Wilberforce
CHAMBERS

Insolvency Conference 2022

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Wilberforce Insolvency Conference 2022

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Speakers

John McGhee QC
John maintains a wide and varied practice in the fields of modern commercial chancery work. He is well known for his acute intellectual analysis of problems and mastery of the detailed facts of a case as for his robust, practical and commercially realistic advice. John has appeared in all the civil courts in England and Wales from the Upper Tribunal to the Supreme Court and in arbitrations both as counsel and arbitrator. His court room presence marries an easy rapport with the court or tribunal, robust and incisive cross-examination and a lightning-fast response to new points as they arise in the case. Chambers and Partners 2022 describes John to be *"extremely bright and decisive with a clear communication style which fills clients with confidence"*.

Lexa Hilliard QC
Lexa is well-respected and is recommended by the legal directories as a leading silk for commercial dispute resolution, commercial chancery, company, insolvency and professional negligence. Her insolvency practice covers all aspects of corporate restructuring and insolvency, both domestic and cross-border. Chambers and Partners 2022 describes Lexa as "*fantastic and just so easy to work with. Lexa is a great advocate, who has the ear of the court. She is down to earth and matter of fact."*
The Legal 500 2022 calls her *"A rare find in that she combines academic rigour with commercial acumen and excellent advocacy skills."*

Marcia Shekerdemian QC
Marcia is a leading practitioner in all aspects of contentious and non-contentious insolvency, company and partnership law as well as commercial litigation. Marcia specialises in all aspects of personal and corporate insolvency and company law, including bankruptcy, administrations, receiverships, liquidations, voluntary arrangements, shareholders' disputes, wrongful trading, misfeasance, disqualification of directors, directors' duties, derivative claims and security and priority issues. She has a particular interest in cross-border insolvency. Marcia is currently representing a consortium of Indian banks (led by the State Bank of India) in bankruptcy proceedings involving guarantee liabilities of over $1 billion. The Legal 500 2022 describes Marcia as *"technically excellent, commercially minded and pragmatic, she also gives great tactical advice".*

Clare Stanley QC
Clare is currently shortlisted as Chancery Silk of the Year for The Legal 500's upcoming awards. Throughout her career she has acted both onshore and offshore in numerous, often high value, insolvency cases (bankruptcy and liquidation, voluntary arrangements, schemes of arrangement). To that practice she brings trial experience, and in-depth legal knowledge of conflict of laws, property, trusts, company and asset tracing. Much of her work is offshore, in particular in the Cayman Islands, involving complex offshore structures, and asset tracing. The Legal 500 describes Clare as "*a total star - she is a fierce cross-examiner, super-smart, hardworking and gets to the key issues instantly".* While Chambers & Partners 2022 say she is "*unflappable and has brilliant knowledge and experience of the law and the court process generally. She has pretty fearsome cross-examination skills and is a very good tactician."*

James Bailey QC

James has substantial experience of handling insolvency matters and has been instructed in high-profile insolvency and restructuring work including *Enron* (Cayman Islands), *Comet* and *the London Underground Public-Private Partnership*. James acted for a consortium led by Canadian billionaire Lawrence Stroll in the successful acquisition of the Force India Formula 1 motor racing team from Indian billionaire. The transaction was exceptionally complex and involved a structure never previously used in Formula 1. Chambers and Partners describes James as *"really analytical, methodical, hard-working and gets to the point quickly*", as well as *"technically astute, a very strong advocate and an excellent team player"*.

David Pollard

David is a leading and highly experienced lawyer in the insolvency field and related areas, in particular the pensions and employment side. His book, "*Corporate Insolvency: Employment and Pension Rights*" is the leading work in the area. A new 7th edition came out in May of this year. It looks at the areas where insolvency law intersects with pensions and employment issues. David has also published other books in the areas of pensions, insolvency and employment law: "*Connected and Associated: Insolvency and Pensions Law*"; "*Pensions, Contracts and Trusts: Legal Issues on Decision Making: Applying Braganza*"; "*The Law of Pension Trusts*"; and "*Employment Law and Pensions*".

Graeme Halkerston

Chambers and Partners 2022 describes Graeme as having "*an encyclopaedic knowledge of all things to do with insolvency and company law"* and that he is "*steeped in offshore experience, especially in insolvency-related matters. He is invaluable in complex insolvency cases because he can provide a reasoned local perspective*". Graeme is often instructed when financial services companies have collapsed acting on the insolvency process and ensuing fraud and professional liability in the English and offshore courts. Many of Graeme's cases involve co-ordinating proceedings in England and offshore jurisdictions; his recent cases have involved parallel proceedings in the BVI, the Cayman Islands, the Bahamas, Jersey and the Isle of Man. A substantial part of Graeme's practice also involves proceedings pending in the United States and he often acts as an expert witness on matters of Cayman and BVI law in US litigation. Graeme is admitted to practice in the BVI and he has held full or limited admission rights in the Cayman Islands from 2007 to 2022.

Thomas Robinson

Tom has a strong commercial / chancery practice with particular emphasis on pensions, insolvency and commercial litigation and arbitration. He has been recommended as a leading junior in insolvency by The Legal 500 and Chambers UK for several years. He is currently co-editing and contributing to a new edition of Sweet & Maxwell's Kerr & Hunter on Receivers and Administrators. He has appeared in the Supreme Court as part of the Nortel litigation and recently led the Wilberforce team in the High Court in Re Baglan Operations Ltd. Chambers & Partners 2022 note Thomas is "*an excellent strategist and an extremely effective advocate*". He "*has never appeared without having complete mastery of his papers and his arguments and is always quick on his feet*."

Daniel Lewis
Daniel practices in the fields of restructuring and insolvency, company law and commercial dispute resolution, including arbitration. In both the insolvency and company law fields he is highly experienced in bringing and defending claims against directors, including claims for misfeasance / breach of duty, asset recovery cases and disqualification proceedings. He regularly acts on claims against directors arising from participation in tax schemes and tax evasion. His insolvency practice has a particular emphasis on cases with an international element, particularly offshore asset recovery cases. Chambers & Partners describe Daniel as *"a very charming advocate who is well liked by courts and is very user-friendly. He's very much a team player and is very commercial", they also note that "he's a pleasure to work with and is good on his feet."*

Bobby Friedman
Bobby is a much in demand senior junior. He is described in the legal directories as a "Rising Star" who is "*staggeringly clever*" and *"noted for his advocacy capabilities and the practical approach he takes to cases*". Bobby specialises in general commercial disputes, with an emphasis on civil fraud; shareholder disputes; insolvency; offshore work; commercial trusts cases; and commercial art and cultural property disputes. Bobby has a busy insolvency practice and has acted in several high-profile and complex cases. He is also a contributing author of Kerr & Hunter on Receivers and Administrators and has been published in International Corporate Rescue. Chambers and Partners 2022 says he is "*incredibly bright and brilliant on his feet".*

Sri Carmichael
Sri specialises in commercial litigation, insolvency, civil fraud and company law. She is recommended as a leading junior for commercial litigation and insolvency in the legal directories, which describe her as *"amazing on her feet*" and *"a very good advocate"* who is *"great to have on your team and well-liked by clients"*. Sri acts for officeholders, creditors, companies and company directors in respect of winding up petitions and injunctions to restrain, antecedent transactions, allegations of misfeasance and wrongful trading, and other issues arising out of liquidations, administrations and CVAs. The Legal 500 2022 describes Sri as, "very aware and able to adapt submissions to suit the situation. Responsive and great to have on your team".

Jack Watson
Jack has already been described in The Legal 500 as **"***a fantastic senior-junior***".** Jack has a busy commercial and chancery practice with significant experience acting in high value and complex disputes regularly in cases involving an international dimension, often appearing on his own against QCs or senior junior barristers. Jack is ranked in The Legal 500 for insolvency and is described as "*a very capable barrister who displays good judgement and strategic thinking".* His insolvency practice encompasses both advocacy and advisory work and he has acted in several high profile, high value cases. He regularly acts for office holders, directors, individuals, and insolvent companies often in cases involving an international or multi-jurisdictional dimension. Jack is also experienced at making applications under s.236 and s.366 Insolvency Act 1986 as well as conducting interviews and private examinations.

Jessica Brooke
Jessica specialises in commercial chancery litigation, with a particular focus on insolvency and commercial disputes. She is an experienced advocate who appears regularly in the High Court, and she frequently acts for both liquidators and respondents in misfeasance claims, often dealing with cases involving asset tracing and allegations of fraud or dishonesty. She advises on and acts in high-value insolvency and commercial proceedings, including those involving cross-border issues and urgent injunctive relief, and she is experienced in all aspects of wider personal and corporate insolvency litigation.

Rachael Earle

Rachael specialises in insolvency and asset recovery. Her practice encompasses all areas of individual and corporate insolvency and she has extensive experience of complex misfeasance claims. Rachael was ranked as a Rising Star in The Legal 500, which noted she *"works extremely hard"* is *"technically very good"* and is *"excellent on her feet".* She is also *"very tough and doesn't back down***"***.* Rachael is often instructed on insolvency cases which are of a complex or urgent nature. She appears regularly in the High Court before ICC Judges. Her experience extends to fraudulent and wrongful trading, misfeasance, antecedent transactions, unlawful dividends and disguised distributions, orders for possession and sale in bankruptcy proceedings. The Legal 500 2022 describes Rachael as: *"An unbelievably sharp junior barrister who instils confidence".*

Jamie Holmes

Jamie frequently appears before the ICCJ's and in the County Court across the full spectrum of insolvency business (personal and corporate), including the reported decision last year of re Rufus/Sands v. Dyer [2021] B.P.I.R. 1594. He has also assisted a number of leaders in Chambers in advising on proposed restructurings. Jamie is ranked in The Legal 500 2022 as a "Rising Star" separately for both commercial litigation and offshore work, in which he is described as *"a supremely bright junior, who leaves no point unconsidered*" and *"exceptionally hard working and a real pleasure to work with, highly responsive and astute, and tactically very good"*. Jamie's insolvency practice forms part of a wider, busy commercial chancery practice and he is well-placed to assist in matters that cross-over into the other specialist areas of his practice in civil fraud (with extensive experience of freezing injunctions and other forms of interim relief), other commercial work, and trusts and probate.

Tara Taylor

Tara has a broad insolvency practice that includes all areas of personal bankruptcy and corporate insolvency. She is often instructed in cases involving allegations of fraud and dishonesty (and related applications for freezing injunctions and other interim relief) and has extensive experience of cases with offshore elements. During several months spent on secondment in the dispute resolution team at a leading international law firm in the Cayman Islands, Tara worked on a number of multi-jurisdictional insolvency matters. She is currently instructed on behalf of one of the former directors of the BHS Group Ltd in claims brought by the group's Joint Liquidators for misfeasance and wrongful trading, valued at over £160m. Tara is ranked as a "Rising Star" for offshore work in The Legal 500, which notes that she is able to *"succinctly outline complex legal questions for the court".*

Daniel Scott

Daniel has a busy commercial chancery practice, with particular emphasis on commercial, fraud, insolvency and property work. He is equally comfortable appearing as sole counsel and as part of a larger team, and enjoys the different challenges posed by both. He has a diverse insolvency practice, and acts regularly for office-holders, directors, creditors, and insolvent companies. He has a particular interest in the intersection between civil fraud and insolvency claims and enjoys acting in misfeasance claims, having acted in a high-value offshore claim brought by a liquidator and the former directors of a company. He has recently appeared in *Counsel General for Wales & Ors v Gareth Allen (as Official Receiver) & Ors* [2022] EWHC 647 (Ch), a case which concerned a challenge to the decision of the Official Receiver to terminate electricity supply to a business park in Wales. The first instance judgment considers the "perversity" test under s.168(5) IA86 and the role of environmental factors in a liquidator's decision-making over whether to continue trading a business, as well as whether the OR is a public authority under the Human Rights Act 1998 for these purposes. An appeal hearing in the Court of Appeal is anticipated shortly.

Joseph Steadman
Joseph has a very busy and diverse commercial chancery practice, spanning all of Chambers' practice areas. He is regularly instructed to appear as sole counsel in High Court, County Court and Tribunal litigation, as well being led as part of a larger counsel team. He has been involved in appeals to the Upper Tribunal and High Court (in his own right) and to the Court of Appeal. He also has a substantial advisory practice. Joseph has experience of working on cases which span a number of jurisdictions and require him to work closely with overseas lawyers and insolvency practitioners. His recent work has involved the Channel Islands, the Isle of Man, Cayman Islands, the British Virgin Islands, Cyprus, Monaco, Malta, and Switzerland. The Legal 500 describes Joseph as "*extremely intelligent, he knows the law backwards, gives very practical advice. He is an ideal person to have on the team".*

Daniel Petrides
Daniel has a thriving commercial chancery practice spanning over all of the Chambers core practice areas. Daniel is often instructed in relation to insolvency and company law matters. He frequently appears in the Company Insolvency List in the High Court, as well as acting in or advising on larger matters both led and unled. He has recently acted successfully (led by James Bailey QC) in High Court trial concerning the true construction of the defendant company's articles of association following the dismissal of the company's founder (*Glass v Previse Ltd).* Daniel has also defended a fraudulent misrepresentation claim arising from the sale of the shares in a financial services company based in Luxembourg. He has experience obtaining and conducting an examination of an insolvent company's former accountant under s.236 of the Insolvency Act 1986.

Lemuel Lucan-Wilson
Lemuel has gained broad experience across Chambers' key areas of practice such as insolvency, company, commercial, trusts and property disputes. He is developing a broad commercial chancery practice. He is happy to be instructed as part of a larger counsel team, or on his own, and has experience of litigation in both roles. He has recently acted as junior counsel for the successful appellants in the Court of Appeal in *Al Jaber v Mitchell* [2021] EWCA Civ 1190 (led by Clare Stanley QC) relating to the scope of witness immunity in the context of examinations under section 236 Insolvency Act 1986. Lemuel is a Bedingfield Scholar of Lincoln's Inn, and holder of the Hebe Plunkett Award. At King's College London, he was awarded a Dickson Poon Scholarship.

Ram Lakshman
Ram practices across all of Chambers' core practice areas, including insolvency, trusts, property, pensions, company and commercial law. He regularly appears as sole counsel in both the High Court and the County Court and is equally comfortable being instructed in his own right or as part of a larger counsel team. Ram's current insolvency matters include acting on behalf of the Joint Administrators of three group companies (led by Lexa Hilliard QC) who are seeking the directions of the court on a suite of complex issues relating to whether various categories of creditors obtained the security interests they were promised. Ram appeared as sole counsel on behalf of the Joint Administrators at a hearing to extend the administrations, and successfully obtained a rare 3-year extension. Ram also recently appeared (led by Jack Watson) in the matter of *Brittain v Ferster & Ors* [2022] EWHC 1060 (Ch), and successfully obtained an extension of the Bankruptcy to its fifth anniversary alongside extensive orders for disclosure of information and documentation. Alongside these substantial led matters, Ram has the usual baby junior diet of bankruptcy and winding up petitions, alongside interim insolvency applications, which he deals with in his own right.

Benjamin Slingo

Ben joined Chambers in 2021 on the successful completion of his pupillage. He is building a broad commercial chancery practice, in which insolvency features prominently. He has gained considerable experience on both sides of applications to set aside statutory demands and has also acted for creditors bringing bankruptcy petitions and seeking to enforce charging orders via orders for sale. Various of these cases have involved difficult procedural issues, especially to do with service. Other recent work has involved: (i) collective investment schemes under the Financial Services and Markets Act 2000, (ii) the setting aside of preferences under s. 340 of the Insolvency Act 1986, and (iii) defending a claim against the directors of an insolvent company in respect of directors' loans. Before joining Wilberforce Ben received a double starred first in history from Cambridge (coming first in his year in the University) and a doctorate in the history of political philosophy. He was also awarded a Distinction on the GDL and was graded Outstanding on the Bar course.

Section 236 – *Al Jaber v Mitchell* [2021] EWCA Civ 1190, [2022] 2 WLR 497

Clare Stanley QC and Lemuel Lucan-Wilson

1. The decision concerned a disputed application to amend the liquidators' points of claim halfway through a part-heard trial of a misfeasance claim. The amendments sought to allege that the answers given and witness statements submitted by a former director (the Sheikh) in a s. 236 Insolvency Act ("**IA 1986**") examination, rendered him liable in deceit, negligent misrepresentation and/or conspiracy because he had knowingly given false responses. It was also alleged that he had committed a breach of fiduciary duty for failing to give the correct responses.

2. It was argued by the Sheikh that these statements, made in the examination, had the protection of witness immunity. Witness immunity or immunity from suit is the doctrine that no participant in judicial proceedings can be liable for their words spoken or actions taken/not taken either civilly or criminally, save for certain exceptions (perjury, contempt and malicious prosecution). The immunity has been abrogated somewhat regarding counsel and expert witnesses, who may each be sued by their own clients, but otherwise remains. The immunity also extends to work which is preparatory to the court proceedings – the taking of a proof of evidence by a solicitor for example, as was the case in Watson v M'Ewan [1905] AC 480.

3. As far as research of both sides went, this was the first time that proceedings had specifically been brought against a s.236 examinee on the basis of providing incorrect information in the answers given.

4. At first instance, Joanna Smith J held that the amendments were not barred by immunity from suit ([2021] EWHC 912 (Ch)). This - save the breach of fiduciary duty claim - was appealed.

What did the Court of Appeal decide?

5. At [61] of Asplin LJ's judgment there is a useful authoritative statement as to what the Court must do when considering whether immunity from suit arises: it is important that the "*precise nature*

of the immunity and the context in which it is said to arise, are considered in detail". In the Court's view, the existence of the immunity may depend on (inter alia):

> "*the role or function of the person who made the statement in those proceedings and the relevance of that role; whether the maker of the statement was in that role or exercising that function when the statement was made; the purpose of the statement; the nature of the proceedings in which it was made, or with which it was connected; how "judicial" those proceedings are; and the extent and nature of the connection between the statement itself and the proceedings*."

