Neutral Citation Number: [2020] EWHC 3485 (Ch)

Case No: **CR-2019-002315**

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
INSOLVENCY AND COMPANIES LIST (CHD)
IN THE MATTER OF THE STRATOS CLUB LIMITED
AND IN THE MATTER OF THE COMPANIES ACT 2006

Royal Courts of Justice
Rolls Building, Fetter Lane,
London, EC4A 1NL

Date: 21/12/2020

Before:

MR NICHOLAS THOMPSELL
sitting as a Deputy Judge of the High Court

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Between:

DIANA LANGER

Petitioner

- and -

(1) JOHN MCKEOWN
(2) THE STRATOS CLUB LIMITED

Respondents

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- -

Ms Anna Lintner (instructed by **Russells**) for the **Petitioner**
Mr Romie Tager QC and Mr Maxwell Myers (instructed by **Brook Martin & Co.**) for the **Respondents**

Hearing dates: 18 – 30 November 2020

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Approved Judgment

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

Covid-19 Protocol: This judgment is to be handed down by the judge remotely by circulation to the parties' representatives by email and release to Bailii. The date for hand-down is deemed to be 10.30 am on 21 December 2020.

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MR NICHOLAS THOMPSELL

INTRODUCTION

1. In June 2018, The Stratos Club Limited ("**Stratos**" or the "**Company**"), through its subsidiaries, owned and operated two lap dancing clubs in Marylebone ("**the Marylebone Club**") and Soho ("**the Soho Club**") both of which traded under the name "*Sophisticats*". The Marylebone Club had had a long trading history and was very profitable. The Soho Club had been acquired more recently, had been expensively fitted out and was not trading profitably, although its turnover had been growing.

2. By the end of February 2019, the Company was an empty shell. The companies in its group held only a small amount of cash, debt receivables and debt liabilities. The Soho Club had been acquired by companies owned by the First Respondent, Mr John McKeown (who I will refer to variously as "**Mr McKeown**" and, for convenience although he is technically only the First Respondent, the "**Respondent**"). The Marylebone Club had closed and had transferred its assets, staff, dancers and trade to other premises owned by a company that operated another lap dancing club based in the Euston area (the "**Euston Club**") which Mr McKeown had recently acquired (or was in the course of acquiring).

3. Mr McKeown was throughout the controlling director of Stratos and all of its subsidiaries and at the relevant times was the largest shareholder of Stratos, holding 50% and then later 75% of the shares. At the relevant times, the Petitioner, Mrs Diana Langer (who I will refer to variously as the "**Petitioner**" or "**Mrs Langer**") was a minority (25%) shareholder in Stratos.

4. Mrs Langer complains that she has been unfairly prejudiced by the conduct of the Company in a number of ways. Chiefly she complains that the sale of the business and assets of the Soho Club, and that of the assets and goodwill of the Marylebone Club, were each undertaken improperly at the instigation of Mr McKeown in breach of his duties as a director and that in acquiring the Euston Club Mr McKeown had diverted from the Company a valuable opportunity which would have allowed the Company to continue trading the business that it had pursued successfully at the Marylebone Club.

5. The Respondent denies each of the instances of unfair prejudice alleged by Mrs Langer. As regards the central allegations, the broad thrust of the Respondent's case is that his actions in bringing about the transfer of the assets and business of the Soho Club and the assets and goodwill of the Marylebone Club operated in the interests of the Company. This was because these assets had no significant value and the transactions benefited the Company. In the case of the sale of the Soho Club, he says that this relieved the Company from an intrinsically loss-making business. In the case of the Marylebone Club, he says that the Company benefited by avoiding liabilities for staff redundancies which otherwise it would have inevitably incurred. As regards the acquisition of the Euston Club, the Respondent denies that this was an opportunity that came to him in his role as a director of the companies in the Stratos group and he denies that it is an opportunity that the Company could ever have been able to take up.

Furthermore, to the extent that any of these events involved a breach of a director's duty, he says that this was remedied by later board and shareholders' resolutions.

6. Mrs Langer also says that she has suffered unfair prejudice as a result of financial mismanagement of the Company and its subsidiaries, including improper payments of salary to Mr McKeown and his friends and family and payments being made from the Company that were not for the benefit of the Company. Each of these accusations is denied by Mr McKeown.

7. Mrs Langer further complains that she has been unfairly prejudiced by being falsely accused of being indebted to the company on a shareholder loan account and through demands being made in a menacing manner for the repayment of these debts. Mr McKeown answers this by saying that the accusations of indebtedness were not false and that requiring repayment of these debts did not unfairly prejudice Mrs Langer.

8. Mr McKeown also refers to various actions taken by Mrs Langer which he says were to the detriment of the Company and which, he says, explain certain elements of his conduct. He says that, even if the Court finds anything in his conduct to criticise, Mrs Langer's conduct should be weighed against his own conduct.

9. Before considering these claims and defences in detail it is helpful to set out the relevant facts, which for the most part are agreed. They are complex and it will assist in understanding the issues involved to commence with a description of the events which took place in a broadly chronological order.

II. KEY EVENTS

10. It is important to understand that there has been a long history of dealings between the parties.

The acquisition of the Marylebone Club

11. The opportunity to acquire the Marylebone Club was identified by Mr Simon Langer ("**Mr Langer**") in 2001. Mr Langer and Mr McKeown had had business dealings before and were friends. By all accounts they became the best of friends, each respecting the other's abilities and taking holidays together. At this point Mr Langer had more experience of operating central London clubs of a similar nature to Sophisticats. Mr McKeown had a more general business experience and was stronger in relation to financial matters. He appears to have taken the lead in negotiating and structuring the acquisition.

12. Mr Langer at this point was developing a romantic relationship with the Petitioner, who later became his wife.

13. The Marylebone Club was acquired in 2001, at which point it was already a well-established club, having achieved a degree of fame (or notoriety) through its being featured on the television programme "Naked in Soho".

14. A notable feature of the arrangements at this point was that they included the payment of a royalty of 5% of net profits in return for the licensing or assignment of the trademark, a logo featuring a stylised "S" with catlike features. This trademark was not

in fact used in the business and I accept Mr McKeown's evidence that the pricing of this was not separately considered in any depth – it was regarded by all parties just as a way of providing a payment in a manner that the seller would find tax effective.

15. Another feature of the arrangement was that the sale agreement was conditional on a Company Voluntary Arrangement being entered into in relation to Mondrealm Limited ("**Mondrealm**"), the company which held the lease for the Marylebone Club.

16. A feature of how the Sophisticats business was operated over the years was that the operating companies and holding companies involved were liable to change to suit the needs of the business; to protect key assets where a company might be at a risk of bankruptcy; and to save tax.

17. At this point the top company through which the Sophisticats business was held was Futureproof Investments Ltd ("**Futureproof**"). The percentage ownership of this company is a matter of some dispute, but it is common ground that its beneficial owners included Mr McKeown, his then wife, Mr Langer, Carlo Cura (a friend and long-time business partner of Mr Langer) and the Petitioner.

18. It seems that the intention was that each of these would have a 20% interest, although it is Mr McKeown's evidence that this interest would be dependent on each having made the same contribution to the financing, which he says was not initially the case. Mr McKeown considered himself the arbiter of this arrangement and arranged for all of the company's shares (initially 510 shares) to be issued to himself, although eventually he did arrange for 20 shares to be issued to the Petitioner and 20 shares to Mr Cura. Mrs Langer did not understand that these were 20 shares out of 550 rather than 20 out of 100 and I formed a suspicion that the choice of giving her 20 shares rather than some other number may have been to give her that impression. Mr McKeown said that he considered himself to be holding the other parties' interests in shares on trust but there was no formal trust arrangement.

19. The rights and wrongs of these arrangements were not fully explored during the trial, and there is no particular reason why they should be. However, I consider it is noteworthy that these arrangements show at an early stage that Mr McKeown was keen to retain control of the company in which he was only a minority holder at this stage and that there was clearly a large degree of trust placed in him by the other beneficial owners.

20. There was some discussion in the evidence of the relative contribution of the different parties to the acquisition of the Marylebone Club and of the early days in running it. It is clear that Mrs Langer played a part in this, through contributing £30,000 in cash; in helping investigate the opportunity for the acquisition by seeing it from the inside as a dancer; and, in the early days, through fulfilling the role of "House Mother", with responsibility for the welfare and conduct of the dancers, as well as having a role in relation to marketing. She was also appointed as a director of Welbeck Restaurants Ltd ("**Welbeck**"), then the operating company for the Marylebone Club, although it is not suggested that she assumed the responsibilities of a director of that company with any great diligence. It would be fair to say that Mrs Langer placed more importance on her contribution than Mr McKeown was prepared to recognise.

21. Mrs Langer's active involvement in the business ceased or largely ceased in 2002 when she had a child, although she remained as a director of Welbeck until that company was liquidated in 2004. Whether her reduction in involvement was her choice or Mr McKeown's is a matter of some dispute, but I do not see it as being of any importance to the current proceedings.

The Futureproof Shareholders' Agreement

22. The ownership arrangements for the business needed to change after Mr Cura died in 2007. In addition, Mr McKeown had split up with his wife and had acquired her interest in the shares. A shareholders' agreement was entered into which confirmed shareholding interests in Futureproof of 50% for Mr McKeown, 25% for Mr Langer and 25% for Mrs Langer. The origins of the Shareholders' Agreement remain shrouded in mystery. None of the witnesses seemed certain about which firm had drawn this up or who had instructed them. Mrs Langer gave evidence that this was drawn up by Brook Martin & Co, who were the solicitors to Mr McKeown and generally to Futureproof and its subsidiaries, but Mr McKeown did not confirm this understanding. It was acknowledged on all sides, however, that the agreement was signed at Brook Martin's offices on Christmas Eve 2009.

23. It seems, however, that the agreement was put in place mainly as a result of Mrs Langer's wishing to have more certainty about the ownership arrangements. There is some evidence of the agreement as having been negotiated, as there are amendments to it that were initialled.

24. One of the matters contended on behalf of Mrs Langer is that this agreement continues to govern the relationship between the shareholders, despite later changes (described further below), as to which company they held shares in, following various corporate reorganisations.

25. To the extent that the contention is that the agreement remained a binding legal agreement, I must reject this contention. The agreement clearly relates to shareholdings in a particular company, Futureproof. There is nothing within it to suggest that it would apply also to further companies. Also, nothing has been pointed to in the conduct of the parties to suggest that they referred back to the Shareholders' Agreement at any later time when things were being done that were clearly incompatible with it.

26. Mrs Langer contends in the alternative that, even if the Shareholders' Agreement did not apply as a binding agreement, it evidenced an understanding as to how the parties would govern their relationship amongst themselves notwithstanding any change in the identity of the corporate entity through which the Sophisticats business was owned or operated. There is, however, no evidence that such an understanding was ever expressed among the parties.

27. This is not, however, to say that the existence of the Shareholders' Agreement is irrelevant to this case. In particular, I consider it to be significant that such an agreement was required at one point, and then at a later point the parties were content for the agreement not to be repeated when Futureproof ceased to be the main holding vehicle. It is also significant that Mr and Mrs Langer did not insist on taking up rights they had under the agreement, even when it was still in force. These facts suggest that Mr and Mrs Langer reposed considerable trust in Mr McKeown.

The DRL "accounting trick"

28. In 2013 an arrangement was entered into for another new company, Devine Restaurants Limited ("**DRL**") to purchase the Sophisticats business. The arrangements (frankly referred to by Mr McKeown as "an accounting trick") were designed to produce a tax advantage relying on the fact that HMRC had contended that the Sophisticats business was being operated not through the various companies involved in the group but through a partnership between Mr McKeown and Mr Langer. This created an opportunity, seized by Mr McKeown's accountant, Mr Chris Adams, to obtain a tax advantage by selling the goodwill of the trading business to DRL. In broad terms the effect of this was to create a positive shareholders' loan account with DRL for Mr McKeown and Mr Langer, which then could be repaid out of emerging profits without generating any income tax for them to pay. This meant that for some months or years they could each receive payments out of the business free of tax. The transaction was backdated to 2011. The backdating of transactions was a feature of how the business was run under Mr McKeown's stewardship.

29. Notable aspects of this transaction are that: (1) it placed a value on the goodwill of the business at that time of £3 million (supported by a desktop valuation by a professional firm called Edward Symmons); (2) it created a means for money to come to the owners of the business otherwise than through dividends, and as a result they got used to being paid out of a shareholders' loan account; (3) it demonstrated a looseness of approach to corporate matters whereby labels were put on transactions to suit the convenience of Mr McKeown (and in this case Mr Langer) and were applied in a backdated manner; and (4) it resulted in the main ownership vehicle for the Sophisticats business becoming DRL, rather than Futureproof.

30. Mr McKeown gave evidence that he considered this arrangement to be an "accountancy trick" and cast doubt over the goodwill valuation underlying this transaction, at one point describing this as "fantasy figures", although he later recanted slightly, thinking that the valuation might just be sustainable if one made a brave assumption about the likelihood of the lease for the Marylebone Club not being terminated early by the landlord.

31. I consider that this transaction does not present a reliable guide as to the value of goodwill even at its date (and there are reasons why the value of the goodwill might be different later on), but I do think that it demonstrates that it was regarded by all parties that the business was capable of sustaining a substantial goodwill valuation.

32. It may be noted that this arrangement on its face disadvantaged Mrs Langer, as a 25% holder of shares in Futureproof. However, Mrs Langer, it seems, was content with the arrangements In all likelihood she was content because her husband effectively benefited from what would have been her share and she was at that time happy not to insist on any distinction between her share and his share. Her lack of objection to the scheme again demonstrates the trust that she was putting in her husband and in Mr McKeown to undertake transactions in her interests.

33. This was the point at which the Futureproof Shareholders' Agreement ceased to have legal effect as the three shareholders swapped their interests in Futureproof for shares in DRL (in the same proportions as before). Mr and Mrs Langer, therefore lost the protections provided in the Shareholders' Agreement. However, it may be worthy of

note that the DRL articles of association did include certain protections for shareholders including pre-emption rights on new issues of shares and on the transfer of shares.

The acquisition of the Soho Club

34. By 2016 the shareholders were becoming concerned that the landlord of the premises for the Marylebone Club was likely at some point to seek to terminate the lease in order to redevelop the property. In order to sustain the Sophisticats business they looked for alternative premises that they could operate from. They fixed upon the Soho Club. This was acquired in 2018 in return for goodwill payment of £620,000. A lengthy and expensive re-fit of the club was undertaken (estimated to cost in excess of £800,000) in order to convert the premises to be suitable for a lap dancing format and to conform with the Sophisticats style.

35. The early trading experienced at the Soho Club proved disappointing. The business was constrained by the fact that the club had a licence which required it to close at 3 am. By contrast the Marylebone Club closed later, at 6 am, and it was the experience that the hours between 3 am and 6 am were some of the most profitable.

36. An attempt was made to extend the licensing hours, but this was unsuccessful. Indeed, to some extent it worsened the licensing position in that the licensing authority accepted an offer to reduce the maximum capacity of the club from 250 customers to 100 customers. This was considered unproblematic for a lap-dancing club but could cause problems if the club ever needed to be converted back to its previous trading format.

37. During the period from its reopening as a Sophisticats club until the point when Mr McKeown bought the Soho Club in 2018 it was trading unprofitably.

The "retirement scheme"

38. As noted above, following the "DRL accounting trick" the parties had got used to taking money out of the business and not by means of a properly declared (and duly taxed) dividend but instead by taking payments (and perhaps, to some extent, by allowing a group company to make personal payments on their behalf) that would be debited to a shareholder's loan account. At some point Mr McKeown's and Mr Langer's accounts became negative and it became apparent that, unless something was done about this, this would result in a large tax bill payable.

39. The company's accountant Mr Chris Adams came up with a scheme that was presented to Mr and Mrs Langer to solve this problem. This involved the three shareholders in DRL selling their shareholdings in DRL to Stratos, which was incorporated as a new company. Stratos would issue shares to Mr McKeown in return for his shares in DRL. He would then become the sole owner of Stratos, and therefore of the group. In return for their shares in DRL, Stratos would pay cash to Mr and Mrs Langer on a deferred payment basis. It was put to Mr and Mrs Langer that this would benefit them by avoiding the tax charge, as they would have repaid their shareholder loans (presumably because Stratos would take this over on an inter-company account) and they would get the consideration for their shares as a capital gain and with the benefit of entrepreneurs' relief.

40. In order to undertake this scheme Mr and Mrs Langer were asked to sign share transfer forms transferring their shares. They did this at the end of March 2017, I am satisfied, without obtaining any proper understanding of the arrangements, beyond that they were designed to save tax as had happened with the previous DRL "accounting trick".

41. In June, some weeks after they had signed their shares away, they had a meeting with Mr Adams who explained the arrangements to them. Essentially the arrangements meant that they would cease to have any shareholding and would receive £2.5 million for their shares (based on a value for the business of £5 million), but this would be received only out of future profits or cash flow generated by the business, as to which there was little or no security. There was a hint that something might be done for them, or at least for Mr Langer, by bringing him back into the business by the back door, but this was not certain.

42. Mr Langer was keen to carry on with this arrangement but Mrs Langer did not accept it.

43. I can understand the concerns she would have had with the scheme – other than perhaps in relation to some deferral or reduction in tax, she would have been losing all of the upside relating to her shareholding, but would still be taking a full risk in the business, since if it failed, she would not receive her consideration.

44. In passing, I note that we have not seen the instructions given to Mr Adams in devising the scheme, and it is by no means clear to me that, if the purpose of the scheme was to deal only with the tax problem, that it required both Mr Langer and Mrs Langer to part with all of their shares (notwithstanding a suggestion in Mr McKeown's first witness statement regarding difficulties caused relating to tax that Mr Langer needed to pay because he had withdrawn his pension early). I am left with a suspicion (but with no more than that) that Mr McKeown saw this as a further opportunity to take control fully of the business, having concluded that Mrs Langer was no longer providing any benefit to the business. If Mrs Langer had accepted this deal, it is quite possible that Mr McKeown might anyway have gone ahead in the future with his purchase of the Soho Club and of the assets of the Marylebone Club and of the tradename and Mrs McKeown would not have seen the bulk of the payments due to her under these arrangements, if indeed she saw anything at all.

45. A notable feature of the retirement scheme for the purposes of this case, is that again it shows that the parties thought that it was possible to put a substantial price (£5 million) on the goodwill of the overall Sophisticats business. In this case Mr McKeown was firm that this was "fantasy figure". I accept that the figure that was used for these purposes was more likely to be chosen as being the highest figure that might be defensible if challenged by HMRC, rather than the parties' genuine assessment of the value. Nevertheless. it does show that the parties once again considered that a value could be recognised. To the extent that Mr McKeown thought that this was a "fantasy figure", but nevertheless was one he was happy to report in tax returns and use for the purposes of calculating a share premium account, it may be considered to cast doubt on the good faith of his approach to accounting.

46. A further notable feature is that once again Mr and Mrs Langer placed trust in the arrangements that were put in front of them and signed the share transfer forms without taking independent legal advice or accountancy advice. They trusted Mr McKeown to

have been acting in their interests. Only as they started to think about what this meant did they (or at least Mrs Langer) lose faith in this. It might be added that Mr Langer also showed considerable trust that Mr McKeown would, notwithstanding the sale, treat him fairly by bringing him back into the business in some way.

