Julian Dobson SOLICITORS Insolvency Lawyers

Insolvency
Legal Update
2020

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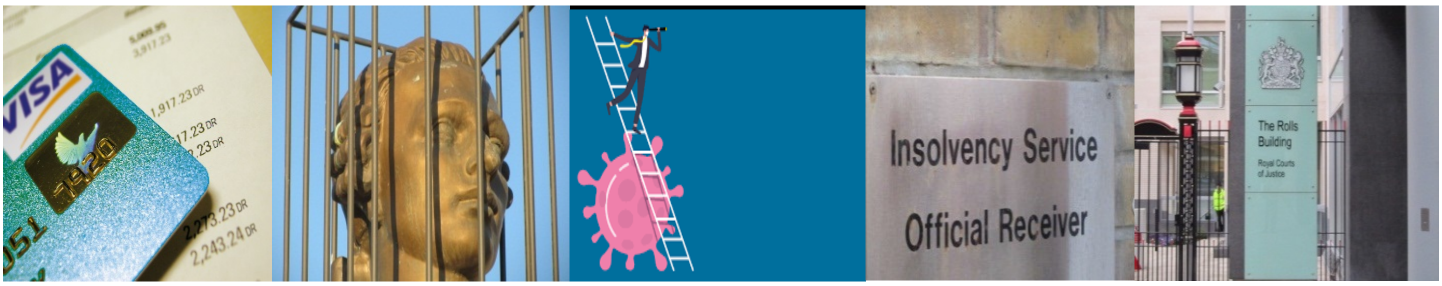

JULIAN DOBSON SOLICITORS

We are solicitors dealing exclusively with insolvency matters. Based in the City of Brighton & Hove, we are close to Brighton County Court, one of the busiest bankruptcy courts in the country. The firm acts mainly for insolvency practitioners throughout England and Wales.

As a firm of solicitors, we have a Licensed Insolvency Practitioner (non-appointment taking). We emphasize a practical approach in our dealings with clients, the courts and others.
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Dearing v Skelton [2020] EWHC 1370 (Ch)

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Dearing v Skelton [2020] EWHC 1370 (Ch)

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Re Debenhams Retail Limited (In Administration) [2020] EWCA Civ 600

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Ezair v Conn Re Charlotte Street Properties Limited (In Administration) [2020] EWCA Civ 687

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Ezair v Conn Re Charlotte Street Properties Limited (In Administration) [2020] EWCA Civ 687

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Ezair v Conn Re Charlotte Street Properties Limited (In Administration) [2020] EWCA Civ 687

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Secure Mortgage Corporation Limited v Harold [2020] EWHC 1364 (Ch)

DECISION

- The appointing personal representatives were unable to prove their title as they had no grant of representation
- The floating charge was held to be enforceable
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Secure Mortgage Corporation Limited v Harold [2020] EWHC 1780 (Ch)

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Brake v Swift [2020] EWHC 1810 (Ch)

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Brake v Swift [2020] EWHC 1810 (Ch)

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Brake v Swift [2020] EWHC 1810 (Ch)

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Bucknell v Wilson [2020] EWHC 1200 (Ch)

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Bucknell v Wilson [2020] EWHC 1200 (Ch)

Ms Wilson

- Argued she was a commercial creditor
- She received less than other creditors
- She no longer had the money
- Limited means/low income
- House would have to be sold
- Damage to business/income
- Acted in good faith
- Change of position defence

Bucknell v Wilson [2020] EWHC 1200 (Ch)

Decision

- Insolvency Test satisfied
- A Desire Rebuttal Test not satisfied
- For discretion to be exercised in favour of Ms Wilson the circumstances would have to be "out of the norm"

Bucknell v Wilson [2020] EWHC 1200 (Ch)

Decision

- It was not the norm for transferee to:
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  - Act in good faith
  - No longer have the proceeds
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- Debtor had guaranteed arrangement fee due to bank of US$75,000 in respect of facility US$500 billion
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Go Capital Limited v Phull [2020] EWHC 1235 (Ch)

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Go Capital Limited v Phull [2020] EWHC 1235 (Ch)

Requirements for guarantee:

- Section 1 Law of Property (Miscellaneous Provisions) Act 1989
- Document must make it clear intended to be a deed
- Signature must be signed in presence of a witness and delivered as a deed

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Go Capital Limited v Phull [2020] EWHC 1235 (Ch)

Decision

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- Nothing in it for guarantor
- Lack of professional care in preparation of documentation
- Guarantee not executed properly
- Not witnessed and nothing to indicate it was a deed

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Go Capital Limited v Phull [2020] EWHC 1235 (Ch)

Decision

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Oyesanya v Jackson [2020] EWHC 542 (Ch)

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Oyesanya v Jackson [2020] EWHC 542 (Ch)

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- No real prospect of Appeal succeeding
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Thomas v Bulathwela [2020] BPIR 430

- Mr. and Mrs. Bulathwela were solicitors and ran two legal practices
- Mrs. Bulathwela was the sole legal owner of Whitchurch Lane property
- Mr. and Mrs. Bulathwela joint owners of Manor Park property
- Mr. & Mrs. B executed legal charges over both properties to Legal Services Commission ("LSC")
- Mrs. B made bankrupt by LSC

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Thomas v Bulathwela [2020] BPIR 430

- Joint trustees issue application for declaration sole legal and beneficial owner of Whitchurch Lane property
- Application opposed by Mr. B on grounds he was joint owner under matrimonial rights
- Directions for filing of witness statements
- Witness statement filed without permission

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Thomas v Bulathwela [2020] BPIR 430

First instance judgment

- Mr. B's claim to beneficial interest in Whitchurch Lane property dismissed
- Reasons:
  1. Claim under Matrimonial Act irrelevant
  2. Mr. B to prove he had an equitable interest
  3. Mrs. B's support of little significance
  4. Mortgage payments did not create resulting trust in favour of Mr. B

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Thomas v Bulathwela [2020] BPIR 430

First instance judgment

5. No common intention to establish constructive trust as no evidence of discussion
6. The fact that Manor Park in joint names indicated decision that Whitchurch Lane would be sole property of Mrs. B
7. No explanation as to why both executed charges in favour of LSC over Whitchurch Lane property

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Thomas v Bulathwela [2020] BPIR 430

Appeal

- Only permitted evidence taken into account
- Effect of mortgage payments
  - Barrett v Barrett [2008] EWHC 1061 (Ch)
- Mortgage payments not sufficient to establish resulting trust for Mr. B
- No constructive trust based on granting of LSC charges
- Appeal dismissed

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Atkinson v Varma [2020] EWHC 1868 (Ch)

- Application by liquidator under s234 and s236 IR1986
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1. May only rely on grounds in application notice unless permission granted

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Atkinson v Varma [2020] EWHC 1868 (Ch)

2. Contempt of Court Order
   (a) the respondent must have known of the terms of the order
   (b) respondent must have acted in breach of the order
   (c) he knew of the facts which made his conduct a breach

4. Penal notice must be put on the order

5. Penal notice may be dispensed with if no injustice

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Atkinson v Varma [2020] EWHC 1868 (Ch)

6. May be held in contempt for making false statement in a document verified by a Statement of Truth

7. To establish false statement in document verified by a Statement of Truth must show:

   i. Statement was false
   ii. Statement would interfere with the course of justice
   iii. Maker had no honest belief in truth of statement and
   iv. Knew likely to interfere with course of justice

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Atkinson v Varma [2020] EWHC 1868 (Ch)

Decision

- Having found that the ground for contempt was established in respect of a number of specific grounds it was also held that he had made false statements in respect of which he had no honest belief in their truth and which interfered with the course of justice
- Further the interference with the course of justice was the intended result.
- Mr. Varma was in contempt of court and the matter was adjourned for sentencing

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Duckworth v Parekh [2020] EWHC 2360 (Ch)

- Application to set aside judgment for misfeasance
- Applicants contend not served with original proceedings
- Rule 7.47 IR1986 (r12.59 2016 Rules)
- Court's power to review rescind or vary any order
- Papanicola v Humphreys [2005] 2 AER 418
- Rule 7.55 (IR86) (r12.64 2016 Rules)

Duckworth v Parekh [2020] EWHC 2360 (Ch)

- Service requirements
- CPR Part 6
- Postal service to "the last usual or last known residence"
- "Current residence"
- Application for alternative service
- 21 Kingsdown Avenue or 97 Pollards Hill South?

Duckworth v Parekh [2020] EWHC 2360 (Ch)

- Service held to be irregular
- Had this caused any "substantial injustice"?
- Was there any defence to the claim?
- Misfeasance judgement for £38,059 payments to:
  - Grosvenor Hale Limited
  - HSBC Life UK Limited
  - Mrs Parekh
  - London Borough of Croydon
  - Travel expenses

Duckworth v Parekh [2020] EWHC 2360 (Ch)

Decision

- Judgment would be set aside if prejudice caused and arguable defence
- Payments made to Mrs. Parekh were a loan
- No entitlement to payment for services rendered
- No entitlement to salary

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Duckworth v Parekh [2020] EWHC 2360 (Ch)

Decision

- Payments did not constitute dividends
- Claim for set off re payments made by Mrs. Parekh, their son and Mr. and Mrs. Parekh to the Company
- Rule 4.90 IR1986 (r14.25 2016 Rules)
- Payments of money that was used for personal purposes does not equal misfeasance

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Duckworth v Parekh [2020] EWHC 2360 (Ch)

Decision

- Monies could have been lent if approved by resolution of members
- Arguable that payments to the Company could be set off against loan accounts
- Judgment would be set aside but only on grounds of arguable defence that payments to the company could be set off against loan account

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Re System Building Services Group Limited (In Liquidation); Hunt v Michie [2020] EWHC 54 (Ch)

Chronology

12 July 2012	Administration
03 July 2013	Conversion to liquidation
24 February 2016	Dissolution
30 June 2016	Mrs. Sharma made bankrupt
25 April 2017	Company restored to Register
03 May 2017	Liquidator appointed

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Re System Building Services Group Limited (In Liquidation); Hunt v Michie [2020] EWHC 54 (Ch)

- Alleged sale of property at undervalue to director
- Liquidator's claim against director for breach of duty/misfeasance
- Director's duties s171-175 of the Companies Act 2006
- Duty to act in best interest of creditors where company is insolvent or likely to become insolvent - BTI 2014 LLC v Sequana SA [2019] BCC 631

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Re System Building Services Group Limited (In Liquidation); Hunt v Michie [2020] EWHC 54 (Ch)

- Directors are not removed from office on administration/liquidation
- Directors may not exercise management powers without consent of administrators
- In liquidation all powers of directors cease save to the extent the liquidation committee or creditors sanction their continuance

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Re System Building Services Group Limited (In Liquidation); Hunt v Michie [2020] EWHC 54 (Ch)

- Paras 61 and 63 Schedule B1 IA1986
- Section 103 IA1986

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Re System Building Services Group Limited (In Liquidation); Hunt v Michie [2020] EWHC 54 (Ch)

- Property valuation
  - 30 December 2009 property purchased by company for £185,000
  - 10 November 2011 accounts for year ending 31 March 2010 value £188,065
  - Administrator's proposals estimated value at £200,000
  - 05 September 2012 Statement of Affairs signed by director value £180,000

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Re System Building Services Group Limited (In Liquidation); Hunt v Michie [2020] EWHC 54 (Ch)

- 25 September 2012 liquidator's independent valuation £195,000
- 12 September 2014 property sold by liquidator to director for £120,000
- July 2014 single joint expert values at £265,000 or £245,000 if works required
- 2016 director markets property at £335,000
- At trial single joint expert values property at £300,000

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Re System Building Services Group Limited (In Liquidation); Hunt v Michie [2020] EWHC 54 (Ch)

Decision

- Directors duties under s170-177 CA2006 continue notwithstanding administration/liquidation
- The director knew the property was worth significantly more than price paid
- The company was clearly insolvent at time of purchase and it was not in the interests of creditors to purchase at below market value

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Re System Building Services Group Limited (In Liquidation); Hunt v Michie [2020] EWHC 54 (Ch)

Decision

- No relief for director under s1157 CA2006
- Institutional constructive trust meant that director held property on trust for company in liquidation
- Director given an allowance for purchase price of £120,000 paid by him

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Re System Building Services Group Limited (In Liquidation); Hunt v Michie [2020] EWHC 54 (Ch)

Decision

- Director given an allowance of £20,000 for repairs spent on property
- Director ordered to pay £65,513 to company in liquidation

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Brittain v Chamberlain [2020] EWHC 1648 (Ch)

- 07 September 2017 North Point Global Limited CVA
- 17 May 2018 Baltic House Developments Limited in liquidation
- 18 February 2020 liquidators proof in CVA for preference under s239 IA1986
- Supervisor rejects proof and liquidator appeals against rejection

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Brittain v Chamberlain [2020] EWHC 1648 (Ch)

Questions

1. Are the liquidators bound by the CVA under section 5(2) IA 1986?
2. If bound by the CVA are the liquidators entitled to prove as creditors in the CVA?

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Brittain v Chamberlain [2020] EWHC 1648 (Ch)

Decision

- Notwithstanding the fact that the liquidators were appointed post-CVA it was held that the preference claim was both a contingent debt and is provable
- At the time of the CVA BHD had clearly been involved in transactions i.e, payments. At the time of the transactions it was assumed that it was insolvent and that liquidation and a preference claim was likely

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Brittain v Chamberlain [2020] EWHC 1648 (Ch)

Decision

- Preference claim should be treated as a debt falling within the CVA regime and is therefore bound within it
- The liquidators are entitled to prove as creditors under the CVA for their contingent provable debt

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Administration

A.R.G. (Mansfield) Limited [2020] EWHC 1133 (Ch)

Defect in appointment of administrators

Facts

The defect in question was a failure to obtain the consent of the Financial Conduct Authority ("FCA") to put the company into administration. The directors having placed the company into administration without appreciating the requirement for the consent of the FCA. FCA consent was granted albeit some three months later.

The company's business was general building contractors. Ongoing difficulties following the 2008 recession eventually led to the company becoming insolvent and a notice of intention to appoint administrators was filed on 07 January 2020. National Westminster Bank as qualifying charge-holder consented to the appointment on 09 January 2020. On 10 January 2020 notice of appointment of administrators was filed.

The purpose of the administration was to achieve a better result for the company's creditors as a whole than would be likely if the Company were to be wound up (without first being in administration). It was a review conducted by one of the administrators' staff in early March that revealed that a previous search of the FCA register had omitted the full-stops and therefore had not disclosed the fact that the company had "appointed representative status" for the purposes of the FCA because it operated a trust mark guarantee scheme which was backed by an insurance policy.

A similar situation had arisen in the case of **Re M.T.B. Motors Limited [2010] EWHC 3751 (Ch)**. In that case the company's name was recorded on the FCA register but without the full-stops after the first three letters. Similarly, the FCA eventually gave consent to the appointed administrators at a later date.