6. Five specific factors then appear to have particularly swayed the Court of Appeal to hold that the witness immunity rule applied to the s. 236 procedure:

    (1) First, although the s. 236 procedure was *sui generis* and not simply witness examination, the fact it took place in court was important, but not conclusive.
    (2) Secondly, the fact that the examination took place as part of wider compulsory winding-up proceedings (commenced by an order of the court) and was intended to facilitate such proceedings was also important. The examination was part of a wider "*judicial proceeding*" supervised and commenced by the court.
    (3) Thirdly, the liquidator and the judge would both have the benefit of immunity from suit for their actions during the examination, and this pointed towards all participants enjoying a similar immunity.
    (4) Fourthly, there were public policy considerations; an open and honest examinee might answer in good faith and yet open himself up to civil liability, potentially causing a chilling effect. Examinees might still be able to have claims made against them for failure to provide information.
    (5) Finally, the suggestion that immunity would undermine the s235 procedure was too hypothetical and insufficient to outweigh the other policy considerations.

7. Although the decision is an important one, its long-term practical effects may be rarely felt; there is a reason it is the first reported case to deal with a liquidator suing an examinee simply for words spoken and written in an examination. Normally, if the examinee gives incorrect information or lies, the liquidator will at some stage consider whether he should be punished criminally for that conduct.

To what types of application does the decision apply?

8. The ratio of the decision is that claims which are based on incorrect answers being given as part of a s. 236 examination (such as negligent misstatement or deceit) are barred under the rule. Similarly, a claim alleging a conspiracy to give false evidence in a s. 236 examination is likely also to be barred; by analogy with the ruling that conspiracy claims are also barred under witness immunity in Marrinan v Vibart [1963] 1 QB 528.

9. What remains unclear from the Court of Appeal's decision (because there was no appeal on this point) is the extent to which witness immunity applies to a claim *not* based on the answers actually given in the examination, but to a claim for *failure to comply with a duty to disclose* wrongdoing; per the Court of Appeal's decision in Fassihi v Item Software (UK) Ltd [2004] BCC 994. Indeed, wider claims against an examinee based on their failure to disclose information (assuming there is a freestanding fiduciary duty to give such disclosure), may be justiciable and not barred by witness immunity, even though there was a s.236 examination.

10. Asplin LJ seemed to agree that such a claim would be possible in principle [102] (but she heard no argument on it, the point having been conceded as arguable), and it is correct that the transcript of the examination under s. 236 would then be admissible evidence to "*prove*" the failure to account or disclose. That may give insolvency practitioners some comfort that there are still tools that can be used to threaten a director who gives incorrect answers; although whether such tools are necessary is open to discussion given the potential criminal sanctions which are available to the office holder.

11. However, this potential lacuna (if it exists) to the witness immunity rule would only apply to former officers or those who owed free-standing duties of disclosure to the company. Thus, the status of the examinee may then dictate whether witness immunity applies. An examinee who is not a former officer and has no freestanding duty of disclosure would be immune from suit in respect of words spoken or written in the s. 236 examination, whereas a former officer would not have such protection.

Voluntary liquidations and information provided under s. 235

12. The Court of Appeal's decision was concerned with a s. 236 examination made in a court supervised compulsory winding up of the company. The Court of Appeal held that immunity from suit was engaged because the s. 236 examination took place in the context of those winding up proceedings, and this was a type of "judicial proceeding" in which all participants are entitled to immunity (see para. 97).

13. But what happens when the s. 236 examination takes place in a voluntary liquidation, where there is no court supervised overarching judicial proceeding, and the liquidator is not a court officer? Does witness immunity have any role to play at all? Similarly, what of answers given under s 235 in a compulsory winding up? Is the examinee immune because his answers were given under the umbrella of the wider "judicial proceeding"?

Voluntary liquidation

14. A voluntary winding-up does not start with an order of the court, and the liquidator is not an officer of the court. However, the liquidator in a voluntary winding up may still apply for a s. 236 examination and the court may order such an examination. Whether it then becomes a "*judicial proceeding*" remains unanswered by Al Jaber.

15. We suggest that the fact that there are no overarching "judicial proceedings" does not automatically mean that the immunity could never apply in a voluntary winding up context. As was argued before Joanna Smith J below, the immunity can attach to non-court proceedings, as was the case in Trapp v Mackie [1979] 1 WLR 377. The Court of Appeal did not think that was the complete answer to determining whether the immunity in fact attached, but where the proceedings are more arguably not "*judicial*" as understood by the rule, it would be open to a litigant to use those criteria – albeit that several of them do not apply to a section 236 examination. Even in a voluntary liquidation the Court will still retain some powers of supervision under s112 IA 1986, including the removal of a liquidator under s108.

16. But, reading between the lines of Asplin LJ's judgment, she was very clearly influenced by the fact that the s. 236 in that case was made in the context of the overarching "judicial proceeding", i.e. the compulsory winding up; see e.g. para. 103: "*To put the matter another way, it seems to me that the section 236 examination, viewed in the context of the court led insolvency proceedings, is*

a part of a "judicial proceeding" for the purposes of immunity from suit." (emphasis supplied). See also para. 81: *"The section 236 examination has to be considered not as a standalone procedure, to be examined forensically against the Trapp v Mackie indicia, but instead it should be viewed in the context of the wider compulsory winding-up proceedings in which it arises which are commenced by an order of the court and which it is intended to facilitate."* (emphasis supplied).

17. However, the other strand to Asplin LJ's reasoning was that if the other participants in the s. 236 examination (i.e. the Judge and the office holder(s)) are immune, it would be "curious" if the only person exposed to liability was the examinee himself (see para. 101).

18. But that was said in the context of the wider compulsory winding up proceedings. In a s. 236 examination in a voluntary winding up the judge would certainly have immunity, but the liquidator would not be an officer of the court and it is difficult to see why he should have immunity. If the liquidator does not have immunity, then it is easier to justify why the examinee should also not have immunity. So, what of a liquidator who negligently conducts a s. 236 examination, and fails to ask the obvious questions? If he is not immune, he can be sued. If he is immune, then so should the examinee be immune – that is surely the only just outcome.

19. If one looks at the factors that the Court of Appeal thought were relevant, that would only leave the inconclusive factor that the examination took place in a court, and the public policy concerns. If the liquidator appointed as part of a voluntary process feels the need to utilise the formal procedure in s. 236 (whilst the process is still voluntary), it is likely that the liquidation itself is not progressing in an archetypal way for a voluntary winding-up, such that the policy considerations underpinning the rule will be particularly important. Liquidators are unlikely to use funds for examinations unless required to do so, and the importance of encouraging both truthful answers to such questions and the co-operation of the examinee will be equally as important whether the procedure is voluntary or compulsory. It should, however, be remembered that such considerations "*fortified*" the decision that witness immunity attached to the examination, rather than being an objective justification of imposing immunity.

20. The similarities between a s. 236 examination in compulsory winding-up proceedings and in voluntary proceedings may be significant enough for a future examinee to claim the benefit of

witness immunity. That said, given how long it has taken for the point to be articulated in compulsory winding proceedings, it seems vanishingly unlikely that the point will even come up (let alone be litigated) in the voluntary winding up context.

Information provided pursuant to s. 235

21. Section 235 provides as follows:

"235.— Duty to co-operate with office-holder.

(1) This section applies as does section 234; and it also applies, in the case of a company in respect of which a winding-up order has been made by the court in England and Wales, as if references to the office-holder included the official receiver, whether or not he is the liquidator.

(2) Each of the persons mentioned in the next subsection shall—

(a) give to the office-holder such information concerning the company and its promotion, formation, business, dealings, affairs or property as the office-holder may at any time after the effective date reasonably require, and

(b) attend on the office-holder at such times as the latter may reasonably require.

(3) The persons referred to above are—

(a) those who are or have at any time been officers of the company,

(b) those who have taken part in the formation of the company at any time within one year before the effective date,

(c) those who are in the employment of the company, or have been in its employment (including employment under a contract for services) within that year, and are in the office-holder's opinion capable of giving information which he requires,

(d) those who are, or have within that year been, officers of, or in the employment (including employment under a contract for services) of, another company which is, or within that year was, an officer of the company in question, and

(e) in the case of a company being wound up by the court, any person who has acted as administrator, administrative receiver or liquidator of the company.

(4) For the purposes of subsections (2) and (3), "the effective date" is whichever is applicable of the following dates—

(a) the date on which the company entered administration,

(b) the date on which the administrative receiver was appointed or, if he was appointed in succession to another administrative receiver, the date on which the first of his predecessors was appointed,

(c) the date on which the provisional liquidator was appointed, and

(d) the date on which the company went into liquidation.

(5) If a person without reasonable excuse fails to comply with any obligation imposed by this section, he is liable to a fine and, for continued contravention, to a daily default fine."

22. In Al Jaber at first instance, Joanna Smith J considered that witness immunity would *not* attach to information given under s. 235.

23. The Court of Appeal however did not reach a conclusion on this issue – preferring instead just to content themselves with finding that a s. 236 examination came within the immunity.

24. It is quite difficult to predict where the line may be drawn as regards the s235 procedure, at least in the context of a compulsory winding up. In a voluntary winding up there is no Judge, no court officer, and no judicial proceeding. It seems unlikely that the liquidator would have immunity from suit in asking the informal questions, and it is unlikely that the immunity could be justified for those assisting the liquidator simply on public policy grounds. As set out in Darker v Chief Constable of the West Midlands [2001] 1 AC 435 by Lord Hope at 446D, the immunity represents a derogation from the right of an aggrieved party to institute proceedings for a wrong, and therefore it requires justification.

25. Where s. 235 is deployed in a compulsory winding up clearly there are the overarching winding up proceedings in place, but the question is whether that would be enough. The Court of Appeal was particularly taken with the analogy to the case of Mond v Hyde [1999] QB 1097 and that the official receiver who had made statements in the course of the bankruptcy had immunity from suit. This therefore points towards s. 235 answers as giving rise to immunity from suit.

26. On the other hand, where information is being given under s. 235 even in the context of a compulsory winding up, there is no judge supervising the process. The information is often provided informally, or certainly with less formality than a court examination.

27. But if the s. 235 answers are given, then those answers given to the liquidator (an officer of the court) are in effect answers being given to the court, thus pointing again to them being part of a wider "judicial proceeding".

28. In Al Jaber Asplin LJ said every case will turn on its own context, and that only one of a number of questions is "how judicial are the proceedings?". The overarching liquidation proceedings does not invariably supply the answer to whether immunity from suit applies. That the Court of Appeal noted this difference potentially suggests some reticence towards giving immunity in respect of information provided under s235.

29. No final decision was made as to whether it was "*information*" or "*evidence*" being provided, so that factor is not likely to be of any great assistance in determining where the line would fall. What is imparted to the liquidator under s. 235 is further away from "*evidence*" than what is acquired under s. 236. Indeed, immunity under s. 235 may have some practical issues; although a formal demand is usually made, the duty of co-operation exists when the liquidator requires information. The formal demand is likely so as to set up any potential fines under s. 235(5), but even relatively informal questions for the liquidator (and the answers thereto) could properly be considered as being given under s. 235. Given the fact-sensitive nature of what co-operation under s. 235 may look like, a future court may also consider that the immunity depends on how the investigation by the liquidator proceeds in practice. The liquidator is investigating the company as part of his statutory and judicial role, and must be exercising that role when information is given to him, and much will therefore turn on what is considered to be the "*nature of the proceedings*" where the information is given.

The *Berkeley Applegate* Jurisdiction

James Bailey QC, Graeme Halkerston and Tara Taylor

(1) General Principles

1. An insolvency office holder is entitled to receive remuneration for services rendered as an office-holder in respect of an insolvent estate payable out of the assets of that insolvency estate,[1] provided that the work concerned was *"dealing with the winding up of the company, involving as it does the getting in of the assets of the company, ascertaining its creditors, paying its liabilities in accordance with the statutory provisions and distributing any surplus ... [not with] work administering the trust property held by the company as trustee ... [and] limited to ... dealing with assets of the company"*.[2]

2. Prima facie therefore, an office holder would not be entitled to remuneration for any work undertaken in realising assets held by a company in which a third party has a beneficial interest, as those assets do not form part of the insolvency estate.

3. As such, if it is clear which assets are held on trust, normally the office holder's involvement in those assets will be limited to accounting for them to the beneficial owner or applying to court for the appointment of a receiver or manager to manage and realise the trust assets for the beneficiaries.

4. However, in many cases the affairs of the company will be complex such that it is unclear whether there is a trust in respect of certain assets. Alternatively, while the existence of the trust may be certain, the identity of the beneficial owners and/or their interest in the trust assets may be unclear. In those circumstances the office holder may find himself in a position where factual investigations, legal advice and/or directions of the court are required in order to determine who owns the assets and to fulfil his/her function to do what is necessary and expedient for the management of the company's affairs.

5. The question then arises how the office holder can be remunerated in undertaking those steps.

[1] Insolvency Rules 2016, r.18.16(1). Paragraph 99 of Schedule B1 IA 1986 (administration); s.115 IA 1986 (voluntary liquidation); rule 6.42 IR 2016 (creditors' voluntary liquidation); rule 7.108 IR 2016 (compulsory liquidation).
[2] *Berkeley Applegate (Investment Consultants) Ltd (No.3)* [1989] 5 BCC 803 at 805.

6. Following the decision in *Re Berkeley Applegate (Investment Consultants) Ltd*, it is clear that the Court does have the discretionary jurisdiction to authorise an office holder to recover the costs of realising assets that fall outside the insolvent estate out of those same assets.

7. In *Re Berkeley Applegate*, the business of the company in liquidation was to place funds on behalf of individual investors, secured by first mortgages over freehold property which were taken out in the company's name. At the commencement of the winding up, the company's assets included cash in various client accounts, as well as the benefit of loans made to borrowers from the company and secured by mortgages. These assets were ultimately held by the Court to have been held by the company on trust for its investors. However, prior to that, the liquidator had carried out a substantial amount of work including preliminary investigations to determine whether liquidation was appropriate, dealing with inquiries from investors and borrowers, ascertaining the company's free assets, managing the company's investments and conducting general liquidation affairs.

8. The liquidator applied for an order that he was entitled to be paid his proper expenses and remuneration out of the trust assets in the event that the non-trust assets of the company were insufficient. The Court held that he was, relying on the general principle that where a person seeks to enforce a claim to an equitable interest in property, the court has a discretion to require as a condition of giving effect to that equitable interest that an allowance be made for costs incurred and for skill and labour expended in connection with the administration of the property. However:

> *"It is a discretion which will be sparingly exercised; but factors which will operate in favour of its being exercised include the fact that, if the work had not been done by the person to whom the allowance is sought to be made, it would have had to be done either by the person entitled to the equitable interest (as in Re Marine Mansions Co. and similar cases) or by a receiver appointed by the court whose fees would have been borne by the trust property (as in Scott v. Nesbitt); and the fact that the work has been of substantial benefit to the trust property and to the persons interested in it in equity (as in Phipps v. Boardman). In my judgment this is a case in which the jurisdiction can properly be exercised."*[3]

9. Care should be taken with the reference to the jurisidiction being "sparingly exercised" in *Berkeley Applegate*. It is a phrase often grasped by investor clients seeking to oppose remuneration applications. While the situations in which the principle is engaged are relatively limited, the Court

[3] *Berkeley Applegate (Investment Consultants) Ltd (In Liquidation)* [1989] Ch.32 at 50H.

will readily sanction remuneration when an office holder finds themselves in the classic situation of an appointment over a collapsed investment company. The reference to "sparingly exercised" is therefore best seen as a reference to the gateway requirements to engage the *Berkeley Applegate* jurisdiction rather than extending also to the exercise of that jurisdiction once the gateway requirements have been established.

10. While the decision in *Re Berkeley Applegate* specifically concerned the remuneration of a liquidator,[4] in principle it is applicable in any situation "*where a person has come otherwise than by officious intermeddling into the position of fiduciaries in relation to the relevant fund and have incurred time and cost in realising the fund and identifying the entitlements of the beneficiaries and paying out to those beneficiaries their entitlements*",[5] including administrators[6], trustees in bankruptcy[7] and specialist offshore office holders[8].

11. Similarly, the principle is not limited to assets held on trust for third party beneficiaries; in *Re Sports Betting Media Ltd (In Administration*)[9] replacement administrators were entitled to payment out of a fund subject to a paragraph 99(4) Schedule B1 charge on account of time spent and disbursements incurred in dealing with an administration consisting only of giving effect to that charge.

12. In determining whether to exercise its discretion to make a Berkeley Applegate order, the following factors have been held to be relevant:

    12.1. The complexity of issues relating to the trust assets (see McPherson & Keay's Law of Company Liquidation 5th Ed. at [9-072]);

    12.2. Whether it was prudent from the beneficiaries' viewpoint to undertake the work done, and whether the benefits attributed to the trust's assets were worth the liquidator's efforts (see McPherson at [8-072]);

    12.3. Whether the beneficial owners of the trust property required the assistance of the court to secure their rights, so that it would be just to impose on them a condition that they can only

[4] *Berkeley Applegate (Investment Consultants) Ltd (In Liquidation)* [1989] Ch.32 at 33A.
[5] *Re Sports Betting Media Ltd (In Administration)* 2007 EWHC 2085 (Ch) at [10].
[6] *Gillan v HEC Enterprises Ltd* [2016] EWHC 3179 (Ch).
[7] *Green v Bramson & Ors* [2010] EWHC 3106 (Ch).
[8] *In the matter of Onetradex Limited* (unreported, 1 October 2020, Smellie C.J.), in the Grand Court of the Cayman Islands, approved *Berekely Applegate* remuneration in favour of Controllers appointed by the local regulator.
[9] *Re Sports Betting Media Ltd (In Administration).*

enforce their rights if they submit to the burden of bearing the relevant remuneration and expenses (*Bell v Birchall* [2017] WLR 667);

12.4. Whether the work undertaken by the office holder was for the benefit of the unsecured creditors and adverse to the interests of the beneficiaries under the trust, in which case a Berkeley Applegate order will not be appropriate (*Gillan v HEC Enterprises Ltd* [2016] EWHC 3179 (Ch) at [102]);

12.5. Whether the work undertaken by the office holder, although of benefit to the beneficiary of a trust, was work that the office holder would have had to carry out in any event on behalf of the general body of creditors, in which case the Court may refuse to exercise its discretion (*Tom Wise Ltd v Fillimore* [1999] BCC 129).

