CARRICK | READ
INSOLVENCY LAW FIRM

UPDATE

June 2016

Welcome to the CRI Insolvency Law Update, a summary of recent judgements and insolvency related reports and news items which we hope you will find of interest

Professional privilege

A recent case has involved consideration of an important point of principle being whether and to what extent a Trustee in Bankruptcy is entitled to obtain documents which were the subject of legal professional privilege in favour of the bankrupt prior to his bankruptcy.

Prior to this case it had always been assumed that a Trustee simply stepped into the shoes of the bankrupt and acquired the benefit of any privilege formerly exercisable by the bankrupt .

In this case the Court ruled that the Trustee had in fact only acquired the benefit of a bankrupt's legal professional privilege with respect to one of three categories of document. The Court provided a detailed judicial analysis as to what a Trustee can and cannot obtain by way of papers and the case will have significant repercussions for Trustees and their investigative processes.

See *Shlosberg v Avonwick Holdings Limited & Others (2016) ECHC1001(CH)*

Pension Drawdown

The bankrupt had elected to withdraw an amount from his pension fund which he was using to pay his household expenditure. He had historically elected to withdraw the maximum amount from his pension fund and was therefore held to be entitled to the maximum withdrawal each year for the purposes of an application for an Income Payments Order.

Carrick Read Insolvency is a specialist insolvency law practice providing legal and technical advice to insolvency practitioners, debtors and creditors involved in the insolvency process.

Carrick Read Insolvency Solicitors
12 Park Place,
Leeds LS1 2RU
T: 0113 246 7878
F: 0113 243 9822
E: thepartners@carrickread.com

The Court also considered whether the bankrupt was entitled to pension funds held in drawdown when no election had been made as to how the funds should be applied. Adopting the decision in *Houghton v Henry* the Court determined that if an election had not been made the mere existence of a drawdown fund was not sufficient to establish an entitlement for the purposes of an Income Payments Order.

See *Hinton v Wotherspoon (2016) EWHC 623 (Ch)*

Issue of Proceedings

The SBEE 2015 removed the requirement for Liquidators to obtain sanction for the issue or defence of proceedings. In this case the Liquidator wished to bring proceedings against BIS which it alleged had caused a loss to the company of $26M. Over 99% of the creditors were opposed to the claim being pursued. The largest creditor HMRC thought it inappropriate and too politically sensitive for the proceedings to be issued.

The Court determined that the following points should be utilised as a guideline:-

1) A decision by Liquidators whether to commence proceedings is essentially a commercial decision which they should take without obtaining sanction from the Court or the Liquidation committee and the Liquidators should act in what they believe to be the best interests of the company and all those who have an interest in its estate.
2) The Liquidators may, but are not obliged, to consult the creditors;
3) Liquidators should normally give weight to the reasoned views of the majority of creditors provided they are uninfluenced .
4) If there is a unanimous view the Liquidators should ordinarily give effect to it.
5) The Court should not generally become involved in giving directions on commercial decisions.
6) The Court should not generally interfere with commercial decisions of Liquidators after the event unless it was a decision taken in bad faith or one that no reasonable Liquidator could have taken.

On the basis that this was an unusual case the Court considered that if there was a creditor even for comparatively small amounts who would lose the opportunity for a material increase in distribution if the claim was not pursued then the decision by the Liquidators that the company should pursue the claim at no financial risk with the assistance of funding could be within the range of decisions that a reasonable Liquidator could take.

See *Longmeade Limited (2016) EWHC 356 (CH*)

Solicitors Costs in Administration

The Court of Appeal determined that Administrators could agree to pay appointed solicitors fees both before and after the end of the administration without the need for any authority to do so under Rule 7.34(1) of The Insolvency rules 1986.

The Administrators had employed a firm of solicitors and agreed their fees . The company was wound up and the Liquidators were

appointed and shortly thereafter the Administrators approved the solicitors final invoice which post-dated the Liquidators appointment. The Liquidators had applied to the Court for an Order for a detailed assessment of the costs . The Court of Appeal dealt with applications concerning the Judge's decision not to order a detailed assessment of the fees and an appeal by the solicitors against an Order that the final invoice had not been properly approved.

The solicitor's appeal was allowed and the Court of Appeal determined that if the Liquidators did not agree with the fees that had been paid then they could bring misfeasance proceedings against the Administrators. There was no power by which Liquidators could require the assessment of costs made in an earlier administration.