The requirement for consent of the FCA is contained in **section 36A** of the **Financial Services and Markets Act 2000 (FSMA).**

What is the effect of breach of statutory requirements?

The court considered the situation where the requirement is mandatory, and a failure invalidates the act in question compared to a situation where it is merely directory and therefore a failure does not invalidate. That approach was modified in the case of **R v Soneji [2005] UKHL 49; [2006] 1 AC 340**, where a more flexible approach was identified by focusing on what consequences Parliament intended as a result of the breach. In addition to considering the consequences of a breach of statutory requirements, the court also had regard to what powers are available to it to deal with such matters.

Tools available to the Court

Rule 12.64 Insolvency (England and Wales) Rules 2016 (r7.55 IR1986) provides as follows:

> "*12.64 Formal defects*
>
> *No <u>insolvency proceedings</u> will be invalidated by any formal defect or any irregularity unless the court before which the objection is made considers that <u>substantial injustice</u> has been caused by the defect or irregularity and that the injustice cannot be remedied by any order of the court*."

Para 104 Sch B1 Insolvency Act 1986

> ***"104** An act of the administrator of a company is valid in spite of a defect in his appointment or qualification."*

In dealing with defects in the appointment of administrators the court has three possible routes:

1. The irregularity or defect does not invalidate the process;

2. The irregularity means the appointment is not valid. The court may rely on paragraph **104** of **Sch B1** to confirm the validity of the acts of the purported administrators, even if the appointment is not itself valid;

3. The court may decide to appoint administrators under its separate power and purport to do so retrospectively.

The Soneji Approach

The focus is:

> "*on the consequences of non-compliance and taking into account those consequences, to consider whether* [as a matter of statutory construction] *Parliament intended the outcome of non-compliance to be a total invalidity*"

In short to ask whether it was a purpose of the legislation that an appointment made in breach of the relevant provision should be a nullity.

The authorities regarding appointments of administrators

Re Awan (a Bankrupt) [2004] BPIR 241

Although a bankruptcy case this has been relied upon in the context of administrators' appointments. The issue was a failure to prove service of the bankruptcy petition. The effect was that the bankruptcy order was one that should never have been made. The Judge was not prepared to apply **r7.55 IR 1986 (12.64 IR 2016)** to waive the defect in service. He did state that he considered there was a substantial injustice which could not be remedied by a court order. In essence he was saying that **r7.55** did not apply in terms of validating the actions taken.

Re G-Tech Construction Ltd [2007] BPIR 1275

In this case the wrong form had been filed with the court. The form that was used was one following the service of a notice of intention to appoint rather than the form where no intention to appoint had been given. Hart J decided that **r7.55 IR 1986** did not apply because <u>insolvency proceedings</u> were never commenced. This is because **para 31 of Sch B1** states that the appointment only takes effect once the relevant forms have been filed under **para 29** which had not occurred. Instead he ordered that the administrators be appointed with retrospective effect dating back to within two weeks of the original appointment. It could not be made earlier as the effect would have been that the administration would have lapsed before the hearing.

Re Blights Builders Ltd [2006] EWHC 3549 (Ch)

Administrators were appointed whilst there was an outstanding petition to wind the company up. This is prohibited under **para 25 Sch B1**. The solution was to give the administrators an indemnity, declare their acts valid under **para 104 Sch B1** and to make a prospective administration order.

Re Kaupthing Capital Partners II Master LP Inc, Pillar Securitisation SARL v Spicer [2010] EWHC 836 (Ch)

Administrators were purportedly appointed over a limited partnership using the prescribed form for companies. As the forms were significantly different the appointment was invalid. It could not be saved by **r7.55 IR 1986** as it went to the validity of the appointment and therefore there were no insolvency proceedings. Further para **104 Sch B1** could not be applied. The Judge left over the further decision of whether or not to make a retrospective appointment.

Re M.T.B. Motors Limited [2010] EWHC 3751 (Ch)

This case concerned the failure to obtain consent of the FCA to the appointment. It was held that the purported appointment was void and the defect not capable of being cured under either **r7.55 IR 1986** nor **para 104 Sch B1**.

Following **G-Tech** the court made an administration order with retrospective effect.

Hill v Stokes plc [2010] EWHC 3726 (Ch)

Here there was a failure to serve a notice of intention to appoint on prescribed persons who had distrained against the company's property who fall within **para 26 (2) Sch B1**. In that case the requirement of **para 28 Sch B1** referring to an appointment being possible only when the requirements of **paras 26** and **27** have been met was to be read as only referring to **para 26 (1)** only. Notwithstanding that the court effectively applied the Soneji Approach in that the defect was not so fundamental as to result in the appointment being invalid.

Minmar (929) Ltd v Khalastchi [2011] EWHC 1159 (Ch)

In this case the appointment was held to be invalid because there had been insufficient directors present at the board meeting and that no notice of intention to appoint had been given to the company under **para 26(2)** even if there was no person falling within **s26(1)**. That failure invalidated the appointment.

Re Derfshaw Ltd [2011] EWHC 1565 (Ch)

This concerned a failure to give notice of intention to appoint to the company. Whilst expressing concern about court's jurisdiction to do so, Morgan J made a retrospective order following G-Tech.

Re Frontsouth (Witham) Limited [2011] EWHC 1668 (Ch)

This was an application to extend an administration order. There had been a previous extension, but this was defective because consent was not obtained from one secured creditor. This meant a further extension could not be granted as the administration had already expired. Henderson J considered that **r7.55 IR 1986** did not apply i.e, because there were no insolvency proceedings as a result the decision was to grant an administration order back-dated 364 days.

Care Matters Partnership Limited [2011] EWHC 2543 (Ch)

This was a failure to give notice to the company of intention to appoint an administrator. The case proceeded on the basis that the appointment was invalid and as the administration had effectively run its course the conditions for the making of a further administration order whether retrospective or otherwise were no longer present and therefore it could not be made.

Adjei v Law for All [2011] EWHC 2672 (Ch)

The defects were a failure to notify a qualifying floating charge holder (QFC) of intention to appoint and errors in the notice of intention to appoint concerning insurance undertakings and EU regulation. The errors in filling in the form were capable of remedy under **r7.55 IR 1986**. The failure to give notice to the charge holder was more fundamental and the appointment was therefore invalid. A retrospective order was made with "some misgivings".

re Bezier Acquisitions Limited [2011] EWHC 3299 (Ch),

In this case the serving of notice of intention to appoint on solicitors was held to be valid. Had it been found to have been a defect then applying the Soneji Approach the Judge would have held that it was a defect that did not result in the invalidity of the appointment.

re Virtualpurple Professional Services Ltd [2011] EWHC 3487 (Ch)

The issue was whether notice of intention to appoint had to be given to the company in circumstances where there was no requirement to give notice to any QFC. This point has now been resolved by amendment to **Sch B1 para 26** by the **Deregulation Act 2015**. Norris J held that the failure to give notice was capable of cure under **r7.55 IR 1986**. He applied the Soneji Approach and that the breach of the rules would not have invalidated the appointment and as such there was no automatic invalidity.

Previously there had been an issue with the serving of notice of intention to appoint under **Para 26(1) Sch B1 IR1986. Para 26(2)** required notice of intention to appoint to be served on prescribed persons. These included parties who had distrained over the company's assets and more importantly the company itself. There was some ambiguity as to whether or not notice had to be served on prescribed persons and the company where there was no QFC or person entitled to appoint an administrative receiver as referred to in **sub-section (1)**. This ambiguity was removed with the amendment brought into **para 26(2)** by the **Deregulation Act 2015** with effect from 01 October 2015. The effect of the amendment was that there was no longer a requirement to give notice to prescribed persons (including the company) where there was no QFC or person entitled to appoint an administrative receiver. Where there is a QFC then notice of intention to appoint must be served on that charge holder (QFC) and notice of intention to appoint must be served on the prescribed persons including the company itself. The position now is that the company or the directors may where there is no QFC make an appointment out of court without giving notice of intention to appoint to anyone or being required to file such a notice in the court. It should be noted that there is no interim moratorium in such circumstances.

National Westminster Bank plc v Msaada Group [2011] EWHC 3423 (Ch)

The defect was in relation to an appointment of an administrator over a partnership and a failure to serve one of the prescribed persons with notice of intention to appoint following Minmar. The failure resulted in the invalidity of the appointment. However, a prospective administration order was made.

Re MF Global Overseas Finance Limited [2012] EWHC 1091 (Ch)

This case concerned the question of what form of prescribed notice should be served at the time of appointment. This would depend on whether notice of intention to appoint had to be served on persons under **para 26(2) Sch B1** even if there was no one on whom noticed had to be served under **para 26(1)**. Being over-cautious the appointors had served a notice of intention to appoint. They subsequently served a notice of appointment based on the service of the notice of intention to appoint. However, if no notice of intention to appoint was required to be served then a different form of notice of appointment (where no notice of intention had been served previously), should have been used.

Mann J interpreted the rules as permitting what had happened on the facts of this case.

Re Ceart Risk Services Limited, (judgment on 3 May 2012)

This case concerned the failure to obtain consent from the regulator under **FSMA 2000**. The Judge applied the Soneji Approach and considered that the flaw was not so fundamental as to invalidate the appointment but that the appointment only took effect when the consent was actually filed. As to the actions of the administrators between the date of filing of the original purported appointment to the date of the filing of the consent, the Judge took the view that they would be validated by **para 104 Sch B1**.

Re Eco Link Resources Ltd [2012] B.C.C. 731

The appointment of an administrator by a QFC was defective insofar as there was a failure to give notice to a prior charge holder. In this case the defect rendered the appointment invalid.

re Assured Logistics Solutions Limited [2011] EWHC 3029 (Ch)

The question concerned the validity of an appointment where there was no charge holder falling within **para 26(1)** to whom notice had to be given but notice had not been given to the company as apparently required by **para 26(2) Sch B1**. (*this has now been remedied*).

In this case it was decided that even if notice had to be given the failure was not so fundamental as to make the appointment a nullity. It was therefore valid and if necessary, resort could be had to **r7.55 IR 1986**.

re BXL Services Limited [2012] B.C.C. 1877 (Ch)

This involved another case of failure to give notice of intention to appoint to prescribed persons under **para 26(2)** where there was no person to whom notice had to be given under **para 26(1)**. Again, it was concluded that even if there was a requirement to give notice, failure to do so would not result in an invalid appointment. The answer was to apply the Soneji Approach.

re Euromaster Limited [2012] EWHC 2356 (Ch)

The defect was that the administrators had purportedly been appointed 11 business days after the filing a notice of intention to appoint. The appointment was therefore outside the 10 day period. Again the Soneji Approach was applied and it was held that Parliament's intention was not to make non-compliance an automatic nullity. As such the appointment would be treated as valid.

Re Care People Limited [2013] EWHC 1734 (Ch)

The question here was whether the appointment was valid where it was said that the QFC had allowed insufficient time for payment after having made a demand. The time allowed for payment before the appointment was 6 minutes. The question was whether the appointment was invalid because at the relevant time the charge was not enforceable under **para 16 Sch B1** due to the insufficient time to repay. Whilst there was a defect in the exercise of the undoubted power of appointment, it was not of such fundamental importance so as to render the appointment a nullity. It was therefore held that the starting point was that the appointment was valid but the question was whether or not to invalidate it under **r7.55 IR 1986**. As there was no substantial injustice the court refused to set the appointment aside under **r7.55**.

re Eiffel Steelworks Ltd [2015] EWHC 511 (Ch)

The potential defect was that notice had not been given of intention to appoint to the company itself in a directors' appointment. It was held that the defect was an irregularity which was validated and not invalidated under **r7.55 IR 1986**.

Re Synergi Partners Limited [2015] EWHC 964 (Ch)

This was an application for a retrospective administration order where a valid administration had expired some time before. The company had purportedly been placed into voluntary liquidation with the former administrators acting as liquidators. Although retrospective orders were considered they were of no assistance and as such the Judge made a winding up order to enable wrongful trading proceedings to be brought.

Re Melodious Corporation [2015] EWHC 621 (Ch)

The appointment by directors of an administrator was held to be invalid because the meeting was inquorate. **R7.55 IR 1986** did not rescue the position.

Re Elgin Legal Limited [2016] EWHC 2523 (Ch)

This case concerned a failure to obtain an extension of the administrators appointment. The court refused to make a retrospective administration order but made a prospective one instead.

Petit v Bradford Bulls (Northern) Limited [2016] EWHC 3557 (Ch)

The application was for a declaration as to the validity of appointment or alternatively a retrospective administration order. Mann J said:

> "*Yet again the almost infinite number of ways in which the appointment of administrators can go wrong and require proceedings in the court in order to try and fix the problem*".

The appointment was by charge holders. The defects were that a charge had not been executed as a deed and secondly, that there was no "*event of default*". The Judge ordered that an administration order should be made with retrospective effect.

Re Spaces London Bridge Limited [2018] EWHC 3099 (Ch)

This concerned the requirement in **r3.24 IR 2016** that the notice of appointment filed with the court must specify the date and time of the appointment. In that case it was held that there was no breach of statutory provisions and the appointment was valid and that it would not have held that the appointment was invalid under **r12.64**.

re HMV Ecommerce Ltd [2019] EWHC 903 (Ch)

The question was the validity of an out of court appointment by directors which was made outside court opening hours. The defect did not affect the validity of the appointment and that any defect was waived as far as necessary under **r12.64**.

Re SJ Henderson & Co Ltd [2019] EWHC 2742 (Ch)

This concerned an out of court appointment by directors filed electronically through the CE filing system outside court hours. The Judge concluded that that this was not permitted in the case of either a director or company appointment. The defect was a fundamental breach and the filing was a nullity. Instead it would be treated as a filing at the time the court formally opened for business.

Re Skeggs Beef Limited [2019] EWHC 2607 (Ch)

This was an out of court notice of appointment by a qualified floating charge holder and whether it could validly be effected out of hours by filing the notice of appointment electronically using the CE Filing system. The court noted that **IR 2016** set out a procedure for out of hours appointments by qualified floating charge holders which had not been followed. In this case it was held that the defect or irregularity was not fundamental and as there was no substantial injustice it would be validated by **r12.64 IR 2016**. The Judge made a declaration that the appointment took effect from the time of the actual filing out of hours.

Keyworker Homes (North West) Limited Judgment 11 November 2019

The issue concerned the question of out of court appointments by directors the filing having been made through the CE Filing system. He considered there was no irregularity and that if there was it would be validated under **r12.64**. In this case however it was held that the appointments were valid because they were in accordance with the requirements of the rules and PDs in question.

Causer v All Star Leisure (Group) Limited

Again, the question was the validity of electronic filing of notices of appointment through the CE Filing system when the courts are closed. The appointment was by a qualifying charge holder and whilst there was an irregularity, it was held that it was curable under **r12.64 IR 2016**.

