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Houghton v Saunders & Ors / Updating report for Feltex Carpets Limited claimants

1. This further updating report is made by me as senior counsel for Mr Houghton (the named plaintiff in this proceeding) and the approximately 1800 qualifying shareholders he represents (the claimants). It includes an update of matters subsequent to my previous updating report dated 4 August 2011.
2. In an interim judgment of French J dated 9.3.11 (as to key rulings) and a further reserved judgment dated 8.6.11 (giving full reasons) the interim stay of the Feltex proceeding has been lifted by the High Court, subject to provision for security for costs of \$200,000 being made on behalf of Mr Houghton. Payment of the required security was made to the High Court on 10 June 2011.
3. The representative order, whereby Mr Houghton represents all the other claimants in the proceeding as the named plaintiff, has been approved by the court. This means that Mr Houghton sues on behalf of all the claimants (ie the qualifying shareholders who have elected to opt-in to the proceeding). There remain four causes of action.
4. The second cause of action in the present statement of claim was struck out by French J. This would have alleged (in its proposed amended form) that the Feltex directors (the first defendants) and Credit Suisse MP (the third defendant) had a duty to disclose to investors that they knew that the prospectus was false and misleading in material respects, but they failed to do so. It would have alleged that this had the effect of disguising the availability to the investors of their remedy under the Securities Act 1978 s37A (the Act) to give notices avoiding the allotment of shares to them and to obtain repayment of their subscriptions. No cross-appeal by Mr

Houghton against this ruling has been filed. It is not considered that this ruling significantly affects the overall thrust and strength of the claim.

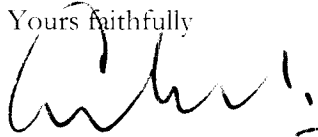
5. In summary, the four other causes of action which remain are based on:
 - alleged misleading and deceptive conduct by all the defendants in the Feltex public offer, the prospectus and the allotment of the shares (the first cause of action)
 - alleged misleading and deceptive conduct by the first defendant Sam Magill (a director and the chief executive officer of Feltex) by his involvement in the practice alleged to have been engaged in by Feltex from around May 2003 of manipulating its earnings and revenue recognition in particular accounting periods and so distorting its financial statements for 2003 and 2004 (this will now become the second cause of action)
 - the prospectus allegedly containing untrue statements, both as to statements made in it and by material omissions, as a consequence of which it is claimed that all the defendants are liable to pay compensation to the investors in terms of the Act s56 (this will now become the third cause of action)
 - Alleged negligence by all the defendants in the public offer, the prospectus and the allotment of the shares (this will now become the fourth cause of action).
6. French J did not consider that she could resolve genuinely disputed facts or expert evidence at this stage. Nor that she could place any significant weight on the finding of the District Court in August last year whereby Feltex directors were acquitted on charges laid by the Ministry of Economic Development. Her Honour was satisfied there were serious questions to be tried arising from the claim brought by Mr Houghton. Also that the JAFL funding agreement with the qualifying shareholders, as amended and approved by the court in May 2010, is appropriate.
7. All the defendants have filed notices of appeal against French J's judgments variously challenging:
 - the lifting of the interim stay order
 - the amount of the security for costs ordered and seeking an increased amount

- the approval of the representative order
 - the dismissal of some defendants' applications to strike out various other paragraphs of the statement of claim.
8. A second amended statement of claim, which deals with various matters arising from French J's judgments, has now been filed. The defendants were given the opportunity to decide if they wish to pursue further their strike out application in respect of specific paragraphs of the statement of claim. Otherwise they were to file statements of defence, which they have done.
 9. On 20 June 2011 the defendants applied to have the proceeding transferred from Christchurch to the Auckland High Court for entry on the Commercial List. This was successfully opposed by Mr Houghton. The application was dismissed by Potter J in the High Court (Commercial List) in Auckland on 7 October 2011.
 10. On 29 November 2011 French J made orders for discovery by the plaintiff and 20 represented qualifying shareholders, randomly selected, and by all the defendants. This is an important step in the pre-trial process in the proceeding.
 11. On 16 September 2011 Mr Houghton applied to have a number of issues determined at a first stage trial before issues of individual loss incurred by qualifying shareholders or any required issues as to individual reliance placed on the prospectus. The application was heard by French J on 7 & 8 December 2011. Her Honour's judgment was reserved but she has since given interim directions as to how this matter and discovery should be progressed.
 12. An application by Mr Houghton to receive a copy of the transcript of evidence and any written statements given in the criminal proceeding *Registrar of Companies v Feeney & Ors* (District Court; Auckland; 2 August 2010) was also successful. This prosecution was against the later directors of Feltex, some of whom are the same as the defendants in Mr Houghton's proceeding.
 13. Importantly, earlier this year JAFL concluded, through a London-based commercial litigation funder, co-funding and adverse costs insurance agreements. The funding agreement is with an associate of Harbour Litigation Funding Ltd, which has a substantial litigation funding business. Counsel considers that these agreements are

sufficient to fund the case and to continue to satisfactorily protect the position of Mr Houghton and the qualifying shareholders he represents, including as to any adverse costs that might reasonably be expected to be made in favour of the defendants if the claim was to fail. The agreements are also considered to meet the requirements specified in the previous judgments of French J and the Court of Appeal. Harbour Litigation Funding Ltd obtained an independent report on the merits of the claim brought by Mr Houghton from a Sydney QC.

14. On 29 July 2011 Mr Houghton applied for an order that these agreements not be disclosed to the defendants on the ground that they were confidential. This was considered to be important. This application was also successful. On 30 November 2011 French J made orders that those documents not be disclosed. Mr Houghton is to provide these documents and other information to the court relating to the co-funder and the insurer.

Yours faithfully

A handwritten signature in black ink, appearing to read 'A J Forbes', with a stylized flourish at the end.

A J Forbes QC

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