

IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION
COMPANIES COURT

Claim No. 584 of 2011

IN THE MATTER OF EUROPEAN HOME RETAIL PLC
AND IN THE MATTER OF FAREPAK FOOD AND GIFTS LIMITED
AND IN THE MATTER OF THE COMPANY DIRECTORS DISQUALIFICATION
ACT 1986
BETWEEN:

THE SECRETARY OF STATE FOR BUSINESS, INNOVATION AND SKILLS

Claimant

and

- (1) STEVAN LLOYD FOWLER**
- (2) NEIL DUNCAN GILLIS**
- (3) NICHOLAS PIERS GILODI-JOHNSON**
- (4) STEPHEN MATTHEW HICKS**
- (5) MICHAEL STEPHEN MACKELCAN JOHNS**
- (6) PAUL MUNN**
- (7) JOANNE ELIZABETH PONTING**
- (8) WILLIAM PETER ROLLASON**
- (9) SIR CLIVE MALCOLM THOMPSON**

Defendants

SKELETON ARGUMENT
OF THE 3rd DEFENDANT NICHOLAS GILODI-JOHNSON
For Trial Before Mr Justice Peter Smith Commencing Monday, 21 May 2012¹

Introduction²

1. Mr Gilodi-Johnson is the only son of Bob Johnson, one of the founders of Farepak. In 1993, its shares were listed on the London Stock Exchange. The listed company was Farepak plc. It subsequently changed its name to Kleeneze plc and then to the European Home Retail plc (“EHR”) in 2005. The original Farepak business at this time was carried on by a subsidiary known as Farepak Food and Gifts Ltd (“FFG”).

¹ This skeleton argument adopts the abbreviations used in the affidavits. For convenience, like the Secretary of State in his opening skeleton argument, Sir Clive Thompson, Mr Gillis, Mr Munn and Mr Johns will be referred to as ‘the non-executives’, even though Mr Gilodi-Johnson also considered himself to be a non-executive director of EHR.

² What follows is a summary of that which is contained in Gilodi-Johnson Aff: Affs 4/1/1-11 paras 1 – 57.

2. Mr Gilodi-Johnson was born in July 1971. After graduating in 1993 and spending a year in Africa, he worked until 1999 as an advertising salesman. He then did an MBA at Oxford and started work for UPC, the largest cable and broadband company in Europe. He worked at the headquarters on corporate strategy.
3. In August 2001, Bob Johnson died unexpectedly at the age of 60. The Johnson family, either themselves or through trusts, owned about 64% of EHR's shares. At the funeral, Sir Clive Thompson, who was a non-executive director of EHR, said the plan was for Sir Clive to become chairman and for Mr Gilodi-Johnson to be a non-executive director as a representative of the Johnson family trusts. Mr Gilodi-Johnson agreed. At all times there was always another representative of the Johnson family trusts on the board. It was first Mr Stephen Roberts, and then Mr Michael Johns (the 5th defendant).
4. While a non-executive director of EHR, Mr Gilodi-Johnson continued to work for UPC. However, in 2002 he decided to work for the Group. He was initially employed by EHR as a Business Development Manager and in about February 2005 he became managing director of FFG. Although he was managing director of FFG, he saw his continuing role on the board of EHR as being a non-executive role representing the Johnson family trusts. In this regard, he was provided with the same documentation and information that the other non-executive directors were given (save that, after March 2006, when the board packs from each of the subsidiaries ceased being provided to the non-executive directors, Mr Gilodi-Johnson requested that they continue to be provided to him).
5. In addition to Mr Gilodi-Johnson, both the EHR Group managing director (Mr Rollason) and Group finance director (Mr Hulland (until the end of 2005)/Mr Fowler (from the beginning of 2006)) were also directors of FFG. Mr Rollason would chair the board meetings of FFG. Mr Gilodi-Johnson's responsibilities lay in the sales and marketing of FFG's business and its general operation..
6. Mr Gilodi-Johnson had high regard for the directors of EHR. He had been a member of the board since 2002 and had seen them in action. He considered Sir Clive to be an impressive chairman and a very experienced businessman. He said the non-executive directors were always on top of their papers and contributed to all meetings. He says Sir Clive would go around the table asking everyone for their views.

7. The other members of the board of FFG were Mr Hicks (4th defendant), Mrs Ponting (7th defendant) and Ms Davy. Mr Hicks was the finance director of FFG. Ms Davy went on maternity leave in February 2006 and never came back. She formally resigned in August 2006 and was not a defendant to these proceedings. Mrs Ponting was in charge of the call centre and IT. She herself was on maternity leave until late February 2006, when she returned to work 3½ days each week.
8. During the events which are relevant to the present proceedings, Mr Gilodi-Johnson was 34 to 35 years old.

The law

9. Much of the law set out in the Secretary of State's opening skeleton argument is common ground. It summarises and sets out many of the principles that the courts have espoused in the 25 years or so since the CDDA 1986 came into force.
10. It is not disputed that ultimately the question the court has to ask is that set out by Jonathan Parker J in *re Barings plc (No 5)* [1999] 1 BCLC 433 at 483 paragraph [A4]³:

“‘Unfitness’ may be shown by conduct which is dishonest (including conduct showing a want of probity or integrity) or by conduct which is merely incompetent. In every case the function of the court in addressing the question of unfitness is to ‘decide whether [the conduct of which complaint is made by the Secretary of State], viewed cumulatively and taking into account any extenuating circumstances, has fallen below the standards of probity and competence appropriate for persons fit to be directors of companies’ (see *Secretary of State for Trade and Industry v Gray* [1995] 1 BLCL 276 at 284, sub nom *Re Grayan Building Services Ltd (in liq)* [1995] Ch 241 at 253 per Hoffmann LJ). This has been described as ‘a jury question’ (see *Re Sevenoaks Stationers (Retail) Ltd* [1991] BCLC 325 at 330, [1991] Ch 164 at 176 per Dillon LJ).”
11. The only allegation of want of probity or integrity made against Mr Gilodi-Johnson is that he sought to mislead the boards of EHR and FFG regarding the developing situation in relation to the forecast inability of EHR to put FFG in funds to pay the Choice payment falling due in January 2006. This is a serious allegation but, as set out in more detail below, it is completely without foundation and unsupported by evidence. What has happened is that the Secretary of State has swept up Mr Gilodi-Johnson into

³ Quoted in part by the Secretary of State at para 80 of his opening skeleton argument.

the allegation against Mr Rollason and Mr Fowler without giving sufficient thought as to the separate knowledge of Mr Gilodi-Johnson and the separate actions of Mr Gilodi-Johnson. This serious allegation should not have been made against Mr Gilodi-Johnson and it should not be persisted in.

12. Once this allegation is put aside, the case against Mr Gilodi-Johnson is, in truth, nothing more than that he acted incompetently in the discharge of his duties as a director.

13. As to this, the relevant principles can be summarised as follows⁴:

- (1) If the defendant's conduct falls short of the required standard of competence, he will be disqualified even though the conduct is not found to be dishonest or lacking in probity.
- (2) It is not necessary to show that the defendant's incompetence was total. However, where the case against the director is based solely on allegations of incompetence, it must be established that he was incompetent or negligent in a very marked degree⁵.
- (3) Whilst incompetence as a director is not easy to define, it denotes a failure or inability to comply with basic obligations.
- (4) A director is very unlikely to be found unfit solely on the basis of commercial misjudgement. For incompetence to justify disqualification, conduct amounting to culpable negligence, rather than mere misjudgement, is likely to be required.

14. Furthermore, the court must be careful to guard against the dangers of hindsight:

“the court must be careful not to fall into the trap of being too wise after the event”: (*Re Living Images Ltd* [1996] 1 BCLC 348 at 356a-c)

⁴ See, generally, *Walters and Davis-White, Directors' Disqualification & Insolvency Restrictions* (3rd ed), paras 5-73 to 5-101. See also *Re Barings plc, Secretary of State for Trade and Industry v. Baker* [1998] BCC 583; and *Re Barings plc (No. 5), Secretary of State for Trade and Industry v. Baker* [1999] 1 BCLC 433, affirmed [2000] 1 BCLC 523.

⁵ *Re Sevenoaks Stationers (Retail) Ltd* [1991] Ch 164, 184C.

15. As the Secretary of State acknowledges, it is not his case that Mr Gilodi-Johnson knew or ought to have concluded that there was no reasonable prospect that either EHR or FFG would be unable to pay their creditors. The Secretary of State accepts that at all material times there was a reasonable prospect of both EHR and FFG being able to pay all their creditors.
16. The Secretary of State's case is that Mr Gilodi-Johnson caused or procured EHR and/or FFG 'to trade at the unreasonable risk of creditors'. However, it is important to note that it is not alleged that at any point in time prior to the eventual demise of the companies ought Mr Gilodi-Johnson (or any other director) to have caused or procured either EHR or FFG to have ceased trading. It is accepted that it *might* be open to the Secretary of State in a particular case to allege that, having regard to the particular state of affairs of the company in question, the continuation of trading per se renders that director unfit, even though there was a reasonable prospect of paying all creditors. But that is not the case sought to be made here.
17. Rather, the case here is that, having regard to the financial state of affairs pertaining to EHR and FFG, Mr Gilodi-Johnson (and each of the other directors of those companies) failed to take one or more steps which they ought to have taken. But, in this regard, it is important to note that a step that it is not alleged the directors ought to have taken was to procure that one or both of the companies should cease trading prior to the date that they did cease trading.
18. Once one recognises that the allegation is that the directors ought to have taken one or more particular steps (and ceasing to trade is not one of those steps), the phrase 'trading at the unreasonable risk of creditors' tells one nothing about the substance of the charges. It is better to concentrate on what exactly it is alleged the directors ought to have done rather than trying to shoehorn that conduct into the phrase 'trading at the unreasonable risk of creditors', which just leads to confusion where it is not suggested that the directors should have ceased trading sooner.
19. At paragraphs 51 to 53 of the Secretary of State's opening skeleton argument it is alleged that it is not a requirement of the making of a disqualification order that the Secretary of State must demonstrate that the alleged misconduct caused specific

identified loss. This is obviously right, but it does not follow that the court merely examines the alleged misconduct without at the same time also examining its causal effect. This is for two reasons.

20. First, as relevant in the present case, s.9 & Sch 1, Part II CDDA requires the court to have regard *in particular* to the extent of the director's responsibility for the causes for the company becoming insolvent and the extent of the director's responsibility for any failure by the company to supply any goods or services which have been paid for in whole or in part. This is not just dealing with the apportionment of responsibility amongst directors. What this is dealing with is the causal connection between the actions of the director and the company becoming insolvent or failing to supply any goods or services. This is a matter which the court must have *particular* regard. A mere failure to comply with a duty which has no causal effect, in that compliance would have made no difference at all, is not as serious a matter as a failure to comply with a duty which causes the company to become insolvent or to fail to supply goods or services.
21. Second, the causal effect of any particular alleged misconduct, or, perhaps more accurately, the foreseeable or likely causal effect of any particular alleged misconduct, is important for the purposes of categorising the seriousness of the alleged misconduct.
22. Finally, the analogy which the Secretary of State seeks to draw at paragraphs 74 to 76 of his opening skeleton argument with the non-payment of Crown debts is a false analogy. The ground of unfitness in relation to a 'Crown debts' allegation is that the director has not paid to the Crown the debts due to the Crown *as and when they fall due* but, instead of providing the necessary working capital, takes unfair advantage of the *forbearance* of Crown to collect its debts. In the present case, FFG did not in any way fail to comply with any contractual obligation to its customers prior to its collapse. There was no *forbearance* on the part of the customers, because there was no contractual obligation which had arisen which they could enforce. They were making pre-payments in respect of obligations performable by FFG in the future. Of course, the directors were under an obligation to take all reasonable steps to ensure that FFG was in a position to comply with its future contractual obligations, as with all obligations which arise in the future, but this is very different from determining not to pay debts which have already fallen due, which is the essence of a 'Crown debts' allegation.

