



Neutral Citation Number: [2017] EWHC 737 (Ch)

Case No: HC-2016-002358

**IN THE HIGH COURT OF JUSTICE**  
**CHANCERY DIVISION**

Royal Courts of Justice  
Strand, London, WC2A 2LL

Date: 06/04/2017

**Before :**

**MR RICHARD MILLETT Q.C. (SITTING AS A DEPUTY JUDGE OF THE HIGH COURT)**

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**Between :**

**SDI RETAIL SERVICES LIMITED**

**Claimant**

**- and -**

**(1) DAVID KING**

**(2) PAUL MURRAY**

**(3) THE RANGERS FOOTBALL CLUB LIMITED**

**(4) RANGERS RETAIL LIMITED**

**Defendants**

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**Richard Hill Q.C. and Joyce Arnold (instructed by Reynolds Porter Chamberlain LLP) for the Claimant**

**William McCormick Q.C. and Ali Reza Sinai (instructed by Kingsley Napley LLP) for the Defendants**

Hearing dates: 22 March 2017  
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**Judgment Approved by the court**

**RICHARD MILLETT Q.C. (Sitting as a Deputy Judge of the High Court):**

**Introduction**

1. This is the hearing of an application made by the Claimant, SDI Retail Services Ltd, (“SDI”), dated 11 August 2016 for permission to continue its derivative claim made on behalf of the Fourth Defendant, Rangers Retail Ltd (“the Company”).
2. The application was made in respect of the claim by Claim Form issued on the same date and accompanied by a lengthy and detailed Particulars of Claim, and supported by a witness statement from Mr Henry Priestley, a solicitor with Reynolds Porter Chamberlain LLP. The First and Second Defendants (“Mr King” and “Mr Murray” respectively) are directors of the Company nominated to its board by the Third Defendant (“TRFC”). Mr Murray is a de jure director of TRFC. It is SDI’s case that Mr King is a shadow or de facto director of TRFC. Both Mr King and Mr Murray are directors (and in Mr King’s case chairman) of Rangers International Football Club PLC (“RIFC”), which wholly owns TRFC.
3. The Company’s business is to license, manufacture, distribute and sell products featuring the brands of Rangers FC, (“the Club”) the well known Glasgow football club operated by TRFC. That business is conducted by the Company pursuant to an intellectual property licence comprised in a written agreement between TRFC and the Company dated 27 January 2015 (“the IPLA”). This was a new version of a license agreement originally entered into in July 2012. Under the IPLA, TRFC granted the Company exclusive worldwide rights to use Rangers’ intellectual property and marks on TRFC’s retail products. The exploitation and enjoyment of the rights granted to it by TRFC under the IPLA was and is the Company’s sole business and its entire *raison d’etre*. But for the IPLA the Company has no business or purpose.
4. The Company is owned 49% by SDI and 51% by TRFC. Their relationship as shareholders in the Company is governed not only by the Company’s Articles of Association (“the Articles”) but also by a detailed written Shareholders’ Agreement between SDI and TRFC dated 31 July 2012 (“the SHA”).
5. In summary, the claim that SDI seeks to bring derivatively on behalf of the Company arises out of the purported termination of the IPLA by TRFC pursuant to its letter of 17 May 2016 in which TRFC alleged that the Company had committed various repudiatory breaches of the IPLA. SDI claims on behalf of the Company (in summary) declaratory and injunctive relief the effect of which is to maintain the IPLA on foot and to claim damages for breach of contract against TRFC and further to claim compensation from Mr King and Mr Murray on the grounds that in breach of their fiduciary duty to the Company they procured TRFC to purport to terminate the IPLA.
6. The application comes before me pursuant to a Consent Order dated 13 October 2016 under which Chief Master Marsh directed that there be no consideration of the application on paper pursuant to CPR 19.9A(9) but that there be an oral hearing of SDI’s application for permission to continue the derivative action. This case has therefore not been subjected to the *ex parte prima face* case stage contemplated by s. 261(2) of the Companies Act 2006 (“the 2006 Act”) but has proceeded directly to the oral hearing provided for by s. 261(4) of the 2006 Act.

### **The factual background**

7. I take the factual background from the evidence contained in the witness statements, namely those of Mr Priestley and Mr Cran (solicitors for SDI) and the witness statements of Mr King and Mr Murray for TRFC and themselves. I also have a witness statement from Mr James Blair, the company secretary of TRFC, whose evidence relates to a specific issue which did not feature in the arguments on the application, but whose role in the events is a relevant consideration.
8. SDI is part of the well known Sports Direct group, headed by the equally well known Michael Ashley. In 2012 TRFC (then called Sevco Scotland Ltd) approached the Sports Direct group about potential business opportunities. That led to the Company being incorporated, with SDI holding 49% as A shareholders and TRFC holding 51% as B shareholders. The role of SDI was to manage the Company's day to day business utilising and exploiting its contacts and distribution channels and resources of the Sports Direct group.
9. The commercial agreements were structured through a series of agreements principally the SHA, IPLA and the Articles. The SHA was entered into at the same time as the original license agreement (defined in the SHA as the "IP License Agreement") which the IPLA later replaced.
10. The SHA, by clause 5, requires that the only business be the Business as defined, which is the carrying out the Licensed Activities, namely the exploitation of the rights granted to the Company under the IPLA. Among other things clause 5 (by clause 5.3 and schedule 3) imposes the responsibility for managing and operating the business of the Company on SDI. The SHA also contains provisions relating to Events of Default, deadlock and other matters relating to corporate governance. The Company is not a party to the SHA.
11. So far as the IPLA is concerned the important provisions are clause 3 (under which TRFC granted the Company exclusive rights), clause 5 (dealing with official Rangers kit and replica kit), clause 10 (the general obligations of the Company under the IPLA), clause 12 (the kit launch program) and clause 20 (the applicable law and jurisdiction clause).
12. The most significant revenue stream is derived from the Rangers replica kit which is designed and manufactured on a yearly basis and purchased in large numbers by the Club's supporters. Revenue is also generated by branded fan-wear and night-wear.
13. As I have already said, the Company has, and could have, no other business other than the right to exploit the rights granted to it under the IPLA, without which it would not be able to continue as a going concern. That much is clear from the terms of the SHA which define the Business of the Company as carrying on the Licenced Activities as defined in the original licence agreement (which was replaced by the IPLA).
14. After the initial arrangements were agreed in 2012 TRFC found itself in increasing financial difficulty. The Sports Direct group agreed to provide financing to TRFC which in turn led to the granting of credit facilities and an interest free loan by other companies in the Sports Direct group, by various agreements entered into between October 2014 and early 2015. In March 2015 there was a change in the control of TRFC and its holding company with the result that Mr King and Mr Murray became directors of the Company, on 4 June and 9 March 2015 respectively. They were

nominated by TRFC to the Company's board pursuant to its rights under the Articles and the SHA.

