.

Regulation 7

89. As to Regulation 7, it only applies if the meaning of the Model 1 Investor Terms is unclear and in my judgment their meaning is not unclear, therefore Regulation 7 is not applicable in this case.

ARE THE MODEL 1 INVESTORS' PROVABLE CLAIMS IN LENDY'S ADMINISTRATION LIMITED OR CAPPED?

90. Mr Gledhill accepts that the judgment of David Richards J (as he then was) in *Re Arm* is authority for the proposition that a creditor who has Limited Recourse to an asset of a debtor for a debt owed to them by the debtor may nonetheless submit a proof of debt for the full amount of their claim in that debtor's insolvency.

91. Mr Gledhill says, however, that when an Administrator (or Liquidator) comes to consider the value at which they should admit such a proof of debt for dividend purposes, they must treat the proof of debt as a claim for a contingent debt, the contingency being the realisation of the asset to which the creditor may have recourse. Where the limited recourse funds have already been realised then the contingency will have crystallised and the proof of debt should be admitted at the value actually realised for the assets (if this is less than the total value of the debt). Where the assets/funds have not yet been realised, then they must be valued, and if valued at less than the outstanding debt, the proof of debt should be admitted at that figure.

92. Ms Toube disputes that Model 1 Investor claims should be valued in this way. She maintains that Model 1 Investors would, if Mr Gledhill is right, suffer a double discount, namely: (a) having to share the proceeds of the relevant Model 1 Borrower Loan with other creditors of Lendy; and (b) only being able to prove for the amount actually recovered from the relevant Model 1 Borrower Loan rather than the full amount of their debt.

93. I asked counsel whether in light of the position taken by Mr Gledhill, further amendment to part (b) of Issue 3 was required because it refers to "provable claims" rather than the value at which the Model 1 Investor' s proofs of debt should be admitted for dividend. Both counsel agreed that the Administrators need directions from the Court as to the value at which Model 1 Investor claims should be admitted to proof and they both agreed that issue 3(b) should be taken to encompass a request that the Court address that question without the need for any formal amendment of issue 3(b).

94. I will deal first with Ms Toube's submission, that if Model 1 Investors have their proofs of debt valued in accordance with the relevant Model 1 Investor's proportion of the realisations of the relevant Model 1 Borrower Loan (where this is less than the total value of principal and interest owed to them) the relevant Model 1 Investor suffers a double discount.

95. I do not accept that there is any element of double discount. The fact that the Model 1 Investors have no proprietary claims against the proceeds of Model 1 Borrower Loans/Security is a consequence of their status as unsecured creditors (in accordance with the agreed answer to Issue (1)). That is not a discount. The Limited Recourse that I have found Model 1 Investors have against Lendy, outside of insolvency, might be regarded as a discount, but it is a consequence of the loan contract that Model 1 Investors entered into with Lendy, which I have found was intended to place that restriction on Model 1 Investors rights to recover against Lendy.

96. I turn now to the decision of David Richards J (as he then was). In *Re Arm*, David Richards J was considering a very different situation to the present. Arm was a Luxembourg registered company and the question was whether the English court had jurisdiction to wind it up. David Richards J took the view that the EC Regulation on Insolvency Proceedings (under which the petitioner sought to establish the jurisdiction of the English court) only applied if Arm was insolvent. He considered that, although Arm's bondholders only had Limited Recourse to the proceeds of certain American life assurance policies (and possibly some bonds), as a matter of ordinary language Arm was insolvent in that the value of the life assurance policies was less than the face value of the bonds. He said that it was useful to test that conclusion against what the bondholders

could prove for in a liquidation of Arm and he said it was his *"clear view"* that they could prove for the face value of their debts.

97. David Richards J does not explain why he was of the "clear view" that bondholders could submit proofs of debt for the face value of their debts, or what the implications of that were for the value at which the bondholders claims should be admitted for dividend (the issue in this case). The remarks are, in my judgment, obiter as David Richards J made them merely to test the conclusion he had already come to, that Arm was insolvent as a matter of ordinary language. I proceed with caution therefore in considering the scope of the decision of David Richards J in *Re Arm* as it applies to the circumstances of this case.

98. Before considering whether Mr Gledhill is right, in submitting that Model 1 Investors should be treated by the Applicants (acting as Administrators of Lendy) as contingent creditors, I will comment on how contractual claims are treated generally for the purposes of admitting them for dividend in a liquidation/administration.

99. When a creditor submits a proof of debt which is based upon their claim under a contract, the proof of debt is valued for dividend purposes at the sum which would be required (if paid in full) to place them in the position that they would have been in had the contract been performed. That will commonly include a claim for loss of profit. In the case of a loan agreement, for example, the claim will include contractual interest, not just the return of capital (at least up to the commencement of the administration/liquidation of the debtor).

100. As a matter of principle, I see no reason why a creditor who agrees that their claim will be limited to the value of certain debtors' assets should not also have their proof of debt limited to the value of the assets that they have agreed their claim will be limited by. That is their contractual entitlement in the same way as a contract which provided for the sale of an asset to a creditor, but which asset was not transferred to the creditor, will (absent rescission of the contract) have their proof of debt valued according to the value of the asset, not what they agreed to pay for it.

101. Given my finding that the Model 1 Investor Terms provide that Model 1 Investors' contractual entitlement was capped at their proportion of the realisations from the Model 1 Investor Loan that they participated in, I see no reason why the value at which their proofs of debt should be admitted for dividend purposes should be any different. The analysis as to exactly how the Model 1 Investor claims should be categorised (contingent claim or otherwise) is in my judgment secondary to that underlying principle.

102. In addition to there being, in my judgment, no reason why Model 1 Investors' proofs of debt should not be valued by the Applicants in accordance with their Limited Recourse contractual entitlements (even if they can be submitted at the full value of capital and interest outstanding), there is a practical reason for allowing or expecting that a creditor who has Limited Recourse to the assets of their insolvent debtor should nonetheless submit a proof of debt without regard to that Limited Recourse. In *Re Arm,* the creditors were unlikely to have known what had been or was likely to be recovered from the Life Assurance policies to which they had Limited Recourse and here the Model 1 Investors certainly would not know (unless Lendy told them) what their proportion of the recoveries from the Model 1 Borrower Loan/Security in which they had participated was or was likely to be. In both cases, the only value that the creditors/Model 1 Investors could realistically put on their proofs of debt is the full value of capital and interest due to them. Valuing the proof of debt, in my judgment, is a different issue and should be done in accordance with (what I have found to be) the Model 1 Investors' Limited Recourse contractual entitlement.

103. As I have said, Mr Gledhill suggests that the Model 1 Investor claims should be treated as contingent liabilities falling within the definition of "Debts" in rule 14.1(5) of the Insolvency Rules 1986 (as amended) and may be proved for as such. The contingency being the final realisation of all monies and security from the Model 1 Borrower Loan which the relevant Model 1 Investor participated in.

104. There is no doubt in my mind that Model 1 Investors are present creditors of Lendy (not contingent creditors). Their status as creditors does not depend upon any contingency. Rather, in my view, the debt that is owed to a Model 1 Investor is of an uncertain amount, unless and until the relevant Model 1 Borrower Loan in which they participated and its security has been fully realised. If all sums that can be realised from the Model 1 Borrower and Model 1 Security in relation to a particular loan have been realised, then the claim of the Model 1 Investor is for the lower of the capital and interest due to them or their proportion (that is the proportion of the Model 1 Borrower Loan that they have funded) of the overall recoveries from the relevant Model 1 Borrower Loan. Where there may be further realisations either from Model 1 Borrowers or Model 1 Security, then the Applicants, as Administrators of Lendy, will have to assess the value of the Model 1 Investor's claim according to what has already been realised from the relevant Model 1 Borrower Loan Security, and what they consider is the likely value of future realisations in relation to the relevant Model 1 Borrower Loan.

105. Finally, and for the avoidance of doubt, I have proceeded upon the basis, as Mr Gledhill suggests, that the decision of David Richards J in *Re Arm* can be distinguished on the basis that the Judge was talking about the value at which creditors who are subject to Limited Recourse can submit proofs of debt, rather than the question of the value at which the Administrators of Lendy should admit Model 1 Investors' proofs of debt for dividend. If the decision of David Richards J cannot be distinguished as I have decided it can be, then, with respect, I decline to follow the decision of David Richards J (as he then was) in *Re Arm* on the basis that: (a) his comments are obiter and therefore not binding on me; (b) he does not explain why he came to the conclusion that he did; and (c) (if his decision extends to the value at which Applicants admit proofs of debt, which I have found it does not) I consider it to be clearly wrong as it fails to give effect to the proper calculation of proofs of debt which are based on contractual claims.

ISSUE (4)

106. Issue (4) is – *"If the answer to the question in issue (3) is 'yes', should the Model 1 Investors' contractual claims be valued in an amount equal to the gross proceeds received by Lendy for the relevant Model 1 Borrower Loan or the net proceeds of that Model 1 Borrower Loan (taking into account the costs of realisation)?"*.

107. I have found that the answer to Issue 3 is yes. Happily Ms Toube and Mr Gledhill are agreed that in those circumstances the answer to issue 4 is "gross".

108. I am content that that is the correct answer because it is agreed between Ms Toube and Mr Gledhill that the only contractual term entitling Lendy to charge a fee for its administration costs is cause 5.2.4 which provides for Lendy to charge a fee of 5% if there is an auction sale, and I am told that there have not been any auction sales.

ISSUES (5)-(10): MODEL 2 BORROWER LOANS AND MODEL 2 INVESTOR TERMS

109. I will deal with the remaining issues in the order that Ms Toube and Mr Gledhill have agreed that they should be dealt with, namely 5,8, 6-7 and 9-10. Before dealing with the first of those

issues, I will set out details of the agreements that Lendy produced for the Model 2 structure, some general background to the introduction of the Model 2 structure by Lendy, and I will record some points about that structure which have been agreed between Ms Toube and Mr Gledhill.

110. The standard Model 2 documents ("Model 2 Standard Documents") are:

a. Model 2 Borrower Loan Agreements entered into by (i) the Model 2 Borrower and (ii) Lendy as agent for the Model 2 Investors. There is a different form of Model 2 Borrower Loan Agreement for individual borrowers and corporate borrowers;

b. a Model 2 term sheet which contains the commercial terms of each loan, signed by the Model 2 Borrower and Lendy ("Model 2 Borrower Term Sheet");

c. terms and conditions for borrowers which are incorporated by reference into the Model 2 Borrower Loan Agreement (stated to be between (i) the Model 2 Borrower and (ii) Lendy as agent for unnamed Model 2 Investors);

d. security documents consisting of:

(i) a standard form of Model 2 Debenture for corporate borrowers, entered into by (1) the Model 2 Borrower and (2) SSSHL as security trustee, which creates fixed and floating security over all of the Model 2 Borrower's property ("Model 2 Debenture");

(ii) Model 2 Legal Charges for individual and corporate borrowers entered into by (1) the Model 2 Borrower and (2) SSSHL as security trustee, which creates security over real property ("Model 2 Legal Charge"); and

(iii) where the Model 2 Borrower is a corporate entity, an individual is required to execute a personal guarantee, granted by the guarantor to SSSHL as agent for the investors and Lendy ("Model 2 Guarantee"); and

e. the contractual relationship between Lendy and SSSHL (on the one hand) and the Model 2 Investors (on the other hand) is governed by the terms and conditions for investors ("Model 2 Investor Terms") which were published on the Lendy Platform and were amended in March 2018 ("Amended Model 2 Investor Terms").

111. Lendy explained the change from the Model 1 to the Model 2 structure to investors by putting a general update on the Lendy Platform before it commenced use of the Model 2 structure in October 2015. I have already referred to this update but will now set it out more fully. The explanation given by Lendy for moving from the Model 1 structure to the Model 2 structure was: *"When you invested in a loan, we kept detailed records of this, but an administrator may consider it a pari passu risk in the event of Lendy Ltd's (highly unlikely) bankruptcy. One bad loan, could in theory, undermine the rest. When we become a pure P2P platform, you lend to the borrower via Lendy Ltd and a "nominee company" called Saving Stream Security Holding Ltd, holds the security on your behalf. The purpose of the nominee company is to manage the investment on*

behalf of all the Lenders so that the borrower only has to deal with a single entity rather than 1000's of individuals which will constantly change as the loan parts are traded. This mitigates bankruptcy risk and the contagion of one bad loan will not affect the others. Saving Stream [i.e. Lendy] *will act as the agent and will manage - the origination of the loan, underwriting decisions, raising the capital on behalf of the lenders, perfecting the security, collecting repayments, distributing repayments to Lenders, paying monthly interest, managing the Lender database and various other activities on the Lenders behalf".*

112. The sense of the explanatory note (although it could have been clearer) was that under Model 2, it would be the Model 2 Investor who would be lending, as principal, to the Model 2 Borrower, and not Lendy.

113. As I will mention in due course (in relation to Issue 8) the exact extent to which Lendy acted as agent for Model 2 Investors is disputed between Mr Gledhill and Ms Toube, but for present purposes, it is agreed between Ms Toube and Mr Gledhill that Lendy did act as agent: (a) for Model 2 Borrowers in arranging to collect funds to fund Model 2 Borrower Loans from Model 2 Investors and entering into Model 2 Investor Terms with Model 2 Investors; and (b) for Model 2 Investors in advancing Model 2 Borrower Loans to Model 2 Borrowers and signing Model 2 Borrower Loan Agreements. The names of the Model 2 Investors who funded a particular Model 2 Borrower Loan were not disclosed to the Model 2 Borrower, but Lendy kept in its own books the details of the Model 2 Investors that funded each Model 2 Borrower and who were, in accordance with Ms Toube and Mr Gledhill's agreement, the lenders as principals to each Model 2 Borrower.

114. I accept that Ms Toube and Mr Gledhill are right to agree that Lendy acted as agent for Model 2 Borrowers and Model 2 Investors in the ways I have just described. The following contractual provisions support Ms Toube and Mr Gledhill's agreement:

(a) The Model 2 Borrower Loan Agreement:

(i) is expressed to be made between the Model 2 Borrower and Lendy *"as agent for the* [investors]". Lendy is referred to as *"the Agent"* throughout the Model 2 Borrower Loan agreement; and

(ii) recital (c) states: *"The Agent is entering into this agreement as the agent of the* [investors]";

(b) the Model 2 Investor Terms provide:

(i) at clause 1.2 that: *"*[Lendy] *is authorised by the* [investors] *to enter into the Loan Contract as agent for the* [investors]*";*

(ii) at clause 8.1 that: *"when you lend money on the platform you … appoint* [Lendy] *to act as agent on your behalf in relation to the loan and instruct* [Lendy] *to sign…the Loan Contract as agent on your behalf"*; and
(iii) at clause 7.8 that: *"a Loan Contract…is between the* [investor] *and the borrower.* [Lendy] *and/or Saving Stream Security Holding has no liability… in relation to the Loan Contract".*

ISSUE (5)

115. Issue (5) is- *"On a proper construction of clause 6.3 of the Model 2 Investor Terms, is the Model 2 Borrower required to pay the default interest to (i) the relevant Model 2 Investors and/or Model 2 Transferees, (ii) to Lendy (as principal) or (iii) in any other manner?"*

116. Clause 6.1 of the Model 2 Borrower Loan Agreement provides that the Model 2 Borrower shall pay interest on the Model 2 Borrower Loan at the interest rate which is stated in the Model 2 Borrower Term Sheet. In the Model 2 Borrower Term Sheet that interest rate is split between interest which is payable to Lendy and interest which is payable to Model 2 Investors. The Lendy standard interest rate is in the range of 0.2 - 0.5% per month from the date of loan agreement until repayment. Model 2 Investors standard interest is normally in the range 0.8%-1%, most commonly 1%.

117. Clause 6.3 of the Model 2 Borrower Loan Agreement provides:
"In addition to the interest payable under clause 6.1, if the Borrower fails to make any payment due under this agreement on the due date for payment, interest on the unpaid amount shall accrue daily, from the date of non-payment to the date of actual payment (both before and after judgment), at 3% per month above the aggregate Interest Rate."
("Default Interest")
The *"Interest Rate"* is effectively defined as the standard interest rate payable to Model 2 Investors plus the standard interest rate payable to Lendy, each as set out on the Model 2 Borrower Term Sheet.

118. The following points are agreed between Ms Toube and Mr Gledhill for Issue 5 (items (c)-(f) are principles of interpretation of agency contracts taken from *Bowstead & Reynolds on Agency (22nd edition 2020) ("Bowstead"*) which I will refer to in more detail below):

(a) Clause 6.3 of the Model 2 Borrower Loan Agreement does not say to whom Default Interest is payable;
(b) Lendy is entitled to collect Default Interest from the Model 2 Borrower;
(c) determining who has legal title to the chose in action constituting the right to sue for Default Interest also determines who has the right to sue the Model 2 Borrower for Default Interest;
(d) where a person contracts as agent for a principal, the contract is the contract of the principal and not the agent and, prima facie, the only person who can sue and be sued is the principal;
(e) the facts of a particular case may, however, lead to the conclusion that both the principal and the agent can sue and be sued, or even that only the agent can sue and be sued it depends on the intention of the parties, to be deduced from the nature and terms of the contract and surrounding circumstances and the test is objective; and
(f) if an agent signs an agreement indicating that they are signing as agent for and on behalf of the principal, the agent is deemed not to have contracted personally, unless it is plain from other parts of the document that the agent intended to be bound by the contract. If that is the case, then the conclusion is that the agent contracted as agent in some respects and as principle in others.