Unwinding the "retirement scheme"

47. Once she understood the effect of the retirement scheme, Mrs Langer was unhappy with it and persuaded her husband also not to accept it. To his credit, Mr McKeown agreed that it should be unwound.

48. It was considered not to be tax effective to simply reverse the arrangements, since stamp duty had already been paid on the share transfer and would be due to be paid again on the transfer back. Instead, it was simply arranged for Mr and Mrs Langer to acquire shares in Stratos, restoring them back to the 25/25/50 shareholding arrangements they had in DRL. This was undertaken in August 2017, although it was said to be backdated to 28 March 2017.

49. Again, this arrangement shows the trust that was placed in Mr McKeown as no separate legal advice was taken. In fact, swapping their shareholdings in DRL for shareholdings in Stratos operated to their disadvantage as minority shareholders since the articles of association of Stratos did not include minority shareholder protections such as a pre-emption right on share transfers. Mr McKeown, as the sole director of Stratos, had very full powers. He could block a sale of a minority shareholding but the minority shareholders had no pre-emption rights or blocking rights if he wished to sell his shares.

50. Again, this shows a pattern of backdating transactions.

The Management Charges

51. In July 2017, an arrangement was made for Mr Langer and Mr McKeown to clear off substantial balances on their shareholder loan accounts by means of issuing substantial fee notes totalling £475,000 each for management services that they were said to have provided to DRL. This device again seems to have been made at the suggestion of Mr Chris Adams in order to clear off a looming tax charge that might otherwise have been applied to the shareholder loan accounts. Mr Langer, in his third witness statement expressed surprise about this, having had no recollection of issuing these fee notes or of registering for VAT to do so and in cross-examination had to be taken to contemporary emails between him and the accountancy firm where the firm asked for his consent to register him for VAT. It emerged when he was re-examined on this point that the invoices and his VAT registration both predated the email providing his consent. I accept his evidence that he paid little attention to this matter and was content to rely on the accountants, as instructed by Mr McKeown, to do what was ever best in order to minimise tax.

52. There is no evidence that these invoices reflected a genuine assessment of the value of services provided. By all accounts they were entered into purely in order to justify payments already made on shareholders' loan account to Mr McKeown and Mr Langer and to avoid, or at least defer, tax.

53. Mrs Langer does not make any complaint about these arrangements, and I think it is natural that she would have accepted them (insofar as she was aware of them) while she and her husband were still together as long as the loan accounts that these invoices cleared off had been advanced equally between Mr McKeown on the one hand and her husband on the other hand.

54. In my view the noteworthy conclusions arising out of this incident are: (1) it provides an example of how transactions were concluded, or perhaps it might even be said fabricated, in the interests of Mr McKeown and those he was looking to benefit (in this case Mr Langer) rather than the Company; (2) it provides a further example of Mr Langer (and I think, therefore, at this stage at least, Mrs Langer) reposing considerable trust in the arrangements that Mr McKeown was instructing the accountants to put together; and (3) it demonstrates that the parties looked beyond the normal proper channels for distributing profits via dividend and saw such devices as rendering management fees as a possible and acceptable way of justifying money that they were taking out of the business.

The Simon Langer share sale

55. By early 2018 Mr and Mrs Langer were having serious difficulties in their marriage. This was not greatly explored in the evidence, but it appears that one major source of dissatisfaction between them was that Mrs Langer considered that Mr Langer was not standing up to Mr McKeown. By the end of February 2018 Mr Langer had moved out of the marital home.

56. The separation was not an amicable one.

57. Mr McKeown at this time provided emotional support to Mr Langer, just as, by all accounts, he had done on the occasion of Mr Langer's divorce from his first wife. Mr McKeown also initially kept on good terms with Mrs Langer and exchanged friendly text messages with her.

58. It appears that Mr and Mrs Langer have more recently reconciled.

59. Mr Langer described his state of desperation at this time as he was facing not only the loss of his marriage but severe financial difficulties owing to tax demands. Against this background Mr McKeown suggested to him an arrangement for him to sell his shares to him, at a valuation to be determined. Again, this arrangement shows the trust that Mr Langer placed in Mr McKeown as on 27 March 2018, he signed a short agreement to this effect without taking any separate legal advice. At this point he expected to receive a substantial sum for his shares.

60. In fact, a value was obtained by a valuation firm called Walton Dodge which valued his holding at £25,000. This took account of the fact that the Soho Club had, by the time this report was produced on 29 August 2018, the Soho Club had been sold, although it does not reflect the full terms of the sale as Mr McKeown later describes them - there is no mention of the settling of outstanding current debts.

61. Mr Langer was clearly extremely disappointed, if not shellshocked, to receive this valuation but he accepted it and completed the transfer of his shares on 5 September 2018. Before he signed this transfer he did receive legal advice, organised by Mr

McKeown's solicitors, Brook Martin & Co., but given by a lawyer that was not part of that firm.

62. Mr Langer now considers that he has been unfairly dealt with and is considering legal proceedings in his own right against Mr McKeown.

Soho Sale

63. It is common ground between the parties that, on or around 29 June 2018, Mr McKeown arranged for the business and assets of the Soho Club to his own Company, John McKeown Clubs Limited ("**JMCL**"). This company was formed on 26 February 2018. It acquired its first subsidiary by acquiring from DRL the shares in Devine Restaurants (Marylebone) Limited ("**DRML**") on 20 April 2018 for £500. DRML was later renamed as "Brewer Street Restaurants Limited" and used as the operating company for the club. No evidence was adduced that this arrangement was properly approved at a board meeting, but this transaction does not itself form part of Mrs Langer's complaint.

64. Although in his witness statement Mr McKeown says that the idea for acquiring the Soho Club only came to him in June 2018 when he was discussing this with Mr Chris Adams, I find it highly likely that this was in serious contemplation earlier than that date. If it was, that gives rise to concerns about the probity of Mr McKeown's dealings both with Mr Langer, since this issue was clearly pertinent to the share sale that had been agreed with him, and with Mrs Langer as it renders statements that Mr McKeown allowed his solicitors to make on his behalf to Mrs Langer's solicitors at that time at best misleading.

65. In the pleadings it was accepted that the price paid was the sum of £10,000. After sales costs, it seems, however, that the Company did not benefit much from this since Brook Martin (who were acting for both the seller and the purchaser) submitted an invoice for £10,000 which appears to have been chiefly to cover its work for this. This seems a large fee for the work done on the lease transfer (which was limited to arranging for the transfer of the lease and obtaining landlord's consent) given the value put on the lease, particularly when it is clear that they did not assist with negotiations and did not provide any commercial advice regarding the transfer of other aspects of the club business. It is possible that this fee may have covered also some other work as it was stated to cover "*shareholdings and transfers of shares and general property advice*", although Mr McKeown could not recall any other property advice that it referred to. It is not clear what advantage DRL as opposed to Mr McKeown obtained from advice on "shareholdings". I take the reference to "*advice on transfers of shares*" to have applied to the transfer of shares in DRML for £500. This was another matter for which JCML also equally benefitted and would have been a small matter as it involved only the drafting of a share transfer form.

66. It emerged in evidence that that the £10,000 may not have been full consideration provided. Mr McKeown gave evidence that the terms of the sale were that JMCL assumed liability for all current liabilities of the Soho Club business (excluding historic VAT liabilities), which he assessed at the board meeting held in July 2019 to ratify these arrangements as being around £100,000 but in his later evidence to the Court assessed at a higher figure of £170,000 to £180,000. In passing, I note that this further consideration was not reported to the Land Registry, and presumably, therefore, not

reported for the purposes of Stamp Duty Land Tax. It may be presumed, therefore that Mr McKeown regarded this payment as not being for the lease but instead of attaching to whatever furniture and fittings were not attached to the property, the inventory of stock, the use of the trading name and trading style and/or other goodwill items.

67. In fact, it is very difficult to work out what the terms were of the sale, and indeed whether there was a sale of the business at all at this stage.

68. The only sale documentation that was entered into at the time related to the transfer of the lease. We saw in evidence only an unsigned copy of this. It was a fairly standard lease transfer agreement. It or something like it must have been executed as JMCL was registered as the proprietor of the premises on 22 August 2018. This document did not provide for JMCL to take over the trading debts of the business: it included the normal apportionments clause on a lease transfer. We also saw some unsigned and undated minutes of DRL and of JMCL that Mr McKeown did not recall. These minutes approved a transfer of the lease to JMCL for £10,000 and the transfer of the trade of the club operated from that address, together with the fixtures and fittings contained therein to Brewer Street Restaurants Limited, for no additional payment.

69. At the time of this transfer staff were completely unaware of the transfer. There was no TUPE transfer of staff which would have been required by law if staff were transferring from DRL to Brewer Street Restaurants Limited. Instead it was explained that staff, although they were paid out of the DRL bank account, were employees of another Stratos group company, which had previously been providing their services by way of secondment to DRL. These staff, it is said, from this date started providing the services by way of secondment to JMCL or its operating subsidiary. This company (or DRL) continued to pay the payroll but would be indemnified for the cost of this by JMCL. I have seen no contemporaneous evidence to substantiate this position. What written evidence of employment arrangements that I have seen all treats DRL as the employer, so I find this explanation puzzling.

70. Neither was there any change to the banking arrangements – proceeds from the ongoing business continued to be paid into a DRL bank account and expenses of the business continued to be debited from a DRL bank account. Mr McKeown says that this was a mere administrative convenience while JMCL or its subsidiary got its own banking arrangements in order. This seemed odd since the evidence was that JMCL had purchased the shares in DRML, which became Brewer Street Restaurants Limited, precisely because that company had a functioning bank account.

71. I make these observations not because I wish to rule that the business transfer did not take place. Both parties plead that it did, and even if it did not take place on this date, it has clearly taken place by now. However, it is necessary to consider what was the deal under which the Soho Club business was transferred in order to determine whether this transfer was properly undertaken and to assess what an independent third party might have paid in order to obtain a similar arrangement.

72. I will return to this issue when I deal with the questions of the propriety of the transfer and of valuation.

The Euston Purchase

73. It had become apparent at least since 2017 that the lease of the Marylebone Club was going to come to an end and that to carry on the profitable business that was being conducted there, new premises would need to be found. Mr Langer and Mr McKeown made various attempts to find new premises.

74. At some point it became clear that a lap-dancing club near Euston station that was being operated by the rival lap dancing group "Secrets" might become available. In fact, both Simon Langer and Mr McKeown had been in contact with the owners of Secrets for some time. Simon Langer gave evidence that he had had a long relationship with Mr Stephen Less of Secrets and he and Mr McKeown had been approached earlier in 2014 about the possibility of some form of joint venture between Secrets and Sophisticats. These discussions were renewed in October 2018 at a meeting between Stephen Less, John McKeown and Mr Langer. At this point it appears that discussions moved on to discussions between Stephen Less's partner, Ben de Haan and Mr McKeown.

75. I accept Mr Langer's evidence that these discussions were in train in the latter part of 2018.

76. The discussions between Mr McKeown and Mr de Haan resulted in the purchase by Mr McKeown of the share capital of Secrets (Camden) Limited, the company that owned the Euston Club premises and from 6 February 2019 he took control of Secrets (Euston) Limited which was the company operating the business. However, the purchase was not completed until sometime later in October 2019 and it was only at that stage that the larger part of the £800,000 purchase price needed to be provided. In the meantime, it appears that Mr McKeown had control of the Euston Club business to the extent that he felt able to run a directors' loan account with it and to make payments from it settling his accounts with DRL.

The Marylebone Sale

77. At some point during February 2019 Mr McKeown decided that the Marylebone Club would transfer its portable assets, its name and its staff to Secrets (Euston) Limited for no payment. He considers, however, that consideration was provided in that the arrangement included a TUPE transfer of staff to Secrets (Euston) Limited, thus reducing the redundancy liabilities of DRL (or of whichever group member may have been employing the staff).

78. Again, there appears to have been no documentation for this agreement and the only evidence for the intended terms of this appears much later in board and shareholder minutes in July 2019.

79. In this case, however, it is clear that the sale did happen. Staff were notified of the transfer of their employment. Arrangements were made to advertise to customers and referrers of business that the Marylebone Club would be moving to Euston. Staff were instructed to redirect taxis from the Marylebone Club to the Euston Club. The move was advertised on social media and on the website.

80. The lease for the premises of the Marylebone Club terminated on 9 February 2019 and the Club closed during the early hours of 10 February 2019. From 11 February 2019 all business was referred to the Euston Club.

III. PROCEDURAL HISTORY AND EVIDENCE

81. Before looking at these steps in detail and the legal issues arising, it is useful to recite some of the procedural history and to say something about the evidence.

82. The Petitioner presented her petition on 2 April 2019, not long after the last of the events recounted above. Subsequently amendments were agreed to her Petition, or were ordered by the Court, most recently at the Pre-Trial Review (over which I presided), with the Respondent being given, and taking, an opportunity to re-amend his Points of Defence.

83. This, and other features emerging out of evidence, caused the parties, and in particular the Respondent, to seek to admit a great deal of evidence extremely late into the process. Some of this I accepted in the interests of fairness and some of this I did not accept in the interests of proportionality, and because the nature of the evidence would not have given a fair chance for the other side to respond.

84. Following a case management conference in December 2019 before Deputy Insolvency and Companies Court Judge Barnett, an order was made for a split trial. Paragraph 2 of that Order provides that the issues for this trial are:

    (a) whether the Respondent has engaged in unfairly prejudicial conduct;

    (b) If so, the appropriate form of relief; and

    (c) If the relief ordered is that the Respondent shall purchase the Petitioner's shares in Stratos at a price to be determined, the appropriate basis and mechanism for the valuation of Petitioner's shares.

85. The trial has involved a large amount of written evidence and over the nine days of the trial a great deal of witness evidence.

86. The financial information, despite the best, and skilled efforts of both counsel and the accountancy experts engaged, is difficult to grasp. This to my mind is largely because of the unsatisfactory way in which Mr McKeown kept accounting records, a point I will return to below.

87. The Petitioner complains, with good cause, that a great deal of financial evidence was disclosed late and with inadequate explanation. In particular, at one stage very shortly before the valuation experts were due to make their reports, a spreadsheet (the "**Adjusted Balance Sheet**") was served, which the Respondent relied on in the proceedings as being an accurate balance sheet and which he considered rendered the balance sheets previously provided as being, in the Respondent's own description, "rubbish". The lateness, and lack of explanation of the significance of this spreadsheet, was unfair to the Petitioner. However, the Petitioner's legal team and accountancy expert did exceptionally well in dealing with these problems.

88. Of the live witness evidence three of the witnesses were relevant only to a particular part of the Petition and I will deal with their evidence when I consider those issues, as I will in relation to the various expert witnesses that were called. Witnesses who were not expert witnesses and whose evidence was pertinent to all or many of the issues included the Petitioner herself, Mr Langer, Mr McKeown and Carmen Alonso, the senior manager within the Sophisticats business.

89. In the case of the first three of these, I need to be mindful that, by their own admission, they have been ready to participate in arrangements that may have presented a misleading impression to a court or another authority, for example there was more than a hint that they had cooperated in trying to minimise Mr Langer's disclosable assets at the time of his divorce from his first wife; Mr McKeown and Mr Langer put forward valuations in a tax context that it appears they had little real belief in; and it seems that Mr Langer and Mr McKeown discussed how they could improve Mr Langer's position in his divorce settlement with Mrs Langer by taking his shares in the Company out of his ownership.

90. Nevertheless, I was generally able to accept that each of these witnesses was trying to deal with the court truthfully, albeit that they may have seen events from their own particular viewpoint.

91. Mr McKeown was overall quite impressive as a witness. He was not easily flustered and took his time in answering carefully. In places he had a good recollection of detailed facts. He was prepared to say things which he would have seen as unhelpful to his case. There were, however, elements of his evidence, such as when he was describing the efforts he made to market the Soho Club, which were not presented with the same degree of clarity and which I am more cautious in accepting.

92. Carmen Alonso gave her evidence remotely and dealt well with the inevitable difficulties that this involves. I found her to be a very good witness. She would, of course, have been mindful that she was giving evidence about her boss in front of her boss, but nevertheless I am satisfied that she tried to answer the questions put to her honestly and truthfully.

IV. LEGAL PRINCIPLES

Section 994

93. Mrs Langer's Petition is for relief under section 994 of the Companies Act 2006. This provides:

(1) A member of a company may apply to the court by petition for an order under this Part on the ground—

(a) that the company's affairs are being or have been conducted in a manner that is unfairly prejudicial to the interests of members generally or of some part of its members (including at least himself), or

(b) that an actual or proposed act or omission of the company (including an act or omission on its behalf) is or would be so prejudicial.

94. As a member of Stratos, Mrs Langer is entitled to apply for relief if she can show that that company's affairs are being conducted in a manner that is unfairly prejudicial to her interests or that an actual or proposed act or omission of that company would be prejudicial.

95. It is important to note that the act must be an act of the company (rather than any act, for example, undertaken by Mr McKeown in his own right and not through his acting as a shareholder or director of the company). However, it is established law that for these purposes the affairs of the company may include the affairs of its subsidiaries, where the affairs of the subsidiary are being conducted in a manner which damages the subsidiary and hence the value of the holding company's interest in the subsidiary. Ms Lintner referred me to *Gross v Rackind* [2005] 1 WLR 3505 and *Re Grandactual Ltd* [2006] BCC 73 and I am satisfied that these provide ample authority for this point, if any were needed.

Identifying unfairness

96. Of course, the central idea within the section is that the Court must find something that amounts to "unfairness".

97. In everyday life, there are many standards that may be applied in judging unfairness and this is a term which the Court should be careful not to constrain, but at the same time not to interpret too widely. As Arden LJ (as she then was) put it in *Re Tobian Properties* [2013] 2 BCLC 567:

> *"The courts must act on a principled basis even though the concept is to be approached flexibly. They cannot decide whether to grant or refuse relief from unfair prejudice on the basis of palm-tree justice".*

98. The starting point for any discussion of this term in relation to its application in section 994 is the decision in *Re A Company, O'Neill & Anr v Phillips & Ors* [1999] 1 WLR 1092. Both counsel quoted in their skeleton arguments at length the words of Lord Hoffman at 1098-1102:

> *"Although fairness is a notion which can be applied to all kinds of activities its content will depend upon the context in which it is being used. Conduct which is perfectly fair between competing businessmen may not be fair between members of a family. In some sports it may require, at best, observance of the rules, in others ("it's not cricket") it may be unfair in some circumstances to take advantage of them. All is said to be fair in love and war. So the context and background are very important."*
>
> *In the case of section 459 [the predecessor in the Companies Act 1986 to s.994], the background has the following two features. First, a company is an association of persons for an economic purpose, usually entered into with legal advice and some degree of formality. The terms of the association are contained in the articles of association and sometimes in collateral agreements between the shareholders. Thus the manner in which the affairs*

> *of the company may be conducted is closely regulated by rules to which the shareholders have agreed. Secondly, company law has developed seamlessly from the law of partnership, which was treated by equity, like the Roman societas, as a contract of good faith. One of the traditional roles of equity, as a separate jurisdiction, was to restrain the exercise of strict legal rights in certain relationships in which it considered that this would be contrary to good faith. These principles have, with appropriate modification, been carries over into company law.*
>
> *The first of these two features leads to the conclusion that a member of a company will not ordinarily be entitled to complain of unfairness unless there has been some breach of the terms on which he agreed that the affairs of the company should be conducted. But the second leads to the conclusion that there will be cases in which equitable considerations make it unfair for those conducting the affairs of the company to rely upon their strict legal powers. Thus unfairness may consist in a breach of the rules or in using the rules in a manner which equity would regard as contrary to good faith."*

99. Put more shortly, the meaning of unfairness will depend on: (i) the terms on which the shareholders have agreed to do business; and (ii) the context, including the nature of the relationship between the parties.

