Neutral Citation Number: [2017] EWHC 1871 (QB)

Claim No: LM-2012-408

IN THE HIGH COURT OF JUSTICE

QUEENS BENCH DIVISION

LONDON MERCANTILE COURT

Date: 28 July 2017

(draft circulated 19 July 2017)

Before:

HIS HONOUR JUDGE WAKSMAN QC

(sitting as a Judge of the High Court)

BHL

Claimant

- and -

LEUMI ABL LIMITED

Defendant

Clive Freedman QC and Simon Mills (instructed by Eversheds Sutherland (International) LLP, Solicitors) for the Claimant

Nigel Tozzi QC and Simon Goldstone (instructed by Squire Patton Boggs (UK) LLP Solicitors) for the Defendant

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: 8-11 and 15-18 May 2017

INTRODUCTION

1. The Claimant in this action, BHL, is a Cayman Islands company. Its sole ordinary shareholder and director is and has at all material times been Lord Karan Bilimoria. He was the founding shareholder of Cobra Beer Limited ("Cobra"). The Cobra brand of beer is well known, originally sold in and for Indian restaurants but now sold generally around the world including, for present purposes, in UK supermarkets.

2. On 11 April 2008 and following a decision to change its invoice discounting provider, Cobra made a written Receivables Finance Agreement ("the RFA") with the Defendant in this action Leumi ABL Limited ("Leumi"), a subsidiary of Bank Leumi (UK) Plc. Following the global economic downturn later in 2008, Cobra began to suffer serious financial difficulties and ultimately was not able to secure the further investment it needed. Nor could it be sold as a going concern. Accordingly, on 29 May 2009 Cobra entered administration. At that time, substantial amounts were owed to it by its customers but in turn, it owed substantial sums to Leumi under the RFA.

3. The Cobra business was enabled to continue following Cobra's administration by the setting up of a separate company, Cobra Beer Partnership Ltd ("Cobra Partnership") in which BHL was a shareholder, and Cobra Partnership acquired Cobra's business. But in addition, BHL entered into a written Indemnity Agreement, also on 29 May 2009, with Leumi, Cobra and the administrators. By the Indemnity Agreement, BHL agreed in particular to indemnify Leumi in respect of any sums due under the RFA.

4. Following Cobra's administration, Leumi took over (although with the assistance of important third parties) the collection of Cobra's receivables on its sales ledger this being the essential source of repayment of the monies owed to it by Cobra under the RFA.

5. Those monies owed included not only the monies advanced to Cobra pursuant to the invoice discounting in the first place, but also certain additional fees charged by Leumi. One fee in particular lies at the heart of this case. It is a "collection fee" charged from 30 June 2009 at a rate of 15% on all receivables collected by Leumi as from 3 June 2009. In total, Leumi collected just over £8m which yielded a fee of some £1.2m. That fee, if payable, fell within BHL's indemnity obligation under the Indemnity Agreement.

6. Pursuant to demands made by Leumi on 11 November 2010 and 9 May 2011, BHL paid to it the sums of £400,000 and £550,000 respectively in relation to the outstanding collection fees. According to Leumi that left a further sum due which was originally said to be some £490,575.86 but which has now been corrected to £271,382.69. There is one short issue on the Counterclaim which I deal with below.

7. On 15 April 2012 BHL issued this present claim against Leumi. It alleges that (a) Leumi was not entitled to charge a collection fee at 15%, (b) BHL had paid the £950,000 to Leumi (referred to above) by mistake of law, and so (c) Leumi should now repay that sum to BHL. In response, Leumi contended that (a) it was entitled to claim a collection fee at 15%, (b) in any event there was no mistaken payment made by BHL and (c) BHL should now pay to Leumi the outstanding balance of the Current Account. I shall set out in more detail the issues arising in this dispute hereafter.

THE RELEVANT AGREEMENTS

The RFA

8. The broad scheme of the RFA is as follows. Cobra could present to Leumi invoices which had been rendered to its customers for the supply of beer and unless any given invoice was disapproved by Leumi, it would pay 90% of the value of the invoice to BHL. This is referred to in the RFA as the "Advance Percentage". Leumi maintained a current account with BHL ("the Current Account") which would record the value of all the advances made to BHL as debit items, along with Leumi's fees and charges. It would then credit to that account all the payments received in respect of those invoices which of course went directly into an account controlled by Leumi although the customers were not aware that the invoices had been discounted. So they thought that they were paying Cobra.

9. In addition, and so that the extent of the collectable receivables could be seen at any point, Leumi also maintained a Receivables Finance Account. This recorded the total outstanding receivables notified by Cobra to Leumi. Once a receivable was paid, its value was debited from the Receivables Finance Account (since it was no longer outstanding) and it was credited to the Current Account. In that way, once a receivable was fully paid, Leumi obtained the full purchase price for its receivable and this was duly credited to Cobra. So, assuming that the receivables were all fully paid, Leumi earned its ultimate profit from the Service Fee (set at 0.15% of each receivable) and the Discount Charge which had been set at 1.5% above base - both of which were subject to increase under clause 10.1 (b) - see below.

10. The sums to be advanced by Leumi to Cobra through the discounting of the invoices were not permitted to exceed £15m at any one time although this limit could be increased to £20m by mutual agreement later. In fact, the limit was increased to £18m. in late November 2008. The duration of the RFA was to be a minimum period of 24 months. Subject to the provisions described below, Cobra was to act as Leumi's agent for the collection of the Receivables. Cobra also agreed that as between itself and its customers, the invoices were payable not more than 90 days following the end of the calendar month during which the beer was delivered.

11. The RFA contained the following express terms:

    (1) By Clause 6.2 a.,

    > "All entries that Leumi make in any of the Client's accounts with Leumi, including records of transfers between accounts, are conclusive and binding on the Client unless they contain a manifest error. In any legal proceedings in connection with this Agreement, the Client will be bound by Leumi's certificate of the amounts due and owing from each of the Parties to the other."

    (2) By Clause 8.4 d.,

    > "The Client may not exercise any right of set-off or counterclaim against monies due from it to Leumi…"

    (3) By Clause 9,

    > "9.1 the Client will pay to Leumi the fees and expenses as set out in Schedule 4 to this Agreement.
    >
    > 9.2 the Client agrees and acknowledges that the sums due and which may become due to Leumi as set out in this Agreement (and the Schedules hereto) are reasonable and as such it is not considered by the Client that any such sums are penal.
    >
    > 9.3 the Client hereby agrees to be bound by any estimate that Leumi may make of such fees, costs and expenses where the same cannot be immediately ascertained and should Leumi include such an estimate in making any calculation under this Agreement such an estimate shall not constitute a manifest error for the purposes of clause 6.2."

    (4) By Clause 10 - COLLECTIONS FROM AND DEALINGS WITH DEBTORS

    > "10.1 Collections from Debtors

a. Leumi has the sole right (but is not obliged) to collect and enforce payment of each Receivable for as long as such Receivable is owned by it pursuant to clause 5.1.

b. If, at any time, Leumi requires the Client to disclose its interest in the Receivables and/or the Client ceases to act as its agent, Leumi shall be entitled to increase the Service Fee to up to 10% and increase the Discount Charge by up to 2% to cover its anticipated additional operating expenses in administering and collecting the Receivables and the Client expressly acknowledges that such increase constitutes a fair and reasonable pre-estimate of Leumi's likely costs and expenses in performing this service on the Client's behalf…".

(5) By Clause 13- TERMINATION

"13.1 Termination Events

Leumi may terminate this Agreement immediately by giving written Notice of termination to the Client upon or at any time after the occurrence of a Termination Event.

13.2 Consequences of Termination

a. Save as expressly provided in this Agreement to the contrary, termination of this agreement will not affect the rights and obligations of either the Client or Leumi in relation to Receivables assigned to Leumi prior to such termination, nor affect the continued accrual of Service Fees, Discount Charges or such other fees and expenses payable under this Agreement in relation to such Receivables..".

(6) By Clause 20 (b), in the event that "dilutions" (i.e. reduction of invoice value by, for example credit or debit notes) exceeded 5% in any given 3 months, Leumi reserved the right to reduce the Advance Percentage by 1% for every 1% the dilutions exceeded 5%;

(7) By paragraph 1 of Schedule 4, Cobra agreed to pay to Leumi, among other things, the Service Fee and such other fees as arose pursuant to the Agreement or as were otherwise agreed between the parties, and by paragraph 3, Cobra agreed to pay the Discount Charge.

(8) By paragraph 2 of Schedule 4 - Expenses -

"The Client will pay to Leumi

a. All bank charges and other costs and expenses… that Leumi may incur… in respect of any bank account to which payments of Receivables are to be credited; and

b. All legal, bank and other costs and expenses (plus any VAT if applicable) that Leumi may incur (including its own administrative and other costs) in any way relating to…

(ii) collecting, enforcing, securing or protecting its rights to or verifying the status or amount of any Receivable, or attempting or purporting to do any of the foregoing; and/or…"

(9) By Schedule 5, the following were included in a list of "Termination Events":

(a) by paragraph 5, if, in Leumi's reasonable view, the nature of the Client's business materially changes or the volume of the Client's business materially adversely changes;

(b) by paragraph 12, if Leumi considers, acting reasonably that there has been a material adverse change in the Clients business, assets or financial condition

(10) by Schedule 6, the following were said to be "Consequences of Termination"

(a) by paragraph 1 b.:

"Leumi may require the Client to repurchase from Leumi all Outstanding Receivables at the Recourse Price or (at the option of Leumi) in lieu thereof the Current Account balance. Upon unconditional receipt of such sum… in cleared funds… ownership of each such Receivable… will be reassigned to the Client…;"

(b) by paragraph 2:

> "if Leumi requires the Client to repurchase any Receivables and the Client fails to do so within 7 days of such demand, Leumi will be entitled to charge the Client an additional collection fee at up to 15% of amounts collected by Leumi thereafter. This collection fee is in addition to any other fee payable by the Client to Leumi under this Agreement. The Client expressly acknowledges that such fee constitutes a fair and reasonable pre-estimate of Leumi's likely costs and expenses in providing such service to the Client".

The Indemnity Agreement

12. This contained the following material provisions:

(1) By clause 2.1 (a), and with effect from the Indemnity Date, BHL would indemnify Leumi in respect of any amount due to Leumi but unpaid by Cobra in connection with the RFA. BHL would pay such amount as if it were the principal obligor;

(2) The "Indemnity Date" meant 6 months after the Effective Date or such earlier date as Leumi shall decide and notified to Cobra in writing, having concluded (acting reasonably) that they have expended all reasonable efforts to collect all outstanding receivables the subject of the RFA;

(3) The "Effective Date" meant the date when the business sale agreement made between the administrators of Cobra and Cobra Beer Partnership became unconditional.

<u>OVERVIEW</u>

13. Prior to its administration and as is frequently the case with invoice discounting, Cobra invoiced its customers without declaring that it was doing so as agent for Leumi. Payments were made into a designated bank account controlled by Leumi. By a letter of demand to Cobra dated 26 May 2009 Leumi required immediate payment of the monies due pursuant to the RFA in the sum of £7,741,756.93, alternatively the purchase of all the remaining collectables (in a higher sum). The letter stated that if neither event happened within 7 days (i.e. by 2 June 2009) then Leumi would proceed to collect the receivables itself and charge collection fees pursuant to the RFA.

14. No payment or purchase was made by Cobra and accordingly, as from 3 June 2009, Leumi was entitled to and did take over the collection of the receivables. Shortly afterwards, it informed Cobra that it would be charging a collection fee of 15% on all receivables collected. As at 3 June 2009 there was about £10.5m. worth of receivables.

15. Since 29 May 2009 Leumi has collected £8.1m. worth of receivables and since 3 June it had collected £7.188m. This difference reflects the fact that between the 29 May and 3 June alone it had collected around £918,000.

16. Most of the collections made by Leumi were made in the first few months. Indeed by the middle of September Leumi had collected over £7m.

17. Soon after taking over the collections, and by 30 June 2009, Leumi had hired Cobra's principal credit controllers, Mr Austin Anwar and Mr Anup Ladwa. It also used the services of a third party collection company called SJB and the legal services of its solicitors, Hammonds. All of those costs and fees were charged separately to Cobra and are not in dispute.