Decision

The failure to obtain the consent of the FCA meant that the purported appointment was a nullity which could only be cured by retrospective appointment. **R12.64** did not apply and a retrospective order was made. Finally, the obtaining of the FCA's written consent is required and must be obtained and lodged at the latest by the filing of the notice of appointment.

Comment

- Apart from highlighting the need to obtain FCA written consent before any appointment is made and that this must be filed at the very latest with the court on the filing of notice of appointment, the case also looks at the myriad of defects that can arise in relation to an administrator's appointment and identifies the approach that should be adopted by the courts in determining how to remedy, if possible, the defect in question.

- This case highlights the need to ensure that when searching at the FCA register to search as many permutations of the company name as possible.

- During this case a letter was received from the FCA in which they suggested that searching by company number would avoid situations as occurred in this case.

Administration

Dearing v Skelton [2020] EWHC 1370 (Ch)

Administrators refusal to allow directors to exercise powers during administration

Facts

The company in question was ASA Resource Group Plc ("the Company"), a holding company which provided treasury and management functions to various mining subsidiaries. The company had become insolvent and administrators were appointed on 01 August 2017. The administrators proposals were approved by creditors with three purposes:

1. To rescue the company as a going concern;
2. To achieve a better result for the company's creditors as a whole than would be likely if the company were to be wound up; and
3. To realise property in order to make a distribution to one or more secured or preferential creditors.

The aim was to achieve the first or second objectives through a sale of subsidiary shares. This resulted in an excess of £23.1m being realised to pay creditors in full with statutory interest. This only depended upon proofs being received, determined and payment being made. The company would then be returned back to the directors as a going concern.

On 20 March 2020 an order was made permitting the administrators to make the distribution to creditors. Notice of intention to declare a dividend had been put in the Gazette on 03 April 2020 and it was anticipated that the whole process would be completed within two months from 13 May 2020. Following this the company would be returned to the control of Mr. Dearing the sole director and applicant in this case.

Mr. Dearing is a member and creditor of the Company. Anticipating the hand-over of the Company as a going concern to the director following completion of the administration, Mr. Dearing sought consent from the administrators to take various steps in preparation. He wanted to appoint a further three directors, open a bank account, rectify the share register, take out indemnity insurance and manage the Company's assets to the extent the administrators are not able or willing to do so. This could include the new directors taking steps to recover a debt of approx. £5m owed to the Company.

The administrators refused to grant consent to the director for the preparatory steps to be taken. As a result, Mr. Dearing applied **Paragraph 74(1) of Schedule B1 to the Insolvency Act 1986** for a direction that the administrators should agree to the actions that Mr. Dearing proposed to take as the director.

Paragraph 74(1) provides:

> A creditor or member of a company in administration may apply to the court claiming that –
>
> (a) The administrator is acting or has acted so as unfairly to harm the interests of the applicant (whether alone or in common with some or all other members or creditors), or ……

Paragraph 74 required Mr. Dearing to establish on the balance of probability that the administrators had acted unfairly to harm his interests as a creditor or member (whether alone or in common with others), and to satisfy the court that relief ought to be granted.

The administrators refusal to grant consent was on the basis:

(i) That the steps did not appear necessary to achieve the purpose of the administration;

(ii) The steps will involve expenditure or give rise to liabilities which could prejudice shareholders and potentially creditors;

(iii) The steps were not adequately explained;

(iv) Where detailed, the steps appeared to fall outside the administrators remit;

(v) There is no urgency as the administrators were about to make a final distribution and their appointment will cease thereafter.

It was also noted that there were disputes as to who owned the Company share capital and the majority shareholder objected to the new directors proposed by Mr. Dearing.

In particular the administrators were concerned that the consent would impact on the surplus available to the Company upon cessation of their appointment.

The role of the administrators is to act to achieve one or more of the purposes prescribed by **Para 3(1) Sch.B1**. In doing so they must act in the interests of all of the creditors. Whilst directors may remain in office no officer of the company may exercise management power without the consent of the administrator (**Para 64**). The administrators are responsible for the management of the company while the directors remain in office. The administrators may decide at any stage to involve a director(s) and permit the director(s) to exercise management powers. This can be for any number of reasons which may include their expertise, reliability or for the reduction of costs and expenses.

The questions arising out of the application were:

(i) Whether the powers Mr. Dearing proposes to exercise either in his own right or with the board of the newly appointed directors are prohibited without the administrators consent Para 64(1); and

(ii) If so, whether the administrators by refusing their consent have acted unfairly and harmed his interests (whether alone or in common with some or all other members or creditors).

Decision

In considering Mr. Dearing's request the administrators had not rejected it solely on the basis that there only remained the requirement to deal with proofs of debt and distribute funds. On the contrary, they had considered Mr. Dearing's request in the light of their responsibility for the management of the Company. Their decision in relation to consent must be in accordance with the approved proposals and the purposes of the administration, and must bear in mind the duty to act in the interests of all creditors.

There was insufficient detail to establish whether or not on the balance of probability the steps were required to be taken to protect the Company's interests and value. There was no evidence that steps needed to be taken before the end of the administration to recover the £4.9m debt.

It was also unclear as to what steps the new directors would take, the costs and risks involved, and what effect it would have on the purpose of the administration and the fulfilment of the proposals.

A particular concern was the fact that the share register may need rectification.

Whilst the opening of a bank account, the purchasing of indemnity insurance and obtaining legal advice all appeared sensible, there were unknown costs ramifications, particularly with regard to the indemnity.

Caution was also required in view of the wishes of the majority shareholder Rich Pro Investments Limited.

ICCJ Jones held that relief would not be granted, and that control will be returned effectively to the director following the conclusion of the administration. Further rescuing a company as a going concern does not simply mean payment of its creditors. It must include leaving the company in a rescued going concern position.

Comment

- The case had been heard in the urgent list and therefore no other shareholders were joined in or attended the hearing. Because the evidence was not fully tested, the court noted the need for caution in considering such applications.

- Following **Re System Building Group Limited (In Liquidation) [2020] EWHC 54 (Ch)**, whilst the statutory and common law duties of directors continue, as was held in that case, the application of those duties were restricted in practice by the statutory prohibition.

- This case highlights the fact that the management and supervision of the company in administration is the remit of the administrators. Whilst the administrators may delegate or consent to certain powers being exercised by the directors, this is a matter for the administrators to decide and determine. With the administrators agreement such powers can be granted to the directors and are a significant feature of so called "light touch" administrations.

Administration

Re Debenhams Retail Limited (In Administration) [2020] EWCA Civ 600

Adoption of employment contracts in administration

Facts

Debenhams Retail Limited ("the Company") had 15,550 employees. Following lockdown as a result of COVID-19 the Company closed its doors on 25 March 2020 and wrote to approx. 13,000 employees informing them that they were being placed on furlough under the Government's Coronavirus Job Retention Scheme ("the Scheme").

On 09 April 2020 the administrators were appointed to the Company by the directors. The purpose of the administration was the rescue of the Company as a going concern. The administrators sought the consent of employees who had been furloughed asking them to give consent to them being furloughed and to a variation in their contracts of employment to accept the reduced payment under the furlough Scheme. Some 12,700 employees responded indicating their agreement. The administrators sought directions of the court under **Para 63 of Schedule B1** seeking a declaration as to whether by participating in the Government Scheme they would be adopting the contracts of the furloughed employees.

Decision first instance

Trower J declined to make the declaration sought by the administrators and held that it was likely that they would be found to have adopted the contracts of employment of the furloughed employees. The order being made under **Para 99(5) of Schedule B1** of the **Act**. However, the order was not in final terms that the contracts of employment would be adopted.

In reaching his decision the Judge followed the decision in **Re Carluccio's Limited (In Administration) [2020] EWHC 886 (Ch)** (Carluccio's). In that case the company went into administration and the objective of the administration was a sale of the business with a view to a better realisation than in liquidation. The administrators wrote to all employees who were proposed to be furloughed offering to retain them on varied terms in effect restricting their wages to the amount received under the Scheme. Of the 2,000 odd employees the vast majority accepted the varied terms as consenting employees. Mr. Justice Snowden considered that when the administrators made an application under the Scheme or made payment to the employees that would amount to adoption of their varied contracts. This would enable a super-priority payment to be made to furloughed employees once the grant monies were received. With regard to the non-responding employees if nothing else happened then the administrators would not have adopted their contracts by the mere failure to terminate them prior to the expiry of the 14 day period. The employees would continue to be employed but would have an unsecured claim only.

The courts considered the terms of the Government Scheme and noted that the furloughed employees remained the employees of their employer and as administrators they could access the Scheme if the purpose of the administration was a sale of the business as a going concern.

On the question of adoption **Para 99 Schedule B1** contains provisions which provide that where a contract of employment is adopted by the administrator any liabilities arising out of it shall be paid in priority to remuneration and expenses of the administrators. No action taken within the period of 14 days after appointment shall be taken to be adoption of the contracts.

It was noted that **Para 99** applies where a person ceases to be an administrator. The super-priority of any adopted contracts of employment means that the sums due will rank ahead of the administrator's remuneration and expenses any amount secured by a floating charge and ordinary unsecured liabilities. This applies to wages or salary which includes holiday and sick pay. It was noted that it does not include redundancy payments and payments for unfair dismissal (see **Allders Department Stores Ltd [2005] EWHC 172 (Ch)**) and does not apply to protective awards or payments in lieu of notice (see **Re Huddersfield Fine Worsteds Ltd [2005] EWCA Civ 1072**).

Because of the terms agreed with the vast majority of employees' wages or salary in excess of the amounts payable under the Scheme would not enjoy super-priority because of the agreed varied terms. It was noted that it may be the case that entitlement to full holiday pay may enjoy super-priority.

The meaning of "adoption" was considered and in particular the decision of the House of Lords in **Powdrill v Watson, Re Paramount Airways Ltd [1995] 2 AC 394** (Paramount). In that case employees had continued to perform services and be remunerated after the expiry of 14 days from the appointment. It was contended that the contracts of employment had not been adopted because letters had been sent to employees in a standard form stating that they were not adopting contracts of employment or assuming any personal liability for any sums that might fall due under them (personal liability arising out of their role as an administrative receiver).

In that case Lord Browne-Wilkinson first of all confirmed that by doing nothing an office holder does not adopt an employment contract neither is it necessary to avoid adoption for the office holder to give notice of termination before the expiry of 14 days after appointment or at all.

As to whether or not contracts of employment were adopted David Richards LJ in Debenhams reviewed the Paramount test. He concluded that:

> "*It is a question of law: is the conduct of the administrator such that he must be taken to have to accept that the relevant amounts falling due under the employment contract enjoy super-priority? It is a wholly objective question, focussed entirely on the conduct of the administrator*."

The issue was therefore whether the administrators have continued the employment of the furloughed employees. The Court took into account various factors including the fact that the administrators will continue to pay wages or salaries up to the limits provided by the Scheme. The furloughed employees who accepted the variation have continued their employment on those terms and in paying the furloughed employees the administrators are acting with the objective of rescuing the Company as a going concern.

Decision – Court of Appeal

Taking into account the above factors, the Court concluded that the administrators had clearly adopted the contracts of the furloughed employees.

The administrators reliance on **Para 66** of **Schedule B1** as statutory authority for the making of those payments was recognised as perhaps the most obvious source of authority for the payments distinguishing it from **Para 99** which only operates where a person ceases to be the administrator. It was noted that in Debenhams as it was in Carluccio's the administrators had been able to agree terms with the vast majority of employees so that it was only in respect of 20% of holiday pay that super-priority may arguably arise.

It was noted that whilst there may be good reasons of policy for excluding action restricted to implementation of the Scheme from the scope of "adoption" under **Para 99,** such exclusion cannot be accommodated under the law as it stands.

Comment

- In Debenhams and Carluccio's the administrators were able to communicate effectively with employees and obtain their express agreement to the variation of their terms of employment. The very high percentage of employees agreeing to vary their contracts of employment in the face of the COVID-19 pandemic assisted the administrators in their task of dealing with the matter.

Administration

Ezair v Conn Re Charlotte Street Properties Limited (In Administration) [2020] EWCA Civ 687

Administrators' attempted use of Section 234 IA1986 to recover properties

Facts

This was an Appeal from an earlier decision on an application made by administrators under **s234(2)** of the **Insolvency Act 1986 ("IA1986")** to require Mr. Ezair to transfer title to six properties to the administrators. That application was successful, and it is against that decision that Mr. Ezair appealed.

The appeal concerned six properties registered in the name of Mr. Ezair. Originally he operated as a sole trader but in 1999 incorporated the business under the name of Northern Estates Limited ("NEL"). Under an agreement referred to as "the 1999 Agreement" Mr. Ezair agreed to sell the properties to NEL in return for the allotment of 98 shares. Completion of the contract did not however take place. This was to avoid payment of stamp duty on the transfers of title.

Charlotte Street Properties Limited ("CSP") was incorporated. Under the "2003 Agreement" NEL entered a contract with CSP to sell the properties to it for £1.3m. The purchase price was financed by an £800,000 loan from Northern Rock, and an inter-company loan from NEL. Subsequently, the properties were shown as assets in the accounts of CSP together with the loans. CSP failed to service the loan and receivers were appointed over the properties. Mr. Ezair reached an agreement with the receivers to release the security over the properties in return for payment of the sum of £903,000. This was achieved by raising a loan of £800,000 to Mr. Ezair from Barclays Bank which was secured over the properties, together with the proceeds of sale of two other properties.

On 12 November 2015 NEL was subject to a winding up order and on 16 October 2017 CSP went into administration. The administrators then made an application under **s234 IA1986** requiring Mr. Ezair to deliver executed TR1 transfer forms in respect of the properties.

First instance

HH Judge Halliwell found that Mr. Ezair held the properties on a bare trust for CSP pursuant to the 1999 Agreement and that as such he was under an obligation to transfer the Properties to CSP and made an order under **s234** to that effect.

Appeal

On appeal further details of the dispute concerning the properties became apparent. In particular Mr. Ezair claimed that he had re-acquired a beneficial interest in addition to the legal interest which he held in the properties.

Arguments centred on the original 1999 Agreement which remained uncompleted. In order to trigger completion, notice was required to be served under clause 6.2. At the hearing of the administrators' application at first instance no notice had been served under that provision. It was also argued that CSP did not have entitlement to serve notice under 6.2 as it was not a party to the 1999 Agreement and had not taken a legal assignment of the benefit of it. After the decision of HH Judge Halliwell the administrators subsequently took a legal assignment of the benefit of the 1999 Agreement in favour of CSP and served notice under the 1999 Agreement under clause 6.2.

Section 234 IA1986

S234(2) gives the court a wide power to direct the transfer to the office holder of any property, books or records to which the company "appears to be entitled". However, **s234** is not intended to provide a definitive ruling about title. **S234** is a summary procedure and it is not an appropriate procedure for determining complex issues of title. It was noted that the administrators had chosen not to pursue their contractual remedies by serving the requisite notices and seeking an order for specific performance. Instead, they opted for the shorter route of using **s234**.