15. Mr King is also the director and Chairman of RIFC, which is the 100% parent company of TRFC, and has been so since 18 May 2015. He and his family are also said to be the ultimate beneficial owners of some 14.57% of the shares in RIFC. Mr Murray is also a director of RIFC, as he has been since 6 March 2015. The other directors of the Company, nominated by SDI, are Mr Barnes since 3 June 2016 and Nigel Conway since 13 June 2016. They replaced SDI's previous nominated directors Mr Ashley and David Forsey.

#### **The lead-up to the purported termination of the IPLA**

16. SDI's principal allegation in this case is that the termination of the IPLA by TRFC was invalid, and it seeks to protect the Company's business from utter destruction by challenging it since the Company cannot itself do so because of the stance taken by Mr King and Mr Murray as directors.
17. It is SDI's case that from the start of their involvement TRFC and Mr King in particular have sought, in alleged breach of fiduciary duty, to denigrate the commercial arrangements between the Club and the Sports Direct group with a view to renegotiating them. It is important background that throughout 2015 and into 2016 the Club's supporters promoted a boycott of the Company's products with the result that the Company's revenues began to decline. The Court is reminded that the boycott started in November 2014. It is also SDI's case that the purported termination of the IPLA by TRFC in May 2016 was not only invalid on its merits but also formed part of a wider collateral strategy, in parallel to the supporter boycott, to force the Company to renegotiate the IPLA on terms that were more appealing to the Club and its supporters.
18. I must make it plain that this is not the trial of the action and that this hearing is not a mini-trial. My use of the word "purported" to describe TRFC's termination of the IPLA is not to be taken as any indication that I have formed a view that it was invalid. Nor is anything in this judgment to be taken as a final decision on any matters which are properly for the trial judge. However, I must consider the factual background leading up to the purported termination of the IPLA because it is relevant to the questions that I do have to decide in order to assess whether the statutory tests which would permit the action to continue are met.
19. On the evidence I have seen, the supporter boycott went hand in hand with repeated public calls by Mr King and Mr Murray for the renegotiation of the commercial relationship between SDI and TRFC (namely the IPLA). I was shown some examples of the evidence. It makes striking reading. For example:
  - (a) The Daily Record of 10 April 2015 quoted Mr Murray as saying "*as you know we are looking into all the contractual relationships with Sports direct – we have been doing it for a month now*".
  - (b) The directors of TRFC made a statement to shareholders on 3 June 2015 referring to the supporter boycott and saying "*the Directors are firmly of the view that the best interests of both the Club and Sports Direct require them to engage with supporters and restructure the existing contractual engagements in a manner*

*which is clear transparent and fully accessible to those who would be the purchasers of the Club's merchandise".*

- (c) In an interview with Mr King published on the Club's website on 9 June 2015 he said *"one of the things that we are looking at is renegotiating the commercial terms of the retail operation"*, which would *"allow us to announce to the fans that we now have an arrangement in place that is going to be good for the Club and from buying from retail and supporting the other commercial operations that the money is coming back into the Club"*.
- (d) On 4 February 2016 Mr King made a statement to the effect that he would *"get redress and compensation for the poor commercial and business practices that the Club has been forced to endure"*, which then prompted a Rangers FC Fan Group to say to the press that *"the Club have basically said that this is a terrible deal, which is the first time the Club have said anything officially about it on the website. We can now justifiably say to Rangers fans that the Board don't even want the deal."*
- (e) On the 7 March 2016 TRFC published on its website a statement entitled *"Dave King Statement – One Year On"* in which Mr King is recorded as having said *"we have now had sufficient time to analyse the voluminous documentation supporting the establishment of the numerous agreements and side agreements with Sports Direct. Discussions have commenced with our legal advisors to review our findings and to devise the most effective legal strategy. This will be presented to the Board for approval at the end of this month... it remains possible that the seemingly inevitable lengthy and costly litigation can be avoided. There is a far better alternative if Sports Direct recognises that the present arrangements are not working for either party and agrees to renegotiate the present arrangements..."* He went on to say: *"it would be an immediate boost for Rangers if the Board can be put into a position to endorse a revised deal prior to the launch of new kit for the coming season"*.
- (f) The supporters' boycott was promoted by, among others, Club 1872 Ltd. This is a group of Rangers supporters' groups. On 3 August 2016 Club 1872 Ltd released a statement urging supporters not to purchase the replica kit sold by the Company. The Company Secretary of TRFC, Mr James Blair, is and was at the time a Director of Club 1872 Ltd. He has provided a witness statement on this application on behalf of the Defendants and is a partner in Anderson Strathern LLP, Scottish solicitors, who act for TRFC, RIFC and Mr King. All of this strongly suggests, at the very least, that the supporter boycott was not merely being tolerated by TRFC and Mr King in particular but actively approved and promoted by it and by him.
- (g) Finally, at TRFC's AGM on 26 November 2016 a member of Club 1872 Ltd asked the following question which was reported by the press on Twitter and a live blog, along with Mr King's response, as *"Q: can fans do anything to assist Mike Ashley's situation?" DK: maybe better to say what fans should continue not doing"*. Mr King's statement was hardly cryptic. His barely concealed hint was that the fans should continue their boycott of the Company's goods, and hence of the Company's business.