18. If one took the monies due under the RFA but stripped out Leumi's fees charged since 3 June 2009 then Leumi would have recouped sufficient from the collections to repay its capital exposure to Cobra under the RFA by 16 September 2009. The sums still owing to it after that date largely consisted of fees and in particular the collection fees which came to a total of about £1.2m.

THE ISSUES

19. These are as follows:-

Sums due to Leumi

(1) Upon a true construction of Schedule 6 paragraph 2, is Leumi entitled merely to its actual costs and expenses of the collections to be calculated after that exercise had ended and subject to a ceiling of 15% thereof i.e. here a ceiling of £1.2m.?

(2) If so, what were its actual costs and expenses?

(3) If not, was the true position that Leumi could charge any fee it wished and without reference to any anticipated or actual costs subject only to a maximum of 15%?

(4) If that is not right either, did Leumi have a discretion to charge a fee based on estimated or actual costs, but which could go no higher than 15% and if so how was it to be calculated?

(5) Is paragraph 2 of Schedule 6 a penalty clause?

(6) If Leumi did have a discretion as described in sub-paragraph (4) above, did it exercise it properly or at all here?

(7) If not, does this mean that Leumi has no claim at all pursuant to paragraph 2 of Schedule 6, or can and should the court fix an alternative fee based on what Leumi could lawfully have charged at the time; if the latter, what would the fee be?

Mistake

(8) If, as a result of the foregoing, BHL has in fact overpaid Leumi, by reference to the payments it made of £950,000 in respect of the collection fees, did BHL do so acting under a mistake of law at the time?

(9) If so, did that mistake cause these payments?

(10) If so, can BHL now recover all of the relevant part of such payments?

Counterclaim

(11) Is Leumi entitled to all or any part of the sum now claimed against BHL by way of counterclaim?

THE EVIDENCE

20. For BHL, I heard from Lord Bilimoria, Dynshaw Italia, a non-executive director of Cobra Partnership but also Cobra's Finance Director from 2001 and its Chief Operating Officer from June 2004, and Vimal Shah, a chartered accountant with PSJ Alexander & Co. who were BHL's accountants and who first became involved in February 2010.

21. For Leumi I heard from Alan Couzins, Leumi's Operations Director since June 2008, James Willis, a client manager since March 2008, Paul Hird, Leumi's CEO since its inception in 2006, and briefly from Robert Weekes, a partner in Squire Patton Boggs (UK) LLP, Leumi's solicitors (previously Hammonds).

22. In addition, there was expert evidence on the following issues:

(1) the extent to which the work carried out by Leumi in the collections was additional to the work it would have carried out in administering the facility if no termination event had occurred;

(2) whether the amount of work undertaken by Leumi in administering and collecting the receivables after 29 May 2009 was reasonably necessary;

(3) the cost to Leumi of providing such work;

(4) what costs might the parties have anticipated that Leumi would incur itself in administering and collecting receivables, had such consideration been made in April 2008 or May 2009; and

(5) a comparison between: the costs actually incurred by Leumi in administering and collecting receivables relating to Cobra, those that might have been anticipated in April 2008 or May 2009; and the 15% collection fee actually charged by Leumi.

23. In the event, the position as at April 2008 did not feature in the expert debate at trial to any real extent.

24. This expert evidence was given in the form of written reports and by way of oral evidence at trial by Peter Birch, a chartered accountant and partner at Deloitte LLP in its financial services audit department on behalf of BHL, and by David Lawler, an accountant and Managing Director of the London Forensic Investigations Group of Navigant, a forensic accounting firm, on behalf of Leumi.

25. This is not a case where there were any major disputes of primary fact. In general I thought that all of the lay witnesses did their best to assist the court. I should add, however, (and as explained below) that I do not accept that Lord Bilimoria was lying or being in any way dishonest in relation to the failure to disclose until some way into the trial, some legal advice which he had obtained from Edwin Coe in 2010.

26. As for the experts, in general I found Mr Birch a more persuasive and careful witness: as will be seen below, he had in my view much more useful experience of "collect-outs" such as the one in issue here and I felt he was less inclined to follow the views of his client as expressed in the witness statements, than Mr Lawler.

CONSTRUCTION OF SCHEDULE 6 PARAGRAPH 2

27. For ease of reference I reproduce paragraph 2 again here:

> "if Leumi requires the Client to repurchase any Receivables and the Client fails to do so within 7 days of such demand, Leumi will be entitled to charge the Client an additional collection fee at up to 15% of amounts collected by Leumi thereafter. This collection fee is in addition to any other fee payable by the Client to Leumi under this Agreement. The Client expressly acknowledges that such fee constitutes a fair and reasonable pre-estimate of Leumi's likely costs and expenses in providing such service to the Client".

28. BHL contends that paragraph 2 allows Leumi only to charge its actual costs and expenses of its collection which can only be done at the end of that process. The reference to "up to 15% of the amounts collected thereafter" is then simply a ceiling on the amount that can be claimed. I disagree for the following reasons:

(1) If BHL is right, the last sentence of paragraph 2 is meaningless and otiose. I agree that it is somewhat formulaic - the same wording is used in clause 10 (1) (b) - but that is not enough to justify disregarding the ultimate sentence altogether; rather this sentence suggests a charge set in advance of all the costs and expenses being known;

(2) Paragraph 2 does not say that it is limited to actual costs and expenses, unlike Schedule 4 paragraph 2, which does;

(3) While the provision refers to "the amounts collected hereafter" this is merely a reference to the collections by Leumi which (by definition) have yet to come. But that does not

mean that the collection fee is only to be calculated and the end of the collections process;

(4) It is hard to see why there needs to be a ceiling of 15% at all, if that is all the 15% reference now is; after all, in the provision which undoubtedly does refer to actual costs and expenses at paragraph 2 of Schedule 4, there is no such limit and in there one has the prospect of very substantial third-party costs;

(5) The scheme of the fee here mirrors the fees chargeable under clause 10 - they can be charged monthly and upfront so that Leumi is not out of pocket;

(6) Of course, if one moves away from actual costs and uses a percentage instead there is always the possibility of charging more costs than might be actually incurred at the end of the day but then that is a function of the term and the use of a monthly fee.

29. In support of its interpretation BHL relies on the case of *Yilport v Buxcliffe* [2013] 1 Ll Rep. 378. Here the Claimant port authority charged the Defendant owner of a ship the subject of a collision at sea, for its services in enabling the vessel to discharge in port. The Defendant said that it could only charge a reasonable amount for its services whereas the Claimant argued that it could charge effectively what it liked subject only to *Wednesbury* unreasonableness. The judge disagreed and upheld the Defendant's argument on the basis that this was a primary right to payment for services - it was not the exercise of discretion subject only to some modest limitations on its exercise.

30. I see all of that in the context of that case but I do not consider that the situation is analogous here. First, on a proper construction, the exercise of determining the "price" is to be done, or can be done, in advance as opposed to only after the work has been completed which is the point at which the costs can be calculated definitively. So on any view paragraph 2 of Schedule 6 connotes a future estimation. Second, in the case here, it is not as if the fee to be charged as a matter of content had to be reasonable. The exercise, being done in advance, is entirely different and the issue is one of process - namely having regard to relevant and not irrelevant materials and then performing a proper estimating exercise. Therefore I do not consider that *Yilport* assists BHL here.

31. Although it is a fee calculated at the outset and applicable consistently to every collection thereafter, this does not mean that Leumi has to decide on the appropriate rate at the very first opportunity. If it would be prudent to wait a short period when some imponderables might have resolved themselves, that could be done also.

32. Accordingly BHL's interpretation is ruled out, in my judgment, by the language and context of paragraph 2.

33. On that basis it is not necessary to undertake a calculation of Leumi's actual costs since these are not the benchmark for the fee. However, I have done so below, because they still have some relevance.

34. Therefore, Leumi has the right to charge an additional fee which is to be applied as a percentage of the collected receivables going forward. A preliminary question arises as to this clause is directed to or, as I put it in *Watson v Watchfinder* [2017] EWHC 1275, (Comm.) what is the "target" of the clause? Both before and during the hearing, Leumi's case was that it was directed to the setting of a fee to compensate Leumi for the additional costs and expenses which it (as opposed to third parties engaged by it) would be put to once it had taken over the collections. However, in its post-hearing note addressing the decision in *Watchfinder*, Leumi contended that the fee had no "target" at all and was not even directed to what the anticipated cost and expenses might have been. Rather it was an untrammelled discretionary power on the part of Leumi to

charge what it likes, provided that (a) it now assumed the role of collecting the receivables and (b) the 15% ceiling is not exceeded.

35. But on that analysis, and if there is no reference point, Leumi could simply charge what it wanted whether that was in order to reduce its own extra costs or not. I consider this to be a commercially absurd interpretation and it also goes against the clear language actually used. In other words this is not some entirely open discretion.

36. Rather, I consider that the provision allows Leumi to charge a fee which is meant to represent or capture or estimate in some way its future costs and expenses in respect of the collection. The language suggests that the fee is to be charged or can be charged in advance of the incurring of the costs and there is obviously a margin of flexibility given to Leumi since by definition it cannot know in advance precisely what those costs will be.

37. I agree that the wording says that these fees are "additional" to other fees. But the last sentence of paragraph 2 refers to the "likely costs and expenses" of collection and this means that it is still conceptually tied to those expenses. Leumi cannot therefore simply charge again, some costs and expenses which have already been charged elsewhere (for example paragraph 2 of Schedule 4) and indeed, neither in its evidence or its original submissions did Leumi suggest that it could.

38. What happened in practice was that Leumi tended to charge third-party costs under paragraph 2 of Schedule 4. As for its own internal costs, these could have been claimed under Schedule 4 paragraph 2, in my judgment, as well - but it seems that this did not usually happen. There may be also a difference between costs recoverable under paragraph 2 of Schedule 6 and the internal costs recoverable under paragraph 2 of Schedule 4 because the latter take the form of actual costs for perhaps individual collections or other tasks, whereas the former is in connection with a general collection which might take some time and is based on a percentage fee itself founded upon an estimate of likely costs. Either way, there cannot be double-counting.

39. On that basis, the "target" of the provision is the recovery of further costs and expenses to be incurred by Leumi as the now collector of the receivables. Accordingly, this is not a case where a percentage can be set without reference to anything; if it were, it would always be set at 15%.

40. Since this provision gives Leumi a power to set in advance a percentage fee, which will apply to all later recoveries, there has to be some qualification thereto, otherwise it could be exercised oppressively or abusively. In my judgment, this is a case where (whether as a matter of construction or the implication of a term) a discretion such as this must be exercised in a way which is not arbitrary, capricious or irrational in the public law sense. See the Supreme Court decision in *Braganza v BP Shipping* [2015] 1 WLR 1661 at paragraphs 27-31, 52-53 and 102-103. For ease of reference I shall refer to these limitations on the exercise of the discretion as "*the Braganza Duty*". The fulfilment of that duty will entail a proper process for the decision in question including taking into account the material points and not taking into account irrelevant considerations. It would also entail not reaching an outcome which was outside what any reasonable decision-maker could decide, regardless of the process adopted. However, the duty does not mean that the Court can substitute what it thinks would have been a reasonable decision.

41. It was also said in *Braganza* that it may well not be appropriate to apply to contractual decision-makers the same high standards of decision-making as are expected of the modern state. I accept that although in this case the decision-maker is a large sophisticated organisation with very considerable experience of performing collect-outs so this point cannot be taken too far.

42. The particular exercise here is the process ending with the setting of a fee. So the aim is to ensure that Leumi is reimbursed all of its costs and it follows that the decision-maker needs to identify

    (1) the amount of the collectible receivables which need to be recovered; the principal aim will obviously be to recover the amounts owed to it;

    (2) the estimated likely costs of the exercise;

    (3) such costs as a percentage of the sum to be collected;

    and once that is done, it is applied monthly thereafter.

43. It follows that if more receivables are collected then Leumi will do better, alternatively if less, then it will be worse off because there will be a reduced total amount of receivables to which the percentage can be applied.