In reviewing the earlier decision Patten LJ considered that the conclusions of the Judge in the earlier hearing were wrong concerning constructive trusts and the benefit of the 1999 Agreement. He identified the administrators' rights as being contractual only.

Decision

Having identified that the administrators' rights in respect of the properties were solely based in contract, Patten LJ considered whether the earlier order should still stand after taking into account the fact that the administrators did not serve the contractual notices until after the earlier decision had been made.

Whilst it was noted that there are cases where it is possible to take into account events that occur after a judgment has been given, in the circumstances of the current case there would be a risk of injustice if the administrators were allowed to rely on the later assignment and notice served by them. As such the appeal was allowed, and the administrators would have to commence new proceedings based on the subsequent assignment and notice, in which Mr. Ezair can then raise any defence that he seeks.

Comment

- This case effectively narrows the scope of **s234IA1986**. Where there is a dispute as to title to property, then **s234** is not going to provide an easy shortcut for recovery.

- One of the disadvantages of an application under **s234** is that there are no pleadings. It can therefore be more difficult to determine the extent and nature of any defence, in particular concerning title to property, until the application has reached an advanced stage, or even been determined.

Administration

Secure Mortgage Corporation Limited v Harold [2020] EWHC 1364 (Ch)

Invalid appointment of administrators

Facts

The administrator was appointed in respect of Secure Mortgage Corporation Limited ("SMC") under a floating charge. SMC sought to challenge the appointment on two grounds:

(a) That the floating charge was not enforceable on the date of the appointment and

(b) Procedural requirements of **Schedule B1** to the **Insolvency Act 1986** were not complied with.

The administrator was appointed by a Mr. Tierney and Mr. Bamber who purported to make the appointment in their capacity as personal representatives of the estate of the late Mr. Peter Nolan ("Mr Nolan").

Previously, SMC had granted a mortgage debenture dated 12 May 1998 to Lancashire Mortgage Corporation Limited ("LMC").

On 14 September1999 SMC was struck off the Register of Companies and then dissolved. Despite the fact that SMC's title to the property vested bona vacantia it remained the holder of the registered title.

On 17 October 2007 Intermedio Financial SA ("Intermedio") became registered as the proprietor of the charge in the place of LMC.

On 01 May 2015 Intermedio was struck off the list of companies however the 1998 charge remained registered in Intermedio's name.

On 07 November 2019 the charge registered in the name of Intermedio's was marked as satisfied at Companies House.

15 August 2018 Mr. Nolan died. Whilst no grant of representation had been taken out, Messrs Tierney and Bamber contended that they were appointed personal representatives under Mr. Nolan's will.

On 29 June 2019 SMC was restored to the Register of Companies. Solicitors acting for the estate of Mr. Nolan expressed concern to HM Land Registry on the grounds that Mr. Nolan had been in possession of the property for 20 years. Their argument was SMC was restored to the Register of Companies as a device to enable a Mr. Henesy to obtain possession of the property. By letter dated 23 July 2019 solicitors for Mr. Nolan's estate demanded repayment allegedly due under the 1998 charge.

Mr. Henesy was the sole director of another company called HCC who advanced monies to SMC the result of which a debenture was entered into creating security in favour of HCC.

On 30 August 2019 Mr. Harold was purportedly appointed administrator of SMC. In the Notice of Appointment, the Appointor was named as "The Estate of the Late Mr. Peter Nolan care of Bishop & Co". It further recorded the fact that the "the Estate" was itself the holder of the qualifying floating charge which was now enforceable.

In the administrator's report he quantified the debt due to Mr. Nolan's estate at £2,317,091 against a value for the property of £500,000. The purpose of the administration was to realise the company's property in order to make a distribution to its secured or preferential creditors. Solicitors for SMC sought copies of assignments of LMC charge detailing how it had become vested in Mr. Nolan's estate. No copies were provided.

Decision

It was noted that Messrs. Tierney and Bamber were unable to prove their title as personal representatives. In order to prove their title before a court of law they must produce a Grant of Representation which they had not done so.

To enable an appointment to be made the floating charge must be enforceable as required by **Para 16** of **Schedule B1**. On the question of enforceability in **Para 16** reference was made to **SAW (SW) 2010 Ltd v Wilson [2018] Ch 213**, in which it was concluded that a floating charge was enforceable regardless of whether there were assets against which the floating charge could be enforced. In that case Briggs LJ further observed that:

> *"a floating charge is…enforceable if any condition precedent to enforcement has been satisfied (such as an event of default) and there remains a debt for which the floating charge stands as security".*

On this point HHJ Halliwell said that he was satisfied the floating charge would generally be enforceable if the criteria detailed by Briggs LJ are satisfied.

On the procedural requirement the notice of appointment did not comply with **Para 18** insofar as it failed to identify the person who made the appointment or state who is the person who is the holder of the qualifying charge. Reference to the term "estate" was not a reference to a person.

Rule 3.17(1)(b) of the **2016 Rules** requires the notice to provide the name and address of the appointor. Again the notice did not do so. Following **Para 19** of **Schedule B1** the appointment will not take effect until the requirements are satisfied. As such the appointment was found to be void.

Secure Mortgage Corporation Limited v Harold [2020] EWHC 1780 (Ch)

Decision

At a further hearing of this case, the court considered the terms of the draft order to be made. Having made an order that the administrator's appointment was void and of no effect it became apparent that the administrator had continued to hold himself out as the administrator of the company post order.

For the administrator it was argued that there was an outstanding appeal and some confusion as to when the order came into effect.

In relation to the consequential provisions for the giving up of the books and records, the matter was further adjourned to enable the administrator to file further evidence in response.

On the question of costs, the applicants sought an order for indemnity costs against the former administrators. It was noted that indemnity costs would only be awarded as opposed to standard costs where the conduct of the parties or the circumstances of the case take the case "out of the norm". On this point it was held that the administrator's conduct had been out of the norm and as such indemnity costs were awarded.

The reason for the order for indemnity costs was that the parties in litigation are expected to cooperate freely in the exchange of relevant information prior to the issue of proceedings. This is a requirement of the overriding objective and the Practice Direction for Pre-Action Conduct and Protocols. The administrator's refusal to provide details of all documents in relation to his appointment meant that his conduct was out of the norm and costs would be assessed on an indemnity basis. The applicants filed a statement of costs for £83,933.50 plus VAT. The VAT element is only recoverable from the respondents if the applicants are not registered for VAT and thus not entitled to input tax credit. On the assumption that the applicants are not registered for VAT the court ordered that an interim payment in the sum of £75,492.30 was payable within 28 days.

Comment

- This case provides some further clarity as to when a qualifying floating charge is enforceable for the purposes of **Para 16**.
- A failure to identify parties correctly in the notice of appointment will render any purported appointment invalid in such circumstances.

Bankruptcy

Brake v Swift [2020] EWHC 1810 (Ch)

Bankrupt's claim to revest cottage and land under section 283A of the Insolvency Act 1986

Facts

This was an application by bankrupt husband and wife Mr. and Mrs. Brake to revest West Axnoller Cottage ("the Cottage") and two small parcels of land in them under **s283A** of the **Insolvency Act 1986 (IA1986)**.

The background to the case is complex and has been the subject of much litigation. Mrs. Brake originally acquired West Axnoller Farm ("the Farm") in September 2004. On the Farm was a substantial dwelling known as Axnoller House ("the House"). By 2006 Mrs. Brake was operating a holiday letting business at the Farm. The Cottage was on the other side of a private lane leading to the Farm.

The Cottage had been purchased by a Mr. and Mrs. White in July 2002. In 2006 Mrs. Brake bought two small parcels of land either side of the Cottage. In 2006 Mrs. Brake borrowed money from bankers Adam & Co secured by a first legal charge over the Farm. The financial crisis of 2008 meant that further funding had to be obtained from an outside investor. In 2010 Mr. and Mrs. Brake entered into a partnership with a Mrs. Brehme. The partnership operated a business known as "Stay in Style" which provided luxurious weekend breaks and hosted weddings. Mr. and Mrs. Brake contributed the Farm as partnership property and Mrs. Brehme contributed capital funding.

On 08 March 2010 the partnership acquired the Cottage which was transferred to Mr. and Mrs. Brake and Mrs. Brehme jointly. The Cottage had been occupied by a Housekeeper for a period of time but was also occupied by Mr. and Mrs. Brake when the House was let, or being used for an event. There was a dispute in the partnership which led to arbitration in 2013. The award by the arbitrator was made in favour of Mrs. Brehme and it was ordered that the partnership be dissolved. Following further litigation and costs orders Mr. and Mrs. Brake were made bankrupt on 12 May 2015. The partnership itself went into administration and then latterly into liquidation.

Adam & Co the bank that originally leant money to Mrs. Brake as security against the Farm appointed LPA receivers who subsequently sold the Farm in July 2015 to Sarafina Properties Limited ("Sarafina"). The Cottage and the two parcels of land were not included in the sale as they were not subject to the bank's charge. Subsequently, Sarafina was sold to Chedington who continued to employ Mrs. Brake to run the weddings and rental accommodation business. Post bankruptcy, Chedington bought the two parcels of land adjacent to the Cottage from the trustee in bankruptcy. The trustee in bankruptcy also entered into a transaction with the liquidators of the partnership in relation to the Cottage to acquire the liquidators' rights in it. Chedington then, in a back to back transaction with the trustee, acquired those rights. Chedington subsequently took possession of the Cottage.

Mr. and Mrs. Brake commenced proceedings against the liquidators of the partnership and the trustee in bankruptcy to unwind the various transactions in particular in relation to the Cottage and the two parcels of land. The Brakes further sought to have the Cottage and land revested in them under **s283A IA1986** on the grounds that the Cottage and the land was their sole or principal residence as at the date of the bankruptcy and that as the trustee had taken no steps to realise them in the three years post bankruptcy, the Cottage and the land should revest in Mr. and Mrs. Brake.

There were three sub-issues:

(1) whether the Brakes as yet unvindicated claim in proprietary estoppel to the Cottage as against the liquidators was an interest in a dwelling-house within **s283A**

(2) whether the adjacent parcels of land fell within the definition of a dwelling-house

(3) whether the Cottage and the adjacent parcels were the Brakes' sole or principal residence at the date of bankruptcy

On entering into the partnership with Mrs. Brehme it was agreed that renovations would take place at the Cottage and that it would be somewhere for them to live whilst the House was being renovated and let. In 2007 Mr. and Mrs. Brake decided that the Cottage was uninhabitable and stated that they did not want to live there. Mr. and Mrs. Brake later contended that they lived in both the Cottage and House between 2010 and 2015 and that in 2015 that the House was their main residence until 2015 when they lived in the Cottage and elected for it to be their principal residence. By the end of 2016 they had moved back into the House.

The bankruptcy order was made on 12 May 2015. That week between 08 and 15 May the House was occupied by guests and Mr. and Brake were living at the Cottage. In their preliminary information questionnaire submitted to the Official Receiver they gave their address as West Axnoller Cottage West Axnoller Farm. On the question concerning freehold land and property they replied, "*Cottage held in trust for partnership one third West Axnoller Cottage*". The trustee did not accept those answers as true as far as they suggested that the applicants lived at the Cottage rather than the House. The trustee having formed the view from other documents that they lived at the House and not the Cottage. In an email to the trustee Mrs. Brake stated, "*that West Axnoller Cottage was our principal residence when the bankruptcy order was made*".

At trial, the documentary evidence tended to show a different picture with electricity bills addressed to the Brakes at West Axnoller Farm for the Cottage supply. Other documents including correspondence also indicated that the Brakes lived at the Farm/House and not the Cottage. Mr. and Mrs. Brake also relied on witnesses who claimed that they visited them at the Cottage on many occasions. The trustee had himself visited the property unannounced on 23 December 2015. Having driven up the long driveway he observed the House "*lit up like a Christmas tree*" whereas the Cottage had no lights on at all.

Mr. and Mrs. Brake sought to rely on **s283A IA1986** which provides as follows:

"(1) This section applies where property comprised in the bankrupt's estate consists of an interest in a dwelling-house which at the date of the bankruptcy was the sole or principal residence of—

(a) the bankrupt,

(b) the bankrupt's spouse [or civil partner], or

(c) a former spouse [or former civil partner] of the bankrupt.

(2) At the end of the period of three years beginning with the date of the bankruptcy the interest mentioned in subsection (1) shall—

(a) cease to be comprised in the bankrupt's estate, and

(b) vest in the bankrupt (without conveyance, assignment or transfer).

It was noted that **s283**A is limited to property which is "comprised in the bankruptcy estate". If the property is not comprised in the bankrupt's estate under that section it cannot revest in the bankrupt.

The interest issue

Mr. and Mrs. Brake claimed that at a meeting held in October 2011 between the partners and Mrs. Brehme, it was agreed that the Cottage would be transferred to them and that they would become the owners in equity of the Cottage or alternatively entitled to a beneficial interest in it. They further claimed that they had acted in reliance on the agreement by applying for a mortgage, paying for a valuation, moving their possessions into a room in the House, and preparing the Cottage. Mr. and Mrs. Brake sought specific performance of the alleged Cottage agreement.

The applicants argued that because the legal estate was held by Mr. and Mrs. Brake and Mrs. Brehme pursuant to the partnership, that was an "interest" for the purpose of **s283A**. The court noted however that the legal estate did not vest in the bankruptcy estate and therefore cannot be "comprised in the bankruptcy estate" for the purpose of **s283A** and therefore will not revest.

It was also argued that the beneficial interest of a partner in a partnership was an interest within the meaning of **s283A**. On this point it was noted that an interest in a partnership is of a nature that it does not give a partner any entitlement to acquire a share of the Cottage to be vested in them individually. Once an asset such as the Cottage became a partnership asset it is subject to the interests of creditors which must be paid before any distribution of profits or return of capital to the partners following dissolution. As an individual partner is not entitled to any specific asset or share neither can his or her trustee be so entitled. In effect the nature of a share in a partnership is an interest in an amount of cash or net proceeds of sale. Whilst the Brakes share in the partnership did fall into the bankruptcy estate as the partnership was insolvent, those interests were worthless. As such **s283A** had no application.

Proprietary estoppel

Mr. and Mrs. Brake further claimed that they had acquired an interest in the Cottage by way of an equity arising by proprietary estoppel.

Proprietary estoppel instead of looking forward looks back and asks whether in the circumstances that have actually happened it would be unconscionable for the promise not to be kept. This is what Mr. and Mrs. Brake were seeking in relation to the alleged oral agreement with Mrs. Brehme to transfer the Cottage to them. The court further noted there are two main kinds of proprietary estoppel.

The first arises when a person makes a statement (intending it to be relied upon) as to the current legal position, such as "I do not own this land" or "you own this land". The person to whom this statement is made in fact relies upon it to his or her detriment. If it is unconscionable for the representor to go back on the representation a promissory [proprietary] estoppel equity arises.