20. Mr King does not deny in his evidence that he made this statement nor has tried to explain it, nor to challenge or explain any of this evidence. He does not accept that he has failed to promote the interests of the Company or that he is favouring the interests of TRFC but instead has sought to place the blame for the continuing boycott on SDI and its appointed directors; and he criticises SDI for failing to make any suggestion as to how the boycott might be lifted or mitigated. It is clear to me from the evidence I have seen and Mr King's response to it that there is, at the least, a strongly arguable case that Mr King has personally endorsed and encouraged the continuation of the supporter boycott in the interests of the Club and TRFC and at the expense of the Company.

#### **The purported termination of the IPLA**

21. At the beginning of 2016, TRFC served a Notice to Terminate the IPLA in accordance with its clause 15.1, which provides that either party may terminate by 7 years' notice in writing. There is no dispute about the validity of that notice. The IPLA will therefore terminate at the beginning of 2023.
22. On 17 May 2016 TRFC served a Notice purporting to terminate the IPLA for breach of contract. It was signed by Stewart Robertson as Managing Director of TRFC on behalf of TRFC. It made numerous allegations of breach of various provisions of the IPLA. The letter stated in terms that "*there is no obligation on us to identify any specific breach upon which we do or may subsequently rely in support of our termination of the agreement and we continue to investigate your conduct in this regard. However, without prejudice to the foregoing we identify below some of the breaches upon which we shall rely, reserving our right to rely upon any other breaches that have occurred*". There then followed allegations of breach of Clauses 5.8, 5.9, 7.5, 10.1.1, 10.1.3, Clause 12, and 10.1 and of an implied term that "*you would take all reasonable steps to protect and promote the value of the Rangers Rights (as defined in the IPLA)*". The letter went on to say (at paragraph 10) that the breaches amounted to a repudiation or renunciation of the IPLA which TRFC purported to accept with the result that the IPLA was discharged. TRFC reserved its rights to claim damages for breach of contract.

#### **The aftermath of the purported termination of the IPLA**

23. On 19 May 2016 Mr Forsey, then a director of the Company, responded on behalf of the Company saying that a substantive response would follow, denying that there was any basis for termination and saying that the purported termination itself amounted to a repudiation of the IPLA, which the Company did not accept. It is questionable, in the absence of a board meeting, to what extent Mr Forsey had actual authority to send that letter on behalf of the Company, but it must be arguable that he had usual or implied authority to do so as a director, given that its purpose was to protect the Company's sole asset, namely the rights under the IPLA.
24. On 20 May 2016 Reynolds Porter Chamberlain LLP, solicitors for SDI, wrote on behalf of SDI to TRFC warning it that it may be necessary for the Company to sue it and asking for its consent (should it be needed) to do so pursuant to clause 12 of the SHA (to which I shall return later).
25. On the same day TRFC responded refusing such consent and saying that the decision whether or not to embark on or threaten litigation is one which should be taken by the board of the Company on the basis of a "*proper analysis by the Board of the factual*

*history as to the performance by [the Company] of its obligations under the [IPLA]. Our appointed Directors are just as entitled as are yours to a full and complete account of that factual history so that they can make an informed decision in their exercise of their fiduciary duties to the Company...".* Pausing there, I should record that neither Mr King nor Mr Murray denied that they were involved in the decision by TRFC to send the purported termination notice; and I have seen no evidence to support any such suggestion. It seems to me at the very least arguable that they were involved in it or at least knew of and approved it. In those circumstances the statement that they could only make a decision that the Company should pursue a litigation challenge to the purported termination notice on the basis of a "*proper analysis of the factual history*" was to my mind cynical and disingenuous. Mr King and Mr Murray were not neutrals. They cannot credibly say (and in fairness do not go so far as to say) that they knew nothing of TRFC's purported termination of the IPLA or the decision-making at TRFC which led to it. It is notable that in that letter TRFC did not offer any solution to the obvious conflict that had arisen.

26. On 27 May 2016 SDI wrote a lengthy and detailed letter purporting to rebut the allegations in the purported termination letter and demanding that the allegations be withdrawn. The letter went on to invite TRFC to agree that if the issue of the validity of the termination could not be resolved between them then it would be determined by the Court on an expedited basis as between TRFC and the Company and that in the interim the IPLA should be treated as remaining on foot.
27. TRFC responded on 1 June 2016 accusing SDI of mounting a proxy defence of the Company, taking the position that the 27 May letter was not from the Company and the Company was yet to respond. Although this was true, this was, I regret to say, another cynical and disingenuous statement by TRFC. The very reason why the Company could not respond for itself was because TRFC's own appointed directors (Mr King and Mr Murray) were taking the position that they needed to be satisfied, based on a full factual and legal investigation, that the Company had a real defence to the purported termination. Indeed, TRFC's letter of 1 June went on to say that "*the first step must be for the [Company's] Board to be given the factual position so that the decision as to the wisdom of embarking on any course can be taken in the light of the true and complete facts*". This was a posture. Mr King and Mr Murray must have known the basis on which TRFC had purported to terminate (or else could easily find out), and must have considered either (i) that it was justified on the facts as alleged by TRFC or (ii) that it was not. The idea that the validity of the purported termination depended on an analysis of facts not known to TRFC, Mr King and Mr Murray is, to put it mildly, a stretch. Moreover, given that the choice for the Company was to defend against the purported termination or go out of business, their expressed position of ignorance about the merits of the termination so that the Company could not do anything without knowing "the factual position" was itself a position in conflict with the Company's best interests.
28. Even by this early point it ought to have been obvious to all Defendants that Mr King and Mr Murray's positions as directors of the Company were hopelessly conflicted. On the other hand, the positions of the SDI-appointed directors to the Company's board were more closely aligned with the interests of the Company. It may very well have been the case that the business of the Company relied upon relationships with other entities in the Sports Direct group which were disadvantageous to the Company. That is a point of which Mr King makes much in his evidence, and much was made by Mr McCormick QC in his submissions on behalf of the Defendants. However, even if that

were so, it ought not to have disabled the Company's board from seeking to uphold the IPLA and thereby protect its sole asset and revenue stream. The relevant comparator was between an allegedly disadvantageous IPLA and no IPLA at all, and *ergo* no business at all for the Company.