PENALTY

44. If I do not accept BHL's construction of Schedule 6 paragraph 2, it then contends that it was a penalty and thus unenforceable. I disagree for the following brief reasons:

    (1) First, on a proper construction of paragraphs 1b and 2, I consider that Cobra's obligation to pay the collection fee was a primary and not secondary obligation. It is not akin to a sum payable instead of damages, in my view. Cobra had a choice whether to purchase the ledger or not and the power to charge the collection fee arose if it did not. The fact that Cobra may have been unable to purchase the ledger makes no difference;

    (2) Even if Cobra's obligation was secondary, it is not a fixed sum or even a particular formula but a fee to be arrived at in the exercise of a discretion tempered by the application of the *Braganza Duty* as I have concluded above. It is not a penal or extortionate provision. It does have a high ceiling and in theory it could lead to a high collection fee but that does not render paragraph 2 penal in my judgment. Moreover, Leumi had a clear legitimate and commercial interest in being compensated for its internal costs of the collect-out, and the process of being able to make an estimate and charge the fee at the outset is commercially legitimate in my view;

    (3) Moreover, Cobra was a large commercial entity and negotiated the RFA on an arms-length basis even if its terms were standard.

45. This conclusion is consistent with the approach to penalty clauses taken by the Supreme Court in *Cavendish Square v Makdessi* [2015] UKSC 67, in particular in the speeches of Lords Neuberger and Sumption at paragraphs 9, 32 and 35, Lord Mance at paragraphs 145 and 152 and Lords Hope and Toulson at paragraphs 243 and 255.

THE FACTS: (1) EVENTS LEADING UP TO THE IMPOSITION OF THE 15% FEE

46. Prior to the making of the RFA, Cobra had appeared as a very good prospect to Leumi. The latter's credit committee, in approving the transaction stated that: "… Despite there being 600 debtors if Leumi ABL were ever in a collect-out situation then by focusing immediately on the top 50 debtors the commitment recovery would virtually be complete. The residual debtors would have of course still be collected but commitment should have been assured by this point which is encouraging and unusual from such a large ledger… The spread of debt is very good but the top 50 debts account for 85% - the best of both worlds."

47. At the same time, Cobra obtained a general overdraft facility from Bank Leumi with an initial limit of £6m.

48. Leumi's first audit report on Cobra was dated 10 June 2008. At that time, the overall sales ledger balance was £12.6m. with £11.6m. of this debt having been approved by Leumi. The

funds in use (i.e. the Current Account balance) were £10.4m.. I quote from this report as follows:

> "An interesting first audit - despite the heavy losses being made by the company, the sales ledger seems very solid (with a very strong debtor book and audit trail to follow). The top 5 customers consist of the likes of Tesco's, Sainsbury's and Asda Stores all of whom attract excellent credit ratings and substantial credit limits through CIFS.… It's fair to say that overdue debt on this client has been high, (currently £1.7m.-14%, over 90 days old as at 31 May). There are 3 main credit controllers looking after the 500 live debtor accounts and recently the individual responsible for chasing the large Supermarket accounts was on Jury Service for nearly 3 months. This had a massive impact for the client - and although Austin is now back at work - he is slowly trying to bring these larger accounts back in terms.… My biggest concern with this client is the level of debit notes that have and can be taken at any one time by the customers. This mainly only applies to the supermarket accounts… Essentially where a supermarket is running a particular promotion on a particular brand of beer-then they will in turn deduct a percentage from the invoice value towards the cost of running the promotion.… From Leumi's perspective there is no way of telling just how much potential dilution arrears within these larger supermarket promotion accounts. Historically dilution has been running at 3.3% and we have indicated that if dilutions exceeds 5% then we can reduce the prepayment. (This will need monitoring in due course).… Summary… I think it fair to say that I have seen smaller companies that seem far better organised-and despite the massive trading losses being incurred by this business-the sales ledger is by far one of the strongest we have seen. Ideally I would like to have seen an 85% pre-payment rate in lieu of debit notes etc but hopefully the client will pick up on collections and we can start to see a cleaner ledger over the coming months."

49. Following on from that audit, there was a meeting on 18 September 2008 between Mr Italia and Mr Chandarana (Cobra's Financial Controller) on behalf of Cobra, and Mr Couzins, Mr Hird and Mr Willis on behalf of Leumi. By that stage, Cobra had tried unsuccessfully to obtain investment from Diageo in order to provide working capital and it was contemplating the sale of its business, at that point said to be worth £100-£200m. Concern was expressed along the lines of the recent audit report including the fact that "the ledger performance" had deteriorated. Also the "debt turn" i.e. how long invoices take to be paid had deteriorated beyond the contractual limit of 85 days but in addition, dilutions had exceeded the permitted 5%. Indeed Leumi had been told of £500,000 worth of credit notes which had to be debited to the Receivables Finance Accounts in terms of the amount of receivables owing. While Leumi noted various breaches of the RFA, it said that it still had a "passion" for supporting Cobra going forward.

50. Mr Italia then wrote to Mr Couzins on 19 September 2008. He said that Cobra's analysis showed that there was £756,500.88 of credit notes that needed to be brought up to date and they should be notified to the ledger by 30 September. This amounted to less than 7% of the total debtor book but a 9% dilutions based on the figures to the end of August. Since the dilutions should not have been more than 5%, Mr Italia proposed the reduction of the advance payment percentage down from 90% to 86% at the rate of 1% per week.

51. Mr Couzins replied saying that the dilutions rate was in fact higher and there should be a 6% reduction to 84%. In addition a management charge of £25,000 plus VAT would also be imposed. Mr Italia responded on 29 September 2008 by saying that substantial amounts of collections were being banked (£480,000 that day and £500,000 the next) and that there was no problem with the current debtors. He suggested 85% as the new limit and this was later accepted by Leumi. He also agreed to payment of the management charge although this was not something expressly provided for in the RFA. Subsequent to that, and as noted above, the parties agreed to increase the facility limit to £18m. He also said that all credit notes would be brought up to date as soon as possible and in no circumstances later than the end of October 2008. They had put systems in place to ensure no delays in raising these going forward. He said that the debtor book looked weakened but this was due to a combination of sales push in May and June 2008 and not being up to date with credit notes, both of which would be under control by the end of the next month.

52. In early 2009 the debt turn was still too high at 94 days and as a result, Leumi imposed a further charge of £30,000 which, again, Cobra did not object to at the time. There was then a proposal for a creditors voluntary arrangement ("CVA") which would be accompanied by a transfer of its assets to a new Cobra vehicle which was intended by that stage to trade in a joint venture with the very large beer conglomerate Molson Coors. An Estimated Outcome Statement "subject to final figures from Company" for the CVA produced on about 18 April 2009 put the sales ledger at £12.7m but with an "admin. trade and wind down value of only £6m". It is not clear who prepared these figures - probably PwC.

53. In the event however there was no CVA because a creditor effectively blocked it by issuing a statutory demand. This meant that Cobra was likely to go into administration.

54. Then, on 24 April 2009 there was a meeting at which Mr Italia said that there was a total issued amount of credit notes of £1.5m. which needed to be notified. Further detail in respect of this was required and on 30 April 2009 Mr Italia emailed Mr Hird as follows:

> "Please find enclosed… Debtor balance workings and backing schedules… Aged Debtor balance as of today… We have tried our level best putting a whole lot resource in the last few days to get everything fully up-to-date including processing credit notes which are still to be authorised in order to give you as clear a picture as possible… I can only sincerely apologise for the level of credit notes that were outstanding and this has taken me by surprise as well - however it is ultimately my responsibility to bear."

55. This was a serious matter because Mr Italia had assured Leumi back on 29 September that credit notes would be dealt with efficiently going forward - see paragraph 51 above.

56. The "debtor book" showed a debtor balance of £13.1m. but after disallowing various items it came down to £11.4m. The net amount owed to Leumi was £10.4m. If one applied a safety margin of 85% to the allowable debt (ie £11.4m) it meant that only £9.7m. should have been advanced as at that date. The net debtor balance was said to have taken into account the credit notes.

57. Meanwhile, at a meeting on 29 April 2009, it had been put to Mr Italia and Lord Bilimoria that there had been sale or return ("SOR") agreements with some customers (which were not permitted under the RFA) and which they vehemently denied. However it does seem as if there were some SOR transactions being effected and this was confirmed in the audit report referred to below.

58. In a draft Statement of Affairs for the administration, the sales ledger was put at £12.38m with a deduction of £2.5m for credit notes but then a further reduced figure for "estimated to realise" of £7.8m.

59. An audit was carried out at Leumi's behest and with Cobra's agreement on Friday 1 May. The material parts of the audit report ("the May Report") are as follows.

    (1) The eligible debt was said to be £10.1m. with funds in the use of £10.8m. An overall low score of 38 was given;

    (2) The narrative report stated as follows:

> "…a) Telephone verification has historically been very difficult due to the nature of the customer base. The Client sells to a mix of large retailers and small distributors. Due to the difficulty verifying debt the auditors selected the largest 15 debtors (56% of the debtor book by outstanding balance) and:… Compared the January February March and April ageings for each debtor to ensure no anomalies existed. Ensured that that all of the top 15 had made recent payments. Waitrose was the exception, this debtor (balance of £753K) had not made a payment since February 2009. The Client stating that the debtor had promised a BACS payment of £90K that had not yet hit the account. This needs monitoring, this debtor was making frequent and regular payments until February… Based on this analysis the auditor was reasonably confident of the validity of the debt. There was a good level of third-party documentation supporting transactions.Although the obvious flaw is that cash testing only confirms trading relationships and historic debt.… It is common practice for salesmen to agree high list prices with large rebate incentives based on

> volume. Unfortunately for LABL there has been a “disconnect” between the sales and finance functions. It appears that sales representatives have the ability to agree rebates without informing finance. As such finance are unable accurately to accrue for rebates. Finance are not aware of the current/potential liability.… On the 30th April the client notified credit notes of £1.5m. to “LABL". The Auditor tested the credit notes and noted that 80% of the sample related to rebates from 2008. The average lag from the date of the debtor debit note/invoice to the credit note was 94 days. The auditor also sampled a number of February credit notes which also generally related to 2008 rebate/marketing contributions. It is worth noting that the February credit notes were not actually assigned to LABL until mid-March. The Client has obviously been suppressing credit notes to maintain availability. The auditor discussed these issues with the Client’s FC who was open and insistent that all claims “received” had now been processed. However, he stated that in January, February and March the sales team were encouraged to sell at high prices with large rebates to improve headline turnover figures. As such the Auditor must assume that claims will be received for this 3 month period. The Client’s trial balance indicates rebate/marketing support expense at circa £150k per month. Therefore the Auditor must assume a potential liability of £450k.
>
> As previously stated it appeared that the Client sales staff have been “encouraged” to sell, almost at any cost. With the top 15 debtors there are 2 mid-tier distributors… who have been delivered and invoiced large quantities of product. It appears the sales representatives involved have agreed that the customers can pay when the goods are sold.… Again this is a sign of an out-of-control sales force. Hopefully this issue is not widespread.… Dilution average 11.4%. However, this figure should be considered in conjunction with the previous unknown retro rebate comments. Debt turn averaged 94 days. At the end of April 20% of the debt was above 90 days. Cash vs sales for the 6 months ended April equated to 84.3%. This statistic is probably a reasonable indication of actual collectability. If the current ledger collected at this percentage, or LABL would achieve £10.9m. in realisations.… In summary although verification was inconclusive the auditor felt reasonably confident that the assigned debts were valid. Recent remittances from the top 15 debtors substantiate trading relationships. The big issue was unknown/hidden dilutions. The client finance team have no understanding of the potential rebate/marketing contributions due to debtors. This situation is reflected in the poor audit score of 38. If LABL support the Client through a restructure new invoices should be funded at a lower advance rate (say 75%) and the client must implement proper controls. The sales team cannot be allowed to agree sales/rebates that adversely impact LAB, credit requests and cash allocation.”

60. At this juncture it is necessary to say something more generally about the processing of credit notes. Mr Italia explained thus: the supermarkets were where most of the credit notes came from or had been sought. They would often arise when a supermarket decided to do a promotion of, for example, “world beers” of which Cobra was one. There would then be costs involved and when, much later, the supermarket was billed for its supplies and after another 90 days (say) for payment, when it made payment, it might deduct the sums which it said represented the promotional costs which Cobra must bear; or putting it another way, the supermarket would be paying less than the usual price by an order of something around 15%. The first that Cobra would know about a specific credit note claim was when the supermarket failed to pay the entire sum due. On enquiry by Cobra, it would then provide its own debit notes to show the figures charged, Cobra would then have to go back and check to make sure that such an arrangement had been agreed along with what the appropriate level of discount was. Then, once the calculation was checked, Cobra could issue credit notes and the sales ledger would be reduced accordingly.