The other kind of proprietary estoppel is where there is no statement made about the present legal position but a promise is made or an expectation created as to the future position. It is not a contract enforceable at law, because there is no consideration. The promise is not enforceable at that point. But if the promise, being intended to be acted upon by the promisee, is so acted upon by the promisee to his or her detriment, and it becomes unconscionable for the promisor to resile from the promise, then the proprietary estoppel equity comes into existence.

An important characteristic of proprietary estoppel equity is that it binds third parties. As such proprietary estoppel equity is property at least for the purpose of falling into the bankrupt's estate under **s283A IA1986.**

The dwelling-house issue

The court then considered what a "dwelling-house" consisted of and whether it included the two parcels of land. Having considered various authorities, the court concluded that the Cottage and the parcels of land were acquired separately by different people at different times and for different purposes. They were in different ownership and different occupation. As such the parcels were not a dwelling-house within the meaning of **s283A** and that an interest in these parcels is not an interest in a dwelling-house.

The residence issue

S283A applies to an interest in a dwelling-house which "at the date of the bankruptcy was the sole or principal residence". The phrase within the section contemplates that a person may have two or more residences at the same time. The OR's technical manual refers to the ability of a bankrupt to elect as to which property was "the principal residence". However, the court was not referred to and could not identify any basis in law for such an election. The court noted that residence does not require physical presence at all times. The test that should be applied should be an objective test and should not depend on the unknowable contents of a person's mind.

Decision

The claim for specific performance would be dismissed because the alleged agreement was oral and as it was not in writing and signed by the parties it did not satisfy the requirements of **s2** of the **Law of Property (Miscellaneous Provisions) Act 1989**.

In considering the evidence, the court noted that the applicants did not call Mrs. Foster. Her evidence as to Mr. and Mrs. Brake's occupation of the Cottage would have been material. The failure to call Mrs. Foster meant that an adverse inference should be drawn against the applicants on this point.

Another witness who gave evidence via video link and who claimed to have visited Mr. and Mrs. Brake at the Cottage on numerous occasions was observed by the Judge to have been prompted in her responses by a third party whilst giving her evidence.

Looking at the actual evidence available to the court in the form of documentary and other evidence, the Judge concluded that Mr. and Mrs. Brake had not changed their principal residence from the House to the Cottage by the date of the bankruptcy order and therefore **s283A** did not apply.

Comment

- This case provides a detailed analysis of what interest may or not vest in the bankruptcy estate. It also provides a detailed examination as to what constitutes a dwelling-house and in particular whether this can include additional land or buildings.

- Notwithstanding the OR's Technical Manual it is not open to a bankrupt to elect between properties as to which is his or her dwelling-house for the purpose of **s283A**.

Bankruptcy

Bucknell v Wilson [2020] EWHC 1200 (Ch)

Court exercises discretion to refuse trustee relief for preference

Facts

15/07/2014	Judgment in favour of Mark Fowlds
04/09/2014	Payment to Ms. Wilson £47,675
19/01/2016	Bankruptcy Petition presented
22/03/2017	Bankruptcy Order against Peter Fowlds

This was an application by the trustees in bankruptcy of Peter Fowlds ("the Bankrupt"). The application was issued against the Bankrupt's step-daughter Ms. Wilson for the recovery of an alleged preference in the sum of £47,675 paid by the Bankrupt to Ms. Wilson. The background to the bankruptcy was that the Bankrupt was in business with his son Mark Fowlds in property development and investment. Following a dispute litigation ensued and the son Mark Fowlds obtained judgment against his father the Bankrupt for £715,876.

Requirements to establish a preference

(a) That Peter Fowlds was a bankrupt

(b) That Ms. Wilson was an associate of the bankrupt. The court holding that the definition of "associate" contained in **s435(8)** of the **Insolvency Act 1986 (IA1986**) included Ms. Wilson as step-daughter of the Bankrupt.

(c) The payment to be made within 2 years of presentation of petition which was satisfied.

(d) That the Bankrupt was or became insolvent as a consequence of the payment – "the Insolvency Test".

(e) That Ms. Wilson was a creditor of the Bankrupt. She was a creditor in respect of forensic accountancy services provided to the Bankrupt.

(f) That Ms. Wilson was put in a better position than she would have been in the event of bankruptcy if the payment had not been made. That was the case.

(g) That the Bankrupt was influenced when making the payment by a desire to produce the preference and because of the presumption in **s340(5)** of the Act. A presumption in the case of associates applied which may be rebutted. This meant that the court had to consider "the Desire Rebuttal Test".

Following the above the court only had to consider the Insolvency Test and the Desire Rebuttal Test in determining whether or not a preference had been made.

The Insolvency Test is either a cash flow or balance sheet test as held in **BNY Corporate trustee Services Ltd v Eurosail-UK 2007-3BL Plc [2013] 1 WLR 1408**.

On the Desire Rebuttal Test, the test was best described in **Re MC Bacon Ltd (No.1) [1990] B.C.L.C. 324** which in summary states, that a man can choose the lesser of two evils, without desiring either.

S340(2) of the Act provides that if a preference is found the court "shall make such order as it thinks fit for restoring the position to what it would have been if the payment had not been made."

That provision establishes that it is a discretionary power and the court may either refuse to make an order or make an order that is less than full restitution. In considering whether to exercise the court's discretion, unfairness can be a factor, however in refusing relief it would be a departure from the norm and would have to be something unusual to justify such a course.

The insolvency court will always have in mind the principle in **Re Condon Ex p. James, [1873-74] L.R. 9 Ch. App. 60** which held that a trustee should not take full advantage of his legal rights if it is unfair to do so. The idea that the rule ex parte James is based in unfairness was upheld recently in the case of **Lehman Brothers Australia Ltd (In Liquidation v MacNamara and Others [2020] EWCA Civ 321.** In that case David Richards LJ said that what is unfair is to be judged society's current morality. It is an objective test and is highly sensitive.

Ms. Wilson did not put forward any evidence with regard to the Insolvency Test, or the Desire Rebuttal Test. She argued that the payment was in consideration for professional work that she had undertaken and as such she was a commercial creditor. She also relied upon the fact that all other creditors with the exception of the son as judgment creditor were paid in full whereas she only received 48% of the outstanding debt. She further argued that at the time of the payment he was preparing an appeal and had not been made bankrupt. She no longer had the payment and therefore it could not be recovered from her. She is a lady of limited means on low income. The only asset that she had was her home which would have to be sold. If sold it would be damaging both to her business/income and to her children. She further argued that she had at all times acted in good faith.

It became apparent that part of her defence was "change of position". This is a defence available to a person whose position is so changed that it would be inequitable in all of the circumstances to require restitution. Whilst such a defence cannot be used in relation to a statutory remedy such as a preference under **s340** it can operate as a factor to be taken into account when deciding whether the court should exercise its discretion.

The court considered the decision in **Re Claridge [2011] BPIR 1529.** That case concerned a transaction at an undervalue under **s339** of the Act. The transferee acting in good faith changed her position by using the money received from the transaction for improvements to her property. In considering what order should be made to restore the position to that it would have been if the transaction had not been entered into it was held that it was an exceptional case to which the discretion identified in an earlier case of **Paramount Airways Ltd [1993] Ch 223** should be applied.

At trial it was noted that the bankrupt had not been called as a witness. He had not been interviewed by the trustees as he had failed to cooperate. It was therefore not possible to cross-examine the bankrupt as to what his intention was in making the payment.

Decision

ICCJ Jones held as follows:

1. The Insolvency Test was satisfied.

2. The Desire Rebuttal Test. On this point it was held that it could be inferred that the payment was made as a result of a desire by the bankrupt to fulfil his legal obligation and this made it hard to rebut the presumption. As such it was unrealistic to conclude that Ms. Wilson had satisfied the Desire Rebuttal Test.

On the question of whether relief should be granted in respect of the preference ICCJ Jones identified a number of factors:

The first factor - The debt arose from a commercial relationship.

The second factor - Ms. Wilson played no part in the making of the preference other than receiving the payment and she acted in good faith.

The third factor - The payment is no longer available to her.

In considering whether or not to exercise the court's discretion not to grant relief it was noted that the facts established what was described as the "prerequisite" for the exercise of the discretion not to grant relief. Namely, that she no longer had the Payment or realisable assets of remaining value purchased from those funds.

The fourth factor - The inability of Ms. Wilson to provide restoration without the sale of her family home. Ms. Wilson and her children would suffer detrimentally and it would affect her business and income.

Considering the family consequences, Ms. Wilson must establish that the overall facts take the case out of the wide scope of the norm. Ms. Wilson's family circumstances on their own do not establish a most exceptional case.

The first and second factors on their own would not be enough to take the case out of the norm. It is necessary to establish the first and second factors together with the prerequisite and again that would not be enough. There must be added to that a change of position or disproportionate consequence which would then move the case out of the norm.

In conclusion it is not the norm for the transferee to:

1. Receive the preference on a commercial basis as their arms length
2. Act in good faith
3. No longer have the preference or its proceeds available
4. Change their position so that it would be inequitable to require restitution
5. Face wholly disproportionate consequences if an order for restitution were made with the result that, in this case, restoration would be unfair and unjust.

Having reached the decision that discretion should be exercised in favour of Ms. Wilson and that restoration would be unfair and unjust, the rule in ex parte James did not come into play.

Comment

- The decision in this case is fact sensitive and in the words of ICCJ Jones:

"there is no danger of this decision opening the flood gates to wash away the importance of s340 of the Act."

- The Judge was troubled by the fact that the bankrupt was not called as a witness which would have helped on the issue of his state of mind. It was recognised that the trustees were in a difficult position in view of the bankrupt's failure to cooperate. Reference was made to comments made by Mr. Justice Birss in **Abdulali v Finnegan [2018] EWHC 1806 (Ch)** in which he indicated that trustees should not rely solely on the presumption but should actively investigate desire and ask questions of the debtor in the context of **s340(4)** of the Act. It is not known whether a questionnaire was sent to the bankrupt concerning such matters and which the bankrupt due to his failure to cooperate did not respond to.

- This case made reference to an earlier 2020 decision of **Lehman Brothers Australia Ltd (In Liquidation) v MacNamara and Others [2020] EWCA Civ 321**. In that case two of the Lehman brothers' companies had claimed against each other and had submitted proofs in the other's insolvency. The companies entered into a Claims Determination Deed which determined the net unsecured provable claim. Unfortunately an error occurred in that one of the claims was undervalued as it was expressed in the wrong currency. Notwithstanding this, the administrators of the other Lehman company refused to allow a further claim to be submitted. This resulted in an application to court to apply for directions. The application sought a relief under the rule of **Ex Parte James** and/or **para 74 Schedule B1 IA1986**. Although initially dismissed at first instance, on appeal the application was allowed. David Richards LJ concluded that:

  "no right thinking person would think it fair for the administrators to stand on their strict contractual rights and refuse to correct a shared mistake for which they were as responsible as LBA".

In allowing the appeal David Richards LJ considered the rule in ex parte James and held that the test is one of unfairness. Unfairness is to be judged in the context of current morality. The test is objective and will be judged by the governing morality of the day. **Para 74** may be invoked to prevent an administrator from relying on rights under a contract as to do so would be unfair. This emphasis on unfairness was an important factor in the decision in **Bucknell v Wilson**.

Bankruptcy

Go Capital Limited v Phull [2020] EWHC 1235 (Ch)

Bankruptcy petition opposed on ground that guarantee was a sham

Facts

A bankruptcy petition was issued against Mr. Phull ("the Debtor") following service of a statutory demand. There was no application to set aside the statutory demand. Go Capital Limited ("Go") alleged that the Debtor had failed to pay a sum due under a Personal Guarantee.

The Debtor opposed the petition on the grounds that the Guarantee was a sham transaction, that his signature had been forged, and thirdly that the Guarantee was not in the form of a deed and as such there was no obligation to make payment under it.

The hearing took part remotely but not without problems. One of the microphones did not work and the electronic bundle had various issues which made it difficult and challenging to navigate.

The Guarantee itself was between Go, Odyssey Energy LLC ("Odyssey"), and the Debtor. The Guarantee was linked to a Joint Venture Funding Agreement ("JVFA"). The overall transaction was complicated and it was difficult to understand the respective parties' interests in the transaction. In essence it involved the provision of USD$500 billion through a bank in Hong Kong. Once the funds were provided Go would pay Odyssey USD$20 billion as a bonus.

The fees and expenses incurred with the bank comprised the petition debt of US$75,000. In the end the main facility was not drawn down and yet Go wrote to the Debtor seeking payment of the USD$75,000. During the course of putting the transaction together the Debtor was required to produce proof that he had sufficient funds in his own bank. He had provided bank statements showing that he had £152,448 in his account and provided a copy of his passport.

The Arguments

1. "Genuinely Disputed Debt"

Whilst no application had been made to set aside the statutory demand, had such an application been made one of the grounds would be that the debt is disputed on the grounds which appear to the court to be substantial. The court noted that the test when considering that ground in relation to an application to set aside a statutory demand would be the same as that when hearing the petition itself or on an application to annul on the ground that the bankruptcy order ought not to have been made. The test is whether there is a genuinely disputed debt.

2. Sham

In asserting that there was a genuinely disputed debt it was alleged that the transaction was a sham. When considering that question the starting point is **Snook V London and West Riding Investments Ltd [1967] 2QB 786**. In that case it described a sham as acts done or documents executed by 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. However to be a sham all the parties involved 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.

In **Hitch v Stone (Inspector of Taxes) [2001] EWCA Civ 63, [2001] STC 214** the following principles in relation to a sham transaction were held:

(a) The court is not restricted to examining the four corners of the document. External evidence may be considered.

(b) The test of intention is subjective. The parties must have intended to create different rights and obligations from those appearing and must have intended to give a false impression of those rights and obligations to third parties;

(c) The fact that an act or document is uncommercial, or even artificial does not mean it is a sham;

(d) The fact that parties depart from an agreement does not necessarily mean that they never intended the agreement to be effective and binding;

(e) Intention must be a common intention.

The Court considered an example of a transaction which is not a sham in **Shalson v Russo [2003] EWHC 1637 (Ch)**. In that case a settlor created a settlement where he purported to divest himself of assets in favour of the trustee. Although 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, unless that intention is from the outset shared by the trustee, such a settlement cannot be regarded as a sham.

3. "The Guarantee"

There are four types of guarantee of a loan these are:

1. A "see to it" obligation i.e, an undertaking by the guarantor that the principal debtor will perform his own contract with the creditor;
2. A conditional payment obligation i.e, a promise by the guarantor to pay the instalments of principal and interest which fall due if the principal debtor fails to make those payments;
3. An indemnity;
4. A concurrent liability with a debtor for what is due under the contract or loan.

The Guarantee in this case was only argued as a "see to it" obligation as in 1 above.