100. My duty then is to consider both what are the terms that the shareholders have agreed should apply to the affairs of the Company and whether there are any equitable considerations which make it unfair for those conducting the affairs of the company to rely upon their strict legal powers.

101. As regards the rules regarding the terms on which the shareholders have agreed that the affairs of the Company should be conducted, these include the articles of association and any collateral agreements and understandings between the shareholders. As was confirmed in *Re Tobian Properties Ltd*, they also include the applicable rights and duties conferred or imposed by statute.

102. I have been invited by Ms Lintner to accept that these terms include the Shareholders' Agreement referred to above, even though this applied to a different company and there is no evidence of the parties referring to it, or acting in accordance with it, at any point. Whilst I do not think that she contends that individual provisions in that agreement would be justiciable (for example the failure to follow the terms set out in this agreement as regards the company obtaining "key man" insurance on each of the shareholders), I am invited to find that there are some fundamental terms that the parties all accept should be binding on them in equity if not law.

103. This is not a contention that I can accept put in that way.

104. What I do accept, however, is that the fact that Mr and Mrs Langer originally agreed sensible arm's length provisions which would have protected their position as shareholders, but then through successive steps allowed these provisions not to be observed and then not to be reimposed when the vehicle for the businesses changed,

provides strong evidence that they both reposed trust in Mr McKeown. He accepted that trust, and in many ways for a long time it appears that he tried (at least within his own view of what was fair in the circumstances) to operate within the perimeter of that trust. As a result of having trusted Mr McKeown and her husband, Mrs Langer has found herself in the position of a minority shareholder, denuded of the minority protections that she had originally argued for, and bound into an unequal relationship under which she could not sell her shares without Mr McKeown's agreement. As sole director, he wielded a veto right on share transfers whilst he had a full legal power to pass any ordinary or special resolution that he chose, and to conclude whatever bargains he should choose with the Company or its subsidiaries.

105. These circumstances all lead me to the view that the circumstances are such as to engage the second limb of Lord Hoffmann's formulation so that, as well as considering legal rights and duties, I should consider whether a particular act undertaken by the company breaches notions of good faith.

106. In discussing these concepts, one often comes across the notion of "quasi-partnership" as being mentioned as something which gives rise to the notion of good faith, but the application of this notion is not confined to those cases, even if the jurisprudence concerning the application of a duty of good faith can be traced back to the decision in *Re. Westbourne Galleries Ltd* [1973] AC 360, which was a "quasi-partnership" case. In the different context of a shareholder's right to obtain a winding up on the grounds that it is "just and equitable", Lord Wilberforce said:

> *"The foundation of it all lies in the words 'just and equitable' and, if there is any respect in which some of the cases may be open to criticism, it is that the courts may sometimes have been too timorous in giving them full force. The words are a recognition of the fact that a limited company is more than a mere legal entity, with a personality in law of its own: that there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals, with rights, expectations and obligations inter se which are not necessarily submerged in the company structure. That structure is defined by the Companies Act and by the articles of association by which shareholders agree to be bound. In most companies and in most contexts, this definition is sufficient and exhaustive, equally so whether the company is large or small. The 'just and equitable' provision does not, as the respondents suggest, entitle one party to disregard the obligation he assumes by entering a company, nor the court to dispense him from it. It does, as equity always does, enable the court to subject the exercise of legal rights to equitable considerations; considerations, that is, of a personal character arising between one individual and another, which may make it unjust, or inequitable, to insist on legal rights, or to exercise them in a particular way."*

107. In this case it is clear that there are considerations of a *"personal character arising between one individual and another"*. These considerations include the remarkably close personal friendship between the two families, the tone and nature of their frequent correspondence with one another, examples of which the Court has seen; the fact that

Mr and Mrs Langer, at least until rifts occurred between them, had a continuing involvement in promoting the success of the business that went beyond the mere status of being a shareholder; and the extraordinary amount of trust that the Langers invested in Mr McKeown. It is also apparent from the way that the corporate structure kept changing, whilst the overall percentage interests of the three owners remained the same, and was expected to remain the same, that the relationship of the parties overarched the specific corporate structure that applied at any one time.

108. Lord Wilberforce went on to say that:

> *"It would be impossible, and wholly undesirable, to define the circumstances in which these considerations may arise. Certainly the fact that a company is a small one, or a private company, is not enough. There are very many of these where the association is a purely commercial one, of which it can safely be said that the basis of association is adequately and exhaustively laid down in the articles. The superimposition of equitable considerations requires something more, which typically may include one, or probably more, of the following elements: (i) an association formed or continued on the basis of a personal relationship, involving mutual confidence–this element will often be found where a pre-existing partnership has been converted into a limited company; (ii) an agreement, or understanding, that all, or some (for there may be 'sleeping' members), of the shareholders shall participate in the conduct of the business; (iii) restriction upon the transfer of the members' interest in the company—so that if confidence is lost, or one member is removed from management, he cannot take out his stake and go elsewhere."*

109. Many of the elements identified by Lord Wilberforce may be considered to apply in this case.

110. The association was formed and continued on the basis of a personal relationship. It is arguable whether there was a "pre-existing partnership" as regards Mrs Langer's participation. HMRC thought that there was one originally between Mr Langer and Mr McKeown, and we understand that Mr Langer is arguing in the draft Particulars of Claim which was presented in evidence in court in relation to his own proposed action against Mr McKeown that one still exists. But, whether or not that is the case, it seems to me that the fact that there was a pre-existing relationship through the mutual shareholdings in Futureproof (which were on an arm's length shareholder, quasi-partnership basis) and that these shareholder agreement arrangements were not repeated as the corporate structure evolved, takes us within or very close to Lord Wilberforce's first consideration here.

111. The agreement or understanding of participation in the business also appears to have been something of a feature here. Whilst neither Mr Langer nor Mrs Langer had formal management roles within the business by the time Stratos was the holding company, Mr McKeown's own evidence was that he did consult Mr and Mrs Langer about various things and that he valued Mr Langer's participation, if not that of Mrs Langer. In my view, Mrs Langer was accepted as a 25% shareholder not solely as a result of her own

contribution during the early days of establishing the Marylebone Club (and any later contributions attributable to her of loan capital), but also because this was the wish of Mr Langer, whom Mr McKeown did regard as his business partner. In the circumstances I think it is reasonable and fair to impress her shareholding with the rights and expectations that Mr Langer might reasonably have had.

112. Finally, in relation to Lord Wilberforce's third consideration, I note that Mrs Langer was not entitled, without restriction, to sell her shares. As a director Mr McKeown would have been able under the terms of the articles of association of Stratos to block any sale.

113. In considering, therefore, the various issues that are before the Court, I will generally take the view that the Court is not restricted to examining the strict legal rights of the parties in considering whether McKeown has acted unfairly, but is also entitled to take into account equitable considerations of a personal nature.

Identifying prejudice

114. Ms Lintner has reminded me that the courts take a wide view of what constitutes "prejudice" suffered by a shareholder - it is a question of fact. However, in *Re. Tobian Properties Ltd*, Arden LJ observed that "*non-compliance by the respondent shareholders with their duties will generally indicate that unfair prejudice has occurred*."

115. Generally, the cases concerning unfair prejudice have found prejudice in the form of damage to the financial position of a shareholder, including reduction in the value of her shares. However, it may also be relevant sometimes to take a wider view.

116. The courts in particular are ready to find unfairness where a respondent puts himself in a position of a conflict of duties or interests and then prefers his own interests. As Fancourt J put it in *Re Edwardian Group Ltd* [2018] EWHC 1715 (Ch):

> *"A breach of duty by which the respondent wrongly puts himself in a position where his duty to the shareholders of the company conflicts with his own interests and then prefers his own interests "by their very nature cause[d] all of the shareholders prejudice ... That kind of conflict is corrosive of good administration and trust between shareholders and directors."*

117. With these general considerations in mind, I turn to the specific instances of unfair prejudice pleaded by the Petitioner.

V. FINANCIAL MISMANAGEMENT

118. It is convenient to look first at the allegations of financial mismanagement as these have an effect on a number of the other matters raised.

General comments

119. There are a number of specific allegations which I will deal with later, but first it is worthwhile commenting on the overall way in which these companies were being managed.

120. I have already referred to various incidents where financial matters that were important to the companies involved were only determined with the benefit of hindsight and it is apparent that this was part of a pattern of an approach to accounting under which Mr McKeown paid little regard to which company or individual might be the proper owner of any funds available or the proper person responsible for making the payment.

121. It seems that his practice was to make payments from whichever pocket had money in it and then only later to decide where the cost should be allocated. Payment of his and others' personal expenses were made out of company accounts. Payments of amounts due from DRL were made on his personal credit cards. After the Soho Club had been sold its bank accounts were put at the disposal of the company that had bought it. Payments of amounts due to DRL were made out of one or other of the companies running the Euston Club (even, it seems, before he had acquired full ownership of it).

122. As a result, it is only with the greatest difficulty that the correct treatment of payments can be discerned. For example, in the latter part of the trial a great deal of time was spent trying to establish whether Mr McKeown had taken for his own benefit a payment of £340,000 made by the landlord at the Marylebone Club by way of a payment on termination of the lease there. This payment was due to Mondrealm Limited, a subsidiary of DRL but was received by Mr McKeown into his personal bank account. He explained this on the grounds that Mondrealm Limited did not have a bank account and he did not want this money to be placed in DRL's bank account as he had concerns for the solvency of DRL. Mr McKeown produced evidence late in relation to this matter in the form of a spreadsheet. This showed how he, or one of the companies running the Euston Club, had defrayed various costs, which he said were attributable to DRL. However, even with the benefit of his explanations these financial arrangements were not readily understood.

123. I am reluctant to find any motive of dishonesty in these arrangements. I believe that Mr McKeown did always intend to settle accounts between himself and the various companies. However, it is clear that this cavalier approach to accounting and to stewardship of DRL's cash fell far short of the duties he had as a director to keep proper books of account. The financial position of the companies at any point could only be determined with the benefit of expert forensic accountancy and with the full cooperation of Mr McKeown both in explaining entries on ledgers and in reconciling these between the various corporate bank accounts involved and his personal bank and credit card accounts.

124. Having regard to this overarching point, I will return to the specific allegations of financial mismanagement.

Excessive Salary

125. The Petitioner complains that the Respondent has caused the Company or its subsidiaries to pay Mr McKeown an excessive salary. It appears that for some time, probably since mid-2017, Mr McKeown was drawing or considered himself to be accruing a salary at the rate of £350,000 per annum, although this may have been at a

lower rate in some periods. No evidence was adduced as to whether this salary had ever been properly approved by the board of DRL or any other company.

126. A director is required to consider the interests of the shareholders as a whole when setting his own remuneration. A failure to do so will amount to a breach of duty even in the absence of bad faith, as was found to be the case by Mr Hollington QC sitting as a Deputy Judge of the High Court in the case of *Re Blue Index Ltd* [2014] EWHC 2680. I am not satisfied that Mr McKeown took any meaningful steps to determine whether his level of salary was fair or affordable by DRL.

127. I accept the Petitioner's case that the Petitioner became aware of this salary only on 8 July 2020 following disclosure made in the course of this litigation, and that this was contrary to indications that Mr McKeown had previously given via his solicitors and in his Re-Amended Points of Defence.

128. The Petitioner makes a further point that the payment of a salary at this rate was contrary to an understanding between him and Mr and Mrs Langer reached in 2015 or 2016, which was that he should receive a salary of £50,000 "*in order to cover his expenses*". Despite any such earlier understanding, I do not think that it was unreasonable that Mr McKeown should be drawing a salary that was commensurate with the responsibilities he was undertaking.

129. There appear to have been a number of different elements to his role.

130. It is clear from the evidence of Carmen Alonso and Mr McKeown's own evidence that he acted as a chief executive of the business, taking all major strategic decisions and taking onto himself the management of such matters as the legal proceedings and planning applications made on behalf of the businesses. It appears also that he performed a role of closely scrutinising the financial performance, running over the takings for each evening and signing off on payments. He was also often physically present in the evenings at one or other of the clubs. He was not alone in running the clubs and had a very able lieutenant in Carmen Alonso and a larger team of managers but clearly his services had value to the business.

131. Both parties were given an opportunity (albeit only a brief one, since this issue emerged as one for expert evidence only at the Pre-Trial Review) to adduce expert evidence as to whether £350,000 a year was a reasonable level of salary for the role that Mr McKeown was undertaking.

132. The Petitioner's expert on this point was her forensic accountant, Mr Burns. Mr Burns considered carefully the role that Mr McKeown was undertaking reviewing all of the witness evidence that was available at the point of his report in doing this. He did not adduce any external information about comparable salaries (no doubt for the same reasons that the Respondent's expert, Mr Hodgen, mentions in his report on this point), but considered that it was reasonable to set Mr McKeown's salary by applying a 50% uplift to the wages of the other most senior business manager, Carmen Alonso.

133. Mr Hodgen, the Respondent's accountancy expert reported on this issue also. He considered that the sector in which the Sophisticats businesses operate is not large enough to provide satisfactory comparative data and noted that he was unable to find any recruitment or remuneration consultant professionals that could provide expert

opinions. Mr Hodgen criticised Mr Burns' approach, considering that this did not properly reflect the difference in responsibilities between Carmen Alonso and Mr McKeown. This opinion appeared to be based largely on Mr McKeown's witness evidence. He was not really able to suggest a satisfactory alternative approach to valuing these services but concluded that £350,000 was a reasonable figure, taking comfort from a comparison with the wages of Mr Simon Warr, who fulfilled a similar role within the Platinum Lace lap dancing group, and who was reported to receive a similar level of remuneration. This did not strike me as being a helpful comparison since the Platinum Lace group included six clubs. In addition, I understand that the group is owned by Mr Warr, so it is impossible to say whether his level of salary also contains a degree of profit extraction. The same is true in relation to Mr Less's salary from Secrets, which Mr McKeown mentioned as original point of comparison. That group had a larger number of clubs than Sophisticats and Mr Less also was an owner so that it would be difficult to say whether or not his salary contains a degree of profit extraction.

134. Having considered the evidence given by both experts, I think the approach taken by Mr Burns seems to be a reasonable one and I accept it in preference to Mr Hodgen's opinion. I find therefore that, to the extent that at any point Mr McKeown did take a salary that was in excess of £202,500 per annum, that level of salary was excessive.

135. I also consider that it was not reasonable for DRL (or whichever other company within the group was paying Mr McKeown, which seems to be uncertain) to continue to bear all of this salary once Mr McKeown had arranged for the Soho Club to be sold to his company and was dividing his time between the Marylebone Club and the Soho Club. It should be assumed that during this period, from the sale of the Soho Club until the closure of the Marylebone Club, the amount of Mr McKeown's salary attributable to his work for DRL should be reduced to one half of this figure. From the closure of the Marylebone Club, it would not have been reasonable for Mr McKeown to continue to accrue any substantial salary.

Improper payments of salary to friends and family

136. The Petitioner complains that the Respondent has caused the Company or its subsidiaries to pay an unjustified or excessive salary to various of his family and friends and that this was incompatible with his duties to the Company. These complaints need to be considered individually.

Paul Longland

137. We heard evidence that Mr Longland was a long-standing business associate of Mr McKeown. He had undertaken work for DRL for some time but retired in 2015, and was paid an ex gratia payment on the occasion of his retirement. The Petitioner complains that he continued to be paid after this date.

138. Mr McKeown's evidence on this point was that following his retirement (and relocation to Spain), Mr Longland continued to provide services to DRL as a non-executive director of DRL and that he was paid for this service at the rate of somewhere between £12,000, and £14,000. Clearly, he was a director and this is a responsible role that can justify a stipend. He does not however appear to have been a particularly active director and this level of remuneration may well have been overgenerous. I do not think,

however, that the case has been made that this was set at an excessive level and so I will not find that this was improper, but I will leave it to a valuer as to whether this is something that should be adjusted when assessing the Fair Maintainable Operating Profit of the business.

Maya Hawie

139. According to the analysis undertaken by the Petitioner's forensic accountancy expert Mr Burns (which I have no reason to doubt), Maya Hawie was paid £11,498 (including the cost of employers' National Insurance) in the year ended 5 April 2017 and £24,086 in the period ending 31 July 2018.

140. Ms Hawie provided a witness statement and appeared in person to be cross-examined on this. It was apparent from her evidence that she did undertake a certain amount of part-time work for DRL, but that the payments she had received for this were in excess of the value of those services, and instead were justified by services that she was providing for a separate music company (or partnership - there was some conflicting evidence on this) in which Mr McKeown had an ownership interest, SYPM Music Limited. She was proud of the work she was doing for that company, which clearly was at a higher level than the low-level administrative work that she was undertaking for DRL.

141. She estimated that, whilst the proportions would have varied from time to time, overall 70% of the money she was paid by DRL was in respect of work done for SYPM. I am content to accept her estimate of this apportionment and I find that 70% of her salary costs should be regarded as excessive for DRL.

Diana Zeidina

142. Diana Zeidina is Mr McKeown's live-in girlfriend. Mr McKeown met her when she was a dancer one of the Sophisticats clubs. Between April 2016 and August 2018 she was put on the DRL payroll and according to Mr McKeown's evidence earned a total of some £36,623.35. The Petitioner claims that she did not work for DRL, or that, if she did, she was over-remunerated for the services provided.

143. She provided a witness statement and was cross-examined on this in court. Whilst I have no doubt that she did do some work for DRL, her duties seem to have been exceptionally light. She explained them as answering the telephone at their joint home, sometimes responding to emails that Mr McKeown had received and helping organise Mr McKeown's diary. Her most time-consuming job appears to have been on a Friday when she would retype (or cut-and-paste) payroll information so as to create a bulk payment instruction for DRL's bank to pay salaries. This appears to have involved something like 20 – 25 entries. She says that she worked a minimum of 20 hours a week, but I find this difficult to believe from the description of what she did, the lack of awareness that other employees within the firm had of what she was doing, and the fact that no emails or correspondence seemed to have been generated in her name. She did not appear to have a good understanding of how the payroll arrangements worked and I think it is fair to regard the work that she was doing as unskilled work. I understand that she was paid something like £300 per week from 2015 rising to £21,991 per year in 2017. This level of payment seems excessive for the work involved and I cannot but conclude that in making these arrangements Mr McKeown was motivated

in benefiting his girlfriend (to whom by all accounts he had been a very generous boyfriend). A more reasonable level of payment might be of the order of £20 per hour for 5 hours a week and I think that anything above this should be regarded as excessive.

144. Mr Burns has also identified that between August 2018 and February 2019, the sum of £2,231.70 per month was paid from DRL's account for a property that was occupied by Diana Zeidina (and, it is understood, Mr McKeown). This is not disputed but the Respondent considers that this was justified on the basis that it had been agreed with Mr Langer. Mr Langer denies this. I do not think that Mr Langer's consent or otherwise affects the fact that making such payment was a breach of Mr McKeown's duties to DRL and to Stratos. This payment also should be regarded as an instance of excessive remuneration.