13. In general, work undertaken by an office holder to determine whether certain assets are trust assets or assets of the insolvent entity will not be considered work for which the beneficiaries under the trusts should pay (see *Gillan v HEC Enterprises Ltd* at [103]). But this is a fact sensitive inquiry and the other factors listed above may permit the provision of remuneration when the involvement of the office holder could assist a swift and cost-effective resolution of any issues for the benefit of the stakeholders.

14. Similarly, where the insolvent entity is engaged in pre-existing litigation at the time the office holder is appointed in which the insolvent entity and the trust beneficiaries have adverse interests and the office holder incurs costs in relation to that litigation, prima facie those costs should be dealt with under the court's jurisdiction as to the costs of litigation and not pursuant to the *Berkeley Applegate* principle (see *Gillan v HEC Enterprises Ltd* at [101]).

(2) Pre-emptive Costs Orders

15. Whilst in *Berkeley Applegate* the liquidator's application was not made before considerable costs had been incurred, it is plainly sensible for an insolvency practitioner faced with a situation where work needs to be carried out on assets which are (or may be) held on trust, to apply to the court in advance for a direction that he is entitled to charge for future work out of those assets. Otherwise, the practitioner runs the risk of then being out of pocket if the court refuses to exercise its discretion in his favour.

16. Edward Nugee QC alluded to this concern in *Berkeley Applegate* itself at 53E:

"But the liquidator is entitled to know at this stage that his proper expenses and remuneration will be paid if necessary out of the trust assets, and that he will not be left at the end of the winding up with the possibility of receiving no recompense for his work or having to bear part of the expenses out of his own pocket"

17. This risk is potentially a very serious practical obstacle to the operation of the liquidation or other insolvency regime. It is one thing for the office holder to have concerns about working for free (not that one would expect him/her to be enthusiastic about such an occurrence), but there is every risk of them working at a loss as a result of needing to incur the costs of solicitors and most likely counsel. If the administration of the insolvency regime takes one into the territory of *Berkeley Applegate*, the legal issues being confronted are unlikely to be straightforward. Indeed in many of the cases where *Berkeley Applegate* relief has been invoked, the legal issues resembled a hideous blend of trusts, company and commercial law exam questions.

(3) Potential disputes between office holders and third parties asserting beneficial interests over assets held by the insolvent entity

18. While pre-emptive relief is commonly granted, the Court will exercise caution if the proposed work involves potential disputes between the insolvent company and third parties claiming to be trust beneficiaries. In *Re Biddencare,* [1993] B.C.C 757; [1994] 2 BCLC 160, the parent company, Biddencare Ltd, went into liquidation. Its subsidiary, Hartford Fire Insurance Co., sought directions as to whether moneys held in three bank accounts belonged to it. The liquidators of Biddencare sought a direction that:

" ... all proper fees and proper charges, costs, disbursements, expenses and liabilities of and incurred by or on behalf of the joint liquidators in their capacity as liquidators of Biddencare Ltd, including for the avoidance of doubt such fees, charges, costs, disbursements, expenses and liabilities incurred in responding to, investigating and (if thought fit) defending, compromising or complying with proprietary claims against assets vested in Biddencare Ltd, do rank as a charge on the assets held by or to the order of or reputedly belonging to or hereafter recovered for Biddencare Ltd in priority to any proprietary claims but without prejudice to the ultimate incidence thereof as between trust and other assets or as between proprietary claimants."

19. The size of the proprietary claims exceeded the assets of Biddencare, and the affairs of that company were in such a mess that it was anticipated that further proprietary claims would appear in due course. Mary Arden QC (sitting as a deputy judge of the High Court) observed that the costs direction sought had no limit in time or amount, and conferred no power on the court to disallow any costs upon the trial of the substantive application.

20. The liquidators were represented by Michael Briggs QC (now Lord Briggs), who advanced three arguments as to why the court had jurisdiction: (i) the court should perform a balancing exercise between the aggrieved claimant, and the interests of the office holder who was undertaking an exercise that had to be done by someone at some point, based on *PWC v Dixon* [1983] 2 All ER 158; (ii) jurisdiction could be derived from *Re Beddoe* [1893] 1 Ch 547; (iii) a liquidator is not obliged to seek a fighting fund from creditors (as is ordinarily the case) if there are special circumstances, following *Re Westdock Realisations Ltd* (1988) 4 BCC 192. The purported beneficiary, Hartford Fire Insurance Co., resisted, represented by Gavin Lightman QC

21. The judge observed and found as follows. There was a balancing act to be performed. The *Re Beddoe* jurisdiction line of cases also led to *Re Evans* [1986] 1 WLR 101 in which the Court of Appeal concluded that adult beneficiaries should pay to defend the trust in question, the parallel being that it should be the creditors of the company that should pay to defend the assets under attack. Further, whereas in *Westdock*, Sir Nicholas Browne-Wilkinson V-C had recognised the need for the due administration of an office holder's duties to get a determination by the court in respect of disputed property, and gave the example of large classes of creditors, with representative members joined into the proceedings since the sum due to each individual was too small to justify participation, and whereas an agreement to cover all costs out of the fund is often entered into at the start, that does not give rise to a general rule appliable in all cases.

22. This led the judge in *Biddencare* to conclude that a *Westdock* type order will only be made in very exceptional cases. She observed (at 765d):

> *"The courts have to bear in mind that a pre-emptive order is unusual and can clearly result in injustice if the other party establishes his proprietary claim over assets which have been reduced by the payment of the costs of resisting his claim. It is the other creditors in the liquidation, and not the applicant, who should bear the burden of the costs of unsuccessfully defending the applicant's claim.*

I do not see in this case any countervailing factor of sufficient weight to outweigh these factors. As it is, on the material which I have, in my judgment, the balancing exercise which the court must perform in this case produces the clear answer that no pre-emptive order should be made. If I am wrong on that, I accept Mr Lightman's submission that the court cannot be satisfied that it is likely that an order would be made at trial for the payment of the liquidators' costs out of the assets the subject of the applicant's claim, even if the liquidators were unsuccessful. This is hostile litigation."

23. So it seems the existence of hostile litigation (where the winner expects to recover costs) would generally operate as a bar to a pre-emptive costs order, because it would run contrary to the costs outcome at trial if the claimant won and recovered its assets on trust from the company in liquidation.

24. Needless to say, every case turns on its facts, and it is beyond the scope of this note to consider every eventuality. However useful illustrations involving liquidators can be found in *Alsop Wilkinson v Neary* [1996] 1 WLR 1220, *Re Telesure Ltd* [1997] BCC 580, *Tom Wise Ltd v Fillimore* [1999] B.C.C, *Re Local London Residential Limited* [2004] EWHC 114 (Ch); [2004] 2 BCLC 72 and *Re Trident Fashions plc* (unreported, 12th October 2005).

25. However a practical way to assist in such claims similar to *Biddencare* can be the invocation of the jurisdiction identified in *In Re M F Global UK Ltd (in special administration) (No.3).*[10] *MF Global* type orders are particularly useful in the early stages of a collapsed investment vehicle to allow the crafting of directions to quickly and efficiently resolve potential claims, and more importantly to allow the accelerated distribution of assets to client beneficiaries when the directions process identifies that no competing claims are made over that client's assets or part of those client's assets.

26. In *M F Global*, a broker dealer collapsed into insolvency and the terms of the CASS 7 trust resulted in the pooling of client monies. There were a large number of claims and potential claims over the trust monies. The Court recognised that the administrators in assessing trust claims were in a similar position to an office holder facing numerous creditor claims (at [9]) and that there was a need for a mechanism to deal with claims they had rejected informally by the administrators and potential claims otherwise there could be no distribution from the estate until all claims had been fully and finally identified and determined (at [13]).

[10] [2013] 1 WLR 3874, David Richards J.

27. The administrators proposed, and the Court approved, a mechanism that mirrored the English proof of debt procedure: submission of written claims by claimants together with supporting evidence, acceptance or rejection of claims by the administrators together with the provision of reasons for the same and the time-limited right of appeal against any rejection (at [17]). The approved mechanism also provided that the administrators should not have any liability for any distribution of assets to any trust claimant who subsequently asserted or established a claim (at [21]). David Richards J. reviewed the inherent jurisdiction of the Court in relation to trusts and considered that this jurisdiction permitted a mechanism for such directions to deal with trust property (see paragraphs [25]-[32]).

28. Directions broadly similar to those approved in *MF Global* can provide a practical means of allowing an office holder to invite, review and provide some initial form of adjudication on proprietary claims over assets held by the insolvent entity. Such directions were ordered in the context of a collapsed online broker dealer in *In the matter of Onetradex,*[11] in which the directions provided for the notification of claims to the provisional liquidator, the preliminary adjudiciation of such claims by the provisional liquidator and the sanctioning of the transfer of trust assets agreed between the provisional liquidator and the claiming client. Consistent with the principles in *Biddencare*, the directions provided that if the *MF Global* process did not result in an agreed resolution then the management of any remaining disputes would be remitted to the Court for further directions. The process was described by the Court as "*a procedure which properly balanced the interests of established clients to a timely return of their money with the interests of persons with serious but unresolved claims*."[12]

29. The jurisdiction applies not only in company liquidations, but also to trustees in bankruptcy. However the existence of hostile litigation remains a problem. In *Credit and Mercantile Plc v Kaymuu Ltd* [2014] BPIR 1127, a trustee in bankruptcy sought to take fees from assets held on trust on the basis that he was seeking to protect the interests of the creditors in the bankruptcy. As a matter of sentiment, it probably did not assist that the trustee was unsuccessful in the relevant litigation by the which the estate sought to avoid the contention that the primary asset of the estate was held on trust for another. In any event, the court observed (at [223]-[224]):

> *"[223] However, the discretion will not normally be exercised in favour of a person pursuing, or investigating whether to pursue, an interest adverse to that of the beneficiary, i.e. where the person seeking the allowance maintains that the beneficiary is not entitled*

[11] *In the matter of Onetradex Limited* (unreported, 1 October 2020, Smellie C.J.) at [22].
[12] At [22].

to the property from which the allowance is sought; as distinct from the situation where the allowance is sought in respect of work done for the purposes of advancing, enforcing and giving effect to the beneficial interests of those entitled to the trust property: see per HHJ David Cooke in Green v. Bramston at paragraphs 35-36.

[224] While HHJ David Cooke did not rule out the grant of an allowance from trust property in respect of work done to advance an interest adverse to the person subsequently found to be the beneficiary under the trust, it is clear that he considered that this would be wholly exceptional. I agree. In such a case it is not enough to show that the work done "benefited" the beneficiary by helping to show that his claim was good despite the efforts of the doer of the work to argue the contrary. Unsuccessful litigants often do work in their own interest, the fruits of which turn out to favour their adversary's; yet they are normally ordered, for their pains, to pay costs not receive them."

(4) *Gillan v HEC* : a cautionary tale

30. Finally, any discussion of the application of the *Berkeley Applegate* jurisdiction would not be complete without reference to the position the office holder found himself in in *Gillan v HEC*.

31. In *Gillan*, two companies (HEC and DPO) had contracted with various members of the rock music band Deep Purple to provide certain services and to account for royalties. Those companies were the subject of litigation concerning the beneficial ownership of the copyright in recordings and compositions. The companies went into administration and the administrators found themselves in a somewhat typical *Berkeley Applegate* factual matrix – office holders in control of a company whose assets might belong beneficially to another.

32. Mr Justice Morgan observed:

"[30] Property in which the company does not have a beneficial interest is not "the property of the company" as that phrase is used in Schedule B1 to the 1986 Act. If the company holds property on trust for others, an administrator does not become a trustee of that property. The company remains the trustee. Accordingly, an administrator does not owe the duties of a trustee to the beneficiaries under the trust. However, an administrator's functions and powers extend to doing anything necessary or expedient for the management of the affairs of the company. This gives an administrator power to do

what is necessary or expedient in certain respects in connection with property held by the company as trustee."

33. The Court was quick to recognise that in such circumstances, it is often appropriate for an administrator to apply to court for directions as to what is to be done, and that it is often appropriate for the court to permit the administrators to administer funds held on trust, *Re M F Global UK Ltd (No.3)* being such an example.

34. Unfortunately the administrators, having professed their intended neutrality in the litigation, proceeded on an assumption that there would be no question as to whether they would be paid in respect of the work they chose to do, whether out of the company's assets or the trust assets. As the learned judge observed (at [40]): "*The administrators' attitude was that they knew best and, in addition, they were entitled to be paid for the work they chose to do out of the assets owned by the Claimants.*"

35. Ultimately the court was not prepared to grant broad *Berkeley Applegate* relief. It considered carefully the categories of work that were said to have been done, and concluded that the sums claimed by the administrators in relation to the litigation should be dealt with under the court's jurisdiction as to the costs of litigation and not under *Berkeley Applegate*. It also refused to allow the costs for work that was beneficial to the unsecured creditors and adverse to the interests of the beneficiaries. The learned judge observed (at [104]):

> "*There are features of this case which distinguish it from Berkeley Applegate and Allanfield, relied upon by the administrators, and, indeed, from the type of case considered in Re Lehman Bros International (Europe) Ltd (No. 2) and in Re M F Global UK Ltd (No. 3) . This was not a case where a company in administration held substantial funds on trust for a large number of beneficiaries where the obviously most convenient course was for the administrators to administer the trusts and distribute to the beneficiaries. This is a case of two companies which had failed to perform their contract with the Claimants and had been sued as a result. At an early point, following the companies entering into administration, the Claimants sought the administrators' consent to continue the proceedings. I consider that the administrators ought to have given that consent. It would then have been for the Claimants and the estates of the managers and any other rival claimant to sort out the dispute, by pursuing the litigation and/or by attempting to settle it. The administrators did not give the consent they should have given. Further, they did not seek directions as to what they should do. They decided that matter for themselves. Part of the time, they acted in the interests of the unsecured creditors and not in the*

interests of the beneficiaries, as described above. The administrators also seemed to think that they could appoint themselves as mediators of a settlement between various parties but without the consent of those parties. They seemed to think that if they acted in that way they would be entitled to charge the beneficiaries remuneration for so acting. In the event, insofar as the administrators took on the role of mediators between beneficiaries, they did not bring about a settlement of the issues between them and conferred no real benefit on them. The administrators have spent considerable time and incurred considerable costs in opposing the Claimants' applications for consent to continue the litigation and in pursuing their own applications for orders that they be paid their remuneration and charges."

The moral of the story must therefore be this. The Court will generally be sympathetic to an office holder finding himself at the controls of a trust, and if it is sensible for him to administer it, and he asks first, he will most likely be permitted to take his costs of so doing from the trust. But if he makes assumptions as to his entitlements, and seeks to become entangled in litigation pertaining to the trust, those costs will not be permitted, and he runs the risk of tainting his application as a whole.

Contested reconstructions – how best to withstand the anticipated challenge

Lexa Hilliard QC, Zoë Barton QC and Jamie Holmes

(Written contribution from Alice Hawker)

VIVE LA DIFFERENCE: Emerging differences between schemes, plans and CVA's

Why there should be so many differences between schemes, restructuring plans and CVAs is a matter of history and possibly some sadistic civil servants. Whatever the reason, the differences do create headaches for us and can be very confusing for those who seldom dive into this area. This section of the discussion is aimed at identifying the main differences between the 3 types of restructuring mechanism so that when confronted with clients in financial difficulty you will have an initial roadmap to take them down in order that they can consider their options:

Part 26 Scheme	**Part 26A Restructuring Plan**	**CVA (outside an insolvency process)**
Solvent companies can scheme as long as the scheme is a "compromise" or "arrangement"	A company has encountered or is likely to encounter financial difficulties that are affecting or will or may affect its ability to carry on business as a going concern[13]	Insolvency not mandatory
Creditor selection – creditors or a class or classes[14]	Creditor selection – creditors or a class or classes[15]	All creditors (and members)
Secured creditors in a class can be schemed	Ditto	A secured creditor must consent[16]
Prior documentation required – New Practice Statement Letter & Explanatory Statement	Prior documentation required – New Practice Statement Letter & Explanatory Statement	None – but proposal and statement of affairs must be sent to nominee[17]
Different classes – if rights (not interests) of creditors are so	Ditto – although potentially different considerations	None

[13] CA 2006, s.901A (A). The purpose of the plan must be to "eliminate, reduce or prevent, or mitigate the effect of, any of the financial difficulties" referred to in (A): CA 06, s.901A(3)(b).

[14] "The ability of a company in financial difficulty to propose a compromise or arrangement to some, but not all of its creditors is one of the most flexible and valuable features of the scheme jurisdiction" of creditors to which it will propose a compromise or arrangement": *Re Virgin Atlantic Airways* [2020] EWHC 2376 (Ch) at [62] – also see fn 17 below.

[15] Ibid.

[16] IA 86, s.4(3): Neither the company nor its creditors may approve any proposal or modification which affects the rights of a secured creditor of the company to enforce its security except with the concurrence of the creditor concerned.

