AMB LAW

INSOLVENCY UPDATE

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Welcome to the 22nd Edition of **AMB Law's *Insolvency Update***. This is a watershed moment in the history of AMB Law as we will complete five years in business on 30 April 2018. That's five years without going bust, getting sued or struck off or otherwise disgracing ourselves. With effect from 1 May 2018, we will operate as a limited company – **AMB Law Limited**. We will write separately to all our clients and contacts but essentially there should be a seamless transition from the old firm to the new – all contacts, terms and personnel will remain the same as before.

GDRP

Readers may not have noticed but there is some more red tape coming into force on *25 May 2018*. So … if you would like to continue to receive bumph from this firm, please email *office@amblaw.co.uk* with **GDPR YES** in the subject line.

MISCELLANEOUS

Performance Bond Triggered by Insolvency

Re County Contractors (UK) Ltd

The defendant sought to avoid liability under a JCT performance bond given in respect of the above company. Its pretext was that the beneficiary of the bond was obliged to prove both breach of contract by the company and also causation in relation to its loss.

Coulson J in the TCC found that County's insolvency triggered the balancing account provisions in clause 8.7 which, in turn, created a debt from County to the beneficiary. Non-payment of that debt could itself constitute a sufficient breach to trigger the performance bond.

Definition of 'Contributories'

Re Burnden Holdings (UK) Ltd

The case involved an application by a contributory to inspect the proofs of debt submitted in the liquidation. The shares were fully paid up and the liquidator questioned whether the applicants were in fact 'contributories' which is defined as a member required to contribute to the company's assets in the event of its liquidation.

A clever argument but the court held that all members were liable as contributories even if the value of their contribution was nil.

The applicant still failed to inspect the proofs as the court agreed that the claimant had failed to demonstrate a legitimate interest in examining the proofs of debt.

Not been a good period of time for these directors – see the back page below.

Formation of Contract by Email Exchange

Re MEEM SL Ltd

A potential buyer's solicitor entered into an email correspondence with an administrator in relation to the purchase of certain *choses in action* from the company. The main terms of a deal were agreed and the buyer contended that a binding contract had been concluded. The administrator denied this on the basis that it was clear that the emails were mere negotiations.

David Halpern QC found that there had been no offer capable of acceptance and, accordingly, no contract was formed. This appears largely to have been based upon the administrator's reference to getting his solicitor to draft the necessary deed.

The judge found that the buyer knew that the administrator intended to instruct his solicitor and, accordingly, the email exchange between them was impliedly subject to contract.

In our view this is a fairly generous reading of the correspondence and the administrator should certainly consider himself lucky. The whole farrago could easily have been avoided had the correspondence been marked '*Subject to Contract*' – practitioners should learn what that phrase means and use it (and also learn the difference to *Without Prejudice!*). (*click here to see* our note on *Avonwick Holdings v Webinvest*).

Acceleration Clause Not Penal

ZCCM Investment Holdings plc v Konkola Copper Mines plc

Not an insolvency case but a situation relevant to many insolvency matters. The High Court rejected an argument that an acceleration clause in a settlement agreement was unenforceable as a contractual penalty.

Actually, we were not aware that anyone thought that they would be but it's nice to have it expressed.

No Special Treatment of Litigant in Person

EDF Energy Customers Ltd v Re-Energized Ltd

Not an insolvency case but one of interest to IPs. The court dismissed an appeal against a winding up order. The company had been represented by its director who had tried to run the same arguments that had already been dismissed on an injunction application. The company argued that it was unfairly prejudiced because it was unable to run all the

possible legal arguments due to its lack of representation.

The court dismissed the application. The fact that a party chose to represent itself was not a reason to afford it special treatment or to disapply procedural rules.

cf Reynard v Fox in Bankruptcy section below.

ADMINISTRATION

Court Cures Defective Admin Appointment

Re Astrosoccer 4 U Ltd

The directors of the company had purported to appoint administrators at a time when, unbeknownst to them, a winding up petition had already been presented.

In earlier proceedings, The Technology and Construction Court had considered that the directors were simply seeking to avoid payment of a debt by filing a Notice of Intention.

The directors issue an admin application and asked the court to backdate the appointment to the date of their Notice of Intention.

The High Court found that all the criteria for an admin appointment were present and granted the request.

Although in *Re Business Dream Ltd* the Court had held that a Notice of Intention filed whilst a petition was pending could still give rise to a moratorium, it is clear that an appointment of administrators could not follow from such a notice.