Katherine Then-Berg

145. Katherine Then-Berg is Mr McKeown's daughter. According to Mr Burn's analysis, she was paid £39,092 (including the cost of employers' National Insurance) in the year ended 5 April 2017 and £51,103 in the period ending 31 July 2018.

146. She was not called as a witness but confirmed in her witness statement that she had not worked for DRL but received these payments because they were due to her husband for the work that he was undertaking for DRL and were instead paid to her because her husband was suffering from addiction problems and this was a way of protecting him. Mr McKeown confirmed this in his evidence. When asked why he had had to put his daughter on the payroll, rather than just paying over some of her husband's salary to her, he added a further justification that this was more tax efficient (presumably because it would have allowed the payments to be taxed at a lower tax rate). Mr McKeown's own case then suggests an intention to mislead HMRC.

147. It has been put to me in Ms Lintner's closing argument that if the monies paid to Mrs Then-Berg are added to those paid to her husband this comes to a salary payment (including employer's National Insurance) in excess of £80,000 a year, which does seem excessive for the role that he played, which we understand to be a relatively junior administration role.

148. Mr McKeown in his witness statement gave evidence that the total amounts paid to Mr and Mrs Then-Berg were not excessive and his witness statement contained figures showing a lower level of combined salary at around £60,000 per year (in this case not including employer's National Insurance). He compared them to the payments being made to Heidi Tonkin, who I assume is not related to, or a close friend of, Mr McKeown, who had responsibility for the general administration of the Clubs, and who Mr McKeown stated to be at the same level. From the description given of their respective roles I would have thought Heidi's position to be slightly senior. In fact, Mr McKeown's own figures tabled in his witness statement show that the total paid to Mr and Mrs Then-Berg were consistently higher than that shown to Heidi Tonkin by a varying amount.

149. Whilst I can accept that her husband was genuinely employed and that there were reasons why his pay should be routed via her, this merely transfers the issue to the question whether Mr McKeown was acting in the interests of the Company when setting the remuneration for the services that her husband was providing to the Company at the

level that they were set. Given the apparently excessive total remuneration, and the unorthodox and unjustified way of accounting for part of the payment, I think that I should find that the payments made to Mr McKeown's daughter should not be regarded as having been properly justified in the interests of the Company to the extent in any year they were, taken with her husband's remuneration, higher than those paid to Heidi Tonkin unless the difference can be shown to have been justified by the hours worked.

Joe McKeown

150. Joe McKeown is Mr McKeown's son. He is married to Michaela McKeown, having met her working at the Soho Club. He had had experience working in the Marylebone Club since January 2012. On returning from university in December 2016 he took on a full-time position as Assistant Manager at the Soho Club. It seems that he was well paid for a 24-year-old, as he was, when he started in that position. By 2017 he was earning in excess of £66,000.

151. The Petitioner complains that between August 2018 and 2019 somewhere between £1,800 and £1,900 per month was paid from DRL's account for a property in Ealing occupied by Joe McKeown and his wife. It is accepted that these payments were made, and Mr McKeown and Joe McKeown explain these as being a top up to Joe McKeown's salary, pointing out that a similar top up to salary was given to Mr Langer's son who was also working in the business as a manager.

152. This explanation is difficult to accept, given that from July 2018 Joe McKeown was working exclusively for the Soho Club which no longer belonged to DRL and his wife ceased working sometime in or before August 2018, taking maternity leave from which she did not return. I do not accept the argument that these payments were backdated remuneration for work previously undertaken and so I find that these payments should not have been made by DRL.

Riley McKeown

153. Riley McKeown is Mr McKeown's daughter. The Petitioner complains that she received payments and did not work or provide services to the Company or its subsidiaries. The sums in this case seem to be relatively small – a little over £2,000 per year. Mr McKeown in his witness statement stated that he thought it to be appropriate for her to receive a small salary as she works at a "low-level", generally working from home but sometimes at the Soho Club mainly with "copying and data entry".

154. We have seen nothing to corroborate Mr McKeown's witness statement as to the work done, nor any explanation why the copying and data entry undertaken could not have been undertaken by the other administrators working in the club. Given the conclusions I have reached in relation to the other cases mentioned above, I consider it more likely than not that these payments were not justified, or justified in whole, and that they were motivated more by the affection that Mr McKeown has for his daughter than any consideration of the business needs of the Company. I think that these payments should be regarded as improper.

155. It is impossible for the Court to be sure about the extent of the work undertaken or the proper level of payment for it, but overall, I think that there is enough evidence to find that there has been a pattern of Mr McKeown setting up arrangements for DRL to pay

amounts to members of his family and his girlfriend that are in excess of those justified by looking at the business needs of the Company.

Improper payments of personal expenses

156. A further complaint made in Mrs Langer's Petition was that there were a number of payments that Stratos or DRL have been invoiced which relate to expenses that were not for the benefit of the Company or its subsidiaries, but were rather for the personal benefit of Mr McKeown.

157. These included a number of travel expenses that had been recorded as business expenses in the accounts of DRL. On 23 October 2020, after exchange of the expert evidence, Mr McKeown produced for the first time a document presented as a statement of his director's loan account for the period 1 May 2018 to 28 February 2019 in which these travel expenses were recorded as personal expenses and debited to his loan account.

158. Mr McKeown has explained that it was his normal way of operating to charge personal expenses such as this to the business, but then after the end of the financial year to analyse such expenditure and, where he judged that it was personal in nature, to regard this as a director's loan made to him. As discussed above, I consider that this way of operating does not meet the requirements expected of a director to keep proper books of account.

159. Other payments complained of by the Petitioner include invoices from Brook Martin and from Mr Tager relating to these proceedings or the discussions leading to them. In this case the Respondent argues that the fees involved were a proper expense for DRL.

160. In general, I do not consider that this argument is well founded. Whilst Stratos is a respondent to this action, for technical reasons, the essence of the current dispute is between Mrs Langer and Mr McKeown and this was true also of much of the earlier correspondence which related to the possibility that Mr McKeown would buy Mrs Langer's shares. Generally, the improper use of a company's resources on disputes between shareholders constitutes misfeasance on the part of the company's directors and is capable in itself of constituting unfairly prejudicial conduct (see *Re Hydrosan Limited* [1991] BCLC 418 Ch D).

161. The Company has no interest in who are its shareholders and Stratos's money, and still less that of DRL, a subsidiary of Stratos, should not be used in relation to disputes between them.

162. However, there was one element of the dispute at that time which was properly a dispute between the Company (or DRL) and Mrs Langer. This is the dispute as to whether Mrs Langer owed money on a shareholder loan account. That issue was one that the proper creditor for that money (probably DRL, as that is the owner of the bank account where these payments came from) could seek advice on.

163. In giving his evidence Mr McKeown accepted that he benefited from the advice that these invoices related to, although he insisted that the Company benefited from them also. He was unable to suggest in what proportions these benefits might fairly be attributed.

164. I think it is appropriate to apportion the invoices between the loan account issue and the remainder of the issues and matters in play. It would be disproportionate to undertake a forensic exercise on this point and I think it would be proportionate for me to rule on this on the basis of the evidence that I have seen so far. I find that it is appropriate that DRL bears 25% of these expenses and that the remainder should be considered an expense on behalf of Mr McKeown and should have been borne by him.

165. Further examples of payments made to the benefit of Mr McKeown have been identified by Mr Burns, the Petitioner's forensic accountant. They relate to transfers from DRL's Marylebone Club bank accounts to accounts used for the Soho Club in the net amount of approximately £245,000 that were paid after the date on which the Soho Club business was transferred to JMCL. The debt owed by Brewer Street Restaurants Limited to DRL was not recorded in any of the accounting documents disclosed by the Respondents prior to exchange of the expert reports. I was not able to reach any conclusion in the time that the Court had to consider these matters as to whether the explanations provided for these payments were justified or not. In view of the order that I propose to make, I do not think it is necessary that I get to the bottom of this question.

VI. THE SOHO TRANSACTION

166. The main facts concerning the Soho Transaction have been set out above.

Breaches of duty

167. The first question to ask about this transaction is whether it involved any breach of duty on behalf of Mr McKeown. For these purposes we need to consider both the duties Mr McKeown had as a director under company law and the requirements of the articles of association of the companies involved, DRL and Stratos.

168. The duties of a director have been developed by the common law and are now codified within Chapter 2 of Part 10 of the Companies Act 2006. They reflect the fact that a director is a fiduciary – he is in effect an agent and a trustee for the company and therefore owes strict duties. They include duties:

(a) to act within the company's constitution (section 171 (a));

(b) to exercise his powers for the purposes for which they were conferred (section 171 (b));

(c) to act in a way considered by him, in good faith, to be most likely to promote the success of the Company for the benefit of its members as a whole (section 172);

(d) to exercise reasonable care, skill and diligence in the performance of his functions as a director of the Company (section 174);

(e) to declare interests to the board of directors in relation to transactions or arrangements with the company in which he is interested (section 177); and

(f) (except in relation to transactions or arrangements he has with the company), to avoid conflicts of interest unless the matter has been duly authorised (section 175).

169. The duty to act *bona fide* in the interests of the company was considered (before its codification in the Companies Act 2006) in the Court of Appeal's decision in *Bishopsgate Investment Management Ltd (In Liquidation) v Maxwell (No.1)* [1994] 1 All E.R. 261. Here the point was made that:

> *"If a director chooses to participate in the management of the company and exercises powers on its behalf, he owes a duty to act bona fide in the interest of the company. He must exercise a power solely for the purpose for which it was conferred. To exercise the power for another purpose is a breach of his fiduciary duty."*

170. In this case Mr McKeown says that he was undertaking the Soho Transaction in the interests of DRL, and therefore in the interests of Stratos. He says that his motivation was to stem the losses that DRL was experiencing within the Soho Club.

171. When pressed on why then he thought he was acting in the interests of his other company, JMCL, he confessed that he did have other motivations. He was keen to take a more complete control of the running of the Club. He said, "*We had three sons, they needed jobs*". I understand that this may have been a reference to Joe McKeown, James Langer and Toby Cura. Also, having provided a personal guarantee for the lease he was keen to take control of the lease, perhaps fearing that other indebtedness within DRL might threaten the ability of DRL to fulfil its obligations on the lease, thus exposing him personally.

172. It may be seen, therefore, that on his own admission he did have a mixture of motives in causing the transaction take place. This at the very least calls into question whether there was a breach of his duty to use his powers as a director for the purposes for which they were given.

173. Putting this point aside, it is fair to ask whether a reasonable director in his position would have reached the conclusion that this sale was in the interests of DRL and of Stratos. That question is highly influenced by the question whether the sale was at a proper value considering the nature of what was sold and what was known about the business at that time. The interests of the Company were not limited to stemming the losses (even assuming that the only way that they could be stemmed was by the sale of the Soho Club, a point that is hotly disputed by the Petitioner). These interests extended to obtaining the best price reasonably achievable on that sale.

174. A director that was acting bona fide in the interests of the company would be expected to take steps to test out the market and to obtain a professional valuation in order to ensure that he was doing the right thing. Failure to do these things may be considered to lead to a breach of the requirement to exercise reasonable care, skill and diligence, as well as casting doubt on the good faith of the transaction proposed.

175. In this case, the balance of evidence is that Mr McKeown did not take such steps. Mr McKeown's assessment of the value of the assets of the Soho Club was, according to

his own evidence, based on a discussion that he had with Chris Adams. It was known that the lease of the premises was an important element of this value, but it appears that no expert valuation was obtained before the sale and I do not think that there was any meaningful attempt to test the market.

176. There is no written evidence that any instructions were given to any sale agents. Mr McKeown explains this by his desire to keep the fact that the Club was for sale secret as this might unsettle staff and the dancers. He says that he did speak to two agents and in doing this satisfied himself that there was no market for the Soho Club. However, there is no contemporaneous evidence on this, and this was one of the few areas where his oral evidence was less than detailed. It is notable, given the importance of this point, that he did not obtain witness statements from the agents that he spoke to. It may well be that he did have some sort of a conversation with agents, but I strongly doubt whether this was of a type that amounted to a serious test of the market, which would have required a proper briefing of an agent and obtaining advice in writing. In particular we have no idea whether the agent might have responded differently if it had known that offers above £10,000 would be considered and that the Sophisticats name might be licensed to sweeten the deal. I consider, therefore, that it is more likely than not that Mr McKeown was in breach of his duty to exercise reasonable care, skill and diligence.

177. Certainly, I consider that Mr McKeown was in breach of his duty to exercise reasonable care skill and diligence in the way that the Soho Transaction was put into place. There was no proper documentation of the agreed transaction. A single firm of lawyers was used to represent both sides so that there was no one ensuring that DRL's interests were being considered. If, as Mr McKeown contends, an important term of the transaction was the indemnification by JMCL of current trade and employee creditors and an ongoing indemnification for staff costs, no care was taken to secure this payment, even by reducing it to an enforceable agreement in writing. It appears that no consideration was given to whether JMCL, a recently formed company with no material share capital, was a good credit risk in relation to these matters.

178. In the absence of a proper valuation, and in the absence of evidence of proper instruction to marketing agents, the Court should be suspicious of the motivations of a sole director undertaking this action. The secrecy with which the transaction was carried out (so that even staff concerned did not know about this even after it had happened) and the fact that it is questionable whether even the other director of DRL knew about it before it had happened add to the suspicion.

179. There are two separate sets of provisions that apply to regulate director's duties when it comes to conflicts of interest.

180. First, in relation to transactions or arrangements with the company where he is interested in the transaction or arrangement, he is under a duty to declare this interest of the board of directors under section 177 and, in order to meet his obligations to act in accordance with the company's constitution, will need to follow the procedures in the company's articles of association. These duties were engaged when JMCL purchased the assets, goodwill and business of the Soho Club from DRL.

181. Secondly, in relation to conflicts of interest other than in relation to such transactions there is a duty under section 175 to avoid conflicts of interest unless the matter has been

duly authorised. This duty was engaged through his establishing through JMCL a competing business with DRL's retained business at the Marylebone Club.

182. Once under separate ownership, the Soho Club and the Marylebone Club were (whether Mr McKeown recognised it or not) in competition with one another for customers, for introducers of business, for staff and for dancers and Mr McKeown had placed himself in a position where he had an ongoing conflict of interest between these two businesses. He was in a position to divert opportunities from one club to the other on a daily basis and no independent sanction had been given (until much later – as discussed further below) for the existence of this continuing conflict of interests. Whether or not he took advantage of this position, he should not have placed himself in such a position without the appropriate sanction.

Required approvals

183. The transactional conflict of interest that arose from the purchase is governed by section 177 of the Companies Act 2006; article 14 of DRL's articles of association and article 14 of Stratos's articles of association.

184. Section 177 of the Companies Act 2006 provides that conflicts of interest arising from transactions or arrangements with the company must be declared to the other directors before the company enters into the transaction or arrangement. There is no evidence that such a declaration was made.

Articles of Association

185. As the sale was from DRL and needed to be approved by the DRL board, the first thing to consider is the articles of association of that company. These provide the following in relation to conflicts of interest:

> *"A Director who is in any way either directly or indirectly interested (whether through persons connected with him as defined in section 346 of the [Companies Act 1985, as amended] or otherwise) in any contract, transaction or arrangement (whether or not constituting a contract and whether actual or proposed) with the Company or in which the Company is interested, shall declare the nature of his interest at a Meeting of the Directors in accordance with section 317 of the* [Companies Act 1985, as amended]. *Subject to such disclosure a Director shall be entitled to vote in respect of any such contract, transaction or arrangement (whether actual or proposed) in which he is interested and he shall be counted in reckoning whether a quorum is present."*

186. There is no evidence of any meeting of the directors of DRL being called to approve this transaction. Indeed, it is unclear whether the other director (Mr Paul Longland) of DRL was aware of this transaction at the time. Mr McKeown's evidence was that he did tell Mr Longland about this at some point and that he was "*told rather than asked*".

187. As this transaction was so important to Stratos it should also have been considered at the level of the Stratos board.

188. The Stratos articles of association go further than the statutory duties applicable to transactional conflicts of interest by placing more onerous requirements on directors. Article 14(9) requires not only that a director's conflict of interest arising from a transaction or arrangement with the company be declared, but that, when all the directors of the company are conflicted (as is the case here), the company shall pass the conflict to the company's shareholders for approval by ordinary resolution:

> *"(1) If a proposed decision of the directors is concerned with an actual or proposed transaction or arrangement with the Company in which a director is interested, that director is not to be counted as participating in the decision-making process for quorum or voting purposes."*
>
> *(2) But if paragraph (3) applies, a director who is interested in an actual or proposed transaction or arrangement with the Company is to be counted as participating in the decision-making process for quorum and voting purposes.*
>
> *(3) This paragraph applies when:*
>
> *(a) The Company by ordinary resolution disapplies the provision of the articles which would otherwise prevent a director from being counted as participating in the decision-making process;*
>
> *(b) The director's interest cannot reasonably be regarded as likely to give rise to a conflict of interest; or*
>
> *(c) The director's conflict of interest arises from a permitted case.*
>
> *(4) For the purposes of this article, the following are permitted causes:*
>
> *(a) A guarantee given, or to be given, by or to a director in respect of an obligation incurred by or on behalf of the Company or any of its subsidiaries;*
>
> *(b) Subscription, or an agreement to subscribe, for shares or other securities of the Company or any of its subsidiaries, or to underwrite, sub-underwrite, or guarantee subscription for any such shares or securities; and*
>
> *(c) Arrangements pursuant to which benefits are made available to employees and directors or former employees and directors of the Company or any of its subsidiaries which do not provide special benefits for directors or former directors.*
>
> *(5) For the purposes of this article, references to proposed decisions and decision-making processes include any directors' meeting or part of a directors' meeting.*

> *(6) Subject to paragraph (7), if a question arises at a meeting of directors or of a committee of directors as to the right of a director to participate in the meeting (or part of the meeting) for voting or quorum purposes, the question may, before the conclusion of the meeting, be referred to the chairman whose ruling in relation to any director other than the chairman is to be final and conclusive.*
>
> *(7) If any question as to the right to participate in the meeting (or part of the meeting) should arise in respect of the chairman, the question is to be decided by a decision of the directors at that meeting, for which purpose the chairman is not to be counted as participating in the meeting (or that part of the meeting) for voting or quorum purposes.*
>
> *(8) Where the number of non-conflicted directors is less than the quorum for the purposes of approving a resolution authorising any situation or transaction constituting a conflict as anticipated by the Companies Acts, the quorum shall be all the disinterested directors.*
>
> *(9) When all the directors of the Company are conflicted, the Company shall pass the conflict to the Company's shareholders for approval by ordinary resolution."*

189. It was put on behalf of the Respondent in his Re-Amended Points of Defence that Article 14(9) was not engaged by the Soho and Marylebone Transactions, on the basis that those transactions were with DRL and did not directly or indirectly involve Stratos.

190. Ms Lintner has submitted that such an argument is inconsistent with the references to "*the Company or its subsidiaries*" in Article 14(3); there would be no requirement for certain transactions with Stratos's subsidiaries to be excepted from the requirement to pass conflicts to Stratos's shareholders unless the requirement generally applied to transactions with Stratos's subsidiaries. I accept this argument.

191. Accordingly, I find that the conflict of interests involved in this transaction was not properly notified in accordance with the articles of DRL and was not properly approved in accordance with the articles of Stratos.

