Trinity Term
[2014] UKSC 41
On appeal from: [2013] CSIH 13

JUDGMENT

Henderson (Respondent) *v* Foxworth Investments Limited and another (Appellants) (Scotland)

before

Lord Kerr
Lord Sumption
Lord Reed
Lord Carnwath
Lord Toulson

JUDGMENT GIVEN ON

2 July 2014

Heard on 14 May 2014

Appellant
Craig Sandison QC
Usman Tariq
(Instructed by Halliday Campbell WS)

Respondent
Lord Davidson of Glen Clova QC
David Thomson
(Instructed by Burness Paull & Williamsons)

LORD REED (with whom Lord Kerr, Lord Sumption, Lord Carnwath and Lord Toulson agree)

Introduction

1. Letham Grange is a neoclassical mansion built in the 1820s, with extensive landscaped grounds. In modern times the house was converted into a hotel, and the grounds were laid out as two golf courses. The hotel became popular with golfers, and was also used by judges sitting on circuit in the nearby town of Forfar. The hotel closed in 2011, but remains known to Scottish judges as the subject-matter of a long-running legal dispute. That dispute has now made its second appearance in the United Kingdom's highest court.

2. The hotel and its golf courses ("the subjects") were bought in November 1994 by Letham Grange Development Company Ltd ("LGDC") for slightly over £2m. On 12 February 2001 LGDC sold them to the second appellant, 3052775 Nova Scotia Ltd ("NSL"), a company based in Canada. The consideration recorded in the disposition was £248,100. In December 2002 LGDC went into liquidation, and the respondent, Mr Henderson, was appointed as its liquidator. The value of the subjects at that time was estimated at about £1.8m. In January 2003 NSL granted a standard security (ie a charge) over the subjects in favour of the first appellant, Foxworth Investments Ltd ("Foxworth"), another company based in Canada. Later that year the liquidator began proceedings against NSL in the Court of Session, in which he sought the reduction (ie setting aside) of the 2001 disposition on the grounds that the sale was a gratuitous alienation, an unfair preference or a fraudulent preference. The action had a lengthy history. Ultimately, the liquidator obtained decree by default in 2009, when NSL failed to be represented at the hearing fixed for the proof (ie trial). It is not argued that that decree gives rise to any plea of res judicata in the present proceedings.

3. The liquidator then began these proceedings, in which he seeks the reduction of Foxworth's standard security. His action is brought on the basis that the disposition to NSL was a gratuitous alienation susceptible to reduction under section 242 of the Insolvency Act 1986 ("the 1986 Act"). That section, so far as material, provides that an alienation made by a company within two years of the commencement of its winding up is challengeable by the liquidator, and that on such a challenge being brought, the court shall grant decree of reduction unless, in particular, "the alienation was made for adequate consideration": section 242(4)(b). Although a proviso to section 242(4) preserves "any right or interest acquired in good faith and for value from or through the transferee in the alienation", the

liquidator argues that Foxworth cannot bring itself within the scope of that proviso, since it knew, at the time when it obtained the standard security, that LGDC was in liquidation and that the sale by LGDC to NSL was open to challenge under section 242. In that regard, reliance is placed on the fact that the relevant decisions of all three companies – LGDC, NSL and Foxworth – were made by their common director, Mr Liu, who was their directing mind and had full knowledge of all the material circumstances.

4. The proceedings are defended primarily on the basis that the sale by LGDC to NSL was made for adequate consideration: in addition to the sale price of £248,100 recorded in the disposition, NSL had, it is claimed, also assumed debts of £1.85m owed by LGDC to Mr Liu and members of his family. On that basis, it is argued, Foxworth fell within the scope of the proviso to section 242(4): it had obtained the standard security in good faith and for value.

5. The Lord Ordinary, Lord Glennie, held after a nine day proof that the sale of the subjects by LGDC to NSL had been made for adequate consideration. Although the price recorded in the disposition was far below the value of the subjects, that price had not, he held, been the entire consideration for the sale: NSL had in addition assumed liability for debts of £1.85m owed by LGDC to Mr Liu and members of his family. The disposition had not therefore been susceptible to reduction under section 242. It followed that Foxworth had obtained its rights under the standard security in good faith. There was no live issue as to whether the standard security had been obtained for value. The standard security was therefore not liable to reduction: [2011] CSOH 66; 2011 SLT 1152.

6. On the liquidator's appeal against that decision, an Extra Division of the Inner House held, after a hearing which lasted six days, that the Lord Ordinary had erred in law: he had not made a finding that the assumption of any debts by NSL had occurred at the time of the sale, and had therefore formed part of the consideration for the sale. In the absence of such a finding, it was held, the Lord Ordinary had not been entitled to hold that the alienation of LGDC's property had been made for adequate consideration or, given Mr Liu's knowledge of the circumstances, that Foxworth had obtained the standard security in good faith.

7. Furthermore, the Extra Division considered that the Lord Ordinary had in any event failed to give satisfactory reasons for the factual conclusions which he had reached on the evidence before him, and that the matter was therefore at large for the appellate court. On the basis of the material which it considered, the Extra Division held that the sale by LGDC to NSL had been a gratuitous alienation, and that Foxworth had not obtained its rights under the standard security in good faith or for value. Decree was therefore granted for the reduction of the standard security: [2013] CSIH 13; 2013 SLT 445. The Extra Division did not require to deal with a

cross-appeal by Foxworth and NSL against the Lord Ordinary's decision in relation to expenses ([2011] CSOH 104).

8. Foxworth and NSL now appeal to this court against the decision of the Extra Division, and also against the Lord Ordinary's decision in relation to expenses.

An outline of the evidence

9. It may be helpful at this stage to summarise the principal aspects of the evidence.

10. In his evidence, Mr Liu explained that LGDC had been established as a special purchase vehicle for the acquisition of the subjects in 1994. He was its sole shareholder. The purchase was financed out of loans of over £2.3m made to LGDC by himself, his wife and his parents. The loans came from accounts held with Sanwa Bank in Canada. £200,000 was borrowed from the bank, the borrowing being guaranteed by another family company, Coquihalla.