See *Hosking & Another v Slaughter and May (2016) EWCA CIV474*

Guidance on the going concern basis of accounting

Further to the case of *Ralls Builders Limited (in Liquidation)* referred to in our March newsletter the Financial Reporting Council has issued new guidance on the going concern basis of accounting and reporting on solvency and liquidity risks.

The new guidance was issued on 18th April 2016 and is aimed at directors of companies that do not apply the UK Corporate Governance Code

The guidance focuses on disclosures that are material and emphasises that information is material if its omission or misrepresentation could be reasonably expected to influence the economic decisions of users. Further detail is provided in FRS 102.

Failure of Voluntary Arrangements

Supervisors applied to the Court for the bankruptcy of the debtor on the basis that she had breached the terms of the IVA by failing to disclose the existence of a known creditor and also re-mortgaged her property.

In the first instance the Judge used her discretion not to grant a Bankruptcy Order and the Supervisors appealed.

On appeal Mrs Justice Proudman held that the discretion had to be exercised in accordance with legal principles and the primary concern lay in the interests of the creditors and the debtor's transparency was essential. Generally a debtor would be made bankrupt if they defaulted on payments. In this case the debtor had persuaded the creditors to agree to the IVA and then misled them and in the circumstances a Bankruptcy Order should be made.

See *Varden Nuttall Limited v Michelle Louise Baker (2016)*

Regulating conflicts between Administrators and Liquidators

The Court allowed the winding up of eight companies in the same group and considered the statutory powers of the Court to appoint Liquidators, to approve a memorandum of understanding between the new Liquidators dealing with allocation of work and to grant

the Administrators their discharge. The case reinforced the framework established by paras 98 and 75 of Schedule B1 Insolvency Act 1986 and the need for Liquidators to ensure that matters against previous office holders are investigated promptly and proportionately in terms of costs.

See *Angel Group Limited & Others (2015) EWHC 3624 (CH*)

Third Parties (Rights Against Insurers) Act 2010

A statutory instrument has recently been passed providing that the Third Parties (Rights Against Insurers) Act 2010 will come into force on the 1st August 2016 some six years after it was first passed.

The Act will replace and generally streamline procedures previously in place. The most significant changes will be:-

1) The Act will allow a Third Party with a claim against an insolvent company to proceed directly against the insolvent company's insurer without having to first proceed against and establish the liability of the insolvent company.
2) A Third Party will be allowed to request information in relation to the relevant insurance policy from the insured provided that the Third Party reasonably believes that the insured has incurred a liability to it.

Matrimonial Orders

After failing to pay his builders , the debtor who subsequently became bankrupt charged the Property to his father and sister in law. His wife divorced him and the property was put in trust for the benefit of the debtor's children with his ex-wife having exclusive occupation as part of the divorce settlement Court order.

Subsequently a Bankruptcy Order was obtained against the debtor.

The Trustee in Bankruptcy issued proceedings claiming the charges were void and shams and that the divorce settlement in respect of the property was a transaction at an undervalue or a transaction to defraud creditors.

The Judge followed the Court of Appeal decision in *Hill v Haines* and held that an Order for ancillary relief whether by consent or not cannot be challenged as a transaction at an undervalue unless there was a factor that would effect its validity such as fraud, mistake, misrepresentation or collusion. The Court found that the charge granted to the father was void as a sham but that the charge to the sister in law was valid.

See *Sands v Singh (2016) EWHC 636 (Chancery*)

Offers Pending Bankruptcy

The bankrupt offered to compound the debt prior to the hearing of a Bankruptcy Petition against him and sought to appeal his bankruptcy on the basis that the Judge incorrectly held that the petitioning creditor did not act unreasonably.

The Court determined that for the rejection of an offer to be held unreasonable it must be shown that no reasonable hypothetical creditor would have rejected the offer.

.

It is an objective test. In this case it was not considered that the petitioning creditor had acted unreasonably as the bankrupt's offer to compound the debt extended to less than a quarter of his liability.

See *Brian Herbert Cooke v Dunbar Assets Plc (2016) EWHC 579 (CH).*

Challenge to the Appointment of Administrators

Administrators were appointed to a company by Nationwide. Some years after the Administration two creditors challenged the appointment of the Administrators.

The security under which the Administrators were appointed was granted in relation to a property purchase loan. Another lender CHL had the benefit of a prior floating charge security over present and future assets. CHL's security provided for automatic crystallisation of the CHL floating charge and it was argued that the Nationwide security was created in breach of a clause in the CHL floating charge and that the CHL security crystallised immediately before the Nationwide security was granted. In those circumstances there would be no assets over which the Nationwide security could attach.