23. The skeleton argument will now proceed to consider the facts and the specific allegations made against Mr Gilodi-Johnson. As the Secretary of State rightly identifies, his case falls into two distinct periods: the period up to and including 31 January 2006, when Choice was not paid the full amount owed to it and it went into administration; and the period after 31 January 2006.
24. It is important not to bring to the earlier period any hindsight from the latter period. There is no suggestion that up to the collapse of Choice Mr Gilodi-Johnson was aware that there was any prospect of not getting the same trading terms from Choice for the Christmas 2006 season that had been provided in respect of the Christmas 2005 season. It was the collapse of Choice and the inability to get the same terms previously offered by Choice that produced the financial problems which eventually led to the demise of the EHR Group. The financial issues that faced the EHR Group after the collapse of Choice were different to those that existed prior to the collapse of Choice.

The period up to 31 January 2006

25. In respect of this period an allegation is made against Mr Rollason, Mr Fowler and Mr Gilodi-Johnson that they
- “ ... sought to mislead, alternatively failed adequately to inform the other directors of EHR and FFG with regard to the developing situation regarding the forecast inability to pay the January Choice payment in full and on time.”
26. In order to make good this allegation against Mr Gilodi-Johnson, it is first necessary to establish that he knew that there was a forecast inability to pay the January Choice payment in full and on time. It is only if he knew this that one can even begin to accuse him of seeking to mislead his fellow directors or failing to inform them.
27. There is no evidence at all that Mr Gilodi-Johnson knew that it had been forecasted that FFG would not be able to pay the January Choice payment. The payment was due to be made on Monday 30 January 2006. Mr Gilodi-Johnson was due to, and did, fly out of the country on Saturday 28 January 2006. He was due to be away for two weeks. On Friday, 27 January 2006, before he left, he signed the CHAPS payment to Choice for the full amount in the belief and understanding that the full payment would be made on the Monday. It is difficult to have more probative evidence of his ignorance that it was

forecasted that the amount could not be paid. While abroad on Monday 30 January 2006, he was telephoned by Steve Hicks to be told that the full payment had not been made. This was a surprise and a shock to him.⁶

28. In addition, the Secretary of State even goes as far as to allege that one of the matters that renders Mr Gilodi-Johnson unfit to be concerned in the management of a company is that he gave no warning to Choice that there was a problem in making payment until the very last moment and that prior to then positive assurances had been given that payment would be made on time.⁷ He could hardly give a warning to Choice that there was a problem when he did not know himself that there was a problem. As for allegation that Mr Gilodi-Johnson gave positive assurances to Choice, the Secretary of State's affidavit contains no evidence of this whatsoever and it is clear that Mr Gilodi-Johnson gave no assurances at all to Choice
29. The Secretary of State also alleges that Mr Gilodi-Johnson knew that Choice itself was in financial difficulties because it had been made clear to EHR that another debtor of Choice's had indicated that it could not pay Choice on time.⁸ This is one of the matters that the Secretary of State says contributes to Mr Gilodi-Johnson being unfit to be a director. But the meeting at which it is alleged Choice had made it clear that another debtor could not pay Choice on time was a meeting attended by Mr Rollason and Mr Fowler, not Mr Gilodi-Johnson.⁹
30. This is all very typical of the Secretary of State's case against Mr Gilodi-Johnson in the period up to 31 January 2006. There is a complete failure to distinguish Mr Gilodi-Johnson's knowledge and actions from those of Mr Rollason and Mr Fowler.
31. The foundation of Mr Gilodi-Johnson's alleged knowledge of the forecast inability to pay Choice is the consolidated Group cash flow forecasts, the forecasts which the

⁶ Gilodi-Johnson Aff: Affs 4/1 paras 58-65, pages 11-12 ; para 258, page 49; para 307, pages 59-60.

⁷ Burns Aff 1: Affs 1/10/385 para 1038.12.

⁸ Burns Aff 1: Affs 1/10/385 para 1038.12.

⁹ Burns Aff 1: Affs 1/5/138 para 340.

Secretary of State says were prepared at Group level from about October 2005.¹⁰ As set out in paragraph 129 of the Secretary of State's opening skeleton argument:

“By November 2005, consolidated cash flow forecast information produced within EHR was highlighting the risk of a funding gap, in other words an insufficiency of cash even under the proposed new Bank facility which was then still in negotiation, to eventuate in late January or very early February.”

32. These Group cash flow forecasts, however, were not seen by Mr Gilodi-Johnson and the Secretary of State has never put forward any evidence to suggest they were. He says he was not routinely copied in to consolidated Group forecasts and he cannot remember seeing any in the period of November 2005 to the end of January 2006. He was not aware that they were predicting that the bank facility would be exceeded in the week commencing 30 January 2006.¹¹ The first one he recollects seeing is the one that was attached to Mr Rollason memorandum to the EHR board dated 2 February 2006.¹²
33. It has to be remembered that although Mr Gilodi-Johnson was an executive director of FFG he was a non-executive director of EHR and in fact only received the same information that the non-executive directors of EHR received. They would not be copied into the consolidated Group forecasts, certainly not at this period. As Mr Gilodi-Johnson says in evidence, he was not involved in the day to day financial management of the Group. That was not his responsibility. He was managing director of one of the subsidiaries, FFG, and sat on the board of EHR as a non-executive director, in effect as a representative of the Johnson family, the majority owners. He played no role in the preparation of the Group forecasts.¹³
34. As already pointed out, the Secretary of State has produced no evidence that Mr Gilodi-Johnson saw any consolidated Group forecasts during this period.¹⁴ Mrs Burns appears now to accept this in her reply in her 4th affidavit at para 82¹⁵:

¹⁰ Burns Aff 1:Affs 1/5/106-7.

¹¹ Gilodi-Johnson Aff: Affs 4/1/40 para 216

¹² Gilodi-Johnson Aff: Affs 4/1/40 para 208.

¹³ Gilodi-Johnson Aff: Affs 4/1/40 para 208.

¹⁴ Gilodi-Johnson Aff: Affs 4/1/11-12 paras 58-65.

¹⁵ Affs 2/3/31.

“Mr Gilodi-Johnson also states in his affidavit at ¶58 that he, as a non-executive director, was not routinely copied into the consolidated group forecasts. It does seem to be the case that very little by way of forecast material was provided to the non-executive directors.”

So it now appears to be accepted that the primary evidence relied upon in the case against Mr Rollason and Mr Fowler was not seen by Mr Gilodi-Johnson. Yet the allegation that Mr Gilodi-Johnson sought to mislead his fellow directors in relation to the forecasted inability to pay Choice is persisted with.

35. In the allegation against Mr Rollason and Mr Fowler, the Secretary of State relies on discussions and communications between one or both of them and HBOS. Mr Gilodi-Johnson was involved in no communications or discussions with HBOS at that time. He did not know that HBOS had been approached on 20 January 2006 for an increase in the facility.¹⁶ The first that he recollects he knew about this was in Mr Fowler’s finance report dated 25 January 2006 for the EHR board meeting on 25 January 2006, where it was said¹⁷:

“Borrowing levels against facility remain tight and the importance of cash conservation is being impressed on the subsidiaries.

A three month £5.0 million overdraft facility has been requested from the BoS to provide a safety net.

The forecast January interest cover calculation whilst currently meeting requirements also remains tight.”

36. The minutes for the EHR board meeting on 25 January 2006 record the following¹⁸:

“Borrowing levels *from 30 January* for a three month period are highlighting a potential need for additional facilities. The Bank of Scotland has been informed. In addition payment terms with suppliers are being extended and all payments in excess of £10,000 have to be processed through a Group clearance procedure.” (Emphasis added).

37. As Mr Gilodi-Johnson emphasises in his evidence, this says that borrowing levels from 30 January for a three month period highlighted a potential need for additional facilities. He did not understand that the facility would not permit the payment to Choice in full

¹⁶ Gilodi-Johnson Aff: Affs 4/1/46 para 238.

¹⁷ D13/2/156.

¹⁸ C1/4/81.

on Monday, 30 January 2006.¹⁹ Indeed, as set out above, on Friday, 27 January 2006, Mr Gilodi-Johnson's last day in the office before being abroad for two weeks, he signed the CHAPS payment for the full amount to be paid to Choice in the expectation and belief that it would be paid in full. So how can Mr Gilodi-Johnson have sought to mislead his fellow directors in this regard?

38. Further, the numerous internal Group discussions or communications relied on by the Secretary of State during November and December 2005 and January 2006 against Mr Rollason and/Mr Fowler of the forecast funding gap did *not* involve Mr Gilodi-Johnson. He is not a party to any of these. At para 77 of Mrs Burns' 4th affidavit, she says:

“In relation to this time period, Mr Gilodi-Johnson states at ¶¶213 to 220 of his affidavit that he never received any correspondence that would have alerted him to the possibility of EHR breaching its facility headroom. *Be that as it may*, the Secretary of State's case is that he was on notice of the point by virtue of (at least) his attendance of the EHR board meeting on 30 November 2005 and the FFG board meeting on 15 December 2005, at which relevant matters were discussed.”
(Emphasis added)

39. One assumes that the grudging “Be that as it may” is an acceptance that Mr Gilodi-Johnson is right. So not only did Mr Gilodi-Johnson not see the consolidated Group forecast, and was not involved in the discussions with HBOS, the Secretary of State now also accepts that Mr Gilodi-Johnson did not see any correspondence or take part in any discussions relied on that would have informed him that there was a forecasted inability to pay Choice, or even, for that matter, a forecasted funding gap. So, again, how can the Secretary of State possibly continue with the allegation that Mr Gilodi-Johnson sought to mislead his fellow directors?
40. Yet, although the Secretary of State accepts that Mr Gilodi-Johnson did not see the relevant correspondence that the Secretary of State alleges demonstrates that there was a forecasted inability to pay Choice at the end of the January, the Secretary of State cannot bring himself to give up the serious allegation that Mr Gilodi-Johnson sought to mislead his fellow directors and, as set out in the passage two paragraphs above, relies on the following in support of that allegation:

¹⁹ Gilodi-Johnson Aff: Affs 4/1/11 paras 60-63.

“Be that as it may, the Secretary of State’s case is that he was on notice of the point by virtue of (at least) his attendance of the EHR board meeting on 30 November 2005 and the FFG board meeting on 15 December 2005, at which relevant matters were discussed.”