11. A contemporary letter dated 4 November 1994 from Mr Gardner, a partner in MacRoberts, the solicitors acting for LGDC in connection with the purchase, confirmed that he had received a transfer of £1.9m from Sanwa Bank in Canada and a further £350,000 from Mr Liu's father. Mr Liu also produced letters sent by himself, as a director of LGDC, to his wife and his parents, setting out the amounts which each of them had lent to LGDC and the terms as to repayment. A similar letter to Coquihalla was also produced. The letters purport to have been signed by Mr Liu and the recipients on various dates in December 1994. A fax dated 2 December 1994, containing the same details as to the loans, was also produced, which Mr Liu said had been sent to Mr Gardner after he had requested such details.

12. The borrowing from Sanwa was due to be repaid in October 2000. By then it amounted to £248,100 inclusive of interest. In his evidence, Mr Liu said that LGDC was at that time in dispute with its former accountants, and did not have accountants who could properly record an injection of funding into the company. In those circumstances he decided that the easiest way to repay Sanwa would be for LGDC to sell the subjects to another vehicle company for the amount required. The new vehicle company was NSL.

13. In relation to this evidence, the Lord Ordinary observed that Mr Liu did not explain in detail, perhaps because he was never asked, why the sum could not have been advanced to LGDC as a loan. The absence of accountants did not appear to him to be a credible explanation, given the lack of formality surrounding the initial

family loans to LGDC. The Lord Ordinary commented that the reason for the transaction remained a mystery.

14. According to Mr Liu, he was told by Mr Gardner that the proposed price was not enough, since it did not reflect the value of the subjects. Mr Liu responded that, if the cash price was not enough, he would have NSL assume the liability to repay part of the sums lent by himself and his family to LGDC. After Mr Gardner confirmed in writing that £248,100 was not enough, Mr Liu agreed with his wife and parents that NSL would assume LGDC's liability to the extent of £1.85m. He did not tell Mr Gardner that the assumption of liability had occurred. Mr Liu gave unchallenged evidence that, following the sale to NSL, the sums due to Sanwa in respect of the Coquihalla loan were repaid.

15. Mr Liu accepted in cross-examination that he and his wife and parents made claims in February 2003 in the liquidation of LGDC, in respect of the loans described in the letters dated December 1994, which were excessive if, as he claimed, liability for £1.85m of the debts had been assumed by NSL. He stated that a mistake had been made by Brodies, the solicitors acting on his behalf. He had not corrected the mistake when he signed his claim form. The claims were subsequently adjusted so as to exclude the part of the loans which was said to have been assumed by NSL. The adjusted claims were rejected by the liquidator in their entirety, with the consequence that Brodies were unable to move a motion that a new liquidator should be appointed. Mr MacPherson, the solicitor at Brodies who prepared the claims, was not called as a witness, and in those circumstances the Lord Ordinary did not accept that the claims had been the result of a mistake on his part.

16. A letter from Mr Gardner dated 7 February 2001 was produced. In the letter, Mr Gardner noted that LGDC was "between accountants", and advised that if the transfer of the subjects was at a figure under its true value, "then such a transfer could be attacked in the future by any liquidator of [LGDC]". The disposition was executed by MacRoberts, as the company secretaries of LGDC, on 12 February 2001. A letter from NSL to LGDC, dated 28 February 2001, was also produced. It acknowledged that, in addition to the purchase price, NSL would also assume £1.85m of debt owed by LGDC to the Liu family. The letter was signed by Mr Liu using the name "J Michael Colby". He explained in evidence that he had decided to use a western name when conducting business in the West, as he felt that he was at risk of discrimination as an ethnic Chinese. Resolutions of NSL dated 26 January and 7 February were also produced. The former stated that NSL would purchase the assets of LGDC for £248,100. The latter stated that NSL would "further assume £1,850,000 UK Pound Sterling of extra other debt liability of [LGDC] to the Liu family".

17. According to Mr Liu's evidence, NSL's acquisition of the subjects was financed by a loan of £300,000 advanced to it by Foxworth. A standard security in respect of the loan was executed but was not registered. In 2003 Foxworth assumed liability for debts totalling £1.7m owed by NSL to the Liu family. A fresh standard security was then executed and registered in respect of a personal bond for £2m, comprising the £1.7m of debt and the earlier loan of £300,000. That is the standard security challenged in the present proceedings.

18. Evidence was also given on behalf of Foxworth and NSL by a number of other witnesses. Mr Liu's son, who had been involved in running the family business, was called to answer allegations that he had destroyed records relating to LGDC and NSL. The Lord Ordinary records that "he struck me as an honest witness and on these matters I accept his evidence". Another director of NSL gave evidence, but her recollection of that company's taking over loans from LGDC was uncertain, and the Lord Ordinary did not feel able to place reliance upon it. Mr Liu's wife and parents gave evidence that they left the running of the family's business interests to him. They confirmed that they had lent money for the purpose of LGDC acquiring the subjects, and that they had been told about, and had agreed to, NSL assuming responsibility for their loans. In relation to those events, however, the Lord Ordinary did not regard their evidence as providing independent support for Mr Liu's account.

19. Mr Gardner also gave evidence. In relation to the purchase of the subjects by LGDC, he confirmed sending the letter dated 4 November 1994. There was never any doubt in his mind that the £2m or so that he received was provided by or on behalf of members of the Liu family. He had written to Mr Liu on 7 November 1994, requesting details of the breakdown of the funds. He said that he had not received a response. He had no recollection of receiving the fax dated 2 December 1994 or the letters from LGDC to Mr Liu and his wife and parents dated December 1994. The Lord Ordinary commented that it would be surprising if Mr Gardner had received no response to his request: it was not consistent with his general approach to this matter for him simply to let the matter drop.