192. Whilst these breaches are sufficient to show unfairness, they may not be sufficient to show real prejudice. Mr Tager drew my attention to various cases including the decision of David Richards J in *Re Coroin Limited* [2012] EWHC 2343 (Ch) where he said, "*where the act complained of have no adverse financial consequences, it may be more difficult to establish relevant prejudice*".

193. The Respondent's case is that this transaction was not detrimental to the shareholders of Stratos as it removed a loss-making business from them and as the price paid was fair in the circumstances.

Valuing the Soho Club

194. It is necessary then for the Court to form a view on the value of the transaction. Expert evidence was obtained on this point. Unfortunately, the experts differed markedly on the valuation.

195. The Petitioner's experts valued the Soho Club business or assets as at 29 June 2018 at £1.504 million. The Respondent's experts considered that it had no value.

196. Whilst a business can be valued either as a going concern or as the sum of its assets, it was common ground amongst the valuation experts that in this case it is appropriate to value what was transferred on an assets basis.

197. Looking at these assets, the most important of them was the lease and we heard expert valuation evidence in relation to this.

198. Both experts had similar conclusions regarding the factors applicable to the premises and the lease.

199. There were factors which a purchaser would find positive. These included the position of the premises in the heart of the pleasure district which is Soho; the fact that the premises enjoyed a rare Sexual Entertainment Venue Licence (although the Respondent's expert was doubtful whether this would add anything to the value); the recent fit out so that the quality of fixtures and fittings was good.

200. Both valuers also agreed that there were a number of factors which would render the lease less attractive to the target market. These included the shortness of the lease (which I will discuss further later); the fact that the SEVL licence required the club to close at 3 am, which was considered to have an effect in limiting the ability to generate profits; and the fact that another licence condition limited the number of customers at any one time to 100. This was not thought to be a practical limitation as regards the use as a lap dancing club, however unless this was reversed (or an alternative licence held by the landlord could be brought into play) it would limit the ability to make profits through a more conventional type of nightclub where it was necessary to have a larger density of clientele in order to generate both the right atmosphere and the right prospects for profit. A further fact was that both experts agreed that the property was over-rented, although they disagreed as to the extent of this.

201. Whilst the experts agreed that these were all factors to go into the valuation, they differed markedly on what weight should be attached to these factors.

202. The Respondent's valuer, Mr Watson considered that the short lease was a very significant factor. The lease was due to expire in 2021 and, although it enjoyed protection under the Landlord and Tenant Act 1954, from his knowledge of the area he considered it to be very likely that the landlord would resist an application under the Landlord and Tenant Act for a new lease on the grounds that he would wish to redevelop. He considered that there was a compounding effect between the shortness of the lease; the fact that the property was over rented and was only suitable within its licence conditions as a lap dancing club; and the fact that it was not generating profit. These factors combined together to make the lease completely unattractive to any purchaser within the likely market, and therefore the lease should be given a nil value.

203. The Petitioner's valuer, Mr Bunn acknowledged these factors, but differed on the extent of their importance. In particular he did not think that the property was as over-rented; he considered that the existing track record of profitability did not reflect what would be achievable by a reasonably efficient operator and that there were still prospects for growth in turnover given the relatively short history of trading as a lap-dancing club. As regards the length of the lease, he did not think it was credible that the landlord would be proceeding with the redevelopment in 2021. There was little prospect for a redevelopment of the whole building as there was at least one residential long lease granted within the premises. The only potential for redevelopment would have been to combine the club premises (which were largely at basement level, except for a small frontage for entry at ground level) with the ground floor property which was currently let as a retail outlet. A new lease had been recently granted to that property expiring in 2024, and so that seemed to be the earliest that any such plan could be implemented, even if such a plan would be attractive to the landlord, which he doubted.

204. Mr Bunn provided a very thorough valuation closely based on RICS valuation methodology. On this basis he came to a value as at the date of transfer (29 June 2018) of £800,000. This was arrived at as an approximate midpoint between two different methodologies which he employed following the RICS. The first method was based on an assessment of the Fair Maintainable Operating Profit, which he calculated at £434,000 and then applying a multiple of this to reach a capital value. In his view a normal multiple would be four times this level of profit, however allowing for certain issues affecting this lease, including the short length of the lease and licence restrictions he reduced that to a multiple down to two times profits, providing a valuation of £868,000. He also considered what evidence was publicly available of other transactions in the market and considered that the evidence from this led him to a value of £750,000. It was notable that many of the transactions involved substantial payments being made for businesses that were not currently profitable. Taking an approximate midpoint between these two approaches he arrived at a valuation of £800,000.

205. The approach of the Respondent's valuer Mr Watson was also thorough, although less overtly forensic and, I judged it to be very much influenced by the evidence that the Respondent had given about the realities of the business and his own view, based chiefly on the changing nature of the area, that a purchaser would assume that a redevelopment was imminent.

206. We have no reliable direct evidence as to the landlord's intentions on this latter point – I was invited to rely on a late-submitted copy of a text message on Mr McKeown's telephone about this, but I do not think it is appropriate I should give this any consideration as there was no opportunity for the Petitioner to look into the provenance of this message, or indeed to cross-examine the person who had sent it.

207. Mr Watson was working from slightly different figures to Mr Bunn as regards the current trading of the company. He was working from the figures in the Adjusted Balance Sheet whereas Mr Bunn was working off the management accounts that had previously been provided (and which covered a slightly different trading period). The chief difference between these figures related to the treatment of VAT, which is discussed in more detail below. As regards this point I think it is more reasonable to follow the approach that Mr Bunn followed.

208. The two experts also differed as to the approach to analysing costs. There was much discussion as to whether it was realistic to reduce labour costs to the extent that Mr Bunn had assumed. I am wary of accepting Mr Bunn's approach of extrapolating from an industry average where the definition of the industry was wider than that of this type of lap dancing club. I am satisfied that there was scope for an operator to reduce costs, probably substantially, but I doubt that it was a safe assumption that a purchaser would expect to reduce labour costs from 42.3% to 30% of turnover and at the same time maintain a quality experience and continue to grow revenue. Mr Bunn had allowed for the uncertainty that a buyer would have in having to depend on postulated rather than demonstrated profits by adopting a lower multiple for the postulated profits, but that does not answer the question of what level of costs a reasonably efficient operator would assume.

209. Certainly, there was scope to reduce costs. As we have seen, Mr McKeown had been generous in the approach to staff pay in relation to his own friends and family, and indeed to Mr Langer's family. It is also likely that a new operator might have thought he could reduce staffing levels - Mr Langer gave in his witness statement a credible explanation of how the club might have operated with reduced staffing. As a result, I consider that it would be reasonable to assume that labour costs might get closer to what Mr Bunn thought to be an industry average of 30% than that they would remain at the current level.

210. Mr Bunn had also projected for future increases in turnover. Mr Bunn assumed £3 million fair maintainable trade based on continuing the sales growth between 2017 and 2018. Mr Watson discounted this on the grounds of the restrictive licensing hours. My view is that Mr Bunn's approach was more realistic and was more likely to be the assumption a purchaser would take.

211. The experts also disagreed on the level of the market rent, with Mr Bunn putting this at £250,000 per annum and Mr Watson putting this at £195,000 per annum. The Court is not well placed to judge between these two opinions, but as generally I have favoured Mr Bunn's analysis as to turnover and potential profitability, it seems to me that these issues would translate also into the rental market, and therefore I will prefer his view on this point.

212. Given such diametrically opposed opinions in relation to the prospects for the premises, based on what appeared to be largely an agreed set of facts, it is difficult for the non-expert to choose between the two approaches. However, I am largely persuaded by the thorough analysis taken by the Petitioner's expert.

213. I think that he was right in thinking that a potential purchaser would see some prospect for profit, notwithstanding that the club was currently making losses. He (or she) would no doubt, seek to obtain a thorough understanding of the current profitability but he would base his assessment on his own forecasts of revenue and of costs, thinking about how he would staff the Club, and what he would pay his staff. He might take the view that was put forward by Mr Langer in his witness statement that the club could be run with a much lower level of staffing. He would, certainly, in considering the existing financial information adjust the current expenses to take out special factors such as the fact that various members of the family were being overpaid.

214. I think that he would also expect there to be further growth in turnover for what was still a new business (notwithstanding that there may have been some levelling off of turnover towards the end of this period). I think that he would have taken comfort from the Landlord and Tenant Act protection in relation to the length of the lease and would have assumed that he would have at least until 2024 to take a profit out of the transaction.

215. Furthermore, on the lease renewal he might have expected the element of over-renting on the premises to be reversed which would have improved margins and profitability. He might even have seen the prospect for combining the basement and ground floor flat as a positive, since it might be something that he could take advantage of – this had been something which the Respondent and Mr Langer had considered themselves as a possibility since it would be possible to have a conventional bar upstairs, which might be profitable in its own right, and could provide a more discreet form of entrance to the club premises which would be attractive to some customers.

216. I also do not think it can be assumed that a purchaser would entirely discount the possibility of obtaining an extension to the 3 am licence which was being seen as an important constraint on the profitability of the business. Mr McKeown and Mr Langer had been happy to take this risk not long before. Clearly the prospects had worsened given that the extension had been refused once, but this did not mean that there was no chance at all of this. Indeed, we heard that Mr McKeown after the change of control made a further application for an extension. If he had thought there was no possibility of this, he would not have wasted the significant professional fees involved.

217. It is beyond the expertise of this court to arrive at the judgement that such a purchaser would have made. All this court can do is to judge the reasonableness of the assumptions made by the two experts, and their approaches. As a result of the factors discussed above it is my assessment that the Respondent's valuer was being overly pessimistic. The features to which he made reference as justifying a nil valuation had been taken account of in the Petitioner's valuer's analysis. Whilst it may be possible to give some of these features, and in particular the length of the lease, greater weight, I was not at all persuaded that a nil valuation was appropriate. I therefore find that the lease did have a positive value at the time of transfer.

218. Acknowledging the points that the Respondent's valuer has made and his assessment of the importance of them, I am prepared to see that this might be less than the £800,000 assessed by the Petitioner's valuer and in particular I can see that a less heroic assumption about the ability to cut labour costs would affect the calculation. In view of the points I have recognised above about the potential to cut costs, I will not split the difference between the assumption made by the two experts but I find it reasonable to assume that a reasonably efficient operator would expect to cut costs to 33% rather than the 30% assumed by Mr Bunn. This assumption would reduce the operating profit margin Mr Bunn calculated by three percentage points from 25% to 22% and would reduce the Future Maintainable Operating Profit as calculated by Mr Bunn from around £434,000 to around £344,000 and I think that I should adopt this as a more realistic figure. If Mr Bunn's multiple were applied to this figure, then the value emerging from the profits multiple approach would be reduced to **£688,000**. Mr Bunn also offered as another point of comparison his judgement of the value based on what comparative transactions he could find, and on this basis assessed the value at **£750,000**. I take some comfort that this figure is of the same order of magnitude, but I think it is appropriate

to take the lower figure based on a profits multiple, given the scarcity there was of truly comparable market information and the different conclusions that Mr Watson reached on the comparable transactions. I therefore find that the value of the lease at this date was **£688,000**. This figure is far less than DRL had invested in this property, taking account of the £620,000 paid for the lease and the considerable amounts (understood to be in excess of £800,000) that have been spent on fitting out, but it must be accepted that this was not an appropriate way of looking at the value of the open market of the lease.

Brand Valuation

219. The second important element of the value of the business was the brand. Here again the Court was presented with two very different approaches to the valuation.

220. The Petitioner's valuer was Mr David Haigh, the CEO of Brand Finance. He was clearly an experienced expert valuer of brands and franchises and operated mainly in that part of the business world where these were important assets driving the business. It was his profession to recognise and consider the exploitation of brands and franchises.

221. He helpfully in his report explained the difference between different definitions of the concept of "brand". He focused on two definitions.

222. The first of these, which was generally accepted by both experts and was referred to in the proceedings as the concept of "brand" was: "*a name, term, sign, symbol or design, or a combination of them, intended to identify the goods or services of one seller or group of sellers and to differentiate them from those of competitors*".

223. He also focused on a broader definition where this concept of brand which included, in addition to those items a bundle of intellectual property rights and other intangible assets that would be included in a licence of the business system or a franchise. These items could include such matters as training, know-how and human capital support. This broader definition was generally referred to by both experts as a "franchise". In his view, which he had formed having regard to the witness statements of Mr McKeown and Ms Alonso this would include the relationships with dancers and taxi drivers; operating procedures, including management style; management know-how; the Sophisticats payment systems; memorable iconography; as well as trademarks and associated intellectual property.

224. He stated his opinion that any business, or at least any service business, could be franchised.

225. In his report, he applied these definitions to the Sophisticats business following a recognised valuation methodology used for brand valuation. Various methodologies were possible, but he considered that the most appropriate methodology was one called "royalty relief method". This measured the value of the brand as the value of expected royalty payments assuming that the brand is not owned but licensed. It required a royalty rate to be determined after an in-depth analysis of available data from licensing arrangements for comparable brands and an appropriate for brand earnings between licensor and licensee.

226. This royalty rate would then be applied to the estimated forecast revenues over the useful economic life of the brand giving a figure for "brand earnings". The value of this calculated future revenue stream would then be discounted to calculate a net present value.

227. Both experts agreed that the royalty relief method was an appropriate approach, if one assumes that there is something in the brand to value.

228. Mr Haigh calculated values for a putative new owner of the Soho Club might pay for a licence of the brand to use at that club and what a putative new owner of the Euston Club might pay for a licence to use the brand at that club.

229. The Respondent's expert in relation to brand valuation was Mr Hodgen, who is a forensic accountant, rather than a professional consultant on brands. He was modest about his brand expertise but clearly did have experience about valuing the goodwill of a business.

230. He agreed that, if a brand had any value the royalty relief method was an appropriate way of valuing it, but he considered that there was no value. He did not think it realistic that a third party would pay to get the use of the name and other business signifiers or that there was any prospect of a wider franchise. He considered that any likely buyer of the business would be an existing operator and would already have its own brand and its own business systems.

231. I think it was evident that Mr Hodgen, in forming his view on what were the drivers of success in this business, based his opinion quite substantially on what Mr McKeown had said. In particular, he was disposed to follow Mr McKeown's views that it was Mr McKeown's personal reputation that was important to the clubs and any intangible value relating to reputation and know-how was associated with him personally and not to any franchiseable system or to the brand.

232. As a result, Mr Hodgen considered that the most someone would pay for the brand was the cost of introducing and publicising a new name and logo to create a new brand. He considered the cost of this to be £5000, but it was apparent that this figure was arrived at after discounting what he considered to be the value of a boost to business brought about by the prospect of launching the new name. He would not be drawn on what he thought was the gross figure.

233. I did not find this convincing. I consider his assumption that the purchaser would need to be the owner of an existing operation and brand not to be justified. The brand and franchise aspects could be attractive to a senior manager working in another club who wanted to launch his own business and did not own the brand or business systems applicable at the other club. This indeed was the case in relation to Mr McKeown.

234. Mr Haigh's approach to valuing the brands was robustly contended during Mr Tager's cross-examination of him. This cross-examination revealed that Mr Haigh had not thought very deeply about what it was he was valuing – he settled on an assumption that it was a licence with an unlimited life at the Soho or Euston Club, on the basis that the clubs could move it to a successor club. This did not seem realistic to me. I think we should assume that a purchaser of the Soho Club who wanted to take it with the

brand would negotiate a price concomitant with the remaining expected life of the lease (which, as we have seen, was itself a matter of dispute).

235. Having heard the views of both experts I consider that there was value in the brand. The Sophisticats name had been established for some 20 years. It had been featured on television. It was well known within the business, garnering press coverage and ratings amongst online comparison sites. It had a website and social media presence. It had repeat customers. Perhaps more importantly it had a reputation with the dancers (who by all accounts were key to the offering) and with introducers of business, in particular taxi drivers and rickshaw drivers.

236. I was unimpressed by the argument that this business reputation attached solely to Mr McKeown, rather than to the business and its name and style. No doubt Mr McKeown's management had established the conditions to develop this reputation, but the day-to-day dealings of customers, and dancers and taxi drivers were with the management on the ground. A purchaser who acquired both the name and access to these staff would be getting the benefit of these reputational aspects. It was clear from the evidence from Carmen Alonso that Mr McKeown was not the only person in whom the business connection resided.

237. It is also pertinent that at this stage Mr McKeown remained a director and employee of DRL and as such was not free to exploit the business know-how and connection of DRL for a competing company, and therefore even to the extent that any of these elements of goodwill were associated with him, they were not his to use for the benefit of what would become a competitor with the retained Sophisticats business.

238. Within Mr Haigh's valuation I was offered a choice of valuing the "brand" alone and valuing the "franchise value".

239. To determine which was the more appropriate valuation, I have considered what actually was provided to JMCL, and therefore what should be assumed to have been on offer to another purchaser. This is difficult to reconstruct since there was no agreement in relation to this. But it appears, from the way that the Soho Club was operated that these terms included:

(1) a free loan of experienced and trained staff and of software and systems and accounting support subject only to paying their cost of salary - in an arm's-length deal DRL would have charged an uplift and the cost of employment;

(2) the use of Mr McKeown's services as general manager (releasing him from his duties not to compete, and making the know-how that he had gained through working for DRL available to the new owner);

(3) the contacts and connection and reputation of the club; and

(4) financial support through the use of a DRL bank account and the operation of an inter-company account which at times provided a source of liquidity.

240. These advantages strike me as being valuable and to be over and above what a purchaser would get merely by purchasing the lease.

241. Mr McKeown’s evidence was unsatisfactory on this point but it appears also that it was within his contemplation that the arrangements might also include a lucrative arrangement to obtain commissions through referring customers to the Marylebone Club, which also would have had a value if it had been a term of the arrangement.

242. In my view, if a deal had been done on arm’s length terms along the lines of the deal that JMCL in practice enjoyed, DRL could have expected, in addition to receiving the value of the lease, to receive a management fee for the ongoing services that DRL was providing to support the new business of the purchaser, including the provision of Mr McKeown's services himself. It is of course impossible for the Court to know what this would be, but it would be reasonable for example to consider that a commercial rate might be based on an uplift on the costs of employment of the staff involved for as long as this support was provided and that 50% of the cost of employing Mr McKeown would be charged under this arrangement, and would be subject also to this uplift.

243. If these arrangements had been made, I think it would have been correct not to look at any further element of "franchise" within the arrangements, although as discussed above, a brand payment should have been considered.

244. This approach was not put to me in argument since the full details about the Soho Club transaction emerged only late in the proceedings. I do not think that the Court should substitute its own approach for valuing the transaction for those put before it as expert evidence. However, what I find about the benefit that JCML was obtaining from this arrangement has a bearing on how I think that I should approach the question of whether the arrangements should be treated as a mere licence of a brand or as the provision of a “franchise”. Whilst these arrangements were not of the type one would find in a typical franchise, it seems to me that they offered very equivalent benefit. They provided in a different way many, if not all, of the components that Mr Haigh identified as being what might be expected in the licence of a franchise. Therefore I think that it is appropriate to look at the valuation on the franchise method as assessed by Mr Haigh.