41. It is not clear what ‘notice’ it is said Mr Gilodi-Johnson had of ‘relevant matters’ at these meetings. But if it were only at board meetings that Mr Gilodi-Johnson was put on ‘notice’ of ‘relevant matters’, how can it be alleged that he sought to mislead his fellow directors about information which he himself only had notice of at board meetings? Unless, presumably, it is alleged that he had notice of matters at an FFG board meeting which he then sought to mislead the directors of EHR about, or vice versa? The Secretary of State does not even begin to particularise matters such as this.

42. In the Secretary of State’s opening skeleton argument at para 136 it is said:

“Mr Gilodi-Johnson says that he was aware of a need for cash conservation in January and February 2006, but was not aware that there was a risk the facility would be exceeded. His position is that he was not routinely copied into the Group’s consolidated forecasts and does not recall seeing any in the period November 2005 to the end of January 2006. The Secretary of State’s position is that he was (at least) on notice of the risk by virtue of his having received Mr Hulland’s email of January 2005, as well as his attendance at the EHR board meeting on 30 November 2005 and 21 December 2005 and the FFG board meeting on 15 December 2005, at which relevant topics were discussed and questions could and should have raised.”

We now have two additional matters relied on, namely, Mr Hulland’s email of 7 January 2005²⁰ and the board meeting of EHR on 21 December 2005.

43. The reference to Mr Hulland’s email of January ‘2005’ is not a typographical error for ‘2006’: the Secretary of State really is relying on an email received in January 2005 as evidence that Mr Gilodi-Johnson knew at the end of 2005/beginning of 2006 that FFG would be unable to pay Choice at the end of January 2006. This is simply unreal. It was at a time before Mr Gilodi-Johnson had started working for FFG. At the time, he was still employed at EHR as a business development manager and it was in that context that he was copied in to the email. That email²¹ to Mr Rollason, with a copy to inter alia Mr Gilodi-Johnson, had forecast a minimum cash requirement at the end of January

²⁰ Chron 2/1/1.

²¹ Chron 2/1/1.

2006 of £43 million, and contemplated a request to HBOS for an increase in facilities to £55 million. This was in the context of a then facility of £40m.

44. Yet the board minutes for EHR for 21 December 2005²² contain a statement that the Group's overdraft position at November was £2.6m lower than forecast and that the board had approved a new £40m facility from HBOS. There was no recorded suggestion that this would be insufficient and Mr Gilodi-Johnson has no recollection of any such discussion.
45. So whatever Mr Hullah's email of 7 January 2005²³, nearly twelve months earlier, had contained, it would have appeared to Mr Gilodi-Johnson as out of date at the end of 2005, even if he had remembered it. The email of January 2005 had said that there would be a minimum cash requirement of £43m at the end of January 2006 and was contemplating a request to HBOS for an increase in facilities to £55m. The facility that was negotiated with the bank at the end of December 2005 was £40m, and, as far as Mr Gilodi-Johnson was concerned, he had not been told that that was anything other than a sufficient facility, albeit it would be substantially utilised from the middle of January through February 2006.
46. But how does Mr Hullah's email of 7 January 2005²⁴ and the matters discussed at the board meeting of EHR on 21 December 2005 provide any evidence in support of the allegation that Mr Gilodi-Johnson sought to mislead his fellow directors as to the forecasted inability to pay Choice at the end of January?
47. Having discarded these two matters one is left with Mr Gilodi-Johnson's notice of relevant matters at the EHR board meeting on 30 November 2005 and the FFG board meeting on 15 December 2005 (although it is not understood how they support an allegation of seeking to mislead fellow directors). These two meetings will now be considered.

²² C1/3/77.

²³ Chron 2/1/1.

²⁴ Chron 2/1/1.

48. In the Chief Executive's Review for the 30 November 2005 EHR board meeting²⁵, it was reported that:

“The overdraft at 31st October was £3.8 million which is £1.7m favourable to budget due to favourable working capital movements.”

49. The Finance Report for the same meeting²⁶ said:

“Cash balances are £1.7m better than Budget and £6.3m better than forecast.”

50. The board minutes for EHR for 30 November 2005 record the following²⁷:

“Mr Hulland reported that cash projections for the final quarter showed that the Group would be close to its borrowing limits in February 2006 requiring careful control of cash resources.”

51. As Mr Gilodi-Johnson points out in his evidence, he was not told that the Group would *exceed* its borrowing limits. He believed from what he was told that the Group would be *close* to its borrowing limit in February 2006 and that this would require careful management. As he says, he understood that this was being dealt with by the Group's management team.²⁸ Again, it is not clear what the connection is with this meeting and the alleged seeking by Mr Gilodi-Johnson to mislead his fellow directors

52. As to the reference to the FFG board meeting on 15 December 2005, the following is recorded in the minutes of the meeting²⁹ after Mr Hulland joined the meeting:

“There was discussion of the Group overdraft position in late January and through February. There was a need for cash planning and conservation during this period for all divisions of the Group. Cash flow forecasts should be reviewed.”

53. The following day Mr Hicks emailed his comments on a “review of cash” then under preparation to, among others, Mr Gilodi-Johnson and said that FFG would try to minimise cash outflows from the middle of January and through February by tight

²⁵ D10/5/388.

²⁶ D10/5/413.

²⁷ C1/3/74.

²⁸ Gilodi-Johnson Aff: Affs 4/1/42 para 217.

²⁹ C2//2/84.

control of supplier payments.³⁰ As Mr Gilodi-Johnson says in evidence³¹, he had no reason to expect that the Group bank facility would in fact be exceeded and that he had confidence in Mr Rollason, Mr Hulland and Mr Hicks (FFG finance director), all of whom were at the meeting.

54. Again, what is the connection between the Secretary of State's reference to this meeting and the allegation that Mr Gilodi-Johnson sought to mislead his fellow directors about the forecast inability to pay Choice at the end of January? What he is told in the FFG board meeting on 15 December 2005 is substantially the same as that which is told to the board of EHR at its meeting on 21 December 2005, where it was stated in the finance report as follow³²:

“Cash: as usual we are carefully reviewing cashflow over the key January/February period when cash outflows peak and inflows from Farepak customers are relatively low. We anticipate that our facilities will be substantially utilised during this period.”

As Mr Gilodi-Johnson says in evidence³³, the report stated that it was anticipated the EHR's facility would be 'substantially utilised' during January and February 2006: it did not say that it would be exceeded or that debts would not be paid.

55. So, again, what is the relevance of this meeting to the Secretary of State's allegation that Mr Gilodi-Johnson sought to mislead his fellow directors about the forecasted inability to pay Choice at the end of January?
56. Even if it be the case that (as set out in para 136 of the Secretary of State's opening skeleton argument) 'relevant topics' (whatever that might mean) were discussed at the EHR board meeting on 30 November 2005 and 21 December 2005 and the FFG board meeting on 15 December 2005 and that 'questions could and should have been raised' (what questions?), this does not begin to make out the serious allegation being made

³⁰ Chron 2/12/240-1.

³¹ Gilodi-Johnson Aff: Affs 4/1/43 para 224.

³² D12/1/30.

³³ Gilodi-Johnson Aff: Affs 4/1/44 para 225.

against Mr Gilodi-Johnson that he sought to mislead his fellow directors, or even failed to bring matters to their attention.

57. If this allegation is to be pursued, it is incumbent on the Secretary of State to set out clearly the case that Mr Gilodi-Johnson has to face and to identify the specific evidence relied upon. It is necessary for the Secretary of State to separate the case of Mr Gilodi-Johnson from that against Mr Rollason and Mr Fowler and to identify exactly what the case is against Mr Gilodi-Johnson. The Secretary of State must identify what is claimed to be the source of Mr Gilodi-Johnson's alleged knowledge of the forecast inability to pay Choice. To rely on information that Mr Gilodi-Johnson received in board meetings gets the Secretary of State nowhere in respect of the allegation that Mr Gilodi-Johnson sought to mislead his fellow directors.
58. The Secretary of State must then identify in respect of each of FFG and EHR what exactly it is said Mr Gilodi-Johnson did which the Secretary of State contends amounted to Mr Gilodi-Johnson seeking to mislead his fellow directors. Is the Secretary of State relying on any written communication? Or is it something Mr Gilodi-Johnson said orally? This must be explained.
59. As a general comment, it is difficult to see what possible motive Mr Gilodi-Johnson could have to *seek* to mislead his fellow directors. He was a member of the family that directly or indirectly controlled a majority of the shares in EHR. It was in his interests that the best decisions were made. Why would he seek to mislead his fellow directors? If he knew that there was a forecast inability to pay Choice at the end of January, surely he would have been the first person who would have wanted the non-executives to know so as to get their advice and input as to what should be done.
60. Even if the Secretary of State is not going to pursue against Mr Gilodi-Johnson the serious allegation that he sought to mislead the directors of EHR and FFG, it is still necessary to give proper particulars of the lesser charge that he failed adequately to inform the other directors of EHR and FFG with regarding the forecast inability to pay the January Choice payment. It is still necessary to identify what knowledge he had about the forecast inability to pay Choice which others did not which he should have communicated, and on what occasion and how it is alleged it should have been

communicated. This has to be done in respect of each of the boards of FFG and EHR, as the allegation is in respect of both. As there is no evidence that Mr Gilodi-Johnson knew of a forecasted inability to pay Choice at the end of January, it is difficult to see how he could have failed to pass this information on to his fellow directors.

61. In paragraph 148 of the Secretary of State's opening skeleton argument it is alleged that Mr Gilodi-Johnson knew more than the non-executive directors of EHR because he was also on the board of FFG. It is said that Mr Gilodi-Johnson was aware of 'creditor-stretching' and the proposal to borrow cash from HFH and was present at the FFG board meeting of 9 January 2006 at which this latter issue was discussed. These matters do not, of course, go anywhere near establishing that Mr Gilodi-Johnson knew that there was a forecasted inability to pay Choice at the end of January 2006, but each will be considered separately.
62. 'Creditor stretching', as the Secretary of State terms it, consists of the steps taken from 24 January 2006 to control payments made by subsidiaries and to limit their authority to make payments without authority to payments of £10,000³⁴.
63. Mr Gilodi-Johnson considered what the Secretary of State refers to as 'creditor stretching' to be a prudent and commercial policy where the bank facility was predicted to be substantially utilised.³⁵ In any event, the minutes of the EHR board meeting for 25 January 2006³⁶ show that all directors were told that payment terms with suppliers were being extended and that all payments in excess of £10,000 had to be processed through a Group. The notion that Mr Gilodi-Johnson kept this from the directors of EHR is without foundation.
64. So the only matter that Mr Gilodi-Johnson might have known which the non-executives did not immediately know was the proposal to borrow money from Home Farm

³⁴ See Burns Aff 1: Affs 1/5/134 at paras 327ff.

³⁵ Gilodi-Johnson Affs 4/1/47 para 248.

³⁶ C1/4/81.

Hampers (the joint venture company with Findel (FFG 40%, Findel 60%)). The following discussion took place at the FFG board meeting on 9 January 2006³⁷:

“There was discussion on Home Farm cash and the Group’s ability to use its 40% share. WPR was discussing with Keith Chapman of Findel.”