20. Mr Gardner also spoke to a fax which he had received from Mr Liu dated 23 February 1995 in which Mr Liu said that the split of the loans was to be between eight members of his family. Mr Liu had described this as a thought which was never implemented. Mr Gardner was not aware of anything happening which suggested otherwise than that the arrangements described in the 1994 letters were entered into and remained in operation. In relation to the sale of the subjects by LGDC to NSL, Mr Gardner confirmed having sent the letter dated 7 February 2001, warning of the risk which would result from a sale at an undervalue, following a discussion of that risk with Mr Liu. There had been mention of the loans during his discussions with Mr Liu in February 2001, but he had not been told that the consideration included the assumption of the loans.

21. Evidence was also given by the liquidator and members of his staff. The letters dated December 1994, recording the loans made to LGDC by members of the Liu family, did not feature in the files of LGDC. Nor did the letter dated 28 February 2001 from NSL to LGDC, relating to the assumption of the loan.

Error of law?

22. As I have explained, the critical issue under section 242(4)(b) is whether "the alienation was made for adequate consideration". That was clearly understood by the Lord Ordinary. He summarised the liquidator's case as being that "the disposition of the subjects by [LGDC] to NSL was not made for adequate consideration": in particular, "the consideration of £248,100 referred to in the disposition … was not adequate consideration having regard to the value of the subjects". He summarised the case advanced on behalf of Foxworth and NSL as being that "the disposition … was not at an undervalue because the price of £248,100 stated in the disposition did not represent the whole consideration": in particular, "the consideration for the disposition included the assumption of debt", namely £1.85m owed by LGDC to members of Mr Liu's family. He summarised the liquidator's response as being that he challenged the assertions made by Mr Liu about the 1994 loans, and challenged "the defenders' case that in 2001, as part of the consideration for the subjects, NSL assumed the debt which the company owed to the Liu family". The liquidator sought to establish, in particular, that the documentation relating to the assumption of the loan had not been prepared on the dates which it bore, but had been produced subsequently in order to support a false case.

23. In relation to this matter, the critical paragraph in the Lord Ordinary's opinion is in the following terms:

> "It is not clear to me on the evidence when the documentation purporting to evidence the assumption of the loan by NSL was created, or indeed when the decision was made that the amount of debt assumed would be £1. 85 million rather than some other figure. Mr Liu acted for both LGDC and NSL (albeit under different names) and also took the necessary decisions so far as concerned the loans from members of his family. To that extent, once the decision was made, the documentation could follow later. It was not suggested in argument that the subsequent creation of documents to record the assumption of the loan as part of the consideration for the sale in any way invalidated what had occurred if the decision had in fact been made to assume part of the loan as part of the consideration. I find that that decision had been made." (para 90)

The Lord Ordinary accordingly concluded "that the sale from LGDC to NSL was made for adequate consideration and was not a gratuitous alienation." (para 92)

24. There was no argument before the Lord Ordinary to the effect that, even if the debt assumption had taken place, that had occurred at a point in time which was too late for it to qualify as consideration. Before the Inner House, however, that argument was advanced by the counsel and solicitors newly instructed on behalf of the liquidator. It was accepted by the court. In relation to para 90 of the Lord Ordinary's opinion, Lady Paton, with whose reasoning the other members of the court agreed, stated at paras 75-76:

> "The consideration allegedly given in exchange for the granting of the disposition of Letham Grange to NSL required to be enforceable (ie able to be vindicated) at the time when the disposition was granted on 12 February 2001. On the Lord Ordinary's own findings, however, there was no enforceable obligation binding NSL to repay Liu family loans as at that date. Taken in context, I am quite unable to read the words 'part of the loan' in the penultimate line of para 90 of the Lord Ordinary's opinion as being referable to the precise or calculated figure of £1.85 million but, even if they were so read, I doubt whether, in the absence of any documentation whatsoever, the 'decision' in question could properly be regarded as any more than a statement of intent on the part of Mr Liu. … It was not open to the Lord Ordinary to accept that consideration was given in exchange for the disposition granted in the form of some vague obligation undertaken by NSL to repay Liu family debt."

25. In relation to the first point made by Lady Paton, the Lord Ordinary was aware that an obligation on the part of NSL could only constitute part of the consideration for the sale if it was undertaken as the counterpart of the obligations undertaken by LGDC in relation to the sale. He distinguished at para 90 between the question, on which those then acting for the liquidator had focused, whether the documents evidencing the obligation existed at the time of the sale or were created subsequently, and the question whether "the decision had in fact been made to assume part of the loan as part of the consideration". He answered the latter question in the affirmative. It is possible that, when he referred to "part of the loan", he meant some wholly indeterminate amount, but only if he had failed to realise that a decision to assume liability for an amount which was entirely unquantified, and incapable of quantification, would not give rise to an enforceable obligation. I would decline to attribute an elementary error to an experienced judge if his words can reasonably be understood in a different sense, as they can in the present case, where the £1.85m was indeed "part of the loan".

26. It might be said that the Lord Ordinary could have dealt with this matter more clearly, but it is understandable that his opinion should have dealt in greatest detail with the points on which the parties had joined issue: in particular, whether the documents had been created on the dates that they bore, and whether, rather than when, any obligation was undertaken.

27. In relation to Lady Paton's second point, Mr Liu gave evidence to the effect that a decision to assume the indebtedness had been taken on behalf of NSL, with the agreement of the relevant members of his family, before the sale was completed. Subject to the separate criticism that he failed to deal adequately with the evidence, to which I shall turn next, the Lord Ordinary was entitled to accept that evidence and, on that basis, to find that an enforceable obligation had been undertaken, rather than a mere statement of intent.

Failure to deal adequately with the evidence?

28. Lady Paton described the way in which the Lord Ordinary had erred in his approach to the evidence at para 78 of her opinion:

> "He did not take the final step of (i) clearly recognising that there was a significant circumstantial case pointing to a network of transactions entered into with the purpose of keeping Letham Grange (valued at £1.8 million) out of the control of the liquidator, and (ii) explaining why, nevertheless, he was not persuaded that the liquidator should succeed. Rather the Lord Ordinary dismissed or neutralised individual pieces of evidence without, in my view, giving satisfactory reasons for doing so, thus dismantling the component parts of any circumstantial case which was emerging from the evidence, but without first having acknowledged the existence and strength of that circumstantial case, and then explaining why he rejected it."