MS TAYLOR'S CASE

119. I will now summarise Mr Gledhill's case, on behalf of Ms Taylor. In doing so, for reasons of brevity, I will refer briefly to certain matters that I will explain in more detail later, when discussing and coming to my conclusions on Issue 5. Mr Gledhill says that:
(a) the question of who can sue the Model 2 Borrower direct for Default Interest depends upon the wording of the Model 2 Borrower Loan Agreement, construed against the admissible background, because it is the Model 2 Borrower Loan Agreement which provides, at clause 6.3, for the payment of Default Interest;
(b) whilst, for the purposes of the Model 2 Borrower Term Sheet, Lendy acts both as agent and principal, Lendy is specifically stated to act as agent, in signing the Model 2 Borrower Loan Agreement, for the Model 2 Investors who funded the Model 2 Borrower Loan. The prima facie position is therefore that Lendy acted as agent for the Model 2 Investors for all purposes in relation to the Model 2 Borrower Loan Agreement (including receiving Default Interest);
(c) in *Lederer v Allsopp LLP* [2018] EWHC 1425 (Ch), a borrower under a Model 2 Borrower Loan claimed that there had been a breach of an obligation to lend to it and the

borrower sought details of the names and addresses of the Model 2 Investors who had participated in its loan who were, on its case, principals to its loan. Zacaroli J found that Lendy acted only as agent and the Model 2 Investors who had participated in the loan were the *"real contracting party"*, and therefore the borrower was entitled to details of the Model 2 Investors who acted as principals in their loan. Mr Gledhill concedes that *Lederer* does not directly answer the question of whether Model 2 Investors can sue Model 2 Borrowers for Default Interest but it does, he says, answer the question of who may be sued by the Model 2 Borrower and Mr Gledhill says that an agent cannot generally be entitled to sue the other party to the contract if they are not also liable to that other party because there would be no consideration to support the liability of the other party to the agent;

(d) the Applicants' primary case is that all Default Interest is payable to Lendy for its own account but this would mean that if there was a default, Model 2 Investors would get no additional interest as a result of that default. Even Lendy, pre-administration, suggested that Model 2 Investors would receive some additional interest if a Model 2 Borrower Loan went into default (see bonus accrual below);

(e) the fact that Lendy was authorised to collect Default Interest from Model 2 Borrowers does not mean that it was entitled to keep it for its own account, or that Model 2 Investors could not also sue Model 2 Borrowers for Default Interest because:

(i) Lendy signed the Model 2 Borrower Loan Agreement as agent, and the starting point is that the right to enforce that contract lay with the Model 2 Investors, as principals;

(ii) nothing in the Model 2 Borrower Loan Agreement justifies the conclusion that Lendy could sue for Default Interest to the exclusion of Model 2 Investors;

(iii) the Model 2 Borrower Term Sheet specifies that part of the non-default interest rate goes to the Model 2 Investors and part to Lendy, but Lendy never had to sue for non-default interest because it was deducted from the advance, so the provisions of the Model 2 Borrower Term Sheet in relation to non-default interest are not relevant to the right to sue for Default Interest;

(iv) even if, internally, Default Interest defrayed Lendy's higher costs of administering overdue loans, the intention of the parties must be objectively assessed from the terms of the Model 2 Borrower Loan Agreement and clause 6.3 describes the charge as Default Interest, not costs or charges. Interest is a reward for the risk run by a lender in making a loan and not a fee, cost or charge for additional administrative work; and

(v) if it was intended that Lendy was to have the Default Interest this could have been put in a separate agreement (as the non-default interest was in the Model 2 Borrower Term Sheet), but instead it is in the Model 2 Borrower Loan Agreement, in respect of which Lendy is stated to act as agent.

(f) Lendy was authorised under the Regulated Activities Order ("RAO") by the FCA to operate a Peer-to-Peer lending platform. That authorisation provided for Lendy merely to facilitate the making of loans by lenders who joined its platform to borrowers, not to lend money itself, and interest is the reward for the risk taken by the Model 2 Investors in lending to the Model 2 Borrowers;

(g) if Lendy is entitled to Default Interest it creates a conflict between Lendy and the Model 2 Investors in a shortfall situation ("Model 2 Shortfall");

(h) clause 5.3 of the standard form of Model 2 Guarantee is consistent with the Model 2 Investors being entitled to Default Interest because it says "Lenders" shall not be entitled to receive interest under both the guarantee and the Model 2 Borrower Loan Agreement and "Lenders" are defined as the Model 2 Investors and not Lendy. Model 2 Borrowers would know the terms of the Model 2 Guarantee when entering into Model 2 Borrower Loan Agreements;

(i) the Applicants refer to clause 9 of the Model 2 Investor Terms as giving Lendy an entitlement to part of the Default Interest and clause 13.4 of the Amended Model 2 Investor Terms providing for all Default Interest to be paid to Lendy, but that cannot be right because: - - there is no basis for concluding that it was agreed between Model 2 Investors and Lendy that Lendy could charge Default Interest for its own account; and - even if this was agreed, investors could still sue Model 2 Borrowers for Default Interest because entitlement to sue for the Default Interest depends on the terms of the Model 2 Borrower Loan Agreement and not the Model 2 Investor Terms because Model 2 Borrowers are not party to the Model 2 Investor Terms; and

(j) the bonus accrual which Lendy said they would pay to Model 2 Investors if a Model 2 Borrower Loan went into default does not indicate that Default Interest should be paid to Lendy because: - Lendy only traded as a Peer-to-Peer platform for around five years and there were frequent changes to what it said it was offering to investors; - a bonus accrual was first mentioned in an email to Model 2 Investors dated 12 September 2017 but it does not mention Default Interest; - the Amended Recovery Policy does say that the bonus accrual is a proportion of Default Interest, but it did not appear on the Lendy Platform until around August 2018; and - Lendy cannot derogate from the rights that Model 2 Investors already had to the Default Interest, by merely mentioning Default Interest when telling Model 2 Investors about the bonus accrual, particularly when the bonus accrual was presented as a benefit to Model 2 Investors.

120. As for the Applicants' alternate case, that Default Interest should be split pro rata between Lendy and the Model 2 Investors in the same proportions as non-default interest, Mr Gledhill says:

(a) clause 6.3 of the Model 2 Borrower Loan Agreement which provides for Model 2 Borrowers to pay Default Interest is additional to and separate from clause 6.1 which provides for the payment of non-default interest (as set out in the Model 2 Borrower Term Sheet);

(b) if Default Interest was to be split between Lendy and Model 2 Investors in the same proportions as non-default interest, then the Model 2 Borrower Term Sheet should have said so; and

(c) Default Interest is in any event different from non-default interest: (i) Mr Powell and Mr Melton confirmed that they knew that Lendy charged Model 2 Borrowers non-default interest, but not Default Interest: (ii) non-default interest was deducted up front, so there was no need for Lendy to sue for it; and (iii) the Applicants' case that Default Interest covered the additional cost of administering loans in default is speculative and unlikely to be correct, given that Default Interest was so high.

THE APPLICANTS' CASE

121. Ms Toube's primary position, on behalf of the Applicants, is that Lendy is entitled to all of the Default Interest for its own account, but if that is wrong, Ms Toube's secondary case is that Default Interest should be shared pro rata between Lendy and the Model 2 Investors who participated in each Model 2 Borrower Loan Agreement in the same proportions in which they are entitled to non-default interest.

122. Ms Toube's primary case is based on the following:

(a) There is no suggestion in the Model 2 Investor Terms that Default Interest would be payable to Model 2 Investors; and

(b) the Amended Recovery Policy provided that a bonus accrual would be payable to Model 2 Investors. It describes the bonus accrual as being payable to Model 2 Investors: in the event that the Model 2 Borrower Loan that they participated in was not redeemed on the repayment date, the bonus accrual is described as part of the Default Interest. Model 2 Investors being entitled to all of the Default Interest is inconsistent with the bonus accrual being part of Default Interest.

123. Ms Toube's alternate case, that Default Interest should be shared pro rata between Model 2 Investors and Lendy in the proportions in which non-default interest is payable, is based on the following:

(a) clause 6.3 of the Model 2 Borrower Loan Agreement says that Default Interest is payable at 3% above the aggregate Interest Rate;

(b) the aggregate Interest Rate is the aggregate of the non-default interest payable to Lendy and the non-default interest payable to the Model 2 Investors, as set out in the Model 2 Borrower Term Sheet;

(c) as Default Interest is payable at 3% above the aggregate Interest Rate, the most natural and fair construction of clause 6.3 is that Default Interest should be split pro rata between Lendy and the Model 2 Investors by reference to the non-default interest payable to each of them as set out in the relevant Model 2 Borrower Term Sheet (generally 1% per month to the Model 2 Investors and 0.5% per month to Lendy); and

(d) it makes commercial sense for Default Interest to be split in the same proportions as non-default interest.

124. Ms Toube's answers to the points made by Mr Gledhill are as follows:

(a) Mr Gledhill does not challenge Lendy's claim for non-default interest which the Model 2 Borrower Term Sheet provides for (or its claims for fees). Lendy therefore must be taken to have contracted as principal in relation to non-default interest (and fees). In the same way, Lendy contracted as principal for Default Interest;

(b) the standard form Model 2 Guarantee, at clause 5.1 says that the guarantor pays interest to the "Beneficiaries" at the rate set out in clause 6.3 of the Model 2 Borrower Loan Agreement and the "Beneficiaries" are defined as both the Model 2 Investors and Lendy, so confirming that Lendy is entitled to interest as principal. Whilst clause 5.3 of the Model 2 Guarantee only refers to Model 2 Investors being prevented from charging interest under the personal guarantee as well as the Model 2 Borrower Loan Agreement, this simply means that that restriction does not apply to Lendy, rather than being an indication that only Model 2 Investors and not Lendy are entitled to Default Interest;

(c) *Lederer* is only relevant in determining liability under the Model 2 Borrower Loan Agreement and not rights under it;

(d) whilst the regulatory regime under which Lendy operated is relevant to the construction of the Model 2 Borrower Loan Agreement, it is not determinative; and, in any event, if charging Default Interest is contrary to the RAO, so is charging non-default interest and Mr Gledhill does not challenge Lendy's right to receive non-default interest for its own account;

(e) Mr Gledhill refers to fees and non-default interest not being paid by Model 2 Borrowers to Lendy because they are deducted from the loan advance to the Model 2 Borrower, but legally the deduction of non-default interest and costs from the advance to the Model 2 Borrower amounts to payment by the borrower; and

(f) interest is not just a reward payable to a lender for the risk they take in lending. In any event, Mr Gledhill does not challenge Lendy's entitlement to non-default interest, so he

can hardly maintain a stance that the Default Interest must be paid to the Model 2 Investors for that reason.

DISCUSSION AND CONCLUSION ON ISSUE 5

APPLICABLE PRINCIPLES

125. The approach which I will take to determining who, as between Lendy, on the one hand, and the Model 2 Investors who participated in the relevant Model 2 Borrower Loan, on the other, is entitled to Default Interest (or if not exclusively, in what proportions) is as follows:

(a) I will apply the principles which Ms Toube and Mr Gledhill agreed apply specifically to the interpretation of agency contracts (as set out in *Bowstead*) namely:

(i) if the Model 2 Investors have legal title to the chose in action represented by the claim against Model 2 Borrowers for Default Interest, then the Model 2 Investors will have the right to all the Default Interest, even if Lendy can also sue for Default Interest (*Bowstead paragraphs* 6-099-6-100);

(ii) prime facie, where a person acts as agent, the contract is that of the principal and only the principal can sue or be sued (*Bowstead paragraph* 9-002);

(iii) that prime facie position may be displaced if, having regard to the nature and terms of the Model 2 Borrower Agreement and the surrounding circumstances, the intention of the parties is different to the prima facie position (*Bowstead paragraph 9-005*); and

(iv) if the agent signs a contract as agent they are deemed not to have contracted personally unless it is plain from other terms of the contract that the agent is to be bound by it, in which event, the agent may be taken to contract both as agent and principal (*Bowstead paragraphs* 9-036-9-037); and

(b) subject to those points, I will apply the principles set out by Lord Neuberger in *Arnold v Britton*, as clarified by Lord Hodge in *Wood v Capita Insurance Services Ltd*, in construing the Model 2 Borrower Loan Agreement (which provides for the payment of Default Interest) to decide, to whom it was intended that Default Interest should be paid (and if appropriate in what proportions) and if any applicable presumption is rebutted (see *paragraph* 81 above for those principles). For present purposes, the following summary of those principals suffices:

(i) the meaning of the words has to be assessed in the light of: the natural and ordinary meaning of the clause; any other relevant provisions; the overall purpose of the clause; the facts and circumstances known or assumed by the parties at the time that the document was executed; and commercial common sense; but disregarding subjective evidence of any party's intentions;

(ii) if the meaning of the wording of the clause is plain, then I should give effect to that plain meaning without reference to the factual background;

(iii) commercial common sense should be judged by reference to how matters would or could have been perceived by the parties or by reasonable people in the position of the parties, at the date the contract was made;

(iv) I should be slow to reject the natural meaning of the words simply because the natural meaning would produce a result which appears to be very imprudent for one of the parties;

(v) only facts and matters known to the parties when the contract was entered into can be taken into account; and

(vi) the extent to which textual analysis or contextual analysis is used depends on the circumstances of the particular case. Textual analysis of the contract alone may be sufficient if the wording is clear; but if it is not, more emphasis on a contextual analysis may be appropriate.

APPLYING THE BOWSTEAD PRINCIPLES

126. Each Model 2 Borrower Loan Agreement has been signed by Lendy as agent for the Model 2 Investors that participated in the relevant Model 2 Borrower Loan. In consequence, Lendy is deemed not to have contracted personally in relation to the Model 2 Borrower Loan Agreements unless it is apparent from reading the Model 2 Borrower Loan Agreement as a whole, that it was intended that Lendy would also act as principal (for the purposes of all or part of the Model 2 Borrower Loan Agreement).

127. I am not satisfied that Lendy should be deemed to have acted solely as agent for the Model 2 Investors and not personally (as principal) for any reason in relation to the Model 2 Borrower Loan Agreement. I have come to this conclusion for the following reasons:

(a) Lendy signed the Model 2 Borrower Loan Agreements as agent for the Model 2 Investors and is therefore deemed to have contracted personally, unless it is plain from other parts of the Model 2 Borrower Loan Agreement that Lendy nonetheless intended to be bound by the Model 2 Borrower Loan Agreement (*Bowstead paragraph* 9-036);

(b) clause 6.1 of the Model 2 Borrower Loan Agreement states that the Model 2 Borrower must pay interest on the Loan at the Interest Rate and "Interest Rate" is defined as the Interest Rate set out in a the Model 2 Borrower Term Sheet. In my judgment this means that the Model 2 Borrower Term Sheet is incorporated into the Model 2 Borrower Loan Agreement;

(c) the Model 2 Borrower Term Sheet provides for the Model 2 Borrowers to pay non-default interest to Lendy and Model 2 Investors at different specified rates. Lendy has signed the Model 2 Borrower Term Sheet as principal;

(d) Lendy must therefore be acting as principal under the Model 2 Borrower Loan Agreement at least to the extent of the matters covered by the Model 2 Borrower Term Sheet (including non-default interest payable to it); and

(e) this means that I cannot conclude that Lendy is deemed to act as agent for the Model 2 Investors for all purposes under the Model 2 Borrower Loan Agreement.

128. Nonetheless, only the Model 2 Borrower Term Sheet which I have found to be part of the Model 2 Borrower Loan Agreement (by incorporation) specifically provides for Lendy to act as principal. In consequence, I consider the prima facie position to be that Lendy contracts as agent for Model 2 Investors in relation to all other aspects of the Model 2 Borrower Loan Agreement (including Default Interest) because Lendy has signed the Model 2 Borrower Loan Agreement as agent for the Model 2 Investors, so, prima facie, the legal right to sue for Default Interest is vested in the Model 2 Investors who participated in the relevant Model 2 Borrower Loan Agreement (*Bowstead paragraph* 9-002).

129. The prima facie conclusion that the legal title to the right to sue for Default Interest lies with the Model 2 Investors can be displaced if the intention of the parties, objectively ascertained, is that Lendy would have legal title to sue Model 2 Borrowers for Default Interest (*Bowstead paragraph* 9-005*).*

IS THE PRIMA FACIE CONCLUSION THAT MODEL 2 INVESTORS HAVE LEGAL TITLE TO THE DEFAULT INTEREST DISPLACED?