The legal requirements for the execution of a deed are contained in **section 1** of the **Law of Property (Miscellaneous Provisions) Act 1989** ("the 1989 Act") sub-section 2 which provides that:

(2) An instrument shall not be a deed unless—

(a) it makes it clear on its face that it is intended to be a deed by the person making it or, as the case may be, by the parties to it (whether by describing itself as a deed or expressing itself to be executed or signed as a deed or otherwise); and

(b) it is validly executed as a deed by that person or, as the case may be, one or more of those parties.

Section 1(3) of the 1989 Act provides that—

(3) An instrument is validly executed as a deed by an individual if, and only if—

(a) it is signed—

(i) by him in the presence of a witness who attests the signature; or

(ii) at his direction and in his presence and the presence of two witnesses who each attest the signature; and

(b) it is delivered as a deed.

4. "Forged signature"

For the Debtor it was argued that his signature on the deed was a forgery. No evidence from a handwriting expert was produced. Further the Debtor argued that there was nothing in the transaction for him and there was no reason for him to guarantee a payment to HSBC for fees and that further there was no evidence that HSBC had in fact charged any fees.

Decision

Chief ICCJ Briggs outlined that he did not need to make a finding that the transaction was a sham merely whether there was a substantial dispute or genuine triable issue. Whilst he had grave misgivings about the efficacy of the transaction that did not mean there was a genuine triable issue.

In determining whether or not there was a substantial dispute he noted that the documentation contained many errors indicating a lack of professional care for such a large transaction. Further Go's own evidence did not deal with the dispute about signature or provide any evidence as to payment of the fees of HSBC.

As to the allegation of forgery there was no expert evidence. The hearing of a bankruptcy petition is not a suitable forum to decide such a question and the unusual nature of the transaction led to the conclusion that the Debtor had raised a substantial dispute.

On the Guarantee there was a failure to execute it properly because firstly the signature was not witnessed, and secondly there was nothing on the face of the Guarantee that describes it as such or in any way makes it clear that it is intended to be a deed. Lastly, the Guarantee was not delivered as a deed. There was no consideration for the Guarantee and as it was not executed as a deed, the lack of consideration was fatal. The Debtor is not bound by the Guarantee.

Comment

- This case provides a useful reminder as to the requirements that need to be established in order to demonstrate that a transaction is a sham. It also highlights the distinction between an alleged sham transaction and a mere deception.

- This decision also examines the formalities required to establish liability under a guarantee and confirms that failure to comply with those formalities will render the guarantee invalid.

- During the hearing Go had explained that they had presented the bankruptcy petition because "*it was a quick and inexpensive way to enforce the debt*". This drew a sharp rebuke from the Judge who pointed out that insolvency proceedings are class actions and should not be used as a debt collection process. A petitioner seeking to use bankruptcy proceedings for the enforcement of a debt in this way faces the prospect of an adverse indemnity costs order.

Bankruptcy

Oyesanya v Jackson [2020] EWHC 542 (Ch)

Appeal against order for possession and sale

Facts

Mr. Oyesanya was a senior medical consultant who was made bankrupt by Trafford Council on 02 March 2015. On 10 June 2016 his joint trustees in bankruptcy were appointed one of whom was the respondent in this case. The bankrupt remained undischarged due to a failure to cooperate with his trustee.

The application was for permission to appeal and if granted, to hear the appeal immediately thereafter. Previously, on 04 February 2019 an order for possession and sale was made in the County Court at Manchester in respect of the property known as 74 The Downs, Altrincham, Cheshire ("the Altrincham property"). That property was registered in the sole name of the bankrupt and was the bankrupt's home with his wife. Previously, there had been a claim that his wife had a beneficial interest in the property however, following a direction of the court, his wife failed to intervene or provide any evidence to support such a claim.

The matter came back before the court when the respondent trustee applied to stay the possession application. This was on the basis that there was another residential property in Harrow North West London ("the Harrow property") which was in the process of being sold by the mortgagee. It was anticipated that this would produce sufficient surplus to the bankruptcy estate which would mean that there was no requirement to sell the Altrincham property.

Unfortunately, following the sale of the Harrow property by the mortgagee, there was a deficiency of about £121,000 in the bankruptcy and therefore the trustee applied for the stay on the possession proceedings to be lifted. At that hearing the bankrupt applied to adjourn the proceedings on medical grounds. The District Judge made a declaration that the Altrincham property had vested in the trustee but adjourned the consideration of whether to make a possession order to another date. The possession application came before District Judge Khan on 04 February 2019 at which the Judge refused an extension of time in which to file medical evidence or to adjourn the proceedings. An order for possession and sale was made at that hearing. Subsequently, on the bankrupt's application the possession order was stayed pending determination of an application for permission to appeal.

Rules concerning appeals

The Judge reminded himself of the rules relating to appeals and summarised the position as follows:

1. Under **CPR rule 52.21(1)**, an appeal is limited to a review of the decision of the court below, unless the court considers that in the circumstances it would be in the interests of justice to rehear the case:

2. no fresh evidence shall be admitted on the appeal "unless the court considers otherwise".

3. an appeal will be allowed where the decision was:

    a. wrong - wrong means wrong in law, wrong in fact, or wrong in the exercise of discretion;

   b. unjust, because of serious procedural or other irregularity in the proceedings below.

4. the court below must have given reasons for its decision.

Grounds of appeal

The bankrupt's grounds for appeal were summarised as follows:

1. error of law;
2. wrong exercise of discretion;
3. serious procedural or other irregularity resulting in injustice;
4. article 6 of the European Convention on Human Rights;
5. errors of fact;
6. perversity;
7. new evidence available.

The court then considered the transcript of the judgment of District Judge Khan on 04 February 2019 at which the order for possession and sale was granted. The bankrupt argued that the District Judge was wrong to refuse an application to adjourn on medical grounds. It was noted however that the bankrupt need not have addressed the court on that occasion but could have obtained legal representation or have been accompanied by so-called McKenzie friend. The bankrupt did none of that and chose to go ahead on his own account.

The bankrupt also challenged the refusal to grant an adjournment on his claim to be unable to conduct the hearing on medical grounds. On this point the court referred to the decision in **Levy v Ellis-Carr [2012] EWHC 63 (Ch)**. In that case the Appellant had gone to their doctor and requested a letter. In considering the letter the Judge concluded that it fell short of the medical evidence required to demonstrate that a party is unable to attend a hearing or participate in the trial. Such evidence should identify the medical attendant, give details of his familiarity with the party's medical condition, (detailing all recent consultations), should identify with particularity what the patient's medical condition is and the features of that condition which (in the medical attendant's opinion) prevent participation in the trial process. It should provide a reasoned prognosis and should give the court some confidence that what is being expressed is an independent opinion after a proper examination.

In the current case it was noted that the Judge at the earlier hearing had taken into account the medical evidence produced by the bankrupt, and also his demeanour at the hearing, together with the history of the case. On this point the appeal court considered the District Judge had made no error of law or procedure.

The bankrupt alleged that the Harrow property was sold at a gross undervalue. Also that the costs and expenses of the bankruptcy were far too high.

The Altrincham property was valued at £680,000 with an outstanding mortgage of £374,000. This would have meant that on the sale of that property there would have been a surplus available to the bankrupt. It was noted that the surplus was being eroded as the litigation continued. On the undervalue point, the sale had been by the mortgagee and not the trustee. The question was raised as to whether the District Judge should have stayed his hand in relation to the possession application for the Altrincham property and first investigated the possibility of a claim being made against the bank that it sold the Harrow property at an undervalue. The Altrincham property had a significant value and could be easily realised at modest cost. On the other hand, there was the prospect of speculative litigation against the bank at potentially significant cost before it was even known whether or not it was worth pursuing. In those circumstances, the District Judge could not be criticised for acceding to the application to proceed with the possession and sale of the Altrincham property.

Excessive costs and expenses

The bankrupt argued that the trustees' costs were excessive. However, no formal challenge had been made to those costs under **rule 18.35** of the **Insolvency (England and Wales) Rules 2016**, or otherwise. Matthews J commented that:

> "*It appears that on this point the applicant has been willing to wound and yet afraid to strike…*".

As to possible overcharging the Judge concluded that there was no evidence of any overcharging.

The bankrupt also argued that creditors had been paid in full. However, the bankrupt had not put forward any evidence to confirm that position.

Decision

The court found that the District Judge had given adequate reasons for his decision and that whilst fresh evidence will not be admitted under **CPR rule 52.21(2),** unless the court orders otherwise, the bankrupt had failed to identify and particularise any fresh evidence.

HHJ Paul Matthews held that:

There was no real prospect of the applicant succeeding in the appeals against any of:

(i) the refusal to extend time for the service of medical evidence,

(ii) the refusal to adjourn the hearing of 4 February 2019 on medical grounds,

(iii) the possession order,

Permission to appeal be refused,

The stay of the possession order and the suspension of the possession warrant would be lifted and the warrant could be enforced.

Comment

- This case dealt with a number of articulate challenges made by the bankrupt against the actions of the trustees in bankruptcy. Despite the court warning the bankrupt that the costs of the bankruptcy would continue to increase whilst his litigation continued, the bankrupt was unperturbed and continued with various applications which had a significant impact on the ultimate costs and expenses of the bankruptcy.

Bankruptcy

Thomas v Bulathwela [2020] BPIR 430

Husband of bankrupt claims beneficial interest in property

Facts

Mr. and Mrs. Bulathwela were both solicitors. They ran two legal practices which ran up substantial debts with the Legal Services Commission ("LSC"). Mrs. Bulathwela was the sole legal owner of the property known as 311 Whitchurch Lane Edgeware. ("Whitchurch Lane") Mr. and Mrs. Bulathwela were also the joint owners of another property at Manor Park Edgeware in which they lived ("Manor Park"). Whitchurch Lane was an investment property which had been let out to the couple's daughter and her husband. In June 2009, Mr. and Mrs. Bulathwela executed a legal charge over Whitchurch Lane to secure their joint indebtedness to the LSC. A similar charge was given over their property at Manor Park.

On 07 July 2015 Mrs. Bulathwela was made bankrupt on the petition of the LSC.

The joint trustees in bankruptcy were appointed and they issued an application in respect of both properties. In relation to the Whitchurch Lane property they sought a declaration that they were the sole legal and beneficial owner of the property. Mr. Bulathwela opposed the trustees' application claiming that he had an:

> "*interest as a joint owner and under the matrimonial rights*" in respect of the Whitchurch Lane property.

He referred to both properties as ones in which:

> "*I have interest as a joint owner and under the matrimonial rights*". On Whitchurch Lane, he said "*according to my understanding as the husband of [Mrs. Bulathwela], I too [have] the rights to possess 50% interest on the property under the Matrimonial Act*".

The matter came before DJ Hart on 25 January 2017 who gave directions which enabled either Mr. or Mrs. Bulathwela to make an application if they wished to file further witness statement evidence. No such application was made. Later, Mr. Bulathwela filed a witness statement although none of it related to the beneficial interest in Whitchurch Lane.

There was then a further hearing at which the trustees sought an adjournment because they had discovered there was a tenancy granted to the bankrupt and her husband's daughter. Directions were given to produce the tenancy agreement and an account for the rent. The Judge also refused permission for Mr. Balathwela to rely on the witness statement that he had filed without first having made an application for permission.

Then Mrs. Bulathwela filed a witness statement on 23 March 2017 concerning the tenancy in favour of her daughter. It also contained at paras. 9-11 purported evidence as to Mr. Bulathwela's beneficial interest in Whitchurch Lane. In particular it stated:

1. The deposit was from "family money" and was provided by her husband but she could not provide documentary evidence.

2. Her and her husband were of the understanding that Mr. Bulathwela had a right to one half of the property.

3. Mr. Bulathwela was the main bread-winner of the family

4. Both she and her husband offered the property as security for the LSC debt because they believed they were meant to own equal shares of the properties.

The matter came back before the court on 31 October 2017 and the Judge noted that Mrs. Bulathwela's evidence went beyond the direction and as such she refused permission for the respondents to rely on paras 9-11 of Mrs B's witness statement.

First Instance Judgment

The Judge dismissed Mr. B's claim to a beneficial interest in the Whitchurch Lane property for the following reasons:

1. Mr. B's claim to a right under the Matrimonial Act was irrelevant to the current application.

2. Without a trust deed the starting point was that "equity follows the law". As the legal title was vested in Mrs. B alone it was for Mr. B to prove he had an equitable interest on the basis of a resulting or constructive trust.

3. Mrs. B's support for her husband was of little significance as it was in her financial interest to do so.

4. As far as a resulting trust was concerned there was no evidence which established any financial contribution. His payment of mortgage instalments was only relatively recent and was to assist his daughter who could no longer afford the rent. Those mortgage payments did not establish a beneficial interest under a resulting trust.

5. In order to establish a constructive trust it will be necessary to find a common intention. Whilst this could be inferred there was no evidence of any discussion between Mr. and Mrs. B which might establish an express common intention. On the contrary Mr. B's statement of assumption of an automatic legal entitlement meant that any such discussion was unnecessary.

6. The fact that Manor Park was in joint names tended to suggest that a decision was taken in relation to Whitchurch Lane that it would be the sole property of Mrs. B.

7. The only evidence supporting Mr. B's claim was the LSC charge over Whitchurch Lane. There was no evidence to explain why the deed was granted by them both. The Judge concluded the evidence was insufficient to establish an inferred common intention.

The Appeal

On appeal the parties were in agreement as to the approach to be taken. The starting point is to consider whether on the basis of the evidence as a whole, there is to be an inferred common intention that the beneficial interest was to be shared between Mr. and Mrs. B. It is only if there is insufficient evidence to reach a conclusion on this that it is necessary to revert to the question of whether there is a presumption of resulting trust arising from contributions made to the purchase price.

Decision

Taking into account that only the permitted evidence was considered, there was no evidence of any financial contribution by Mr. B. The only permitted evidence related to payments in respect of the mortgage. On that point the court was referred to the judgment of David Richards in **Barrett v Barrett [2008] EWHC 1061 (Ch)** in which the position was explained as follows:

> "Contributions to mortgage instalments do not stand in the same position as direct contributions to the purchase price. They may be intended to confer a beneficial interest on the payer, but equally they may be intended as an advance to the mortgagor, entitling the payer to be subrogated pro tanto to the mortgagees rights or they may, as John contends in this case, be intended as payments in lieu of rent. To establish that they are intended to confer a beneficial interest, they must be referable to an agreement or arrangement made at the time of purchase that the payer should be responsible for the mortgage instalments either on terms that he should have a commensurate beneficial interest or in circumstances from which such an intention can be inferred – (see **Carlton v Goodman**)".

The evidence on the mortgage payments made by Mr. Bulathwela fell short of evidence sufficient to give rise to a resulting trust and were not referable back to an agreement to invest at the time of purchase. As such there was no basis to set aside the judge's conclusion based on resulting trust.