61. It follows that the need to issue a credit note might only be apparent a number of months after the event to which it referred. Mr Italia accepted that after Leumi had first voiced its concerns about dilutions in 2008, Cobra had tried to introduce a more efficient system but it was still some way off as at May 2009. While that means that the process for recording debit and credit notes as soon as possible was not working efficiently, this did not mean that Cobra was deliberately sitting on the invoices or “suppressing” them so as to obtain the maximum amount of discount funding from Leumi. I accept the evidence of Mr Italia on this point. He gave his evidence carefully and consistently in my view.

62. So while the auditor used the word “suppression” I accept that Mr Italia did not deliberately hide the credit notes as it were. But the lack of an efficient recording system was one reason

why the credit notes surfaced much later than the invoices to which they related. I also accept Mr Italia's evidence (and it was not challenged) that the delay in notifying the credit notes was also caused by the departure of some members of the sales teams (who may not have recorded all the details of the promotion before they left) and a push in marketing.

63. Having disclosed the credit notes in April 2009, they were all, according to Mr Italia, posted to the ledger in May 2009 at the latest.

64. I also accept the basic point made by Mr Italia (and not really challenged) that while non-notified credit notes would affect the sales ledger because the receivables owing must now be reduced by the amount of the credit notes, none of that goes to the collectability of the underlying receivables especially since the credit notes tended to arise from promotions at the supermarkets whose ability to pay could be assumed.

65. That is why, according to Mr Italia, Leumi had the extra comfort of the ability to reduce the Advance Percentage concomitantly with any percentage increase in dilutions over 5%. Indeed, that delayed credit notes were something of a feature of Cobra's business was to some extent recognised by Mr Willis who, in a file note back on 15 October 2008 stated that because Cobra had not become aware of the relevant deductions by the supermarkets until the time of payment, it could not maintain a debit note register that would give an advance figure of potential dilutions.

66. This feature of the business would explain why as at 13 February 2009 Tesco had only notified credit notes of £173,353.30 and yet by 29 April 2009 a total of £528,265.56 had been raised.

67. That said, there were still some later credit notes emerging; thus on 28 May, Ms Sayers of SJB emailed Mr Willis and Mr Couzins to say that Gilbeys had issued debit notes which then exceeded the amount owed by £110,000, of which Cobra had said it was not aware. One debit note related to the period January to 19 May 2009, but the invoices clearly showed that the three invoices from 31 March were invoiced at the net price (ie less the deduction). Mr Couzins emailed it to Mr Italia saying it was yet another unwelcome surprise. Mr Italia responded that this was unbelievable "£6 – retro? Don't know what to say." He said that hoped that their agreement not to draw down on £250-300K would help here and Jaimin would now investigate. In evidence, Mr Italia said that the reference to the retro was to a high selling price at £6 and he could not believe that someone would have agreed that. Otherwise (as he had said in respect of the May report) they were doing some promotions and so credit notes over that period were expected. There was some uncertainty going forward hence the reference to surprises but on the other hand the Advance Percentage had now been reduced to cover the further dilution and SJB had verified debtors at just under £5m.

68. Also there had been historic problems with Waitrose because it would often claim deductions which then had to be investigated and Cobra then went back to them on what they had claimed. On 6 May Waitrose had paid £94,000 but claimed £212,000 in debit notes and one of them was for stock worth £100,000 ultimately returned to the Wincanton warehouse. Mr Italia could not say whether Leumi had been alerted to this at the time.

69. In the meantime, and certainly before 1 May 2009, Leumi had been contemplating that it would take on the collection of the outstanding receivables on the assumption that Cobra's business might cease. It was clear from April that the business and assets of Cobra would be transferred to a new entity which would then form part of the joint venture with the Molson Coors as noted above.

70. By an internal email dated 15 April 2009 from Mr Couzins to Mr O'Keefe, he said that the debt turn was still 99 days as at 15 April and this was a 15 day deterioration since November month-end. There had been no improvement despite the raising of more than £1m of credit notes in March. He also said that "contractual fees due including residue of term service fees - 12 months

of 24 month agreement remaining - Collections fees - 15% of collections.. I have the specific clause details to hand to refer the client to."

71. On 22 April 2009 Mr Italia had emailed Mr O'Keefe to ask whether Leumi would charge a collection fee but he did not deal with this in reply save to say that the parties and their lawyers should meet to discuss the CVA.

72. I have referred above to the letter of demand. At that point, £7.74m. was due from Cobra to Leumi including all the ongoing fees. Administration of Cobra then followed on 29 May. The 7 day period for Cobra to repurchase the debt expired on 2 June 2009.

73. On 2 June, Mr Italia wrote to ask exactly what fees would be charged by Leumi. Mr Couzins replied on 18 June to say that he would let them know in due course but they would be calculated according to the RFA but absolute figures could not be given until the collections had been completed "as this is a percentage of collections to be taken into account".

74. Then, by a letter dated 1 July 2009, Leumi informed Cobra that the principal fees would be an increased discount charge of 3.5% pa above base and a collection fee of "up to 15%". And "as we do not know the aggregate amount of collections that we will make we are unable to precisely state the total Additional Collection Fees that will be payable."

75. In fact, the first collection fee was charged to the Current Account on 30 June 2009 in the sum of £473,838. This represented 15% of the £3.158m. of Cobra receivables which were collected in June.

76. Between 26 May and 2 June some £918,000 was collected from the receivables as already noted. And by 3 June, the amount outstanding on the Current Account was £6.82m. At that stage total receivables were £10.5m.

THE FACTS (2): THE DECISION TO CHARGE A COLLECTION FEE OF 15%

77. At the outset I should note that 15% was not only the maximum – it would be a large fee here because the debt to Leumi was £6.82m by 3 June and more before. On any view it would be more than £1m.

78. It is reasonably clear how Leumi came to fix 15% as the relevant charge. The person who actually fixed it was Mr Couzins.

79. It appeared from the evidence that Leumi had, as a matter of practice, always charged the maximum where the provision gave a fee which could be "up to" a particular percentage. Leumi said that sometimes it would go down to 10% but that was not where there was a range of up to 15% but where the maximum for that particular contract would be set at 10%. So that point is not of much assistance here. In addition, Mr Couzins could not recall any instance where he had charged less than the maximum available. He also referred to the case of another client, Logic Systems Management - but again that was only about the percentage negotiated at the time of the agreement not the price charged at collect-out. Finally, he referred to the case of Burford - but that was rather different: there, on the administration of the customer Leumi agreed in advance with the administrator to limit its fees at £100,000. So there is no evidence of any case where Leumi had a discretion to charge a fee of up to a particular percentage and did not then charge the maximum.

80. Furthermore, the "up to 15%" fee was often described at the time as simply "15%" (or in the case of other examples simply the maximum percentage) which reinforces the notion that there was usually no attempt to say that something less than the maximum was appropriate. See for example paragraphs 32, 52, 55 and 58 of Mr Hird's witness statement. Perhaps this was shorthand, but in my judgment it was telling.

81. Further, some of Mr Couzins' emails referred to a charge of 15% as if it was the norm. See for example, his email to Mr O'Keefe of 15 April 2009 (referred to above) and his email to Hammonds dated 2 June 2009 where he said that "procedurally we normally calculated 15% of collections achieved on a monthly basis… at the end of the month". Equally, the emails from Mr Couzins to Mr Italia on 18 June and 1 July 2009 are consistent with the simple application of a 15% charge.

82. In cross-examination, Mr Couzins accepted, after having said that there was an "agreement" to charge 15%, really he had decided it himself although he had a very brief word with Mr Willis effectively to tell him. In reality, and Mr Couzins did not really demur from this in evidence, there was no attempt at calculating an appropriate percentage based on the likely collectable receivables as against what Cobra owed at the time and having regard to that the likely cost of any collect-out. It is not as if Leumi was inexperienced in collect-out situations. Mr Couzins himself had been involved in 100-150 collections in the course of his career, and Mr Hird had been involved in 200-300 overall, and in the 8 years at Leumi, he had overseen some 50 collect-outs. So Leumi must in truth have had a considerable amount of data about how much collect outs can and do cost over a range of cases-none of that was put into evidence at all and there is no suggestion that in fixing 15% Mr Couzins or anyone else at Leumi had regard to previous collect-out experience. Nor, in fact, was Mr Hird consulted in the process here at all.

83. In truth, the exercise was no more than Mr Couzins asserting the right to charge 15% "because it was the right thing to do".

84. All of this is at odds with paragraph 7 of the Further Information given by Leumi on 3 August 2012 where it suggested that a number of factors were taken into account when deciding the fee. In the light of the frank evidence of Mr Couzins, this was clearly an attempt at *ex post facto* justification. I agree with BHL's submissions that for Mr Couzins merely to say in evidence as he did that this was a complex case does not demonstrate that the discretion was seriously exercised at all.

85. The lack of any real consideration of the matter was illustrated when it was put to Mr Couzins that since the discount charge had been increased in order to take account of Leumi's costs and expenses of the collections going forward, that extra charge should have been factored in when considering what the collection fee should be so as to avoid any double counting. He accepted that it should have been but then could not recall if it had been considered at the time. The reality in my view is that clearly it had not, and Mr Couzins seemed to be at a loss when this was put to him.

86. I accept that a decision was taken to charge 15% and also that before the decision was taken it had been presaged to some extent and BHL had at some points worked on that assumption -see, for example, Mr Italia's email exchange with PwC on 18 May 2009. But this is entirely irrelevant. The question is not whether Leumi decided to charge 15% - it plainly did - but whether there was any real exercise of the discretion granted by paragraph 2 of Schedule 6 and in my judgment it is obvious that there was not.

87. For the same reason the fact that others at various points thought that Leumi would charge 15% or perhaps more is irrelevant to what Leumi did or not do to reach that figure. The belief that it might be 15% is of course consistent with a belief that right or wrong, this is what Leumi was entitled to charge under the RFA (see below).

88. Even if it were thought, somehow, that there was an exercise of the discretion (which I reject) it was wholly defective:

    (1) There was no attempt to calculate likely costs and expenses and no attempt to use data from previous collect-out experience;

(2) There was no consideration of the extent to which any collection process was likely to be materially carried out by third parties especially in the later stages where the collections would become more difficult and if so, whether those expenses would be charged separately, as indeed they were here;

(3) There was no consideration given as to whether a short delay in setting the charge would give Leumi an important breathing space in which to form a more informed view as to the proper percentage to be applied. As noted above, at one point, even Mr Couzins recognise that the charge might not be capable of being applied at the outset, as he in fact told Mr Italia. While Leumi did liaise with Hammonds at an early stage apparently to ensure that it acted correctly, this does not alter the need to give itself more time and as Mr Couzins accepted the fact that he had to report to the Board could not justify not delaying the application of the charge;

(4) Much was made of the general perception that this was going to be a difficult collection and the suggestion that the fact of Cobra's going into administration would heighten this because some debtors who would normally pay might be encouraged not to; but all of this was in very general terms and cannot in any way remove the need to undertake a process by which some sensible estimate of costs could be reached by reference to how much Leumi needed to raise in the collections process (by reference to the monies outstanding to it), how long it thought the process might then take and in the light of all of that what its own justifiable internal costs might be;

(5) Otherwise, the reasons given above as to why there was no exercise of discretion at all apply equally here.

89. Accordingly, to the extent that there can be said to have been some exercise of the discretion, it was wholly arbitrary, irrational, manifestly failed to take into account important relevant factors, and it cannot be supported.

90. It is an entirely separate question whether, if the discretion had been properly exercised, a figure of 15% or some other percentage could rationally have been arrived at – this is dealt with below.

CONSEQUENCES OF THE FAILURE TO APPLY THE DISCRETION PROPERLY

91. Ultimately, by the end of the trial, there was no real dispute between the parties that if I should conclude (as I do) that the discretion under Schedule 6 paragraph 2 was not exercised at all or improperly, then the court should, or at least is entitled to, consider the counterfactual, that is to say what percentage would or could BHL have arrived at, had it sought to apply the discretion in a lawful manner?

92. That consensus must be correct. There is, in my judgment, no basis for saying in this case that where the discretion was not properly exercised the result is that Leumi can recover nothing by way of a collection fee.

93. Had most of the 15% charge not already been paid by BHL, and had this been Leumi's claim for sums due under paragraph 2 of Schedule 6 then one would simply reduce its claim accordingly to the most that it could lawfully have recovered.