The Court held that the Nationwide security and the appointment of the Administrators was valid. Where monies are loaned for property purchase and a related security is taken, the purchase of the property and the granting of the security are one indivisible transaction. The assets to which the Nationwide security related were never subject to the CHL security.

See *Property Edge Lettings Limited (2015) EWHC 4069*

Section 236 Order against resident abroad

The company was placed into compulsory liquidation and prior to liquidation it transferred monies to a trust located in Hong Kong. The Official Receivers as Liquidator applied for an order under Section 236 (3) Insolvency Act 1986 that the principle Trustee, resident in Hong Kong, produce a Witness Statement with supporting documents in relation to the company's affairs.

The Court was required to ascertain whether Section 236 could have exterritorial effect and decided that the Court should apply a balancing exercise to determine whether an order under Section 236 was appropriate and whether it imposed any unnecessary or unreasonable burden on the respondent.

In this case it was concluded that an order for the production of a witness Statement would be made against the person resident abroad.

See *Re Omni Trustees Ltd (in Liquidation) (No. 2) [2015] EWHC 2697 (Ch)*

Surrender of Lease

A tenant had gone into administration and two months into the administration, the Administrators vacated the premises stating that the tenants ceased to have responsibility for the premises. A month later the Administrators returned the keys saying that the premises were not being used and offering surrender for no payment.

The landlord took steps to secure the premises.

Carrick Read Insolvency

Newsletter June 2016

A year on, the landlord marketed the premises through agents whose marketing particulars offered a long leasehold with vacant possession.

After six weeks the premises were removed from the market.

It was held that the landlords actions did not amount to an acceptance that the lease was at an end. Of particular interest is the fact that acceptance of the keys by the landlord did not indicate a surrender. The Court held that one party has to hold the keys to prevent the pointless passing of the keys back and forth as the parties seek to avoid making any admissions.

The case highlights the need for unequivocal conduct on the part of both parties for a surrender by operation of law to occur.

See *Padwick Properties Limited v Punj Lloyd Limited (2016) ECHC 502 (CH).*

Voluntary redress payments are not caught by a paragraph 99 charge

The company was dissolved in 2012 and the National Westminster Bank made a provisional determination of redress relating to interest rate swaps entered into by the company. NatWest indicated that it would make a formal offer of redress capable of acceptance by the company if the company was restored to the register. The Administrators of the company sought an order that NatWest pay the redress direct to them without requiring the company to first be restored. They argued that they were the only ones with an economic interest in the redress payment.

The Court determined that NatWest was not under any obligation to pay the redress , it being an informal voluntary offer to pay and it was not an asset of the company falling under the.

Paragraph 99 charge. In those circumstances it was either for the directors or Liquidators to deal with or collect in and distribute the redress payment.

See *Walker & Another v National Westminster Bank Plc (2016) EWHC 315 (CH).*

Lease Value

Carrick Read was recently involved in the case of *Re Crosscastle Limited* which required the Court to determine the value of a lease sold in an administration sale. The company operated two Spar brand convenience stores in Battersea subject to leases. A creditor had loaned money to Crosscastle secured by two charges over the lease of one of its two premises. There was no mention of goodwill in the charges.

Pursuant to the administration the whole of the business was sold.

The business passed into liquidation and the lender and the Liquidator could not agree upon the value of the charges subsequent to which the Liquidator applied for directions. The issues to be determined by the Court were :-

1) What proportion of the goodwill of the business attached to the lease and;
2) What was the value of the lease plus any adherent goodwill.

Experts appointed differed widely in their assessment of the value of the relevant goodwill but the experts agreed that the value of the lease of the premises if sold separately as an empty unit was nil or nominal. The only real value was in the adherent goodwill.

The Court held that the proportion of goodwill adhering to a lease was a question of fact. It

determined that given the type of business operated by Crosscastle 50% of the goodwill of the business carried on at the premises adhered to the lease.

Practitioners should be aware that even where a lease has little or no value if sold by itself, security over such lease may still be valuable.

Re Crosscastle (2016) (unreported)

The contents of this Update provide only a brief overview of the more important cases and reports. If you should require any detailed advice concerning these changes then please do not hesitate to contact us.

Contact Details

For more information or to discuss how we may be able to assist your business, please contact:

Andrew Laycock
T: 0113 3804313
F: 0113 2439822
E: ALaycock@carrickread.com

David Barker
T: 0113 3804312
F: 0113 2439822
E: dbarker@carrickread.com

Jennie Blagg
T: 0113 3804893
F: 0113 2439822
E: JBlagg@carrickread.com