Administrators' Decision Irrational

Promontoria v Craig

Administrators had used their powers to require incumbent fixed charge receivers to vacate office the day after their appointment as administrators. On the facts, the court found that decision to have been irrational.

The court's remedy was not, however, to exercise its inherent jurisdiction over the administrators to interfere with their decision. Instead, the court re-appointed the receivers and ordered a lifting of the para 43 moratorium so as to enable the charge holder to exercise its proprietary rights through its receivers.

Whilst this decision turned on its own facts, the court's remedy is interesting. It is also interesting that the administrators were ordered to pay the costs personally (ie *not* as an expense of the admin).

Administrators Removed Over Pre-Pack Conflict Of Interest

VE Vegas Investors IV LLC

This case has been reported to death amidst a high level of *schadenfreude* so we shall not go into detail. But it should be a salutary lesson to IPs that they cannot take a Nelsonian view of the facts and the need at all times to be mindful of the possibilities of conflicts. This is a difficult area as the Court has oft recognised that an officeholder's position inherently involves conflict and that conflict of interest is an IP's daily bread and butter.

Payment of Fees from Post-Admin Funding

Re MK Airlines

At first instance one of the former administrators had been ordered to repay to the company £854,000 in remuneration and £26,000 in lawyers' fees that had been drawn ahead of other admin expenses.

A putative purchaser of the business had provided substantial funding to enable the administrators to keep trading and thus to protect the company's operating licences. The administrators had paid the monies into the company's account and the registrar at first instance held that they were company assets subject to the ordinary rules of distribution.

On appeal, the court held that it was open to a third party to provide funding subject to certain conditions and that could include the payment of the administrator's costs and fees. Such monies were not therefore covered by rule 2.67 [now rule 3.52]. There was no overall loss to the company and the administrator was not liable for misfeasance in relation to the £854,000.

There had been no creditor approval obtained in respect of the solicitors' £25K pre-admin fees and the administrator was ordered to repay these personally.

LIQUIDATION

Defective Deemed Consent

Cash Generator Limited v Fortune

Liquidators had been appointed via the deemed consent procedure but notice had not been sent to all creditors including the company's franchisor (a major creditor entitled to possession of all stocks), the employees or the landlord. The liquidators had promptly sold all the company's assets.

The franchisor challenged the validity of the liquidators' appointment and, alternatively, sought their removal for having sold the assets without investigation.

The court held that the appointment remained valid on the basis that the legislation did not provide for invalidity. The sanction for not properly following the rules was that it was a criminal offence on the part of the directors.

We think that this decision is quite surprising. In the modern era there has been a plethora of cases in which appointments have been deemed invalid for small technical errors. Not to give notice to a substantial number of creditors is more than a slip of the pen.

Preference Claim Struck Out

Re Brady Property Developments

This case has been widely reported for having been struck out. The main ground was purely technical in that the liquidator, having already discontinued a misfeasance action, failed to get leave to bring a different claim against the same respondents as is required by CPD 38.7.

The generally more interesting aspect however, is in relation to the court's dismissing the claim as an abuse of process notwithstanding that the liquidator was fulfilling his statutory functions. Even if the company was successful against the respondent

directors, the only person to benefit from litigation would be the liquidator himself as any monies paid would simply flow back to the respondents. This is a not uncommon state of affairs where recalcitrant directors are also the main creditors of a company. Office holders need carefully to consider whether there would be any *real* benefit of proceedings in such a case.

Low Burden of Proof For Injunction

Re Mulalley & Company Limited

A stat demand was served on the Company based on a debt that had been assigned to one of the Respondents by a subbie.

The Company challenged the stat demand on the grounds (i) that its contract with the subbie prohibited assignment without the Company's consent, (ii) that some of the debts had been paid and (iii) that some had not yet fallen due. The authenticity of assignment was also disputed.

The High Court granted the company an injunction against the presentation of a petition. The burden of proof was low and the court was did not need to determine if the dispute was valid. It was enough that the challenge was in good faith and have sufficient substance to justify its being determined in a civil action.

Fraud Allegation Not Made Out

Re Instant Access Properties Ltd

IAPL had received substantial sums in commissions on property sales and those monies were paid away to two unrelated companies which were owned by the directors of IAPL. IAPL's liquidators brought proceedings against the directors for breach of duty which essentially amounted fraud.

The case was dismissed on the facts as the court found that the directors had not acted dishonestly as they had not used their position to gain a benefit and had not breached their fiduciary duties. The liquidators also claimed that the directors had broken the rule against self-dealing in receiving a substantial cash benefit via the two external companies. The court, however, rejected this too on the basis that the directors had acted honestly so the issue of breach of duties did not arise.