245. In relation to value, Mr Haigh offered a number of assumptions, including those related to the length of the expected flow of royalties. He offered a choice of an unlimited economic life royalty, 10 years, 20 years, or to the end of the lease. I think that this needs to be looked at in relation to the realities on the ground. As discussed above, it seems that the likely assessment that a purchaser would make about the lease was that the Soho Club could continue to be operated until 2024 but that there was a serious risk of the landlord requiring the property back at this point. In these circumstances it is highly unlikely that a purchaser would pay upfront for an indefinite licence. Most likely he would recognise the value of the licence only up to that point.

246. Also, it is likely that the management support of the type I have described above would cease to have value once the new management has absorbed the lessons of how to run a successful Club.

247. I also have my doubts as to whether the valuation assumption of a compound average growth rate of 8.4%, given the evidence I saw about both the slowing growth rate in the Soho Club and the wider headwinds facing the lap dancing industry (albeit that they have been compensated by a reduction in competition as well-known clubs have closed).

248. Having regard to these factors, I think it is appropriate to start from the most cautious assumption as regards the economic life of the royalty that Mr Haigh offered, which assessed the franchise value of a licence for the Soho Club at £247,000, and then to discount this.

249. I take on board, however, the point offered by Mr Hodgen that many of the potential purchasers for this business would not have paid either to acquire the name and reputation or the wider intangibles relating to know-how and business connection since they would have been operating in the business and may have their own brand, know-how and business connection. If the only purchaser to have been found was of this nature, that purchaser might have been willing to pay nothing for these advantages. Strictly this observation may be at odds with the fundamental convention on valuations which assumes a willing buyer and a willing seller, but I think the Court is at liberty to depart from this convention, to a certain extent, when it is trying to work out what would have realistically happened in the circumstances under consideration.

250. On the other hand the purchaser could have been a new entrant to the market - perhaps an existing manager who had come out of another business and was debarred from using the name and know-how relating to that business.

251. Given this uncertainty, and given also the fact that the Soho Club had been trading unprofitably (even with all the advantages of the brand), I doubt whether a new operator would be prepared to pay the price that emerged from Mr Haigh's desktop calculations. I think it is appropriate not to take the full value of £247,000 which emerges from Mr Haigh's desktop calculations. I think it is appropriate to assume that had the sale been on arm's length terms it would have included a payment of **£125,000** to acquire a Sophisticats "franchise" comprising the use of the Sophisticats name and logo and the level of management support in transferring the business know-how and trade connection at the Soho Club to the new owner that was in fact afforded.

252. It will be apparent from the above that I consider that the Soho Club, along with the use of the brand, and all of the arrangements to provide JMCL with support from the ongoing Sophisticats business (including making Mr McKeown available by releasing him from his duties to Stratos and DRL to spend time managing the Soho Club) had a value that was in excess of the £10,000 that was paid, and indeed was in excess of any value that may have been in the wider terms of the deal if the deal indeed was that JMCL would take over the current liabilities attributable to the Club.

253. In my view the fair value is **£813,000** comprising:

(a) **£688,000** for the lease, including fixtures and fittings and inventory, as I accept the contention put forward by Mr Tager that these were covered within the lease valuation

(b) **£125,000** to cover the brand licence and management support provided.

254. In addition, as Brook Martin & Co were acting on both sides, I think it should be assumed that the Brook Martin legal fees of £10,000 (plus VAT) were shared equally between the two parties. Although the Brook Martin fee may have covered some other elements, to the extent that these other elements related to the transfer of shares in DRML, JCMCL was an equal beneficiary of this. To the extent that they related to

advice on "shareholdings", the suspicion must be that Mr McKeown rather than DRL was the true beneficiary of that advice.

255. This approach assumes that expenses of the Soho Club were dealt with in the normal manner (i.e. by apportionment) rather than being indemnified, so that DRL would have had to pay itself, without any indemnification any bills relating to its own period of trading. It assumes instead that JMCL did assume responsibility for all wages and expenses attributable to the Soho Club from 29 June 2018. This should have included responsibility for one half of Mr McKeown's salary and expenses; all bank charges attributable to the DRL bank account which was being used by the Soho Club; and any licensing or software fee applicable to any software or technology used by the Soho Club (or where this was jointly used by the Marylebone Club one half of such costs).

256. I have not allowed in this valuation any payment for any expectation of the stream of revenue deriving from commissions to be paid by the Marylebone Club for referring on the 3 am trade. I think that we should assume instead that a term of the licence was that the Soho Club would continue to refer customers to the Marylebone Club (or any other Sophisticats club owned by Stratos that had a later licence) for no payment.

VII. THE EUSTON TRANSACTION

Did the Euston Transaction breach Mr McKeown's director's duties?

I have already described the facts relating to the acquisition of the Euston Club.

257. These facts in my view create a case for Mr McKeown to answer that he has breached his director's duties under sections 175 (1) – (2) of the Companies Act 2006 to avoid conflicts of interest, in particular those arising from the exploitation of opportunity. Section 175 states the following:

> *"(1) A director of a company must avoid a situation in which he has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company."*
>
> *(2) This applies in particular to the exploitation of any property, information or opportunity (and it is immaterial whether the company could take advantage of the property, information or opportunity)*
>
> *(3) This duty does not apply to a conflict of interest arising in relation to a transaction or arrangement with the company.*
>
> *(4) This duty is not infringed—*
>
> *(a) if the situation cannot reasonably be regarded as likely to give rise to a conflict of interest; or*
>
> *(b) if the matter has been authorised by the directors.*
>
> *(5) Authorisation may be given by the directors—*

(a) where the company is a private company and nothing in the company's constitution invalidates such authorisation, by the matter being proposed to and authorised by the directors; or

(b) where the company is a public company and its constitution includes provision enabling the directors to authorise the matter, by the matter being proposed to and authorised by them in accordance with the constitution.

(6) The authorisation is effective only if—

(a) any requirement as to the quorum at the meeting at which the matter is considered is met without counting the director in question or any other interested director, and

(b) the matter was agreed to without their voting or would have been agreed to if their votes had not been counted.

(7) Any reference in this section to a conflict of interest includes a conflict of interest and duty and a conflict of duties."

258. The phrase "*possibly may conflict*" was held in the celebrated decision in *Boardman v Phipps* [1967] 2 AC 46 to mean "*the reasonable man looking at the relevant facts and circumstances of the particular case would think that there was a real sensible possibility of conflict*".

259. The duty to avoid this type of conflict can be waived by the directors or by the shareholders but this must be done through an approval given without the participation of the director whose duty is to be waived. As the sole director of Stratos, Mr McKeown could not waive this type of conflict of interest by approval of the directors since he was an interested director. Neither could he vote on a shareholder resolution that would have the effect of waiving the conflict.

260. Mr Tager has advanced two arguments for the Respondent as to why this duty was not breached in this case. He put these points far more elegantly than I do but broadly his contentions rest on two arguments. First, it is argued that this opportunity did not come to Mr McKeown in the course of his duties as director of Stratos or DRL, but rather it arose from his own personal connection. The second is that no harm has been done to Stratos or DRL since they could not themselves have availed themselves of this opportunity.

261. I consider that both arguments are flawed both on the facts and on the law.

Did the opportunity arise in the course of Mr McKeown's duties as a director?

262. Whilst Mr McKeown may have had a long association with Mr Stephen Less and/or with Mr de Haan of Secrets, I think it is clear that the opportunity relating to the Euston Club came to him because of his connection with Sophisticats. It was known in this small industry that Mr McKeown and Mr Langer worked together in relation to Sophisticats. I accept Mr Langer's evidence that the first approach of possible dealings between Secrets and Sophisticats was made via him. It is clear that these early

discussions involved the Sophisticats business. I do not think that it is credible to suggest that Mr McKeown came by this opportunity otherwise than as a result of his involvement in the Sophisticats business.

263. Even if I am wrong on this question of fact, there is authority that in determining whether an opportunity is one to which section 175 applies, it is not necessary to show that the company had some pre-existing interest in the opportunity in question. In *Re Bhullar Bros Ltd, Bhullar v Bhullar* [2003] BCC 711, the Court of Appeal held that:

> *"In a case such as the present, where a fiduciary has exploited a commercial opportunity for his own benefit, the relevant question, in my judgment, is not whether the party to whom the duty is owed (the company, in the instant case) had some kind of beneficial interest in the opportunity: in my judgment that would be too formalistic and restrictive an approach. Rather, the question is simply whether the fiduciary's exploitation of the opportunity is such as to attract the application of the rule".*

264. In the current case, the Sophisticats business carried on by Stratos and its subsidiaries was facing certain death after DRL had sold the Soho Club, unless some alternative premises could be found for it to operate from. Mr McKeown knew this and he exploited this opportunity for himself, without taking any meaningful steps to explore the ability of Stratos to take this opportunity. This seems to me to be precisely the type of circumstances where the fiduciary's exploitation of the opportunity should attract the application of this rule.

Could Stratos have exploited this opportunity?

265. In relation to the second argument, that the rule does not apply because Stratos could not have exploited this opportunity, I am equally unconvinced on both the facts and the law.

266. The contention that Stratos could not have exploited this opportunity rests essentially on two arguments. Again, Mr Tager has put these more eloquently than I can, but they boil down to this. The first is that Stratos and its subsidiaries did not have the liquid assets to meet its liabilities and to find the necessary investment to acquire the company which ran the Euston Club. The second is that DRL had, and was known to have, an enormous VAT liability which it was unable to meet and so was balance sheet insolvent at this point and so could not and should not have taken on the risks of acquiring a new club.

Would the Company have had the cash to do this?

267. In judging the first of these points, in the context of the current action, I am required to look at the financial situation of the companies involved not as it was, but as it would have been had there been no breach of duty or other act amounting to unfair prejudice against a shareholder.

268. As I have found that there were breaches of duty relating to the sale of the Soho Club, I need to reverse the effect of these breaches. There are two ways I could do this. I could assume that the sale never happened, or I could assume that the sale did happen,

but it happened at a fair price so that the sale was not contrary to the interests of the group.

269. In deciding which approach to take, it is fair that I should take the approach that most benefits the Company in all the circumstances. The effect of this sale being in breach of duty would have given the Company, had it acted against the errant director, a choice between obtaining damages or rescinding the contract. I think we should assume that the Company, had it had this choice in February 2019, would have chosen to take the money. I should assume therefore that the Company or DRL would have had the £813,000 purchase price I have calculated sitting in its bank account (although it would have had to have paid the outstanding bills for its costs of trading up to the date of that sale which were, I am told, indemnified by JMCL).

270. From my analysis above it may be seen that I have found that DRL was not being managed solely in the interests of the DRL but that payments were accruing to Mr McKeown's family and girlfriend that were not justified by the business needs of the company. For the purposes of assessing whether Stratos could afford to make this payment, it is fair to assume that these payments would not have been made and that the cash involved with them would be available to the Company. It will require more forensic work to establish what these amounts were, but between them I am satisfied that there was a substantial amount of money that has been paid out that was not in the interests of DRL, including through the overpayment of salary to Mr McKeown and other matters. Had these payments not been made, the cash spent on them also would have swelled the bank account of DRL.

271. As a result of the inadequate and labyrinthine approach to accountancy that Mr McKeown adopted and the late delivery of much of the financial information, it is very difficult to work out what were the current assets of DRL in February 2019 and what they would have been if Mr McKeown and his companies had settled all debts with DRL including matters debited to DRL which should have been debited to Mr McKeown's director's loan account. Mr Burns produced a balance sheet based on figures provided by the Respondent which he adjusted to add back various amounts including:

- £370,000 that was transferred to Mr McKeown between July 2018 and February 2019 and is not recorded in DRL's accounts as a loan to JMK by DRL;
- £245,000 paid to the Soho Club after it was transferred to JMCL; and
- £340,000 lease termination payment for the Marylebone Club which was owed to Mondrealm (the holder of the Marylebone Lease), a subsidiary of DRL that had no liabilities

to find DRL as having a £370,839 positive balance sheet as at February 2019. This was without taking account of any increased payment that DRL might have obtained on the sale of the Soho Club.

272. Mr McKeown challenged that many of these unaccounted items were outstanding and in view of the opaque accounting system used it is very difficult to work out whether Mr Burns' conclusions were correct. An attempt was made in court to follow through some of the payments which I have to confess I could not follow – this seemed the

accountancy equivalent of "Find the Lady". I have seen enough, however, to be satisfied that amounts owing to DRL by the Petitioner or his companies could be a substantial amount, taking account of various items that Mr McKeown now accepts were properly to be debited to his loan account, the £340,000 received from the Mondrealm landlord and the various legal expenses that had been charged to DRL that more properly relate to Mr McKeown's personal matters. The Marylebone Club also should have been making substantial profits during the rent-free period that it enjoyed towards the end of its lease.

273. It must be assumed that if Stratos or DRL had entered into the arrangements with the owners of the Euston Club, this would have been on no less favourable terms than those negotiated by Mr McKeown for himself. The effect of those terms seems to have been that he only needed to make a payment of £200,000 upfront and refinance a £67,000 rent deposit and then was given the ability to run the Euston Club, and benefit from its cash flow including the ability to divert that cash flow to other debts immediately. The payment of the balance of the £800,000 purchase price became due only came some months later. Had Stratos obtained the same terms, it too could have found a way to benefit from the cash flow from trading at the Euston Club in order to pay what was due.

274. I cannot be certain, but I find it highly likely that in the absence of the various elements of breach of directors' duties referred to above, DRL or Stratos would have had ample liquid resources.

Was the Company prevented from doing this as a result of historic VAT liabilities?

275. The second contention advanced as to why the Company could never have purchased the Euston Club is that it was at this time balance sheet insolvent as a result of large historic VAT liabilities said to amount to some £4.5 million.

276. These alleged VAT liabilities fall into three categories.

277. The first of these categories relates to VAT arising from DRL's practice regarding the treatment of taxi drivers who brought customers to the Clubs. The Club's practice was to allow taxi drivers to receive a tip of £20, being an amount equal to the door fee, otherwise payable by the customer to the Club. The Club regarded itself as having waived the door fee, so that there was no need to charge VAT on this amount. HMRC took the view that the door fee had been charged and was subject to VAT and that the payment to the taxi driver was an expense (which did not give rise to any matching VAT input tax except in the rare case where the taxi driver was registered for VAT). HMRC, assuming that it was correct in its analysis, was entitled to look back four years for the unpaid amount of this VAT and could also charge penalties and surcharges for the late payment of it. Whilst an earlier figure had been given for this potential liability of a much larger sum, as at February 2019, it seemed that the amount that HMRC would assess for the unpaid VAT was £245,000 and a provision of £225,000 had already been made in the accounts of DRL for this. It is possible that interest and penalties might have added to this, but of itself this looks like a manageable sum for DRL to find.

278. The second category of VAT related to VAT assessments raised by HMRC after the Marylebone Club ceased trading in February 2019. These assessments clearly were incorrect and it appears arose solely because Mr McKeown and the accountants had

failed to inform HMRC that DRL had ceased trading and failed to submit VAT returns for the remainder of 2019. These assessments, totalling some £510,231, therefore, did not represent a genuine liability. HMRC would be expected to reverse them once it was satisfied that the Marylebone Club had ceased trading.

279. The third category of unpaid VAT related to a payment system used at the Clubs called "Sophisticash vouchers". This system worked as follows. A customer wishing to obtain a private dance from one of the dancers could purchase a voucher at a premium to its face value so that he would pay £24 (later £25) for a voucher with a face value of £20. At the appropriate juncture he would give the voucher to the dancer. The dancer would later redeem the voucher from the Club at a discount to its face value, receiving £16 for this. This type of arrangement, with some variations, was common within the lap dancing industry.

280. Sophisticats, in common with other similar operators, had taken the view that no VAT was chargeable in relation to the vouchers as they should be characterised as the provision of a financial service that was not subject to VAT. This approach had been under attack from HMRC. At the time in question it was known that HMRC had successfully claimed against Secrets on the basis that the premium over the face value was chargeable to VAT. It was known that HMRC was in the course of a claim against Platinum Lace for the whole of the voucher (or its equivalent at Platinum Lace) to be subject to VAT, on the basis that it was not a financial service but was, in effect a pre-payment for the services of the dancer. It later transpired in December 2019 that HMRC won its case against Platinum Lace on this basis in a First Tier Tribunal case, *Romina Ltd v HMRC* [2019] UKFTT 736 (TC).

281. Calculations have been put forward on behalf of the Respondent that if it were assumed that the approach taken in *Romina* were applied to the Sophisticats business there was a very large potential VAT liability due in respect of previous years' trading. These calculations put the liability at a figure above £4.5 million. If anything like this figure was in fact due it would have rendered the company responsible for the VAT insolvent.

282. There is some uncertainty about whether this company was DRL or another subsidiary of Stratos that was issuing the vouchers, since HMRC in at least some of its correspondence appeared to accept that Devine Restaurants (Services) Ltd was issuing and administering the vouchers but it was Mr McKeown's evidence that this was planned for the future rather than being the position in the past.

283. It is not for this Court to determine whether this liability was due. This is a matter between HMRC, who are not represented in these proceedings, and the relevant company. The matter I need to consider is whether in February 2019 the potential for such a catastrophic assessment for back VAT was one which rendered DRL insolvent on a balance sheet basis and/or made it otherwise impossible for Stratos to contemplate acquiring the Euston Club.

284. What evidence there is about the knowledge available to Mr McKeown and to the board of DRL at the time on this issue points firmly to the opposite conclusion.

285. First, there is no evidence that HMRC has rendered any assessment in relation to this element of VAT. The most that can be said is that HMRC have been asking questions about the voucher system which show this to be a matter of interest to HMRC.

Secondly, this is a matter that the directors of DRL must have considered in signing off the accounts for DRL for 2018. These accounts were not signed off until September 2019 and they made no provision for this magnitude of VAT. Other accounting evidence put forward by Mr McKeown also made no such assessment of such a claim. The Marylebone Club balance sheet as at 28 February 2019 contained in the Management Accounts for DRL disclosed on 26 May 2020 for the period to 28 February 2019 does not include a VAT liability of this magnitude. Neither did the Walton Dodge Report assess a liability at this level. It noted that HMRC were "*considering*" a VAT claim in relation to the vouchers which "*could amount to a further £240,000*".

286. Furthermore the actions of Mr McKeown in the latter part of 2018 and in 2019 are not those of a director who believes that his company has no prospect of avoiding insolvent liquidation. At no point did he call in an insolvency practitioner to advise him about wrongful trading. He continued to undertake uncommercial actions, such as overpaying members of his family and friends and taking loans from the Company which he would have known would be criticised had DRL gone into insolvent liquidation.

287. From the evidence that I have seen, it is clear that Mr McKeown was aware of, and worried about the VAT issue as at February 2019, but he had not yet concluded that this was sufficiently likely to crystallise as a liability on the balance sheet of the companies involved. It is likely that he thought that there was a strong possibility that some VAT might be payable on the premium at which vouchers were issued on a similar basis to what had been found in the Secrets case rather than on the whole value of the vouchers. He did not think that even this was legally certain (or he would have started to charge VAT on this basis) but he did think it to be sufficiently likely that he prepared for this by increasing the price of the vouchers from £24 to £25. This view is compatible with what his solicitors, Brook Martin said on his behalf in their letter dated 21 December 2018. They said that "*it was and remains necessary for DRL to build up its cash reserves to enable it, if necessary, to meet the contingency of the £240,000 "vouchers" liability*".