29. Notwithstanding the position taken by Mr King and Mr Murray as directors of the Company, TRFC (and Mr King and Mr Murray) conducted themselves at all times on the basis that the IPLA had been validly terminated. They pursued what Mr Hill Q.C., for SDI, referred to as a two-fold strategy. First, they continued to thwart the Company in its ability to respond to the purported termination notice by Mr King and Mr Murray taking the position that they needed information, both in correspondence in May and June and at the 29 June 2016 board meeting, which I address below.
30. Secondly, they interfered with the commercial relationships established between the Company and third parties. Specifically Mr King told Puma, one of the most important of the Company's sub-licensees, that it should not supply the Company. It seems that at a meeting on 17 June 2016 between Puma and Mr Barnes (by now a Director of the Company) Puma (through its Mr Spencer) told Mr Barnes that Mr King had asked Puma to novate the agreement between the Company and Puma to TRFC. Mr King has not denied that evidence or explained what happened.
31. In addition, TRFC also wrote to other sub-licensees on 1 June 2016 telling them that they no longer had a valid sub-licence to sell Rangers branded products and asking them instead to telephone TRFC's Managing Director to discuss a direct licencing arrangement between TRFC and the relevant sub-licensee. Neither Mr King nor Mr Murray has sought to deny this evidence or their involvement in or knowledge of these events.
32. The fact that TRFC was proceeding by 1 June 2016 unequivocally on the basis that the IPLA was at an end serves to support further my conclusion that the position taken by TRFC in its 1 June 2016 letter, that its appointed Directors to its Company's Board needed all the facts in order to work out if the termination was valid, was a posture. The suggestion that Mr King and Mr Murray were genuinely taking a position that was anything other than wholly aligned with that of TRFC in its dispute against the Company is not credible. Mr McCormick submitted (at [75] of his skeleton) that "any sensible director" would, when the question whether the Company should sue TRFC for breach of contract was asked, seek a full explanation as to why TRFC was wrong to allege the breaches of the IPLA it did. That submission presupposes that such a "sensible director" was wholly unconnected with TRFC and the purported termination of the IPLA and was able to bring an independent mind to bear, acting with single-minded loyalty to the Company. Mr King and Mr Murray were simply not in that position. Mr McCormick's analogy, beguilingly simple though it is, is false on the facts of this case so far available.
33. A board meeting took place on 29 June 2016 at which these conflicts were discussed. Mr King and Mr Murray insisted on having full information about the background to the Company's proposed response to the termination. The SDI-appointed director refused to provide it. Mr King and Mr Murray for their part complained that they were being hampered in taking a decision and denied any conflict of interest, complaining instead that the Company's dealings operated unfairly to the advantage of the Sports Direct group and to the disadvantage of the Company, and by extension, the Club. This



approach, whereby the Company was simply a “look-through” and the real relationships were as between the Club and Mike Ashley, underpinned not only the Defendants’ conduct but the whole approach to the role of the Company taken by the Defendants before me.

34. The deadlock that had arisen was, as far as I can see, entirely due to the stance taken by Mr King and Mr Murray. In simple terms, there was no reason why the Company should provide Mr King and Mr Murray with the detailed material with which the Company was going to rebut the allegations made by TRFC, particularly in circumstances where the decision that Mr King and Mr Murray were required to make would, properly analysed, not need that information and where there was nothing to stop Mr King and Mr Murray reporting straight back to TRFC (as, indeed, clause 8.6 of the SHA entitled them to do).
35. These proceedings were then commenced in August 2016, supported by Particulars of Claim and the detailed witness statement of Mr Priestley.
36. On 19 September 2016, Kingsley Napley LLP (who had said in their letter of 2 September 2016 that they acted for TRFC) wrote a lengthy letter on behalf of TRFC (and possibly for Mr King and Mr Murray too) (“the 19 September letter”) comprising some 11 pages and thirty headline questions and sub-questions, and requesting access to numerous documents and records. In the event, TRFC (through Mr Blair) was afforded access to the Company’s financial records. The 19 September letter stated that the information was needed by Mr King and Mr Murray in order to decide whether the Company should contest the purported termination. Kingsley Napley LLP said that *“neither [Mr King nor Mr Murray] has decided that [the Company] should not make a claim.”*
37. The fact that Kingsley Napley LLP were able both to act on behalf of TRFC and yet to demand the information in order for Mr King and Mr Murray to decide as directors of the Company whether the Company should sue TRFC simply underscores not only the self-evident conflict of interest they had but the hollowness of the stated need for the information. It was the continuation of the self-same posture adopted by Mr King and Mr Murray from the outset. The 19 September letter, if nothing else, demonstrates that Mr King and Mr Murray were not genuinely taking a position that was anything other than wholly aligned with that of TRFC. Mr Hill Q.C.’s observation in his oral submissions that Kingsley Napley LLP acts in this litigation for TRFC, Mr King and Mr Murray is well made. There is clearly no conflict between them, and never was.
38. I also reject Mr King’s suggestion at [23] of his witness statement that “both sides are equally conflicted”. Although it may well have been more to SDI’s advantage than to TRFC’s that the IPLA continue, that is to ignore the position of the Company. It is unquestionably not to the advantage of the Company that its entire business should be terminated.
39. On close examination of the 19 September letter, when one tries to tie the questions back to the allegations in the purported termination letter, it is clear that the vast majority do not actually relate to complaints forming the basis of the purported termination of the IPLA at all, but rather were questions more broadly designed to test whether or not SDI had mismanaged the Company in breach of its obligations under the SHA. The questions were not being asked for the further education of Mr King and Mr Murray as directors of the Company but in order to fore-arm TRFC in a battle against

SDI under the SHA. That issue has now become crystallised in TRFC's own action, to which I refer below. Suffice it to say that I am not concerned with the merits of that claim, but merely (as I touch on later) whether it provides a suitable procedural framework for the vindication of the Company's own claims to challenge the purported termination of the IPLA.