65. The possibility of borrowing money from Home Farm apparently came to nothing as Findel refused the request. In evidence, Mr Gilodi-Johnson says he was not included in the detail of the discussion about using Home Farm’s cash. He says it seemed to him that this was a sensible policy to pursue in the light of the fact that the bank facility would be substantially utilised. There was apparently a subsequent proposal that Home Farm should pay a dividend earlier than its year end, when it was normally paid.³⁸ Mr Gilodi-Johnson says in evidence that he was not copied in on the relevant correspondence and he has no recollection of this suggestion.³⁹
66. It is unclear how this leads to the conclusion that Mr Gilodi-Johnson knew that there was a forecast inability to pay the January Choice payment in full and on time and what exactly it is that he said (either in writing or orally) which constituted seeking to mislead his fellow directors, either his fellow directors on the board of FFG or his fellow directors on the board of EHR. It is also unclear as to why the proposal to borrow from Home Farm was necessarily a matter to be brought to the attention of the EHR board, or, more importantly, why Mr Gilodi-Johnson is being criticised for not bringing it to the attention of the EHR board.
67. One notes with interest paragraph 154 of the Secretary of State’s opening skeleton argument:

“To the extent that any of the Defendants lacked relevant knowledge of the cashflow situation and/or the steps taken in January 2006 to attempt to avoid a breach of the facility, the Secretary of State’s position is that such Defendants failed properly to make relevant inquiries and/or that *Messrs Rollason and Fowler* failed properly to keep the relevant boards informed.” (Emphasis added)

³⁷ C2/3/85. [Note: at this time all FFG board packs were sent to the directors of EHR so this information would have come to the attention of all directors of EHR.]

³⁸ Chron 3/4/55.

³⁹ Gilodi-Johnson Aff: Affs 4/1/47 para 243.

Here it is only alleged that it was Messrs Rollason and Fowler who failed properly to keep the relevant boards informed. It is not suggested that Mr Gilodi-Johnson failed to keep them informed.

68. If the Secretary of State is to continue to pursue the lesser charge of failing to bring to the attention of his fellow directors the situation regarding the forecast inability to pay the January Choice payment, full and proper particulars must be given.
69. The only allegation that is really left against Mr Gilodi-Johnson in respect of the period to 31 January 2006 is in truth the same allegation that is made against the non-executive directors, namely, that there was enough to put them on notice of a potential problem such that they 'should have asked relevant questions and found out the position'⁴⁰. It is said that they should have ascertained how close the Group was expected to be to the limit of the facility and how much it was expected HBOS would be prepared to cover.⁴¹
70. But it is not said what different steps should then have been taken, and it is not said how matters would have turned out differently if this had been done. More importantly, it is not said what Mr Gilodi-Johnson could have contributed to what Mr Rollason and Mr Fowler (and before him, Mr Hulland) were doing. It is Mr Gilodi-Johnson's case that it was perfectly proper for the Group Chief Executive and Finance Director to be left to deal with the Group overdraft and HBOS and that there was no additional benefit that he personally could have brought to bear on the matter.

The period from 31 January 2006 to 10 April 2006

71. The collapse of Choice left FFG without a multi-redemption voucher. The collapse of Family some two weeks later left FFG without a hamper packer.
72. The Choice voucher was replaced by Grass Roots' Bonus Bond, which could also be redeemed in numerous retail outlets. The agreement with Grass Roots was signed by Mr Gilodi-Johnson on behalf of FFG on 7 April 2006.⁴² The essential terms were as follows. FFG agreed to order Bonus Bonds from Grass Roots in the Autumn/Winter of

⁴⁰ Secretary of State's opening skeleton argument para 141.

⁴¹ Secretary of State's opening skeleton argument para 141.

⁴² Chron 5/2/120.

2006. It required FFG to pay for the Bonus Bonds prior to delivery of the same to FFG at their face value less a discount of 7.5%. An 'escrow account' was to be established by Grass Roots at Lloyds TSB into which the monies were to be paid. Monies were only to be withdrawn by Grass Roots in settlement of monies owing to retailers for the redemption of the Bonus Bonds. If Grass Roots became insolvent the monies in the account were to be payable to FFG. A charge was also granted over the account to FFG to secure this obligation. Interest earned on the monies while in the escrow account, less bank charges, was payable to FFG.

73. Negotiations for alternative solutions had continued right up to the time that the agreement with Grass Roots had been signed. In particular, FFG had been considering a joint venture with Sodexo and the purchase of multi-redemption vouchers from Provident. Findel had also been considering creating its own multi-redemption voucher.
74. Dealing with the fallout from the collapse of Choice and the negotiations with alternative suppliers was largely the responsibility of Mr Gilodi-Johnson.⁴³ Mr Gilodi-Johnson only got back in the office after being abroad for two weeks on Monday, 13 February 2006. While away he had been working on the fall out of the Choice collapse almost full time by telephone and email.⁴⁴ In particular, he had been assessing what support there might be amongst retailers for a newly constituted Choice.⁴⁵ One week after getting back he prepared his Business Report dated 20 February 2006 for the FFG board meeting on 21 February 2006.⁴⁶ This sets out what had taken place during the three weeks since the collapse of Choice.
75. He explained that as Choice vouchers represented some two thirds of FFG's savings club sales, its collapse caused considerable consternation amongst FFG's customers and the retailers who were redeemers of the voucher. He said it triggered 'a proverbial tsunami' of calls, emails and letters to FFG's service centre both from customers with unredeemed vouchers from their 2005 order and those who were concerned about their

⁴³ Much of the documentation in the Chronological Bundles for February, March and April (up to 7 April).

⁴⁴ Gilodi-Johnson Aff: Affs 4/1/49 para 258.

⁴⁵ Gilodi-Johnson Aff: Affs 4/1/55 para 283.

⁴⁶ D20/1/16.

2006 order. The service centre operated at full capacity of 50 seats for extended hours. Those with unredeemed vouchers were asked to return them and to select alternative vouchers from the FFG range. Some customers requested refunds and some requested a credit against their 2006 order. Some of them requested the M & S vouchers that FFG offered, which provided a lower margin for FFG. Many customers decided to cancel their 2006 orders in the absence of an alternative multi-redemption voucher. He said that a replacement multi-redemption voucher was critical.

76. He said the options open to them included (a) the creation of their own multi-redemption voucher; (b) Park's 'High Street' voucher and (c) the Provident voucher. He said each was being investigated. He said the first option was the most attractive but many retailers had lost substantial sums as a result of the collapse of Choice. Whatever option was pursued, he said they were likely to require some form of payment up front or into escrow to mitigate their risks. He concluded:

“... most retailers have asked for payment upfront for vouchers, which not only has a cash flow impact but also increases operational pressures...”

77. As regards the subsequent collapse of Family Hampers into administration, he said that an offer had been tabled by Home Farm (the joint venture between FFG and Findel) for their savings club. This was accepted but a cautious appraisal of the TUPE implications by the lawyers suggested the risks were too high. Park then stepped in and bought the business. The collapse of Family Hampers he said contributed to the sensitivity of FFG's suppliers and it would increase distribution costs as FFG had made savings by combining FFG's hamper volumes with those of Family. It also meant that FFG had to find someone else to pack their hampers.

78. At the board meeting on 21 February 2006⁴⁷, Mr Gilodi-Johnson updated the board on progress on a new multi-redemption voucher. He said that Provident had suggested up front payment but he had responded with a proposal for an escrow account. He issued a comparison of Choice, High Street (Park's voucher) Provident, Capital Bonds and Grass Roots' Bonus Bonds. It was decided to get lawyers to draft an escrow account. It was also decided that a budget would be drawn up on various different assumptions. Mr

⁴⁷ The minutes are at C2/4

Rollason advised that Park had offered to pack hampers on the same basis as the Family contract.

79. Mr Rollason's Chief Executive's Review dated 24 February 2006⁴⁸ for the EHR board meeting on 1 March 2006 dealt in detail with the situation at FFG and the consequence of the demise of Choice and Family (much of the factual information having been supplied by Mr Gilodi-Johnson⁴⁹):

“This has made [retailers] very nervous about vouchers as a whole and we are currently having to pay for the majority of our vouchers up front, as indeed are Park. This is likely to continue in the future and it is highly unlikely that we will have the three month credit in the future that we have had in the past. If this were to disappear it would cost Farepak about £0.5 million per annum.”

80. He went on to explain that an offer had been made for Family but had been withdrawn due to TUPE difficulties and that Park had purchased the business, giving it 66% of the market.

81. He said they had been looking at the long term future of FFG. He pointed out inter alia that any replacement multi-redemption voucher for Choice would be likely to be at lower discount rates, that payment would have to be made up front and that interest would be lost. He said Peter Johnson of Park had asked him to give a price for the sale of FFG and Home Farm. He concluded his report as follows:

“Whereas previously I would not have recommended considering an offer for Farepak or Home Farm as it would not have reflected the value of the cash and the interest, I now believe that we should re-consider due to the following:

- Park now effectively controls the industry
- We are being squeezed on voucher margins.
- We are having to pay for vouchers up front thereby losing any interest or cash advantages for the three months after October.
- We will have to invest up to £800k to stand a chance of maintaining any profitability at all.

⁴⁸ D14/1/16.

⁴⁹ In any event, at this time all the subsidiaries' board packs were still being sent to the directors of EHR, so the directors of EHR would have received Mr Gilodi-Johnson's report for the FFG board meeting on 21 February 2006.

I would, therefore, recommend that I re-approach Peter Johnson to get a formal cash offer from him for both Farepak and Home Farm.”

82. At the EHR board meeting on 1 March 2006⁵⁰, the board agreed with the recommendation.

83. Even though the plan was to sell FFG, it was still imperative in the interim that steps were taken to source an alternative multi-redemption voucher. The steps taken are set out in Mr Gilodi-Johnson’s Business Report dated 17th March 2006⁵¹ for the FFG board meeting to be held on 20 March 2006. As he said in his introduction:

“The effects of both Choice and Family going into administration have continued to occupy the bulk of management time. Negotiations with alternative multi-redemption voucher providers are proceeding well, however time is against us and the retailers are not making it easy. Unfortunately, our ability to secure advantageous discount rates from the retailers is hindered by the urgent need for our customers to know what product they are paying in advance for. The aim is to be in a position to market the replacement voucher by the end of the month.”

84. He explained that they were dealing with Provident, Grass Roots and Sodexo but that research suggested that Grass Roots’ Bonus Bond was the most attractive option. He said that the impact of Choice had led to the expectation that sales would be down by some 11.6% compared to the previous year.

85. Mr Rollason reported at the next meeting of EHR’s board on 22 March 2006 on the steps he had taken to sell FFG and Home Farm:

“Agreement was reached with Findel on a turnover ratio basis split of consideration on the sale of Farepak and Home Farm.

Park were offered both for £24.0 million. The counter-offer was £12.0 million.

Park were unwilling to consider issuing shares or increasing their offer with a deferred element.

A further approach to obtain an increased offer, which would include a deferred element, is to be made.

Park did confirm they would be prepared to offer us High Street vouchers and pack hampers for Christmas 2006.”

⁵⁰ The minutes are at C1/5/82.