94. In the event, of course, most of the charge was paid by BHL which is why BHL now claims repayment by way of restitution. But equally, even if the claim for mistake is made out (see below) BHL would not be able to recover the whole of it to the extent that any part of it could legitimately have been claimed by Leumi at the time.

ACTUAL AND ESTIMATED COSTS: OVERVIEW

95. I consider first what Leumi's actual costs, in the event, should be taken to be. I have of course rejected BHL's case that all that Schedule 6 paragraph 2 provided for was actual costs up to a

ceiling of 15% of recoveries. But it is useful to undertake this calculation (a) in case I am wrong on the question of construction and (b) in any event it may provide a useful sense-check for any calculation of estimated costs bearing in mind of course that the Court cannot apply hindsight to that latter exercise.

96. The expression "estimated costs" must here be directed to the highest percentage which Leumi could rationally have determined, had it exercised its discretion properly and at the time when such discretion should have been exercised.

ACTUAL COSTS

The state of the evidence

97. No actual records of anyone's time on this collection was made contemporaneously even in note form. Leumi's evidence consists simply of the estimates given by Mr Couzins, Mr Hird and Mr Willis for the amount of time they thought they spent. Mr Lawler, in his calculations of the actual costs seeks also to add an element for the time of the less senior collecting staff namely Samantha Carver (Tressider) who was in charge of collections generally, and as assisted by Debbie Cross, Greg Smith and Mr Woodward ("the Collection Staff"). But no attempt was made by Leumi itself to estimate the time spent by the Collection Staff in any real detail and none of them gave evidence.

98. There are no other costs to be considered because the legal costs were charged separately as were the payments to Mr Anwar, Mr Ladwa, and SJB.

Charging Basis

99. Mr Birch for BHL first assessed what he considered a reasonable amount of time would have been for each of the Management Staff to have spent on this collection. But then he says that in the absence of any real evidence to the contrary, strictly, no losses have in fact arisen because the salaries of the Management Staff are fixed or "sunk" costs and therefore would have been spent anyway. It is not as if Leumi suggested that it had to bring in extra staff to do the work which the Management Staff should have been doing but did not do because they were too busy dealing with the BHL collect-out.

100. Notwithstanding that view, what Mr Birch actually did was to take the hourly rate implicit in the salaries of the Management Staff and apply it to the number of hours that he considered would have been reasonably spent. On that basis the maximum actual cost figure is £22,500. If the hours spent were as claimed by Leumi, this figure would rise to £66,000. He made no allowance for Collective Staff time because there was no evidence to support it.

101. On the other hand, Mr Lawler did not use actual salary-based hourly costs for precisely the reason that they are fixed. But instead he took an "opportunity cost" approach. This is a much higher hourly rate and represents the contribution of that member of staff to Leumi as a whole. A proportion of salary costs would not achieve this since no account would be taken of the profits made by Leumi. So instead Mr Lawler takes total salary costs of £1.955m. as against gross profits being £7.31m. (both figures for 2009) and thus considers that on average each staff member contributes 3.7 x his salary.

102. On that footing, Mr Lawler takes as the relevant staff costs, the hourly rate implicit in their salary but multiplied by 3.7 to achieve the "opportunity" version of the hourly rate. See paragraphs 7.120-7.122. On that footing the hours given by the Management Staff for the time spent on the collect-out would yield a figure of £231,000. However Mr Lawler then adds an estimated amount of time for the Collection Staff of one day per week for 2 years on the part of Ms Carver and otherwise one hour per week for 2 years on the part of Mr Woodward, Ms Cross and Mr Smith. This raises the total to £316,000.

103. The rationale for using opportunity cost is that if the member of staff was not having to deal with the exercise in question, here the BHL collect-out, then it follows he would be available to do some other work for Leumi which in fact could not be done because he was not available. In principle, I can see that an opportunity cost analysis could be valid and Mr Birch does not reject it entirely, either. However, he says that the calculation here should not factor in an opportunity cost evaluation since Collection Staff were not in profit-making roles and as for the Management Staff there is no real evidence that they were prevented from performing other aspects of their work. Thus, on the facts of this particular case, the opportunity cost evaluation could not yield anything of substance.

104. As to the underlying evidence, Mr Couzins does not say what he would have been doing absent work on the BHL collect-out. Nor does Mr Willis who was not engaged in business development either. Mr Hird did say that he was diverted from other work and that there were lost opportunities to develop other business but this is all quite vague. There was no attempt by Leumi, or its expert, to see if there was any business lost for example by seeing if inferences could be drawn from the difference between turnover and profits for 2009, 2010 and 2011 as compared to other years.

105. On an actual basis, therefore, I cannot see how any assessment can include any element for opportunity cost.

Conclusions on Actual Costs

106. I set out below a table of the Management Staff time spent on the BHL collection as (a) assumed by Leumi (b) in the view of BHL and (c) in my view. The overall claim period as contended for by Leumi was May 2009- January 2011.

	Leumi	BHL	Court
Couzins	430	60	215
Hird	165	30	90
Willis	1152	720	650

107. I reach my view of the time to be attributed for the following reasons:

(1) In the case of Mr Couzins, some of the time he claimed is not properly attributable to BHL anyway for example reporting to shareholders and his costs for April and May 2009 which is before the collection fee period started. Accordingly I reduce his time by 50% to 215 hours;

(2) As for Mr Hird, while I would not disregard the time he spent in personally delivering a consignment of beer to the cricket club to raise some further money, I consider that the hours claimed of 165 are excessive. Again there is no documentary support and I consider the appropriate figure to be 90 hours;

(3) Mr Willis estimated that 40% of this time was spent on this collection over the whole period yet in the letter of 22 January 2010 it was said (or later said to be implicit – see Hammond's letter of 26 March 2010) that all reasonable collection efforts had been made by then. On that footing, it is very hard to see how he could have been spending 40% of his time after January 2010 or even 20% of his time. There is no note of any

kind to support his time estimate and I consider that the figure should be reduced from 1152 to 650;

108. Using my figures but adopting Mr Birch's salary-implied hourly rate, the result is £33,260. Had the opportunity cost model been appropriate the figure (on the basis of my estimated hours) would have been £125,000.

109. In my view, there is no evidential basis for me to add any time for the Collection Staff but if there should be some allowance for them and if opportunity cost was appropriate, I would have added no more than £50,000.

110. In my judgment, those figures are generous when it is borne in mind that by 16 September 2009 Leumi's capital exposure (i.e. excluding all fees) had been recovered, in circumstances where the collection fee was by far the largest element. Account also has to be taken at least to some extent of the increase in the Discount Charge. If (contrary to my view) the correct basis of recovery under paragraph 2 Schedule 6 was actual costs and expenses, therefore, the collection fee element would be very substantially reduced and this would itself reduce the time needed to collect out because the amount of fees to be recovered would be so much less.

ESTIMATED COSTS

Introduction

111. The exercise here is to determine the highest percentage fee which Leumi could have charged without being in breach of its *Braganza Duty*.

112. This can only be done by reference to the materials before me even if other materials exist which might have proved useful. Thus I cannot be assisted by potentially highly relevant information about the costs and timings of previous collect out operations known to Leumi because this has not been provided. Moreover, to the extent that Leumi contend that any cost estimate must err on the side of generosity because of the uncertainty going forward, I cannot take much note of that since Leumi deprived itself of the data from those previous collections which would have reduced much of the uncertainty, in my view.

113. It is also important, again, to note that whatever may have been the difficulties perceived by Leumi about the Cobra ledger at the time, Leumi was not entitled simply to look at those in the round and then leap immediately to 15% or some other high percentage. Its *Braganza Duty* required it to attempt to translate all of that into a rational estimate of its internal costs going forward. This is a point which underlay much of Mr Birch's evidence in my view, and which I found persuasive (see below).

Relevant Facts

114. I accept the point made by BHL that although any monthly collection fee could not start until 3 June 2009, if the position was very uncertain, as Leumi says that it was, as at the beginning of June, Leumi could and should, rationally, have waited for a few weeks to see how in fact the collections would pan out. This is in the context of £918,000 being collected in the last week of May and around £3m in the month of May. As to that Leumi contended that not much significance should be attached to such figures - they were no more than the normal rate of collections - but that does not diminish their significance when it is Leumi's case that at around this time Cobra ought to be viewed as being in an <u>abnormal</u> situation.

115. As to whether the credit controllers from Cobra (who had obviously been very effective in the course of April and May) would join Leumi as opposed to going to the new company or somewhere else, BHL was in regular touch with them anyway and the uncertainty had been removed by the end of June at the latest when they agreed to come over. Equally, collections

proceeded apace in the course of June with a further £3.15m. coming in. As a result, the Current Account had reduced from £6.82m on 2 June to £4.5m by 30 June.

116. So on any view, had Leumi waited until the end of June then the position would have been very much clearer and in an optimistic direction. This point is not seeking to apply hindsight but rather to show that the rational way for Leumi to deal with the uncertainty perceived was to delay making the decision as to the fee. There was no prejudice to it in so doing because it would still be applied as from 3 June.

117. But in fact, there was much useful information to be had as at 2 June. First, SJB as an efficient third-party collection agent had been in place since 7 May and by the end of that month they had verified about £5m. worth of invoices. In addition of course by that time, it was known that there would be no further funding of Cobra save in respect of new invoices (likely to be modest given that it went into administration on 29 May) and with a reduced Advance Percentage. It is right that SJB also referred to some £2.6m of credit notes but it seems that most of these had in fact been picked up. The sales ledger as at 2 June was £10.5m after taking account of the credit notes. On that footing the debt from BHL was around 65% of the sales ledger.

118. Also, over the course of May some £3m. had been collected and Leumi had also acquired about £986,000 of unsold stock from Wincanton. As and when that was sold, the proceeds would be credited to the Current Account in the usual way. Leumi contends that this is an irrelevant factor but I disagree.

119. In addition, there was at least the prospect of Mr Anwar and Mr Ladwa coming to work for Leumi. By 30 June they had both agreed to continue the Cobra collections as contractors to Leumi. I do not accept that it was simply assumed that they would not come and if that was the assumption, it was an unreasonable one.

120. There was of course the concern which had been expressed about the credit notes (including the particular examples of Waitrose and Gilbeys given above) and while there would have been some uncertainty going forward I accept that the vast bulk of them had already been dealt with and taken into account. The May Report itself had allowed for a further £450,000 worth on top of those reported because of current promotions. As to the May Report generally, obviously that had to be considered although it had positive as well as negative points, as noted above. And I accept that while I do not find that there was "suppression" in a any deliberate sense, the auditor had used that word and it would have some impact on Leumi. But again, one has to look at the position as at 2 June when things (and collections) had moved on.

121. In his witness statement, Mr Willis made particular reference to large outstanding supermarket debts and thus matters of concern. Much of this is after June 2009 but the point of his narrative was to show the extent of supermarket debt as at the commencement of collect-out. I think the position was considerably overstated. For example,

    (1) Tesco: it was alleged that Tesco owed £157,000 at the beginning of the collect out. It did, but in June/ July it had also paid over to Leumi over £500,000 and Mr Willis did not refer to this; also there had been some £400,000 worth of payments in May; so it is not as if overall Tesco could be described to be a bad payer;

    (2) Morrisons: here a debt of £288,000 as at 20 August was referred to Hammonds; but in fact on 30 June, a payment of £585,000 had been made;

    (3) Asda: a debt of £50,000 was said to have been difficult to collect but in fact Asda had paid £205,000 in June and £125,000 in July; all that Mr Willis highlighted was that Leumi could recover only £10,000 out of the £50,000;

    (4) Bookers: this owed £75,000 but again, it had paid out £325,000 not long before;

(5) Sainsbury: reference was made to a debt of £73,000 whereas £330,000 had been paid in June/July and a pre-collect out payment in May of £560,000;

(6) Waitrose: here Mr Willis had stated that when the collect out moved in-house Waitrose owed £330,000. But in fact £350,000 had been paid in early May.

122. I accept BHL's submission that the presentation by Mr Willis of these debts was misleading because it suggested that they were general difficulties of collection with these customers. But the detailed individual ledgers shows that this was not so.

123. I accept that the supermarket credit notes going back some way, as noted by the papers underlying the May Report, appeared much larger than Cobra had sought to notify in February 2009 but as Mr Birch pointed out that depended to some extent as to when they had surfaced. Also these were only a modest proportion of the total amounts due and as noted by SJB essentially these supermarkets were sound debtors. As Mr Willis had to accept in evidence a very large amount was collected before there was a need to contact Hammonds.