40. Although the 19 September 2016 letter does contain some questions going to the details of the Company's response to the purported termination of the IPLA (principally about clause 12 and sub-licenses), most of the questions were fishing for information which might indicate further breaches (for example questions 25 and 27). Strikingly, one of the questions was about what steps SDI and its appointed directors had taken to end the supporter boycott (question 18). Given the apparent encouragement given by Mr King and Mr Murray to the supporter boycott, that question was rich indeed. It also ignores the fact that there was no obligation under the IPLA to stop the supporter boycott, and none was identified.

### **The TRFC action**

41. On 17 February 2017 Kingsley Napley LLP wrote to SDI on behalf of TRFC alleging that SDI was in repudiatory breach of the SHA and purporting to accept the repudiation and terminate it. The same day, TRFC commenced proceedings ("the TRFC action") against SDI in respect of the alleged breaches, which principally concern allegations that in breach of clause 5.3 of the SHA SDI failed to manage the business of the Company in accordance with the contractual standards imposed on SDI. Although the parties agreed an extension for SDI's defence and counterclaim, this was not sought or granted on the basis of the outcome of this application. The parties have agreed that SDI's Defence in the TRFC action should await the outcome of this application. The relevance of the TRFC action to this application is that the Defendants say that these derivative proceedings should not continue on their own separately but can and should be brought as part of the TRFC action. I return to this subject below.

### **The statutory tests**

42. Against that background, I can turn to the statutory tests which govern the continuation of derivative proceedings such as the present.

#### **(1) S. 260(3)**

43. S. 260(3) of the 2006 Act provides:

A derivative claim under this Chapter may be brought only in respect of a cause of action arising from an actual or proposed act or omission involving negligence, default, breach of duty or breach of trust by a director of the company.

44. A shadow director is treated as a director for this purpose: s. 260(5)(b).
45. It is not disputed that Mr King and Mr Murray were involved in the decision by TRFC to purport to terminate the IPLA. Indeed, they have given evidence about why this was thought to be desirable. Mr King admits that he publicly stated that the IPLA needed to be renegotiated. His position is that renegotiation of the IPLA would be in the Company's best interests because it would end the supporter boycott and improve the

Company's profitability (see King at [37]). With respect, I find that a little unreal. If what Mr King had really wanted was an end to the boycott, he would have called for it. He did rather the opposite. If he had had the best interests of the Company at heart, he would have sought a renegotiation between the Company and TRFC, in which he and Mr Murray could not have been involved, while the IPLA was still extant. The whole point of terminating the IPLA was to force the Company to renegotiate (if that is really what Mr King wanted) from a position of weakness.

46. The allegations of breach of fiduciary duty on the part of Mr King and Mr Murray are clearly pleaded in the Particulars of Claim. They include involvement in TRFC's decision to purport to terminate the IPLA, the refusal to sanction action by the Company, and the actions taken by TRFC vis-à-vis third parties after the purported termination that I have referred to above. It is plain to me that the action arises squarely out of an alleged breach of duty by Mr King and Mr Murray.
47. The Defendants relied on Article 9.1 and 9.2 of the Company's Articles to contend that the fiduciary duties of Mr King and Mr Murray were attenuated such that what they did or did not do was not a breach of their fiduciary duty. Articles 9.1 and 9.2 read as follows:

**"Directors' conflicts of interest**

9.1 Subject to Article 9.2, notwithstanding the fact that a proposed decision of the directors concerns or relates to any matter in which a director has, or may have, directly or indirectly, any kind of interest whatsoever, that director may participate in the decision-making process for both quorum and voting purposes.

9.2 If the directors propose to exercise their power under section 175(4)(b) of the Companies Act 2006 to authorise a director's conflict of interest, the director facing the conflict is not to be counted as participating in the decision to authorise the conflict for quorum or voting purposes."

48. Articles of association of joint venture companies do commonly contain provisions whereby an appointed director is permitted to prefer the interests of his appointor shareholder to those of the company. Articles 9.1 and 9.2 are not of that type. They are not a broad release from or waiver of fiduciary duties to the Company. At best, they permitted Mr King and Mr Murray to participate in a decision of the Company notwithstanding that they might have any kind of interest in it (not necessarily in conflict with the Company), and always anyway subject to Article 9.2 which disabled them from voting on or authorising their own conflict. That is as far as these provisions go. It does not relieve them from any of the statutory or equitable obligations to act bona fide and in the best interests of the Company.
49. The Defendants also submit that although s. 260(3) permits the claims against Mr King and Mr Murray (subject to the point about Article 9) it does not permit the claim against TRFC. For that they rely on a passage in Iesini v Westrip Holdings Ltd [2010] BCC 420, at [75] and [79]. There Lewison J, citing the Law Commission Report on Shareholders' Remedies, said that the section did not permit a derivative claim to be brought by a shareholder in the name of the company against a third party where the claim depends on a cause of action which has arisen independently of the director's default. The example given by the Law Commission was where the directors refused, for ulterior motives of their own, to procure the company to bring the claim against a third party who had committed a tort against the company. In my judgment that is not

this case. Here, the claim against TRFC does not arise at all independently of the default alleged to have been committed by Mr King and Mr Murray. On the contrary, the act by TRFC in purporting to terminate is pleaded as a breach of fiduciary duty on their part, as are TRFC's dealings with third parties such as sub-licensees and PUMA post-termination on the footing that the IPLA had terminated. Their refusal to sanction the bringing of a claim by the Company was a further alleged breach of fiduciary duty intimately connected with those other breaches, and could be said to be a continuation of those breaches.

50. In my judgment, on the allegations contained in the Particulars of Claim, s. 260(3) is amply satisfied.

(2) S. 262(3): mandatory bars to permission

51. S. 262(3) provides for mandatory bars to the grant of permission to bring a derivative action, which any applicant such as SDI must surmount.

(2) Permission (or leave) must be refused if the court is satisfied—

(a) that a person acting in accordance with section 172 (duty to promote the success of the company) would not seek to continue the claim, or

(b) where the cause of action arises from an act or omission that is yet to occur, that the act or omission has been authorised by the company, or

(c) where the cause of action arises from an act or omission that has already occurred, that the act or omission—

(i) was authorised by the company before it occurred, or

(ii) has been ratified by the company since it occurred.