Her Ladyship then gave five examples of this erroneous approach.

29. I shall discuss those examples shortly. It may however be helpful to preface that discussion with some general observations. The Lord Ordinary was correct to approach the evidence as a whole with an open mind, rather than beginning with a presumptive conclusion in favour of the liquidator's case, and then explaining why he was nevertheless persuaded that the liquidator should not succeed. He understood what the liquidator's case was, as I have already indicated, and he set out the matters advanced on behalf of the liquidator in support of that case, as I shall explain. The fact that he found the liquidator's circumstantial case less impressive than the Extra

Division reflected a careful and nuanced assessment of the evidence, and an understanding of the commercial realities of the situation with which the case was concerned.

30. The circumstantial case which impressed the Extra Division was superficially attractive, if one important circumstance, which I shall shortly come to, was disregarded. LGDC, a company owned and controlled by Mr Liu, went into liquidation. Less than two years earlier, at a time when it was in financial difficulties, all its fixed assets were transferred to another company, NSL, owned and controlled by the same individual. Lady Paton stated at para 85 that the evidence viewed as a whole gave rise to the inference which the liquidator contended for, that is to say, that "the transactions in 2001 and 2003 were carried out neither in good faith nor for value, with a view to placing the valuable heritable property beyond the reach of the liquidator, thus defeating the claims of LGDC's creditors" (para 77).

31. One difficulty with this analysis is that it is not clear from the evidence that LGDC was in financial difficulties in 2001, as Lady Paton states at paras 2 and 16. Although, as with many companies, a balance sheet would have shown that its liabilities exceeded its assets, there was no evidence that it was in trading difficulties at that time, and Mr Liu gave unchallenged evidence that the winding-up occurred as a result of subsequent events.

32. There is however a more fundamental difficulty. If LGDC was heavily indebted to Mr Liu and his family, that circumstance would cast an entirely different complexion upon the inherent likelihood of the liquidator's case. In that situation, it would make little commercial sense for the indebtedness to remain entirely with LGDC after its fixed assets had been transferred to NSL. If the assets were to be shifted to NSL, the obvious step was to ensure that a substantial part of the indebtedness was also transferred to that company. When one further considers (1) that Mr Liu was specifically advised that a transfer of the assets to NSL at an undervalue would be open to challenge, (2) that the assumption of the debt by NSL cost Mr Liu and his family nothing, and (3) that Mr Liu was found by the Lord Ordinary to have an acute business intelligence, it would if anything be surprising if the consideration for the sale to NSL had *not* included the assumption of debts owed to the Liu family.

33. The Lord Ordinary's opinion demonstrates an awareness of this point, which appears to have eluded the Extra Division. At para 83 of his opinion, the Lord Ordinary said:

> "Although there are questions as to the timing of the letters of 5 December 1994 evidencing the Liu family loan, and equally of the 8

> December 1994 letter evidencing the Coquihalla loan, the fact of the loan itself was not challenged. *This is of the utmost importance in assessing much of the other evidence in the case.* It is clear that there was a loan from the Liu family in the total amount shown by the December 1994 letters. This is consistent with Mr Gardner's correspondence at the time. He may not have known of the breakdown of the loan between the various family members – and it is clear that he did not - but he knew that the loan to LGDC to enable it to purchase Letham Grange had been arranged by Mr Liu and came principally from Liu family sources." (emphasis supplied)

He later observed:

> "There is no doubt that he [Mr Liu] has an acute business intelligence. If Mr Gardner pointed out a possible problem with the sale, why would he not try to address that problem? Procuring that NSL, a family company, relieved LGDC, another family company, of part of its liability to repay loans to members of the family, cost him nothing." (para 88)

34. Those passages might be contrasted with para 101 of Lady Paton's opinion:

> "I should add that it is possible that the Lord Ordinary was influenced to some extent by his understanding that the original £2 million which was paid for Letham Grange in 1994 was said to be Liu family money. Nevertheless such a consideration, if well founded (and on the state of the evidence I reserve my position on that matter) does not affect the need to recognise the strong circumstantial case referred to in this opinion."

It appears from this passage that the Extra Division not only declined to accept the unchallenged evidence of the loans to LGDC (loans whose existence was also accepted on behalf of the liquidator before this court), but also failed to grasp its relevance to the case, including the question whether there was in fact a "strong circumstantial case".

The reason for the sale

35. As I have mentioned, Lady Paton gave five examples of the Lord Ordinary's dismissing or neutralising the parts of the evidence which constituted the component

parts of the circumstantial case advanced on behalf of the liquidator, without giving satisfactory reasons for doing so.

36. First, in relation to the reason for LGDC's selling the subjects to NSL rather than, for example, obtaining a further loan from the Liu family, Lady Paton was critical of a passage in the Lord Ordinary's opinion in which he stated:

> "I find the reason for the sale in 2001 to NSL somewhat elusive. As I have said, according to Mr Liu it was because the Coquihalla loan required to be repaid and LGDC did not have any money or the means of raising it. A loan from a family member or a third party might have been the answer, but without accountants Mr Liu could not properly record a loan in the books of the company. Therefore it was agreed to raise the money by selling the subjects to NSL. I find this explanation difficult to believe. The 1994 loans were not properly recorded originally, and there was no reason why an informal arrangement could not have been made. But ultimately this does not matter. The fact is that LGDC did sell the subjects to NSL, whatever might have been the true reasons for that. So the elusiveness of the reasons for the transaction do not impact upon this part of the story. A sale was arranged to NSL." (para 86)

Lady Paton comments (para 80):

> "On the contrary, the lack of a sound reason for the sale in 2001 was a highly significant piece of evidence which should have been kept in mind when assessing the overall picture (including credibility), rather than being dismissed at an early stage as unimportant."

