AMB LAW

INSOLVENCY UPDATE

No. 38 • March 2024

It's back by popular demand - welcome to the 38th Edition of **AMB Law's** ***Insolvency Update*** which is the first one for nearly two years (the 37th edition was abandoned 18 months ago!). A lot seems to have happened in that time – numerous Conservative governments have come and gone and the restructuring and insolvency profession has seen something of a resurgence with numbers on the up in all areas (apart from CVAs which have been largely kiboshed by HMRC's extended preferential status).

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MISCELLANEOUS

Amending a Proof of Debt
Re BV9 Ltd

A creditor submitted a proof of debt for £1 million which arose by way of an interest margin following an assignment of a debt from the creditor to the company. The administrators rejected the claim and the creditor appealed.

At the appeal, the creditor changed its position and argued that its claim in fact arose by way of an unpaid loan and an intercompany running account.

The court upheld the administrators' rejection of the debt and held that it could not rule on the reformulated claim as there had been no application to amend the proof of debt.

This case is unusual and turned entirely on its own rather peculiar facts. Nonetheless, it is a reminder that proofs of debt need accurately to set out the basis of the debt and to provide sufficient evidence to enable officeholders to adjudicate upon them.

ADMINISTRATION

Administrators Not 'Officers' of the Company
R v North Derby Mags ex p Palmer et al

Punters will recall that this was the case about criminal liability for administrators' failure to notify the Secretary of State in advance of mass redundancies. The Supreme Court has held that an administrator under the 1986 Act is *not* an officer of the company over which he is appointed.

This might seem to be a sensible decision in the context of the particular case but the Supreme Court has flown in the face of perceived wisdom and declared that previous authorities were wrongly decided. Its comparison with receivers does not work because receivers never were regarded as officers of the company (that being one of the differences between [admin] receivership and liquidation/ administration). Still, this state of affairs does make sense in the context of this case and better sits with the detached role of administrators.

Former Administrators Can Apply to Increase Fees
Re Good Box Co Labs Ltd

The company moved from admin to a Part 26A restructuring plan and, as a part of that process, the administrators' fees were assessed and agreed by the creditors at £235K. The administrators subsequently sought payment of a cheeky, additional £209K which the plan administrators rejected so the administrators applied to court under rules 18.24 and 18.28.

The administrators' claim ultimately failed on a technicality but the important bit is that the court held that it needed to be 'purposive' in interpreting rule 18 and references to the office-holders should also include former office-holders. Procedurally, the former office-holders were entitled to bring their grievance before the court under r.18.28.

Court's Discretion under Para 71
Re Lyphe Group Limited

Administrators received a number of offers for the business and assets of the company. Three of these were broadly in the same ballpark but the fourth was roughly double the rest. The highest offer came from a party connected with the director who held fixed charge security over the company's assets.

The administrators were not satisfied with information provided by the highest bidder in respect of the source of funding and rejected the offer in favour of a lower one. The director refused to release his security and the administrator had to make an application under para 71.

The High Court held that the question of whether to grant relief under para 71 was wholly a matter of its discretion. The fact that three other independent offers had been made all with a smidgeon of each other tended to suggest that they represented the true value of the assets. In the instant case, the administrators had acted rationally in rejecting the

highest offer based on their fears under the Money Laundering, Terrorist Financing Regs. Given that there were also severe issues of urgency, the court gave the relief sought and allowed the assets to be sold as though they were free from any charge.

LIQUIDATION

Set-Off Balance Not An 'Asset'
Smithson v L'Occitine Limited

The company had been in dispute with a customer pre-liquidation with each claiming substantial sums from the other. When the company went into liquidation, the liquidators applied the mandatory set-off rules and decided that the sum owed to the company by the customer was £309K. For reasons that are not clear, the liquidators then decided to use their powers under s.234 to compel recovery of the sum on the basis that the set-off balance was an asset of the company in the customer's possession.

This assertion was rejected at first instance and again on appeal: the right to recover the balance is a *chose in action* not a form property to which s.234 could be applied and the liquidators needed to issue a part 7 claim.