52. Ss. 2(b) and 2(c) are not in issue. Ss. (2)(a) is disputed. It is well established that to stop the action in its tracks the court must be satisfied (i.e. that the burden lies on the Defendants to show) that no director acting in accordance with section 172 of the 2006 Act (under the duty to promote the success of the company) would seek to continue the claim: see Iesini v Westrip Holdings Ltd (supra) at [86]. The test is an objective one, using the hypothetical director. I am very far from satisfied that no director doing his duty under section 172 would seek to continue the action. I will return to the merits and the size of the claim below, but the simple reason, in short, is that it is at least arguable (I need put it no higher than that) that the purported termination of the IPLA was invalid, and that not to contest the validity of that purported termination would spell the certain end of the Company's entire business. The hypothetical director would only refuse to continue the action if it was incontestable that the IPLA had been validly terminated. In addition, the Company will not have to spend its resources disputing the validity of the termination because SDI has offered to fund the Company's claim and indemnify the Company against any costs orders that may be made against it (although it is hard to see what costs orders could be made against it).

53. Mr McCormick's main point was that no director would seek to continue the action, doing his duty under s. 172, with this degree of paucity of information. SDI, having deliberately refused to provide a full set of answers to the questions asked by Mr King,

Mr Murray and TRFC, has, he says, only itself to blame for the information deficit. I reject this submission. As I have already said, the quest for information was a posture. Mr King and Mr Murray are not in an analogous position to the hypothetical director. The true question is whether the objective hypothetical director (i) reading the SDI letter of 27 May 2016, the Particulars of Claim and Mr Priestley's witness statement, (ii) knowing that the Company's challenge would be entirely funded by SDI, and (iii) knowing that the result of not challenging the purported termination is the instant destruction of the Company's whole business, would refuse to countenance the claim. There can in my judgment be only one answer: no.

54. The only point that gave me serious pause was clause 12.1(n) of the SHA. This provides as follows

*"The Shareholders hereby agree that, subject to 12.3, they shall procure that the Company shall not take any action outside the ordinary course of business and shall not, without the consent of all Shareholders:*

*...*

*(n) institute any litigation, arbitration or other similar proceedings;*

*12.3 Clause 12.1 shall cease to apply immediately upon an Event of Default (as defined by clause 16.1) and shall continue to cease to apply unless and until otherwise agreed with the Non-Defaulting Shareholder ..."*

55. By clause 16.1(h) an Event of Default occurs where "the IP License is validly terminated."
56. There is no question of clause 12.1 being disapplied by clause 12.3 and the occurrence of an Event of Default constituted by the termination of the IPLA since the position of both parties is diametrically opposite to where each side wishes to go. SDI says that the termination is invalid (and so clause 12.1(n) is still operative) and the Defendants say it was valid, thus removing at one stroke the whole foundation of their very objection based on this provision. The SHA does not cater for what happens if the validity of the termination is contested. However, the answer for present purposes need not turn on whether clause 12.1 is or is not disapplied by clause 12.3. The whole point and purpose of the Company, and the concomitant shareholder relationships governed by the SHA, is the Company would exploit the rights granted to it under the IPLA. It cannot sensibly have been the intention of the parties that where the IPLA was terminated by TRFC the Company would have no ability to challenge it. I have noted that the Company is not a party to the SHA, and therefore it did not itself agree to give up all rights of suit against the world, including its own directors or TRFC.
57. It is true that on the plain words of the provision SDI and TRFC agreed that the Company cannot bring any action without the mutual agreement of the shareholders. Mr Hill sought to construe these words as limited to claims against third parties and not against TRFC or the directors of the Company. Although I see much sense in that construction the words used cannot take me there. I paraphrase Lord Neuberger in Arnold v Britton [2015] AC 1619 at [15]: commercial common sense is no substitute for the language used by the parties; the court cannot rewrite the bargain and if it is a bad bargain, so be it. That said, I am also bound not to blinker myself to the

commercial context. As the Supreme Court has very recently found it necessary to state yet again, in Wood v Capita Insurance Services Ltd [2017] UKSC 24, at [13],

“Textualism and contextualism are not conflicting paradigms in a battle for exclusive occupation of the field of contractual interpretation. Rather, the lawyer and the judge, when interpreting any contract, can use them as tools to ascertain the objective meaning of the language which the parties have chosen to express their agreement. The extent to which each tool will assist the court in its task will vary according to the circumstances of the particular agreement or agreements.”

58. What this means in simple terms is that the court must balance literalism, factual background and common sense in equal measure as best it can. Here the solution is not to be found in Mr Hill’s restrictive rewriting of sub-clause (n) but in standing back and seeing the clause as a whole in the context of the wider commercial relationship. The parties agreed between themselves that they would not procure the Company to sue. But the Company is not suing anyone. SDI is suing, as claimant, to vindicate a claim by the Company for alleged damage done to it. The interesting debate under the old common law as to whether the derivative action is a representative action brought in reality by the company has no place after the codification of this part of company law in 2006 and Mr McCormick did not press the point.
59. I do not read clause 12.1(n) as an agreement between the shareholders that no derivative actions would be brought. Mr McCormick’s submission amounted, as he appeared to accept and indeed asserted, to saying that the Company was merely a look-through with no real corporate personality of its own separate from its shareholders and its interests could effectively be ignored. I cannot accept that submission. The terms of (indeed the need for) the SHA are inconsistent with it, and it goes against the whole point of having TRFC grant rights under an arm’s length contract to the Company. A proper balance between “textualism” and “contextualism” produces a reading of the SHA that respects rather than ignores the separate corporate personality.
60. Moreover, it is important to read the SHA together with the IPLA since the whole purpose of the SHA was to regulate the relationships between the shareholders of the Company, whose sole business was to operate and enjoy the IPLA. The IPLA contains, at clause 20.1, an applicable law and jurisdiction clause in wide form, covering “any dispute or claim arising out of or in connection with” the IPLA or its subject matter or formation, including non-contractual disputes or claims. If clause 12.1(n) was a total bar on the Company suing TRFC for breach of the IPLA, or vice versa, without the consent of TRFC and SDI, it would make the dispute resolution clause in it optional at the instance of one or other of the parties. It is plain that the parties intended, when entering into the IPLA, to give each party complete autonomy from each other as to the enforcement of all rights and obligations thereunder. It cannot have been the intention of the parties either to the IPLA or the SHA that the Company could only sue TRFC if TRFC agreed with SDI that it should, or vice-versa. That is commercially absurd. In order to avoid that absurdity it is not only possible but necessary to read the clause as not precluding the shareholders from bringing derivative proceedings.
61. Accordingly, the hypothetical director would not consider himself bound by clause 12.1 not to continue the action because the Company is not the claimant.
62. I have dealt with clause 12.1(n) when considering s. 263(2)(a) because it is arguably relevant to the application of that provision. I would, however, accept Mr Hill’s