130. In *paragraph* 9-005 of *Bowstead*, it is suggested that the prima facie conclusion that the Model 2 Investors have the legal right to sue for Default Interest may be displaced if, having regard to the nature and terms of the Model 2 Borrower Loan Agreement and the surrounding circumstances, the intention of the parties is different to that prima facie position. I regard that as too general a statement of the principles to be applied in determining the intention of contracting parties under a written contract. I will instead apply the principles of contractual construction set out in the speech of Lord Neuberger in *Arnold v Britton,* as clarified by Lord Hodge in *Wood v Capita Insurance Services Ltd,* which I have summarised in paragraph 125(b) above in deciding whether the prima facie position is displaced.

Is the meaning of the words of Clause 6.3 plain?

131. If the meaning of the words used in the relevant clause of the Model 2 Borrower Loan Agreement are plain, then I should give effect to that plain meaning.

132. Clause 6.3 of the Model 2 Borrower Loan Agreement contains the obligation on Model 2 Borrowers to pay Default Interest and it provides as follows:
"if the borrower fails to make payment due under the agreement on the due date for payment, interest on the unpaid amount shall accrue daily, from the date of non-payment to the date of actual payment…. at 3% per month above the aggregate Interest Rate."

133. Clause 6.3 is silent (as Mr Gledhill and Ms Toube accept) on the question of who the Default interest is to be paid to and so its meaning, in this respect, is not plain.

Clause 6.3 read in the context of the Model 2 Borrower Loan Agreement as a whole

134. The only other clause of the Model 2 Borrower Loan Agreement that refers to interest is clause 6.1, which says that the Model 2 Borrowers must pay interest on the loan at the Interest Rate, which is defined as the interest rate for which the Model 2 Borrower Term Sheet provides.

135. The Model 2 Borrower Term Sheet specifies what non-default interest rates are payable by the Model 2 Borrower to both Model 2 Investors who participate in the Model 2 Borrower Loan and Lendy at the rates set out there.

136. The definition of "Interest Rate" in the Model 2 Borrower Loan Agreement is the aggregate of non-default interest payable to the Model 2 Investors and Lendy.

137. An objective reading of clause 6.1, read in conjunction with the Model 2 Borrower Term Sheet, gives no direct indication of the party to who the Default Interest provided for by clause 6.3 is to be paid. However, I consider that the contents of clause 6.1 of the Model 2 Borrower Loan Agreement when read in conjunction with the Model 2 Borrower Term Sheet provide some support for the prima facie conclusion that Default Interest is payable to Model 2 Investors for the following reasons:

(a) clause 6.1 provides that non-default interest is payable as set out in the Model 2 Term Sheet, thereby incorporating the provisions, as to non-default interest into the Model 2 Borrower Loan Agreement;

(b) the Model 2 Borrower Term Sheet provides for the payment of non-default interest to both the Model 2 Investors and Lendy. The Model 2 Borrower Term Sheet is signed by Lendy, as principal (unlike the Model 2 Borrower Loan Agreement which was signed by Lendy as agent for the Model 2 Investors); and

(c) the fact that Lendy signed the Model 2 Borrower Term Sheets as principal suggests that Lendy's entitlement to charge the Model 2 Borrowers non-default interest was deliberately included in the Model 2 Borrower Term Sheets and that the Model 2 Borrower Term Sheets were deliberately signed by Lendy as principal in order to ensure that Lendy had legal title as against the Model 2 Borrower to non-default interest. This in turn suggests that (consistent with the prima facie position) if Lendy was also intended to have legal title to sue Model 2 Borrowers for Default Interest, then Default Interest would have been included in the Model 2 Borrower Term Sheet which Lendy signed as principal, not in the Model 2 Borrower Loan Agreement, which Lendy signed as agent for the Model 2 Investors. In saying this I acknowledge that the practice was for Lendy to deduct non-default interest from the advance to Model 2 Borrowers and Lendy would not therefore normally have to sue for it. Ensuring that Lendy had legal title to non-default interest did however ensure that Lendy was legally entitled to the non-default interest deducted before the net advance was transferred to the Model 2 Borrower.

138. Mr Gledhill relies on *Lederer* in support of his contention that the "true party" to the Model 2 Borrower Loan Agreement and therefore the party with legal title to sue for Default Interest is the Model 2 Investors. Ms Toube says that Zacaroli J only decided in *Lederer* that the "real parties" to the Model 2 Borrower Loan Agreement in that case, for the purpose of being sued by the Model 2 Borrower, were the Model 2 Investors, but Ms Toube says that this does not mean that the Model 2 Investors who participated in a Model 2 Borrower Loan are the legal owners of the right to sue for Default Interest.

139. In my judgment however, absent a term to the contrary in the Model 2 Borrower Loan Agreement, it is unlikely that the legal title to the right to sue for Default Interest would vest in Lendy (in whole or in part) rather than in the Model 2 Investors where the Model 2 Investors are the "real parties" who can be sued by the Model 2 Borrower for breach of the Model 2 Borrower Loan Agreement. The judgment of Zacaroli J in *Lederer* is therefore consistent with my finding that the prima facie conclusion that Model 2 Investors have the right to sue for Default Interest is not displaced.

Commercial common sense

140. As for commercial common sense, I do not consider that this points in either direction:

(a) paying all the Default Interest to Lendy would deprive the Model 2 Investors of any additional interest in circumstances where the Model 2 Borrower Loan went into default (other than possibly the bonus accrual that Lendy referred to in its email of 12 September 2017 and the Amended Recoveries Policy). On the other hand, Lendy would have no additional fee for the likely additional cost of administering loans which were in default if it was not entitled to all of the Default Interest;

(b) Default Interest was charged at a very high rate (3% above the aggregate Interest Rate, so normally around 4.5% per month) that is likely to be significantly more than the additional cost to Lendy of administering loans in default and, on the other hand, would be a very generous level of additional interest for the Model 2 Investors to earn; and

(c) commercial common sense, applied to the interpretation of a written agreement does not look, as Lord Neuberger made clear in *Arnold v Britton,* to produce some form of subjectively fair commercial outcome for the parties, but rather at the question of whether a particular construction of the contract would produce a result that does not make commercial sense. In this case I cannot say that either providing for the Model 2 Investors to receive all of the Default Interest, or for Lendy to receive all of the Default Interest, would produce a result that lacks commercial sense. Recourse to commercial common sense does not displace the prima facie conclusion that Model 2 Investors are entitled to all the Default Interest.

Facts and circumstances known to the parties when the Model 2 Borrower Loan Agreements were entered into

141. The first Model 2 Borrower Loan Agreement was completed on 27 October 2015. Thereafter Model 2 Borrower Loan Agreements were entered into as and when sufficient money had been committed by Model 2 Investors, willing to participate in a Model 2 Borrower Loan to fund it in full. The last Model 2 Borrower Loan was signed on 18 September 2018. The standard form Model 2 Borrower Loan Agreement was never altered.

142. In *Arnold v Britton,* Lord Neuberger made it clear that the correct time to consider the relevant background facts as an aid to interpretation is the date upon which the relevant agreement

was entered into. There were multiple dates upon which this occurred. The same issue arose with the standard form Model 1 Investor Terms under Issue 3, namely, is the correct date for considering the relevant factual background when the standard documents were created, or the date on which each (in this case) individual Model 2 Borrower Loan Agreement was entered into? My answer is the same as for the Model 1 Investor Terms (and for the same reasons see paragraph 81(d) above), and that is that the date for considering the background facts should be when the Model 2 Borrower Loan Agreement/Model 2 Borrower Term Sheets were created (September 2015).

143. I am not satisfied that any of the factual background to the circumstances in which standard form Model 2 Borrower Loan Agreements/Model 2 Borrower Term Sheets were created, when looked at cumulatively, displace the prima facie conclusion that Model 2 Investors are entitled to the Default Interest. I have come to this conclusion for the reasons that follow.

144. Mr Gledhill says that Lendy was not a lender and interest is the reward paid to a lender for the risk it takes in lending its money to a borrower whereas fees are the way in which a facilitator of lending is rewarded.

145. I accept that fees, rather than interest, would more usually be charged by an intermediary who introduces lenders to borrowers, but the problem with Mr Gledhill's argument is that it is common ground that Lendy did charge non-default interest (albeit at a much lower level than the Default Interest) to Model 2 Borrowers. For that reason, I do not regard Lendy's role as an intermediary between Model 2 Investors and Model 2 Borrowers as supporting the prima facie conclusion that Model 2 Investors are entitled to Default Interest.

146. Ms Toube says that the email of 12 September 2017 and Amended Recovery Policy refer to Model 2 Investors being entitled to receive a bonus accrual if a loan was not paid on time, and they both support the contention that Lendy was entitled to the Default Interest. I do not agree for the following reasons:

(a) on 12 September 2017 Lendy sent an email to Model 2 Investors which said that a bonus accrual would be paid to Model 2 Investors if a Model 2 Borrower Loan went overdue, but the email does not mention Default Interest at all;
(b) the second mention of a bonus accrual payable to Model 2 Investors is in the Amended Recovery Policy, which Lendy appears to have placed on the Lendy Platform in around August 2018. This document does refer to a bonus accrual being paid to Model 2 Investors as a proportion of Default Interest, but it does not say anything about Default

Interest, or who it is payable to. At best, the Amended Recovery Policy may imply that Lendy is intended to keep the balance of the Default Interest;

(c) both the email of 12 September 2017 and the Amended Recovery Policy were produced long after the Model 2 Borrower Loan Agreement was first used on 27 October 2015 (and in the case of the Amended Recovery Policy only shortly before the last Model 2 Borrower Loan Agreement was entered into on 18 September 2018);

(d) I accept Mr Gledhill's point that if, prior to sending the email of 12 September 2017 and publishing the Amended Recovery Policy, the Model 2 Investors were entitled to Default Interest, then the email and/or Amended Recovery Policy could not take away that right;

(e) in my judgment, at best the email of 12 September 2017 and Amended Recovery Policy are indications of Lendy's subjective view of the right it had to Default Interest expressed long after the standard form Model 2 Borrower Loan Agreement was created and the first Model 2 Borrower Loan Agreement was entered into. As such, the email and Amended Recovery Policy are an inadmissible aid to interpretation of clause 6.3 of the Model 2 Borrower Loan Agreement; and

(f) as I will refer to shortly, in answering Issue 8, Lendy appears to have changed its mind (or position) as to who, as between Lendy itself and Model 2 Investors, was entitled to priority for money due to them from a Model 2 Borrower, if there was a Model 2 Shortfall (to one more favourable to itself), and it is certainly possible that Lendy took a different view of its entitlement to Default Interest (or wanted to) in 2017/2018 than it did in earlier years.

The Applicants' alternate case

147. Ms Toube's alternative case, on behalf of the Applicants, is that Default Interest should be split pro rata between the Model 2 Investors and Lendy in the proportions that they were entitled to receive non-default interest. I am not satisfied that the matters Ms Toube puts forward in support of her alternative case are sufficient to displace the prima facie conclusion that the Model 2 Investors are entitled to the Default Interest:

(a) Ms Toube refers to the content of the standard form Model 2 Guarantee which, at clause 5.2 says that *"the guarantor will pay interest to the Beneficiaries… at the rate as stated in clause 6.3 of the Loan Agreement…."* The Loan Agreement is the Model 2 Borrower Loan Agreement and "the Beneficiaries" are defined as both the Model 2 Investors and Lendy. So says Ms Toube the standard form Model 2 Guarantee anticipates that Default Interest charged under clause 6.3 of the Model 2 Borrower Loan Agreement is split between the Model 2 Investors and Lendy. However:

(i) the standard form Model 2 Guarantee merely guarantees the performance of the Model 2 Borrower under the Model 2 Borrower Loan Agreement, and cannot define what those liabilities are or to whom they are owed. It is clause 6.3 of the Model 2 Borrower Loan Agreement that provides for the payment by the Model 2 Borrower of Default Interest and it does not say to whom Default Interest is payable;

(ii) clause 5.3 of the guarantee says that "Lenders" are not entitled to receive interest under the Model 2 Borrower Loan Agreement and interest under the guarantee. "Lenders" are defined as meaning the Model 2 Investors only. There is no obvious reason why clause 5.3 should only restrict Model 2 Investors from claiming interest under the Model 2 Borrower Loan Agreement and the Model 2 Guarantee and not Lendy;

(iii) clause 5.3 appears superfluous as the Model 2 Guarantee guarantees the performance of the Model 2 Borrower under the Model 2 Borrower Loan Agreement and there is no basis for interest being charged under the guarantee as well as the Model 2 Borrower Loan Agreement in any event; and

(iv) I am afraid that clause 5.3 is another example of the poor drafting of Lendy's standard documents and I have no confidence therefore that the use of "Beneficiaries" in clause 5.2 contemplated that both Model 2 Investors and Lendy would be entitled to share in the Default Interest;

(b) Ms Toube says that it would make commercial common sense for the Default Interest to be split between the Model 2 Investors and Lendy in the proportions in which they receive non-default interest. However, as I have already said, it is clear from Lord Neuberger's speech in *Arnold v Briton* that when the Court has regard to commercial common sense in construing written contracts, this does not mean seeking to achieve a "fair result" between the parties, or one that they might be expected to have agreed. It seems to me that Ms Toube's appeal to commercial common sense, in circumstances where clause 6.3 itself gives no indication of who is entitled to Default Interest, let alone that it should be split in some way, is really a suggestion that the Court should aim to achieve what might subjectively be regarded as a fair result, rather than one that objectively the parties may be taken to have intended.

For those reasons, Ms Toube's alternative case, that Default Interest should be divided pro rata according to their entitlement to non-default interest, also fails to displace the prima facie conclusion that the relevant Model 2 Investors are entitled to Default Interest.

ISSUE (8)

148. Issue (8) is – *"Has Lendy breached any of its fiduciary duties regarding its charging fees and interest for its own account in connection with the Model 2 Borrower Loans? If so:*

(a) what is the appropriate form of relief for Model 2 Investors and/or the Model 2 Transferees;

(b) is Lendy entitled to an equitable allowance to cover its costs as agent; and

(c) if the answer to the question in issue (8)(a) is 'yes', how should that allowance be calculated in principle?"

149. Mr Gledhill confirmed that Ms Taylor does not pursue an argument that Lendy owed fiduciary duties to Model 2 Investors in charging fees and non-default interest to Model 2 Borrowers. In consequence of that, Issue 8 is only concerned with Default Interest.

A CHANGE IN THE QUESTIONS UNDER ISSUE 8 (BASED ON MY FINDINGS ON ISSUE 5)?

150. On 6 July 2021, whilst I was in the process of preparing the draft of this judgment, I sent an email to Ms Toube and Mr Gledhill. In that email I raised the issue of whether, if I decided that the answer to Issue 5 was that Model 2 Investors had legal title to the Default Interest, the questions raised by Issue 8 would need to be adapted to reflect my decision on Issue 5 and I invited counsel also to attempt to agree what the answers to those questions would be in that scenario.

151. In response to my email, Ms Toube and Mr Gledhill agreed that if I decided that the Model 2 Investors had legal title to the Default Interest then, to the extent that Lendy received Default Interest and applied it for its own purposes, that would constitute a breach of Lendy's fiduciary duties to Model 2 Investors because:

(a) it is common ground that Lendy acted as agent for the Model 2 Investors in collecting and applying monies received from Model 2 Borrowers/Model 2 Security in accordance with the contractual rights of the Model 2 Investors and Lendy; and

(b) if Lendy applied Default Interest for its own purposes, when Model 2 Investors had legal title to the Default Interest, Lendy would breach its fiduciary duty to account to the Model 2 Investors. Ms Toube and Mr Gledhill agreed that this would only leave the question (under Issue 8) of whether Lendy is entitled to an equitable allowance to cover its costs as agent in those circumstances.

152. As I have answered Issue 5 to the effect that the Model 2 Investors have legal title to the Default Interest, it is accordingly the agreed position of counsel that Lendy acted in breach of its fiduciary duty to the Model 2 Investors by applying Default Interest for its own use, rather than accounting to the Model 2 Investors for it.

153. Before going on to consider the remaining question of whether Lendy is entitled to an equitable allowance to cover the costs it incurred as agent, I will clarify (as requested by Ms Toube) that, on the basis that the Applicants have confirmed that they are (as I would expect them to, and save for a portion of the Default Interest that they have used to pay some disbursements) holding the Default Interest that came into their hands, following their appointment as Administrators of Lendy, pending the outcome of their application for directions, there is no question of Lendy having breached the fiduciary duties that it owed to Model 2 Investors, following the appointment of the Applicants, by not accounting to those Model 2 Investors (yet) for Default Interest.

AN EQUITABLE ALLOWANCE FOR LENDY?