⁵¹ D20/2/125-127

86. No sale proved possible and it was in the light of this that the next board meeting was brought forward to 10 April 2006 to deal with the prospective cash flow problem. A paper⁵² was presented by Mr Rollason and Mr Fowler which showed that the facility would be exceeded from October 2006 to April 2007, peaking at an excess of some £15.6m in November 2006. They set out the options: (a) approach HBOS to request a seasonal facility; (b) a disposal of FFG together with a rights issue; (c) a disposal of FFG, Kitbag and a smaller rights issue; (d) a rights issue. At the board meeting it was resolved (a) to approach HBOS with a request for a two year seasonal facility (b) to invite a representative of the Johnson Trustees to the meeting and (c) if HBOS refused, to pursue the disposal of FFG together with a rights issue.
87. The time frame of some four working weeks from the collapse of Choice to the EHR board meeting of 1 March 2006 to try to assess the consequences of the collapse of Choice and make a decision as to what to do in the light of those consequences was not at all unreasonable.⁵³ Once the problems were identified, the decision was taken on 1 March 2006 to sell FFG. Forecasts were already being prepared as part of the budgeting process. When it did not prove possible to sell FFG, detailed forecasts were prepared for the Group on the assumption that FFG would remain a Group company and the board met on 10 April to assess the options. That was all a reasonable and proportionate response to the position the Group found itself in.
88. Mr Gilodi-Johnson saw FFG as a profitable and valuable business, albeit it needed some restructuring. He saw it as worth significantly more than its balance sheet figure, as he says was subsequently demonstrated by the (rejected) offer by Park for £12m.⁵⁴ By the time of the collapse of Choice, the catalogues for Christmas 2006 had already gone out and orders and part payments were being received. FFG had a lot of goodwill and it was important to preserve that goodwill for the benefit of FFG and its customers.⁵⁵

⁵² C1/7/92.

⁵³ Gilodi-Johnson Aff: Affs 4/1/54 para 279.

⁵⁴ This included an offer for Home Farm as well, the joint venture between FFG and Findel.

⁵⁵ Gilodi-Johnson Aff: Affs 4/1/57 para 233; 4/1/58 para 295;

89. Throughout 2006, Mr Gilodi-Johnson was aware that continuing to trade would result in cash being swept into the Group HBOS account. There was nothing from a practical point of view that could be done about this. HBOS would not allow any variation. The money was in any event charged to HBOS. The only way that could be avoided would be to cease to trade. He says he did not need legal advice to be told that.⁵⁶ Mr Gilodi-Johnson's view was that a trust account was only ever a practicable option once FFG had decided to stop trading⁵⁷.
90. Indeed, it is difficult to put it any better than the s.447 Inspectors put it when reporting to the Secretary of State⁵⁸:

“The suspension of the 2006 savings cycle or the cessation of the sweep of savings to EHR could not ... have been carried out without causing the immediate collapse of the EHR Group.”

91. Thus, the future funding problem was identified early on and it was dealt with by seeking to sell FFG. When that did not prove possible an urgent board meeting of EHR was held on 10 April 2006 to determine the way forward. Mr Gilodi-Johnson submits this was the proper and correct response to the collapse of Choice. He denies that his conduct demonstrates any incompetence in the discharge of his duties as a director.

The period from 10 April 2006: EHR

92. After the 10 April 2006 EHR board meeting, Mr Gilodi-Johnson had little involvement in the dealings with third parties relating to the attempts to raise finance, other than through his attendance at board meetings. Mr Gilodi-Johnson's time was taken up with running FFG on a day to day basis. He did accompany Mr Rollason and Mr Fowler to their meeting with HBOS on 24 April 2006, he did see ABN AMRO with Mr Johns on 10 May 2006, and he did attend meetings with HBOS on 29 August and 2 October 2006, but on all four occasions the reason for his attendance was in effect because he was a representative of the Johnson family and the trustees.

⁵⁶ Gilodi-Johnson Aff: Affs 4/1/58 para 296.

⁵⁷ Gilodi-Johnson Aff: Affs 4/1/84 para 464; 4/1/92 para 516; 4/1/98 para 558; 4/1/99 para 562.

⁵⁸ L1(2)/356.

93. Mr Gilodi-Johnson took no part in the negotiations with Grass Roots that commenced in the middle of June 2006. These were undertaken principally by Mr Rollason. Mr Gilodi-Johnson's knowledge of these negotiations is confined to what he was told about them by Mr Rollason.
94. His conduct as a director of EHR during this period can largely be analysed by considering what happened at the board meetings of EHR.

EHR board meeting on 4 May 2006⁵⁹

95. Following the 10 April 2006 EHR board meeting the next meeting was held after Easter on 4 May 2006. In the interim, at the meeting on 24 April 2006 with HBOS, and HBOS' follow up letter dated 27 April 2006⁶⁰ to Mr Rollason, HBOS had said that it would not fund the required increase in the facility. Nevertheless, in tandem with this, discussions had been taking place with ABN AMRO about a possible rights issue. A meeting had taken place on 19 April 2006. This was followed by an initial draft produced by ABN AMRO. This first draft was not seen by Mr Gilodi-Johnson. He did, however, receive a later draft⁶¹ on 27 April 2006, when it was forwarded to him by Mr Rollason.⁶² This contained a number of different scenarios to the initial draft. The final paper was presented to the board for the 4 May 2006 meeting. ABN AMRO said it would be necessary to attract new investors, and for the Johnson family not to take up their rights and accept a dilution.
96. ABN AMRO's concluding paragraph stated as follows⁶³:

“As stated above, we think that under Scenario 1 a 2008 p/e rating for the company of 14.9x TERPS⁶⁴ and 12.7x t issue price for new investors is not sufficiently low to attract new investors, who will be looking for a rating closer to 8x. If we can persuade the market to accept an upgrade in the PBT figure to £5m as we have shown in Scenario 2, where the 2008 p/e rating for the company falls

⁵⁹ C1/8/100.

⁶⁰ Chron 6/4/223-4.

⁶¹ Chron 6/4/172-198.

⁶² Gilodi-Johnson Aff: Affs 4/1/73 para 385.

⁶³ D14/7/184.

⁶⁴ 'Theoretical ex-rights price'.

to 13.5x TERPS and 11.5x at issue price for new investors, this would help in marketing any rights issue to investors.”

As Mr Gilodi-Johnson points out in evidence, the PBT for 2008 subsequently proved to be £6.5m⁶⁵: see paragraph 102 below.

97. A large number of different options were considered at the board meeting, as the minutes testify.⁶⁶ The preferred option was the rights issue in conjunction with a sale of FFG. Mr Gilodi-Johnson recollects a discussion as to whether they should also pursue in tandem a sale of some of the other business. His initial view was that other options should be pursued in tandem but the opinion was expressed by others that this would interfere with the rights issue as it would confuse potential investors and thereby destabilise the rights issue. He says he saw the reasoning of this, and having not previously been involved in a rights issue, he believed it was appropriate to give weight to the views of those who had. As he points out, the board of EHR had members with considerable experience in corporate finance matters.⁶⁷ Furthermore, it has to be remembered that a rights issue was not in the interests of the Johnson family, because it would lead to a dilution of their shareholding. Nevertheless, he was persuaded this was the right route to go down and considered it to be the right route.
98. Because the rights issue would require the Johnson family to accept a dilution of their shareholding, its progress would need their consent. As Mr Gilodi-Johnson says in evidence, the Johnson family trustees approved the proposed rights issue the day it was put to them.⁶⁸
99. The description by the Secretary of State⁶⁹ of the rights issue being “the only ray of hope” is plainly wrong, as many of his witnesses agree. It was the preferred option. If it did not work, other options which had been discussed were available to pursue.⁷⁰
- The Secretary of State says that other options should have been pursued in tandem.

⁶⁵ Gilodi-Johnson Aff: Affs 4/1/76 para 401.

⁶⁶ C1/8/95a.

⁶⁷ Gilodi-Johnson Aff: Affs 4/1/76 para 403; Gilodi-Johnson Aff: Affs 4/1/82 para 451.

⁶⁸ Gilodi-Johnson Aff: Affs 4/1/76 para 400.

⁶⁹ Burns Aff 1: Affs 1/7/206 at para 546.

⁷⁰ Gilodi-Johnson Aff: Affs 4/1/75 para 399.

This was a judgment call for the directors to make. This was not a board dominated by one individual. It was not composed of ‘yes’ men. It included experienced businessmen and professionals, each of whom had something different to bring to the table. Each decided on the course of action that was in fact pursued. It is difficult to see how the Secretary of State can make out a case that each was incompetent to such a level that a disqualification order is merited. The evidence all points the other way: the decision taken by the board was obviously the correct decision because so many independent experienced businessmen and professionals came to the same conclusion.

EHR board meeting on 31 May 2006⁷¹

100. A paper prepared by Mr Fowler and dated 26 May 2006 entitled ‘Group Funding’ was sent to the directors beforehand.⁷² This pointed out that HBOS had appointed PwC to perform a business review on the Group, a copy of the executive summary of which was attached. The main conclusion was that there was a funding gap which needed resolution. This, of course, had been obvious to the directors for some time.
101. Mr Fowler’s paper said that work continued with ABN AMRO and attached a draft timetable, aiming for an announcement of the rights issue in the week commencing 17 July 2006.
102. He also attached a draft summary forecast for the year to April 2008, which showed a profit before tax and amortisation of £6.5m, a £3m increase over the year to April 2007. This growth was to come primarily from the internet businesses. He pointed out that the draft forecast was £0.5m higher than ABN AMRO indicated was required to produce an acceptable P/E ratio for the proposed rights issue.
103. He said that ABN AMRO had been engaged to investigate the possibility of their debt re-structuring arm providing finance for either the ‘£20m debt spike’ or the ‘full debt requirement’. He said both of these financing arrangements were short-term solutions as they would be provided at high interest rates, but he said that they would provide funding certainty should problems arise on the time of a July rights issue.

⁷¹ D15/2 (board pack); C1/9/96 (minutes).

⁷² D15/2/67.

104. The minutes of the meeting held on 31 May 2006⁷³ disclose that Park had offered £7m for the trade and assets of FFG. The board agreed that this was insufficient. It was noted that apart from the extra complexity a sale would add to the process of the rights issue, the sale would reduce bank facility headroom for the majority of the year and this would increase risk. It was therefore agreed not to pursue a sale at this time.
105. As regards the rights issue, it was noted that the Johnson family trustees supported the rights issue. Importantly, it was reported that a meeting had been held with ABN AMRO on 30 May at which the draft profit numbers of the year to 30 April 2008 had been discussed that ABN AMRO believed that given those numbers a rights issue to raise £20m “was realistic”. The timetable for the rights issue was discussed and the board were also told that ABN AMRO’s debt advisory team had been appointed to explore additional funding alternatives. As regards the need for an announcement, this was discussed and it was agreed that corporate finance advice would be sought from Macfarlanes.
106. It is difficult to see how the Secretary of State can realistically criticise the conduct of Mr Gilodi-Johnson, or any of the other directors. At the meeting of 4 May 2006 it was decided to pursue a rights issue with an attempt at the same time to sell FFG. It was decided not to seek a disposal of other business because that might interfere with the rights issue. At the meeting held on 31 May 2006 he is told that the p/e requirements for 2008 required by ABN AMRO had been exceeded and that ABN AMRO had advised that a rights issue “was realistic”. He is also told that at the same time ABN AMRO’s debt advisory team had been appointed to explore additional funding alternatives if the rights issue was not successful. None of this was an area within his particular expertise. It was being dealt with Mr Rollason and Mr Fowler. Mr Gilodi-Johnson could add nothing to the process and EHR had the benefit of four experienced non-executives to subject the work of Mr Rollason and Mr Fowler to critical analysis, which they did.