On the question of whether or not there was constructive trust based on the granting of the LSC charge, the appeal court would not interfere with the original decision that it was not sufficient to establish a constructive trust in favour of Mr. B.

The court considered the question of whether Mr. B should have been allowed to rely on further evidence in respect of his claim for a beneficial interest in Whitchurch Lane. On this point the appeal court refused the application to admit new evidence.

The appeal was dismissed.

Comment

- This case is a useful reminder as to the approach that should be adopted by the court in considering a claim to a beneficial interest in a property and in particular what is required to establish interest by way of resulting trust and/or common intention.

- A point of particular interest in this case was the attempt to rely on the making of payments by the non legal owner towards the mortgage to support his claim for a beneficial interest. Whilst mortgage payments can amount to the establishment of a beneficial interest, this decision explains in more detail what is required for mortgage payments to amount to a beneficial interest.

Liquidation

Atkinson v Varma [2020] EWHC 1868 (Ch)

Liquidator's application to jail director for contempt of court

Facts

This was an application by liquidators of Grosvenor Property Developers Limited (in liquidation) ("the Company") to commit Mr. Varma to prison for contempt of court. The liquidators claimed that Mr. Varma had failed to disclose his assets and that he had made false statements as to what had happened to the Company's money.

The Company had been formed with the apparent purpose of acquiring the Grosvenor Hotel in Bristol. This was then to be redeveloped into studio flats and sold to investors. Approx. £7m was paid to the Company by investors but the hotel was never acquired. The Company went into compulsory liquidation on 14 November 2018.

The liquidators' enquiries into the Company and its director included an interview in which Mr. Varma stated that whilst he was the registered shareholder the Company's true owner was a Mr. Singh. When asked about a £3m payment by the Company to a Dubai company Grosvenor Consultants FZE ("GCFZE"), Mr. Varma replied that this was an investment by the Company in diamonds and jewellery.

The liquidators applied for a private examination under **s236** of the **Insolvency Act 1986 ("IA1986")** and for the delivery up of Company property under **s234**. Mr. Varma failed to attend the examination and ultimately produced just nine pages of documents. This included a business consultancy agreement between Mr. Varma and the Company, an invoice from GCFZE to the Company for £4.95m for jewellery and a settlement agreement. In the meantime, the liquidators obtained a worldwide freezing order against Mr. Varma and GCFZE which included a provision requiring Mr. Varma to give information about his assets. Mr. Varma, through his solicitors, replied stating that he was the sole owner of GCFZE and that it had notional value only. He also delivered up his passport with a number of pages torn out. He later explained that his dog had eaten his passport.

Various applications and orders ensued which included ordering Mr. Varma to produce letters of authority to banks in order that bank statements may be obtained and to provide documentary evidence as to the proceeds of sale of a flat in Hallam Street. In the meantime, on the liquidators' application an order was obtained against Mr. Varma to pay sums of £1,361,315 and £3,122,841 representing equitable compensation for breach of duty as a de facto director of the Company. Following on from this the liquidators made an application to commit Mr. Varma to prison for contempt.

The court first of all considered what is required in order to commit someone to prison for contempt of court. The following principles apply:

(1) The liquidators may not, without permission, rely on any grounds of contempt other than those set out in the application notice;

(2) In order to establish that a respondent is in contempt of court through disobedience of a court order, it is necessary to establish the following to the criminal standard of proof:

(a) that the respondent knew the terms of the relevant order;

(b) that he acted (or failed to act) in a manner which involved a breach of the order, and

(c) that he knew of the facts which made his conduct a breach;

(4) **CPR 81.9** requires a penal notice to be put on an order if it is to be enforced by committal;

(5) The requirement for a penal notice may be dispensed with where the lack of such a notice causes no injustice to the respondent;

(6) A person may be liable in contempt for making a false statement in a document verified by a statement of truth **(CPR 32.14);**

(7) To establish contempt by making a false statement in a document verified by a statement of truth, it is necessary to establish beyond reasonable doubt:

(1) that the statement in question was false,

(2) that the statement has, or if persisted in would be likely to have, interfered with the course of justice in some material respect, and

(3) that at the time the statement was made the maker had:

(a) had no honest belief in the truth of the statement, and

(b) knew of its likelihood to interfere with the course of justice.

The court then proceeded to go through the allegations of contempt contained in the application notice and the alleged false statements.

The jewellery and diamonds deal

Mr. Varma in his statement alleged that funds of approx. £3.1m paid to GCFZE were paid against the sale of jewellery and diamonds to the Company. The liquidators disputed this and said that there was no such deal and it was a straight misappropriation of Company money.

On this point the court noted that there was a commercial improbability to the transaction and that there was no real evidence of the existence of the jewellery and diamonds. Similarly there was no evidence of any insurance for the valuables. The story of the jewellery and diamonds was an attempt to justify otherwise non legitimate payments made by the Company to GCFZE. The explanation that the Company was controlled by a third party Mr. Singh was also dismissed. A settlement agreement that was purportedly signed in Mumbai on 11 June 2018 was found to have been created to make pursuit of the Company money more difficult. It was also noted that Mr. Varma attended a doctors surgery in Mayfair on the day he purportedly signed the settlement agreement in Mumbai. Mr. Varma had previously claimed that a document was held in a fingerprint lock safe in Dubai. Later he produced the document but without ever visiting Dubai.

HH Judge Jones applied the highest criminal standard of proof namely beyond reasonable doubt and concluded that the statement that £3.1m paid to GCFZE was paid against the sale of jewellery and diamonds to the Company was false and that Mr. Varma could not have had an honest belief in its truth.

The court then looked at the alleged breach of the orders previously made. The first was:

Failure to deliver documents to liquidators' solicitors

Mr. Varma had produced via his solicitors a total of nine pages. He also claimed that he had no electronic documents because he deletes all relevant emails at the turn of each calendar year and he threw out his laptop in January 2019 as the screen went blank. The Judge stated that he did not believe either statement, but because there was a lack of a penal notice on the relevant order he did not find that this ground for committal had been made out.

Failure to attend private examination

The Judge noted that he had to be sure that Mr. Varma did not have a genuine reason for his non-attendance. He noted that Mr. Varma had underlying health issues and therefore was unable to be sure that he did not have such a genuine reason. This allegation of contempt was not established.

Failure to tell the liquidators' solicitors where spending money came from

Again, because of the higher standard of proof the court was not willing to find that Mr. Varma was in contempt based on inference only.

Failure to deliver up passport

Mr. Varma had delivered up his passport albeit with torn pages. Again, this was insufficient to find the ground of contempt had been established.

Failure to inform liquidators' solicitors within 48 hours

Mr. Varma had a shareholding in a company called My Casa PBSA Ltd. It was alleged that he had failed to disclose the shareholding which had an estimated value of £14,000. The court noted that Mr. Varma was a wealthy man worth millions of pounds. His claim that he had lost his wealth in Dubai property transactions was found not to be true. There was also the allegation that he had interests in multiple properties. Having considered various alleged property interests it was noted that whilst the liquidators had not identified to the Judge's satisfaction any particular undisclosed assets by or for Mr. Varma as at April 2019, the Judge nevertheless concluded that Mr. Varma had acted in breach of this order by failing to inform the Applicants solicitors of all of his assets. Nevertheless, the order contained a penal notice and on this point the court found that the ground for committal had been established.

Failure to serve affidavit with information as to assets

The previous order required information be given concerning the assets of GCFZE. Mr. Varma was the director of that company and was found personally liable for GCFZE's failure to comply with the order. This ground for contempt was therefore established.

Failure to provide signed letter of instruction to banks

Having been ordered to provide letters of instructions to banks to enable access to bank statements to be obtained, a signed letter of authority was provided to the liquidators' solicitors albeit after the deadline stated. On this point the court noted that there was a penal notice attached to the order, and that the ground of contempt had been established.

Failure to provide liquidators with documents showing where proceeds of sale of Hallam Street went

Having considered the documents that were produced the court did not find this contempt allegation made out.

Failure to sign authority letters

This was pursuant to an earlier order which required such letters to be provided in relation to solicitors and other entities. This breach was made out and notwithstanding the fact that the order did not contain a penal notice, it was decided that the requirement for such a penal notice would be waived as there was no injustice to Mr. Varma.

Decision

The court also further identified false statements in affidavits concerning disclosure of assets and bank statements. In respect of such statements it was noted that Mr. Varma could not have had an honest belief in the truth of such statements. Further those false statements interfered with the course of justice in a material respect. He not only knew the likelihood that false statements would interfere with the course of justice but he intended that result. Mr. Varma was therefore found to be in contempt of court. The case was adjourned for sentencing.

Comment

- This case demonstrates that parties may go to considerable lengths to avoid disclosing their assets. In this case the liquidators fully utilised their powers under sections **236 and 234** of the **Insolvency Act 1986.**

- Whilst the liquidators sought on a number of occasions to request the court to rely on an inference that certain allegations were made out the court was reluctant to rely on inferences for the purposes of establishing whether or not the criminal standard of proof had been made out for contempt of court.

Liquidation

Duckworth v Parekh [2020] EWHC 2360 (Ch)

Misfeasance – application to set aside judgment

Facts

This was an application by Mr. and Mrs. Parekh to set aside a judgment that had been obtained against them by the liquidator of Truewood Limited (In Liquidation) ("the Company").

The alleged misfeasance was improper receipt of payments from the Company which carried on business as a DIY shop.

The basis for the application was that Mr. and Mrs. Parekh alleged that they had not been served with the application or its evidence and were therefore unaware of the proceedings when the judgment was given. The application was under **Rule 7.47(1)** of the **Insolvency Rules 1986 ("IR1986")** ("the Rules") **(r12.59 2016 Rules)** which applied to the application which was issued on 22 November 2016 before the **Insolvency (England and Wales) Rules 2016 ("2016 Rules")** which came into force on 06 April 2017. That Rule allows the court to review rescind or vary any order made by it in exercise of that jurisdiction. The powers of review are to be exercised in accordance with the guidance in **Papanicola v Humphreys [2005] 2 AER 418**. That guidance being:

(1) The court has a wide discretion to review, vary or rescind.

(2) The applicant must demonstrate the existence of circumstances which justify exercise of discretion in their favour.

(3) Circumstances must be exceptional

(4) They must involve a material difference to what was before the court which made the order i.e, something new

(5) No limit on factors which may be taken into account

(6) If new evidence which could have been made available, then an explanation as to failure to produce will also be a factor.

(7) In a case involving non-attendance why did the applicant not attend and how speedily did he make his application?

Further **Rule 7.55(IR86) (r12.64 2016 Rules)** provides:

> "No insolvency proceedings will be invalidated by any formal defect or any irregularity unless the court before which objection is made considers that <u>substantial injustice</u> has been caused by the defect or irregularity and that the injustice cannot be remedied by any order of the court."

It was further noted that the Court of Appeal had stated that it will almost always be just to set aside a judgment which is irregular for want of service.

Requirements for service

Rules 12A.16 and **12A.17 IR1986** provide that **Part 6** of the **CPR** applied and that an application notice is to be treated as a claim form for the purposes of service. The Liquidator relied upon postal service under **CPR Part 6 Rules 6.3(c)** and **6.9(c)**. Postal service on an individual of a claim form, in this case the application notice, must satisfy the following requirement(s).

Part 6 of the **CPR** requires a postal service must be to "*the last usual or last known residence*". If the claimant has reason to believe that the defendant no longer resides at that address, then reasonable steps must be taken to ascertain the "*current residence*". In which case service must be at the current residence.

If the current residence is not ascertained and the claimant considers there is an alternative place where service may be effected including by post, an application for alternative service must be made under **CPR Part 6 Rule 6.15**.

If the current address cannot be ascertained and there is no alternative place of service, the Claimant must serve at "*the last usual or last known residence*".

The liquidator served the application notice at 21 Kingsdown Avenue whereas the applicants contended that their usual and last known address was 97 Pollards Hill South. It was argued that the Kingsdown address was incorrect because that had been let out at the relevant time. It was also discovered that the Pollards Hill address had been transferred to the applicants' sons. It was upon learning of the transfer of the Pollards Hill property that the liquidator discovered the Kingswood property as a result of a search at HM Land Registry. Various other arguments were put forward as to why service had not been effected properly.

Decision on service

Knowledge of the sale of Pollards Hill gave reason for the liquidator to believe that Mr. and Mrs. Parekh no longer resided at that address. The liquidator had taken reasonable steps to ascertain the current residence and it was reasonable to carry out a Land Registry search to ascertain whether Mr. and Mrs. Parekh owned another property. The fact that the only other property identified was the Kingswood property, produced the possibility that it was their residence.

At this point further enquiries were required, i.e, attendance at the property or written correspondence. In the absence of any other evidence to confirm that the property had become their usual last known residence, the current residence had not been ascertained. This meant that the liquidator had to consider whether Kingswood Avenue was an alternative place where service might be effected. In this case an application for an order for alternative service should have been made under **CPR Rule 6.15** but was not.

Even if the Kingswood Avenue address was not an alternative place where service might be effected, the obligation would have been to serve at Pollards Hill. This was not done.

In this case there was good reason to set aside the irregular judgment but subject to considering the application of **r7.47(1),** the guidance in **Papanicola v Humphreys** and **r7.55**. This brings into play a consideration as to whether or not any substantial injustice has been caused. Whilst there had been an injustice to the extent that the judgment obtained could be enforced, this would not be the case if there was no defence to the claim. This meant that the court had to consider the nature of the applicant's defence to the misfeasance claim.

Misfeasance claim - was there any defence?

The misfeasance judgment was for a total of £38,059 arising out of wrongful transfers or payments. This included payments to Grosvenor Hale Limited a company owned by Mr. Parekh and managed by his sons.

The last accounts for the Company recorded an £8,000 salary for Mrs. Parekh but no director's loan account. Amongst the payments were payments made to HSBC Life UK Ltd in respect of a personal private pension and payments by way of an alleged salary for Mrs. Parekh. There were also payments to London Borough of Croydon for rates in respect of their home and travel expenses of £8,000. Mr. and Mrs. Parekh claimed that they worked in the business without payment and that salaries would be reconciled at the end of year against their personal drawings.

Decision

The starting point is that a judgment would normally be set aside where it has not been served correctly provided prejudice had been caused and there is an arguable defence.

Part of the arguable defence was the concept of set off. On this point ICC Judge Jones held that the payments made to Mrs. Parekh as a director during the year were a loan. She had no entitlement to that sum for services rendered. Those payments could not be considered to be salary. Salary would normally be a fixed sum paid on a regular basis which the sums in this case were not. Further the payments could not be a dividend as the formalities of the **Companies Act 2006** had not been met.

The fact that she was not paid a salary but nevertheless worked as a director was not grounds for entitlement to any sum from the Company. The position with regard to Mr. Parekh who was not a director was that whilst he was arguably retained by the Company in consideration for a quantum meruit payment the failure to pay that amount would still leave an unliquidated debt. The position was the same as if he had been a director there would be no contractual liability until the company had agreed that he should receive a payment in a determined amount.