[17] IA 86, s.2(3).

dissimilar as to make it impossible for them to consult together – if the scheme fails will there be more to unite than divide the creditors in the class?[18]		
Convening hearing: Classes Whether any jurisdictional roadblock[19]	Ditto – but also creditors can be excluded at this stage if court satisfied that they do not have a genuine economic interest[20]	No convening hearing but nominee must report to court within 28 days whether the proposed CVA has a prospect of being approved and implemented[21] Unregistered companies under s.221 IA 86 not permitted[22]
Lock up fee permitted if disclosed and offered to all: Work fee permitted as long as not significant and not dependent on sanction[23]	Ditto	Not typical – but risk is of an unfair prejudice or material irregularity challenge[24]
Meetings – no specific period of notice required and no specific method[25]	Ditto	Meetings - 14 days' notice of qualifying decision procedure[26]
Sanction – majority in number and 75% in value of each class	Sanction – 75% in value of each class – no numerosity requirement[27]	Approval - Majority in number of members and creditors and 75% in value of all creditors
Court can sanction[28] even if a class dissents if having regard to the value of the company's assets that class has no economic interest in them[29]	Court can sanction if a class dissents if A: none of the members of the dissenting class would be any worse off than they would be in the	No court sanction required

[18] *Re Primacom Holding Gmbh* [2013] BCC 201 at [44] to [45].
[19] Is the entity a company liable to be wound up under the IA 1986 and has a sufficient connection with the UK.
[20] CA 06, s.901C(4).
[21] IA 86, s.2(2).
[22] IA 86, s.1(4) (a) a company registered under the CA 06 in England and Wales (b) a company incorporated in an EEA State; or (c) a company not incorporated in an EEA State but having its COI in a member State (other than Denmark) or in the UK.
[23] *Re Bibby Offshore Services Plc* [2017] EWHC 3402 (Ch) at [26] to [27]; *Re Noble Group Ltd* [2019] BCC 349 (sanction judgment) at [55]-[56]; *Re NN2 Newco Ltd* [2019] EWHC 1917 (Ch) at [46].
[24] But see *Re New Look* [2021] Bus LR 915 at [86]—[105] & [299]-[304]; *Regis UK Ltd* [2021] EWHC 1294 (Ch) at [59] – non disclosure in a CVA is not a material irregularity unless there is a substantial chance that the non-disclosed material would have made a difference to the way in which creditors voted at the meeting – although collateral advantages must be disclosed.
[25] *Castle Trust Direct* [2021] BCC 1 at [36] to [44].

[26] R.15.11 2016 IR.
[27] CA s.901F(1).
[28] The "arrangement is such as an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve: *Re National Bank Ltd* [1966] 1 All ER 1006 at 1012.
[29] *Re Tea Corp Ltd* [1904] 1 Ch 12; More recently *Re MyTravel Group Plc* [2004] EWHC 2741 (Ch); *Re Bluebrook Ltd* [2009] EWHC 2114 (Ch) at [25]; *Re Deep Ocean I UK Ltd* [2021] EWHC 138 at [50].

	event of the relevant alternative B: the plan has been agreed by 75% in value of a class of creditors who would receive a payment or have a genuine economic interest in the company, in the event of the relevant alternative[30]	
Sanction requirements: i) Statute complied with ii) class or classes fairly represented iii) is scheme fair which a reasonable creditor would approve iv) any blots or defects?[31]	Ditto – but if cross-class cram down then further considerations as above	Sanction not required – but chairman of meeting must report result of meeting to court[32]
No time bar on second or third schemes[33]	Ditto	Ditto[34]
Challenge? No obvious route after sanction	Ditto	28 days after report filed in court – unfair prejudice or material irregularity[35] or during implementation is dissatisfied with act, omission or decision of supervisor[36]

PROS AND CONS

Given the differences above, and as set out elsewhere in the legislation, will a wedge begin to emerge between plans and schemes? We will consider a few of the trends in recent years.

[30] CA 06, s.901G.
[31] *Re Noble Group Ltd (sanction)* [2019] BCC 349 at [17].
[32] IA 86, s.4(6) – although it is the meeting itself that binds the creditors not the report to court.
[33] See e.g. *Re Amigo II* [2022] EWHC 1318 – 1st scheme convening hearing 14 May 2021; 2nd scheme convening hearing 8 March 2022.
[34] But compare position in IVAs – IA 86, s.252(1)(c).
[35] IA 86, s.6(1)(a) & (b).
[36] IA 86, s.7(3).

1. Lock up agreement and related fees

There have been a large number of decisions considering these in recent years in the context of schemes. It is often overlooked that there are two issues here:

1. Class composition at the convening hearing. This is the subject of most of the cases.
2. The issue for the sanction hearing of whether sufficient information has been given to enable an intelligent and honest creditor to reasonably approve the scheme, so as to satisfy the Court that the results of the meeting are fairly and properly representative of the interests of the class as a whole[37].

The more typical issue is whether the fact that some creditors have been locked up 'fractures' the class, requiring a separate meeting that may give rise to an effective veto on the part of the very people the company could not lock up. It is well-established that the mere fact that some creditors have been locked up does not fracture the class[38]. It is also well-recognised that lock up agreements can have numerous benefits. They are often presented by a group of creditors (often an ad hoc committee of bondholders) who provide bridging finance and front other costs of the scheme, who in turn want a degree of certainty[39]. They can also reassure the Court at the sanction stage as to the likely enforceability of the scheme outside the jurisdiction[40].

What has proved more controversial are the various benefits that lock up agreements often provide for. The cases in this area can be reduced to broadly three principles:

1. The guiding principle has been expressed in a number of ways but is essentially whether the benefit is being offered as a 'bounty' in the event that the scheme is approved, as opposed to it being something that will be incurred in any event and/or which has an independent commercial rationale.
2. A further significant factor will be whether the benefit was open to all creditors.
3. Even failing both of the above, many cases are decided on the basis that the sum in question was simply not material[41].

[37] This second point can be seen in particular in the failure to obtain sanction in *Sunbird* [2020] EWHC 2493 (Ch) (Snowden J) and see also 'Amigo' or *All Scheme Ltd* [2021] EWHC 1401 (Ch) (Miles J).
[38] *Re Telewest* [2004] EWHC 924 (Ch) [53] (David Richards J).
[39] *Codere* [2020] EWHC 2441 (Ch) [57-60] (Falk J).
[40] *Codere* [2020] EWHC 2683 (Ch) [35] (Falk J).
[41] See the guidance in *Re Noble Group* [2018] EWHC 2911 (Ch) [149] (Snowden J).

Broadly the same considerations apply whatever the form of payment, although the Courts appear to have applied greater scrutiny as the boundaries are pushed. (A) 'consent fees' in favour of those who agree to lock up, even where these vary depending on how early that was done, tend to survive if they meet 2 and/or 3 above. As do (B) the payment of the various professional fees incurred by the creditor propounding the scheme. Where (C) those fees have not yet been incurred and/or include a success fee, they have proven more controversial[42].

Are plans being approached any differently? If we were to include a further principle (4) to those above from the scheme cases it would be that the Courts have often expressed reluctance at granting an effective veto to those not being locked up[43]. This consideration does not apply to plans at all if a cram down is sanctioned. Indeed the considerations are reversed: the company now only needs one (locked up) class of in the money creditors to vote in favour.

This may begin to have a significant impact at the sanction stage, as to whether the Court should exercise its discretion in favour of a cram down. We come on to this below. But otherwise, thus far, the Courts appear to be taking broadly the same approach with plans as with schemes and applying the same three guiding principles 1-3 above[44].

2. The cram down power

The cram down power is an obvious and inevitable difference between schemes and plans, as it is not available in a scheme case. It can only be exercised if the two jurisdictional criteria A-B set out in s901G are met. The focus to date in the authorities has primarily been on determining the 'relevant alternative' and whether those to be crammed are 'no worse off'; there has been less emphasis on Condition B. In any event, even where both Conditions are met, that is not enough. There is still a discretion for the Court to sanction, or not.

Much has been written about the cram down power in the past two years and it is a large topic in and of itself. Our focus is on three points:

[42] See in particular *Codere* [2020] EWHC 2441 (Ch) (Falk J), *Port Finance* [2021] EWHC 378 (Ch) (Snowden J) and *Safari* [2022] EWHC 781 (Ch) (Adam Johnson J); the latter two suggesting that transparency was a significant factor in allowing the matter to then be left to the creditors to vote upon.
[43] See e.g. *ColorOz* [2020] EWHC 1864 (Ch) [110-111] (Snowden J).
[44] *Hurricane* [2021] EWHC 1418 (Ch) (Zacaroli J) and *ED&F Man* [2022] EWHC 433 (Ch) (Michael Green J).

1. Lock up agreements (again). At least a degree of reservation has been expressed, albeit *obiter*, as to whether the Court would sanction a plan where lock up agreements have been used to ensure the Conditions of the cram down power were met[45]. Relatedly, it has been suggested, again *obiter*, that where the possibility of artificiality in the creation of the various classes (to ensure that the cram down Conditions are satisfied) becomes apparent only at the sanction stage when the cram down power is sought to be exercised, that may be a ground on which the court will be prepared to revisit – at the sanction hearing - the conclusion that it reached on classes at the convening hearing[46].

2. A number of cases have now also referred to the possibility that the class composition analysis at the convening stage may involve different considerations to those in a scheme case, in particular as to the need to avoid an artificially large number of classes[47]. As above, this is the opposite concern to that in the scheme cases.

3. The guidance emerging from the authorities on the exercise of the cram down power to date suggests that the discretion at the sanction stage is a very real one, notwithstanding that where the two jurisdictional Conditions are met it has been said that the application will have a 'fair wind' behind it[48]. Even putting aside the valuation issues, this may in time result in sanction hearings for plans looking rather different to those for schemes.

3. The timing of hearings

Scheme cases often move at pace. Indeed an applicant will often rely on the alleged urgency of the application, failing which it is said that the company will be forced to enter into some less-advantageous insolvency process, as part of its underlying commercial rationale.

The plan cases have suggested a number of competing considerations in this regard. The jurisdictional hurdles to invoke the cram down power give rise to the possibility of protracted disputes as to valuation, and the Courts have held that this should not undermine the potential utility of Part 26A in

[45] See e.g. *Virgin Atlantic* [2020] EWHC 2376 (Ch) at [50] (Snowden J).
[46] *DeepOcean* [2021] EWHC 138 (Ch) [41] (Trower J).
[47] See e.g. *Virgin Active* [2021] EWHC 814 (Ch) [62] (Snowden J).
[48] *DeepOcean* [2021] EWHC 138 (Ch) (Trower J); *Virgin Active* [2021] EWHC 1246 (Ch) (Snowden J); *Hurricane* [2021] EWHC 1759 (Ch) (Zacaroli J); and *Amicus* [2021] EWHC 3036 (Ch) (Sir Alastair Norris).

an urgent case. At the same time, protections must be preserved for those seeking to oppose a plan, in particular a class that is to be crammed down[49].

Further, it is clear that the Court will not take an allegation of urgency at face value. Indeed it is in part for this reason that the plan in *Hurricane* failed: the Court not accepting the alleged urgency, and holding that there were prospects for various steps to be taken in the time available, in the alternative to the proposed plan and cram down.

Equally, even where there is urgency, the Court will be concerned to ensure that there is sufficient time for all interested parties to properly participate[50].

TENANTS' OBLIGATIONS – What are your best options to deal with significant liabilities against landlords?

Tenants will welcome the robust approach taken by Courts in recent cases in which the Court has made clear that it will look pragmatically at CVA proposals and Part 26A restructuring plans. This may prove troubling for landlords, who expect a contractual entitlement to a fixed income stream which does not sit comfortably within the rescue culture embodied in insolvency legislation.

After an attempted challenge to the *Debenhams* proposal was rejected in 2019[51], in a recent seminal decision Zacaroli J rejected the landlords' challenge to the *New Look* CVA[52]. Various landlords challenged the *New Look* Proposals' terms on three bases: challenging the limit of the CVA jurisdiction; material irregularity and unfair prejudice.

What are the main lessons to ensure a CVA stands up to landlord challenges?

1. Ensure that the statutory majority shares sufficiently similar rights with the minority it seeks to bind.

[49] See as to both of these considerations *Virgin Active* [2021] EWHC 1246 (Ch) [130] (Snowden J).
[50] This can be seen from both *Virgin Active* and *National Car Parks* [2021] EWHC 1653 (Ch) (Trower J).
[51] *Discovery (Northampton) Limited and ors v Debenhams Retail Ltd and ors* [2019] EWHC 2441 (Ch).
[52] *Lazari Properties 2 Ltd and ors v New Look Retailers Ltd and ors* [2021] EWHC 1209 (Ch) .

2. If claims for future rent are to be discounted, take an equal approach across landlords and consider what discount is justifiable: 25% in *New Look* was not materially irregular but 75% in *Regis*[53] was 'unjustified'.
3. It is typically permissible to treat creditors differently where it is 'essential' to the rescue of the business, such that payment in full of (e.g.) suppliers is needed to ensure business continuity.
4. Termination rights for unhappy landlords should be included as a matter of course in CVA proposals to address unfairness.
5. There is a gap in the rules on the electronic voting procedure: they do not provide a clear route for postponement[54] such that it could only be adjourned through a court order. Such application would be 'novel and would carry risks'.
6. Where a CVA strips a landlord of its right to pursue the tenant's guarantor, this must be adequately compensated to avoid unfair prejudice[55].

Whilst it is notoriously difficult to challenge a CVA, especially after the landlords' unsuccessful root and branch challenge in *New Look*, there is some scope:

1. Consider 'vertical' and 'horizontal' comparators[56]. Think laterally about other ways to attack the CVA and see *Regis* for inspiration of a successful challenge where the company's shareholder had wrongly been treated as a critical creditor.
2. Just because the same result may have been achieved in a part 26A plan, does not preclude a finding of unfair prejudice[57].

The introduction of the new Part 26A jurisdiction may seem more concerning to landlords. The power of cross class cram down enables a company to restructure its lease liabilities despite opposition from dissenting classes of landlords. However, a restructuring plan arguably presents a better forum for landlords to defend their interests *before* sanction and therefore offers a more efficient alternative.

[53] *Carraway Guildford (Nominee A) Ltd and ors v Regis UK Limited and ors* [2021] EWHC 1294 (Ch).
[54] *Ronald Young v Nero Holdings Ltd and ors* [2021] EWHC 2600 (Ch).
[55] See *Mourant & Co Trustees Ltd and anor v Sixty UK Ltd (in administration)* [2010] EWHC 1890 (Ch).
[56] See discussion by Zacaroli J at [107 – 110] of *New Look*.
[57] See the differences highlighted by Zacaroli J between the two at [199] of *New Look.*

Part 26A restructure is a powerful tool for tenants as recently exemplified by Snowden J's approach in *Virgin Active*[58]. Snowden J was satisfied that landlords would not be worse off than in the 'relevant alternative' and exercised his discretion to sanction the plans. Points to consider:

1. How to categorise a lease portfolio? See [59 – 64] of *Virgin Active.* There is no requirement to include all of a company's creditors. Where appropriate, leases may be excluded but this would need to be justified at the sanction hearing.
2. Even where there are good commercial reasons for differential treatment between unsecured creditors, a plan should not discriminate arbitrarily or capriciously.
3. What is the 'relevant alternative'? It is not what will occur on the balance of probability, but what is most likely to occur as at the date of the hearing (although in reality, what is the difference between the two tests?).
4. The Court will not have the usual reluctance (as it would under schemes of arrangement) to differ from the vote where cross class cram down is applied under Part 26A[59].

[58] *Re Virgin Active Holdings Ltd* [2021] EWHC 1246 (Ch).
[59] *Re DeepOcean 1 UK Ltd* [2021] EWHC 138 (Ch) at [46].

Developments in directors' duties

ESG and directors' duties

Bobby Friedman

1. The issue of directors' duties in the context of ESG is a particular "hot topic" and it is to be expected that the scope of directors' duties in this context will continue to be the subject of discussion – and litigation - for some time.

2. At present there is relatively little decided case law on the topic. However, in *McGaughey v Universities Superannuation Scheme* [2022] EWHC 1233 (Ch) Leech J dealt with an application for permission to bring a derivative claim against the trustee company of a pension scheme. The Claim was brought on four bases, one of which was the alleged failure of the current and former directors of the trustee company to "*create a credible plan for disinvestment from fossil fuel investments*". It was said that this "*has prejudiced and will continue to prejudice the success of the Company"*. The premise of this part of the Claim was that the pension scheme continued to invest directly and indirectly in fossil fuels, and that, while it had announced it would aim to be carbon neutral by 2050, the directors had failed to form an adequate plan to deal with the financial risks involved in such investments. It was also said that the directors had failed to take into account relevant considerations, including the Paris Agreement in 2015. An attempt was made to argue that the directors had furthered their own interests by putting their own beliefs above the interests of the beneficiaries and the trustee company.

3. The case put forward by the Claimants seems to have been very thin. The evidence that there had been significant detriment to the beneficiaries was based largely on *Financial Times* articles, a study from Imperial College, and the evidence of a witness without expertise in the area. In contrast, the trustee company put forward detailed evidence about how the directors had exercised their discretion concerning investment, including by taking legal advice, surveying members, and aiming for net zero by 2050.

4. The Claim was rejected on the basis that there was not sufficient evidence that the company had suffered a financial loss; and because the Claimants had not suggested that they had themselves suffered loss. It is also interesting that the Court cited with approval *Cowan v*

Scargill [1985] Ch 270, a decision concerning trustee investment duties. The Court inferred that it was on the basis of that decision that the argument could not be made that the trustee company had a duty to sell fossil fuel investments for ethical reasons.

5. This is unlikely to be the end of the story. ClientEarth has announced in recent months that it is pursuing a derivative action against the directors of Shell, arguing that the directors are in breach of their Companies Act 2006 duties. That case is likely to lead to a much more detailed and focused consideration of the issues concerning ESG and directors' duties. Moreover, there may well be cases where claimants are able to make a much more cogent case of direct financial loss than the Claimants in *McGaughey*.

6. There are more fundamental questions that are likely to be litigated at some point in time. While it might be assumed that directors owe their duties to shareholders (other than in the insolvency context where the interests of creditors come into play), it is to be expected that the point will be taken that the duty is to stakeholders more broadly. If that argument were to succeed, then it might be possible to show a breach of duty on a wider basis than previously envisaged. Moreover, in circumstances where ethical, green investments are widely seen as desirable – and investments in fossil fuels and the like less desirable – it can be envisaged that there will be an increasing number of circumstances in which directors or trustees might argue that, taking into account the interests of the shareholders or the beneficiaries, there is a sufficient commonality of view on the point that there should be disinvestment from fossil fuels or other such investments.