154. On the footing that legal title to the Default Interest vests in the Model 2 Investors, in my judgment, Lendy is not entitled to an equitable allowance for the following reasons:

(a) the equitable principle that a party who has breached their fiduciary duties to another may be awarded an equitable allowance by the Court for work done and expenses incurred by them is based upon some benefit having accrued to the beneficiary of the fiduciary duty as a result of the breach of fiduciary duty which would make it equitable to make an allowance to the fiduciary, out of that benefit, for the work that they had carried out and expenditure that had been incurred by a fiduciary in producing that benefit;

(b) I have found that the Model 2 Investors had legal title to the Default Interest and were entitled to receive it from Lendy;

(c) if Lendy had complied with the fiduciary duties that it owed to the Model 2 Investors, then it would have accounted to the Model 2 Investors for the Default Interest that it received;

(d) it is common ground that Lendy did not charge fees or interest to Model 2 Investors for the administrative work that it carried out for the benefit of the Model 2 Investors (including collecting Default Interest), instead Lendy charged interest and fees to Model 2 Borrowers to cover all of its administrative costs. The costs of collecting Default Interest ought therefore to have been covered by the fees and non-default interest charged by Lendy to Model 2 Borrowers (on the footing that Model 2 Investors are entitled to the Default Interest) in any event;

(e) in any event, collecting Default Interest was not a breach by Lendy of the fiduciary duties that it owed to the Model 2 Investors, the breach was failing to account to the Model 2 Investors for the Default Interest it had collected; and
(e) no benefit accrued to the Model 2 Investors as a result of Lendy failing to account to them for Default Interest which they were entitled to (on the contrary, the Model 2 Investors lost out as a result of Lendy not accounting to them for Default Interest).

In my judgment, for those reasons there is no basis for me awarding an equitable allowance to Lendy for the costs which it incurred in collecting Default Interest, or otherwise.

155. I should make one final point regarding the position following the appointment of the Applicants, and that is that the parties have agreed that the Applicants (acting as Administrators of Lendy) may in principle agree with the Conflict Administrators (acting on behalf of SSSHL) a "service charge" for the costs incurred by Lendy after the Applicants' appointment, in performing the functions of SSSHL regarding the enforcement of securities held by SSSHL (as security trustee) in relation to Model 2 Borrower Loans, which service charge may partly include the costs of collecting Default Interest. As a result, the Applicants did not pursue a claim for an equitable allowance for these post appointment costs in any event.

WHAT IF I AM WRONG ABOUT THE ANSWER TO ISSUE 5?

156. In case I wrong in my answer to Issue 5 (that Model 2 Investors have legal title to the whole of the Default Interest), and instead Lendy is entitled to all or part of the Default Interest, I will proceed now to answer the questions as originally raised in Issue 8 on the footing that (contrary to my finding on issue 5) Lendy is entitled to all or part of the Default Interest.

157. Issue 8(a) (which now relates only to Default Interest) splits down into three separate issues, namely:
(a) what fiduciary duties, if any, did Lendy owe to Model 2 Investors in connection with all the Default Interest charged by Lendy to Model 2 Borrowers for its own account;
(b) did Lendy breach any of its fiduciary duties by charging Default Interest to Model 2 Borrowers for its own account, if it did not have the informed consent of the Model 2 Investors to do so; and
(c) did Model 2 Investors give their informed consent to Lendy charging Default Interest to Model 2 Borrowers for its own account?

MY FACTUAL FINDINGS-DISCLOSURE BY LENDY TO MODEL 2 INVESTORS OF: (A) DEFAULT INTEREST; AND (B) THE PRIORITY OF PAYMENTS IF THERE WERE A SHORTFALL

158. Before turning to the three questions posed by Issue 8 (a), I will set out my findings as to what Lendy disclosed (to Model 2 Investors and the FCA) about (a) Lendy charging Default Interest to Model 2 Borrowers; and (b) the priority in which monies owed by Model 2 Borrowers to Lendy on the one hand and the Model 2 Investors participating in the relevant Model 2 Borrower Loan on the other hand would be paid in the event that there was a Model 2 Shortfall. My factual findings are particularly relevant to the third question under Issue 8(a) (namely, did Model 2 Investors give their informed consent to Lendy charging Default Interest for its own account), but they are also relevant to the first and second questions, under Issues 8(b) and 8(c), and so it is convenient to make my factual findings now.

Default Interest

159. As already noted, Default Interest was charged to Model 2 Borrowers under clause 6.3 of the Model 2 Borrower Loan Agreement. Clause 6.3 provides that the Default Interest rate is the aggregate of the interest rates payable by Model 2 Borrowers to Model 2 Investors and Lendy, commonly 1% per month payable to Model Investors and 0.5% per month payable to Lendy. 3% per month above the aggregate Interest Rate was therefore normally 4.5% per month or 54% per annum. The Default Interest rate is therefore substantially higher than the non-default interest rate.

160. It is common ground that Model 2 Investors were not able to view a copy of the Model 2 Borrower Loan Agreement or the Model 2 Borrower Term Sheet on the Lendy Platform, notwithstanding that clause 7.4 of the Model 2 Investor Terms says that Model 2 Investors would be shown the Model 2 Borrower Loan Agreement before they decided whether or not to participate in a Model 2 Borrower Loan.

161. Ms Toube says that Mr Powell was provided with a copy of a Model 2 Borrower Loan Agreement, when he requested it from Lendy's solicitors and that this demonstrates that Lendy was "happy" to provide a copy of the relevant Model 2 Borrower Loan Agreement on request by a Model 2 Investor.

162. The burden of proof lies on Lendy to prove what access it gave Model 2 Investors to Model 2 Borrower Loan Agreements. I am not satisfied that Lendy was, as Ms Toube describes it, "happy" to provide Model 2 Investors with copies of Model 2 Borrower Loan agreement for the following reasons:

(a) whilst it is true that Lendy's solicitors did provide Mr Powell with a copy of a Model 2 Borrower Loan Agreement, the context in which they did so was as follows:
(i) Model 2 Investors were told by Lendy in September 2018 that the Borrower under loan DFL 017 was threatening legal action against the Model 2 Investors who participated in its loan;
(ii) Mr Powell sent an email to Lendy asking for a copy of the Model 2 Borrower Loan Agreement relating to loan DFL 017. Lendy responded that Mr Powell should request a copy from Lendy's solicitors, which he did and those solicitors provided Mr Powell with a copy of the relevant agreement; and
(iii) this does not demonstrate a willingness on the part of Lendy to provide, on request by Model 2 Investors, a copy of a Model 2 Borrower Loan Agreement. The solicitor would be obliged to provide the Model 2 Borrower Loan Agreement for loan DFL017 to Mr Powell because Mr Powell was in effect one of its clients, as one of the principles to loan DFL017 (even if Lendy gave instructions to those solicitors);

(b) the fact that clause 7.4 of the Model 2 Investor Terms stated that Model 2 Investors would be able to view, on the Lendy Platform a copy of the Model 2 Borrower Loan Agreement which they were considering investing in, but it was in fact not available to view on the Lendy Platform may suggest that Lendy had reconsidered whether giving Model 2 Investors easy access to Model 2 Borrower Loan Agreements suited its best interests; and

(c) no evidence has been produced by Lendy that it ever provided a Model 2 Borrower Loan Agreement to a Model 2 Investor.

163. In finding that Lendy has not proved that it was "happy" to provide a Model 2 Borrower Loan Agreement to Model 2 Investors if requested, I do not find that it would have refused to do so, merely that there is no direct evidence of how it did or would have reacted to a request to it from a Model 2 Investor for a copy of a Model 2 Borrower Loan Agreement. On the evidence, requesting a copy of the relevant Model 2 Borrower Loan Agreement from Lendy was the only way in which Model 2 Investors could get to see a copy of the relevant Model 2 Borrower Loan Agreement.

164. Even if Lendy was happy to provide copies of Model 2 Borrower Loan Agreements to Model 2 Investors on request, I do not consider that this amounted to effective disclosure to Model 2 Investors of the fact that Lendy was charging Default Interest, either at all or at very high levels to Model 2 Borrowers. I make these findings for the reasons that follow.

165. The Frequently Asked Questions ("FAQ") section of the Lendy Platform contains certain information regarding fees and interest Lendy charged:

(a) in answer to the question *"what are the fees"* it states *"unlike many (P2P) lenders we do not charge our investors any fees or commission on their investment…";* and

(b) "since its launch by Lendy Ltd in 2013 [Lendy] *has made its profit from the difference in interest rates charged to borrowers and paid to investors. All* [Lendy] *investors receive a fixed monthly interest of 1% whereas Lendy Limited charges interest at 1.5% per month on average… We feel this is a fair margin as the administrative costs that are associated with sourcing new projects for investment, and ensuring all property is secured with a legal charge, are substantial"*.

166. So, Model 2 Investors reading this part of the FAQ section of the Lendy Platform would reasonably gain the impression that the interest charged by Lendy to Model 2 Investors was, on average 0.5% per month. There is no suggestion in the FAQ section that Lendy charged Default Interest to Model 2 Borrowers at all, let alone at a much higher level than non-default interest.

167. I have already dealt under issue 5 (see paragraph 146) with what Lendy told Model 2 Investors about its intention to pay a bonus accrual to Model 2 Investors and I have concluded, for the reasons set out there, that Lendy's communications regarding a bonus accrual to Model 2 Investors were not sufficient to alert Model 2 Investors to the fact that Lendy was charging Default Interest for its own account

168. None of Lendy's emails updating Model 2 Investors on developments mention Lendy's fees or charging structure or Default Interest.

Priority of Payments

169. The position that Lendy presented to Model 2 Investors in relation the priority of payments as between Lendy on the one hand and Model 2 Investors on the other is important. This is because only if Lendy was suggesting that it would be paid monies owed to it by Model 2 Borrowers in priority to Model 2 Investors could Model 2 Investors reasonably be concerned to enquire what Lendy was charging Model 2 Borrowers because only if Lendy had priority over Model 2 Investors for the fees and interest it charged Model 2 Borrowers would what Lendy charged to Model 2 Borrowers have any direct effect on the Model 2 Investors' recovery of principal and interest (if there was a Model 2 Shortfall).

170. Nothing specific seems to have been communicated by Lendy to Model 2 Investors about the priority of payments out of recoveries from Model 2 Borrowers/Model 2 Security as between Lendy and Model 2 Investors, until March 2018. Prior to that point Lendy had provided various general assurances to Model 2 Investors. For example the "How it works" section of the Lendy Platform said that Lendy would make every effort to minimise the risk to its investors and to ensure where possible that they would be paid in full and on time and the "Investors Special update" emailed to Model 2 Investors as late as 23 February 2018 insisted that the recovery of Model 2 Investors' capital and interest was Lendy's *"number one priority".*

171. On 5 March 2018, Lendy published the Amended Model 2 Investor Terms on the Lendy Platform. The accompanying email stating that one of the *"main additions"* to the amended terms was: *"a clarification and strengthening of clause 13.3 which relates to investor protection in the event of a distressed sale of an investment asset."*

172. I have found that, contrary to that description of clause 13.3, clause 13.3 provided, for the first time, that Lendy's claims against Model 2 Borrowers (for interest, fees and commission) would rank ahead of Model 2 Investors' claims against Model 2 Borrowers (for capital and interest), subject to SSSHL/Lendy being stated to have a discretion to decide on a different order of priority.

173. On 13 April 2018 Lendy, sent by email to Model 2 Investors the Recovery Policy. Under the heading *"priority of payments"*, the Recovery Policy said

"Unless Lendy is receiving a payment from a borrower in connection with an extension, the funds forwarded by the borrower shall be applied to the amount owing with the following priority:

(1) Capital (loan) amount

(2) Interest accrued

(3) Bonus Accrual

Lendy will only take any portion of interest or fees owing to them once all of the above have been satisfied. Only once each tier has been fully satisfied will funds be put towards the next. E.g. the whole capital amount must be paid before funds are put towards interest accrued, and all interest accrued must be paid before funds are put towards bonus accrual."

174. There was therefore an inconsistency between clause 13.3 of the Amended Model 2 Investor Terms which provided for interest and fees under the Borrower Loan Agreement (payable to Lendy) to be paid ahead of the capital and interest owed to Model 2 Investors (subject to any

exercise of discretion by SSSHL/Lendy to vary that order of priority), and the Recovery Policy (published a little over a month later) which made it clear that interest or fees due to Lendy would only be paid after capital, interest and any bonus accrual was paid to Model 2 Investors in full.

175. Both the FCA and Mr Powell raised concerns about the new clause 13.3 in the Amended Model 2 Investor Terms.

176. The FCA wrote to Lendy on 6 March 2018 saying that a *"minded to refuse"* (Lendy's full Peer to Peer authorisation) letter was being prepared and expressing concern that the new clause 13.3 subordinated Model 2 Investor claims for principal and interest to Lendy's own fees and it asked for confirmation of whether that point had been previously communicated to Model 2 Investors.

177. On 13 March 2018, in another email, the FCA said that Lendy did "not provide any information about its *"unpaid fees, costs and expenses"*, and lenders had no means of establishing for themselves the likely risk if an asset sale leads to a shortfall…, adding *"We consider this to be material information the lenders should have been provided with prior to them making a decision to invest. This information would help lenders formulated a view as the likely risk of losing their investment."*

178. The FCA, in their emails of 6 March 2018 and 13 March 2018, had raised issues about both new clause 13.3 of the Amended Model 2 Investor Terms and that Lendy had not told Model 2 Investors about what it was charging to Model 2 Borrowers. Those two issues combined meant that it appeared that if a Model 2 Shortfall occurred, Lendy would rank ahead of Model 2 Investors, prejudicing their ability to recover their capital and interest for charges, fees and interest which Model 2 Investors had no details of.

179. On 16 March 2018, Lendy's Head of Compliance, Paul Coles replied to the FCA email of 13 March and dealt with both issues. He confirmed that
"All capital payments received are apportioned to ensure that investors receive full repayment before settling any interest and/or costs payable to, or paid out by, Lendy. Therefore Lendy will always apportion the monies on the following basis:

(1) Capital payable to investors
(2) Interest payable to investors
(3) Bonus accrual payable to investors
(4) Money owed to Lendy…….

Lendy has never prioritised its costs over and above those of investors in the event of a shortfall from an asset sale. The minor update to the payment waterfall seeks to further clarify (and therefore strengthen) investor protection in the case of these or similar sale events. Furthermore, I can confirm that Lendy has absolutely no plans to change the payment waterfall to promote its costs above investors. This is a key foundation stone of the business.

On this basis we have not historically detailed the costs incurred by lending on the platform since they are not relevant to the recovery to investors …"

180. After receiving Mr Coles' email of 16 March 2018, the FCA did not pursue the matter further and on 11 July 2018 (4 months later), the FCA granted full authorisation to Lendy to operate a Peer to Peer lending platform. It is reasonable to infer, and I do so, that the assurance given in Mr Coles' email of 16 March 2018:
(a) resulted in the FCA not pursuing the issues of priority and disclosure to Model 2 Investors of what Lendy charged to Model 2 Borrowers in interest and fees; and
(b) resulted in the FCA granting full authorisation to Lendy, either at all or at least without first requiring Lendy to disclose to Model 2 Investors what Lendy was charging to Model 2 Borrowers in interest and fees.

181. On 30 April 2018, Mr Powell sent an email to the Lendy support team noting the inconsistency between the new clause 13.3 of the Amended Model 2 Investor Terms and the Recovery Policy.

182. On 8 May 2018, Lendy's legal team replied to Mr Powell noting the inconsistency and stating that the priorities set out in the Recovery Policy were correct, and that the Amended Model 2 Investor Terms would be amended so that they corresponded with the Recovery Policy.

183. When nothing was done to publish an amendment to the Amended Model 2 Investor Terms, Mr Powell sent three further emails to Lendy to confirm that the Amended Model 2 Investor Terms had not been amended as the legal team had said they would be. In his final email of 3 October 2018, Mr Powell stated: *"how do I escalate this to a complaint or should I just go straight to the regulator noting that your terms and conditions are wilfully misleading to your customers"*.

184. By email dated 10 October 2018, the Lendy compliance team replied that *"our legal team is presently discussing your questions relating to our terms and* [conditions]. *We have noted that you have mentioned that you wish to raise a complaint, if this is still the case, can you please let me know via reply.."*

185. What in fact happened, in spite of the assurances given by Lendy to both the FCA and Mr Powell, was that Lendy published the Amended Recovery Policy, at some point in August 2018, which confirmed that the priority of payments was as set out in the Amended Model 2 Investor Terms. I find that the publishing of the Amended Recovery Policy on the Lendy Platform in August 2018 involved Lendy reneging on the assurances that it gave to the FCA in March 2018 and to Mr Powell in May 2018 that Model 2 Investors would have priority over Lendy if there was a Model 2 Shortfall.

