AMB LAW

INSOLVENCY UPDATE

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Welcome to the 32nd Edition of **AMB Law's** ***Insolvency Update***. We are not sure what to say about the market at present. Apart from one or two obvious exceptions to the rule, our perspective is that the mid-market of our profession remains squarely in the doldrums with utilisation rates and new instructions and enquiries at an all-time low. On the plus side, we can at least meet up with colleagues and contacts so we do not need to cry into our beer alone.

If you would rather not receive these ***Updates*** of if you have colleagues who would like to be added to the list, please email *office@amblaw.co.uk*.

MISCELLANEOUS

Coronavirus Provisions

Winder based on a stat demand stayed until	30/09/2021
Other winders stayed until	30/09/2021
Temp Insolv PD remains in force until	30/09/2021
Commercial property recovery stayed until	25/03/2022*
Wrongful Trading suspension ended on	30/04/2001

** in Wales, it's 30/09/2021*

Valuation of Shares Following Company's Collapse

Dinglis v Dinglis

This is a case from last year that revolved around a s.994 petition presented by a minority shareholder in respect of unfairly prejudicial conduct by the majority shareholder. The minority shareholder was successful on his petition and in December 2019 the majority shareholder was ordered to buy his shares at a price based on the share price the previous summer.

Then came the Covid-19 pandemic – the company ceased trading and the company's value collapsed leaving the majority shareholder required to buy out the minority at a grossly over-inflated price. Unsurprisingly, the majority shareholder applied to have the order varied to take account of the price collapse.

The application was rejected. It was illogical to suggest that the original order should be varied in line with subsequent events (*cf* all those family law cases with the same arguments around ancillary relief). Further, as a matter of policy, litigation is intended to bring finality and the pandemic was not sufficiently extraordinary to warrant unpicking a properly made order.

The circumstances of this case will not be unique and, as we start to climb out of lockdown, they are likely to appear fairly often. The judgment would make a good read for anyone with a client in this situation.

The *Quincecare* Duty

Re Stanford International Bank Ltd

Readers will recall that the so-called *Quincecare* duty relates to a bank's implied duty to take reasonable care when carrying out its customer's instructions. In this case the liquidators sued HSBC for breach of that duty as the bank had paid out £116 million at a time when it knew that the company was insolvent and thus reduced the amount that would be available to the liquidation estate.

The Court of Appeal has held that the liquidators' claim was doomed to failure as amounts paid out were all paid to creditors of the company who, accordingly, suffered no loss. The amounts paid out simply reduced the amount of creditors in the liquidation.

Note too that, in the same judgment, the Court of Appeal also kicked into the long grass the liquidators' claim of dishonest assistance by the bank as the claimant was unable to point the finger at any dishonest individual. Such a claim could not be made generically against an organisation.

Scope of Professional Negligence

Manchester Building Society v Grant Thornton

Not an insolvency case *per se* but a decision that is relevant to all of us (and not just for epicaricacy).

Where a professional advisor owed a duty of care, the scope of that duty would be determined by the purpose for which the advice was being given. In other words, even if the advisor were negligent and the claimant's loss flowed from that negligence, the advisor might only be liable for losses which arose from within the scope of the duty – ie losses in respect if which the advice was sought.

In this case (involving the accounting treatment of certain interest swaps which skewed the client's balance sheet), the

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advisor was found to have been negligent. Damages were reduced by 50% contributory negligence to account for the claimant's premature rush to close out certain swaps which exacerbated its losses.

Directors' Liability for Litigation Costs

Goknur Gida Maddeleri Enerji Imalet Ithalat Ihracat Ticaret Ve Sanayi AS v Aytacl)

Again, this was not an insolvency case but the principle is relevant. The defendant was a director of an insolvent company against whom the claimant had been involved in litigation. The claimant argued that the director had funded and controlled the litigation for his own benefit and, accordingly, sought a non-party costs order.

The Court of Appeal set the test for awarding costs against a non-party as follows:

1) The party had controlled and funded the litigation;
2) The party stood to benefit personally; and
3) The party was guilty of *mala fides* or impropriety in pursuit of the litigation.

The court emphasized that the bar would be set high.

Immunity from Suit under s.236

Re MBI International & Partners Inc

The Court of Appeal has held that examinees being examined under s.236 should enjoy the same immunity from suit as a witness in a trial in respect of answers given during the examination. This is essentially a matter of public policy to facilitate an officeholders' investigations into the affairs of the company over which he is appointed by encouraging examinees to give full answers without fear.

Assignee Cannot Rely on s.212

Manolete Partners v Hayward and Barratt Holdings Ltd

The claimant had taken an assignment of certain of the liquidators' antecedent transaction claims and, as is common in such cases, also took an assignment of the company's claims against the directors for breach of duty arising out of the same facts.

ICCJ Briggs held, however, that whilst the company's claims against the directors for breach of duty properly vested in the claimant, it was not open to the claimant to pursue those claims by way of an insolvency application relying on s.212. Section 212 provides a summary remedy and is available only to liquidators whose office cannot be assigned. If Manolete wanted to proceed against the directors for breach of duty, it would need to do so by way of an ordinary part 7 claim.