288. It is reasonable to conclude, therefore, that as at February 2019 DRL's understanding of its VAT liabilities was that there was a liability for back VAT in relation to the payments to taxi drivers, but this had been fairly fully provided for in its accounts. There was a possibility, falling short of a one which it needed to note on its accounts as a contingent liability, that back VAT might be payable in relation to the premium charged on vouchers, and this was considered to be in the order of £240,000, or possibly more with interest and penalties if these were imposed. There was a concern that a much larger VAT liability might be assessed in the future in relation to the full face value of the vouchers, but this was not yet enough of a concern that DRL should take it into account in deciding its ability to undertake transactions. On the basis of such an understanding, the past VAT issues did not render DRL insolvent at this point or present to greater difficulty for it to consider the acquisition of the Euston Club.

289. On the basis of what I find to be his understanding of these liabilities at this point, and having regard to the care that Mr McKeown took to ring fence liabilities in the past, I think it is likely that had Mr McKeown decided on behalf of Stratos that it should go ahead with the acquisition of the Euston Club by purchasing the shares in Secrets (Camden) Limited together with Secrets (Euston) Limited he would have done so within Stratos rather than DRL and thus would have insulated Stratos from such a

catastrophic back VAT assessment. This is a further reason for believing that the VAT issue was not one that would have prevented Stratos from purchasing the Euston Club had it been given the opportunity to do so.

290. For the above reasons, I reject also submissions made on behalf of the Respondent that the owners of Secrets would have refused to sell to the Company because they would have been concerned about the Company's financial position.

291. I reject also the contention that the acquisition of the Euston Club was a speculative venture, too risky for the Company to take on. The Euston Club had a secure lease and no licensing problems – its 7am licence afforded the profitable trade after 3am, and it could benefit from an arrangement with the Soho Club for clients recruited in Soho to be transferred to it. Sophisticats had developed a successful trading format and both Mr McKeown and Carmen Alonso appeared satisfied that this could be replicated at the Euston Club to beneficial effect. I accept that there was a degree of risk as to whether clients would be as happy with the less salubrious environs of Euston as they had been in the Marylebone area, but this risk was mitigated by the fact that the Euston Club already had its own established clientele which provided a base that could be built on. In circumstances where Mr McKeown was happy to take the personal risk of this transaction, mortgaging his flat to undertake it, it is not credible to believe that it is one that he would have thought to be too risky for the Company, particularly where the alternative was certain death for the Company.

Would Stratos' inability to pay have excused Mr McKeown's appropriating the opportunity?

292. Even if it is not correct that this opportunity would have been one that the Company could have pursued but for Mr McKeown's failures in his duties, I am convinced by Ms Lintner's submission that where an opportunity is likely to be commercially attractive to the company, the director comes under a duty to bring it to the attention of the company, regardless of whether the company could or would have taken the opportunity. This is apparent from dicta in *Bhullar v Bhullar*:

> *"Whether the company could or would have taken that opportunity, had it been made aware of it, is not to the point: the existence of the opportunity was information which it was relevant for the company to know, and it follows that the appellants were under a duty to communicate it to the company."*

293. The argument was directly addressed in *Davies v Ford* [2020] EWHC 686 (Ch), where it was put to the Court that "*where a company is insolvent and not able to trade, and is therefore incapable of exploiting any business opportunity presented to it, there is no conflict in a director seeking for himself to exploit that same opportunity.*" Adam Johnson QC (sitting as a Deputy High Court Judge) had no hesitation in rejecting this contention and the terms on which he did this bear repeating in this case:

> *"With respect, it seems to me that that cannot possibly be correct, because if it were it would cut across one of the most basic principles of fiduciary law, namely that a fiduciary cannot escape liability by saying that the benefit acquired in breach of duty was not one the principal could have acquired or exploited….*

> *... Inability to take advantage of any relevant property, information or opportunity is immaterial to the assessment of whether the duty is owed; and to my mind it can make no different to that analysis to say ... that the reason for the inability is the insolvency of the company.*
>
> and
>
> *...It is no answer to a claim for breach of duty for a trustee to say that the opportunity he has exploited was not one which could ever have been taken up by the beneficiary. That is an entirely conventional analysis which, as Mr Shaw pointed out, has been the law for at least 300 years, since the trustee in Keech v Sandford ..."*

294. In the current case it was plainly obvious that Stratos, facing the termination of the lease of the Marylebone Club, would have a keen interest in the opportunity to acquire the Euston Club and Mr McKeown's decision instead to take this opportunity for himself was plainly a decision to allow a conflict between his interests and those of Stratos.

295. The strict rules that a fiduciary (which includes a company director) cannot avail himself personally of an opportunity where to do so would place him in conflict with the interests of the company has a long heritage. In *Keech v Sandford* [1726] 25 ER 223, a trustee was held in breach of duty for taking a new lease in his own name, even though the landlord had refused to renew the lease in the name of the infant beneficiary. Lord King LC held:

> *"This may seem hard, that the trustee is the only person of all mankind who might not have the lease: but it is very proper that the rule should be strictly pursued, and not in the least relaxed; for it is very obvious what would be the consequence of letting trustees have the lease, on refusal to renew to the cestui que use ..."*

296. This rule, and the application of it requiring an account of profits even where the company in question could not benefit from an opportunity obtained by the fiduciary in the course of his service, does indeed seem hard. However, the current case provides a vivid illustration of the need for the rule and the reason why it has remained a part of the common law for almost 300 years. If Mr McKeown had been aware of this rule and had believed that it applied so that he was debarred personally from the Euston Club opportunity, I am quite sure that he would have applied his considerable financial acumen to finding a way for Stratos to buy the Euston Club. If cash was tight, he would have persuaded suppliers and HMRC to give time for payment.

297. Although the breach of duties involved in this transaction were by Mr McKeown rather than by the Company, the circumstances still should be considered as involving acts or omissions by the Company amounting to the conduct of its affairs in a manner that is unfairly prejudicial to Mrs Langer (so as to engage section 994 of the Companies Act 2006) as the Company could and should have prevented him from undertaking this action.

VIII. THE MARYLEBONE TRANSACTION

298. I have already described the facts relating to the acquisition by Mr McKeown's company of the assets, trademark, trading name and goodwill of the Marylebone Club. It is notable that these were sold for no payment, but Mr McKeown argues that consideration was provided in that by accepting a TUPE transfer of staff Mr McKeown's company saved DRL from suffering redundancy costs, which he assesses to be at least £55,000.

299. The Petitioner contends that £55,000 did not represent full market value for what was transferred.

300. The legal issues applicable in this case are similar to those that I have already considered in relation to the Soho Club. Mr McKeown was under the duties that I have enumerated at paragraph 168 above. This was another point where there was a transactional conflict of interest governed by section 177 of the Companies Act 2006 and the articles of association of DRL and of Stratos. As with the Soho Transaction, it does not appear that at the time of the transaction a conflict of interest was declared as required under the DRL articles or was approved in accordance with the procedures set out in the Stratos articles. Proceeding with the transaction in such circumstances was of itself a breach of duties by Mr McKeown.

301. However, in this case, if we look solely at this sale transaction by itself, ignoring the question of whether DRL could have purchased the Euston Club, I think that Mr McKeown has a better case, that the transaction involved him exercising his powers for the purposes for which they were conferred; to act in the way most likely to promote the success of the company for the benefit of its members as a whole and to exercise reasonable care, skill and diligence in the performance of his functions.

302. By February 2019, with the lease for the premises of the Marylebone Club, coming to an end it was clear that there would need to be a sale. There would have been a highly limited market for what was on offer by this point. Save possibly as regards the trademark and wider brand or franchising opportunities it was unlikely that the assets transferred could be put to better account, and clearly it was in the interests of DRL to transfer its staff and to avoid redundancies. On this occasion, I do not think that Mr McKeown can be criticised for not undertaking any wider marketing of the assets and, unlike the Soho Club transaction and with the exception of price, the arrangements appears to be on what would be recognisably arm's-length terms. Perhaps the only criticism might be a failure to exercise reasonable care, skill and diligence in failing to have these terms adequately documented, but it is not obvious that DRL or Stratos has suffered to any extent as a result of that.

303. Whereas in the case of the Soho Club I consider that there was, in addition to the transactional conflict of interest, an ongoing non-transactional conflict of interests that needed to be considered, this is not the case in relation to this transaction (taking it separately to the issue about the Euston Club). After this transaction, Stratos and DRL were no longer in the lap dancing business (except insofar as they might have found someone who might pay for a licence for the residual rights in the Sophisticats name and trading style).

304. The reasonableness of this transaction (looked at by itself) turns on the question of whether an adequate price was paid for what was transferred. If the price was reasonable, then the only material breach of director's duties might arise from the failure to observe the procedural requirements of the articles of DRL and Stratos. These failures, by themselves, may not be sufficient for the Court to grant relief if they did not cause material prejudice to the interests of Mrs Langer as shareholder.

305. The key question, then is what was the value of what was transferred.

306. The assets transferred included the inventory of drinks and perhaps some loose furniture and fittings. The other aspects of the transfer included the transfer of staff and of the brand and the reputation and, so far as it did not attach purely to the premises, the goodwill of the business.

307. One of the issues disputed is whether these arrangements amounted to the transfer of the Marylebone Club to new premises or whether this was merely a transfer of disparate assets. I think that the arrangement should be considered to be a transfer of business. Certainly it was accepted that this was the transfer of an "undertaking", as it was assumed that the Transfer of Undertakings Protection of Employees Regulations applied to the transfer. There was clearly a concerted effort to transfer all elements of the goodwill and reputation of the Marylebone Club to the Euston Club, including by presenting this as a relocation of the business in all external communications and changing the website and social media postings to reflect this. The evidence of Carmen Alonso was that following this transfer the Euston Club was an amalgamation of the former Secrets Club and the Marylebone Club's business, but there seems to be little doubt that it was the Sophisticats name and format that was adopted and that following the transfer of staff the business followed the Sophisticats management style, including the rules that it adopted as regards the conduct of patrons and of the dancers.

308. In my view, the transaction should be regarded as one that involved the transfer, in so far as possible, of the portable goodwill of the Marylebone Club and an outright transfer of the Sophisticats name, brand and trading style.

309. This conclusion takes us back to the work of the experts in valuing the brand.

310. I have already commented on the approach taken by each of the experts to brand valuation. In my view the starting point must be to consider what is being offered here. Once again this is difficult to discern since there was no contemporaneous documentation of the transaction. It was suggested later in the board minutes ratifying this transaction that what was given was a licence of the Sophisticats name and trading style, but this was another of Mr McKeown's exercises in hindsight and I question whether that is a realistic way of looking at this. Once DRL had ceased trading (and had not secured an ongoing licence of the Sophisticats brand, so as to secure itself a continuing source of revenues) its ability to profit from the brand would have dwindled rapidly.

311. In these circumstances, had it been negotiating at arm's-length, I think it is far more likely that it would have negotiated an outright assignment of the brand, rather than a limited licence, and I think it is appropriate to assume for the purposes of valuing the transaction that should have been done that this was the case.

312. When I was considering the Soho transaction, I decided it was appropriate to value the brand on the basis of a "franchise value" acknowledging that, whilst the arrangements did not have the traditional features of the franchise, they involved the transfer of management know-how, training and ongoing management support in a manner that was highly analogous.

313. I am less certain that the same approach could be taken in relation to the transfer of the Marylebone Club operations. On the one hand the transfer involved the wholesale transfer of the cadre of experienced management, who took with them all of the systems, procedures and know-how that they had gained through working for DRL. On the other hand, a cynical purchaser might decide in the circumstances that he could recruit those staff without the cooperation of DRL.

314. Also in this case, I think it is more difficult to argue that Mr McKeown's position as a director and employee of DRL meant that DRL was entitled to constrain him from working for the transfer of the company and to put a value on allowing him to do so. He could have simply resigned. He was not subject to any restrictive covenants.

315. Nevertheless, the fact that the transaction involved the transfer of staff was not merely a convenience to the seller in avoiding the cost of their redundancy, but was a huge benefit and opportunity to the purchaser who obtained their training, know-how and expertise and the benefit of the established teamwork they had developed. Generally I think the purchaser had the better of the bargain relating to the transfer of staff and would have paid, rather than required to have been paid for it.

316. As a result I do not think that the taking on of redundancy liabilities was sufficient consideration for what was transferred. The portable assets that were transferred should be valued at their fair marketable value.

317. Given what I find about the Euston Club, and what I am going to say about remedies, it is not necessary for me to fix a value for what the brand was. Given that the way that I think that this should be looked at is quite different to the way that it was looked at in the reports of both experts, it is difficult for me to put a figure on what I think that the brand is worth based on the opinion evidence that I have seen so far. All I will say is that I think that there was a positive value there.

IX. THE EFFECT OF THE RATIFICATIONS BY THE BOARD AND SHAREHOLDERS

318. After presentation of the Petition, Mr McKeown arranged for meetings to beheld to provide a retrospective approval and ratification of his conflicts of interest arising from the Soho and Marylebone Transactions.

319. These meetings took place on 31 July 2019 and included:

(a) a board meeting for DRL at which the board of directors (consisting of himself and Mr Longland) adopted resolutions: (i) approving and ratifying his conflicts of interest in the Soho and Marylebone Transactions; (ii) releasing him from any duty he might have had to offer the opportunity to purchase the Euston Club to DRL, on the basis that DRL was not in a position to take up that opportunity;

(b) a board meeting for Stratos at which he (as the sole director) caused Stratos to: (i) authorise him to represent Stratos at an Extraordinary General Meeting ("**EGM**") of the shareholders of DRL to vote on the resolutions at that meeting and (ii) waive the notice requirements for that meeting;

(c) an EGM of DRL at which he caused the DRL shareholders (consisting solely of Stratos, represented by himself) to adopt resolutions approving and ratifying his conflicts of interest and releasing him from his duty to offer the Euston Club to DRL.

320. On 12 December 2019, Mr McKeown held an EGM for Stratos, at which (as the sole shareholder present, holding 75% of the voting rights) he caused the Stratos shareholders to ratify and approve resolutions approving and ratifying his conflicts of interest and releasing him from his duty to offer the Euston Club to Stratos.

321. I agree with the argument put to me on behalf of the Petitioner that these ratification resolutions do not assist Mr McKeown in relation to the current action. If his actions were unfairly prejudicial, as I find that they are, that unfair prejudice is not cured by these later resolutions.

322. This is expressly recognised in *Hollington on Shareholders' Rights:*

> *"A breach by a director of his duties to the company is capable of being treated as a breach of the bargain between shareholders … and hence as amounting to unfair prejudice for the purposes of the statutory unfair prejudice remedy, whether or not (in general) the breach has been ratified or is capable of ratification by the members in general meeting."*

323. If anything, bringing about these ratification resolutions could be regarded as a further act of unfair prejudice, particularly in the case like this one where wider duties of good faith are engaged.

X. THE LOAN ACCOUNT ALLEGATION

324. Mrs Langer complains that she has been unfairly prejudiced by being falsely accused of being indebted to the company on a shareholder loan account and through demands being made in a menacing manner for the repayment of these debts.

325. The amounts in question relate to payments made to her or for her benefit between August 2017 and March 2018.

326. I can accept that Mrs Langer (despite having served as a director) does not have a sophisticated understanding of company law or the mechanism by which dividends are declared and paid. The payments were being made out of the business, and only at times when the company had received revenue to allow it to do this and I am sure that she saw this as being a distribution of or on account of profit.

327. I accept also her evidence that she did not realise that she was building up a substantial shareholder loan account with DRL or Stratos.

328. It is true that there were various points when it should have been apparent to her that she and/or her husband was receiving monies in excess of the amounts they were each declaring as dividends on their respective tax forms. It is true also there were various discussions, including a discussion with Mr Chris Adams about the Retirement Scheme when it should have been apparent to her that monies received by her or her husband were not been treated as dividends. To some extent she may have been closing her eyes to the realities but it is some mitigation that this issue had always been discussed in the context of taxation, rather than in the context of personal indebtedness and she may have seen the distinction between shareholder loan and dividend as being a distinction belonging to tax rather than having any consequences for her personal indebtedness position against the Company or DRL.

329. Certainly, she and her husband had got used to a position that whenever a shareholder loan became a problem it was fixed by some device such as issuing an invoice or valuing a sale of goodwill.

330. A great deal of time was spent discussing Mrs Langer's beliefs, but her beliefs do not get to the heart of the complaint that she has pleaded. The question about whether the amounts that she has received were dividends or not is a question of fact. These payments could only have been dividends had there been a properly declared dividend first from DRL to Stratos and then from Stratos to its members. There is no suggestion that this ever happened.

331. As a matter of fact, therefore, any payments that she did receive must have been either gifts (which would have been an improper distribution to a shareholder and would in any event be liable to be repaid) or sums in anticipation of dividend, giving rise to an indebtedness that might reasonably be labelled a shareholder loan account. It was not unfair to Mrs Langer to maintain shareholder loan accounts in this way.

332. Where I think Mrs Langer was dealt with unfairly was that she was allowed to build up these accounts without being provided with a proper understanding that they were leading to indebtedness or of the level of that indebtedness, and certainly without any discussion of the circumstances in which they might need to be repaid. She was I am quite sure encouraged to believe that they would be dealt with either by the payment of a dividend or through some other device. If she had any belief about her obligation to repay, it would have been that this would be only as a last resort where Stratos or DRL was in insolvency proceedings.

333. Mrs Langer was first told about this indebtedness and the scale of it in a letter sent from Brook Martin on 26 March 2018. The information provided to her about this has been inconsistent. On 18 April 2018, Brook Martin provided a "loan account" schedule totalling £105,580.53 and asked for Mrs Langer's proposals to settle the alleged debt. On 5 October 2018, BSG Solicitors LLP (instructed by DRL, through Mr McKeown) wrote to her and made a written demand for payment in the sum of £40,135.55. On 23 September 2020, Mr McKeown exhibited to his second witness statement a schedule purporting to show her loan account with DRL between 1 August 2017 and 3 March 2018, with a closing balance of £50,092.

334. Even now there are detailed questions as to what is put forward as the accounting for this loan schedule and Mrs Langer has identified repayments that were credited to Mr Langer's loan schedule that she claims should have been added to hers.

335. My conclusions on this point, therefore, are that Mrs Langer was not unfairly prejudiced by the allegation that there was a loan account. However, she was unfairly prejudiced by the way that this was allowed to mount up without her being given a proper account of how this debt was growing and by the absence of any proper accounting for how this debt was said to have arisen. I consider also that she was unfairly prejudiced by the way that the debt was called in, and in particular by the written demand served in October 2018. Demanding repayment in that way of her (and without making similar demands at the same time of Mr McKeown in respect of his loan account or of Mr Langer) was clearly an attempt to intimidate Mrs Langer. It was also in breach of the informal understanding that Stratos and DRL, through Mr McKeown had allowed to arise that she would not be expected to repay except by way of set-off against later dividend payments or other forms of distribution of profits (although any such understanding would have had to have been subject to the caveat that a demand might be made where the relevant company needed to make this demand to repay its own creditors).

336. Having allowed the shareholder loans to exist, Mr McKeown should have taken every opportunity possible to clear off the loans by declaring dividends. He found ways from time to time to clear the loan accounts for himself and for Mr Langer such as through issuing invoices but not for her. To the extent that he was not able to declare dividends because the expenses of DRL had been inflated by payments or benefits to his own family, the damage done to Mrs Langer by having these amount outstanding represents a further way in which Mrs Langer was unfairly prejudiced by these excessive expenses. I will look to link these points in the order that I propose to make.