186. My factual findings, in summary are:

(a) the FAQ section of the Lendy Platform (in place at the time that Lendy changed to the Model 2 structure in October 2015) informed Model 2 Investors that Lendy was charging Model 2 Borrowers non-default interest for its own account at the rate of 0.5% per month. It is reasonable for the Model 2 Investors to have assumed, based on that information, that that was the only interest that Lendy was charging to Model 2 Borrowers unless and until they were told otherwise;

(b) there is no evidence of Lendy mentioning Default Interest in any of its communications with Model 2 Investors until August 2018 when, in telling Model 2 Investors about a bonus accrual that Lendy intended to pay to them, the bonus accrual was described as being a portion of Default Interest, but this reference was a very oblique reference to Default Interest with no detail of the circumstances in which Default Interest was payable, how much was payable, or who it was payable to. I do not regard this as alerting Model 2 Investors to the existence of Default Interest, let alone its terms or that it was payable to Lendy. In any event, the reference to Default Interest came a matter of weeks before the final Model 2 Borrower Loan was advanced on 18 September 2018 and therefore very few Model 2 Investors will have seen this reference to Default Interest before they decided to participate in a Model 2 Borrower Loan;

(c) the Amended Model 2 Investor Terms published on 5 March 2018 in clause 13.3 suggested that, (absent Lendy or SSSHL exercising its discretion to the contrary) if there was a Model 2 Shortfall, fees and interest owed by Model 2 Borrowers to Lendy would be prioritised over capital and interest owed to Model 2 Investors. This was followed up however a little over a month later by the Recovery Policy, published on 13 April 2018 which stated that, if there was a Model 2 Shortfall, payment of capital and interest due to Model 2 Investors would have priority over any monies owed by Model 2 Borrowers to Lendy;

(d) queries raised by the FCA and Mr Powell, following the publication of the Amended Model 2 Investor Terms on 5 March 2018, were met by reassurances from Lendy that, if

there was a Model 2 Shortfall, monies due to Model 2 Investors for capital and interest would be prioritised over monies owed by Model 2 Borrowers to Lendy. In the case of the FCA the assurance was very specific and, on the basis of that assurance, Mr Coles, of Lendy, also represented that publication to the Model 2 Investors of the fees and interest that Lendy was charging to Model 2 Borrowers would not be relevant to Model 2 Investors;

(e) I have inferred that the FCA, based upon Mr Coles' assurances: (a) accepted that disclosing to Model 2 Investors what Lendy was charging to Model 2 Borrowers (including Default Interest) would not be relevant to the investment decisions of Model 2 Investors and therefore the FCA stopped pressing Lendy to disclose this; and (b) granted full authorisation to Lendy to operate a Peer to Peer lending platform, when it would not otherwise have done so, or granted full authorisation without requiring Lendy to disclose that detail to Model 2 Investors; and

(f) Lendy went back on the assurances that it gave to both the FCA and Mr Powell by producing the Amended Recovery Policy in August 2018 which referred to the order of priority of payment being as set out in the Amended Model 2 Investor Terms.

WHAT FIDUCIARY DUTIES DID LENDY OWE TO MODEL 2 INVESTORS IN CONNECTION WITH DEFAULT INTEREST WHICH IT PURPORTED TO CHARGE FOR ITS OWN ACCOUNT?

Matters agreed between counsel

187. Ms Toube and Mr Gledhill agree the following applies in relation to the fiduciary duties of Lendy:

(a) in so far as Lendy acted as agent for the Model 2 Investors, it owed fiduciary duties to those Model 2 Investors (although Ms Toube qualifies that by saying that the fiduciary duties only apply if there was a reasonable expectation on the part of the Model 2 Investors that Lendy would put aside its own interests in favour of the interests of the Model 2 Investors);

(b) the fiduciary duties that Lendy owed to the Model 2 Investors (insofar as it acted as agent for them (and on Ms Toube's case in so far as the Model 2 Investors had a reasonable expectation that Lendy would put aside its own interests in favour of theirs) include:
(i) a duty not to put themselves in a position or enter into transactions in which Lendy's interests may conflict with their duty to the Model 2 Investors, unless the Model 2

Investors consented, with full knowledge of all the material circumstances as to the nature and extent of Lendy's interest (*Bowstead paragraph* 6-046); and

(ii) a duty not "*to acquire a benefit from a third party without the consent of the Model 2 Investors and to account to the Model 2 Investors for any benefit so obtained*" (*Bowstead paragraph* 6-079);

(c) what had to be disclosed by Lendy to the Model 2 Investors in order to obtain their informed consent depends upon the attributes of the Model 2 Investors and the surrounding facts; and

(d) Lendy has the burden of proving that there has been sufficient disclosure of the material circumstances, for Model 2 Investors to give their informed consent and that they did consent.

IN WHAT RESPECTS DID LENDY ACT AS AGENT FOR MODEL 2 INVESTORS?

Counsel's submissions on the extent of Lendy's agency

188. Ms Toube says that Lendy's role as agent is defined by the Model 2 Investor Terms and is confined to: (a) signing the Model 2 Borrower Loan Agreement on behalf of Model 2 Investors (clause 8.1.1 of the Model 2 Investor terms); (b) amending the Model 2 Borrower Loan Agreement after it was signed (clause 9.8.1); and (c) negotiating and settling any dispute with Model 2 Borrowers (clause 9.8.2). Ms Toube asserts specifically that Lendy did not act as agent for the Model 2 Investors in negotiating with Model 2 Borrowers the terms of the Model 2 Borrower Loan Agreement, because that agreement was offered on the Lendy Platform for Model 2 Investors to participate in after its terms had been agreed by Lendy with the Model 2 Borrower.

189. Ms Toube makes the following points in support of her submission that Lendy's role as agent is restricted to those matters where the Model 2 Investor Terms state that Lendy acts as agent for the Model 2 Investors:

(a) clause 24.8 of the Model 2 Investor Terms states that *"Nothing in these terms and conditions is intended to, or shall be deemed to, establish any partnership or joint venture between the parties, nor constitute either party the agent of the other for any purpose"*. Ms Toube accepts that clause 24.8 is badly drafted because (even on Ms Toube's case) Lendy acted as agent for the Model 2 Investors in signing the Model 2 Borrower Loan Agreement, amending the Model 2 Borrower Loan Agreement and settling disputes with Model 2 Borrowers. Ms Toube suggests however that the meaning of clause 24.8 is that

Lendy does not act as agent for the Model 2 Investors other than in the ways identified in the clauses of the Model 2 Investor Terms;

(b) Ms Toube says that SSSHL acted as security trustee and as such it held legal title to the Model 2 Security and therefore only it, rather than Lendy, was entitled to enforce Model 2 Security. Lendy did not therefore act as agent for the Model 2 Investors in enforcing Model 2 Security; and

(c) because the Model 2 Investors knew that Lendy was in business to make a profit and that it charged interest and fees to Model 2 Borrowers, there was no reasonable expectation by the Model 2 Investors that Lendy would act in the interests of the Model 2 Investors, in preference to its own interests (to recover interest and costs owed to Lendy by the Model 2 Borrowers). In this respect, Ms Toube refers to the judgment of Lady Arden in *Children's Investment Fund v Attorney General* [2020] 2 WLR 461 (SC), which she says is authority for the proposition that fiduciary duties are only owed where there is a reasonable expectation that the party alleged to owe the fiduciary duties will act in the interests of the other party, in preference to their own interests.

190. Mr Gledhill did not seek to argue that Lendy acted as agent for the Model 2 Investors in negotiating the terms of the Model 2 Borrower Loan Agreement, rather he said that Lendy acted as agent for the Model 2 Investors in: (a) ensuring that Model 2 Borrowers were creditworthy; (b) ensuring that the security taken from Model 2 Borrowers was adequate for the value of the Model 2 Borrower Loan; and (c) ensuring, so far as possible, that the amount of principal and interest due to Model 2 Investors was recovered either from the Model 2 Borrowers, or by realising Model 2 Security, for which Lendy was responsible.

191. Mr Gledhill says that it is clear that Lendy acted as agent for the Model 2 Investors in those three ways from (a) information published by Lendy on the Lendy Platform; (b) information contained in emails sent by Lendy to Model 2 Investors; (c) the Recovery Policy; and (d) clauses in the Model 2 Investor Terms, all of which (Mr Gledhill says) Lendy intended the Model 2 Investors to rely upon. Mr Gledhill also says that the authorisations obtained by Lendy from the FCA to operate a Peer to Peer lending platform which describe the extent of Lendy's role as the platform operator also support his submissions as to the extent of Lendy's agency.

192. As to the three points made by Ms Toube in support of her case that Lendy's agency was limited to those respects in which the Model 2 Investor Terms specified that Lendy acted as agent, Mr Gledhill says:

(a) Clause 24.8 of the Model 2 Investor Terms should simply be disregarded because it is inconsistent with Lendy acting as agent for Model 2 Investors at all and it is common ground that Lendy did act as agent for Model 2 Investors for some purposes;

(b) Clause 8.1.3 of the Model 2 Investor Terms provides that Model 2 Investors authorise Lendy to act on behalf of SSSHL in enforcing Model 2 Security. The mere fact that SSSHL held legal title to the Model 2 Security and acted as agent for Model 2 Investors/Lendy in enforcing it does not alter the reality of the situation that it was Lendy that decided how and when to enforce Model 2 Security; and

(c) at best Model 2 Investors knew that Lendy was charging some fees and non-default interest at an average of 0.5% per month to Model 2 Borrowers, but they were not made aware that Lendy was charging Model 2 Borrowers Default Interest at a very substantially higher rate than non-default interest. Non-default interest was, in any event, deducted by Lendy from the advance to the Model 2 Borrower so there was a reasonable expectation that Lendy would not compete with Model 2 Investors for its fees/interest if there was a Model 2 Shortfall.

My findings-the extent of Lendy's agency

193. I am satisfied that Lendy did accept responsibility to act as agent for Model 2 Investors, in: (a) taking steps to ensure that Model 2 Borrowers were creditworthy; (b) ensuring that the project which was being funded was viable; and (c) ensuring that security taken for the Model 2 Borrower Loan would provide acceptable headroom above the value of that loan. I have reached those conclusions for the following reasons:

(a) the Lendy Platform included a page entitled *"How it works"*, the heading to which stated : *"we secure loans against professionally valued UK property".* It then explained that:
(i) *"When a borrower approaches our parent company Lendy Ltd they begin a full and in-depth assessment of the project. Professionally qualified chartered surveyors are instructed to value the property being used as security to ensure any loan is a maximum of 70% of the Open Market Value. If the borrower and security meet the criteria the loan is secured with a legal charge … "*; and
(ii) *"We make every effort to minimise the risks for our investors and to ensure, where possible, that all investments are repaid in full and on time. To date we have a 100% success rate with our repayments … we feel confident that we have a thorough and robust system in place to protect all* [Lendy] *investors"*;

(b) in a weekly update to Model 2 Investors dated 25 August 2017, Lendy said that, while it was *"not able to protect investors from capital loss, we do take our responsibilities very*

seriously … Lendy already has a robust due diligence process, which includes a five phase, multi-step (49 in fact) credit assessment overseen by our Credit Committee";

(c) in an email sent to Model 2 Investors on 9 October 2017, Lendy said it was *"one of the only profitable fintech property platforms….but we've also managed risk carefully, and always striven to strike the right balance between loan supply and investment demand"*; and

(d) Lendy therefore held itself out to Model 2 Investors as: (i) assessing the credit worthiness of Model 2 Borrowers: (ii) assessing the viability of the project that the Model 2 Investors were considering funding; and (iii) ensuring that the loan did not exceed 70% of the open market value of the security.

194. I am also satisfied that Lendy accepted responsibility to act as agent for Model 2 Investors in managing and making decisions about the recovery of Model 2 Borrower Loans, including where they went into default. This is clear from the following clauses of the Model 2 Investor Terms published on the Lendy Platform (to which no material amendment was carried out in the Amended Model 2 Investor Terms which replaced them on the Lendy Platform in March 2018):

(a) by clause 8.1.1, Model 2 Investors agreed to *"appoint* [Lendy] *to act as agent on your behalf in relation to the loan and instruct* [Lendy] *to sign the Loan Contract as agent on your behalf"*;

(b) by clause 8.1.2, Model 2 Investors appointed SSSHL to act as security trustee, and instructed Lendy *"to sign such security documents as agent on your behalf"*;

(c) by clause 8.1.3, Model 2 Investors authorised Lendy to give instructions on their behalf to SSSHL *"in relation to the security documents and their enforcement"*;

(d) by clause 9.6, Model 2 Investors agreed that Lendy, *"in its absolute discretion … (acting as agent on your behalf) may agree with the borrower to restructure the loan and amend the Loan Contract"*;

(e) by clause 9.8.1, Model 2 Investors constituted Lendy their agent for the purposes of *"negotiating and agreeing amendments to the Loan Contract"*; and

(f) by clause 9.8.2, Model 2 Investors also constituted Lendy their agent for the purpose of *"negotiating and settling any dispute relating to the Loan Contract"*.

195. I am satisfied that Lendy gave specific assurances to Model 2 Investors that it had robust policies in place to deal with loans that went past the contracted repayment date and that it would put Model 2 Investors interests first in operating those policies. This is apparent from:

(a) the weekly update to Model 2 Investors dated 25 August 2017 referred to in paragraph 192(b) which continues as follows… *"But Lendy is not stopping there. It is committed to*

having the best recovery processes in the P2P industry, to help protect investors' hard-earned investments";

(b) in an "Investor Round-up" email dated 13 April 2018, Lendy said that the purpose of the Recovery Policy (which it had only recently published on the Lendy Platform) was *"to give our investors comfort about the robust procedures Lendy has in place to protect them in the case of the borrower's default"*;

(c) in the Recovery Policy itself Lendy:

(i) assured Model 2 Investors that their capital and interest would be paid in priority to Lendy's own *"portion of interest or fees"*;

(ii) stated *"Borrowers are not infrequently granted extensions to their loans … to prevent loans falling past due and to improve the position of Lendy investors who will continue to receive interest for the extended period, Lendy is careful to ensure that in granting an extension it is not increasing the risk profile of a particular loan"*;

and (iii) stated that "*Where a borrower is unable to repay their loan in full but is able to repay their loan in part Lendy will encourage and incentivise a borrower to do this. The key benefit to partial repayment of a loan is that it enables the return of capital to platform investors and reduces the risk profile for the remaining capital by reducing the loan to value ratio*"; and

(d) in an *"Investor Update Special"* emailed on 23 February 2018 to Model 2 Investors, Lendy assured Model 2 Investors that: *"We have never taken the support of our investors for granted, and nor shall we ever. You are our number one concern and protecting your interests and hard-earned capital is our top priority … Our job is to be the champion of our investors and protect your interests. And it is for this reason that we take any potential losses very seriously. Where we might be faced with a recovery shortfall, we will pursue every avenue available to us to recover investors' capital in full, along with interest accrued and any bonuses owed"*.

196. Finally, I am also satisfied that it is clear from the matters I have set out in paragraphs 193 -195 above that Lendy assumed responsibility for seeking to recover Model 2 Borrower Loans, including where they were in default and taking enforcement action, including realising Model 2 Security (which Model 2 Investors authorised Lendy to give instructions to SSSHL to enforce on their behalf). The role of agent that Lendy assumed responsibility for in connection with the recovery of Model 2 Borrower Loans is not limited, as Ms Toube submits, to amending Model 2 Borrower Loan Agreements and negotiating settlements with Model 2 Borrowers. As for the three points made by Ms Toube in support of her submission that Lendy's role as agent was so restricted:

(a) I am satisfied that clause 24.8 of the Model 2 Investor Terms is standard wording, used where there is no intention that the relevant agreement will establish a partnership or joint venture between the parties to it and there is no intention that one party will act as agent for the other at all. Ms Toube accepts that clause 24.8 does not reflect the true position. She submits that the intention of clause 24.8 is to confirm that Lendy would only act as agent for Model 2 Investors to the extent spelt out in the Model 2 Investors Terms. I do not accept that analysis of the intention of clause 24.8, if that were the intention, the clause could simply have said, "save to the extent set out in these terms neither party acts as agent for the other…" (or similar wording);

(b) whilst SSSHL acted as security trustee, holding security provided by Model 2 Borrowers on behalf of Model 2 Investors/Lendy and legal action to enforce that security would be regarded as taken in SSSHL's name, clause 8.1.3 of the Model 2 Investor Terms provides that Model 2 Investors authorise Lendy to give instructions to SSSHL with regard to the enforcement of the security which it held. It is common ground that it was Lendy that decided when and how to enforce Model 2 Security and took enforcement action using its staff and not SSSHL. As the choices on enforcement action were made by Lendy, I am satisfied that it was in practice Lendy that acted as agent for Model 2 Investors in making those choices, notwithstanding that legal title to the Model 2 Security was held in and enforcement action was taken in SSSHL's name; and

(c) the Model 2 Investors were aware that Lendy was in business to make a profit and were aware that Lendy was charging fees and non-default interest to Model 2 Borrowers. However, for the reasons I have set out in paragraphs 162-186 above I am satisfied that:
(i) Model 2 Borrower Loan Agreements were not easily accessible to Model 2 Investors (they were not on the Lendy Platform);
(ii) details of Default Interest charged to Model 2 Borrowers were only contained in the Model 2 Borrower Loan Agreements;
(iii) Lendy might have been willing to provide Model 2 Borrower Loan Agreements to Model 2 Investors on request, but Model 2 Investors had no reason to believe, until at least August 2018, that Lendy was charging Model 2 Borrowers anything other than fees and the non-default interest (the FAQ section of the Lendy Platform said Lendy were charging non default interest at an average of 0.5% per month to Model 2 Borrowers, substantially less than Default Interest);
(iv) at least until the Amended Model 2 Investor Terms were produced in March 2018, the pronouncements made by Lendy to Model 2 Investors about recovering principal and interest owed to Model 2 Investors would suggest to Model 2 Investors that Lendy would not be competing with Lendy to get paid if there was a Model 2 Shortfall and from March 2018 the position was still not clear cut (the purpose of clause 13.3 of the Amended Model

2 Investor Terms was misrepresented to Model 2 Investors in the covering email and it was contradicted by the Recovery Policy published the following month (until the Amended Recovery Policy was produced in August 2018, a few weeks before the final Model 2 Borrower Loan was advanced)); and

(v) in consequence, Model 2 Investors in my judgment did have a reasonable expectation that Lendy would act in the interests of Model 2 Investors in recovering money from Model 2 Borrowers and enforcing Model 2 Security, notwithstanding that they knew that Lendy was in business to make a profit and charged fees and non-default interest to Model 2 Borrowers.