submission that it properly only becomes relevant under the discretionary parts of the test under s. 263(3)(e). The basic question for the purposes of the mandatory bar under s. 263(2)(a) is whether no hypothetical director seeking to perform his duty to promote the success of the company under s. 172 would continue the claim, and not whether there are particular constraints on the claimant shareholder from acting in the particular case.

(3) Ss. 263(3) and (4): discretionary factors relevant to the grant of permission

63. Ss. 263(3) and (4) provide discretionary factors relevant to the grant of permission to a claimant to continue with a derivative claim. They are as follows:

(3) In considering whether to give permission (or leave) the court must take into account, in particular—

(a) whether the member is acting in good faith in seeking to continue the claim;

(b) the importance that a person acting in accordance with section 172 (duty to promote the success of the company) would attach to continuing it;

(c) where the cause of action results from an act or omission that is yet to occur, whether the act or omission could be, and in the circumstances would be likely to be—

(i) authorised by the company before it occurs, or

(ii) ratified by the company after it occurs;

(d) where the cause of action arises from an act or omission that has already occurred, whether the act or omission could be, and in the circumstances would be likely to be, ratified by the company;

(e) whether the company has decided not to pursue the claim;

(f) whether the act or omission in respect of which the claim is brought gives rise to a cause of action that the member could pursue in his own right rather than on behalf of the company.

64. As Roth J pointed out in Stainer v Lee [2011] BCC 134 at [29], there is no particular standard of proof that has to be satisfied, but the court must consider a range of factors to come to an overall view. It may be in the interests of the company to pursue a weaker case for a very large sum, or a very strong case for a smaller sum. The evaluation is not mechanistic. I address in turn each of the relevant factors that are in issue on this application.

*(a) whether the member is acting in good faith in seeking to continue the claim*

65. The Defendants have not alleged, at least in terms, that SDI is seeking to bring the claim in bad faith. The furthest they go is to say that “what really motivates” SDI is its desire to maintain its income not as shareholder in the Company but as part of the Sports Direct group. In other words, SDI is really seeking to continue the IPLA in order to promote the interests of Sports Direct group at the expense of the Club.
66. There may, or may not, be something in that allegation. In order to get to the bottom of it one would have to get into the detail of the terms on which the Company had arranged its dealings with other companies in the Sports Direct group. This will form part of the TRFC claim. I have not sufficient detail here to be able to assess with any

accuracy whether the allegation is well founded or not. However, even assuming that it is well founded, the (assumed) fact that the Company's interests are being subjugated to the interests of the Sports Direct group (with an indirect adverse impact on TRFC) is powerfully counterbalanced by the fact that if the purported termination of the IPLA is allowed to stand the Company will have no business at all. The fact that there might then be renegotiation is scant comfort to the Company. Similarly, I do not consider that SDI is disabled from standing up for the Company merely because it has its own commercial interests which are to be pursued at the expense of the Company, since that price must on any view be worth paying given the alternative.

67. In summary, although I can well see that SDI has its own business interests in keeping the IPLA alive which are not identical to the interests of the Company, the degree of alignment is far closer than that being offered by the Defendants. In any event, SDI is not acting in bad faith in pursuing the claim.

*(b) the importance that a person acting in accordance with section 172 (duty to promote the success of the company) would attach to continuing it*

68. In Iesini v Westrip Holdings Ltd Lewison J said of this sub-section, at [85]:

“As many judges have pointed out (e.g. Warren J in Airey v Cordell [2007] BCC 785, 800 and Mr William Trower QC in Franbar Holdings Ltd v Patel [2009] 1 BCLC 1, 11) there are many cases in which some directors, acting in accordance with section 172, would think it worthwhile to continue a claim at least for the time being, while others, also acting in accordance with section 172, would reach the opposite conclusion. There are, of course, a number of factors that a director, acting in accordance with section 172, would consider in reaching his decision. They include: the size of the claim; the strength of the claim; the cost of the proceedings; the company's ability to fund the proceedings; the ability of the potential defendants to satisfy a judgment; the impact on the company if it lost the claim and had to pay not only its own costs but the defendant's as well; any disruption to the company's activities while the claim is pursued; whether the prosecution of the claim would damage the company in other ways (e.g. by losing the services of a valuable employee or alienating a key supplier or customer) and so on. The weighing of all these considerations is essentially a commercial decision, which the court is ill-equipped to take, except in a clear case.”

69. I cannot embark on a mini-trial, but I do have to consider the strengths of the claim in order to come to a provisional view (see Iesini at [79]). In this case that is not a complicated process.
70. As to the merits of the claim, Mr Hill's skeleton argument (at [47]) sets out with admirable clarity and succinctness the claims, the evidence in support and the responses to them. I take those as read and will not lengthen this judgment further by setting them all out here. What matters is the Defendants' response. They do not address the merits of the claims head on in their evidence despite having had many months to do so. They have not, for example, produced a draft Defence that they would serve which would show that the claims were bad and that TRFC's termination notice was unimpeachable. Mr Hill submits that the absence of substantive response is telling. In my judgment it does not necessarily indicate that there is no defence, but the fact that the Defendants have chosen not to engage in any material way on the merits means that



I can only assess the claims based on what SDI has said. On that information the claims articulated in the Particulars of Claim and as supported by Mr Priestley's witness statement seem to me, provisionally, to be powerful and well-substantiated enough that a person acting under s. 172 would attach importance to them. That is particularly so given that the alternative is that the Company, to whom the hypothetical person under the subsection owes the duties under s. 172 in the first place, would suffer the total loss of its business.