37. I am unable to agree with this criticism of the Lord Ordinary. He began his discussion of the case by stating that it "turns on the credibility of Mr Liu" (para 81). He then listed a number of criticisms of Mr Liu's credibility which "were well made and, in an ordinary case (if there is such a thing) would likely be regarded as fatal to the defenders' case". These included "difficulty in seeking to understand the underlying purpose of the sale to NSL". This was one of a number of matters which were "formidable obstacles for the defenders to overcome" (para 82). It is clear, therefore, that he appreciated the significance of the absence of a clear explanation for the sale when assessing credibility.

38. The Lord Ordinary then considered the significance of the unchallenged and "overwhelming" evidence that there had been a loan from the Liu family to LGDC

in the total amount shown in the December 1994 letters. This he rightly described as being as "of the utmost importance in assessing much of the other evidence in the case" (para 83). That was so for a number of reasons. First, since that evidence was not in doubt, it provided a sound foundation for the assessment of the evidence which was disputed, in so far as it bore upon it. Secondly, as I have explained, it affected the inherent probability of Mr Liu's claim that part of the indebtedness of LGDC to the Liu family had been assumed by NSL at the time when the fixed assets of the former company were sold to the latter. Thirdly, it was also relevant to an assessment of the demeanour of Mr Liu and the manner in which he answered questions put to him by counsel for the liquidator: put shortly, if the loans were genuine, it followed that Mr Liu had a genuine grievance against the liquidator (who had previously declined to accept the Liu family's claims in the liquidation, and had in consequence avoided being removed from office), which could explain a reluctant and almost truculent manner.

39. In the light of his finding that the loans had been made in the amounts shown in the 1994 letters, and the implications of that finding which I have explained, the Lord Ordinary concluded his assessment of credibility by finding that Mr Liu was "endeavouring to tell the truth, so far as concerned the essentials of his case, and that the parts of his evidence that concerned those essentials could be relied on" (para 84).

40. Having made that crucial finding – after, as I have explained, taking account of the lack of a clear explanation for the sale to NSL – the Lord Ordinary then went through the history of events in chronological order. It is in that context that he again discussed the sale to NSL, in the passage which was criticised by Lady Paton. He had previously discussed in some detail the various questions which arose in relation to the reason for the sale (paras 77-79). He noted that Mr Liu was not cross-examined in depth on the rationale for the sale to NSL or on other ways in which the debt to Sanwa might have been repaid: Mr Liu "was not directly challenged along the lines that there was no commercial purpose" (para 76), "was never asked why [the £1.85m] could not have been advanced by way of a loan" (para 77), and "was not asked about this ['why NSL was introduced if it did not have the money to pay LGDC'] in any detail" (para 78). He also noted that "the reasons behind it [the fact that Foxworth did not assume the £1.85m debt] were not explored in evidence" (para 79).

41. In the context in which the passage in question appeared in his opinion, the Lord Ordinary was correct to say in para 86 that the reason for the sale did not matter. He had by then decided that the Liu family had lent over £2m to LGDC in 1994, and there was no doubt that LGDC had sold the subjects to NSL in 2001. What was important at that stage of the analysis was the amount of the consideration for the sale, and in particular whether it included the assumption of £1.85m of the loan. The answer to that question did not depend upon the reason for the sale, but essentially

upon the credibility of Mr Liu. In so far as the elusiveness of the reason for the sale bore upon Mr Liu's credibility, it had already been taken into account.

The claims in the liquidation

42. Lady Paton's second example of the neutralising of a piece of evidence was a comment made by the Lord Ordinary in relation to the claims submitted on behalf of the Liu family in the liquidation of LGDC, which did not initially take account of the assumption of part of the loan by NSL:

> "It seems to me to be perfectly possible that Mr Liu, in instructing his lawyers in that case, did not at that moment put two and two together so as to realise that the assumption of £1.85 million of the loan by NSL had the effect of reducing the debt due by LGDC to the family members." (para 91)

Lady Paton observed that Mr Liu had not himself put forward that explanation, and stated:

> "In my view, it is significant that Mr Liu … failed to discount the Liu family claims … This strand of evidence was important, and tended to suggest that the consideration given for Letham Grange had indeed been £248,100." (para 81)

43. The Lord Ordinary did not overlook the significance of this evidence. In his discussion of the matters adverse to Mr Liu's credibility, he said:

> "Most damning of all, perhaps, is the fact that when presenting a claim in the winding up and pressing his case in the sheriff court proceedings in 2003, Mr Liu instructed his lawyers as to the amount of the family loan outstanding to date without any hint of there having been an assumption of part of this debt by NSL. This was a crucial element in the calculation of the sums claimed in the winding up. If NSL had assumed part of the debt, the sums owing by LGDC would have been *pro tanto* reduced." (para 82)

44. When the Lord Ordinary referred to this matter again in the passage criticised by Lady Paton, he had by then concluded, after taking this matter into account, that Mr Liu was nevertheless a credible witness on the essential matters in dispute. The Lord Ordinary had also concluded, by that stage, that the assumption of the debt

formed part of the consideration for the sale. He then stated, in the earlier part of the paragraph criticised by the Extra Division:

> "In coming to this conclusion I have taken account of all the various criticisms of Mr Liu's evidence, including in particular his failure to take account of the assumption of the loan when first presenting his case … in the sheriff court proceedings" (para 91).

He need not have gone on to suggest a possible explanation for Mr Liu's failure to tell his lawyers about the assumption of the debt until 2003: at that stage of his analysis of the case, it did not matter. The fact that he suggested an explanation – one not entirely unrelated to Mr Liu's evidence that he was a busy man with business interests around the world (para 74) – does not vitiate his conclusion.

Changes in Mr Liu's position

45. Lady Paton's third example of the dismissal of a significant piece of evidence concerned changes in Mr Liu's account of what he had told Mr Gardner about the consideration for the sale. The Lord Ordinary, it was said, did not expressly refer to these changes, and appeared to take no account of Mr Liu's ultimate position that he deliberately did not tell Mr Gardner about the enhanced consideration (para 82).