7. More generally, the importance of ESG will drive how directors decide what is in a company's best interests. In circumstances where there are potential reputational downsides to a company in investing in environmentally unfriendly investments, or undertaking environmentally problematic activities – and in a world in which a sharp focus on social media may quickly lead to company boycotts, it can readily be seen how a director might be nervous about such activities. Indeed, for an ESG-focused director, such considerations may well lead to an overall decision to move away from such investments, or to actively promote ESG-friendly practices, even if at an up-front cost to the company. These decisions can be far more readily justified than might have been the case even a few years ago.

Directors' duties and tax avoidance

Daniel Lewis

1. A director is entitled to arrange a company's affairs to minimise its tax liability, providing that this does not cross the line into dishonest tax evasion. Either a scheme is successful in avoiding the tax charge prescribed by legislation or it does not, but entry into the tax avoidance scheme is not itself a breach of duty. This point was made by Patten J in *Re AG (Manchester) Ltd (formerly known as The Accident Group Ltd) (in liq.)* [2008] B.C.C. 497 at [166] to [168], in the context of disqualification proceedings, but of equal application to the question of breach of duty:

> *"166. Companies like anyone else are at liberty to arrange their affairs in a way which minimises the tax liability of themselves and their employees provided that they act lawfully. It goes without saying that it would be both unlawful and an issue of fitness for the directors of a company to enter into a scheme which was intended to defraud the Revenue…*
>
> *168. A tax scheme which does not satisfy the requirements of s.239 of the Taxation of Chargeable Gains Act 1992 is not per se a fraud on the Revenue nor is it unlawful. It is simply ineffective with the result that the payments made bear the tax which they would otherwise have attracted. Although one is entitled to disapprove of artificial schemes of this kind, it is quite another thing to regard their promotion as conduct which renders a person unfit to be director of a company. There is no suggestion in this case of any attempt being made by Mr Watson or the other directors to conceal from the Revenue the true facts of the trust arrangements. Once disclosed, it would be a matter for each director as the taxpayer to deal with any refusal by the Revenue to recognise the effectiveness of the scheme."*

2. Claims against directors in relation to tax avoidance schemes tend to fall into three categories:

   Claims where the transactions by which the intended tax avoidance was effected are unlawful per se. These usually involve an allegation that the payments amounted disguised distributions which were ultra vires. *Toone v Ross (Re Implement Consulting Ltd)* [2020] 2 B.C.L.C. 537 is a recent example of this.

Claims where the decision to enter into or continue with the tax avoidance scheme is said to have been in breach of the director's fiduciary duties. *Re Vining Sparks UK Ltd* [2020] S.T.C. 410 was one such unsuccessful claim involving an allegation of dishonesty against the director; *Hunt v Balfour-Lynn (Re Marylebone Warwick Balfour Management Ltd)* [2022] EWHC 784 (Ch) was another, but this time involving breach of the *Sequana* duty to consider the interests of creditors.

There are also the cases where the transactions by which the tax avoidance was effected are attacked under anti-avoidance provisions in the Insolvency Act 1986 (**'IA86'**); for instance, an allegation that the transactions fall within section 423 as transactions defrauding creditors (see, for example, *Re Marylebone Warwick*).

3. Which, if any, of these claims will be available to the liquidator will depend to a great degree upon the characterisation of the payments by which the tax avoidance was effected. Some of the advantages and pitfalls of each of these routes of claim are discussed below.

(1) Tax schemes to effect disguised distributions

4. Tax schemes often involve providing rewards to the employees (who are also the shareholders) other than by conventional (and conventionally-taxed) remuneration. This may involve the payment of money to the employee/shareholder through a trust arrangement (such as an EBT) or the allotment and then purchase of shares by the company.

5. The principles applicable to such claims are now well-established:

The question of whether the transaction is a distribution is a question of substance, not one of form or how the parties chose to describe it (*Progress Property Co Ltd v Moore* [2011] 1 WLR 1 at [1]).

The question of whether the distribution contravenes Part 23 is answered objectively by reference to the relevant accounts; the factual or legal knowledge or understanding of the company is irrelevant (*It's a Wrap (UK) Ltd v Gula* [2006] BCC 626 at [43]).

The application of Part 23 is strict and cannot be eroded by a plea of ratification (*Bairstow & Ors v Queens Moat Houses plc* [2002] BCC 91).

6. In *Implement* profits were extracted from the company, paid to an employee benefit trust (later an interest in possession fund), from which payments to the shareholders were effected. It was alleged that these transactions were in substance distributions to the shareholders, and therefore ultra vires (in addition to which claims for breach of duty in failing to take account of the interests of creditors and under section 423 of the IA86 were also made).

7. The disguised distribution analysis was accepted by Chief ICC Judge Briggs. He concluded (at [80]): (i) "looking through the eyes of the Company, that the payments… are to be characterised as a return of capital to the shareholders"; and (ii) that since the formalities required under Part 23 of the Companies Act 2006 (**'CA06'**) were not complied with, it followed that the returns of capital were unlawful.

8. That conclusion is not without some logical difficulties. First, the directors' evidence was that the payments were intended to reward employees and to incentivise them to remain with the company. More importantly, that is the basis upon which the company was assessed for tax. In *RFC 2012 plc (in liquidation) (formerly Rangers Football Club Plc) v Advocate General for Scotland* [2017] 1 WLR 2767 the Supreme Court decided that money paid into an EBT was intended to operate to give each employee access to the use of the money paid into the principal trust, that this money was to be treated as employee's remuneration for employment and subject to tax and that the employer company was required to have made the necessary deductions to pay the Revenue for PAYE and NIC.

9. That creates a logical contradiction in the position adopted by the liquidator in *Implement* and in disguised distribution claims in general. On the one hand he claimed that the payments were in substance distributions when viewed, as the Judge said, "through the eyes of the Company". On the other hand, the payments resulted in assessments and determinations for PAYE and NIC based upon their characterisations as remuneration for employment. It would be up to the liquidator whether to admit HMRC's proof for these claims. How can the liquidator argue one way in court and then accept the opposite position at the proof stage?

10. Secondly, the decision in *Implement* gives no credence to the argument that the payments were affected through trusts. Neither the trusts nor the trustees were impugned by the liquidator, nor was any finding to this effect made. How then can payments through a trust with, it must be assumed, trustees acting properly and independently be characterised in substance as a single transaction amounting to a distribution? In contrast in *Vining Sparks*, the lack of any

allegation of sham as to the arrangements entered into with the EBT meant the liquidators had to accept that the artificial elements of the arrangements truly existed (at [171]).

11. The judgment of Michael Green QC (then sitting as a Deputy Judge) in *Chalcot Training Ltd v Ralph* [2020] S.T.C. 1537 was critical of *Implement*, for its failure to consider whether there had been a genuine exercise of the power to award remuneration, the complicating factor of the interposition of the EBT and the difficulty reconciling the treatment of the transactions from a tax and company law perspective.

12. *Chalcot* was a somewhat extraordinary case since the company was seeking to re-characterise payments which were ostensibly directors' remuneration as unlawful dividends. The company wanted to do so in order to avoid determinations in respect of income tax and NICs and sought declarations that the agreements by which the scheme had been effected were void. Perhaps unsurprisingly, HMRC described this tactic as "brazen" since it was the very individuals who caused the company to use the scheme for three years running who were seeking to set aside the same transactions on the grounds that they were not the real transactions that they and the Company entered into.

13. The Deputy Judge held that the legal test for characterising the payments in issue was as follows:

> *"(1) The test is not a purely objective one;*
>
> *(2) The subjective states of mind of those deciding upon the transactions in question, in this case the payment of remuneration, can be relevant facts for the purposes of determining "the true purpose and substance of the impugned transaction";*
>
> *(3) The way those parties have chosen to describe the transaction both in the documents governing the transaction and also in other documents such as the Company's accounts (which were signed off on the basis that they showed a true and fair view) can also be relevant facts to be taken into account because they may indicate not only the true nature of the transaction but also what those deciding on the transaction considered it to be;*

(4) Ultimately, the Court will have to decide whether there was a genuine exercise of the power to award remuneration or whether that power was being used (or abused) to disguise the true nature of the payments which were really distributions to shareholders;

(5) In deciding whether there was a genuine exercise of the power to award remuneration, particularly in a solvent company, the directors will be judged in the way that other commercial decisions are adjudicated upon; the Courts will generally not interfere in commercial decisions taken by directors and a wide " margin of appreciation " is allowed (see eg. Para.120 of Re AMT Coffee Ltd [2019] EWHC 46 (Ch) , an unfair prejudice petition under s.994 of the Act, in which excessive remuneration was one of the allegations).

14. The company unsuccessfully appealed on narrow grounds relating to the allotment of shares at a discount ([2021] EWCA Civ 795). The findings at first instance summarised above were not challenged.

15. While the result in *Chalcot* is explicable on the basis that the company could not have its cake and eat it too, it does call into serious doubt the application of the law on disguised distributions to schemes of this nature. It is usual for the payments into schemes to be justified on the basis that they represent remuneration (for the obvious reason that the company is hardly likely to characterise the payments are disguised distributions). This was a feature of the schemes in *Chalcot*, *Implement*, *Vining Sparks* and *Marylebone Warwick*. If that characterisation is accepted, then the "easier" claims relying upon the strict approach to repayment of disguised distributions (as in *Implement*) will not be available. Instead the liquidator will have to bring the "harder" fault-based claims for breach of duty (as in *Marylebone Warwick* and *Vining Sparks*).

(2) Breach of duty in entering into and continuing tax schemes

16. There are two duties of particular relevance to claims against directors for breach of duty in relation to the operation of tax schemes:

The duty to act in the way the director considered in good faith would be most likely to promote the success of the company for the benefit of its members as a whole (section 172 of CA06); and

The duty to consider the interests of creditors where the company is or is likely to become insolvent (the *Sequana* duty). A further refinement to the *Sequana* duty is a duty to specifically consider HMRC as a "large creditor" when entering into tax avoidance. The existence of a duty to consider the interests of a particularly large creditor was recognised by Joanna Smith J in *TMO Renewables Limited (in Liquidation) v Yeo* [2021] EWHC 2033 (Ch) at [391(iii)].

17. The important point about the section 172 duty is (ordinarily) its subjectivity. It is not for the Court to impose its own assessment of what was in the company's best interest (*Re Regentcrest plc (in liq.) v Cohen & Anor* [2001] B.C.C. 494 at [120]). Only where there is no evidence of consideration of the best interests of the company, or a very material consideration has been overlooked, is the Court entitled to substitute its own objective assessment (*HLC Environmental Services* [2014] B.C.C. 337 at [92]).

18. It is for this reason that the director's reliance upon professional advice is of such importance. The *fact* that such advice has been sought demonstrates the director's consideration of the company's best interests. The *content* of that advice – assuming that it is in favourable as to the prospects of the scheme achieving its intended tax consequences and is from a reputable and apparently reliable source – entitles the director to adopt the scheme.

19. That the respondent directors had professional advice is therefore the most important reason for of the failure of the liquidators' claims for breach of duty in both *Vining Sparks* and *Marylebone Warwick*. In both cases the advice came principally from the promoters of the scheme. In *Vining Sparks* ICC Judge Jones held at [191]:

> *"Whilst the general guidance is that independent advice should normally be obtained, the guidance is not absolute and does not determine the subjective, good faith test. In the context of the backdrop evidence and the advice in fact received from Baxendale Walker and later Baxendale Walker MDP, it cannot be concluded that Mr Bernard acted in bad faith because no reasonable director could have concluded that Employee Scheme and the failure to claim the amounts due in respect of PAY and NIC from the Parent Company would promote the Company's success."*

A similar finding was made in *Marylebone Warwick*.

20. In both, the liquidator's case was that the advice of the scheme promoter was questionable and should not have been relied upon by the director. In *Marylebone Warwick*, the advice came from a "top-level" firm of tax advisors. The liquidator's attempts to impugn that advice were unsuccessful, including the suggestion that independent legal as opposed to taxation advice should have been sought ("a distinction without a material difference") or that there was a conflict of interest ("BDO had no 'vested interest in the company continuing to operate the Scheme' beyond the amour propre of any professional for the advice they were giving"). Given its source, the advice in *Vining Sparks* was perhaps more open to question, but without concrete grounds for doubting its accuracy, the director was held entitled to rely upon it.

21. The advice received also feeds into the application of the *Sequana* duty, and the additional duty to consider the interests of HMRC as a large creditor. As with the section 172 duty, that such advice is obtained demonstrates the directors considered the interests of creditors and HMRC specifically (*Marylebone Warwick* at [288]-[289]).

(3) Insolvency Act remedies for tax schemes

22. The anti-avoidance provisions of the IA86 have been something of a makeweight in claims against directors for tax avoidance. It is difficult to envisage a situation where transactions might fall foul of section 238, for instance, and not amount to a breach of duty, still less where section 423 is relied upon. While the steps by which the scheme is effected are likely to be transactions at an undervalue for the purposes of section 238, it is usually necessary to claim under section 423 to benefit from the unlimited look-back period.

23. While section 423 does not (despite its title) require fraudulent intent, it does require that the scheme have the purpose of prejudicing HMRC's claims. Usually legitimate tax planning (i.e. honest, whether or not effective) is entered into for the purposes of reducing a company's tax burden. It is not usually part of the purpose that the money be transferred to frustrate HMRC's potential future claims, even if that is a necessary consequence of the steps taken. The observations of Leggatt LJ in *JSC BTA Bank v Ablyazov* [2019] BCC 96 at [15] applied in *Marylebone Warwick* are likely to apply to any legitimate tax scheme:

> *"As Arden LJ emphasised, it is not enough to bring a transaction at an undervalue within s.423 that the transaction had the consequence of putting assets of the debtor beyond the reach of creditors. That is so even if the consequence was foreseeable or actually foreseen by the debtor at the time of entering into the*

transaction. Evidence that the debtor believed that the transaction would result in putting assets beyond the reach of creditors may support an inference that the transaction was entered into for the purpose of doing so, but the two things are not the same. To illustrate the distinction using a less homely example than that given by Arden LJ, a commander may order a missile strike on a military target knowing that it will almost certainly cause some civilian casualties. But this does not mean that the missile strike is being carried out for the purpose of causing such casualties."

Conclusions

24. Opinion has turned against tax schemes, compared to the period up to 2012 when many of EBT and conditional share schemes were widely promoted and operated. That will lead to a natural tailing-off of claims against directors for their operation, subject to two countervailing factors. First, it will often have taken many years for the company's tax liabilities to be settled and even longer for the companies involved to enter liquidation. Secondly, since the directors are also usually the beneficiaries of these schemes, the claims for breach of duty are subject to no limitation period. Claims continue to be made, although in the light of these recent cases their prospects of success appear more limited.

Liabilities of directors and IPs as "associated' with the company

David Pollard

Director as an associate

1. A director is someone who is "associated" with the company under s 435 of the Insolvency Act 1986 (***IA 1986***). In addition a director or a shadow director will be "connected with" the company under IA 1986, s 249. This association flows from the office and does not depend on any degree of shareholding in the company by the director.

2. For further detail on this, see David Pollard, '*Connected and Associated: Insolvency and Pensions Law*' (2021, Bloomsbury Professional).

3. Such association does mean that it is easier for an IP to seek a reversal of a transaction under the provisions in IA 1986.

4. Various other consequences of an "association" (or connection) include:
    - An associate of an employer can be the subject of a moral hazard order (financial support direction or contribution notice) by the Pensions Regulator under the statutory powers in the Pensions Act 2004.
    - Debts owing to connected persons need to be separately counted in a CVA;
    - Substantial disposals to a connected person (which includes an associate) within the first eight weeks of an administration require either creditor approval or a report from an "evaluator" – IA 1986, Sch B1, para 60A.

Who is connected or associated?

5. Directors (and officers) are associated with the company (IA 1986, s 435(9), applying s 435(4)) and hence connected with the company (IA 1986, s 249).

6. Shadow directors are not, as such, associated with the company but they are connected with it – IA 1986, s 249.

7. The term "officer" as used in IA 1986, s 435 probably in practice has the meaning given by IA 1986, s 251: An 'officer' includes a director, manager or secretary. The term "manager" is not expressly defined further.

IP as an associate/connected person

8. The question arises as to whether an insolvency practitioner acting in relation to a company is also connected or associated with the company.
9. The administrators of a company appointed under IA 1986 will each usually be officers of the company. In *R (Palmer) v Northern Derbyshire Magistrates' Court* [2021] EWHC 3013 (Admin), [2022] ICR 531, the Divisional Court confirmed that administrators were each an officer of the company over which they were appointed. This was for the purposes of the potential criminal offence of failing to notify the Secretary of State in relation to proposed collective redundancies under the Trade Union and Labour Relations (Consolidation) Act 1992. This was not a case on s435, but in my view it will be likely that an administrator will be considered an officer of the company for that purpose too.

10. Similarly liquidators would be officers and so are (probably) administrative receivers.

11. It is less clear whether a nominee or supervisor of a company voluntary arrangement (CVA) or a monitor of a Part A1 moratorium are officers (even if they are insolvency practitioners).

Manager

12. The term 'manager' means someone who manages: *Giles v Barton* (1875) LR 10 QB 329 and *Re Western Counties Steam Bakeries and Milling Company* [1897] 1 Ch 617 per Rigby LJ at p632.

13. However the term "manager' is vague and must be construed in context: *R v Boal* [1992] QB 591, CA at 597E and *DPP v TN* [2020] IESC 26 at [144]. It may be that the term "manager" is given a wider view for cases, such as the application of the insolvency clawback provisions, where the end result is not a criminal conviction on the manager[60] – contrast:

[60] In *DPP v TN* [2020] IESC 26, following an extensive discussion of the Irish and UK cases, the Irish Supreme Court made this point at [80].