124. Mr Tozzi said that particular importance had to be given to the extensive write-down of the ledger in the draft outcome statement for the administration referred to in paragraph 52 above. But first, it was only a draft and second the much more pertinent document was the May Report. As to the cash v sales percentage of 84.3% in the latter, I do not accept that it was unreliable simply because Cobra then went into administration. There was no firm evidence that debtors would act differently and on the face of it, they did not. Leumi could see the pattern by 2 June. I deal further with these matters below.

125. It was also argued that the fact that Molson Coors decided not to buy the ledger off Leumi was itself a bad sign. I do not accept this - there could be various reasons why Molson Coors was not prepared to buy it - it does not follow that there would be serious difficulties in the way of collection.

126. Although there are frequent references in Leumi's witness statements to a difficult and troublesome account, in my judgment, the truth is that even as at 2 June, the collections appeared to be moving swiftly with substantial sums coming in, and any difficult cases would be later, and dealt with by Hammonds, whose fees would be charged separately, the same being true of SJB.

127. There is no specific direct evidence from any of the Leumi employees as to how long and how much time they thought the collect out process would take or at least how long it would take in order to recover the capital exposure and applicable fees. They could not add in any collection fee until they had worked out how long the process was likely to be in what the costs of recovery would be. However, when Mr Willis was cross-examined about the actual pattern of debt recovery in the 3½ month period from the end of May when £7m. was recovered he accepted that this would not have come as a surprise to him and he thought that this would be obvious: in other words a very substantial proportion of the debt would be recovered very quickly. Although he had said earlier in cross-examination that this would not be an easy collection, in my judgment he was accepting later that he would have known, had he thought about it, that as at 2 June, he could expect a very substantial proportion of the recoveries to have been collected quickly. His real point was about the size of the "tail" of the recoveries and how long that might take. But at that stage, for those residual difficult debts, that is where the lawyers and collection experts would come in and they would be charged for separately.

The Expert Evidence

Mr Lawler

128. First, there is the evidence of Mr Lawler who has assumed that the Collection Staff would spend all their time on the first year with 2 of them staying on for the second year and one in the third

year. For Mr Willis, it would be 80% of his time in the first year, 40% in the second and 20% in the third. For Mr Couzins it would be 40%, 20% then 10% and for Mr Hird it would be 20% 10% and 5%. Using the "opportunity cost" formula, this would then yield a total estimate of cost of £1.4m. See paragraphs 7.5.8 – 7.5.10 of his report. This is very considerably more than the actual costs, computed on the same basis, but Mr Lawler justifies it because there would have to be "an assumption that the collection would have taken place in-house and in respect of lower realisations and therefore a more complex review and reporting requirement". I regard that suggestion is totally unrealistic. At best there was an initial uncertainty as to whether the Cobra credit controllers would come but it was always known that third-party collectors would come in for the more problematic debts.

129. I consider that the figure of £1.4m is manifestly excessive.

130. First, it is unsupported by any evidence of previous collect-out experiences which Mr Lawler, as an expert, could and should have asked for from his client. Second, his starting point seems to have been his figures for Leumi's actual collection costs which I have judged to be much too high anyway - see paragraphs 103-110 above. Third, he uses the opportunity cost model which is not straightforward for the reasons given above and would need the support of evidence showing that the result of the time spent by the Management and Collective Staff on this exercise would lead to the realistic prospect that other business would be lost as a result. Fourth, it fails to take account of the very significant recoveries made prior to 2 June and the fact that by then there was at least a prospect of the Cobra collectors coming over. Fifthly, it does not take account of the fact that the obvious course in any event if the uncertainty was as great as Leumi would have it, was to delay the decision for a few weeks at which point the prospect for a relatively fast and efficient recovery of most of the ledger was clearly then in prospect. Sixthly, Mr Lawler also added in as a factor, the possibility of fraud or "fresh-air invoicing" but in truth there never was any evidence of that at all and I consider that suggestion to be pure speculation.

131. In addition, I did not find Mr Lawler generally to be as reliable or impressive a witness as Mr Birch. Indeed, while he is a specialist forensic accountant, he accepted in evidence that he was not a debt collecting expert and could not give evidence as such on the collectability of ledgers.

132. In addition, his evidence on a number of points was unsatisfactory and showed an unwillingness to concede anything. For example, he pointed out that one of the risky or difficult factors going forward was the high proportion of old debts as at the end of May. But he did not actually say what that proportion was and did not put it in his report. He did not say either that many of the old debts had been paid in May without creating further indebtedness from Cobra since the new funding was now so limited. His only answer to this was to say that the "suppression of invoices" and the fact of Cobra's impending administration would "trump" this point. While he said that he had taken into account in his deliberations the significant payments made in May, he did not say so in his report.

133. He then said that he simply accepted the views expressed in the witness statements from Leumi without any critical examination. And it was he who introduced the wholly speculative notion of fraud and fresh-air invoicing, referred to above.

134. The fact that SJB actually certified £5m. worth of valid invoices was put to him and he said that he did not know the extent of their work. But he did not seek to find out and simply said that this could not given much comfort to Leumi, post-administration. The following exchange is revealing (Day 7 pages 125-126):

> "Q. We looked this morning at the £4.997 million verification as at 26 May. So given that all of that work had been done, this is another example of you ignoring May so that you can make a comment that's untrue that Leumi wouldn't know if there had been any fresh air invoicing or pre-invoicing until it tried to collect?

A. No.

Q. No what?

A. No, my Lord. I don't know what SJB did or the extent of the work that they performed. Certainly what it didn't do is give a massive amount of comfort to Leumi that these debts would be collectible post-administration. And I stand by the comments that I make in 5.6.1, 2 and 3. Leumi didn't know if there would be any fresh air invoicing until it tried to collect the customer.

Q. How do you know if there was comfort that was given by SJB or not to Leumi?

A. It's a fair question. You are inviting me to put myself in the mind of Leumi. Let me say I think it's reasonable for Leumi to assume that -- yes, the work done by SJB was useful. It will have given them a degree of comfort. Does it trump the existing problems that I set out in these sections of the report, including suppression of invoices? And the answer is no."

135. Mr Lawler accepted that he was postulating an "utter nightmare" scenario for the collect out which he said could go on for longer than 3 years and resulted in zero realisations. I have to say that I found that evidence to be absurd, not least in the light of the acceptance by Mr Willis that there could be £7m. of debt recovery in a short space of time. And there was no evidence whatsoever to suggest that the majority of the ledger was simply irrecoverable as at 2 June 2009. Mr Lawler sought to justify his position on the basis that there is "very little else I could go on". That was not so; had he made proper enquiries of his client about previous collections and time spent and how it tended to assess the collect-out fees, the extent to which they knew they would use third parties etc he would have been in a much more informed position. But he did not do so.

Mr Birch

136. Mr Birch, on the other hand was a much more careful and considered witness. He had no operational experience of undertaking collections himself but as an auditor, he had conducted reviews of the collectability of receivables of businesses which had received invoice financing from his clients. Some of these were cases where his clients (like Leumi here) were in a collect-out situation and so he was aware of their experience of this. Which included situations where his clients were halfway through a collect-out and had to judge how much cash they would collect based on the speed of cash coming in and when they last had a payment etc.

137. He had also been seconded to a financial services institution as head of finance for 13 months when the collection of loans and receivables was a significant area of focus. He took the view, fairly to my mind, that his experience of collections was useful in assessing the collectability of a debtor going forward. It was put to him that his experience could not possibly be compared to that of Mr Couzins and Mr Hird. Of course that is correct, but it does not mean that he cannot comment on the extent of collections work going forward here especially when Leumi had signally failed to provide any of its own data.

138. Mr Birch was also prepared to make concessions in a number of areas for example in respect of matters which could cause Leumi legitimate concern.

139. On the issues as to the likely duration and cost of the collect out as at 2 June, Mr Birch accepted that the extent and late notification of credit notes was a concern but he also said that these had been reflected in the figures by that date. He considered that weight would also have to be given to the substantial amount of collections that occurred in April and May 2009 and that the majority of the debt was clearly collectable and quickly. There was also more value in the ledger than the outstanding debt to Leumi. Further, he thought that the timescale of the actual collection as it happened, was fairly typical for a collect-out situation like this. That was something he thought could have been taken into account when estimating the costs at the time.

140. In cross-examination, Mr Birch was taken to a large number of factors which, it was put to him, were negative for Leumi going forward. In some cases he challenged those propositions. For

example, on the question of the £6m realisation figure in the draft outcome statement referred to in paragraph 52 above, he made the point that since the note accompanying that figure was not available, it was not possible to say how it had been arrived at. He also pointed out that by the date of the start of the collect-out, there was more current information anyway.

141. Further, when taken to total credit note figures for example said to be £2.36m for May, he said that much of it would have related to April and that "you have [just before the collect-out] seen the worst of it, almost".

142. On the question as to whether 84.3% cash v value noted in the May Report was still reliable going forward when Cobra would be in administration, he accepted that factors associated with administration like possible redundancies or lack of enthusiastic staff, might reduce that percentage a little but in truth those factors did not diminish the collectability of the underlying debts - rather they might slow down the pace of collection a little. Indeed he said that the prospect of Leumi being able to take on former Cobra staff was quite good because such staff might often accept an offer of employment and he based this on his experience of how collect-outs had worked and how businesses had managed them. But he accepted that some staff might go elsewhere including the "new" Cobra and there might be a need to employ other experienced credit controllers instead. But he said that a good controller would get to grips with these issues quickly and while the pace of the collection process might be slowed down somewhat, it would not affect the eventual receipt. He was quite prepared to accept that he would have been concerned at the way in which the credit notes had come out and where Cobra management had appeared to give the wrong figures and he accepted that some time would have to be spent investigating the position. But he did not regard this as some insuperable obstacle and again, it all came back to the question of how long the collect out would take here.

143. In his view, the anticipated collect out process could not possibly be viewed as taking 3 years and he did not see it as a "nightmare" situation. He pointed out that as at 2 June, the ledger was performing in line with the ordinary course and when no new invoices were going to be added to the ledger and the payment terms were 30 to 90 days, then the debt would run off quickly. His expectation was that the cash would be collected across the ledger as a whole and while one could pick out certain problematic debts there were a lot of customers paying in term and on time. There was no reason to suppose this would not continue and where within two to three months the ledger would be very much smaller.

144. He also had made the point that any estimate as at May 2009 should be on the basis of past experience of collections. In this regard he said that he had reviewed about 30 collect out of which about 30% would have been the same size as this case, also with 550-600 debtors. And in fact here, despite the credit note situation, the invoice "conversion" into cash rate (i.e. the extent to which invoices were fully paid) was 84%.

145. Mr Birch's view was that the process here might take 3-6 months. I consider that this is much more realistic than Mr Lawler's estimate. It is true that in his report Mr Birch had not given a time estimate at all because he had not been asked to do so, but in my judgment the door to all of this had been opened in cross-examination by Mr Tozzi.

146. In re-examination what was then put to him was a likely "worst-case scenario" but not a theoretical disaster. On this he said that there would be collections at a slower pace. The most would be in within 3 months but it might take 4 to 5 months to get to the point that was in fact reached here by September ie after the 3 months it actually took to recoup the capital exposure. This evidence was objected to on the basis that he had not initially thus far given evidence of the timescale of any "nightmare scenario" collect-out. But there is nothing in this point. Mr Lawler's estimate of 3 years had been squarely put to Mr Birch on more than one occasion in cross-examination and he was entitled to express a view of a "nightmare scenario" basis in re-examination. As it turns out, Mr Birch is not far wrong since the capital exposure of Leumi was

recovered by September 2009 and there was enough from those recoveries to pay the debt and most of the fees by January 2010.

147. It is right to point out that in his report, Mr Birch chose an estimated cost going forward as equivalent to his figures for actual costs. That is too much of a short-cut and does involve the application of hindsight. That is why it was more helpful to have his evidence on time-scale, in a context where Mr Lawler's estimated costs could not possibly be right.

ANALYSIS

148. In the light of all of that, it is necessary to undertake a counterfactual which will produce a period of time which it is rational to assume Leumi staff could be involved in the collect-out and from which some estimate of costs could be made. This can then be translated into an appropriate percentage collection fee. The starting point is thus the process outlined in paragraph 42 above.