IN CHARGING DEFAULT INTEREST FOR ITS OWN ACCOUNT, DID LENDY ACT IN BREACH OF ITS FIDUCIARY DUTIES TO MODEL 2 INVESTORS?

Acting in Breach of Fiduciary Duties (Absent Informed Consent)

197. Ms Toube and Mr Gledhill agree that the fiduciary duties that an agent owes to its principal include:
    (a) a duty not to obtain a benefit from its position as agent without the informed consent of the principal; and
    (b) a duty to avoid conflicts of interest save, again, to the extent that the principal gives informed consent to the agent acting in circumstances that give rise to a conflict of interest.

198. Mr Gledhill says that Lendy breached both of those fiduciary duties that it owed to Model 2 Investors by charging Model 2 Borrowers Default Interest for its own account without obtaining the informed consent of the Model 2 Investors to Lendy doing so and thereby: (a) placed itself in a position in which its interests and those of Model 2 Investors would conflict if there was a Model 2 Shortfall; or (b) obtained an unauthorised benefit from its position as agent.

199. I am satisfied that charging substantial amounts of Default Interest in whole or in part for its own account would give rise to a conflict of interest for Lendy when it acted as agent for Model 2 Investors in pursuing Model 2 Borrowers who were in default and in enforcing Model 2 Security in three ways:
    (a) if there was a Model 2 Shortfall, then there at least may be competition between Lendy charging Default Interest to Model 2 Borrowers in whole or in part for its own account

and Model 2 Investor's claims to recover capital and interest owed to them by the Model 2 Borrower. Such a conflict would only not exist if Lendy always prioritised Model 2 Investor claims over its own claims. It is, however, far from clear that it did this (as it provided assurances to the FCA and Mr Powell that it would always prioritise Model 2 Investor claims over its own claims against Model 2 Borrowers, in spite of the content of the Amended Model 2 Investor Terms in March 2018, but then issued the Amended Recovery Policy in August 2018, which made it clear that Lendy would have priority for its charges/interest over Model 2 Investors);

(b) the conflict is all the more acute because SSSHL was given a discretion to determine the order in which liabilities owed by Model 2 Borrowers were discharged which discretion in practice was operated by Lendy, representing a further conflict if Lendy charged Default Interest in whole or in part for its own account because Lendy could choose whether to prefer itself for Default Interest or Model 2 Investors for their capital/interest; and

(c) if Lendy was entitled to all or a substantial part of Default Interest, then its financial interests would be best served by a Model 2 Borrower going into default and remaining in default for a substantial period of time, whereas Model 2 Investors' best interests might be best served by Model 2 Borrowers discharging capital and interest owed to them under the relevant Model 2 Borrower Loan on time or as soon as possible after they became overdue. This conflict would arise whether or not ultimately there was a Model 2 Shortfall.

200. Ms Toube emphasises that Lendy did not act as agent for Model 2 Investors in negotiating the terms of Model 2 Borrower Loan Agreements with Model 2 Borrowers because the Model 2 Borrower Loans were offered to Model 2 Investors after they had been negotiated and agreed between Lendy and the Model 2 Borrower. The Default Interest formed part of the Model 2 Borrower Loan and so, says Ms Toube, Lendy did not act as agent for the Model 2 Investors in agreeing that Model 2 Borrowers would pay Default Interest and therefore it owed no duty to disclose to Model 2 Investors that it was to receive Default Interest under the terms of the relevant Model 2 Borrower Loan Agreement. Mr Gledhill did not put his case on the basis that Lendy did act as agent for Model 2 Investors in negotiating the terms of the Model 2 Borrower Loan Agreements.

201. Having found that Lendy placed itself in a position where its own interests and those of the Model 2 Investors may conflict (in connection with Lendy acting as agent for Model 2 Investors in pursuing Model 2 Borrowers who were in default and enforcing Model 2 Security), it is not necessary for me to consider whether Lendy also received the benefit of Default Interest in whole or in part for its own account in the course of acting as agent for Model 2 Investors without the

informed consent of the Model 2 Investors and therefore in further breach of its fiduciary duties. For completeness I will, however, say that, absent the informed consent of the Model 2 Investors, Lendy did act in breach of its fiduciary duties by receiving Default Interest, wholly or partly for its own account, for the reasons that follow.

202. Model 2 Borrower Loan Agreements were standard documents and there is no evidence that clause 6.3 which provided for the charging of Default Interest was ever altered in any Model 2 Borrower Loan Agreement. Lendy did not therefore in any real sense negotiate with Model 2 Borrowers for the payment of Default Interest, it was included in every Model 2 Borrower Loan.

203. It seems to me that Lendy cannot escape the conclusion that it acted as agent for Model 2 Investors in agreeing Model 2 Borrower Loans with Model 2 Borrowers simply due to a timing issue:

(a) Lendy knew that the loan it was negotiating with Model 2 Borrowers would, once it was agreed, be offered to Model 2 Investors; and

(b) it seems to me that there is nothing in principle to prevent a party from acting as agent for an individual or individuals who have not yet been identified but who they know will be identified shortly, particularly if they will come from a class of persons already identified (here Model 2 Investors who had been admitted to the Lendy Platform).

204. In any event, even if Lendy did not act as agent for the Model 2 Investors in agreeing the terms of the Model 2 Borrower Loan Agreements with Model 2 Borrowers, in my judgment Lendy in:

(a) offering Model 2 Borrower Loans to Model 2 Investors to participate in;

(b) not providing Model 2 Borrower Loan Agreements on the Lendy Platform to be viewed by Model 2 Investors;

(c) including summary details on the Lendy Platform of the Model 2 Borrower Loans which were being offered to Model 2 Investors to participate in; and

(d) including in the FAQ section of the Lendy Platform details of non-default interest that Lendy charged to Model 2 Borrowers,

was accepting responsibility for informing Model 2 Investors of the material terms of the Model 2 Borrower Loan that they were being offered the opportunity to participate in (which Lendy signed as agent on their behalf), and created a reasonable expectation on the part of Model 2 Investors that Lendy would act in the best interests in the Model 2 Investors in providing Model 2 Investors with details of the material terms. Charging Model 2 Borrowers significant amounts of Default Interest in whole or in part for its own account was, in my judgment, material and should therefore have been disclosed when the relevant Model 2 Borrower Loan was offered on the Lendy Platform for Model 2 Investors to participate in.

Informed Consent

205. As for whether Model 2 Investors gave informed consent to Lendy charging Default Interest, Ms Toube refers to the decision of Simon J in *FHR European Ventures LLP v Cedar Capital Partners LLP* [2011] EWHC 2308 (Ch) in which Simon J said at paragraph 77 and 78 of his judgment *"It is not enough for an agent to tell the principal that he is going to have an interest in the purchase, or to have a part in the purchase. He must tell* [the principal] *all the material facts. He must make a full disclosure" and the burden of proof falls on the agent to prove that he has made full disclosure…."*. However, Ms Toube places particular reliance on what Simon J went on to say at paragraph 81(ii) of his judgment *"Where the principal knows the agent will receive a commission and could have discovered what the commission was, but did not take the trouble to enquire, a misapprehension as to the amount of the commission will not mean that there has been no informed consent …"*

206. On the premise (contrary to my finding on Issue 5) that Lendy was entitled to Default Interest, in whole or in part, I am not satisfied that there has been full disclosure of the material facts to Model 2 Investors that: Default Interest was being charged to Model 2 Investors; that it was charged wholly or partially for Lendy's account; or that Lendy may compete with Model 2 Investors in the event of a Model 2 Shortfall:

(a) Ms Toube says that Model 2 Investors were told that Lendy earned fees and non-default interest. However they were not told about the very substantially higher Default Interest, charged to Model 2 Borrowers and there was nothing to alert Model 2 Investors to the existence of Default Interest until August 2018 (shortly before the last Model 2 Borrower Loan was advanced) and even then there was only a fleeting and oblique reference to Default Interest when Lendy told Model 2 Investors that it would pay a portion of Default Interest to them as a bonus accrual. This situation is different from that to which Simon J was referring in *FHR* where a principal is put on inquiry that the agent is receiving something, by way of commission, but is given no detail of what that commission is. Here, Model 2 Investors were told about fees and non-default interest earned by Lendy but (at least until August 2018) nothing about Default Interest, they were not therefore put on enquiry that Lendy was earning anything in addition to the fees and non-default interest which had been disclosed to them;

(b) in my judgment, Model 2 Investors will have reasonably believed until at least March 2018 that Lendy would prioritise payment of Model 2 Investors capital and interest over any sums charged by Lendy to Model 2 Borrowers. Even in March 2018, the effect of clause 13.3 of the Amended Model 2 Investor Terms was misrepresented to Model 2 Investors and was contradicted a month later by the Amended Recoveries Policy. So long as Model 2 Investors

thought that Lendy ranked, for any money owed to it by Model 2 Borrowers, behind Model 2 Investors, in a Model 2 Shortfall, the charges that Lendy levied to Model 2 Borrowers would appear to have little material effect upon Model 2 Investors; and

(c) therefore, Model 2 Investors were not alerted either to the fact that Lendy was earning Default Interest (or its very high amount) or that what Lendy was charging Model 2 Borrowers and that might result in Lendy competing for payment of that Default Interest (in a Model 2 Shortfall) with Model 2 Investors claims for capital and interest.

An Equitable Allowance?

207. Here I am considering whether an equitable allowance should be paid to Lendy in circumstances where, contrary to my finding on Issue 5, Lendy is entitled in whole or in part to Default Interest charged to Model 2 Borrowers, but for its breach of its fiduciary duties to Model 2 Investors.

208. It is common ground that the question of whether Lendy should receive an equitable allowance only applies to the pre-administration period because costs incurred by Lendy in collecting Default Interest after the appointment of the Administrators of Lendy, may be covered by a service charge which the parties have agreed in principle the Administrators of Lendy may charge to SSSHL (see further paragraph 155 above).

209. It is also common ground that *Lewin on Trusts (20th edition 2020)* ("*Lewin*") at *paragraph* 45 – *049,* sets out the basis of the jurisdiction to award an equitable allowance to a fiduciary who acts in breach of their fiduciary duties. Whilst the commentary refers to the awarding of an equitable allowance to a trustee, Mr Gledhill and Ms Toube agree that the principles apply to a fiduciary in the same way. Where relevant *paragraph* 45 – 049 of *Lewin* provides as follows (footnotes excluded):

"In ordering a trustee to account for a profit, the court may make him an allowance for his skill and labour in making the profit. The basis of this jurisdiction is that it is inequitable for the beneficiaries to take the profit without paying for the skill and labour which has produced it. The jurisdiction is to be exercised only in exceptional circumstances, and where to do so cannot have the effect of encouraging a trustee to put himself in a position of conflict of interest and duty. The conduct of the trustee will be taken into account in determining the scale of the allowance. For a trustee whose conduct is blameless, the scale might be liberal and might include a profit element; for a trustee whose conduct is open to criticism, the scale is likely to be less liberal; and for a trustee guilty of dishonesty or a surreptitious dealing there might be no award at all….".

210. Mr Gledhill says that it would not be appropriate to award Lendy an equitable allowance for the work that it has carried out in collecting Default Interest because:

(a) there is no windfall gain for Model 2 Investors, instead Model 2 Investors have suffered substantial losses;

(b) Lendy has already received arrangement and exit fees and non-default interest, and there is no evidence that Lendy will be substantially under-remunerated for its efforts in collecting Default Interest pre-administration if it is not paid an additional sum by way of equitable allowance;

(c) Lendy must already have received a substantial amount of Default Interest pre-administration which cannot now be recovered by the Model 2 Investors so it cannot be right that this Court provides Lendy with any additional remuneration;

(d) Lendy acted wrongfully at least in failing to provide copies of Model 2 Borrower Loan Agreements to Model 2 Investors and effectively hiding the charging of Default Interest from Model 2 Investors; and

(e) Lendy's non-disclosure of Default Interest is made worse because of the regulatory context in which it took place. It is wrong to award an equitable allowance to Lendy when Lendy was regulated by the FCA and misled the FCA as to its intentions in relation to the priority of payments in the event of a Model 2 Shortfall, thereby avoiding the FCA requiring Lendy to disclose Default Interest to Model 2 Investors and gaining full authorisation from the FCA to operate a Peer-to-Peer lending platform.

211. Ms Toube says:

(a) the collection of Default Interest by Lendy did produce a benefit for Model 2 Investors and Lendy should be compensated for the time, effort and expense that it incurred in collecting that Default Interest;

(b) I should decide in principle whether Lendy should receive an equitable allowance and then the quantum of the equitable allowance can be assessed later. That will ensure that Lendy is not over compensated for the time and effort and costs that it expended pre-administration in collecting Default Interest; and

(c) there has been no breach by Lendy of the requirements set out in rule 6.1.9 of the Conduct of Business sourcebook ("COBS") issued by the FCA, because that rule requires the authorised firm to provide details of its charges to clients and commission paid to it by another party. The Default Interest charged to Model 2 Borrowers does not fall into either of those two categories.

212. Had I decided that Lendy was entitled, in whole or in part, to Default Interest collected from Model 2 Borrowers, I would not have ordered that Lendy should recover an equitable allowance

for the work that it carried out in collecting Default Interest prior to the appointment of the Applicants. My reasons are as follows:

(a) the jurisdiction is only to be exercised in exceptional circumstances and, in my judgment there are no exceptional circumstances here justifying the exercise of the jurisdiction in favour of Lendy, to the contrary, for the reasons set out below there are good reasons not to;

(b) whilst it is true that Model 2 Investors have suffered substantial losses by not recovering the capital and interest owed to them by Model 2 Borrowers, I do not consider that this rules out the possibility of awarding an equitable allowance to Lendy for any benefit Model 2 Investors will receive from the payment of Default Interest to them. It is, however, in my judgment, a factor against awarding Lendy an equitable allowance because if I allow an equitable allowance to Lendy then it will further increase the Model 2 Investors' losses (not as is normally the case, where an equitable allowance is allowed, where it merely reduces the principal's profit);

(c) Lendy has not satisfied me that it will not have received fair recompense for the administrative tasks undertaken by it before the appointment of Administrators, including the collecting of Default Interest. In the circumstances it is by no means clear that Lendy has incurred any time, cost and expense in collecting Default Interest which it has not already been remunerated for. Whilst Ms Toube's suggestion, that deciding at this stage only in principle that Lendy is entitled to an equitable allowance but leaving the quantum of the equitable allowance to be decided later would ensure Lendy is not over remunerated, I consider the burden falls on Lendy to demonstrate (before I order that an equitable allowance should be paid in principle and an inquiry as to how much should be paid) that there is a real possibility that it has not already received remuneration for the work which it undertook pre-administration, in collecting Default Interest, and it has not done so;

(d) although I have no direct evidence on this, I accept Mr Gledhill's point that it is likely that Lendy received a material amount of Default Interest pre-administration which the Model 2 Investors will not be able to recover. As the basis of the equitable jurisdiction is that the beneficiaries should account out of profit that they receive for the skill and labour expended in producing that profit:

(i) it cannot be right that the Model 2 Investors should account for an equitable allowance in relation to a profit that they may not have received/ will not receive; and

(ii) even if some Model 2 Investors have received or will receive Default Interest, I am not satisfied that Lendy should receive an equitable allowance taken out of any Default Interest paid to Model 2 Investors when Lendy has received and utilised for its own purposes Default Interest which it ought to have accounted to Model 2 Investors for; and

(e) whilst I have not found that Lendy deliberately hid from Model 2 Investors the fact that it was charging Model 2 Borrowers Default Interest, Default Interest was not referred to anywhere on the Lendy Platform until August 2018 (only a month before the last Model 2 Borrower Loan was advanced), and even then the reference was oblique (see paragraph 146(b) above). Importantly, however, I have found (see paragraphs 179-180) that Lendy did provide an assurance to the FCA that it would always ensure that Model 2 Investors would be paid interest and capital owed to them by Model 2 Borrowers, before Lendy received any payment itself from Model 2 Borrowers and that, based on that assurance, the FCA did not press Lendy to disclose the existence and quantum of Default Interest to Model 2 Investors. Lendy then went back on that assurance. These are factors against awarding an equitable allowance to Lendy because they amount, in my judgment, to surreptitious dealings by Lendy in respect of the Default Interest that it was charging to Model 2 Borrowers. The fact that Lendy may not have breached rule 6.1.9 of COBS does not detract from this point.