CVAs / RESTRUCTURING PLANS

Legitimate Interest in CVA Challenge

Nero Holdings Ltd v Young

The company applied to strike out a landlord's challenge to its CVA based on an alleged breach of the directors' duties to the creditors in failing to explore potential buy-out offers for the company. The strike out application was on the basis that the challenger landlord had no legitimate interest in the outcome and was being funded by the hostile bidders to challenge the CVA. The court held that the landlord's hope that the CVA failed gave it a sufficient interest in the outcome and that it was proper that the CVA should be properly examined and tested by the court.

Restructuring Plans

Re Virgin Active Holdings Limited

This judgment has been analysed to death elsewhere and far better than we can do it so we shall not dwell.

Suffice to say that Snowden J's judgment is an obvious *must-read* for anyone looking at a plan. In relation to the '*no worse off*' test for the cram-down, the judge held the court was required to compare the impact on dissenting creditors under the plan against the most likely alternative outcomes. The judge held that the court could use its discretion to compare likely outcomes based on the evidence before it and it was not necessary to be obtain market valuations or similar.

In terms of the court's overall discretion to sanction a plan, the judge held that it was not the case that sanction would be automatic if the pre-conditions were met and the plan was just and equitable. In the current case, the dissenting creditors were largely landlords who would be '*out of the money*' whether the plan was allowed or not. On that basis, they had no skin in the game and their objections could be crammed down.

LIQUIDATION

Petitioner's Burden of Proof on Covid Petition

Re A Company (000068 of 2021)

It is now well established that there is a two-stage process in determining whether a winder can proceed during the pandemic. First, the company must show that it has been financially affected by Covid and this is a very low threshold. Secondly, the petitioner has to show that the company would still be insolvent if the effects of Covid were ignored.

In respect of the petitioner's burden of proof, the court held that it was insufficient simply to compare the level of the company's debt with earlier years. Nor was the fact that the underlying contract was entered into post-pandemic determinative of the company's insolvency.

Given that the restrictions are set to come to an end on 30 September, it may be unlikely that anyone will present a petition at this stage. For those that do, this case is a timely reminder that they

DIRECTORS

Basis of Director's Belief

Re Arise Networks Ltd

The company was wholly dependent on the transfer of working capital from Nigeria to fund its business in the UK and the USA. Notwithstanding Government restrictions on the transfer of funds being introduced in 2014, the company continued to incur substantial liabilities based on its

director's immutable belief that it would be able to continue trading.

Even though the court did not make a finding of dishonesty against the director, it found that his conduct was to the detriment of the company's creditors (to the tune of £7 million) and that he was in breach of his duties to the creditors. The director was disqualified for seven years.

Director's Agency v Liability

Tattersalls Ltd v McMahon

The director of a company attended an auction to purchase assets on behalf of the company. The auctioneer's terms stated that any actual bidder would be jointly and severally liable for a purchase together with the principal on whose behalf he was acting. Predictably, our hero's bid was successful but the company failed to pay. The auctioneer sued the director in reliance on its terms.

The court held that the director was clearly liable and that he could not rely on the third party protections in ss. 40 and 43 of the Companies Act 2006. The company's liability was not in question and that did not diminish the director's personal liability under the contractual terms.

This is something that crops up on things like credit applications (and AMB Law's engagement letters) - directors need to be clear about what they are signing and what they may be taking on personally.

Director's Failure to Provide for Debts

Re Avacade

The company managed to rack up substantial debts (£16 million) to HMRC arising out of various dodgy tax planning schemes. In the months leading up to liquidation, the directors caused the company to repay various loans to themselves whilst failing to make provision for any debts due to the creditors including, in particular, HMRC. The court found that the directors had acted in breach of their duty to the creditors as a whole and the directors were each disqualified from acting as directors under the CDDA.

BANKRUPTCY

Validation Orders and Legal Costs

Re Mallya

The rules relating to the making of validation orders reflect those for companies under s.1237 in that the debtor needs to show that his is solvent and the order has to be for the benefit of the debtor's creditors. Additionally, the court will also usually allow the debtor to incur the legal costs of defending his position.

In this case, the debtor had a validation order covering his reasonable living (not shabby at £22½K pcm) and legal expenses but he sought a further order in respect of the costs of litigation in India which related to the validity of the underlying judgment on which the petition was based – ie not the direct petition costs.

The court held that the so-called *Sinclair* exception under s.284 was narrow and could only apply to legal costs directly associated with the petition. Accordingly, the costs of litigation abroad could not be subject to a validation order.

The court is likely to have been influenced by the fact that the application related to a pot of money held in court. If it had acceded to the application, it would effectively be releasing those funds without control and outside the jurisdiction.

'Place of Residence'

Re Su Hsin Chi

Since 2013 there has been a new version of s.265 (which governs the court's jurisdiction respect of bankruptcy petitions) and the old test of 'personally present' in the jurisdiction has been replaced by one of (i) domicile or (ii) within the previous three years being ordinarily resident or having a place of residence or place of business.