In respect of the various other payments it was held there was no potential set off or arguable defence. Similarly, there were no defence or potential set off concerning sums paid/received as personal or otherwise unexplained expenditure. However, it was now impossible to have a fair trial as the directors did not have the financial books or records notwithstanding their obligation to maintain proper accounting records.

Certain sums were identified as having been paid by Mrs. Parekh, their son and Mr. and Mrs. Parekh to the Company. The payment from the son merely left a debt to be proved by him in the liquidation. With regard to the payments made by Mr. and Mrs. Parekh it is arguable that they were repayment of existing loans or should be credited to their loan account and set off within that account.

It was noted that normally **r4.90 IR1986** (**r14.25 2016 Rules**) providing for set off where there are mutual dealings would apply, it was submitted that as the claim is for misfeasance there is no right to set off.

On this point ICC Judge Jones noted the fact that the money paid by the Company was used for personal purposes does not mean payment was a misfeasance. It could have been lawfully lent if approved by a resolution of the members. However, there was no evidence of any board meeting authorising the loans but authorisation can be assumed from the payments by the Company permitted by its director. It was therefore at least arguable that the loans to the Company will have been set off against the loan accounts of Mr. and Mrs. Parekh when the payment was made had accounting records been kept. If not in any event they should be set off in the liquidation as mutual dealings.

As such the judgment would be set aside but only on the grounds of the arguable defence that the debt has previously been repaid by the payments identified as having been made by Mr. and Mrs. Parekh to the Company or should be set off against those payments being loans made by Mr. and Mrs. Parekh.

Comment

- This case demonstrates the importance of ensuring that applications are correctly served on parties. It also provides a useful reminder as to the detailed requirements of the **CPR** in this regard.
- Whilst case law indicates set off cannot operate where there has been misfeasance, in this case the Court was willing to allow the possibility that set off could take place where a director had made payments to the company and they were to operate as repayments of a loan account or in reduction of the outstanding balance. The Court also acknowledged that this could take place under **r4.90 IR1986** (now **r14.25** of the **2016 Rules**).

Liquidation

Re System Building Services Group Limited (In Liquidation); Hunt v Michie [2020] EWHC 54 (Ch)

Director's duties after administration/liquidation

Facts

This case concerned System Building Services Group Limited (In Liquidation) ("the Company").

Chronology

12 July 2012	Administration
03 July 2013	Conversion to liquidation
24 February 2016	Dissolution
30 June 2016	Mrs. Sharma made bankrupt
25 April 2017	Company restored to Register
03 May 2017	Liquidator appointed

The administrator/liquidator in this case was an insolvency practitioner who following judgment being awarded against her in the case of **Top Brands v Sharma [2014] EWHC 2753** of £548,074.56, was then made bankrupt on 30 June 2016.

Mr. Hunt took over a number of cases from Mrs. Sharma under a block transfer order including this one. Following an application to restore the Company to the Register Mr. Hunt was appointed liquidator and subsequently issued an application against Mr. Michie and a further company called Systems Building Services Limited ('SBSL'). Mr. Michie was at all material times the Company's sole shareholder and director. He was also employed by SBSL and subsequently acquired a substantial shareholding in it and became its sole director.

The applicant liquidator decided not to pursue any claims against the former liquidator/administrator following her bankruptcy, as to do so would not have been in the interests of creditors. Mrs. Sharma had proved unhelpful in relation to enquiries made by the liquidator which ultimately meant that not all the Company's books and records were recovered.

The liquidator's claims consisted of a number of separate heads the most significant being in relation to a property known as 55 Crown Road, Billericay Essex CM11 2AD ("the Property"). The liquidator alleged that Mr. Michie who remained a director of the Company had purchased the Property from the former liquidator at a substantial undervalue (£120,000) for his own benefit and without regard to the interests of creditors as a whole. Further, it was alleged that Mr. Michie acted in breach of duties owed by him to the Company as its director under **s171-175** of the **Companies Act 2006** ("CA2006") including in particular his fiduciary duty to act in the best interests of the Company's creditors as a whole from the time at which the Company became insolvent. The remaining claims against the director consisted of monetary claims for an alleged loan account, remuneration and unaccounted expenses.

The duties of directors were summarised as follows:

1. **s171** provides:

   A director must only exercise powers for the purposes for which they were conferred.

2. **s172(1)** states a director must act in the way he considers in good faith to promote the success of the company for the benefit of its members as a whole.

3. **s172(3)** goes on to provide that the duties imposed by **s172(1)** and **(2)** have effect "subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company".

4. **s174** provides a director of a company must exercise reasonable care, skill and diligence.

5. **s175** states a director must avoid a situation where he has or can have a direct or indirect interest that conflicts or possibly may conflict with the interests of the company.

The applicant's case focused largely on **s172.** The duties are of a fiduciary nature.

Duty to act in the best interests of creditors applies where the company is insolvent or likely to become insolvent following which the interests of the company are regarded as the interests of the creditors alone. Their interests are generally regarded as becoming paramount. Reference being made to the recent case of **BTI 2014 LLC v Sequana SA [2019] BCC 631**.

It was common ground that Mr. Michie remained a director of the Company notwithstanding administration and subsequent liquidation. **Paras 61** and **63 Schedule B1** of the **Insolvency Act 1986 ("IA1986")** and **s103 IA1986** make it clear that directors are not removed from office on the company going into administration or liquidation and that a director may not exercise any management powers without the consent of the administrator and that on entry into liquidation all powers of the director cease save to the extent the liquidation committee (or absent that the creditors) sanction their continuance.

There was debate as to whether and if so to what extent the general duties defined in **s170-177 CA2006** survive the Company's entry into a formal insolvency process. It had been argued for Mr. Michie that those general duties did not continue. On this point it was noted that there was nothing in case law either before or after the **CA2006** to suggest that such duties cease on a company's entry into a formal insolvency process. As such those duties continued notwithstanding the Company entering into administration and CVL.

The Property

The Property was originally purchased by the Company on 30 December 2009 for £185,000. In the Company's audited accounts for the year ending 31 March 2010 its value was stated to be £188,065. The mortgage on the Property was £124,722. The Property remained at the same value in the amended accounts for the same year which were signed by Mr. Mitchie on 10 November 2011.

Following administration, the Administrator's Proposals estimated the value of the Property to be £200,000. The figure having been provided by Mr. Michie. In the Statement of Affairs signed by Mr. Michie on 05 September 2012 Mr. Michie stated the estimated value of the Property was £180,000. He was unable to explain why the value of the Property had dropped £20,000 in the space of five days.

Mrs. Sharma did obtain an independent valuation on 25 September 2012 which valued the Property at £195,000. Discussions then took place between Mr. Michie and Mrs. Sharma following which Mr. Michie paid the sum of £40,000 having offered £120,000 for the Property. Eventually a sale was completed following Mr. Michie transferring the balance of £80,000 to Mrs. Sharma's client account. Completion having taken place on 12 December 2014. Just over two years' later Mr. Michie put the Property up for sale originally for £365,000 but reduced that to £335,000. The single joint expert at trial valued the Property at £300,000. With the value at July 2014 being £265,000 in good repair and £245,000 if works were required as had been claimed. There was no marketing of the Property or any Zoopla or other evidence produced to support the price agreed.

Decision

ICC Judge Barber held as follows:

1. At all material times Mr. Michie knew the Property was worth significantly more than the price he paid for it.

2. The Company was clearly insolvent at the time of purchase and it was not in the interests of creditors as a whole for Mr. Michie to purchase the Property off market at significantly below market value.

3. Mr. Michie would not be granted relief under **s1157 CA2006** on the grounds that he acted honestly and reasonably and that having regard to all the circumstances of the case he ought fairly to be excused.

4. In the absence of any relief under **s1157** an institutional constructive trust arose by which Mr. Michie held the Property on trust for the Company in liquidation. He was given an allowance for the purchase price of £120,000 paid by him.

5. Mr. Michie also claimed that he had spent £20,000 on repairs. As the Company's books and records were incomplete and that was not the responsibility of Mr. Michie, this was a factor taken into account in allowing Mr. Michie £20,000 for the repairs/improvements that he claimed he had carried out.

6. With regard to the other claims these were eventually calculated at £65,513 plus interest which Mr. Michie was ordered to pay to the Company.

Comment

- Normally where an asset is found to have been sold at an undervalue by the insolvency practitioner in office, this will lead to the claim for misfeasance being brought against the administrator/liquidator alone or jointly with any directors involved. In this case, as the former administrator/liquidator was bankrupt, there was little point in pursuing such a claim.

- The claim for alleged repairs/improvements carried out by the director of the Property although not fully substantiated by evidence, was nevertheless allowed as it was found that the lack of records was not something that could be attributed to the director. Instead, the Judge relied on other factors such as the difference in valuation prepared by the single joint expert, the fact that the sales marketing particulars for the Property had referred to significant repairs/improvements, and the fact that the works were carried out by friends/associates of the director and as such the repairs were handled on a less formal basis.

- The facts of this case are somewhat unusual but nevertheless directors may consider resigning as directors following entering into a formal insolvency process to avoid any such claim that they continue to owe fiduciary duties to the company pursuant to the provisions in the **Companies Act** post insolvency.

Voluntary Arrangement

Brittain v Chamberlain [2020] EWHC 1648 (Ch)

Can liquidators with a contingent claim prove in a CVA?

Facts

North Point Global Limited (the "Company") entered a CVA on 7 September 2017. Baltic House Developments Limited ("BHD"), a subsidiary of the Company, was wound up by the court on 17 May 2018 and the Applicant liquidators appointed.

The liquidators of BHD submitted a proof in the CVA dated 18 February 2020 based on a preference claim under **s239** of the **Insolvency Act 1986** ("**IA1986**") in respect of payments made by BHD to the Company for £841,000. The supervisor rejected the proof and the liquidators' appealed against that decision.

The questions the court had to determine were:

1. Are the liquidators bound by the CVA under **s5(2) IA1986**?
2. If they are bound by the CVA are the liquidators entitled to prove as creditors in the CVA?

S5(2)(b) provides as follows:-

> "(2) The voluntary arrangement—
>
> (b) binds every person who in accordance with the rules—
>
> (i) was <u>entitled to vote</u> in the qualifying decision procedure by which the creditors' decision to approve the voluntary arrangement was made, or
>
> (ii) would have been so entitled if he had had notice of it, as if he were a party to the voluntary arrangement."

The supervisor argued that the liquidators of BHD were not liquidators at the time and that if notice had been given to them they would not have had any entitlement to vote. As such they are not bound by the CVA.

The Company's business operated through a number of subsidiaries. BHD was a special purpose vehicle for the purpose of making sales at Baltic House, Norfolk Street Liverpool. This involved selling individual student apartments to investors. Most of BHD's funds were paid to connected parties prior to liquidation. The property involved was sold and the proceeds used to discharge secured creditors. There were no significant assets in the estate.

BHD had originally lodged a proof in the CVA voting in favour. Subsequently the supervisor reported that the directors had received tax advice and that they now proposed to raise invoices to clear inter-Company loans and rectify the position and that the accounts would be amended and re-filed.

There were then a series of variations to the CVA which were approved by creditors. During the course of the variations it was reported that claims from associated creditors including the one from BHD had been withdrawn. In the meantime, the liquidators lodged a revised proof in respect of inter-Company payments. The supervisor subsequently rejected that proof reasoning that the payments made by BHD were in respect of expenses incurred by the Company on behalf of BHD. The liquidators responded by expressing concern at the rejection of their claim and raising a claim by way of preference against the Company.

The supervisor's response was that the right to a preference claim did not arise until such time as the liquidators were appointed, which was after the approval of the CVA. The supervisor continued that as a post CVA debt, it was not provable in the CVA. The liquidators contended that the preference claim was a contingent claim and that they were entitled to make the claim which was submitted in the name of BHD. There then followed correspondence between the supervisor's solicitors and the solicitors acting for the liquidators in which evidence of intention to prefer together with evidence of insolvency was requested. On the latter point the liquidators relied on the proof of HMRC showing sums due from 2015 onwards. The liquidators' proof by way of preference was also rejected, and the liquidators appealed against that rejection.

The court considered **Re T&N Limited [2005] EWHC 2870 (Ch)**. In that case the company had been involved in asbestos mining which had resulted in employees claims for asbestosis. David Richards J held that future tort claimants were contingent creditors and therefore "creditors" for the purposes of CVA's. Such claims were contingent liabilities however future asbestos claims were not provable debts in the winding up of T&N. This turned on the provisions of the **Insolvency Rules 1986 ("IR1986"). R12.3 IR1986** which whilst it included contingent claims such as future asbestos claimants, the Rule required that claims be provable as "debts". This meant looking at **r12.3 IR1986** and further, **r13.13 IR1986**.

In particular **r13.12(2)**:

> "(2) In determining for the purposes of any provision of the Act or the Rules about winding up, whether any liability in tort is a debt provable in the winding up, the company is deemed to become subject to that liability by reason of an obligation incurred at the time <u>when the cause of action accrued</u>."

In **T&N** it was decided that the effect of that clause was to exclude as provable debts tort claims where the loss had not accrued (and therefore the cause of action in tort had not arisen) prior to the date of liquidation. The result being that contingent tort claims are provable provided that the cause of action accrued before the liquidation date.

Decision

Are the liquidators bound by the CVA under s5(2) IR1986?

It was accepted that a preference claim is both a contingent debt (whether or not provable) falling within the CVA regime, and one that is in fact provable in a bankruptcy or liquidation. At the time of the CVA BHD clearly had entered into a legal relationship with the Company having paid sums to it in satisfaction of debts. Further it must be assumed that it was then insolvent and that liquidation and a preference claim was likely.

The Judge noted that as far as possible debts should be brought within the CVA regime. With this in mind, the preference claim should be treated as a debt falling within the CVA regime. Further such a class of contingent claims are bound by the CVA. If the liquidators had been in office at the time the CVA was approved they would be bound. As such the liquidators claim are bound by the CVA in this case.

Are the liquidators entitled to prove as creditors under the CVA?

In answer to this question, the court held that the liquidators' claim as a contingent debt is a provable debt under the CVA.

This just left the question of valuation of the claim. Whilst the liquidators argued the supervisor had been hostile and was therefore unsuitable to value the claim, the court did not consider that that argument took the case out of the norm and as such the question of valuing their contingent claim would fall to the supervisor.

Comment

- Initially the application had been brought in the name of one of the liquidators only even though it was a joint appointment. On this point the court made it clear that notwithstanding the power to act joint and severally, the claim must be pursued in the joint names of both liquidators.

- The proof which detailed the preference claim had been submitted in the name of BHD and not the liquidators. Whilst ultimately no point was taken on it at the hearing itself, nevertheless the proof for the preference claim should have been in the name of the liquidators and not BHD.