337. Mr McKeown's failures in this regard may be considered to be a breach of his duty to act with due skill care and diligence. It certainly was in breach of the duties of good faith that I find he had assumed to Mrs Langer.

XI. MRS LANGER'S CONDUCT

338. I am invited to consider certain acts by the Petitioner which the Respondent considers should affect my assessment of the unfairness alleged by the Petitioner and my decision about granting any relief.

339. The matters complained of include firstly complaints that the Petitioner and her husband during 2016 and 2017 frequented the Clubs and consumed excessive drink and drugs on the premises, putting the Clubs' licences at risk.

340. Secondly, it is complained that in 2018, she provided evidence against the Respondent which was used by Sophisticats' principal competitor, Mr Simon Warr of Platinum Lace to oppose the Respondent's application to extend the operating hours of the Soho Club (after its ownership had passed to JMCL). Her evidence related to an allegation that the Respondent had facilitated a mortgage fraud through falsely representing the employment status or earnings of Ms Maya Hawie. In relation to this matter, on which the Court heard some evidence, I was satisfied that Mrs Langer did have a genuine belief that some sort of fraud was being committed, albeit that this belief appears to have been ill founded. Mrs Langer explained her motivation as being to redress wrongs that she considered that Mr McKeown had done to Simon Warr in relation to his own

licensing hearing. This may have formed part of her motivation, but I am sure that she was also motivated by an animus against Mr McKeown.

341. Thirdly, it is complained that the Petitioner leaked confidential information to Mr Warr that she had obtained in connection with negotiations for her to sell her 25% shareholding in Stratos that was designed to assist Mr Warr in a hearing concerning security for costs against DRL.

342. Fourthly, it is alleged that the Petitioner exerted considerable pressure upon one of the Respondent's witnesses of fact, Mr Pat Keogh, with a view to discouraging him from giving evidence in support of the Respondent's defence to the Petition.

343. The wrongdoing and/or misconduct on the part of the petitioner in an unfair prejudice case can affect both the assessment of the alleged unfairness relied upon by the petitioner and the court's decision whether to grant relief where unfair prejudice is found.

344. This was for example the case in a decision given by Morgan J in *Interactive Technology Corp v Ferster* [2016] EWHC 2896 (Ch*).*

345. However, for these considerations to apply, there needs to be either a strong connection between the conduct in question and the matters that the Petitioner is complaining of or for the conduct to be so egregious that it needs to be weighed against the unfairly prejudicial conduct complained of.

346. These conditions were met in the *Interactive Technology Corporation* decision where it was clear that the petitioner's own bad behaviour led to the conduct complained of by the Petitioner and where Morgan J regarded the petitioner's fault to be "*many times graver than the relevant conduct of* [the respondents]".

347. These conditions are not met in relation to any of the matters complained of above. The matters which I have found to be unfairly prejudicial cannot in any sense be linked to any of the matters complained of by the Respondent. To the extent that they have been established, they demonstrate the breakdown in the relationship between the Respondent and the Petitioner, but they do not excuse the Respondent from his actions. They do not render the prejudice that she has suffered any less unfair.

348. Perhaps an argument could be made that the second and third allegations were such as to breach any bond of trust between Mr McKeown and Mrs Langer, so that their relations from that point should be judged solely by reference to their contractual and legal duties and entitlements without the overlay created by a good faith relationship. If that is the case, I do not think it has any bearing on my conclusions regarding the various instances of unfair prejudice which, with one exception, are grounded in breaches of duties under the articles or of directors' duties. The one exception relates to the demand made for repayment of the Shareholder Loan issue but even in that case I have found a breach of a duty of due skill and attention that is relevant in allowing the loan accounts to balloon without keeping Mrs Langer properly informed about the liabilities she was accruing.

349. Other than that, the most that can be said in relation to these matters is that when considering what remedies should be given for the unfair prejudice, the Court should

accept that the relationship between the parties has broken down and should concentrate on a remedy that will provide a clean break between the parties.

350. Whilst I am discussing Mrs Langer's conduct, I should mention another point which was made against her during the trial. It was pointed out that it was hypocritical for her to be complaining about the way that Mr McKeown put his own friends and family on the DRL payroll when her own family were benefiting in a similar way. In particular her stepson Oliver Langer was employed by the company on a retainer to provide IT support and for a period her niece, who was providing domestic help to Mrs Langer, was also on the payroll.

351. There is something in this point. I think that it is true that the expectations of both parties, before they fell out, was that a liberal approach would be taken to the employment of family members and this was acceptable provided there was a balance of benefit. However, the scale of benefit to Mrs Langer's family appears to have been substantially smaller than the benefits provided to Mr McKeown's friends and family and the employment of Mrs Langer's niece stopped in March 2018 when Mr McKeown sought to "regularise" the position, whereas the excessive payments to Mr McKeown's friends and family continued. Also, there is a qualitative difference between accepting benefits for your family as a shareholder and taking them as a director.

352. I will however take some account of this issue in the remedy I am proposing to order.

XII. WHAT RELIEF SHOULD THE COURT ORDER?

Principles underlying my decision

353. To summarise my findings so far, I consider that the Petitioner has made out her case that she has been unfairly prejudiced by the way that the Company's affairs have been conducted in a number of ways:

(a) through the financial mismanagement I have described above;

(b) through the sale of the Soho Club that was made to Mr McKeown's companies at an undervalue;

(c) through Mr McKeown taking the opportunity to acquire the Euston Club for himself when this opportunity should have been made available to the Company;

(d) though the sale of the assets of the Marylebone Club to Mr McKeown's companies at an undervalue;

(e) through the way that Mrs Langer's shareholder loan account has been administered.

354. Taken together these instances of unfair prejudice have caused material financial damage to Mrs Langer and she is entitled to a remedy for them.

355. Under section 994 the Court has a wide discretion as to the remedy it provides. It is appropriate that when deciding this the Court should give due weight to the desires of the injured party as to the remedy she seeks. In this case the Petitioner has requested

as her remedy the purchase of her shares by the Respondent at a price to be determined. Whilst other remedies are possible, I consider that this is a suitable remedy.

356. Under the Order of the Court dated 11 December 2019, a split trial was ordered. The issues set down for this trial are:

(a) Whether the Respondent has engaged in unfairly prejudicial conduct;

(b) If so, the appropriate form of relief; and

(c) If the relief ordered is that the Respondent shall purchase the Petitioner's shares in Stratos at a price to be determined, the appropriate basis and mechanism for the valuation of the Petitioner's shares.

357. In relation to this last point, in the interests of proportionality and having seen the enormous divergence of opinion that the professional valuers have had on valuation matters, I should as far as I can close down matters that are in dispute on which this Court has heard adequate evidence. Conversely, where I feel this Court has not seen adequate evidence, I should allow this to be collected at the next stage.

358. In framing an appropriate order, I think it is important to stand back and look holistically at the cumulative effect of the various actions of the Company and its subsidiaries that have given rise to unfair prejudice. Taken individually it is difficult to put a valuation on how different items have had an economic effect on the Petitioner, but taken as a whole it can be seen that the effect has been to transfer the entire Sophisticats trade from a company in which she was a 25% shareholder to companies in which she has no interest, and in the meantime to have denied her any return from her shareholding (if it is assumed that she will repay the shareholder loans) for a considerable time whilst the Respondent, and his family and friends have been enjoying income from the business.

359. In particular, from the evidence I have seen there is a strong likelihood that the value of the Sophisticats businesses is greater than the sum of the parts. The fact that the Soho Club exists allows business, when the Soho Club closes at 3am, to be referred to the Euston Club. This mitigates both the disadvantages of the earlier closing hours in Soho and the less fashionable address of the Euston Club. It also seems that the more upmarket brand and reputation, and better operating standards developed at the Marylebone Club also may have operated to the advantage of the trading at the Euston Club once it started to operate as a Sophisticats club.

360. For these reasons, I think that the remedy afforded to the Petitioner should be one that seeks to capture the value of the whole of the business, excluding the Soho Club, which should be assumed to have been sold on arm's length terms with a licence for the Sophisticats brand which included a term allowing the Marylebone Club and its successor the Euston Club the benefit of the referral arrangement.

Order for the purchase of Mrs Langer's shares

361. With these points in mind, I propose to make an order on the principles described below, with such additions or embellishments as the parties may wish to put to me when this judgment is handed down where I consider such matters to be helpful.

362. I propose that the First Respondent be ordered to purchase the shares held by the Petitioner in Stratos Clubs Limited at a price to be determined as follows:

(a) The price shall be calculated as 25% of the value of the shares of a top company of a group of companies comprising Stratos Clubs Limited, its subsidiaries as at the Valuation Date (discussed below) and Secrets (Camden) Limited and its subsidiaries as at the same date (together the "**Deemed Group**"). It may be noted that in framing this in this way I am providing that there should be no discount to reflect the fact that Mrs Langer's shares are a minority holding.

(b) For the purposes of the valuation the following assumptions shall be made:

(i) That the sale is between a willing seller and willing buyer at arm's length having full sight of the financial and other information applicable to the companies that are currently subsidiaries within the group headed by Stratos Clubs Limited, but with only the financial information in relation to Secrets (Euston) Limited/Secrets (Camden) Limited and its subsidiaries that would have been available to Mr McKeown on the Value Date.

(ii) That control of Secrets (Euston) Limited/Secrets (Camden) Limited was acquired by Stratos Group Ltd on 10 February 2019 on the same terms that Mr McKeown in fact acquired that company, with such acquisition being completed on 1 October 2019 and that the staff and assets of the Marylebone Club transferred to Secrets (Euston) Limited on the same date and on the terms that they did so transfer.

(iii) That at the time of the valuation the business consists of the Euston Club trading as Sophisticats with the full benefit of the goodwill, the Sophisticats brand and the assets of the Marylebone Club as well as those of Secrets (Euston) Limited/Secrets (Camden) Limited. This business should be valued as a going concern, having regard to the track record of the Marylebone Club and of the Euston Club and the trading and prospects of the Euston Club.

(iv) That the Euston Club has, and before that the Marylebone Club had, the benefit of referrals of trade from the Soho Club without paying any commission to JMCL or Brewer Street Restaurants Limited for it and that this will continue.

(v) That the Deemed Group has full ownership of all rights that the Company or its subsidiaries had in the Sophisticats brand (including the name, the unregistered trademark and any other associated intellectual property or right, subject only to a licence provided to the owners of the Soho Club in return for which no royalty payment is due.

(vi) That where there are shared expenses between the business attributable to the Soho Club and that of the Marylebone Club and subsequently the Euston Club, including any overhead costs of management or central administration or audit they are fairly apportioned.

(vii) That historic and future turnover should be assessed on the assumption, as regards VAT on vouchers, that the premium relating to the vouchers is subject to VAT but not the full face value of the vouchers. This assumption may be rebutted if further persuasive contemporaneous evidence is adduced that shows that the perception of

the Company had changed as at the Value Date from that which I have found it to be in February 2019. Such evidence would include that the relevant company had received an assessment for VAT on a different basis or had started charging VAT on a different basis or had called in insolvency practitioners or had accounted for a different measure of VAT liability in statutory accounts dating that had been approved and signed earlier than 1 October 2019.

(viii) That historic and future turnover should be assessed on the assumption, as regards VAT on payments of entrance fees rebated to taxi drivers, that such amount was fully assessable to VAT. This assumption may be rebutted in the same way.

(ix) That the payroll expenses of the business have been rationalised to those appropriate for the efficient running of the business and that all redundancy costs to have been expended.

(x) That in measuring the profitability of the Deemed Group for the purposes of this valuation that the following principles shall apply:

(aa) such operating costs relating to the Group do not include any operating costs that have been identified in this judgment as being excessive or unjustified;

(bb) that DRL sold the assets of the Soho Club on 28 June 2018 on the basis mentioned in paragraph 251 to 256 above and from that date had no exposure to the profits or losses of that Club;

(cc) on the assumption that the proper provision to be made for the historic VAT liabilities of DRL discussed above are those provided for in its balance sheet dated 30 June 2018 and no further provision is required. This assumption may be rebutted in the manner that I have described above. Furthermore, it should be assumed that those liabilities are ring-fenced within DRL (and any other companies which it was in a VAT group with as at 10 February 2019) and so if they are shown to be substantially greater the Company will have the benefit of limited liability.

Choice of Valuation Date

363. It should be ordered that the Valuation Date should be set at 1 October 2019, being the date on which the acquisition of the Euston Club was finalised.

364. In setting this date, I have considered the wide flexibility that the Court has in these circumstances. Whilst there is a general approach that the date of valuation should be the date of judgment, this is a principle that the Court will depart from in appropriate cases. Following the decision in *Re Cumana Ltd* [1986] BCLC 430, the Court will be prepared to set an earlier valuation date where after the date of the wrongdoing and after the date of the petition there is a subsequent fall in the market where the conduct of the respondent was to deprive the petitioner of his or her asset. This reflects the fact that it is unfair for the wronged shareholder to accept the risks of a business that he or she has been excluded from and where this is found not to have been being managed in the interest of shareholders.

365. As I have found, there are numerous ways in which the Respondent has breached his duties as a director and the effect has been to deprive the Petitioner of her share in the business. In this case, 10 February 2019 was the date on which the Petitioner was effectively deprived of her share in the business. The Petition was brought on 2 April 2019. These dates are both well before the current pandemic and I think it would be open to me to choose either of them as the Valuation Date.

366. However, the order I am proposing to make is intended to put the Petitioner in the position that the Petitioner shall be bought out as if she had had the benefit of the acquisition of the Euston Club, and this acquisition was not secured until 1 October 2019 when a condition was met. There is logic, therefore, in making this the appropriate date for the valuation. If an earlier date were chosen, there could be sterile arguments as to whether the condition would be met and the sale would be completed.

367. There is also a practical advantage of taking 1 October 2019 as the valuation date in that it should allow some assessment to be made of the trading of the Euston Club as a Sophisticats club, rather than this being a matter of pure speculation for the valuation experts to take different views over.

Order relating to shareholder loans

368. The remedy proposed above is, in my view, fair and effective to deal with all of the instances of unfair prejudice that I have found except those in relation to the management of the shareholder loan account and in relation to the various items of financial mismanagement that I have found to be substantiated. In my view there is a connection between these two points since the financial mismanagement (taken with the sale of the Soho Club at an undervalue) may have had an effect on the ability for dividends to be declared that would have cleared off some or all of any shareholder loan account. It is too difficult for the Court to assess this at this juncture what the finances of Stratos would have looked like if the finances had been managed in the interests of shareholders. Even if DRL was not trading profitably at the end a different approach to financial management that more fairly balanced the interests of the shareholders might have been possible, for example of Stratos (or the company that we are told was employing the staff) could fairly have charged a management fee to DRL for its services allowing a small income to come up to Stratos that might have justified a dividend.

369. I cannot be certain, therefore, whether in the absence of the financial mismanagement Mrs Langer would still have had a shareholder loan account at the level that it now is and if she would have allowed this to run up in the way that it appears that it has if she knew that it would be repayable and might be called in at any time. However, certainly it does not seem fair that Mr McKeown, in the position of trust that I have found him to be in, was taking (in one way or another) more than his due whilst leaving Mrs Langer to repay the amounts that she had received which she had thought to be on account of profits.

370. In order to deal with these points, I propose to order that the Respondent should assume the liability to repay Mrs Langer’s shareholder loans account up to the lesser of (i) the full value of such shareholder loan account; and (ii) 25% of the sum of the Excess Salary and the Excess Payments.

371. For these purposes, the "**Excess Salary**" means the net of tax salary received by the Respondent that is in excess of the amounts I have found that it is proper for him to receive as set out in paragraphs 134 and 135 of this judgment but ignoring the last sentence. The "**Excess Payments**" means the net of tax, salary or subsidised rental payments and other payments that I have found to be unjustified or excessive in paragraph 136 to 164 of my judgment above, but only for the period from 1 March 2018 to the Valuation Date. I am restricting this since I take the view that, as the Petitioner's family also had benefited in the past from unjustified or excessive payments of salary, she was not in a position to complain about this until 1 March 2018 when the Respondent said that matters should be put on a more regular basis.

372. I hope that with the further disclosures that were made late in this process that it will be possible to determine and agree the amounts of Excess Salary and of Excess Payments and of the balance of Mrs Langer's shareholder loan account, but I cannot rule out that further expert forensic accountancy work may be needed for this.

Mechanism for valuation

373. Ms Lintner has requested on behalf of the Petitioner that, if the Petitioner is to be granted the remedy of the purchase of her shares at a valuation, the Court should order a single valuer to undertake this valuation, in order to speed up the process. She has argued, I think correctly, that this would not be incompatible with the order that was given for a split trial.

374. Mr Tager, on behalf of the Respondent has resisted this proposal.

375. I confess that I have been tempted by this suggestion and have initially seen some merit in this approach, if it could lead to a shorter outcome.

376. However, when I considered what order I would make, and how this would preserve fairness between the parties, I am led to doubt whether this would indeed lead to a shorter outcome or to less costs. If I were to include the appointment of a single valuer as part of the order, I think it would need to be in the following terms:

(a) That a single valuer be appointed to undertake the valuation mentioned above, and the calculation of "Excess Salary and of "Excess Payments" and of the balance of Mrs Langer's shareholder loan account. The valuer shall be chosen by agreement between the parties, or in the absence of agreement appointed by the Court from a shortlist where each party may nominate up to three firms to the shortlist.

(b) The valuer shall be instructed to produce the first draft of his or her report within six weeks of appointment.

(c) Each party shall give full support to the valuer and make available all information that the valuer may reasonably request promptly.

(d) The valuation shall be provided in draft to each party and each party shall be entitled to make representations to the valuer concerning the valuation before its finalisation and an opportunity to reply to the points made by the other party.

(e) Either party may also apply to the Court if any of the instructions to the valuer need to be clarified.

(f) The parties shall agree a timetable for these further steps, or in the absence of agreement one will be imposed by the Court.

(g) Following receipt of representations from the parties the valuer shall finalise the report and shall present it to the Court for confirmation.

(h) At a hearing to confirm the valuation the parties may make representations to the Court, but these representations should be limited to representations as to whether the valuation complies with the order or orders made by the Court.

377. Having looked at what such an order might involve, I am not at all persuaded that this would be quicker, or involve less cost, than the more conventional approach of the parties each coming back to the Court with their own valuation, the expert valuers having first met and tried to reduce the differences between them.

378. Furthermore, I hesitate to approach the valuation on this basis, which as far as I can discern is not one that has been blessed by any precedent. I am left with a feeling that it might be considered a dereliction of duty for this Court to outsource its responsibilities to an external valuer, but I have not been able to discern any guidance on the matter.

379. I am prepared to be addressed further on this point by Counsel if either Counsel, having seen how I would tackle the appointment of a single valuer in an order, considers that this does have some merit. However, unless I can be persuaded to the contrary, I will make an order for a further hearing, in the conventional manner, to determine the valuation.

XIII. CONCLUSION

380. This judgment is being handed down remotely. An early hearing should be convened to consider the matters consequential upon it following the Christmas vacation.

381. Finally, I would like to record my thanks to Counsel on both sides for the very professional way in which this case has been presented and also to record my thanks to the solicitors involved, particularly Russells who took most of the brunt of the preparation of bundles, for the efficient and helpful way in which these were compiled. This case has involved considerable complexity and a great deal of evidence and the Court would not have been able to deal with this within the time allotted without the considerable assistance that it has been rendered.