ISSUE (6)

213. Issue (6) is- *"Were any of the relevant clauses in the Model 2 Investor Terms not properly incorporated into the contract between Lendy and Model 2 Investors (on the basis that they were onerous or unusual or otherwise)?"*

214. Mr Gledhill agreed that, as Ms Toube has confirmed that she does not rely upon any term in the Model 2 Investor Terms to support her case on Issue 10 (other than by way of general background), the question of incorporation of terms into the contract between Lendy and the Model 2 Investors does not arise.

ISSUE (7)

215. Issue (7) is- *"Do any of the relevant clauses in the Model 2 Investor Terms constitute 'unfair terms' under Part 2 of the Consumer Rights Act 2015?"*.

216. Mr Gledhill only relies upon Part 2 of the Consumer Rights Act 2015 in challenging Lendy's claim to all or part of the Default Interest collected from Model 2 Borrowers. In those circumstances, it is common ground that Issue 7 only needs to be decided by me if:

(a) Lendy is contractually entitled to the Default Interest charged to Model 2 Borrowers in whole or in part for its own account (I have found it is not); and

(b) Lendy, in the course of acting as agent for Model 2 Investors, in charging Model 2 Borrowers Default Interest wholly or partly for its own account: (i) obtained a benefit for itself; and/or (ii) placed itself in a position where its own interests and those of the Model 2 Investors for whom it acted as agent conflicted (I have found they did); but

(c) the Model 2 Investors gave informed consent to Lendy obtaining such benefit/placing itself in such a position of conflict (I have found they did not).

217. Given what is common ground between Mr Gledhill and Ms Toube and my findings in relation to Issues 5 and 8, it is unnecessary for me to deal with Issue 7.

ISSUE (9)

218. Issue (9) is – *"Based upon the answers to the questions in issues (5)-(8), do the Model 2 Investors and/or the Model 2 Transferees have a legal or equitable proprietary interest in any of the following:*

(a) any Default Interest payable by a Model 2 Borrower to Lendy under a Model 2 Borrower Loan Agreement;

(b) standard interest payable by a Model 2 Borrower to Lendy under a Model 2 Borrower Loan Agreement; and

(c) any of the fees payable by a Model 2 Borrower to Lendy pursuant to a Model 2 Borrower Loan Agreement."

219. Mr Gledhill does not advance a claim on behalf of Model 2 Investors to a legal or proprietary interest in standard interest (that is non-default interest) or the fees payable under the Model 2 Borrower Loan Agreements to Lendy. He confines Model 2 Investors' claims to Default Interest.

220. Mr Gledhill accepts that, for the purposes of Issue 9, and based on my findings in relation to Issue 5, the position is as set out in a Ms Toube's skeleton argument namely (in summary):

(a) the Model 2 Investors/Transferees can assert an equitable proprietary interest in Default Interest received by Lendy in respect of the particular Model 2 Borrower Loan in which they have participated;

(b) the relevant proceeds must be capable of being traced in accordance with the equitable rules of tracing. If the proceeds cannot be traced, then no proprietary claim would exist; and

(c) in the alternative to a proprietary claim, the Model 2 Investors/Transferees would be entitled to claim an account of profits from Lendy, but this is a personal remedy and would rank as an unsecured provable claim.

ISSUE 10

221. Issue (10) is –**"***Should the Secured Liabilities be discharged pro rata between Lendy on the one hand, and Model 2 Investors and/or Model 2 Transferees on the other hand, or in some other manner?"*

222. Having decided that legal title to Default Interest lies with the Model 2 Investors and not with Lendy (in whole or in part) and in light of the fact that I have been told that non-default interest and fees were deducted by Lendy from the initial advance to the Model 2 Borrowers and applied for its own account, relatively little may depend, in value terms, upon the answer to Issue 10, nonetheless I will endeavour to answer it.

THE RELEVANT TERMS

223. Clause 21.1 of the Model 2 Debenture provides:

"All monies received by the Security Agent, a Receiver or a Delegate pursuant to this deed, after the security constituted by this deed has become enforceable, shall (subject to the claims of any person having prior rights and by way of variation of the LPA 1925) be applied in the following order of priority:

- 21.1.1 in or towards payment of or provision for all costs, charges and expenses incurred by or on behalf of the Beneficiaries, the Security Agent, (and any Receiver, Delegate, attorney or agent appointed by it) under or in connection with this deed, and of all remuneration due to any Receiver under or in connection with this deed;

- 21.1.2 in or towards payment of or provision for the Secured Liabilities in any order and manner that the Security Agent determines; and

- 21.1.3 in payment of the surplus (if any) to the Borrower or other person entitled to it."

224. Clause 15.1 of the Model 2 Legal Charge is in materially identical terms to clause 21.1 of the Model 2 Debenture.

225. "*Secured Liabilities"* are defined (in both the Model 2 Debenture and the Model 2 Charge) as *"all present and future monies, obligations and liabilities of the Borrower to the Beneficiary whether actual or contingent and whether owed jointly or severally, as principal or surety or in any other capacity together with all interest (including without limitation, default interest) accruing in respect of those monies, obligations or liabilities pursuant to any Finance Document"*.

226. *"Beneficiaries"* includes Lendy, SSSHL and Model 2 Investors/Transferees.

THE PARTIES' POSITIONS

227. Ms Toube, for the Applicants, says that SSSHL's discretion as Security Trustee can only properly be exercised by applying the proceeds pro rata between the Secured Liabilities (that is Lendy and the Model 2 Investors/Transferees). Mr Gledhill, for Ms Taylor, says that I can and should direct that the liabilities owed to Model 2 Investors/Transferees by Model 2 Borrowers are paid in priority to the liabilities that they owe to Lendy.

228. Ms Toube's case in summary is as follows:

a. the purpose of the trust was both to pay capital and interest to Model 2 Investors and to pay costs and interest to Lendy, not simply to pay capital and interest to Model 2 Investors;
b. the discretion must be exercised honestly and in good faith, not arbitrarily, capriciously or irrationally (*Braganza v BP Shipping Ltd* [2015] 1 WLR 1661 (SC)). Only a pro rata distribution would satisfy those tests;
c. the conduct of a beneficiary should not be treated as a factor relevant to the exercise of a discretion as to how money should be distributed between beneficiaries;
d. even if the conduct of a beneficiary is a relevant factor, now that Lendy is in administration, any monies that are paid to Lendy will go to its unsecured creditors including HMRC which is owed some £5.5 million. Punishing Lendy for its conduct is therefore punishing its unsecured creditors which the Court should not do;

e. as the Applicants, being the Administrators of Lendy, have a statutory duty to treat creditors fairly (paragraph 74 of Schedule B1 to the Insolvency Act 1986 and *Re Condon, ex p James* (1873-74) LR 9 Ch App 609)) only a pro rata distribution would be fair;

f. clause 12.7 of the Model 2 Investor Terms provides that, if there is a shortfall… "The lenders [Model 2 Investors] shall only be entitled to recover their proportionate share of such recoveries"; and

g. it is accepted that, in his email to the FCA dated 16 March 2018, Mr Coles, Lendy's Head of Compliance, informed the FCA that Lendy would prioritise sums owed to Model 2 Investors ahead of any interest and costs owed to Lendy, however that assurance is inconsistent with clause 21.1.2 of the Model 2 Debenture and clause 12.7 of the Model 2 Investor Terms, which did not provide for the Model 2 Investors to be given priority over Lendy. In any event:

(i) there is no evidence that the email 16 March 2018 was distributed to Model 2 Investors (so there is no question of an estoppel); and

(ii) there is no need for the Court to reach any conclusion as to whether Mr Cole was trying to mislead the FCA, because the email cannot be relevant to the construction of clause 12.1.2 of the Model 2 Debenture.

229. Mr Gledhill's case for Ms Taylor in summary is:

(a) the main purpose of the trust was to ensure, so far as possible, that capital and interest due to Model 2 Investors were recovered and paid to them, if there was a default, and it was fundamental to Lendy's ability to raise capital that it could provide reassurance to Model 2 Investors of this;

(b) SSSHL, as trustee has surrendered its discretion to decide upon the priority in which distributions should be made to the Court, which should act "as a reasonable trustee could be expected to act in the circumstances";

(c) there is nothing in *Braganza* to suggest that, where a trustee has a discretion to distribute a fund amongst a class of beneficiaries, pro rata distribution is the only rational or proper basis on which the discretion can be exercised. If the position were otherwise, then in reality there would be no discretion;

(d) if the Court exercises a discretion instead of a trustee, it is similarly not constrained to do so on a pro rata basis (*McPhail v Dalton* [1971] AC 424 (HL) *2* per Lord Wilberforce);

(e) simply because assets received by the Administrators of Lendy have to be applied by them pro rata in discharge of creditor's claims does not justify the Court distributing the security proceeds pro rata between Model 2 Investors on the one hand and Lendy on the other. The trust is not insolvent and the Court is exercising its own discretion;

(f) Lendy's behaviour/representations on the question of priority are relevant to the exercise of the Court's discretion:

(i) clause 12.7 of the Model 2 Investor Terms is consistent with Lendy not making claims against security proceeds where there is a shortfall;

(ii) in communications sent by Lendy to Model 2 Investors it was represented that protecting the position of Model 2 Investors was Lendy's top priority;

(iii) the effect of clause 13.3 of the Amended Model 2 Investor Terms was misrepresented in the email sent to Model 2 Investors enclosing a copy of it. That email suggested that the clause was intended to strengthen the position of Model 2 Investors but it undermined their position by providing that, if there was a shortfall, amounts due to Lendy would be prioritised over monies due to Model 2 Investors;

(iv) Lendy told the FCA in March 2018 (addressing the FCA's concern about clause 13.3 of the Amended Model 2 Investor Terms) that Lendy always subordinated its claims for fees and interests to those of Model 2 Investors;

(v) Lendy did not supply copies of Model 2 Borrower Loan Agreements on the Lendy Platform and so Model 2 Investors had no way of knowing what interest/costs Lendy was charging Model 2 Borrowers other than what Lendy told them. The FCA told Lendy on 13 March 2018 that it considered that details of all fees and interest charged by Lendy to Model 2 Borrowers was material information that Model 2 Investors should be provided with in, order for them to decide whether or not they wished to invest. The FCA did not however pursue the point after being told by Lendy (on 16 March 2018) that it would prioritise capital and interest owed to Model 2 Investors over costs and interest due to Lendy (which on the face of it meant that the level of fees and interest charged by Lendy to Model 2 Borrowers would have no direct effect on the risks of Model 2 Investors not recovering their investments);

(vi) the Recovery Policy published in April 2018 confirmed that Lendy would only appropriate monies received from Model 2 Borrowers for its interest and costs once all monies owed to Model 2 Investors had been paid;

(vii) Mr Powell pointed out the discrepancy between clause 13.3 of the Amended Model 2 Investor Terms and the Recovery Policy and was assured that the Recovery Policy was correct, and the Amended Model 2 Investors Terms would be amended to be brought in line with the Recovery Policy. In the event, Lendy produced an Amended Recovery Policy, apparently placed on the Lendy Platform in August 2018 which deleted the reference to Model 2 Investors being paid ahead

of Lendy and instead said that the order of priority of payments would be, as in the Amended Model 2 Investors Terms;

(viii) the Recovery Policy (which said that Model 2 Investors would have priority) was sent to Model 2 Investors by email, the Amended Recovery Policy was simply placed on the Lendy Platform with no announcement; and

(ix) in those circumstances it is fair for the Court to exercise its discretion to distribute Model 2 Security proceeds to Model 2 Investors in priority to Lendy. This would give effect to the main purpose of the trust and it would be unconscionable to allow Lendy to participate in the limited funds available, given its conduct; and

(g) Lendy's insolvency should make no difference because:

(i) under the Model 1 structure, Lendy was both the lender and charge holder, when the move was made to the Model 2 structure, Lendy could still have been chargeholder, holding realisations on trust for investors. Instead of that, SSSHL was put in place as security trustee to protect the security structure from the insolvency of Lendy;

(ii) it would be strange if Lendy's insolvency was a matter of weight in the exercise of the Court's discretion when the sole purpose of appointing SSSHL as security trustee was to protect the security structure from an insolvency of Lendy;

(iii) equity still favours Model 2 Investors over Lendy's unsecured creditors because Lendy's unsecured creditors must be taken to have been willing to run the risk of Lendy's insolvency; and

(iv) harm to Model 2 Investors if the discretion is not exercised in their favour is obvious, as many Model 2 Investors are elderly and/or of limited means, whereas harm to Lendy's unsecured creditors is not; and

(v) Lendy's unsecured creditors include substantial claims made by or by parties associated with Lendy's director/senior employees.

DISCUSSION AND CONCLUSION ON ISSUE 10

The Purpose Of The Trust

230. Mr Gledhill says that the purpose of the trust was to demonstrate that Model 2 Investors would be protected from the insolvency of Lendy, by appointing SSSHL as security trustee and vesting Model 2 Security in it, so that Lendy could attract investors to the Lendy platform.

231. Mr Gledhill may be right as to why Lendy established SSSHL as security trustee, but the motive for establishing SSSHL as security trustee is not necessarily the purpose of the trust.

232. In my judgment, the purpose of the trust, as is clear from clause 21.1 of the Model 2 Debenture, is to realise Model 2 Security, in order (subject to first paying the costs, charges and expenses incurred in enforcing Model 2 Security) to discharge the "Secured Liabilities" which is principally the capital and interest due to Model 2 Investors and cost fees and interest due to Lendy.

The Basis On Which The Discretion Should Be Exercised

233. I accept Mr Gledhill's submissions that:

(a) SSSHL has surrendered to the Court SSSHL's discretion to decide how the Model 2 Security proceeds should be applied as between the Model 2 Investors who participated in the relevant Model 2 Borrower Loan and Lendy. I am not therefore concerned with reviewing the exercise by SSSHL of its discretion as trustee, but instead with exercising the Court's discretion ("the Discretion");

(b) any duties that the Administrators of Lendy owe to its creditors to act fairly between them is not relevant to the exercise of the discretion that the Court has to decide regarding how the proceeds of Model 2 Security should be distributed, as between the relevant Model 2 Investors and Lendy. This is because:

(i) SSSHL and not Lendy is the trustee;

(ii) the trust (that is the trust, the subject matter of which is the proceeds of the Model 2 Security) is not insolvent; and

(iii) I am, as already noted, exercising the Discretion as to how the Model 2 Security proceeds should be distributed; and

(c) in exercising the Discretion, I should act *"as a reasonable trustee could be expected to act having regard to all in the circumstances"* (*Lewin paragraph* 39-099);

Is A Pro Rata Distribution The Only "Proper" Distribution?

234. Ms Toube refers to *Braganza* as confirming that where a party exercises a discretion, they must do so honestly and in good faith, and should not exercise the discretion arbitrarily, capriciously or irrationally.

235. The circumstances in *Braganza* were very different to this case, because in *Braganza* the defendant was exercising powers to hold an inquiry as to the circumstances of the death of the claimant's

husband, its employee, the outcome of which affected the defendant's obligation to pay death in service benefits to the claimant. There is nothing, says Mr Gledhill, in *Braganza* which supports the conclusion that the discretion, in this case can only be exercised in favour of a pro rata distribution, as between the relevant Model 2 Investors and Lendy. If that was the case, says Mr Gledhill, then there would be no real discretion vested in SSSHL (surrendered by it to the Court).

236. In support of his proposition, that a proper exercise of an absolute discretion to choose between beneficiaries, can involve an unequal division of the fund amongst the beneficiaries, Mr Gledhill refers to the judgment of Chadwick LJ in *Edge v Pensions Ombudsman* [2000] Ch 602 (CA). In that case, the trustees of a pension scheme decided to exercise their discretion, concerning the application of a surplus held in the scheme, by returning some of the surplus to the employers and by reducing the contributions of and enhancing the benefits of employee members of the scheme, but not enhancing the benefits of pensioners.

237. The Pensions Ombudsman took the view that the trustees had acted in breach of trust in failing to act impartially as between the two classes of beneficiary (employees and pensioners). The trustees were employees and the Pensions Ombudsman considered that they had placed themselves in a position of conflict by preferring the interests of employees (including themselves) to those of pensioners. The Pensions Ombudsman directed that the amendments that the trustees had carried out to the scheme to allocate the surplus be set aside. The trustees appealed to the High Court against the Pensions Ombudsman's decision. The High Court allowed their appeal. The appeal of the Pensions Ombudsman to the Court of Appeal was dismissed.

238. The trustees said that the basis of their decision to return part of the surplus to the employers and the remainder of the surplus to employees was that they wanted to increase the number of employee members in the scheme which numbers had been falling (by providing additional benefits to employees), and wished to assist employers to survive the recession, thereby also helping to maintain membership numbers.

239. At page 627 D-F of *Edge*, Chadwick LJ said as follows:

"Properly understood, the so-called duty to act impartially - on which the ombudsman places such reliance – is no more than the ordinary duty which the law imposes on a person who is entrusted with the exercise of a discretionary power: that he exercises the power for the purpose for which it is given, giving proper consideration to the matters which are relevant and excluding from consideration matters which are irrelevant. If pension fund trustees do that, they cannot be criticised if they reach a decision which appears to prefer the claims of one interest – whether that

of employers, current employees or pensioners – over others. The preference will be the result of a proper exercise of the discretionary power."