It will be interesting to see how this issue pans out – we had always understood that the dishonesty was not a precursor to bringing a claim for breach of fiduciary duty including conflict of interest or secret profit.

DIRECTORS

Removal of Liquidators

Re Jamaica Tavern Ltd

The case involved a disgruntled 50% shareholder and director seeking to remove the liquidators for various spurious allegations of misconduct. The case is interesting but largely turns on its own facts as the application appears to have been wholly without merit.

One interesting bit of judicial comment was in relation to the alleged invalidity of the pre-liquidation administration appointment which had been made on a creditor's application. That creditor's claim was ultimately rejected but the Court held that the administration nonetheless remained valid as it was the subject of a Court order.

Directors to Repay Remuneration

Re P V Solar Solutions Ltd

Interesting case on the question of directors' duties and paying themselves from an insolvent company. The court made a number of clear and useful assertions:

1) If the company is insolvent, the directors owe a duty to act in the best interests of its creditors. This is not new but it's always nice to have it spelled out again.
2) The directors' payments to themselves put at risk the creditors' prospects of payment and so constituted a breach of duty.
3) Although the directors were 100% shareholders they could not rely on the *Duomatic* principle because they had not, *qua* members, expressly focussed their minds to the issue of the remuneration.
4) The directors' *quantum meruit* argument (ie that they ought to be paid for their labours) was roundly rejected. We have long railed against this line of argument which seems to us to have no legal basis and contrary to the notion that one cannot be remunerated for the office of director *per se*.

But Compare …

Re Pinetum Limited

This was another case where liquidators sought to recover from the directors substantial sums of money that the directors had paid themselves (including £185,000 in the months leading up to liquidation) as "interim dividends".

The court held that the directors could not have intended nor could they be expected to work for nothing and so the payments to them should have been properly classified as remuneration.

This was despite the facts:

- that the payments had been recorded as dividends,
- that no PAYE/NIC had been paid,
- that the directors had no contracts,
- that the articles and equity prohibited such payments.

In our view this is a nonsense – the company was insolvent, failed to maintain proper accounting records and failed to pay its creditors, yet the directors paid substantial sums of money to themselves as and when they felt like it. It is also too simplistic to say that the directors cannot have been expected to work without a salary – their commercial interest could equally have been in building up the underlying value of the company.

Failure To Notify QFCH Of Appointment

Re Domestic & General Insulation Limited

Notice of a proposed resolution to wind up must be given under section 84(2A) of the Act to any QFCH *even*

if the relevant floating charge is not yet enforceable and could not, accordingly, intervene.

That stated, the failure to give such notice does not invalidate the winding-up resolution or the related appointment of a liquidator. If a QFCH wished to object to a CVL, it could petition for a winding-up or apply for an admin. The court made a slightly odd comparison with the notice provisions in administration which it felt should be applied differently as administration is a new, statutory regime.

BANKRUPTCY

Litigant in Person's Claim Struck Out
Reynard v Fox

Apart from having the best name ever, this case is another blow to litigants in person seeking special treatment. The bankrupt brought proceedings against his trustee seeking damages for breach of contract. The claim was struck out by the High Court for disclosing no discernible cause of action. The fact that the claimant was a litigant in person did not mean that he should be given any special indulgent. In any event, there was nothing else that the court could do – a claim is struck out under CPR 3.4(2) because it is not sustainable or it would be unfair to allow it to proceed.

The judge noted that the court would always try to assist litigants and might allow some leeway on the margins – particularly if it involved an obscure or complicated procedural rule – but the very fact of being a litigant in person did not entitle a party to any special treatment.

Transfer to Wife Was Undervalue Transaction
Re Hagan

The bankrupt had sought to make financial provision for his wife and son by putting various properties (including the matrimonial home) in trust for their benefit and agreeing to pay the mortgages on those properties. The trustee challenged those dispositions as undervalue transactions.

The wife claimed that the transactions had been in consideration for her agreeing to her husband's right to continue to see her and their son. The court held that such an agreement could not amount to valuable consideration as no legal right was conferred upon the husband.

Scottish Barony Does Not Vest In Trustee
Senior-Milne v Official Receiver

Some years prior to his bankruptcy, the bankrupt had bought himself a barony which had been put in trust with himself having a life interest. The bankrupt brought an action against the OR alleging that the OR should have used his interest in the barony to create new baronial titles that could have been sold for the benefit of the estate.