149. As at 3 June 2009 when the collect-out would start, the basic position was this:

(1) There was £6.82m. on the Current Account to be recovered, inclusive of all fees save the collection fee;

(2) The sales ledger stood at £10.5m. which took into account the credit notes notified in April and May;

(3) Rounding the £6.82m. up to £7m., Leumi needed to recover at least £7m. and to allow sufficient time for that to be done;

(4) There was ample coverage for this in the outstanding sales ledger and even if this was reduced to 85% of £7m., it still left £8.9m. i.e. about £1m. more than was needed.

150. Some weight would have to be given to the possibility of yet further credit note issues emerging but on the ground, as it were, these were not likely to be substantial. Otherwise, there was no reason to suppose that the outstanding debt would not be recovered and recovered relatively quickly. There would undoubtedly be some more difficult debts which formed the "tail" of the ledger but the real costs at that stage would be those of third parties not Leumi itself. There was at least the prospect of Mr Anwar and Mr Ladwa coming over from Cobra.

151. I do not agree that Leumi should be looking to collect significantly more than was necessary to discharge Cobra's indebtedness to it. Once that was recovered it would be a matter of deciding whether or not to reassign to Cobra for example. While it is true that collections did go on through 2011 and 2012, Leumi also treated 22 January 2010 as being the cut-off point for a reasonable collection process and of course one reason why Leumi went beyond 2010 is because it had to recoup its very large collection fee (or the balance outstanding on the basis that most of the fee had been paid by BHL).

152. In the light of all of that, it is difficult to see why more than 6 months of Leumi's own time should be required on the collect-out process.

153. However, something extra must be allowed for the fact that Leumi would also need to collect the (proper) collection fee whatever that might be, and also something for contingencies to include any further internal time spent when third parties like SJB and/or Hammonds were involved in collecting the more difficult debts, though this should not be too much. On that footing, I consider that a rational maximum time period could be 12 months but on the basis of implicit salary costs not the "opportunity cost" model and of course there is no evidence that Leumi would itself have used such a model or even considered it.

154. Some credit must be also given for the fact that the Discount Charge was increased, again on account of Leumi's internal collect-out costs.

155. One way to gain a figure for 12 months internal costs would be to use Mr Lawler's table at paragraph 7.5.8 of his report but to take only the first year's costs. On that footing, the resulting figures would be as set out in the table below.

	Couzins	Hird	Willis	Collector 1	Collector 2	Collector 3	Total:
Hours	809	404	1619	2024	2024	2024	
Value £	41,260	30,000	39,000	52,700	24,300	24,300	£212,000

156. If £212,000 is added to the already rounded up figure of £7m., then that produces a round figure of £7.2m. which needed to be recovered. £212,000, as a percentage of that, is about 3%. But Leumi is not expected to make a very precise calculation and indeed looking to the future, it could not do so. I therefore consider that on those broad figures it might be entitled to take a percentage figure of 4%. This would represent £288,000 as a proportion of £7.2m. so there would be some further significant room for manoeuvre. One could equally arrive at a similar sum by projecting somewhat beyond 12 months but using different percentages of time.

157. All of the above is on the basis that it was rational for Leumi to have made a decision as at 2 June. In fact, for the reasons already given, I do not consider that it was, and if they left it for a few more weeks then it would have been plain that the exercise would be straightforward.

158. However, I have given Leumi the benefit of the doubt for the purpose of this analysis. What this means is that in my view, 4% is the absolute maximum that Leumi could have charged in order to remain in compliance with its *Braganza Duty*. In fact, collections of about £8m. were made. 4% of that is £320,000.

159. As a sense-check, that is very much more than my determination of the actual costs and a little more even than Mr Lawler's maximum figure for actual costs using his opportunity costs model.

160. Accordingly, the monthly fee chargeable to BHL was much less than the amount it was in fact charged. On the face of it, this would mean that if the mistake claim succeeds, BHL will be able to recover the excess. I leave it to the parties to produce a revised calculation of the amount of the collection fee in fact due each month and what the consequences of this are.

MISTAKE

The Basic Facts

161. The 15% collection fee was charged to the Current account as follows:

(1) £473,838 on 30 June 2009;

(2) £364,561 on 31 July 2009;

(3) £141,250 on 28 August 2009;

(4) £92,111 on 1 October 2009;

(5) £27,495 on 30 October 2009;

(6) £27,843 on 30 November 2009;

(7) £15,495 on 4 January 2010;

(8) £12,540 on 29 January 2010;

(9) A total of £5,356 on 24 February 2010;

(10) £5,529 on 26 February 2010;

(11) £4,562 on 31 March 2010;

(12) Thereafter, some further fees in modest amounts.

162. Following demands made by Leumi pursuant to the Indemnity Agreement, BHL made two payments to Leumi in respect of the collection fees: £400,000 on 11 November 2010 and £550,000 on 9 May 2011.

163. BHL's pleaded case is that both of these payments were made under a mistake of law in that the sums demanded were not properly due from Cobra under the RFA and hence not due from BHL under the Indemnity Agreement. The proposition that they were not properly due (in the amounts claimed) is clearly correct in the light of my findings above.

164. The principal evidence from BHL on this question comes from Lord Bilimoria.

165. On 22 January 2010 Leumi made a written demand on BHL's solicitor, Mr Rogers at Clyde and Co. The letter said that the balance of the receivables stood at £3.5m. but as at 18 December 2009 the disputed/uncollectible debt was £2.5m. and in addition there were bad debts of £758,000. The Current Account balance at that time was £1.5m. and discount and collection fees would continue to be debited under the terms of the RFA. In view of the above, Leumi declared that collection of the receivables would be insufficient to fully repay the RFA Current Account. Accordingly they asked what steps needed to be taken to ensure money is flowing into BHL which will be paid to Leumi in accordance with the Indemnity Agreement.

166. Then, on 26 March 2010 Hammonds wrote to Mr Rogers seeking from BHL payment of the amount said to be owing on the Current Account which was now £1,475,522.96. That included the accrued collection fees of about £1.2m. Of course, since the collection fees had actually been charged monthly on the running account, in one sense most of them had been discharged. However, neither side took a point on this and both acted on the basis that the £950,000 paid was in respect of the collection fees. Or to put it another way, absent the imposition of the collection fees, the account would not have required that payment.

167. On 29 April 2010 and following a meeting which took place subsequent to the letter of 26 March, Mr Shah wrote to say that dividend payments to BHL from Cobra Beer Partnership were expected to commence on a monthly basis from September/October 2010 and BHL expected to settle its Leumi obligations within 12/18 months.

168. Thereafter, Leumi and Hammonds chased as to when the dividends were going to be paid.

169. In October 2010 BHL received the first such dividend of £473,000 which would have been sufficient to pay the first collection fee charged on the same amount. By his email dated 4 October 2010 Mr Shah referred to the forthcoming dividend and added that "we wanted to review the penalty fees you have charged".

170. On 13 October 2010 Mr Shah said that BHL had now received a "small dividend" payment and a cheque would shortly go out to Leumi in accordance with the Indemnity Agreement. On 14 October 2010 he wrote again, referring to the £473,000 dividend but adding that "we all need to agree on the matter of the assignment of the debtors and what is reasonable for Leumi to charge for their fees".

171. On 19 October 2010 Mr Willis wrote to Mr Shah and said among other things that "there will be no movement on our contractual fees which have been charged entirely properly and in accordance with the contract and we expect to be paid these in full."

172. Lord Bilimoria was not happy about this. In an email dated 19 October 2010 he wrote to Mr Italia and Mr Shah that "I hate these guys tone-they are such awful bullies - Vimal [Shah] don't take any nonsense from them and try to negotiate their rip-off fees…." As to what could be done about this, Mr Shah wrote two emails to Lord Bilimoria on 2 November: "Given that interest is accruing on outstanding amounts, I think we should send the £400,000 to Leumi… It will at least show a sign of good faith on our part. Unfortunately with regard to their charges it is more a matter of their goodwill as contracts etc are already signed and they are sticking to their contractual terms. James [Willis] insists that Leumi ABL's principal has not yet been recovered"… "Spoke to James at Leumi who has the paperwork ready to assign debts. His credit team will not assign without sight of some funds. Interest is being compounded daily as per the Invoice Discounting agreement. At present this is non-negotiable. I suggest that we do pay the £400,000 as a sign of good faith on our part. We can then follow through with checking of their charges. Trying to agree some standstill in return for speedier payment. To this end we may need some interim financing from a third party."

173. Lord Bilimoria responded as follows "… There is no chance of any funding from anyone-why should funding be required? We should pay them £400K now. They assign the debtors we try to recover what we can and use that to pay them more. Next May when we receive our next dividend we should be able to pay them another £500K and the balance in October when we receive our interim dividend. They should not charge any interest. They should waive their penalty fee after deducting the collection charges they have incurred so far. Please try and get them to agree to the above and if necessary we can all meet to agree it asap…."

174. On 8 November Leumi chased again for the £400,000 and threatened legal proceedings. Mr Shah said in an email to Lord Bilimoria that it had agreed to reassign the remaining Cobra debts but only once the £400,000 had been received. That payment was made on 9 November 2010 but Leumi immediately chased the remaining £73,000 available from the dividend.

175. On 11 November Mr Willis continued to chase and pointed out that the charges made by Leumi had been set out in the letter of 1 July 2009 (see paragraph 74 above) which had made reference to the fee of "up to 15%". Lord Bilimoria then emailed Mr Shah saying that if it was "up to 15%" then they did not have to charge 15% and "we could argue it was extortionate".

176. In fact, following later correspondence, the further £73,000 was not required to be paid at that stage. Thereafter, Leumi kept pushing BHL as to when the next dividend was due.

177. By April 2011 Lord Bilimoria had become aware that Leumi had charged 15% across the board since the commencement of the collect out and he said he was "outraged" that he should have to pay this fee in addition to the other third party charges which Leumi had passed on. He said that he told Mr Shah not to pay to Leumi any more dividend monies until an arrangement was agreed with Leumi over its collection fees and the assignment of the debts. In fact, the relevant email dated 7 April 2011 referred to an exit fee not a collection fee.

178. On 12 April, Squire Sanders, as Hammonds was now called, wrote requesting payment by 15 April of the amount of the next dividend payment of £550,000. On the same day Andrew Land of asset managers Och Ziff emailed Mr Italia to ask "I assume that from a legal point of view we have no choice but to pay Leumi the dividend but we are holding back in order to persuade them to assign the debt to us?" Mr Italia responded a few minutes later "yes you are right". There has been some debate as to what the latter expression meant. In my view, it clearly referred to the position said to be have assumed by Mr Land which included that there was no choice but to pay, from the legal perspective.

179. In the course of cross-examination, Lord Bilimoria was asked on several occasions whether he had sought any legal advice, even if informally prior to 4 October 2010 which is when Mr Shah had sent the email referring to "penalty". He said he had not at that stage, not to his memory.

180. However, subsequent to the completion of Lord Bilimoria's evidence I was informed by Mr Freedman that Mr Shah had drawn to the attention of BHL's representatives the existence of some documents that had not been previously seen in respect of earlier advice from Mr Ali Zaidi of Edwin Coe, and this led to the disclosure of the papers in connection with that advice.

181. Part of the background to the seeking of that advice was the fact that BHL was attempting to see if it could recover the VAT paid by Cobra in respect of what transpired to be bad debts which could not be collected or (in the case of credit notes) could not be collected in their full amount because if so, any refund of VAT could be used to pay the fees charged by Leumi.

182. That the origin of the advice lay in the VAT question can be seen from Mr Shah's original email dated 1 July 2010. Thereafter Mr Zaidi obtained a brief opinion from Counsel on the VAT question. At 24/6468-6479 there is a variety of internal notes and memoranda following on from Counsel's opinion.