46. I am unable to agree with this criticism. The Lord Ordinary set out in full the explanation given by Mr Liu in his witness statement, which he adopted as part of his evidence in chief. That included the statement:

> "It was agreed with each of my family members that liability to repay £1,850,000 of the total sum lent would be assumed by [NSL] *and I told Dan Gardner that*." (para 42)

The Lord Ordinary emphasised the final phrase. He then noted that, in cross-examination, Mr Liu gave evidence that he told Mr Gardner that NSL would assume responsibility for the loans, but did not tell Mr Gardner the amount of the loans or that the assumption of liability had already occurred. The Lord Ordinary noted that, in re-examination, Mr Liu said that what he had told Mr Gardner was that he would adjust the price to what was necessary. The Lord Ordinary returned to the point in his discussion of credibility, noting as one of the points made by counsel for the liquidator that Mr Liu "did not tell Mr Gardner in terms that the consideration for the sale included an assumption by NSL of £1.85 million of the Liu family debt owed by LGDC" (para 82). As I have mentioned, he later said that in coming to his conclusion he had taken account of all the criticisms of Mr Liu's evidence (para 91).

47. The Lord Ordinary was therefore aware that Mr Liu's position in relation to what he had told Mr Gardner changed during his evidence, and he took that into account. He clearly regarded it as significant that Mr Liu finally accepted that he had not told Mr Gardner that the loan had been assumed as part of the consideration. The changes in position were of course relevant to the credibility and reliability of Mr Liu's evidence. The Lord Ordinary discussed that matter fully, and acknowledged the strength of the points made. Nevertheless, as he said, "having seen Mr Liu over a considerable period in the witness box, and having heard him at length under persistent and skilful cross-examination", he formed the view that his evidence was credible and reliable so far as concerned the essentials of the case (para 84).

48. It is true that the Lord Ordinary did not refer expressly to a passage during Mr Liu's cross-examination, quoted by Lady Paton, in which he gave what appears to have been a rather emotional answer to the effect that the reason he had not told Mr Gardner that the debt had been assumed was because the deeds had already been prepared by then, and he felt that he would look like a fool if he asked for them to be corrected at that stage. There is however no reason to suppose that this passage in the evidence was overlooked, merely because it was not expressly mentioned. An appellate court is bound, unless there is compelling reason to the contrary, to assume that the trial judge has taken the whole of the evidence into his consideration: *Thomas v Thomas* 1947 SC (HL) 45, 61; [1947] AC 484, 492, per Lord Simonds; see also *Housen v Nikolaisen* [2002] 2 SCR 235, para 72.

The discrepancy between the 1994 and 1995 correspondence

49. Lady Paton's fourth example of the dismissal of significant evidence was the Lord Ordinary's treatment of the discrepancy between the letters of December 1994, attributing the loan to LGDC to four members of the Liu family, and the fax of 23 February 1995, where eight members of the family were mentioned. Lady Paton commented that the Lord Ordinary did not draw the "obvious" inference that the letters did not exist in 1994 or 1995, when the letters were not shown to Mr Gardner, or in 2002, when the letters were not found by the liquidator in the records of LGDC, but were compiled by Mr Liu for his own purposes. The Lord Ordinary "chose in effect to dismiss the potentially significant discrepancy" by "making the assumption that the money lent was all 'Liu family' money", and taking the view that nothing turned on whether the letters were written in 1994 or some time later (para 83).

50. The Lord Ordinary discussed at length the evidence relating to the December 1994 documents and the fax of 23 February 1995 (paras 35-37 and 54-56). I have already summarised some of that evidence. He noted fully the points made by counsel for the liquidator:

> "The originals of such letters had not been produced. No explanation had been given for this. Being written in English, they cannot have been intended primarily for the benefit of the members of the family, whose native language was Chinese and who had very little English. They must have been intended as a record of the loans to LGDC. Yet they were not passed to MacRoberts (who acted as company secretary) in 1994. They were not found in the books and records of the company at the commencement of the liquidation. Nor were they shown to Mr Gardner when he asked about the loans. Even when he asked for particulars of the loans, he was not told of these details. Indeed, in the early months of 1995 Mr Gardner was being told that the funds made available to LGDC had come from different lenders (including the family members) and in different amounts." (para 67)

51. The Lord Ordinary discussed the issue again when he considered the credibility of Mr Liu's evidence, stating that he accepted that there was some doubt about when the 1994 letters were produced, since they were not shown to Mr Gardner at the time of LGDC's purchase of Letham Grange in circumstances where one would one have expected them to have been shown to him had they been in existence at that time (para 82). But he also observed:

> "On the other hand, although there are questions as to the timing of the letters of 5 December 1994 evidencing the Liu family loan, and equally of the 8 December 1994 letter evidencing the Coquihalla loan, the fact of the loan itself was not challenged." (para 83)

52. The Lord Ordinary was correct to take the doubt about the date of the letters into account when assessing Mr Liu's credibility, as he plainly did: it was one of the "formidable obstacles" to be overcome. But he was also correct to identify as the central question whether the loan had been made, rather than whether particular evidence vouching the loan was all that it bore to be. In relation to that question, in the critical paragraph of his opinion, the Lord Ordinary observed that although there were questions as to the timing of the letters evidencing the Liu family loan, the fact of the loan itself was not challenged. It was clear that there was a loan from the Liu family in the total amount shown by the letters. As the Lord Ordinary explained, that was consistent with Mr Gardner's evidence and his correspondence of that time (para 83). The Lord Ordinary concluded, in relation to this chapter of the evidence:

> "I am satisfied that the loans were made by members of the Liu family to LGDC, in the amounts evidenced in the December 1994 letters, for the acquisition of Letham Grange. It is clear from the evidence that all decisions about this were effectively taken by Mr Liu. His family members relied on his advice. I am not persuaded that the split