- *In re A Company* [1980] Ch 138, CA (wide view - judge power to require documents to be produced); with
- *Registrar of Restrictive Trading Agreements v W H Smith & Son Ltd* [1969] 1 WLR 1460, CA (narrow view: order for attendance) or *R v Boal* [1992] QB 591, CA at 596 to 598 narrow view: (criminal conviction).

Insolvency legislation

14. The reversible transaction provisions in IA 1986, ss 238 and 239 are outlined in more detail below. They have special provisions in relation to persons connected or associated with the company.

    Broadly:

    (a) Voidable transactions

    If a transaction is in favour of such a connected party then the onus of proof can be reversed in one of the tests required to void the transaction. Ordinarily the insolvency practitioner would have to show an intention to prefer, but this is presumed (the presumption can be rebutted) if the counterparty is a connected party.

    (b) Time limits for challenges under IA 1986

    If a person is a connected party, this will extend the time limits for the challenge of an antecedent transaction under IA 1986, ss 239 and 245, and will change the burden of proof required for certain of the elements required to establish an offence under these sections.

Insolvency: Reversible transactions

A chart summarising the reversible transaction provisions applicable to companies is below.

Summary of ss 238, 239 and 245

	Section 238 – transactions at an undervalue	**Section 239 – preferences**	**Section 245 – floating charges**
Company needs to be 'insolvent' at the transaction date?	Yes	Yes	Chargee connected with the company – no Chargee not **connected** with the company – yes: s 245(4)
Insolvency presumed unless the contrary is shown?	Yes, if transaction with a person who is **connected** with the company – s 240(2)	No	No
Who can claim	Administrators or liquidators	Administrators or liquidators	Administrators or liquidators
Time limit before insolvency process started ("relevant time")	2 years – s 240(1)(a)	2 years if preference is given to a person who is **connected** with the company (otherwise than by reason only of being its employee) – s 240(1)(a). Otherwise, 6 months – s 240(1)(b)	2 years if charge is in favour of a person who is **connected** with the company – s 245(3)(a). Otherwise, 12 months – s 240(3)(b)
What transactions?	Transaction at an undervalue in the form of a gift or at significantly less value than consideration provided by the company – s 238(4). Court will not make an order if it considers that: ● the company entered into the transaction in good faith and for the purpose of carrying on its business; and ● at the time it did so there were reasonable grounds for believing that the transaction would benefit the company – s 238(5)	● puts a creditor in a better position; and ● company must be influenced by a desire to prefer. A desire to prefer is presumed unless the contrary is shown, if the preferred person is **connected** with the company (otherwise than by reason only of being its employee) – s 239(6)	Grant of a floating charge The invalidity only applies to the extent that any security exceeds the aggregate of (broadly) the value of the goods or services paid or supplied on or after the creation of the charge – s 245(2).

15. Similar provisions to ss 238 and 239 apply in an individual bankruptcy – IA 1986, ss 339 to 342.

16. Conversely, IA 1986, s 423, dealing with transactions at an undervalue if made for the purpose of putting assets beyond reach of a creditor, does not expressly use the terms

"connected" or "associated"[61]. In practice in an application under s 423 it is likely to be easier for a person to prove an undervalue or an improper purpose where the transaction involves someone who is closely associated (by whatever test).

Section 238: Transaction at an undervalue

17. A transaction at an undervalue arises where a company makes a gift or otherwise enters into a transaction on terms that the company receives no consideration or enters into a transaction for a consideration the value of which, in money or money's worth, is significantly less than the value, in money or money's worth, of the consideration provided by the company – IA 1986, s 238(4).

18. The court can set aside transactions entered into by the company at the 'relevant time' – s 238(2). The 'relevant time' is a period of two years ending with the onset of insolvency, whether or not the party was connected – s 240. The company must be unable to pay its debts at the time of the transaction or become unable to do so as a result – s 240(2). Where the transaction was with a connected person,[62] there will be a presumption of such insolvency (so the burden of proof is reversed).

Section 239: Preferences

19. A company gives a preference to a person if:
    - that person is one of the company's creditors or a surety or guarantor for any of the company's debts or other liabilities; and
    - the company does anything (or suffers anything to be done) which has the effect of putting that person into a position which, in the event of the company going into insolvent liquidation, will be better than the position he would have been in if that thing had not been done – IA 1986, s 239(4).

20. The company must have 'desired' to prefer the creditor, surety or guarantor – s 239(5). Where the transaction was with a connected person the burden of proof is reversed: there is

61 See eg John Briggs and John Tribe '*Muir Hunter on Personal Insolvency'* (Update to March 2021, Thomson Reuters) at 3-3078.

62 But see below where the connection is by reason of being an employee.

a rebuttable presumption that the company intended to put that connected person (other than an employee) in a better position – s 239(6).

21. The transaction must have taken place within the 'relevant time'. For a connected person this will be a period of two years ending with the onset of insolvency, for anyone else it will be a period of six months ending with the onset of insolvency – s 240(1).

22. As with transactions at an undervalue, the company must be unable to pay its debts at the time of the transaction or become unable to do so as a result – s 240(2). But unlike transactions at an undervalue, there is no presumption of insolvency where the preference was to a connected person.

Section 245: Invalid floating charges

23. A floating charge on a company's undertaking or property is invalid if:
    a. it was made within the 12 months ending with the onset of insolvency – s 245(3)(a); and
    b. in the case of a charge to a person connected with the company, at the time the floating charge was created, the company was unable to pay its debts within the meaning of IA 1986, s 123 or becomes unable to pay its debts as a consequence of the charge – IA 1986, s 245(4).
24. The invalidity only applies to the extent that any security exceeds the aggregate of (broadly) the value of the goods or services paid or supplied on or after the creation of the charge – s 245(2).

25. There are two differences where the charge is created in favour of a person connected with the company:
    a. the invalidity period is extended to two years prior to the onset of insolvency (rather than 12 months) – s 245(3)(a); and
    b. there is no need for the administrator or liquidator challenging the charge to show that the company was insolvent at the time or became insolvent as a result – s245(4).

26. A floating charge in favour of a person connected with the company (like any other) will still be valid to the extent that any security exceeds the aggregate of (broadly) the value of the goods or services paid or supplied on or after the creation of the charge and interest - IA 1986, s 245(2).

Time for connection

27. In all three cases, the connection test applies as at the time of giving the preference or transaction at an undervalue or creation of the charge. If the counterparty is not connected with the company at the time of the impugned transaction it is irrelevant for this purpose if it becomes connected later.

28. If the counterparty is connected with the company at the time of the transaction, the differences noted above remain applicable even if the connection is lost later – *Unidare*[63] (charge) and *Darty Holdings*[64] (preference).

Employee as a connected person

29. Employees are usually connected with their employer (IA 1986, ss 249 and 435(4)). However the reversible transactions provisions in ss 238 and 239 (but not s 245) modify their application to a person connected with the company in cases where the only connection of a person is as an employee of the insolvent company. Such employees are not, if that is their only connection[65]:

    - subject to the presumption as to the relevant desire under s239(5) for establishing a preference – s 239(6); or
    - subject to the extended two year preference period before the start of the insolvency process applicable to transactions with other connected persons in relation to the

63 *Re Kilnoore Ltd: Unidare plc v Cohen* [2005] EWHC 1410 (Ch), [2006] Ch 489 (Lewison J) at [32].

64 *Darty Holdings SAS v Carton-Kelly* [2021] EWHC 1018 (Ch) (Miles J) at [109].

65 The employee modifications did not apply in the pre IA 1986 decision in *Re Clasper Group Services Ltd* [1989] BCLC 143 (Warner J) (a case under the Companies Act provisions applicable before IA 1986 came into force). In that case a payment to an employee was reversed as being a preference. The employee was the son of the sole shareholder and director.

giving of an undue preference – s 240(1)(a). Instead the standard six month period applies – s 240(1)(b).

30. Perhaps rather oddly, the presumption in s 240(2) that, in the case of a connected person, the company is unable to pay its debts, applies to an employee. There is no modification for employees in s 240(2).

31. There is no modification in relation to transactions at an undervalue in s 238 extending the standard two year time period for transactions with connected persons. And there is no shortening of that period for employees either.

32. An employee who was 'connected' for some other reason (eg was a director of the insolvent company) is not able to rely on these modifications. There is an example of this in *Katz v McNally*[66] where directors were forced to repay the amount that the company had paid to them in respect of various loan accounts because they could not rebut the presumption that the payments were an undue preference. Similarly *Re Brian D Pierson (Contractors) Ltd*.[67]

33. Conversely in *McTear v Eade*[68] the relevant LLP members were able to rebut the presumption.

34. Similar rules in relation to employees to those in ss 239(6) and 240(1)(a) apply in an individual bankruptcy: IA 1986 ss 340(5) and 341(2).

[66] *Re Exchange Travel (Holdings) Ltd (No.4), Katz v McNally* [1999] BCC 291, CA on appeal from *Re Exchange Travel (Holdings) Ltd (No 3)* [1996] 2 BCLC 579 (Rattee J).

[67] [1999] BCC 26 (Hazel Williamson QC, sitting as a deputy High Court judge).

[68] [2019] EWHC 1673 (Ch), [2019] BCC 1155 (ICC Judge Jones) at [202].

Sham trusts

John McGhee QC and Rachael Earle

What is a sham trust?

"…it means acts done or documents executed by the parties to the "sham" which are intended by them to give to third parties or to the court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intend to create….for acts or documents to be a "sham," with whatever legal consequences follow from this, all the parties thereto must have a common intention that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating."

Snook v London and West Riding Investments Limited [1967] 2 QB 786 per Lord Diplock

What is *not* a sham trust?

- Illusory trusts look at the objective question of whether, on a proper construction of the trust deed, there was an intention on the part of settlor to dispose of the beneficial interest; sham trusts look at the subjective question of whether the settlor and the trustee intended to dispose of the beneficial interest.

- Rectification relates to genuine mistakes; sham trusts involve deceit.

- Forged documents are not genuine documents; sham trusts are genuine documents (it is the intention which is not genuine)

- IA 1986 claims, such as transactions defrauding creditors or TUVs, relate to transactions; with a sham trust there is no transaction because the beneficial interest has not in reality been transferred away (but often pleaded as alternatives).

Purpose of the doctrine?

Allows Courts to step outside the normal construction process and to *not* give effect to the ordinary meaning of a written document.

What must the C prove?

(1) An intention that there should be no trust or otherwise that the trust instrument should not take effect according to its terms; and

(2) An intention to give a false impression to third parties or the Court.

(*Hitch v Stone* [2001] EWCA Civ 63 at [64 -69] and *Pankhania v Chandegra* [2012] EWCA Civ 1438 at [20]).

Whose intention is relevant?

Where a trust appears to have been unilaterally declared by the settlor over property which the settlor holds as trustee (a self-declaration of trust), it is the intention of the settlor alone that is decisive (see *Painter v Hutchinson* [2007] EWHC 758 (Ch) at [115]).

Although a common intention between the settlor and any trustee is required, it is sufficient that the trustee went along with the settlor's wishes and / or did not care what he or she was signing (*Midland Bank v Wyatt* [1997] 1 BCLC 242) and / or that he or she was recklessly indifferent (*Minwalla v Minwalla* [2005] 1 FLR 771 at [54-55]).

To establish the requisite intention, evidence is admissible of conduct after execution of the trust instrument (see *AG Securities v Vaugham* [1990] 1 AC 417 (HL) [475-476] and *Hitch v Stone* at [65]).

Subsequent intention

Can a *bona fide* trust become a sham?

"The settlor may have an unspoken intention that the assets are in fact to be treated as his own and that the trustee will accede to his every request on demand. But unless that intention is from the outset shared by the trustee (or later becomes so shared), I fail to see how the settlement can be regarded as a sham."

Rimer J in *Shalson v Russo [2003] EWHC 1637 (Ch), at page 342*

"A document which originally records the true common intention of the parties may become a sham if the parties later agree to change their arrangement but leave the original document standing and continue to represent it as an accurate reflection of their arrangement."

Ben Nevis Forestry Ventures v CIR [2008] NZSC 15, at [33].

But query whether the situation described in *Ben Nevis Forestry Ventures above simply means that the trustees were acting in breach of trust and not that the transaction had become a sham?*

Can a new trustee save the day?

Provided that the new trustee complies with the terms of the trust deed and exercises his or her powers in accordance with the terms of the trust deed, the trust is not a sham trust (even if it was before).

Effect?

A sham trust is void.

"The Revenue must show that clause 2 is ineffective, not simply that it was voidable. No authority has been cited to us which would suggest that a sham transaction could on its own be other than a void transaction. There being no statutory provision in point here, that consequence would in my judgment follow."

(*Hitch v Stone,* at [87].)

Standard of proof

"… lawyers find it difficult to grapple with the concept of sham, presumably on the basis that, subject to questions of mistake (which can give rise to rectification or rescission), there is a very strong presumption indeed that parties intend to be bound by the provisions of agreements into which they enter, and, even more, intend the agreements they enter into to take effect… Because a finding of sham carries with it a finding of dishonesty, because innocent third parties may often rely upon the genuineness of a provision or an agreement, and because the court places great weight on the existence and provisions of a formally signed document, there is a strong and natural presumption against holding a provision or a document a sham."

National Westminster Bank PLC v Jones [2001] 1 BCLC 98 per Neuberger

Evidence required

- Is there contemporaneous documentation surrounding the alleged trust deed? E.g. is it referred to anywhere else?

- How has the settlor treated the property or assets allegedly subject to the trust? E.g. entire beneficial interest in property allegedly transferred to children but parent declares rental income on the property in his / her personal tax returns.

- Has settlor acted as mere nominee? E.g. made distributions instantly on settlor's request / made unsuitable investments which indirectly benefit settlor.

Practical tips to avoid sham arguments

- Ensure settlors and trustees understand nature of the relationship and that trustees must act independently;

- Do not reduce the irreducible core! Do not include provisions in the trust deed that are inconsistent with the irreducible core of obligations owed by the trustees to the beneficiaries (see *Armitage v Nurse* [1998] Ch 241).

Developments in personal insolvency

Marcia Shekerdemian QC, Sri Carmichael and Jessica Brooke

Below are summaries of some of the most interesting and important personal insolvency cases from the past 18 months to add to your knowledge bank.

A. *Re Fowlds (also known as Bucknall v Wilson)* [2021] EWHC 2149 (Ch) – 30 July 2021

1. Headline: Where all the required elements of a preference under s.340 of the Insolvency Act 1986 ("IA 1986") are established, the court will only refuse to exercise its discretion to grant relief under that provision in very unusual or exceptional circumstances. ICC Judge Jones was wrong that a change of position was a strong factor relevant to the court's exercise of its discretion, with such conduct only exceptionally being relevant.

2. Facts: A bankrupt's payment to his stepdaughter ahead of his bankruptcy as part-payment for professional accountancy services provided was held to be a preference. However, the first instance judge (ICC Judge Jones) refused relief partly on the basis that it would be inequitable to require restitution because the stepdaughter had acted in good faith and no longer had the preference or its proceeds, having changed her position.

3. Judgment: The Trustees' appeal against the refusal of relief was dismissed on the basis that, irrespective of the misplaced weight the ICC Judge put on the stepdaughter's change of position, it would not be just or fair to order her to make repayment when this would force her to sell her home.

4. The appeal judge criticised the first instance judge's analysis in respect of change of position. The correct overarching test as to whether relief should be granted under s.340 IA 1986 is whether, exceptionally, it is "fair and just" that no order for relief be made. In this instance, the position of the stepdaughter other than in respect of her change of position was sufficiently exceptional to justify refusal. Rarely will it be appropriate for a court to give any weight to a change of position as a factor when making its discretionary determination given the policy

behind the statute of providing restorative relief to a class of creditors (as balanced against the impact on one innocent preferee/transferee). Change of position is also not a defence to preference or transaction-at-an-undervalue claims.

5. Relevant factors justifying a refusal of relief were the commercial justification for the payment to the stepdaughter, the lack of preferential treatment of the stepdaughter over other creditors who were not "associates" under s.435(2) IA 1986, in that she was paid less than other creditors, and the fact that it was effectively a single-creditor bankruptcy, such that there was less reason than usual to favour the interests of the class of creditors over those of the preferee.

B: ***Kireeva v Bedzhamov*** **[2022] EWCA Civ 35 - 21 January 2022**

6. Headline: The Court of Appeal decided that the 'immovables rule' trumps 'modified universalism'.

7. Facts: A Russian bank obtained a judgment in Russia against a Russian debtor, based upon a personal guarantee. The bank successfully petitioned for the debtor's bankruptcy, although, by this time, he had fled to England. The Russian Trustee in Bankruptcy asked the English court to (1) recognise the bankruptcy, and (2) assist her in realising two valuable properties in Belgrave Square for the benefit of creditors.

8. Judgment: The interesting part of the Court of Appeal judgment concerns the Trustee's application regarding the Belgrave Square properties, and addresses the conflict between the 'immovables rule' and 'modified universalism'. The immovables rule means that, as a matter of English law, rights relating to English land are governed exclusively by English law, and a foreign court has no jurisdiction to make orders in respect of the land. Modified universalism is the principle that the English court should, so far as consistent with local law and policy, co-operate with foreign courts to ensure that all a debtor's assets are distributed to creditors.

9. On the facts of the case, the Trustee was compelled to rely upon the common law to seek assistance from the English court. Whilst she accepted that she did not have title to the Belgrave Square properties, she submitted that, as she could exercise dominion over the bankrupt as his trustee, his real property was held for her. Alternatively, she asked the court to exercise its *in*

personam jurisdiction over the bankrupt, and compel him to transfer the properties, or prohibit him from dealing with the properties.

10. The majority in the Court of Appeal found that, as a matter of English law, not only did the English properties not vest in the trustee, she had no interest in or right to such property, irrespective of the position under Russian law. It was not proper to provide assistance to the trustee in order to circumvent the immovables rule.