Desire to Prefer in Wrongful Preferences
Re CGL Holdings Limited

For a transaction to be impeachable under s.239, the company's desire to prefer must be present at the time of the operative decision to effect the transaction, not when the transaction was effected (if that was a later date). The decision turned very much on the particular facts of the case but the judgment contain interesting commentary on the question of 'operative decisions' – we anticipate that this will become the next hotbed of litigation in preference clams.

Default Judgment and Third Party Rights Act
Scotland Gas Networks plc v QBE UK Ltd

The issue arose as to whether a judgment in default would be sufficient to trigger an insurer's liability under the Third Party (Rights Against Insurers) Act 2010. In this case, the insured company had gone into liquidation after proceedings were issued against it for compensation for SGN's costs of repairing and rerouting a gas pipeline damaged by the company. The company failed to appear at an interlocutory hearing and the court awarded the claimant its £3 million by way of judgment in default.

The claimant sought to pass this on to the company's insurers who resisted payment on the basis that, for liability under the Act to be triggered, there needed to have been a decision based upon the merits of the case – ie a default judgment was insufficient.

The Court of Session (it being a Scottish case) agreed with the claimant – the language of the Act was simple and did not differentiate between different forms of judgment so one in default was sufficient. Whilst this is probably a welcome decision for most, it could create a problem for insurers where companies, faced with insolvency, simply cannot be bothered to defend an insured claim. The insurers will need to look to a contractual obligation on the insured to do so.

DIRECTORS

Order Against Misfeasant Director
Re Pure Zanzibar Ltd

The director of a travel company continued to take bookings and deposits from customers long after its ATOL licence had expired and in respect of which it had no prospect of providing holidays.

The director was disqualified for seven years for *'woefully reckless and incompetent conduct'*.

This is, apparently, only the second case on compensation orders following disqualification. Whilst it is not clear what the test for causation should be, ICCJ Barber held that on any basis the director had caused the customers to lose their deposits and he was ordered to pay them compensation of £81,000.

One aspect of this case that is not discussed and is one that perpetually astonishes us is as to how on earth a director who has flagrantly defrauded customers can be disqualified for *only* seven years. The Insolvency Service is habitually seeking longer periods against directors who may have missed a couple of VAT payments which strikes us a great deal less culpable. Just saying.

Dishonest Assistance under s.212
Re Gamenation (UK) Limited

The respondent in this case was not a director of the company but was clearly closely involved to the point of being a *de facto* director. There was no claim against the respondent in respect of any breach by her of any duty to the company. Liquidators brought proceedings under s.212 for dishonest assistance in respect of the respondent's assisting the director in various breaches of duty.

The respondent brought an application for strike out on the basis that the claim did not fall within s.212 as there was no breach of duty by her. ICCJ Agnello dismissed the strike out application and held that the respondent could be found liable under s.212 by assisting a third person (in this case, the director) who *had* been in breach of duty to the company.

BANKRUPTCY

No Duty to Act 'at all costs'
Re Brakes

The Brakes' litigation saga seems to have gone for decades. Readers may recall that the bankruptcy trustees' decision not to intervene in possession proceedings was deemed 'perverse' (*that decision was reported in our 37th edition which was abandoned. Sorry).* Whilst the court maintained that it would not routinely interfere with a trustee's decision-making, it would do in this case.

The Court of Appeal has overturned the first instance decision. Although trustees had a duty to act in the interests of creditors, it was not a duty to act in the interests of creditors "*at all costs*". The trustees – as experienced professionals – had a statutory discretion to decide what steps to take and their conclusion was that intervening was unlikely to result in a benefit for creditors as the potential

recoveries were paltry compared to the downsides and the possible risks of litigation.

This has long been a thorny issue for officeholders in impecunious estates. Our position was always been and remains that officeholders are under a duty to undertake at least a minimum effort in order to secure the assets (eg inspecting, changing locks etc) but that duty would not extend to spending *real* money by becoming embroiled in litigation.