183. It then seems that Mr Shah asked Mr Zaidi to contact Lord Bilimoria which led to the telephone discussion on 19 July 2010. Mr Zaidi's manuscript notes include a reference to "Bank being unreasonable". Following on from that, Mr Zaidi wrote a long letter to Lord Bilimoria. Much of it concerned the VAT question and the assignment of the debt but it also contained the following passages:

> "… It is understood that the [VAT] refunds amount to approximately £1.5m.. The Bank has been collecting outstanding debts due to Cobra Beer since it went into administration and has managed to recover sufficient sums to set off the monies that Cobra Beer originally out of the Bank. However, in collecting the debts, Bank has charged Cobra Beer a collection fee of 15% on the amount recovered. This fee amounts to approximately £1.5m. and remains outstanding from Cobra Beer.… You have asked me advise on whether there is any basis for claiming the £1.5m. in VAT refunds from Cobra B is administered Administrators so that you can use them to pay off your liabilities of Bank for the collection fee.… **My initial view**….. The Banks collection fee.. Under the Receivables Finance Agreement, the Bank has the right to require Cobra Beer to repurchase a debt from the Bank. If Cobra Beer fails to do so within 7 days of the demand, the Bank can charge a collection fee of up to 15% on the amount of the debt collected by the Bank. If this is indeed the case it will be difficult to challenge the collection fee.… **Further documents and information**.. I hope you find the above useful. In order for me to advise you further and consider what is the best way forward I should be grateful if you would supply me with the following…2. A breakdown of the collection fee that the Bank has charge Cobra Beer..3. Details of the debts that the collection fee relates to, including the amount that the Bank has collected.. If you would like me to collect this information on your behalf please let me know… I look forward to hearing from you.."

184. Lord Bilimoria was recalled to be cross-examined further on these matters. Leumi has suggested that Lord Bilimoria deliberately suppressed the fact and content of this advice and accordingly was lying when he said originally in evidence that to his memory there had been no legal advice before October 2010 (and in fact before September 2011). He denied this and said that he had forgotten about this relatively brief episode.

185. I accept that explanation. I do not think for one moment that Lord Bilimoria had come to court to lie on this (or on any other) point and indeed it would have been strange for him to lie about the existence of this advice which in fact (for the reasons given below) actually supports his case on mistake. Lord Bilimoria struck me as a generally reliable witness doing his best to assist the court but he was fairly "high-level" in his approach and was not always clear on the detail.

186. While dealing with Lord Bilimoria's credibility, another alleged example of a lack of truthfulness advanced by Mr Tozzi was in relation to Lord Bilimoria's evidence that he was shocked to see the letter from Leumi of 22 January 2010 and its reference to a shortfall of £1.4m.. It was put to him that he could not have been because on 16 September 2009 he countersigned Cobra's statement of affairs as at 29 May 2009 for the purpose of the administration. That document "wrote down" the sales ledger from £9.8m. to £7.9m. and on the basis of a debt to Leumi of £9m., there was a shortfall of about £1.1m..

187. Lord Bilimoria accepted that he had signed that document although he understood that the figures there were "very prudent" and although he was aware by September 2009 of Leumi's intended and actual charges he thought he might have forgotten that the monies owed by Cobra to Leumi of £9m. including those fees, especially over £1m. in relation to the collection fees. His own view (borne out by the reality) was that the ledger in general terms was highly recoverable and that is why he was still surprised at Leumi's letter of 22 January 2010. So while I agree he had signed a document showing a shortfall in September 2009 I do not think that any of this makes him out to be a liar.

188. For the sake of completeness, I recalled that much was made of a manuscript note at the bottom of a typed notes of a discussion with Counsel on 2 July 2010 and which referred to "debtor book good on paper but in reality v poor". It would seem likely that came from something which Lord Bilimoria had said although he could not remember saying it and said that he had thought the debtor book was very good and this had been proven. That might be said to have been unrealistic if one had regard to the amount of credit notes but on the other hand, this is something noted in July 2010 by which stage Leumi's exposure to Cobra had been recouped if one disregards the £1.2m collection fee. By that stage, it could not be said that the debtor book was very poor. Perhaps it was a reference to the large amount of credit notes in the previous year and that at least would chime with the issue of attempting to obtain bad debt VAT relief. But on any view (a) I do not consider this note to be relevant to the matters facing Leumi on 2 June and (b) I do not regard it as a matter adversely affecting Lord Bilimoria's credibility.

Was there a mistake?

189. In my judgment, there plainly was.

190. First, the clear thrust of the contemporaneous correspondence referred to above shows a belief on the part of Lord Bilimoria and Mr Shah that the collection fee was payable. The fact that Lord Bilimoria complained about it and thought it was excessive or extortionate does not mean that he did not think BHL was bound to pay it. Nor did his attempts to try and negotiate on it. The reference to a "penalty" by Mr Shah and to "extortionate" by Lord Bilimoria, in the contexts in which they were made, does not alter the position in my view.

191. Second, there is Lord Bilimoria's own oral evidence to the effect that he was mistaken. It is true that this is not stated in terms in his witness statement and I accept that he may have emphasised the mistake perhaps too often in his oral evidence but it is supported by what he was saying at the time. Thus I accept his oral evidence that he thought contractually they had to pay it, even though he thought that the extra amount was unfair and unreasonable and Mr Shah had told him the same. There was also the evidence of Mr Italia who said that it was very clear to them that they had to pay the money so what they were trying to do was to negotiate and do their best to minimise it. Mr Italia said that the monies were paid because he believed that they were contractually obliged to pay it and looking back on it this was a mistake.

192. Third, it is a plausible mistake to make. After all, Leumi was insisting that the fees were due under the contract and one must assume that (in the event) Leumi was mistaken as well, in the light of my findings above.

193. Fourth, the advice given to Lord Bilimoria, albeit brief and subject to further information, supports this. In respect of the collection fee it stated that if there had been a failure to repurchase the debts, as was the case, "it will be difficult to challenge the collection fee." This means exactly what it says. Perhaps if Lord Bilimoria had pursued the matter, supplied further information and taken much more detailed advice, BHL would eventually have ended up with the case it now makes; but he did not. Accordingly the only advice which Lord Bilimoria received about the collection fee was clearly negative from his point of view. I do not accept that the word "difficult" should be read as "capable of challenge but only on narrow grounds

like irrationality" (see paragraph 59 (c) of Leumi's written closing submissions). That is completely unrealistic. The advice at this stage was brief and to the point. I agree that "difficult" does not mean "impossible" but in this context and given that Lord Bilimoria had previously accepted that the fee was payable, although he did not like it, the advice confirmed that view.

194. Nor is there anything in the point that he did not follow it up. He could not really remember why he did not, but that does not matter, and on the question of the collection fee, one can understand if it was not thought worth the candle at that stage, given the negative view then expressed.

195. In addition, Leumi also relies upon clauses 6.2a, 8.4 and 9.3 of the RFA (as cited above). This point had never been pleaded or even presaged in the written opening. So it is something of an indulgence to consider it at all but Mr Freedman did not invite me to disregard it entirely for that reason. In any event there is nothing in it:

(1) clause 6.2 (a) is about the conclusive nature of particular amounts certified as such, not the underlying basis on which fees could be charged;

(2) clause 8.4 (d) is a "no set-off" clause. It is likewise irrelevant to the question of mistake here;

(3) clause 9.3 is about being bound by an estimate of fees cost and expenses where they could not be immediately ascertained; yet again, this does not affect a mistake as to the correct contractual basis for a claim to collection fees;

(4) finally, and importantly, insofar as they could be relied upon to shut off an enquiry into the true charging position between the parties (which I reject) it is far too late to seek to rely upon them when (with the consent of Leumi) precisely that investigation was undertaken during the course of the trial.

Did the mistake cause the payments?

196. Looked at objectively, from the circumstances described above it seems obvious to me that the mistake did cause the payments. If Lord Bilimoria or Mr Shah thought that they were not obliged to pay the money it is inconceivable that those payments would have been made. Of course, they sought to get something in return if possible i.e. the reassignment of the debtor book so that more money could be collected by them, but this hardly means that BHL would have paid the collection fees if it thought it did not have to.

197. In his oral evidence Lord Bilimoria said that they felt they had to pay the money despite the fact that they thought it was unfair.

198. Nor does the fact that BHL did not take any further the brief advice from Edwin Coe mean that it had decided to pay come what may and whether there was any liability or not.

199. In this regard Leumi relied upon the decision of the Court of Appeal in *Leslie v Farrar* [2016] EWCA Civ. 1401. The case itself was very different, being concerned with overpayments to a builder. The claim in mistake was refused (at first instance and in the Court of Appeal) because the parties had in fact agreed with each other that the key point was not to exceed the budget and even though the payments fell outside of what the builder was entitled to charge under the building contract this did not matter since it was still within budget. Hence there was no operative mistake because the claimant had taken a conscious decision to pay the sums without investigating whether they were in fact due because it suited his purpose. In this context, Jackson LJ then quoted the dicta of Lord Abinger CB in *Kelly v Solari* (1841) (M & W 54 where he said:

> "If the party makes the payment of full knowledge of the facts, although under ignorance of the law,… It cannot recover it back again. There may also be cases in which, although he might by investigation

> learned the state of facts more accurately, he declined to do so and chooses to pay the money notwithstanding; in that case they can be no doubt that he is equally bound".

200. I follow all of that but this case is entirely different. It cannot possibly be said that Lord Bilimoria simply was not interested in whether Leumi was entitled to charge the collection fees or not and accordingly declined to enquire further about it. That is an absurd proposition on the facts of this case as recounted above.

201. Mr Tozzi also relied upon the dicta of Lord Goff in *Woolwich v IRC* [1993] AC 70, also cited in *Leslie* at paragraph 34, that

> "… A payment is regarded as a voluntary payment and so as it recoverable in the following circumstances… (b) The payer has the opportunity of contesting his liability in proceedings but instead gives way and pays… So where money has been paid under pressure of actual or threatened legal proceedings which recovery the payer cannot say that for that reason the money has been paid under compulsion and is therefore recoverable by him. If he chooses to give way and pay rather than obtain the decision of the court… The payment is regarded as voluntary and so is not recoverable…"

202. Again, I follow that but this case is not that situation. The reason that BHL paid was not that legal proceedings were threatened. For all the reasons given above it was BHL's genuine view that the monies were in fact due. The added pressure from the threat of legal proceedings at one stage brought does not alter the position.

203. The final set of *dicta* referred to by Mr Tozzi here and as cited in *Leslie* came from Lord Hoffmann in *Deutsche Morgan Grenfell v IRC* [2007] 1 AC 558 (by which time recovery was possible in respect of mistakes of law) at paragraph 27:

> "Likewise, the circumstances in which a payment is made may show that the person who made the payment took the risk that if the question was fully litigated it might turn out that he did not owe the money. Payment under a compromise is an obvious example… I would not regard the fact that the person making the payment had doubts about his liability as conclusive of the question of whether he took the risk, particularly if the existence of these doubts was unknown to the receiving party… It would be more rational if the question of whether a party should be treated as having taken the risk depended upon the objective circumstances surrounding the payments as they could reasonably have been known to both parties, including of course the extent to which the law was known to be in doubt."

204. This last passage is more pertinent. On any objective view, BHL had not assumed the risk of it being decided later that the money was not owed.

205. It is plain that but for the mistake these payments would not have been made. The "but for" test is the appropriate one here; see paragraphs 63 and 64 of the Restatement of the English Law of Unjust Enrichment written by Prof. Andrew Burrows as assisted by an eminent advisory group of judges, academics and others. Merely because this was published in 2012 and so before the decision in *Leslie* is irrelevant because I do not read anything in that case which suggests that the causation test is otherwise.

206. However, in this case I would find that the mistake had caused the payments whether applying the "but for" test or one more favourable to Leumi for example that the mistake must have been the "essential" or "main" cause of the payments. Either way the result is the same.

Conclusions on Mistake

207. Accordingly, to the extent that the £950,000 paid by BHL exceeds the sums which Leumi could properly charge, BHL is entitled to recover it. This will need to be worked out in the manner suggested in paragraph 158 above.

THE COUNTERCLAIM

208. The sum claimed is £271,382.69. There is one issue which is whether the enhanced discount charge which was applied from 1 June 2009 and which forms part of the running account between the parties, was actually payable from that date. This is because it can only be charged under Clause 10.1 b once Leumi required Cobra to notify the customers of its interest in the receivables which happened on 30 June, or when Cobra ceased to act as Leumi's agent (if earlier). In reality it seems to me that Cobra ceased to act as Leumi's agent once Leumi took over the collections albeit that Mr Anwar and Mr Ladwa did not formally contract with Leumi until 30 June. Leumi was, after all, in administration from 29 May. I consider that the enhanced discount charge should have been applied co-terminously with the collection fee ie as from 3 June 2009.

CONCLUSION

209. Accordingly, BHL succeeds on its mistake claim to the extent set out above. I am most grateful to Counsel for the excellence of their oral and written submissions. At the handing-down of this judgment I will hear them on all consequential matters including the form of any order.