EHR board meeting on 27 June 2006⁷⁴

⁷³ C1/9/96.

⁷⁴ C1/10/100.

107. Prior to this the board had received a paper from Mr Fowler dated 23 June 2006 entitled 'Funding'.⁷⁵ He attached monthly profit and loss accounts, balance sheets and cashflows for the year to April 2008, which showed a peak debt in November 2007 of £32m, as compared to £34m in November 2006. He said Ernst & Young were using the forecasts for the two years as a base to produce a working capital report for the rights issue. This was expected 27 June 2006. He said that following the application of a number of sensitivities (set out in appendix 2 to the report) the view of Ernst & Young was that a fund raising of a net £20m provided sufficient headroom. However, Mr Fowler said that, at the time of writing, ABN AMRO were still trying to arrange pre-marketing meetings, but were finding this difficult in a difficult market.
108. As regards debt raising, Mr Fowler's report said that ABN AMRO's debt arm had been unable to secure any in-house finance mainly due to their view that the solution was an equity cash injection and that HBOS' position was that any new debt would rank after their security. He said ABN AMRO had been given permission to contact three outside organisations to ascertain their appetite to provide debt.
109. Finally, Mr Fowler said that discussions had taken place with Grass Roots on 15 June 2006 to try to secure payment on redemption rather than on the issue of the vouchers and a response was promised within two weeks of the meeting. As set out above, Mr Gilodi-Johnson played no part in these discussions with Grass Roots.
110. At the board meeting held on 27 June 2006⁷⁶, ABN AMRO were present. They said that ten non-current investors had been approached but market sentiment had hampered arranging pre-marketing meetings. They said a further ten had been considered but were not approached as they were either closed to new funding or their investment focus did not fit this equity raising. They said that they wished to approach the existing institutional investors and said this would be easier if an announcement had been made as there would then be no issues about imparting what would otherwise be inside information. They thought that by approaching the existing investors they should be able to raise £10m-£12m with the balance of the £20m being possibly raised

⁷⁵ D15/3/121.

⁷⁶ C1/10/100.

from new investors. Finally, they advised that the current multi-pronged strategy of raising funds through equity, mezzanine finance and negotiations with Grass Roots should continue.

111. ABN AMRO then left so that the directors could discuss matters between themselves. It was reported that Numis had indicated that they believed that a net £20m could be raised from a rights issue at 20p per share. It was agreed that further discussions should take place with Numis and that ABN AMRO should be questioned over the ability to move to the AIM market. The board was also told that ABN AMRO's debt arm was meeting Goldman Sachs that day to explore further the raising of funds through mezzanine finance. Meetings were to take place with other providers later in the week. Finally, the board was told that Mr Rollason was meeting with Grass Roots on 11 July 2006 to further discuss payment terms.
112. Mr Gilodi-Johnson's evidence is that, having been told at the previous board meeting that ABN AMRO had considered the rights issue to be realistic, he was surprised with the information that they were now giving the company.⁷⁷
113. On 30 June 2006 EHR made a market announcement⁷⁸:

“The Board of European Home Retail plc announces that futher to the trading update announced on 23 March, the group is trading in line with the revised expectations as set out in that announcement.

However, the Group's voucher provider, Choice, went into administration earlier this year. The result of this has been a change in the environment in the voucher marketplace. The likely effect of this is that future payment terms for vouchers will be less advantageous than in the past. Such a change in payment terms would give rise to an Autumn peak borrowing requirement substantially higher than in previous years and above current bank facilities.

The Board is exploring all options to arrange additional financing for this peak period.”

Mr Gilodi-Johnson was not involved in the discussions leading to the making of the announcement or its terms.

⁷⁷ Gilodi-Johnson Aff: Affs 4/1/82 para 448..

⁷⁸ Chron 12/7/244.

114. Although the next EHR board meeting had been scheduled for 12 July 2006, it was brought forward to 3 July 2006.

EHR board meeting on 3 July 2006⁷⁹

115. At this meeting the directors were updated as to discussions with Numis. It was said that although Mr Hemsley of Numis had initially confirmed that they could raise £20m at 20p per share, Mr Turner, the chairman, was subsequently less enthusiastic and, after a board meeting, confirmed that Numis would not take matters on as they did not currently have capacity.

116. The directors were also told that ABN AMRO were currently organising meetings with current investors to take place in the next 10 days.

117. The directors agreed to continue to pursue all available options: (a) equity fund raising; (b) mezzanine finance; and (c) sell the business as a whole.

118. The board was told that ABN AMRO had been requested to provide a vanilla £10m loan. They were also told that mezzanine finance was being progressed and that after an initial meeting with Goldman Sachs, ABN AMRO's debt department were arranging for a meeting to take place during the week commencing 3 July 2006. In addition, a number of potential buyers of the business were discussed and Mr Rollason was authorised to discuss and provide information to ABN Capital, H Solomon and Bridgepoint. Finally, it was noted that Peter Johnson of Park had verbally stated that he would offer £7m for FFG, thereby increasing the value to the Group as no tax would be paid. However, it was further noted that this did not reduce the need for a cash injection of about £20m.

119. On about 10 July 2006, there was a proposal for the Johnson family trusts to contribute £3m towards a revised rights-issue.⁸⁰

EHR board meeting on 17 July 2006⁸¹

⁷⁹ C1/11/104 (minutes).

⁸⁰ Burns Aff 1: Affs 1/8/248 para 666; Gilodi-Johnson Aff: Affs 4/1/89 para 491.

⁸¹ C1/12/106 (minutes).

120. ABN AMRO attended the meeting at the beginning. They said that existing institutional shareholders were either unwilling to invest or would only invest if a cornerstone investor could be found. As for potential new investors, the meeting was told that the investment was too small or the Group had insignificant asset backing. ABN AMRO said their view was that a rights issue of £18m-£20m was not achievable. They said if the Group demonstrated significant improvement in results, the perception may change. They said that a change in management would be unlikely to change investors' views. Upon ABN AMRO leaving the room, the directors agreed that the rights issue process would stop.
121. The meeting then considered the option of selling the business as a whole. It was reported that neither Bridgepoint nor H Solomon were interested in buying the business. Alchemy had also said they were not interested, but they were being asked to re-evaluate. Finally, it was pointed out that ABN Capital had been provided with information and had said that they would respond during the week commencing 24 July 2006. The meeting concluded that a short-term solution from private equity seemed unlikely.
122. They then went on to consider mezzanine finance. It was pointed out that Bank of America and Morgan Stanley would only take a subordinated position if HBOS wrote off a significant element of their debt, which was unacceptable to HBOS. However, Goldman Sachs had offered, subject to due diligence, a £20m subordinated revolver for 18 months. The financial terms were explained. It was decided to progress the offer from Goldman Sachs although, prior to signing an exclusivity agreement, the possibility of a deal with Deutsche Bank was to be explored.

EHR board meeting on 25 July 2005⁸²

123. A funding report dated 21 July 2006 prepared by Mr Fowler was sent to the directors in advance⁸³. It was said that a meeting had taken place with Deutsche Bank and that a response was expected the following week. It was said that discussions were

⁸² C1/13/119.

⁸³ D15/7/278.

continuing with Goldman Sachs who were pushing for exclusivity. The Working Capital Report prepared by Ernst & Young was also attached.

124. At the meeting itself⁸⁴, the mezzanine finance position was discussed. The board was told that Deutsche Bank were not interested. It was agreed that matters should be progressed with Goldman Sachs who were the only provider that did not require an immediate loan write down by HBOS. It was agreed to grant a two week exclusivity period to Goldman Sachs. As regards selling the business as a whole, it was reported that Alchemy were £15m short on valuation for their own internal rate of return while ABN Capital were still looking at the numbers. It was also reported that Findel had expressed an interest in both the internet businesses and the Group and that three Chinese investors ('4Kids') may be interested in taking a stake in the business. Mr Johns reported that the trustees had approached Philip Newton who was interested in raising £20m from a "fan club", but the board agreed that this was not the best time to pursue this opportunity, although Mr Rollason agreed to meet him.
125. It was concluded that the highest priority was the mezzanine finance process and that no action should be taken to derail this process. It was agreed that due to concerns around confidentiality that only Findel, subject to signing a confidentiality letter would be provided with basic information including the model for the two years to April 2008. They were to be requested to submit an indicative offer prior to any further access to the Group being provided. Finally, it was pointed out that the Working Capital Report showed that the Group had sufficient facility headroom if a £20m cash injection/facility were obtained (the report of course dealt with a rights issue of £20m but the same conclusions would largely apply to any other cash injection).
126. One only has to read the minutes to see that there were reasonable prospects available to EHR, in particular in relation to Goldman Sachs, as they did not require HBOS to write off any of its debt. It was plainly in the best interest of the Group and all its creditors that trading continued in the interim while these solutions were being pursued.

⁸⁴ C1/13/109.

EHR board meeting on 7 August 2006⁸⁵

127. It was confirmed that Goldman Sachs had been given a two week exclusivity period to provide a mezzanine loan. It was also reported that Findel had been provided under a confidentiality agreement with basic financial information and that they would revert by 11 August 2006. It was also reported that: (a) ABN Capital were expecting to respond on 15 August 2006; (b) 3i had expressed an interest and a meeting was to take place on 10 August; (c) a letter had been received from N M Rothschild expressing an interest from a client to buy Kitbag – it was agreed not to proceed with it for the time being; (d) Mr Rollason was intending to meet with potential Chinese investors at the end of August; (e) Grass Roots, although chased, had yet to respond to the request for a different payment profile for vouchers; (f) progress continued in raising the mezzanine loan in that draft legal documents had been produced and the KPMG due diligence report for Goldman Sachs was to be circulated by 8 August – it was intended that the deal would complete on Friday 11 August. There were reasonable prospects of a solvent solution and it is plain that it was right to continue. If trading had stopped everything would have lost. The Group would have collapsed.

EHR board meeting on 21 August 2006⁸⁶

128. On 13 August 2006, Goldman Sachs had said that they were only prepared to lend ahead of HBOS. This was a complete surprise. It was effectively the end of this possible solution as there was no way that HBOS were going to agree to this. This was reported to the meeting. It was also reported that the Deutsche Bank offer had also been rejected and that Grass Roots had confirmed that they were not prepared to issue vouchers on a redeemed payment basis.
129. The board was told that Findel was meeting HBOS on 22 August 2006 to discuss terms which would allow them to make an offer for the Group. They had indicated that the equity element of any bid would be nominal.

⁸⁵ C1/14/114.

⁸⁶ C1/15/127.