Petition Dismissed Where Debt Not Due
Re Al Hindi

Under s.48(2) LTA 1987, rent will not fall due until the landlord has given the tenant notice of an address for service on the landlord (*no, really – it's true. Ed*). In this case, the landlord failed to serve as s.48 notice until *after* he had served a stat demand for unpaid rent and presented the attendant petition.

Unsurprisingly, given the clear wording of, s.48 the court held that the liability to pay rent had not arisen at the time that the stat demand was served and, accordingly, the petition was dismissed.

'Carried on Business'
Durkan v Jones

A debtor lived in LA but had a property in Warwickshire which was let. The debtor challenged a petition that was presented against him on basis that he was outside the jurisdiction.

The court accepted that the debtor was not ordinarily resident in England as he had moved to LA with no intention of returning. However, the court held that the debtor's activity of letting out the property constituted the *carrying on of a business* sufficient to found jurisdiction under s.265(2)(b)(ii) – the size and longevity of the business were not matters with which the court would be concerned.

Trustee's Knowledge for *'Use it or Lose it'* Rule
Re Khilji

If the bankrupt does not inform the trustee of his interest in a property within three months of commencement, the 3-year time limit does not start to run until the trustee *'becomes aware'* of the bankrupt's interest. In this case, the bankrupt had, at her interview with the OR, made oblique reference to a property owned by her late husband who had died intestate and in respect of which she paid the mortgage.

The trustee issued an application for possession and sale 3½ years after commencement but claimed that it was within three years of her *becoming aware* of the bankrupt's interest in the property. The question was therefore as to whether the trustee had been *informed* by the bankrupt of her interest.

Deputy ICCJ Curl held that the trustee had to have actual knowledge of the bankrupt's interest in order for time to start running and the oblique reference to her husband's property was insufficient.

Foreign Judgment May Found Bankruptcy Petition
Re Valeriy Ernestovich Drelle

The bankrupt appealed against the making of his bankruptcy order on the ground, *inter alia,* that the petition had been founded upon a Russian judgment that had not (and could not have) been registered as a foreign judgment.

Richards J, on appeal, upheld the first instance decision dismissing the bankrupt's appeal. There has long been clear authority that a bankruptcy petition can be presented in respect of a judgment made in a foreign court and that the judgment does not need first to be registered in the High Court as it would need to be in order to be enforced within the jurisdiction.

Bankruptcy is effectively a class action and is entirely different from 'enforcement' – presentation of a petition does not equate to taking a step to enforce the judgment.

Cross-Undertaking in Damages
Re Ubhi

Having successfully persuaded the court that it was the norm for a cross-undertaking to be limited to the assets of the insolvent estate, a liquidator of a partnership was granted a freezing injunction against the two former partners. The liquidator's cross-undertaking was limited to £200,000 being the amount in the estate rather than being unlimited which was actually the norm.

The partners challenged the freezing injunction and the Court of Appeal held that the liquidator had misled the court and thus failed in his duty of disclosure. Whilst there have been cases in which an officeholder's cross-undertaking has been limited, it was overstating matters to suggest that that was the usual form of order. The burden would be on the applicant for a injunction to show good reason for the court to allow only a limited cross-undertaking in damages. Accordingly, the puisne judge had misdirected himself and had been wrong to accept a limited undertaking. The injunction was dismissed.

EMPLOYMENT

Stat Demand For Return Of Bonus Upheld
Steel v Spencer Road LLP

An employee's contract provided for him to be paid a discretionary bonus which could be clawed back by his employee if he gave or was given notice within three months of receipt of the bonus. The employee received a bonus of £187K in January and then resigned in February. The employer served a stat demand in respect of the bonus paid.

The employee sought to have the stat demand set aside on the basis that the claw-back provisions amounted to an unlawful restraint of trade. This argument was rejected both at first instance and on appeal to Bacon J* who held that the claw-back provisions were lawful and unremarkable.

* *no relation*

Alistair Bacon
13th March 2024