> between the family members was necessarily decided upon by the time of the transaction (it will be recalled that different splits and, indeed, different lenders were mentioned at various times) and it may, therefore, be that the letters of 5 and 8 December 1994 were written and signed some time later. But nothing turns on this. The loans were made to LGDC and were enforceable according to the terms of the letters - the fact that letters are back dated does not invalidate them in so far as they purport to be a record of a transaction." (para 85)

53. Against the background I have described, the criticisms levelled at the Lord Ordinary in relation to this matter appear to me to miss their target. He considered the timing of the letters with care, particularly for the impact it might have upon the credibility of Mr Liu's evidence. The "obvious" inferences which he is criticised for failing to draw do not appear to me to be obvious. His "assumption" that LGDC's purchase of the subjects had been financed by loans from the Liu family reflected unchallenged evidence, which for some unexplained reason the Extra Division declined to accept. His conclusion that nothing turned on the date when the letters were written was one he was entitled to reach. In essence, his doubts as to the date of the loan letters, in a situation where the existence of the loans themselves was not challenged, did not cause him to conclude that the consideration for the subsequent sale of the subjects had not included the assumption of part of the debt resulting from those loans.

Brevity

54. Lady Paton's final example of the neutralising of a potentially significant strand of evidence is "the Lord Ordinary's brief reference to Mr Gardner's evidence about the disposition from LGDC to NSL". In the passage in question, the Lord Ordinary stated:

> "Mr Gardner gave evidence in detail about the disposition from LGDC to NSL in February 2001. The matter is covered in paras 15-27 of his witness statement upon which he elaborated in his oral evidence both in chief and in cross-examination. I do not need to set out that part of his evidence verbatim here." (para 57)

Lady Paton commented:

> "I consider, however, that the content of Mr Gardner's evidence relating to the 2001 disposition was significant and at times startling, painting a picture of a client (Mr Liu) who was not being

> straightforward with his own solicitor. While there might be no need to set out Mr Gardner's evidence verbatim, an indication of the content of his evidence would have presented a more balanced picture." (para 84)

55. Although the Lord Ordinary did not set out Mr Gardner's evidence relating to the disposition verbatim, he nevertheless gave not merely an indication of its content, but a detailed account of it, in paras 58-64 of his opinion. That account covered the aspects of this chapter of Mr Gardner's evidence which were most damaging to Mr Liu. These included (1) his not having told Mr Gardner that "J Michael Colby", whose signature appeared on the acceptance of the offer of sale, was himself; (2) his not having told Mr Gardner that liability for the £1.85m debt had been assumed as part of the consideration for the sale, and (3) his having in consequence misled Mr Gardner as to the amount of stamp duty payable (a matter which was subsequently rectified).

56. In the circumstances, I cannot see any substance in this criticism of the Lord Ordinary. His treatment of this chapter of evidence was not unbalanced, and did not indicate any failure to understand it or to take it into account. More generally, he gave careful consideration to the arguments and evidence adduced on behalf of the liquidator, and explained why he nevertheless concluded that the liquidator's case should be rejected.

57. I would add that, in any event, the validity of the findings of fact made by a trial judge is not aptly tested by considering whether the judgment presents a balanced account of the evidence. The trial judge must of course consider all the material evidence (although, as I have explained, it need not all be discussed in his judgment). The weight which he gives to it is however pre-eminently a matter for him, subject only to the requirement, as I shall shortly explain, that his findings be such as might reasonably be made. An appellate court could therefore set aside a judgment on the basis that the judge failed to give the evidence a balanced consideration only if the judge's conclusion was rationally insupportable.

Additional observations

58. The principles governing the review of findings of fact by appellate courts were recently discussed by this court in *McGraddie v McGraddie* [2013] UKSC 58; [2013] 1 WLR 2477; 2013 SLT 1212. There is no need to repeat what was said there. There may however be value in developing some of the points which were made in that judgment.

59. In the present case, the Extra Division cited earlier authorities of the highest standing. Lady Paton referred in particular to the well-known dictum of Lord Thankerton in *Thomas v Thomas* 1947 SC (HL) 45, 54; [1947] AC 484, 488:

> "The appellate court, either because the reasons given by the trial judge are not satisfactory, or because it unmistakably so appears from the evidence, may be satisfied that he has not taken proper advantage of his having seen and heard the witnesses, and the matter will then become at large for the appellate court."

As I have explained, Lady Paton found the reasons given by the trial judge to be unsatisfactory; and I have also explained why I take a different view.

60. Her Ladyship also cited a dictum from the opinion of Lord President Hamilton in *Hamilton v Allied Domecq plc* [2005] CSIH 74; 2006 SC 221, para 85, concerned with the situation where "findings of fact are unsupported by the evidence and are critical to the decision of the case". She considered that that test also was met in the present case (para 89). As this court explained in *McGraddie* at para 31, however, that dictum was concerned with the situation where a critical finding has been made which is unsupported by any evidence, rather than the situation where the appellate court disagrees with the overall conclusion reached by the Lord Ordinary upon the evidence. It was therefore not in point in the present case.

61. Lady Paton also cited the dictum of Lord Macmillan in *Thomas v Thomas* 1947 SC (HL) 45, 59; [1947] AC 484, 491, where, after mentioning some specific errors which might justify the intervention of an appellate court, his Lordship added that the trial judge may be shown "otherwise to have gone plainly wrong". As Lady Paton noted, that dictum was cited by Lord Hope of Craighead in *Thomson v Kvaerner Govan Ltd* [2003] UKHL 45; 2004 SC (HL) 1, para 16, where he also cited Lord Shaw of Dunfermline's statement in *Clarke v Edinburgh and District Tramways Co Ltd* 1919 SC (HL) 35, 37 that the duty of the appellate court was to ask itself whether it was in a position to come to a clear conclusion that the trial judge was "plainly wrong". Lady Paton considered that that test also was met in the present case (para 89).