130. The meeting was also told that three private equity companies had received presentations the previous week, but none wished to bid for the whole Group: Sun Capital and ECI however were interested in purchasing Kleeneze and IWOOT.
131. It was said that if the Findel option was not possible it was intended that with the approval of HBOS to approach Park to offer a deal for them to purchase Farepak on a deferred payment plan or for them to offer High street vouchers to be paid on redemption to replace Grass Roots' Bonus Bonds or to provide a loan facility.
132. The board were told that HBOS believed itself to be fully covered by the realisable value of the assets of the Group and that this was driving their decision on any deals.
133. It was reported that a request had been made to HBOS to set up a trust account for Farepak but that this had been refused. HBOS had also said that in the absence of an external funding solution they would wish for FFG to be placed into liquidation, at which point they would continue to support the remainder of the Group. Mr Gilodi-Johnson's view was that there was no possibility of a trust account being agreed to by HBOS.
134. It was at this point in the meeting that Tim Lewis (corporate finance) and Simon Beale (insolvency) from Macfarlanes joined the meeting. They advised that based on the possibility of the Findel offer being realistic no action was required at either EHR or FFG.
135. Mr Johns and Mr Gilodi-Johnson said that the directors should continue to progress the Findel deal.
136. The end of the minutes of the meeting record the following:

“Sir Clive Thompson stated that one option was if the Johnson family were to inject a significant investment of circa £6.0-£8.0 million into the business as this would enable other investors to inject funds. Another alternative is for the Johnson family to loan the Group £20 million.

Messrs Gilodi-Johnson and Johns stated that an investment of this magnitude was not possible.”

Market announcement 23 August 2006⁸⁷

137. EHR requested that its shares be suspended with immediate effect pending an outcome to its current discussions regarding increased facilities for its peak borrowing period and publication of its preliminary results. It also announced that there would be a delay in the preparation and audit of its preliminary results of the year ended 30 April 2006.

EHR board meeting on 30 August 2006⁸⁸

138. On 29 August 2006 a proposal had been put to HBOS by which (a) Park would offer vouchers on deferred terms and subsequently acquire FFG; (b) the Johnson family trustees would inject £3m by way of subordinated loan from the end of September; and (c) there would be phased asset disposals. This has become known as the 'Park I' proposal. Because of the commitment by the Johnson family trustees, Mr Gilodi-Johnson had attended the meeting with the bank on 29 August 2006.
139. At the board meeting on 30 August 2006, Mr Rollason informed the board that this had been rejected by HBOS on the basis that there was an inherent uncertainty on the amounts and timing of the disposals and, more importantly, the proposal required the bank to allow substantial sums to be retained by EHR. The bank's preference was for a pre-pack sale to Findel via administration. Mr Rollason reported that HBOS were unhappy that the Johnson family had not offered to invest money earlier. Mr Gilodi-Johnson's case is that there was simply not that sort of money available.
140. At the end of the meeting the board discussed the possibility of the Johnson family trustees providing equity to a potential investor. The proposal was for a £10m investor to obtain approximately 50% of the total share capital with the Johnson family's interest being reduced to 14%-15%. After a private discussion between Mr Gilodi-Johnson and Mr Johns, Mr Gilodi-Johnson agreed to discuss this with the Johnson family trustees and respond the following day. This he did. The trustees were willing to permit an investor to have 50.1% of the total share capital of EHR if the investor

⁸⁷ C1/16/121.

⁸⁸ C1/17/122.

were able to inject £13m. This resulted in an extension of time by the bank until 11am on 1 September 2006.

141. The following day Mr Rollason reported to HBOS that Park were meeting with their bankers with a view to acquiring FFG for £6m and lending £13m to EHR in exchange for 50% of the share capital. He said he believed this was a serious offer. Apparently the bank indicated that if this proposal came to fruition it would continue to support the Group.
142. The bank was ready to appoint receivers with a pre-pack sale to Findel but Findel lowered its offer price and it fell through.
143. This led to what has been referred to as 'Park II'. The precise details of 'Park II' changed over time, but, in essence, by the end of September 2006 it involved
 - (1) A £3m loan from the Johnson family trusts, subordinated to HBOS;
 - (2) £1.875m of IWOOT loan notes and £3.1m of earn-out payments to be converted to a loan of £4.975m;
 - (3) Park to provide a loan of £3.5m (in the form of deferred payment terms (£3m) and an additional £500,000);
 - (4) Park to acquire FFG for £6m; and
 - (5) Kitbag to be sold for £15m.
144. On 7 September 2006 a further request had been made to HBOS by FFG to set up a trust account. This was refused the following day. This again was inevitable.

EHR board meeting on 19 September 2006⁸⁹

145. Mr Rollason reported that HBOS had been pursuing a pre-pack solution with Findel up until late on 1 September 2006 but that at the last minute Findel had reduced their offer. HBOS had then decided that their loss on the Findel deal was too large and as a

⁸⁹ C1/18/134.

consequence they had expressed an interest in Park II. He set out the then basis on which Park II was proceeding. This offered a real prospect of a solvent solution.

EHR board meeting on 4 October 2006⁹⁰

146. By now Findel had come back on the scene. The purpose of the meeting was to consider giving HBOS permission to speak to Findel and Deutsche Bank to explore the possibility of a sale of the business. The board agreed on the understanding that HBOS had to have regard in any solution to maximising funds to all creditors, and in particular FFG creditors.
147. On 10 October 2006 HBOS telephoned Mr Rollason to say that they would not support Park II and that they wanted him to work alongside PwC to complete a sale of parts of the business to Findel. The board of EHR met on 12 October 2006⁹¹ and resolved to request HBOS to appoint administrative receivers to EHR. Partners in PwC were formally appointed on 13 October 2006.

Conclusion: EHR April to October 2006

148. Numerous options were pursued, many of them at the same time. There was at all times a reasonable prospect of avoiding an insolvency. The directors made the right decisions at the right time. There was little Mr Gilodi-Johnson could personally add to this process. It was right to leave it to Mr Rollason and Mr Fowler and to draw on the experience of the non-executive directors at the board meetings. Mr Gilodi-Johnson was managing FFG on a day to day basis. Nothing during this period demonstrates incompetency on the part of Mr Gilodi-Johnson in the discharge of his duties as a director of EHR.
149. There is also an allegation made in respect of EHR throughout the whole of the relevant trading period that the directors failed in their duties to ensure that the board of FFG was properly aware of the factual position from time to time, that it was considering the position from the perspective of FFG and in its best interests and that any conflicts of duty in the case of FFG directors who were also directors of EHR

⁹⁰ C1/21/140.

⁹¹ C1/20/144.

were being properly addressed. As Mr Gilodi-Johnson was himself a director of FFG, these allegations add nothing at all to the case against Mr Gilodi-Johnson in relation to FFG and he does not intend to deal with them further.

The discharge by Mr Gilodi-Johnson of his duties as a director of FFG

150. The Secretary of State alleges that until the market announcement on 30 June 2006 Mr Hicks and Mrs Ponting were not made aware of the position EHR was in in relation to repayment of the monies swept up to it by way of loan. This will be dealt with below.
151. First, however, the following paragraphs summarise the numerous FFG board meetings that took place on and after 24 July 2006.
152. **24 July 2006 board meeting** (attended by Mr Rollason, Mr Fowler, Mr Gilodi-Johnson and Mr Hicks)⁹². Mr Rollason reported that the Group was in discussions with a number of parties to provide the additional funds required as noted in the market announcement. He said this included a payment plan with FFG's voucher provider which would track more closely the historic cashflows and hence redemption of vouchers rather than payment on issue. He said these discussions were likely to reach a conclusion in the next few weeks. Mr Gilodi-Johnson had no first hand knowledge of these discussions with Grass Roots: his knowledge came from what Mr Rollason told him. The minutes go on to provide:

“The Board noted that Farepak was at present neither cashflow insolvent nor balance sheet insolvent. The Board took the view, however, that in light of the cash requirement which may become due in November of this year, it was still prudent for it to consider which of the various courses of action available to it at present would best serve the interests of Farepak's creditors.

The consequences of

1. placing agents' cash in a trust account;
 2. Calling for the inter-company account with EHR to be repaid immediately,
- were explored.

It was agreed, however, that both courses of action would jeopardise the Group's funding and hence affect Farepak's ability to make future payments.

⁹² C2/8/100.

In contrast, in light of the discussions reported by Mr Rollason above, the Board had good grounds to believe that Farepak would continue to be able to honour its obligations to its customers if it were to maintain its current arrangements with EHR.

Therefore, it was resolved that the current arrangements would be maintained at least until the outcome of present discussions was known, although the situation would continue to be monitored.

There being no further business the meeting terminated.”

153. **8 August 2006 board meeting**⁹³. The following is recorded:

“Mr Rollason confirmed that the position in relation to the current financing arrangements of the Company in relation to agents’ cash and Group cash sweeping arrangements, as noted at the meeting of the Board on 24 July 2006 was unchanged. Mr Rollason confirmed that any change in the current arrangements would be notified to the Board immediately.”

The minutes also mentioned that confirmation of arrangements with Grass Roots for 2006 and the multi-redemption voucher offer for 2007 was outstanding.

154. **22 August 2006 board meeting**⁹⁴. There were only three attendees, Mr Gilodi-Johnson, Mr Hicks and Mrs Ponting. Mr Gilodi-Johnson told the meeting that HBOS had refused consent to set up a trust account. His own view is that that this was always inevitable.⁹⁵ He updated them as to the on-going proposals for Findel and Park to buy the Group or Farepak respectively⁹⁶. The board concluded that there were still grounds to believe that FFG would continue to be able to honour its obligations to its customers. They did, however, decide to end the ‘sweep’, as a possible insolvency was approaching. Mr Gilodi-Johnson’s evidence is that he did not consider that this made any difference as he thought that all monies were charged to HBOS in any event.⁹⁷ It would in any event be likely to bring everything down because HBOS would not agree to it. Eventually it had to be reinstated.

⁹³ C2/9/102.

⁹⁴ C2/10/116-7.

⁹⁵ Gilodi-Johnson Aff: Affs 4/1/99 para 558.

⁹⁶ Gilodi-Johnson Aff: Affs 4/1/101 para 573.

⁹⁷ Gilodi-Johnson Aff: Affs 4/1/101 para 574.

155. Mr Gilodi-Johnson sought and was given detailed legal advice by Simon Beale of Macfarlanes as to the position of FFG on 24 August 2006 in the light of the Findel deal no longer progressing. In essence Mr Beale said that FFG needed to assess whether EHR stood no real prospect of being able to make the repayments to FFG. If that was the case they should stop taking money from customers.⁹⁸ Further advice was received on 25 August 2006.⁹⁹ This was the first occasion that Macfarlanes advised that the FFG board might need to obtain separate legal advice. At no time subsequently, however, did they consider that any conflict of interest prevented them from advising both FFG and EHR and they did not subsequently advise that separate advice was needed.
156. **25 August 2006 board meeting.**¹⁰⁰ The purpose of this meeting was to provide an update on FFG's financing arrangements, in particular, the progress of a deal with Park. Mr Gilodi-Johnson was not able to attend this meeting. The board concluded on the basis of information provided by Mr Fowler that FFG would continue to trade.
157. **30 August board meeting.**¹⁰¹ The board was informed of the 'Park I' proposal. They decided that there were good grounds to believe that Farepak would continue to be able to honour its obligations to its customers and creditors.
158. **31 August 2006 board meeting (first)**¹⁰². The meeting was told that the Johnson family trustees were prepared to release 50.1% of the total share capital to an investor provided that the cash injection was £13m. The meeting was told that Mr Rollason was discussing the proposal with various investors. It was decided to continue trading.

⁹⁸ Chron 18/3/323.

⁹⁹ Chron 18/3/347.

¹⁰⁰ C2/11/119.

¹⁰¹ C2/12/136.