C: ***Prince Hussam Bin Saud Bin Abdulaziz Al Saud v Mobile Telecommunications Company KSCP* [2022] EWHC 744 (Ch) – 31 March 2022**

11. Headline: Roth J considered whether a debtor ***'has had a place of residence, in England and Wales' 'at any time in the period of three years ending with the day on which the petition is presented'*** in the context of the court's jurisdiction to make a bankruptcy order under s.265 IA 1986.

12. Facts: A bankruptcy petition was presented against a member of the Saudi royal family who was resident in Saudi Arabia. The creditor applied for permission to serve the petition out of the jurisdiction, and the court considered whether the creditor had a good arguable case that the court had jurisdiction to make a bankruptcy order. The creditor relied upon s.265(2)(b)(i) IA 1986, that the debtor has had a place of residence in England and Wales in the period of three years ending with the day on which the petition is presented.

13. Judgment: The relevant period for which the court had to consider was February 2017 to February 2020. The debtor had not returned to England since March 2018. He had permission from his mother to stay in a London property which was owned by her but had not stayed there any time during the relevant period, although he was registered for council tax on the property. The debtor also had permission to stay in other properties owned by family members when he came to London and had stayed at one of these properties in February/March 2018. Despite these limited links to England and Wales, the Judge had *'no doubt'* that the creditor had a good arguable case that the debtor had a place of residence within the jurisdiction.

D: *Allen v Mittal* [2022] EWHC 762 (Ch) – 1 April 2022

14. Headline: A bankrupt successfully raised a limitation defence where the Trustee in Bankruptcy's application to suspend discharge had not been properly served before a hearing at which an interim order was made.

15. Facts: A Trustee in Bankruptcy issued an application to suspend discharge on 10 June 2021, with discharge occurring on 18 June 2021. The relevant provisions regarding service were those in CPR Part 6, and there was insufficient time to effect service between the issuing of the application, and the date of discharge. An interim suspension order was made on 17 June 2021.

16. Judgment: Deputy ICCJ Agnello QC found that, whilst the court had jurisdiction to make an interim suspension order, and to hear the application on a without notice basis or on the basis that time is abridged, the court would expect evidence which supported an application made effectively in breach of the relevant service rules. In this case, no application was made seeking that an interim suspension application be made without notice, and the application did not seek an abridgement of time. The position was comparable to that regarding the service of claim forms in Part 7 proceedings and the expiry of limitation periods. In the circumstances, the court did not have jurisdiction to make an interim suspension order, and the bankrupt had a limitation defence. The Trustee's application seeking post-validation of service failed, as there was nothing preventing the trustee from serving in accordance with the rules.

E: Boris Becker jailed for hiding assets from his Trustees – 29 April 2022

17. Headline: Former tennis champion Boris Becker was sentenced to 2.5 years in prison in April 2022 following his unanimous conviction by a jury of four criminal offences under IA 1986 relating to failing to disclose or concealing millions of pounds worth of bankruptcy assets and loans or attempting to remove assets from the control of his Trustees in Bankruptcy. It is a cautionary tale for bankrupts and highlights their obligation to be transparent and honest when dealing with their Trustees.

18. Facts: The Secretary of State for Business, Energy & Industrial Strategy prosecuted Mr Becker for 24 charges under IA 1986 in respect of his hiding assets after he was declared bankrupt in June 2017 following his failure to repay a $5 million loan to private bank Arbuthnot Latham.

19. Judgment: Mr Becker was found guilty of four of the charges against him. His convictions concerned his transfer of more than £300,000 to his two ex-wives and concealment of both a property he owned in his hometown in Germany and shares he owned in a data company. He was also found guilty of hiding a loan for more than £700,000 that he owed to a bank in Lichtenstein. This conduct constituted offences under ss.353(1)(a), 354(1)(b) and 354(2) IA1986.

20. Bankrupts are usually discharged after one year and released from bankruptcy restrictions, but the Official Receiver secured a 12-year extension to Mr Becker's bankruptcy following its investigation into his undisclosed transactions. As a bankrupt, Mr Becker had an obligation, pursuant to s.333 IA 1986, to cooperate with and disclose his full financial position to his Trustees in order to assist them in their duty to get in and realise the assets in his bankruptcy estate, pursuant to s.305(2) IA 1986. However, the jury found that the sportsman's conduct had been dishonest, such that he had the necessary intention to defraud required for conviction. They were unpersuaded by his claim that he relied on experts who advised him he could legitimately hide his assets.

21. At Mr Becker's sentencing, the Court was told that his actions had deprived his bankruptcy estate, and by extension his creditors, of more than £1.6 million that had not been recovered. The maximum sentence for the offences of which Mr Becker was convicted is 7 years, but there are no specific sentencing guidelines applicable, perhaps because of the rarity of such convictions. The sentence Mr Becker received of 2.5 years was at the lower end of the range of 2.5 – 6.5 years sought by the prosecution.

F: ***Karapetian v Duffy*** **[2022] EWHC 1053 (Ch) – 6 May 2022**

22. Headline: This was an application under rule 15.35 of the Insolvency (England and Wales) Rules 2016 in which the High Court was considering the validity of the decision of a convener of a virtual meeting of creditors, held to consider a debtor's proposal for an individual voluntary arrangement (IVA). The convener had decided to reject part of the creditor's claim for voting purposes. If the creditor's claim had been admitted in full, the proposal would have been approved. The creditor's case was, essentially, that he had been informed of an incorrect time for the virtual meeting by the convener and that this was a material irregularity. Hence, it was argued that the convener's decision to reject their claim should be reversed or varied.

23. Judgment: The Application was dismissed. The court may only order a new decision procedure if it considers that the circumstances which led to the appeal give rise to unfair prejudice or material irregularity.

24. Although the correct meeting time was stated in the proposal documents, an email translation sent subsequently stated the wrong time zone. On realising the error, the creditor emailed details of their claim and proxy form to the convener. However, supporting documents remained queued and unsent in their email outbox.

25. ICCJ Mullen did not consider that the email with an incorrect meeting time was material to why the creditor's debt was not admitted. On re-examining the creditor's claim, he noted that the creditor had only needed to establish a clear prima facie case as to the value of their debt. However, once the debtor raised a respectable question about this, the court had to assess the value of the debt on the balance of probabilities. By this standard, the debt was not proven. The documents provided to the court only evidenced a potential liability to a different third party. There was also no evidence for an alternative claim in damages as asserted by the creditor. Even if the convener had received the relevant documents in time, they could not have safely agreed to value the damages claim at more than £1 for voting purposes (*rule 15.31(3), IR 2016*). Accordingly, even if the supporting documents had been received by the convener, the creditor's vote would not have affected the meeting outcome.

26. The judge emphasised that a convener has to assess the evidence supplied directly to them by the creditor. Here, the creditor had not made enough effort to evidence their debt to the convener but had relied on the debtor to provide information about the debt. Further, the creditor's technology issues were not an irregularity given the adequate time the creditor had otherwise had to provide the relevant information.

27. The takeaways are clear: creditors wanting to vote on an IVA proposal should submit their proof of debt and supporting evidence directly and expeditiously, even if they receive notice of the decision procedure late. Moreover, the Court can and will (re) assess the Creditor's claim itself.

Limitation

Jack Watson

A common problem for insolvency practitioners is limitation. Those investigating the affairs of the company will often find themselves up against tight deadlines not only for investigating claims but for bringing them so as to avoid the expiry of a limitation period.

The limitation period for claims in both contract and tort is six years. The time period for a claim in contract begins to run from the breach. The time period for a claim in tort begins to run from the date that the cause of action arose, usually upon a quantifiable or ascertainable loss being suffered. While this does not include contingent losses/liabilities (Law Society v Sephton and Co and others [2006] UKHL 22; Watkins and another v Jones Maidment Wilson (a firm) [2008] EWCA Civ 134), the courts will rarely find that a loss is truly contingent because it will often be possible to characterise a particular transaction as having given rise to a bundle of rights which, from the outset, as less advantageous to the Claimant than they ought to have received (see Shore v Sedgwick Financial Services Ltd [2008] EWCA Civ 863).

S.32 Limitation Act

One potential means of avoiding a tight limitation deadline is through the use of s.32 Limitation Act. S.32 extends the limitation period in cases of fraud, deliberate concealment by the Defendant or mistake. In such cases the limitation period will not begin to run until the claimant has discovered the fraud, concealment or mistake or could with reasonable diligence have discovered it.

Fraud

The fraud exception in s.32 is tightly drawn. Fraud must be an essential element of the claim (*GL Baker Ltd v Medway Building and Supplies Ltd [1958] 1 WLR 1216, Arcadia Group Brands Ltd and others v Visa Inc and others [2014] EWHC 3561 (Comm)*) and s.32 will not extend to claims based upon unconscionable conduct or for breaches of duty which were carried out dishonestly, not involving fraud: *Sixteenth Ocean GmbH & Co Kg v Société Générale [2018] EWHC 1731 (Comm).*

Concealment

Perhaps of greater assistance to insolvency practitioners is the deliberate concealment exception contained within s32(1)(b) and s.32(2). The burden is on the Claimant to establish deliberate concealment.

The concealment must be of a relevant fact i.e. one which is necessary to the cause of action rather than one which simply improves the prospects of success: *Mitchell v Royal Bank of Scotland plc and others [2017] EWHC 1025 (Ch). As such, concealment of evidence is insufficient if the Claimant already knows of sufficient facts to be able to plead the claim: Kimathi and others v Foreign and Commonwealth Office [2018] EWHC 1169 (QB).*

In Canada Square Operations Ltd v Potter [2021] EWCA Civ 339 the Court of Appeal considered the meaning of deliberate concealment in the context of missold PPI. Relying upon the previous Court of Appeal decision in The Kriti Palm [2006] EWCA Civ 1601, Rose LJ held that "*concealment*" did not require active concealment nor did it require a contractual or other legal duty to disclose. Instead, concealment simply required a duty to disclose arising out of "*utility and morality*". In particular, it was not necessary that the concealment amount to some conduct outside of the cause of action itself.

When addressing the mental element of deliberate concealment, Rose LJ held that recklessness was sufficient to render any concealment deliberate. In the context of s.32(1)(b), this had both a subjective and objective element. Accordingly, the Defendant must realise that there is a risk that they have a duty to tell the Claimant about the relevant fact and in all the circumstances it must be unreasonable for them to fail to do so.

Section 32(2) further provides that, for the purposes of subsection (1), deliberate commission of a breach of duty, in circumstances in which it is unlikely to be discovered for some time, amounts to deliberate concealment of the facts involved in that breach of duty. The Court of Appeal in *Canada Square* helpfully clarified that:

1. Breach of duty may include any kind of legal wrongdoing (citing *Giles v Rhind [2008] EWCA Civ 118)). However, the breach of duty should be the breach of duty subject of the claim (and not a separate duty): Various claimants v News Group Newspapers Ltd [2020] EWHC 1593 (Ch)*

2. *Again, recklessness will suffice to establish deliberate commission of a breach of duty. Thus the Defendant must realise there is a risk that they are committing a breach of duty and in all the circumstances it must be unreasonable for them to take that risk.*

Knowledge

Once concealment/fraud is established, the Claimant must nonetheless establish that they did not have the requisite knowledge. "*The question is not whether the plaintiffs should have discovered the fraud sooner; but whether they could with reasonable diligence have done so. The burden of proof is upon them. They must establish that they could not have discovered the fraud without exceptional measures which they could not reasonably have been expected to take…the test was how a person carrying on a business of the relevant kind would act if he had adequate but not unlimited staff and resources and was motivated by reasonable but not excessive sense of urgency."* (*Paragon Finance v DB Thakerar & Co [1999] 1 All ER 400*)

Challenging office-holder decisions after *Baglan* [2022] EWHC 647 (Ch)

Thomas Robinson, Daniel Scott and Daniel Petrides

Introduction

1. The purpose of this talk is to consider certain key issues that arise in connection with applications brought to challenge the decisions of office-holders in the course of their conduct of an insolvency. There have been recent decisions on this topic under s.168(5) of the Insolvency Act 1986, but the issues go wider than just liquidation and apply to administrators, trustees in bankruptcy and others. We propose to deal with them as follows:

    - First, identifying which applicants a court will accept as having standing to challenge an office-holder's decision;

    - Second, how the Court approaches such a challenge. What test does it apply to decide whether to modify the decision in question?

    - Thirdly, considering the factors that might be relevant in satisfying that test. Two particular ones that we consider below are the fact that the office-holder has taken legal advice, and the fact (if it can be shown) that the office-holder is a public authority for the purposes of the Human Rights Act 1998 (the **"HRA"**). Might that add to the factors that the office-holder should have regard to when taking their decision?

2. All of these issues arose for determination in the recent decision of Norris J in *Re Baglan Operations Ltd* [2022] EWHC 647 (Ch).

3. The case was a challenge brought under s.168(5) against a decision by the Official Receiver to cease electricity supply throughthe land occupied by a now-defunct power station which had been operated by the insolvent company, and arose in extraordinary circumstances. The Official Receiver had been appointed, along with Special Managers, to oversee the company's liquidation, including ensuring the "orderly operation and/or shutdown of [the company's] business".

4. In preparation for disclaiming the land where the power station had been situated, the Offiical Receiver put in place a timetable for the disconnection of a private wire network running

underneath the land from the National Grid in January 2022. However, the private wire network was the sole source of power to the nearby Baglan Energy Park where a number of major factories were located along with the wastewater treatment facilities and flood defences for the Swansea Bay area. The evidence was that the termination of the power in January 2022 would leave the area exposed to severe flood risk at the height of the flood season.

5. Despite this, the Official Receiver adopted the position that, on the true construction of its powers under the Insolvency Act 1986, it was not entitled to take into account risks (however severe) to third party interests; the only relevant factors which it could consider were the extent of its vires and the interests of the company's creditors. Accordingly, it argued that it was not able to take flood risk into account when making its decision as to when the power supply should be terminated.

6. A number of parties, including the Welsh Government, Welsh Water and the local authority successfully challenged the Official Receiver's decision under s.168(5). While it is unlikely that such extreme fact-patterns will arise frequently, the issues of principle raised by the case are capable of arising in a wide range of insolvency situations.

s.168(5)

7. s.168 of the Insolvency Act contains numerous supplementary powers relating to liquidations, including the power to summon general meetings of creditors (s.168(2)) and the power for liquidators to apply to court for directions (s.168(3)).

8. s.168(5) provides as follows:

"*If any person is aggrieved by an act or decision of the liquidator, that person may apply to the court; and the court may confirm, reverse or modify the act or decision complained of, and make such order in the case as it thinks just*".

Standing

9. The first question facing any applicant will be that of standing.

10. In *Mahomed v Morris* [2001] BCC 233 Peter Gibson LJ noted at [24] that while the words "*are very wide at first sight and are not on their face limited to creditors and contributories*", there was (at that time) only one reported decision in which a person not being a creditor or

contributory had been allowed to apply under the section. And in *Re Edennote Ltd* [1996] BCC 718 at 721 Nourse LJ suggested that "*an outsider*" to the liquidation would not normally have standing to apply (although held that it would not be appropriate to provide a complete classification of those who may or may not have standing).

11. The one exception referred to was *Re Hans Place Ltd* [1992] BCC 737 in which a landlord was permitted to challenge a decision by a liquidator to disclaim a lease despite not being a creditor. The decision was explained in *Mahomed* at [26] as follows:

> "*I would accept that someone, like the landlord in* Hans Place Ltd*, who is directly affected by the exercise of a power given specifically to liquidators, and who would not otherwise have any right to challenge the exercise of that power, can utilise s.168(5)".*

12. More recently, in *Brakes v Lowes* [2020] EWCA Civ 1491; [2021] Bus LR 577 Asplin LJ explained the reasoning in Hans Place and *Mahomed* at [82] on the basis that:

> "*The ability to disclaim onerous property under section 178 of the Insolvency Act 1986 is specific to a liquidator and arises in the liquidation. It is not surprising, therefore, that the decision to disclaim should be challenged in the liquidation itself. As Peter Gibson LJ put it in the Mahomed case [2000] 2 BCLC 536, the landlord was directly affected by the exercise of a power granted to the liquidator which he would not have been able to challenge otherwise.*".

13. The narrowness of the test for standing under s.168(5) can be illustrated by the fact that not even all creditors will necessarily constitute 'persons aggrieved' if they the challenge is not in the interests of the class of creditors as a whole:

    a. So, in *Walker Morris v Khalastchi* [2001] 1 BCLC, a law firm which was a creditor of the insolvent company in the sum of £237 which was seeking to prevent the liquidator from handing over documents relating to the company's tax affairs to the Inland Revenue so as to protect its other clients from possible proceedings by the company was held not to have standing because it was seeking to advance the interests of possible debtors rather than creditors.

    b. Similarly, in the very recent case of *Re Edengate Homes (Butley Hall) Ltd* [2022] EWCA Civ 626 the Court of Appeal held that a creditor who sought to challenge the assignment to a litigation funder of possible claims which the insolvent company had

against her and her family was seeking to advance her personal interests rather than that of the creditors generally, and accordingly did not have standing.

14. A different outcome therefore followed occurred on the facts in *Re Edennote,* in which the applicants had been prepared to outbid another party (the former England manager Terry Venables) to acquire the claim against them; selling to the highest bidder was not contrary to the interests of the class of creditors as a whole.

15. We can therefore tentatively suggest that there are three elements to the question of whether a given applicant has standing:

    a. First, they must be directly affected by the proposed exercise of the power. This is a necessary, but not sufficient, ingredient; the courts are astute to protect liquidators from collateral attacks from an infinite array of third parties. The impact on the applicant does not have to be purely financial (*Brake* at [84]).

    b. Secondly, the power being exercised must be one peculiar to the liquidation. Disclaimer would appear to be a paradigmatic example, but there does not appear to be any reason why any other power exercised by a liquidator *qua* liquidator could not, as matter of principle, also be within striking distance.

    c. Finally, the challenge must be consistent with furthering the policy objectives of the insolvency regime as a whole. This may overlap with the more substantive test under the section and invite an iterative consideration of the questions of standing and relief.