240. I am satisfied that the Discretion may be exercised other than by directing that Model 2 Security proceeds are distributed pro rata in accordance with the debts owed by the relevant Model 2 Borrowers to Lendy and to the relevant Model 2 Investors. It seems to me, nonetheless, that the starting point ought to be a pro rata distribution between Lendy and the relevant Model 2 Investors and that I should then consider, if there are any factors which justify my exercising the Discretion in any other way. This is because, I accept that, absent any reason not to, a pro rata distribution is prima facie the fairest and for that reason the proper way of distributing Model 2 Security proceeds between Lendy and the relevant Model 2 Investors. In *Edge*, the trustees set out the reasons why they had chosen to apply the surplus to employers and in-service employees and not to pensioners. The Court of Appeal was satisfied that that was a proper exercise of their discretionary power but if there had been no good reason to pay the surplus to employers and in-service employees and not to pensioners, then it seems to me that a pro rata distribution of the surplus would have been appropriate in that case.

IS THE CONDUCT OF LENDY RELEVANT TO THE EXERCISE OF THE DISCRETION?

241. Ms Toube submitted that, where a trustee has an unfettered discretion (as the Court has here) to decide between beneficiaries as to how a trust fund should be distributed, the conduct of the beneficiaries is not a relevant matter to be taken into account in the exercise of that discretion.

242. Whilst no authority has been brought to my attention in support of or against Ms Toube's submission, it seems to me that the conduct of a beneficiary can, in principle, be a relevant factor for a trustee to take into account in exercising an unfettered discretion to apply a trust fund between beneficiaries. For example, in the case of a simple family discretionary trust, giving an absolute discretion to trustees to allocate the trust fund amongst family beneficiaries, the trustees may well consider what the beneficiaries have done with funds previously distributed to them in deciding on future distributions. If a beneficiary has frittered away money already distributed to them by the trustees, then it seems to me that the trustees could legitimately decide that the purpose of the trust is to provide "tangible benefits" to the beneficiaries and that they should therefore prefer beneficiaries who have not frittered away distributions already made to them (thereby retaining tangible benefits for themselves) when deciding how to make future distributions (or at least consider it as a factor relevant to the exercise of their discretion). When it is appropriate to take the

conduct of beneficiaries into account must be a fact sensitive question, having regard to the purpose of the trust.

243. I will consider first whether Lendy's conduct and the other matters to which Mr Gledhill refers would justify my exercising the Discretion in favour of the Model 2 Investors, without taking into account the fact that Lendy is in administration. I will then go on to consider whether the fact that Lendy is in administration makes any difference to the exercise my discretion.

Ignoring the fact that Lendy is in Administration, should I exercise the Discretion in favour of the Model 2 Investors?

244. I have already found (see paragraphs 169-186 above) that:

(a) prior to 5 March 2018, Lendy gave general assurances to the Model 2 Investors that they were its number one priority and that it would ensure, where possible, that Model 2 Investors would be paid in full and on time. Lendy did not however specifically state, prior to 5 March 2018, whether Lendy or Model 2 Investors would have priority in relation to monies owed to them by Model 2 Borrowers, if there was a Model 2 Shortfall;

(b) on 5 March 2018, when publishing the Amended Model 2 Investor Terms, Lendy misrepresented clause 13.3 of those terms as *"strengthening"* the position of Model 2 Investors in the event of a distressed sale. In fact, clause 13.3 provided for Lendy to receive sums owed to it by Model 2 Borrowers in priority to sums owed by Model 2 Borrowers to Model 2 Investors (subject to SSSHL/Lendy's discretion to alter the order of priority);

(c) the Recovery Policy issued on 13 April 2018 contradicted clause 13.3 of the Amended Model 2 Investor Terms by saying that funds received from a Model 2 Borrower (save for an extension to the loan) would be applied to pay all amounts due to Model 2 Investors before Lendy received any sum due to it;

(d) the FCA and Mr Powell raised concerns about clause 13.3 of the Amended Model 2 Investor Terms (in the case of Mr Powell, he pointed out that clause 13.3 was inconsistent with the Recovery Policy);

(e) on 16 March 2018, Mr Coles, Lendy's Head of Compliance, sent an email to the FCA assuring it that Lendy would always prioritise money owed to Model 2 Investors over money owed to Lendy. After receiving this email, the FCA did not pursue concerns raised in its email of 13 March 2018 to Lendy, that Lendy had not disclosed full details of fees, interest and other charges that it required Model 2 Borrowers to pay to it, and, on 17 July 2018, the FCA granted full authorisation to Lendy to operate a Peer-to-Peer lending

platform (having previously indicated, on 6 March 2018, that the FCA was in the process of preparing a *"minded to refuse"* full authorisation letter);

(f) but for Mr Coles providing the assurances that he did in his email of 16 March 2018, the FCA would have:

(i) continued to pursue issues of priority as between Lendy and the Model 2 Investors and disclosure by Lendy to Model 2 Investors of fees and interest charged by Lendy to Model 2 Borrowers; and

(ii) likely refused to grant full authorisation to Lendy to operate a Peer to Peer lending platform (or at least refuse unless it disclosed to Model 2 Investors full details of costs, fees and interest it was charging to Model 2 Borrowers);

(g) as for Mr Powell's correspondence with Lendy, I have found that he was assured that the Recovery Policy was correct and that clause 13.3 of the Amended Model 2 Investor Terms would be amended in order to confirm that Model 2 Investors have priority over Lendy for sums owed to them by Model 2 Borrowers;

(h) Lendy went back on the assurances that it gave to the FCA and Mr Powell (that Model 2 Investors would have priority over Lendy), by producing the Amended Recovery Policy in August 2018 which it published on the Lendy Platform;

(i) Lendy did not send the Amended Recovery Policy to Model 2 Investors by email (as it had done with the Recovery Policy) or in any other way highlight the introduction of the Amended Recovery Policy or how it had been amended, nor did it revert either to the FCA or to Mr Powell to confirm that it had changed its mind and decided that Lendy should rank in priority to Model 2 Investors in relation to monies owed to it by Model 2 Borrowers; and

(j) in respect of Default Interest, Lendy:

- treated Default Interest as its own (notwithstanding that I have found that legal title to Default Interest belonged to Model 2 Investors);
- did not disclose that it was charging Default Interest to Model 2 Borrowers; and
- breached its fiduciary duties, as agent to Model 2 Borrowers in treating Default Interest as its own (alternatively, if, contrary to my finding on Issue 5, Lendy was entitled to Default Interest, in whole or in part, then I have found that Lendy breached its fiduciary duties to Model 2 Investors by putting itself in a position where its interests and those of Model 2 Investors conflicted; and in obtaining the benefit of Default Interest for itself, in either case without the informed consent of Model 2 Investors).

245. I have found that the purpose of the trust was to discharge capital and interest due to Model 2 Investors and costs, fees and interest properly due to Lendy. I consider that the behaviour of Lendy, which I have summarised in paragraph 244 above, is not only relevant to the question of how I should exercise the Discretion, but determines that I should exercise the Discretion in favour of

Model 2 Investors ranking ahead of Lendy for Model 2 Security proceeds, there being no countervailing factors against that conclusion (leaving aside Lendy being in administration, which I will deal with later). My reasons are:

(a) overwhelmingly the most significant charge that could be levied on Model 2 Borrowers, after the advance of the Model 2 Borrower Loan, was Default Interest;

(b) Lendy appropriated Default Interest for its own use, even though I have found that legally it belonged to the Model 2 Investors, and the Model 2 Investors are very unlikely to be able to recover any Default Interest that was appropriated by Lendy for its own use prior to the Applicants being appointed as Administrators of Lendy (or, if contrary to my finding on Issue 5, Lendy is entitled to Default interest, then Lendy breached its fiduciary duties in the manner set out on the alternate basis in paragraph 244(j) above);

(c) Lendy did not disclose to Model 2 Investors that it was charging Default Interest to Model 2 Borrowers until at least August 2018 (a month before the final Model 2 Borrower Loan was advanced) and then Lendy only mentioned it in oblique terms, thereby preventing Model 2 Investors from challenging Lendy's right to the Default Interest or considering the effect of Lendy seeking to charge significant amounts of Default Interest for its own account, upon the ability of Model 2 Investors to recover capital and interest due to them (a point made by the FCA);

(d) after introducing the Model 2 structure, Lendy assured Model 2 Investors that recovering their capital and interest was its top priority. Model 2 Investors will be justifiably surprised, in light of those assurances, that Lendy: (i) was purporting to charge substantial amounts of Default Interest for its own account; (ii) was, pre-administration, at one point claiming to have priority over Model 2 Investors for the recovery of its charges and the Default Interest; and (iii) now wishes to rank pro rata with the Model 2 Investors for its charges;

(e) when Lendy did finally say something specific about priority, as between it and the Model 2 Investors, it did so by introducing the Amended Model 2 Investor Terms in March 2018, but in doing so it misrepresented the effect of clause 13.3 of those terms by suggesting that it had been introduced for Model 2 Investor protection when, in fact, for the first time it suggested that Lendy would have priority over sums due to Model 2 Investors for its charges and interest;

(f) Lendy then published the Recovery Policy a month later in April 2018 which was inconsistent with clause 13.3 of the Amended Model 2 Investor Terms, the Recovery Policy making it clear that Lendy would not receive any money from Model 2 Borrowers until Model 2 Investors have been repaid in full;

(g) when challenged by the FCA about charging Default Interest to Model 2 Borrowers without providing details of what it was charging to Model 2 Investors, Lendy provided a clear assurance to the FCA that it would always ensure that Model 2 Investors received payment

of all capital and interest due to them before Lendy received any fees and interest itself (including Default Interest) thereby assuring the FCA that what Lendy was charging in Default Interest to Model 2 Borrowers would not prejudice the prospects of Model 2 Borrowers recovering their capital and interest (assuming Lendy could, contrary to my finding above, charge Model 2 Borrowers Default Interest for its own account);

(h) Lendy then reneged on the assurances it gave to the FCA and to Mr Powell (that Model 2 Investors would have priority over Lendy in relation to monies owed to them by Model 2 Borrowers) but it never told either of them that it had done so, it simply amended the Recovery Policy and placed it on the Lendy platform in August 2018 without publicising this to Model 2 Investors; and

(i) on the basis that the purpose of the trust was to discharge capital and interest due to Model 2 Investors and costs, fees and interest properly due to Lendy, it seems to me that where Lendy:

- misappropriated Default Interest belonging to Model 2 Investors for its own use, and that Default Interest can no longer be recovered for Model 2 Investors;
- assured Model 2 Investors, up to publishing of the Amended Model 2 Investor Terms in March 2018, that recovery of their capital and interest was its number one priority; and
- assured the FCA and Mr Powell that, notwithstanding the content of the Amended Model 2 Investor Terms, Model 2 Investors would have priority over Lendy in the event of a Model 2 Shortfall, but then reneged on that assurance; it is appropriate to exercise the Court's discretion in favour of Model 2 Investors having priority over Lendy.

246. Again, if I am wrong about the answer to Issue 5 and Lendy is entitled to Default Interest, then Lendy has breached its fiduciary duties in the manner set out in paragraph 244 (j) above. In those circumstances, I would still take the view that the Discretion should be exercised in favour of the Model 2 Investors having priority over Lendy, because all of the points I make in paragraph 245 above as to why Model 2 Investors should have priority, would apply in those circumstances, save for the nature of Lendy's breach of fiduciary duty and that does not seem to me to be a basis on which the Discretion should be exercised differently.

Does the Administration of Lendy Make any Difference?

247. Ms Toube says that, even if Lendy's conduct would justify my exercising the Discretion in favour of the Model 2 Investors receiving Model 2 Security proceeds in priority to Lendy, Lendy is in

administration and therefore it is the unsecured creditors of Lendy (including HMRC, which is owed £5.5 million), who are wholly innocent of any wrongful conduct on the part of Lendy, who will suffer in consequence of my exercising the Discretion in that way. So, says Ms Toube, taking into account the interests of the unsecured creditors of Lendy, I should direct that Model 2 Security proceeds should be divided pro rata between Lendy and Model 2 Investors.

248. Mr Gledhill says that:

(a) many Model 2 Investors are retired with limited means and will be hit hard by their loss of capital;

(b) there is no evidence that hardship would be suffered by unsecured creditors of Lendy, if priority is given to the Model 2 Investors;

(c) a number of substantial unsecured claims lodged in the administration of Lendy have been lodged by "insiders" who may be regarded as responsible for the misconduct of Lendy, including Mr Brooke (statutory director of Lendy); and

(d) the unsecured creditors of Lendy can be taken to have run the risk of its insolvency, but not the Model 2 Investors.

249. Whilst I accept that what I am being asked to do is to exercise the Discretion that has been surrendered to the Court and that, in doing so, the effect of the exercise of the Discretion upon the unsecured creditors of Lendy could be a relevant factor to take into account, I do not think that I should look through Lendy, the party who I have found acted wrongfully and with a lack of commercial probity, to the effect of the exercise of the Discretion upon the unsecured creditors of Lendy. There are two reasons for this:

(a) even if I had good and reliable information as to what the effect upon Model 2 Investors on the one hand and unsecured creditors of Lendy on the other would be, according to how I exercise the Discretion, it would be difficult to come to a value judgment as to which group is the most deserving of the exercise of the Discretion in their favour. Each group is a disparate group containing individuals (and in the case of Lendy's unsecured creditors, legal entities of all kinds) who have significantly different resources and have incurred significantly different losses from the demise of Lendy. I cannot choose to benefit some members of one group and not others, I must choose to give priority to Model 2 Investors or direct a pro rata distribution of Model 2 Security proceeds, between Model 2 Investors and Lendy. Favouring one group or the other is likely to mean that some members of the unfavoured group may be more deserving than some members of the favoured group; and

(b) more importantly I have hardly any information about the effect upon Model 2 Investors on the one hand and unsecured creditors of Lendy on the other according to how I exercise the Discretion. I therefore consider it unsafe therefore to base the exercise of the Discretion

on some attempt to evaluate whether Model 2 Investors as a whole or the unsecured creditors of Lendy as a whole are more deserving of my exercising the Discretion in their favour.

250. If I am wrong and I should somehow try to evaluate how deserving the Model 2 Investors are compared to the unsecured creditors of Lendy then, on the information before me, it appears that the Model 2 Investors as a whole are more likely to be significantly affected by their losses than the unsecured creditors of Lendy as a whole and that some unsecured creditors of Lendy (or who may be unsecured creditors of Lendy) might be regarded as less deserving. This lends support to my conclusion that the administration of Lendy should not change my view that it is appropriate to exercise the Discretion in favour of the Model 2 Investors:

(a) a material number of Model 2 Investors may be in more dire need financially than Lendy's unsecured creditors, because, as Mr Gledhill says, it appears that, at least a material proportion of the Model 2 Investors are pensioners of relatively modest means who face losing their life savings or a substantial part of them. This is not however universally so: (i) Ms Taylor has substantial assets but has also suffered substantial losses as a result of becoming a Model 2 Investor; (ii) Mr Powell is of modest means but not close to retirement age and he has suffered relatively small losses; and (iii) Mr Melton and his wife are both pensioners and it appears that they did invest their life savings in Model 2 Borrower Loans and they have suffered substantial losses. They appear to answer Mr Gledhill's description of Model 2 Investors, in retirement, suffering dire financial consequences as a result of becoming Model 2 Investors;

(b) Lendy is pursuing substantial claims against its director, Mr. Brooke, alleging fraud, but Mr. Brooke is also the sole shareholder and director of LGL (Lendy's parent company) which claims that it is owed some £600,000 by Lendy. Mr Brooke may fairly be regarded as the directing mind of Lendy when the misconduct to which I have referred took place (being the only director active in the business at the material time and the only statutory director from 26 July 2018). There can be no set off of the claim that Lendy has against Mr. Brooke against the claim that LGL has against Lendy (although if a judgment is obtained by Lendy against Mr Brooke it may be able to enforce that judgment against his shareholding in LGL). In fairness I should say that the Administrators of Lendy say that LGL's claim is disputed;

(c) a former Financial Director of Lendy (not a statutory director) is making a substantial claim for unfair dismissal against Lendy, and if he is successful in his claim he will become a substantial unsecured creditor of Lendy, yet he also may be regarded as a party to the misconduct of Lendy to which I have referred ; and

(d) as Ms Toube says, by far the largest unsecured creditor of Lendy is HMRC which is owed around £5.5m of the estimated unsecured creditor claims of £8.5m. Whilst I accept that the collection of tax by HMRC is important and its failure to do so effects taxpayers generally, nonetheless, as against at least a substantial number of Model 2 Investors, HMRC might be regarded as less acutely in need of funds and better able to absorb what it will lose, if I exercise the Discretion in favour of the Model 2 Investors, compared to the ability of a substantial number of the Model 2 Investors to absorb what they will lose if I exercise the Discretion in favour of a pro rata distribution of Model 2 Security proceeds.