62. Given that the Extra Division correctly identified that an appellate court can interfere where it is satisfied that the trial judge has gone "plainly wrong", and considered that that criterion was met in the present case, there may be some value in considering the meaning of that phrase. There is a risk that it may be misunderstood. The adverb "plainly" does not refer to the degree of confidence felt by the appellate court that it would not have reached the same conclusion as the trial judge. It does not matter, with whatever degree of certainty, that the appellate court

considers that it would have reached a different conclusion. What matters is whether the decision under appeal is one that no reasonable judge could have reached.

63. In *Thomas* itself, Lord Thankerton, with whose reasoning Lord Macmillan, Lord Simonds and Lord du Parcq agreed, said that in the absence of a misdirection of himself by the trial judge, an appellate court which was disposed to come to a different conclusion on the evidence should not do so "unless it is satisfied that any advantage enjoyed by the trial judge by reason of having seen and heard the witnesses could not be sufficient to explain or justify the trial judge's conclusion": 1947 SC (HL) 45, 54; [1947] AC 484, 487-488.

64. Lord du Parcq's speech is to similar effect. Distinguishing the instant case from "those very rare occasions" on which an appellate court would be justified in finding that the trial judge had formed a wrong opinion, he said:

> "There are, no doubt, cases in which it is proper to say, after reading the printed record, that, after making allowance for possible exaggeration and giving full weight to the judge's estimate of the witnesses, no conclusion is possible except that his decision was wrong." (1947 SC (HL) 45, 63; [1947] AC 484, 493)

65. Viscount Simon, while disagreeing as to the result of the appeal, also emphasised the need for the appellate court to consider whether the trial judge's decision could reasonably be regarded as justified:

> "If there is no evidence to support a particular conclusion (and this is really a question of law), the appellate court will not hesitate so to decide. But if the evidence as a whole can reasonably be regarded as justifying the conclusion arrived at at the trial, and especially if that conclusion has been arrived at on conflicting testimony by a tribunal which saw and heard the witnesses, the appellate court will bear in mind that it has not enjoyed this opportunity and that the view of the trial judge as to where credibility lies is entitled to great weight." (1947 SC (HL) 45, 47; [1947] AC 484, 486).

66. These dicta are couched in different language, but they are to the same general effect, and assist in understanding what Lord Macmillan is likely to have intended when he said that the trial judge might be shown "otherwise to have gone plainly wrong". Consistently with the approach adopted by Lord Thankerton in particular, the phrase can be understood as signifying that the decision of the trial judge cannot reasonably be explained or justified.

67. It follows that, in the absence of some other identifiable error, such as (without attempting an exhaustive account) a material error of law, or the making of a critical finding of fact which has no basis in the evidence, or a demonstrable misunderstanding of relevant evidence, or a demonstrable failure to consider relevant evidence, an appellate court will interfere with the findings of fact made by a trial judge only if it is satisfied that his decision cannot reasonably be explained or justified.

68. This approach is consistent, as I have explained, with the Scottish authorities, and also with more recent authority in this court and in the Judicial Committee of the Privy Council (see, for example, *In re B (A Child) (Care Proceedings: Threshold Criteria)* [2013] UKSC 33; [2013] 1 WLR 1911, paras 52-53, per Lord Neuberger). A similar approach has also been adopted by the Supreme Court of Canada (see *HL v Canada (Attorney General)* 2005 SCC 25; [2005] 1 SCR 401, paras 55-56) and by the United States Supreme Court (see *Anderson v Bessemer* 470 US 564 (1985), 573-574).

69. In the circumstances of the present case, in my opinion the Extra Division had no proper basis for concluding that the Lord Ordinary had misdirected himself or had failed to give satisfactory reasons for the factual conclusions which he reached on the evidence, or for concluding that he had gone plainly wrong. It follows that the appeal must be allowed.

Expenses

70. As I have explained, Foxworth and NSL had a cross-appeal which the Extra Division did not find it necessary to determine. The Lord Ordinary found the liquidator liable to Foxworth and NSL in the expenses of the action, but added a proviso that the order for expenses was not to be enforced without a further order of the court. In his opinion, the Lord Ordinary explained that the liquidator had been awarded expenses in the previous proceedings against NSL, and that the award had not been met. He was concerned that it might be unjust to allow Foxworth and NSL to enforce an order for expenses against the liquidator when the latter held an unsatisfied order for expenses in his favour in respect of the earlier action. It was unclear to the Lord Ordinary, at the time when he considered the matter, whether Foxworth and NSL were under the same control or beneficial ownership. The solution which he adopted was to add the proviso. He stated in his opinion that, at the hearing of any motion for an order allowing enforcement of the award, he would expect to be provided with information as to (a) whether the order for expenses in the first action had been satisfied, and if not, why not, (b) the ownership and control of the two companies, (c) whether there were any creditors of Foxworth with an interest to support or oppose the motion and, if so, the extent of their claims and the extent of the assets available to meet those claims, (d) whether any such creditors

supported or opposed the motion, and (e) anything else of relevance. The Lord Ordinary's order in relation to expenses was recalled by the Extra Division.

71. In the present appeal, counsel for Foxworth and NSL argued that, in the event that the Lord Ordinary's decision on the substantive issue were to be restored, his decision on expenses nevertheless should not be in so far as it contained the proviso. The question whether the payment of an award of expenses in favour of Foxworth could be withheld on account of NSL's failure to pay another award of expenses was governed by the law of compensation – which answered the question in the negative - and was not a matter of judicial discretion.

72. Questions in relation to awards of expenses in the Court of Session are generally best determined by that court. In discussion, it was accepted that no prejudice would be occasioned by remitting the question of the expenses of the proceedings in the Outer House to the Lord Ordinary. It was accepted that the non-payment by NSL of the award made in the previous proceedings can be considered and taken into account, along with all other circumstances relevant to the court's exercise of its discretion, at the stage when an award is made, obviating the potential difficulty raised in the cross-appeal.

Conclusion

73. I would accordingly allow the appeal and invite parties to make submissions as to the appropriate form of order.