16. In *Baglan* itself (which concerned disclaimer), the Official Receiver did not seek to contend that the Applicants lacked standing to bring the application. In his judgment at [40] Norris J recognised that he applicants came "*within the narrow class of persons directly affected by the exercise of a power given to the Official Receiver who would not otherwise have the right to challenge their exercise*".

The Correct Test

17. It is easy to find commentators that describe the test for a challenge under s.168(5) IA86 as akin to perversity. Thus Sealy & Milman in the 2021 edition state as follows when commenting on s.168(5): "*the court will only interfere with a decision of a liquidator if it was taken in bad*

faith or if it was so perverse as to demonstrate that no liquidator properly advised could have taken it."

18. Yet the authorities show a more nuanced position. The classic statement, from which the comment in Sealy is derived, is that made in *In Re Edennote Ltd* [1996] BCC 718 at 722, as follows:

"[…] (fraud and bad faith apart) the court would only interfere with the act of a liquidator if he has done something so utterly unreasonable and absurd that no reasonable man would have done it."

19. That applies to what may be called "commercial" decisions by office-holders, but it is not a complete statement of the position. Indeed the wording of s.168(5) allows the court a wide discretion to modify a decision of an officeholder and "*make such order in the case as it thinks just*".

20. Issues of fairness between affected persons can also prompt the court to modify a decision. In *Hellard v Michael* [2010] BPIR 418 at [8]-[9] Sales J noted (in a case dealing with the near equivalent power in s.303(1) in relation to bankruptcy proceedings): [69]

"*The usual test is that laid down in* In re Edennote Ltd *[1996] 2 BCLC 389, which concerned the actions of the liquidator of a company. It is common ground that the same test applies in relation to the actions of a trustee in bankruptcy in a case of personal insolvency. The test for intervention by the court was put in this way by the Court of Appeal, as summarised in the head note: 'Fraud and bad faith apart, the court will only interfere with the act of a liquidator if he has done something so utterly unreasonable and absurd that no reasonable person would have done it.' The basic approach is that the court should be very slow to second-guess commercial decisions made by a trustee in bankruptcy in the exercise of the statutory discretion conferred on him by section 305(2) of the Insolvency Act.*

In my view, however, the test in In re Edennote Ltd *does not exhaustively state the grounds for intervention by the court. As is clear from the provisions of the Insolvency Act 1986, the court retains a general supervisory jurisdiction in respect of trustees in bankruptcy to ensure*

[69] Which provides that the court may give directions or make such other order as it thinks *"fit"*, rather than "*just*" as in s.168(5).

they behave properly and fairly as between persons affected by their decisions. That wider jurisdiction is in issue in the facts of this case." (emphasis added)

21. The touchstone for identifying when a court should apply the test in In re Edennote Ltd and when it should apply a different test is the nature of the decision under challenge. As noted above, a "commercial" decision will attract a high threshold for challenge. It is well-established that the court will be most reluctant to second guess a commercial decision of an office-holder (e.g. the price at which to sell an asset) (see Lightman & Moss (6th ed.) at [2-061]). But where a decision is not simply a commercial one, different considerations will apply.

22. Thus in *Re Buckingham International plc* [1998] BCC 943 the Court of Appeal considered a challenge under s.168(5) IA86 to a liquidator's decision to apply to a US court under the US Bankruptcy Code to restrain steps by certain creditors of the company in liquidation that sought to gain precedence over other creditors in the liquidation by using "garnishment" proceedings in the USA.

23. At first instance Harman J accepted the liquidators' submission that they were seeking to give effect to an overriding principle of *pari passu* distribution of assets among creditors of the same class. Harman J. rejected the challenge to the liquidators' decision. He described the application of the test as follows:[70]

"*In order to consider what exercise the court should make of its powers to 'order … as it thinks just', if s. 168(5) is the proper origin of the jurisdiction, or if this application is truly pursuant to s. 167(3) so that the court is exercising control over its officers, the liquidators, the same basic issue must in my judgment arise. ... The thrust of the decision must be based upon doing justice in the sense of holding an even balance between the interest of the applicants on the one hand and the interest, not of the liquidators who have no personal interest in the result at all, but of the class whom the liquidators represent, that is all the other unsecured creditors of the company in liquidation on the other hand."*

24. Harman J. also relied on Re Edennote Ltd [1996] BCC 718 at 722 in describing his jurisdiction under s.168(5) IA86.[71] The Court of Appeal considered this reliance to be misplaced, as the nature of the decision complained of was not a "commercial one". However the Court of

[70] [1998] BCC 943 at 951.

[71] At 953.

Appeal went on to conclude that Harman J. had posed the right question in the passage quoted above:

> *"Mr Hollington submitted that Harman J was wrong in applying the test in Leon v York-O-Matic Ltd and Re Edennote Ltd. Both those cases were concerned with decisions taken by liquidators as to the realization of assets of the company (in one case a chain of launderettes, in the other a right of action for damages for breach of contract) for the benefit of the general body of unsecured creditors. They were therefore concerned with practical decisions (albeit important ones) as to valuation and disposal, not decisions involving the exercise of judgment as between different creditors' competing claims. The liquidators' application to the American insolvency court was, counsel submitted, of a different character. It was concerned with competing creditors: in particular, with the efforts of one pair of judgment creditors to put themselves into the position of secured creditors before the position was frozen by the onset of the winding up. Mr Moss submitted that that was not (pace Millett LJ) a question of priorities, and no doubt in a technical sense that submission was correct. But in substance the issue was whether the appellants could get to the head of the queue in priority to the general body of unsecured creditors.*
>
> *In our judgment Mr Hollington's submissions are right on this point.* ***When liquidators are exercising their administrative powers to realise assets, the court will be very slow to substitute its judgment for the liquidators' on what is essentially a businessman's decision*** *(see Re Edennote Ltd at p. 722). All the cases referred to by Nourse LJ on the point (from Re Peters, ex parte Lloyd (1882) 47 LT 64 to Harold M Pitman & Co v Top Business Systems (Nottingham) Ltd (1985) 1 B.C.C. 99 ,345) are concerned with decisions as to the disposal of assets.* ***In this case, by contrast, when the provisional liquidators launched their s. 304 petition, they did so for the same purpose as they might (in times when there was a lower level of comity in cross-border insolvency) have sought an anti-suit (or anti-execution) injunction from the English court****: see Re Vocalion (Foreign) Ltd [1932] 2 Ch 196 and the earlier cases there cited. That is eminently a matter for the Companies Court, or for liquidators acting under the control of the Companies Court. It is not a matter for the liquidators to decide at their own discretion in the way in which they might take decisions as to the disposal of their company's assets. In our judgment Harman J did pose the right question when he asked himself (as he did, in substance, at p. 951F of the judgment)*

how the English court would exercise its discretion if the appellants were seeking to obtain execution by attachment of debts in England."

25. In the recent case of Re Baglan Operations Ltd **[2022] EWHC 647 (Ch),** the decision complained of was not one concerning the terms on which assets should be sold in the liquidation, or an equivalent issue regarding realisations in the liquidation where the court should defer to the commercial decision-making of the liquidator. On the contrary, it was a decision that a liquidator had no vires to continue trading the business of a company in liquidation. The Court (Norris J.) agreed this was a matter of law, under Schedule 4 to IA86, and not one for the *Edennote* test.

Relevant Factors

26. An issue that often arises in the context of challenging an office-holder's decision is whether they have taken legal advice and acted in accordance with it. Where the nature of the decision and challenge is one of pure law rather than commercial judgment, then the court is likely to find the taking of legal advice is relevant to the reasonableness of the office-holder's conduct, but irrelevant to the substantive question before the court (as in Re Baglan Operations Ltd [2022] EWHC 647 (Ch)).

27. However when the nature of the decision is one of commercial decision-making, there is no need for an officeholder to take legal advice unless he or she is uncertain as to the relevant legal rights or obligations. That is the effect of the recent decisions in Re Edengate Homes (Butley Hall) Ltd (in liquidation). Although the liquidator in that case did not canvass the market before assigning a cause of action of the relevant company's, the judge held that there was "nothing to suggest that this arose from a failure to understand his legal rights and obligations".[72] Accordingly it was not relied on as any support for an argument that the assignment was perverse and fell to be set aside by the court. The Court of Appeal did not disagree (at [2022] EWCA Civ 626).

28. By contrast, the judge in Edengate Homes commented on the Edennote case mentioned above. He stated that although in that case the liquidator had also entered an assignment without taking legal advice, the facts were different in that the claim potentially being assigned was subject to a security for costs application. He continued that in Edengate, the Court of Appeal "*considered that it was particularly significant that the liquidator had failed*

[72] [2022] BCC 277 at [56].

to take advice and thus failed to understand the tactical implications of the application for security for costs. Had he done so, it would have become obvious that he should make an approach to the applicants themselves" (ibid at [45]).

The relevance of the HRA

29. As Chancery practitioners, it can often be easy to overlook the importance of the HRA and wider human rights considerations in dealing with what are generally private law problems. However, careful consideration should be given to the potential relevance of the HRA when challenging the decision of office-holders.

30. S.6 of the HRA makes it unlawful for a *"public authority"* to act in a way that is incompatible with a Convention Right unless precluded from acting differently by primary legislation. *"Public authority"* includes any person certain of whose functions are functions of a public nature: those acts will be acts of public authority if the nature of the acts is not private. S.6 applies to both 'core' and 'hybrid' public authorities. 'Core' public authorities are generally bodies such as departments of government: see *Aston Cantlow and Wilmote with Billesley Parochial Church Council v Wallbank* [2003] UKHL 37 at [7].

31. One indicator of whether a body is a 'core' authority is that it cannot itself enjoy Convention rights (*Aston Cantlow* at [8]). Furthermore, as Lord Nicholls explained in *Aston Cantlow* at [12], when considering whether a body is a 'core' authority,

> "*Factors to be taken into account include the extent to which in carrying out the relevant function the body is publicly funded, or is exercising statutory powers, or is taking the place of central government or local authorities, or is providing a public service*."

32. The consequence of the categorisation of a body as a 'core' public authority is that it will not be necessary for the Court to consider the nature of the act complained of within the proceedings: see *YL v Birmingham City Council* [2007] UKHL at [141]. Where however, the authority is 'hybrid' in nature, the Court will need to consider whether the act complained of is of a private act, or whether it is public in nature; it is only where the act is public in nature that a hybrid authority comes under the s.6 duty to act compatibly with Convention rights.

33. A *"victim"* of an act of a public authority committed after 2 October 2000 made unlawful by s.6 may bring proceedings against the public authority under s.7 claiming any relief that is just and appropriate. This may therefore provide a direct route for victims to challenge the decision of an office-holder, given that under s.8 of the HRA the Court can award whatever relief or remedy is just and appropriate. Generally, a *"victim"* is not someone who is merely interested in compliance with a public authority's s.6 duty; in the ordinary case he must be directly affected by or threatened with non-compliance, although in some cases substantial indirect effect may be sufficient: see *Marckx v Belgium* (1979-80) 2 EHRR 330 (ECtHR), [27].

34. Interestingly, the editors of *Lightman and Moss on the Law of Administrators and Receivers of Companies* state at §13-071 that an officer of the court (such as a provisional liquidator, a liquidator in a winding-up by the Court or an administrator) is *"clearly a 'public authority' for this purpose."* Even if it could be shown, for example, that a private liquidator is a 'public authority' that would not answer the question of whether such a liquidator is a 'core' or 'hybrid' authority. Given that many of a private liquidator's functions concern the private law rights of the stakeholders of an insolvent company, it seems more likely than not that such a liquidator would be a 'hybrid' authority and that therefore the nature of each act under scrutiny would need to be considered before the duty under s.6 of the HRA were to bite.

35. Even if a party can show that it is a 'victim' and that the office-holder in question is a core or hybrid public authority, it may well then need to show that the office-holder in question would breach (or already has breached) its s.6 duty. It will be appreciated, however, that many of acts of an office-holder in an insolvency will not even touch the sides of human rights considerations. It may well take a case of extreme facts, therefore, for human rights considerations to come to the fore.

36. It may, however, not be necessary to show that the acts of an office-holder would breach the s.6 duty in order to successfully challenge them under s.168 of the IA86. Where the decision taken concerns a matter of law, the Court does not apply the usual perversity test but may substitute its own decision based on the correct reading of the law. Indeed, under the HRA the Court itself is a public authority subject to the s.6 duty. Accordingly, where it can be shown, for example, that an office-holder has not considered whether it is subject to the s.6 duty and/or has wrongly considered that it is *not* subject to that duty, this may produce fertile ground under which to challenge the decision of an office-holder under s.168.

37. The battle lines in this area have not yet been fully drawn out. In *Baglan*, a number of wide-ranging human rights arguments were run by the applicants, all of which were rejected. However, permission to appeal has been granted and it is hoped that the Court of Appeal will lay out a clear framework for the interaction between the HRA (and other human rights considerations) and the functions of an office-holder under IA86. Some of the points of interest which arise from the first instance judgment of *Baglan* are as follows:

    a. It was conceded by the respondents the Official Receiver was at least a 'hybrid authority'. However, the Judge found that the termination or non-renewal of the applicants' electricity and supply agreements was a private act. Of course, it will be appreciated that the question of whether a private liquidator is a public authority (whether core or hybrid) may well have a different answer.

    b. The Judge found that IA86 already accords sufficient protection to Convention rights, such that it is perhaps unlikely that invocation of Convention rights will assist applicants in challenging the decisions of office-holders.

    c. It was also held that a party who is not a 'victim' cannot invoke the HRA in aid of any challenge. This is likely to preclude many applicants from being able to invoke the fact that Convention rights may be breached by the office-holder: e.g. if an office-holder's decision would breach the Convention rights of a company's employees, it seems unlikely that the company itself would be able to pray in aid of those rights.

Environmental Factors

38. While fact-patterns as stark as that which arose in *Baglan* are likely to be vanishingly rare, it is to be expected that in an increasingly environmentally-conscious age, cases generating interactions between environmental concerns and the insolvency regime will only become more common.

39. Cases in which the courts have had to grapple with environmental issues in an insolvency context are scarce. There are, however, a small number of *dicta*

40. In *Re Mineral Resources Ltd* [1999] BCC 422, Neuberger J had to consider an apparent conflict between the regimes of the Insolvency Act 1986 and the Environmental Protection Act 1990. He held

"*there is considerable public interest in the maintenance of a healthy environment…It is the view which prevails both in the popular perception and in the legislative system in this country and, indeed, in most of the developed world….While I accept that the provisions of the 1986 Act relating to winding up and disclaimer are not merely for the benefit of individual shareholders, creditors, debtors and liquidators of companies, but also for the good administration of business and commerce, it appears to me that those interests are of a less wide-ranging and important nature*."

41. In the later case of *Rhondda Waste Disposal Ltd* [2001] Ch 57, the Court of Appeal held that the first instance judge had erred in having "regarded the interests of the creditors of the company as trumping all other considerations" ([42]) and noted that ""*even the most responsible administrator may find himself involved in a situation where the implications of carrying on a company's business are not limited to purely financial matters, but may affect the health and welfare of the community*" ([52]).

42. The remarks of Neuberger J in *Re Mineral Resources* and the approach of the Court of Appeal in *Rhondda Waste* have been cited with approval by the Scottish courts in a number of recent cases: see *Re Doonin Plant Limited* [2018] CSOH 89 and *Re Dawson International* [2018] CSOH 52. They were also cited with approval in *Baglan* at [57] – [58] as providing "*some support for affording significance to environmental concerns in the exercise of insolvency powers*".

43. This is a narrow, but potentially far-reaching line of authority. We doubt that *Baglan* will be the final word on it.

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Jonathan Davey QC	QC 2016	Call 2003
Jonathan Hilliard QC	QC 2016	Call 2003
Max Mallin QC	QC 2017	Call 1993
Julian Greenhill QC	QC 2018	Call 1997
Tiffany Scott QC	QC 2018	Call 1998
Nikki Singla QC	QC 2018	Call 2000
James Bailey QC	QC 2019	Call 1999
Zoë Barton QC	QC 2020	Call 2003
Andrew Mold QC	QC 2020	Call 2003

Full-time Arbitrators:

Jules Sher QC	QC 1981	Call 1968
Sir Paul Morgan	QC 1992	Call 1975

John Child		Call 1966
Thomas Seymour		Call 1975
David Pollard	Solicitor 1980	Call 2017
Gabriel Fadipe		Call 1991
Graeme Halkerston		Call 1994
Emily Campbell		Call 1995
Andrew Child		Call 1997
Edward Sawyer		Call 2001
Stephen Brown	Solicitor 1991	Call 2013
Thomas Robinson		Call 2003
Daniel Lewis		Call 2003
Emily McKechnie		Call 2005
Charlotte Black		Call 2006
Sebastian Allen		Call 2006
James Walmsley		Call 2007
Jennifer Seaman		Call 2007
Benjamin Faulkner		Call 2008
Anna Littler		Call 2008
James McCreath		Call 2009
Emer Murphy		Call 2009
Tom Roscoe		Call 2010
Jonathan Chew		Call 2010
Harriet Holmes		Call 2011
Alice Hawker		Call 2011
Bobby Friedman		Call 2011
Simon Atkinson		Call 2011
Sri Carmichael		Call 2012
Jack Watson		Call 2012
Jessica Brooke		Call 2012
Michael Ashdown		Call 2013
James Goodwin		Call 2013
Rachael Earle		Call 2013
Elizabeth Houghton		Call 2014
Tim Matthewson		Call 2014
Jamie Holmes		Call 2014
Joseph Steadman		Call 2015
Tara Taylor		Call 2016
Daniel Scott		Call 2016
Cara Goldthorpe (unregistered barrister)		Call 2017
Jia Wei Lee		Call 2017
Francesca Mitchell		Call 2017
Daniel Petrides		Call 2018
Lemuel Lucan-Wilson		Call 2018
Caspar Bartscherer		Call 2019
Ram Lakshman		Call 2020
Benjamin Slingo		Call 2020

Caroline Furze (unregistered barrister) Door Tenant	Call 1992

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