¹⁰² C2/13/138-9.

159. **31 August 2006 board meeting (second).**¹⁰³ A further board meeting was held at 7pm. The directors were told that the bank had granted an extension of time to 11am on 1 September.
160. **1 September 2006 board meeting.**¹⁰⁴ It was reported that Park were meeting with their bankers with a view to acquiring FFG for £6m and lending £13m to EHR in exchange for 50% of the share capital. He said he believed this was a serious offer. Mr Fowler said that the bank had indicated that if this proposal came to fruition it would continue to support the Group. As a result of further advice from Macfarlanes it was concluded that FFG should continue trading.
161. **2 September 2006 board meeting.**¹⁰⁵ Mr Gilodi-Johnson and Mr Rollason were not able to make this meeting. The board was updated as to the failure of the Findel offer and were told that HBOS had confirmed that although it had issued demand notices in respect of the debt owed by the Group it did not intend to enforce the notices.
162. **4 September 2006 board meeting**¹⁰⁶. The cash sweep (which had been suspended as a result of the decision at the 22 August 2006 board meeting) was reinstated, on the basis that 'Park II' had been well received by HBOS and that HBOS had confirmed that correctly structured it could offer a very neat solution to the current funding problem. Again, advice had been taken from Macfarlanes.
163. **6 September 2006 board meeting**¹⁰⁷. Mr Fowler reported that HBOS had been provided with cashflow information relevant to the EHR proposal involving Park II and required further time to assess the information. In the light of this, it was decided to carry on trading.

¹⁰³ C2/14/150.

¹⁰⁴ C2/15/158.

¹⁰⁵ C2/16/174.

¹⁰⁶ C2/17/180-182.

¹⁰⁷ C2/18/195-197.

164. **8 September 2006 board meeting**¹⁰⁸. The directors were told that HBOS were still considering Park II. The directors were also told that a request had been made the previous day for a trust account to be set up.
165. **11 September 2006 board meeting**¹⁰⁹. The directors were told that HBOS were still evaluating the proposal, but the request for a trust account to be set up had been refused.
166. **18 September 2006 board meeting**¹¹⁰. Mr Gilodi-Johnson and Mr Rollason could not make this meeting. Mr Fowler told Mr Hicks and Mrs Ponting that PwC were preparing a report on the Park II deal and were expected to report to HBOS on 20 September 2006. The board was also informed of the steps already under way in order to facilitate the Park II deal.
167. **25 September 2006 board meeting**¹¹¹. The directors were updated on the progress of Park II and it was determined that FFG should continue to trade until the result of the refinancing proposal for the Group was known.
168. **27 September 2006 board meeting**¹¹². Mr Fowler was in the chair. He said that HBOS did not believe that the current proposal allowed sufficient headroom within the proposed facility and had requested that investors be contacted with a view to putting more cash into the business. This was to be done. Mr Fowler said that HBOS appeared keen to maintain the solvency of the Group going forward and that Macfarlanes had confirmed that FFG's position remained unchanged. The board agreed that FFG should continue to trade.
169. **2 October 2006 board meeting**¹¹³. The minutes record that Mr Fowler reported that the Johnson family were not prepared to invest or lend any further. An outside investor

¹⁰⁸ C2/19/202-3.

¹⁰⁹ C2/20/209-210.

¹¹⁰ C2/21/213-4.

¹¹¹ C2/22/217.

¹¹² C2/23/221.

¹¹³ C2/24/225.

was prepared to lend on terms which included acquiring part of the family's equity, but the family were not prepared to agree this. He said that Park was willing to put up an additional £0.5m and this had been passed on to HBOS. Mr Fowler said that they would respond to the current proposal by the middle of the week. As a precaution Macfarlanes were being instructed to prepare a contingency action plan to be implemented should HBOS indicate that it was unable to support a solvent solution. After discussion, it was decided that FFG should continue to trade.

170. **5 October 2006 board meeting**.¹¹⁴ The directors were told that HBOS was yet to respond on the latest proposal and that Mr Rollason would be chasing their response the following day.
171. **6 October 2006 Board meeting**.¹¹⁵ The directors were told that HBOS had advised that they would not be in a position to give a response before Monday 9 October 2006. Mr Beale of Macfarlanes advised that FFG should not send out hampers.
172. **9 October 2006 board meeting**.¹¹⁶ The board resolved that in the light of the continuing delay by HBOS a letter should be sent pressing for a resolution.
173. **11 October 2006 board meeting**.¹¹⁷ The board was told that HBOS had rejected Park II and that a pre-pack sale of parts of the Group were to be made to Findel. They were told that Findel was not interested in FFG's business. The board agreed to proceed to administration and would attempt to stop taking customers' money with immediate effect.
174. On 13 October 2006 partners in BDO Stoy Hayward were appointed joint administrators of FFG.
175. Although some criticisms are made of the conduct of Mr Gilodi-Johnson in respect of the above, it is submitted this is completely unjustified.

¹¹⁴ C2/25/227.

¹¹⁵ C2/26/228.

¹¹⁶ C2/27/233.

¹¹⁷ C2/28/236.

176. The Secretary of State's real complaint is that set out at paragraphs 222 to 228 of the Secretary of State's skeleton argument, namely, that the FFG board failed to consider the projected funding gap for 2006-7 and that it was only with the market announcement on 30 June 2006 that Mr Hicks and Mrs Ponting would have become aware of the funding gap.
177. It is accepted that the information which the EHR board had and discussed from February to June 2006 in relation to the funding gap and the means sought to plug it were not discussed with Mr Hicks and Mrs Ponting at any board meeting of FFG during the relevant time.
178. Mr Gilodi-Johnson explains this as follows in his evidence¹¹⁸. He says he took his lead from Mr Rollason in terms of his dealings with the other members of the FFG board with respect to matters concerning EHR and the Group generally. Mr Rollason chaired the meetings and he left it to him to decide what to discuss about the Group's financial position. Because EHR was a listed company he knew that they had to be particularly careful as to what information was given to those on subsidiary boards who were not on the board of EHR, especially given the price sensitivity of such matters. He knew that the future of FFG depended on the ability of EHR to repay money lent to it and other Group companies, but it seemed to him that as three of FFG's board were members of the board of EHR including the chief executive and finance director, it was not unreasonable for Mr Hicks and Mrs Ponting to rely on the three of them to ensure that FFG's position was looked after vis a vis EHR and the group generally. He says he was well aware of his duties to FFG and to ensure that at all times there was a reasonable prospect of being able to pay all its creditors. He makes it clear that he does not want to downplay the roles of Mr Hicks and Mrs Ponting but he points out that a discussion with them at a board meeting of FFG about the financial position of EHR would not have made any practical difference: he says this was simply a product of who were the real decision makers at FFG. As he says, when the issue was discussed with them at board meetings in July 2006, Mr Hicks and Mrs Ponting agreed with the steps that were being taken by EHR. The fact is that FFG was inextricably tied up with EHR and the other Group companies. Mr Gilodi-Johnson's evidence is that Mr Hicks

¹¹⁸ Gilodi-Johnson Aff: Affs 4/1/9-10 paras 50-7.

and Mrs Ponting reasonably left Mr Rollason, Mr Fowler and him to look after FFG's interests in the Group context as the three of them were the ones who were privy to Group information.¹¹⁹

179. Mr Gilodi-Johnson's assessment was that all the money received by FFG was charged immediately to HBOS and that FFG was obliged to 'sweep' it to HBOS every day. To try to set up a separate trust account would not have been permitted by HBOS and to refuse to 'sweep' up the monies everyday would have likely brought down the whole Group. The only practical way that FFG could stop this was to cease trading. The fates of FFG and ERH were inextricably bound up with each other.
180. Nevertheless, Mr Gilodi-Johnson accepts the point that is being made. He recognises that more information could have been discussed at FFG board meetings with perhaps confidentiality undertakings being sought from Mr Hicks and Mrs Ponting in the light of the fact that EHR was a listed company. However, 'group' issues, even if they impacted on subsidiaries, were dealt with at group level and that did not strike him as unreasonable. As he points out, it cannot be said that they deliberately set out to hide anything from Mr Hicks or Mrs Ponting on the basis that the two of them might advocate something contrary to what he and Mr Rollason and Mr Fowler might want to do.
181. The Secretary of State also alleges that FFG ought to have considered whether the terms on which cash would be lent to other group companies should be renegotiated.¹²⁰ The Secretary of State does not state on what terms the cash should have been lent.
182. In putting the alleged misconduct into context a number of matters need to be borne in mind.
183. First, in the s.447 Inspectors report to the Secretary of State they did not identify the failure to inform FFG of certain matters or the failure of FFG to consider its different position as a potential ground of unfitness.

¹¹⁹ Gilodi-Johnson Aff: Affs 4/1/92 para 514.

¹²⁰ Secretary of State's opening skeleton argument para 112.

184. Second, in the Burns Aff 1 there was no suggestion that FFG ought to have considered renegotiating the terms on which it lent to EHR.¹²¹
185. Third, when Macfarlanes advised from July 2006 onwards they advised both EHR and FFG without considering that a conflict between these two companies prevented them from advising both. The first occasion that Macfarlanes advised that the directors *might* need separate advice was on 25 August 2006, but they never in fact subsequently advised that FFG should seek separate advice. Importantly, they never advised that FFG should seek to renegotiate the terms on which cash was lent to EHR.
186. Ultimately, these points may just be jury points, but they do serve to put the alleged misconduct in relation to FFG in its proper context in terms of assessing whether there has been incompetence in the running of FFG of a marked or very high degree that warrants disqualification.
187. One must not judge the February/March 2006 period with hindsight. It is true that each of the subsequent attempts to bridge the funding gap and provide the customers with the goods they had ordered failed, but, as the Secretary of State accepts, there was always a reasonable prospect of a solvent solution. The savings cycle had started before the beginning of February. There was a valuable business which they did not think would fail. Even if the rights issue process had started prior to the attempted sale of FFG in March 2006, there is nothing to suggest that in fact the ultimate outcome would have been any different.
188. As Mr Gilodi-Johnson says in his evidence, he was aware that each week customers were putting in more money towards their orders. He says that at all times from April 2006 onwards he considered that there was a realistic prospect of the companies avoiding insolvency and that customers would be better off by FFG continuing to trade, because this would be more likely to enable FFG to supply the goods ordered.

¹²¹ The first reference one has to this are the Part 18 replies: see, eg, para 8.8 (K1/4/29)

Failing to inform the boards of the developing financial situation from February 2006 onwards

189. Finally, it is alleged against Mr Gilodi-Johnson (and Mr Rollason and Mr Fowler) that from February 2006 they failed to take adequate steps to inform the boards of EHR and FFG of the developing financial situation.
190. As regards Mr Gilodi-Johnson, if the allegation in respect of FFG is that no adequate steps were taken to inform Mr Hicks and Mrs Ponting on the board of FFG of the funding gap and the steps being taken to deal with it, this has already been dealt with above. To the extent that it is alleged that Mr Gilodi-Johnson failed to inform them of other matters during this period, the Secretary of State should give particulars of this allegation.
191. As regards the allegation against Mr Gilodi-Johnson in relation to EHR, he is at a loss to know what it is that it is alleged he knew which he did not bring to the attention of the board of EHR. Again, the Secretary of State should give particulars.

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