In this case, the debtor was involuntarily within the jurisdiction at the time that the petition was presented. The debtor's physical presence here was as a result of certain injunctions preventing his leaving and for part of the time he was actually in prison.

Bacon J* held that the words *'place of residence'* had to be given their ordinary meaning which connoted a sense of permanence and an expectation of continuity which meant the debtor's home or settled place of abode. It did not mean prison or a hotel or other transient place of enforced occupation and, accordingly, the petition was dismissed.

Presumably, if this case had come up prior to the Enterprise and Reg Reform Act 2013, the petition would have been fine.

* - *no relation*

CROSS-BORDER

Correct Application of COMI Test

Re Melars Group Limited

The company's registered office was in Malta. The judge at first instance had concluded that the company's presence in Malta was in fact little more than a post box and actually the company's business was in England and, accordingly, the English court had jurisdiction to make a winding up order.

On appeal Miles J set aside the winding up order. Under the Recast Reg, the assumption was that the registered office was the COMI (ie Malta) which was publicly available information. The first instance judge had not started from this presumption and, in trying to ascertain whether the presumption should be rebutted, had confused the place of the company's operations with the place where the company's interests were administered. The key was to focus on information that was generally available to the public.

Given that the Recast Reg no longer applies the minute niceties of the COMI test are largely hypothetical anyway.

Alistair Bacon
20 August 2021

'Vacant Possession' – the Wholly Trinity

Capitol Park Leeds plc v Global Radio Services Limited
[2021] EWCA 2750

One of the knotty problems often posed to officeholders is the question of what needs to be done to avoid liability for rented premises previously occupied by the company. Given that a failure to hand back the property with vacant possession could lead to the landlord's being entitled to be paid rent as an expense of the insolvency (under the *Lundy Granite* principle as espoused in the *Goldacre* case), this can be a significant issue.

In the *Global Radio* case, the tenant purported to rely on a break clause in the lease which enabled it to determine the lease by giving notice and then giving up vacant possession of the premises. The *'premises'* were defined in the lease as including the physical property together with all the landlord's fixtures and fittings.

In the event, the tenant handed the property back entirely stripped of all such fixtures and fittings (including ceiling grids, floors, ducting etc). As the property was wholly unusable , the landlord argued that the tenant had not complied with the exact wording of the break clause as it had not given up vacant possession of the 'premises' as defined (as the fixtures and fittings formed part of that definition and were missing).

The landlord was successful at first instance and Benjamin Nolan QC found that the outcome of an unusable property was precisely the sort of mischief against which the landlord had sought to guard in defining 'premises' in the way that it did.

The Court of Appeal, however, took a different view. Newey LJ referred to the dictum of Nugee J in *Goldman Sachs v Procession House Trustee (2018)* in which he referred to vacant possession consisting of the trilogy of people, chattels and interests. The Court of Appeal therefore held that the test for whether vacant possession has been given is not concerned with the state of the property *per se* but merely with the property's being devoid of people and chattels that would prevent the landlord using it and also the tenant's abandoning its legal interest.

If, for example, administrators are actively using the premises for trading, clearly they will need to pay rent as an expense of the admin. On the other hand, if the premises are empty and the administrators hand the keys back to the landlord, they will clearly have given up vacant possession and incur no ongoing liability for the rent. Predictably, however, many situations lie somewhere in the middle and the question therefore arises as to what steps the officeholder has to take to ensure the he has given up vacant possession and will not incur any ongoing liability. We now know that the issue will lie in the trinity of people, chattels and interest and that the one most likely to cause a problem is chattels.

In many cases, the insolvent company will have assets remaining at the premises and it becomes largely a question of fact and degree as to whether those assets will prevent vacant possession's being given. By way of illustration, in a trading administration that we dealt with recently, a furniture retailer had a number of shops the majority of which were empty but for a few loose items that could be disposed of in the course of the landlord's clearing the property; they did not prevent the landlords' reletting. Conversely, the company's head office was piled floor to ceiling with heavy furniture as well as all the books and records and IT system for the business. In relation to the offices, the administrators could not be said to have given vacant possession as the landlord could do nothing with the premises until the chattels were all removed – accordingly, the landlord's claim to rent fell to be deal with as an expense.

When faced with this issue, it is important to get early advice – preferably from AMB as the repercussions for the insolvency estate could be enormous.

AMB Law Limited
46 New Broad Street
London
EC2M 1JH

T: +44 (0)20 3651 5646

office@amblaw.co.uk

AMB Law Limited
Epsilon House
West Road
Ipswich
IP3 9FJ

T: +44 (0)1473 276103

Alistair Bacon
Principal

T : 020 3651 5647
M: 07881 554062
abacon@amblaw.co.uk

Matthew Rice
Paralegal

T : 020 3651 5704
01473 276181
mrice@amblaw.co.uk

Stephen Carter
Consultant

T : 020 7329 4242
scarter@amblaw.co.uk