The High Court rejected the claim as (1) the barony did not vest in the OR and (2) the right to create new titles had been abolished by the Heritable Jurisdictions (Scotland) Act 1746/7.

The applicant in this case was a litigant in person – this appears to be something of a theme!

EMPLOYMENT

Equal Pay Claims on Insolvency
Graysons Restaurants Ltd v Jones

Where an employer went into an insolvency process before an equal pay award had been paid in full, those arrears would be treated as "arrears of pay". Accordingly, the appropriate proportion would be met by the National Insurance Fund and only the balance above the NIF cap would transfer to the purchaser under TUPE.

Increase in Statutory Cap
Employment Rights (Increase of Limits) Order 2018

With effect from **6 April 2018** a maximum *"week's pay"* has increased to **£508** per week – it was previously £489 so this represents a 4% pay rise!

CROSS-BORDER

COMI *within* the United Kingdom
Re Screw Conveyor Ltd

The EC Insolvency Regulation applies only to determine jurisdiction on an international platform. The question of determination of jurisdiction between countries within the UK is a matter of national law.

In this case, an English incorporated company had its registered office in England but its COMI was in Scotland. Under Scottish and English law, the Scottish courts could make an admin order only in respect of a Scottish registered company and could not exercise jurisdiction over this company.

The question of COMI was only relevant to establish which EU member state had jurisdiction – beyond that regional determination was a matter of national law.

Foreign Lawyers Not Subject to *ex p James*
Glasgow v ELS Law Ltd

The applicant was the bankruptcy trustee of a company in St Vincent. The company brought negligence proceedings against various advisors and was awarded damages which the judge had ordered to be paid into court rather than to the company. The defendant insurers sought to rely on, amongst other things, the rule in *ex p James* to compel the trustee to pay premiums due to them from the monies in court.

The court held that, even though the English court had recognised the St Vincent liquidation, the trustee was not subject to the control of the English court and was not therefore subject to the rule in *ex p James.*

Alistair Bacon
17 April 2018

No Limitation in Claims Against Directors

Burnden Holdings (UK) Limited v Fielding [2018] UKSC 14
First Subsea Ltd v Balltec Ltd [2017] EWCA Civ 186

Section 21(1) of the Limitation Act 1980 excludes any limitation in respect of claims against trustees either in relation to (a) fraud or (b) conversion of trust property to their own use. Section 21(3) however imposes a six year limitation on any other claim to recover trust property. In the above two recent cases, these provisions have been applied against misfeasant directors.

In Burnden, the defendants were the former directors and shareholders of the claimant ("Holdings") which was the holding company of a number of subsidiary companies. Prior to the liquidation of Holdings, the group had been involved in a complicated restructuring which had involved a section 110 scheme to remove one of the subsidiaries ("Vital") from the group and to transfer Holdings' shares in Vital to a new company ("BHUH"). BHUH was then liquidated and its shares transferred in specie to another company owned by the defendants.

Transfer of Holdings' shares to BHUH had been unlawful and in breach of the defendants' duties as directors. The transfers had, however, taken place six years and three days before proceedings were issued and the defendants sought to strike out the claim on the basis that it was time-barred. The defendants were successful at first instance but lost in the Court of Appeal - the matter then came to the Supreme Court.

Lord Briggs (with whom all the Supreme Court Justices agreed) held that s. 21(1)(b) applied even if there had been no dishonest intent on the part of the defendants. The net result was that they had ended up deriving a benefit from the unlawful transfer of company assets and they ought not to be able to retain that benefit through reliance on a limitation period.

In Balltec a director had resigned and set up his own company in competition to the claimant which sought an account of profits from the director on the basis of his breach of duty. By the time proceedings were issued, a claim for recovery of trust property would have been time-barred under s. 21(3). The Court of Appeal held that, as a director is a fiduciary and effectively a trustee of the company's assets, a claim for an account of profits fell under s. 21(1)(a) which meant that there would be no limitation period.

These cases are useful authorities for office holders seeking to bring claims against directors who may have benefitted from the unlawful treatment of company property. Directors are to be regarded as trustees of the company's assets. Any unlawful disposition of those assets for the directors' benefit will fall within s.21(1) and there will be no limitation period – this would certainly cover any claim for unlawful payments of monies to directors such as unlawful dividends or unauthorised 'salaries'. Furthermore, it matters not that the benefit might only be indirect so the transfer of assets or payment of monies to another company owned by the directors (as in Burnden) will not save them from liability.

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