71. Instead, the Defendants play the information gap card again. They say that they do not have enough information about the merits to be able to form a view on the facts or the law. As is I hope clear by now, I regard that as a wholly untenable position. Mr King and Mr Murray are not to be equated with a person acting in accordance with s. 172, not only because they were and remain hopelessly conflicted but because any unconflicted person would, viewed objectively, place a great deal of importance on continuing the claim, for the reasons I have already given.
72. Mr McCormick went so far as to suggest that SDI was at fault in not producing evidence that it has taken legal advice that the proceedings are merited. I cannot accept that submission. SDI's own legal advice is privileged and the Company has not been in any position to take any such advice. In any event the issue of legal advice is a red herring since the Court must look at the claims and hear the Defendants' submissions about it and decide for itself whether they are sustainable in law. I have heard nothing from the Defendants which would begin to indicate that the claims set out in the Particulars of Claim are without legal foundation, and indeed Mr McCormick made no such submissions.
73. As to the value of the claim, I agree with the Defendants that this is hard to assess, made all the harder by potential causation issues arising out of the supporter boycott, for which TRFC blames SDI and others in the Sports Direct group. However, I am not required to quantify the loss at this stage. It is enough to say that the value of the claim is the difference to the Company between having a business and having no business at all, and that is sufficiently important to pass muster under ss. 263(3)(b).
74. Finally, the Defendants relied on the risk to the Company of an adverse costs order and on reputational risk. So far as an adverse costs order is concerned, that is not a risk since SDI has offered to pay the costs of the litigation and to indemnify the Company. It is not anyway clear to me in what circumstances any costs order would be made against the Company, given that it is not going to play any role other than, perhaps, in giving disclosure.
75. So far as reputational risk is concerned, the Defendants say that the Company's reputation, already poor among fans, will not be improved by the litigation and will lead to a further reduction in revenues. First, since the alternative to the claim is no business for the Company at all, that is an empty point. Secondly, the fact is that TRFC has itself chosen to bring this to a head and terminate, and to pursue its own litigation against SDI. The dispute between the shareholders of the Company is already out in the open.

*(e) whether the company has decided not to pursue the claim*

76. The answer to this is no. As a matter of fact there has been no such decision, nor on the Defendants' own case could there have been, since they say that Mr King and Mr

Murray lacked sufficient information to make a decision one way or the other. As a matter of law, the only decision is the institutional decision contained in clause 12.1(n) of the SHA. I have already explained why I do not consider that that provision is a bar to these proceedings. Clause 12.1(n) is not anyway a decision by the Company, not least since the Company is not a party to the SHA. But even if it amounts to such a decision by the Company, I have a discretion under this subsection in any event to let the claim proceed. In the circumstances, I would not let the institutional decision by the Company in clause 12.1(n) (even if that is what it was) stand in the way of SDI taking the only steps available to protect the Company's business from destruction.

77. The Defendants say that where the party seeking permission to continue a derivative action has prevented the company from making a responsible decision whether or not to pursue its own claim, then that is itself a powerful reason for refusing permission. However, the statutory test is whether the company has decided not to pursue the claim, not whether the company has made no decision one way or the other. In any event, for reasons I have already given, this is not a case where the Company has genuinely been disabled from making a decision. Mr King's and Murray's purported ignorance about the merits of the Company's position, and the position of conflict that they were in, cannot possibly be used as a platform to enable them to knock out the claim on this basis.

*(f) whether the act or omission in respect of which the claim is brought gives rise to a cause of action that the member could pursue in his own right rather than on behalf of the company*

78. The Defendants' case is that SDI has rights it can use to claim what it is entitled to. They suggest that SDI can counterclaim for damages for breach of the SHA in the TRFC action, or can bring s. 994 proceedings.
79. The problem with that submission is that the act or omission in respect of which the claim is brought can only be brought by the Company, and not SDI. That is the basic rule in Foss v Harbottle. First, so far as the claim against TRFC is concerned, SDI is not a party to the IPLA. Clause 19.5 contains a standard exclusion of the operation of the Contracts (Rights of Third Parties) Act 1999, and so there is simply no room for the Defendants to say that SDI can somehow enforce the IPLA for its own benefit. A combination of the rules of privity and separate corporate existence of the Company make that submission unarguable.
80. It is also worth observing that TRFC did not seek to sue the Company in the TRFC action, and although doubtless SDI could counterclaim and seek to join the Company as a part 20 Defendant for some kind of declaratory relief, such a counterclaim would not vindicate the rights of the Company itself.
81. So far as the claims against Mr King and Mr Murray for breach of duty are concerned, again these are claims that only the Company may bring. They owed no duties, fiduciary or otherwise, to SDI.
82. Furthermore, any claim brought by SDI in respect of the matters the subject of the Particulars of Claim, whether as against TRFC or Mr King and Mr Murray, would fall foul of the reflective loss principle, and does not fall within any of the recognised exceptions: see the review of the modern law on that topic by Birss J in Peak Hotels and Resorts Ltd v Tarek Investments Ltd [2015] EWHC 3048 (Ch), at [29]-[31]. As

Birss J pointed out at [58], the fact that the company is deadlocked does not bring the case within the exception to the operation of the principle.

83. A s. 994 petition would not take matters much further since it is not the appropriate procedural vehicle for vindicating the Company's claims in respect of wrongs allegedly done to it. Ultimately the court may well direct the bringing of derivative proceedings anyway under s. 996(2)(c) of the 2006 Act.

(4) S. 263(4): the views of members of the Company who have no personal interest in the matter

84. There are no such persons. It follows that there is nothing for me to consider in the exercise of my discretion.

#### **Conclusion and disposition**

85. For the reasons given above I accede to SDI's application and I grant permission to continue the action. Although the draft order seeks an order for costs in the case, and Mr Hill did not seek to amend his application to seek an order for costs, my provisional view is that I am not precluded from inviting submissions as to costs and I am prepared to hear submissions about the costs of this application unless the parties are able to come to an agreement.