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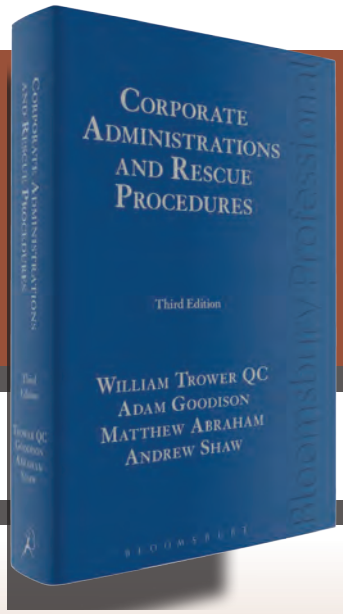


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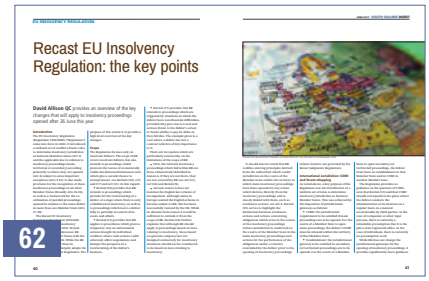


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FROM THE **EDITOR**

MARK ARNOLD QC

# "The breath of an unfee'd lawyer"

Welcome to the June edition of the South Square Digest.

Once more this happy breed of men and women have gathered together to decide what is best for this sceptred isle, this precious stone set in the silver sea, this blessed plot, this nook-shotten isle of Albion. It is the third time our democracy has spoken since 2015. In the first, having tasted coalition government, we decided to return David Cameron and the Conservatives to power, without their Liberal Democrat partners. In the second, a year ago, we decided to leave the European Union. David Cameron relinquished the reins of power; Theresa May took them up. She told us Brexit meant Brexit; served notice of our decision to quit; made ready for a hard Brexit; then, with a working majority of 17 and a 22-point lead over Labour, turned to us and asked: "Are you with me?" And back came the answer: "Erm. No, actually. We're not."

Given a choice between Theresa May's promise of "strong and stable leadership" and Juggernaut Jeremy's vision of government "for the many, not the few", we have effectively chosen neither, or both, and Parliament is hung. Whether Mrs May will be able to work something out with any of the other parties, the DUP in Northern Ireland being perhaps the most likely candidate at the time of writing, remains to be seen, as does her ability to remain in office. Certainly her authority is severely damaged.

An obvious priority for the new government (whoever it is formed by) will be security, and there is much to be done. Following the three recent atrocities at Westminster, the Manchester Arena and, most recently, London Bridge, uppermost in peoples' minds are the victims, their families and friends. Actions speak louder than words at such times, which – horrific as they are – still manage to bring out the best of humanity as strangers instinctively become neighbours.

Shock and disgust at acts of such murderous barbarity turn inevitably to anger and thoughts of retribution. How is a civilised society to deal with the perpetrators of such monstrous attacks on its people? The answer is in the question: in a civilised way. But what does that mean? The problem lies in the fact that the law is helpless when there can be no trial before judge and jury of these killers, who are themselves already dead. Justice in their cases has been denied its object, as they no doubt intended. Attention will inevitably turn to what more can be done to protect people and prevent repetition. As the line drawn between the need to keep society safe

THERESA MAY: WHAT NOW?

and the rights and freedoms of the individual comes under renewed scrutiny, it seems inevitable our human rights laws will be reviewed. So be it, but we will do neither ourselves nor the rule of law any favours if, when doing so, we mistake haste for efficiency.

I understand that the message "keep calm and carry on" (now to be found on mugs, tea-cups, plates and postcards, and who knows what other merchandise) originally graced a poster designed by the Ministry of Information in 1939 to encourage Londoners before the Blitz. At the time, it appears, it was little used as it was considered patronising. Nevertheless, it seems to strike a chord in the British psyche at times like this; there is, of course, no reason whatever to think the British peoples are alone in that regard, although we may sometimes like to think so. It is not to be confused with an invitation to do nothing, to lower our guard, to reduce our vigilance. Nor does it mean we should carry on as if nothing had happened.

The Mayor of London, Sadiq Khan, recently said much the same thing when, following the atrocity at London Bridge, he said there would be more armed police on our streets in the following days, adding that there was "no need to be alarmed". It appears that this may have been misunderstood, or possibly misinterpreted, in some quarters. There again, words mean different things to different people, especially when deprived of context. "When *I* use a word," said Humpty Dumpty to Alice (*Through the Looking-Glass*), "it means just what I choose it to mean – neither more nor less." Quite so. We over here are still experiencing some difficulty with "covfefe".

Another high priority, of course, will be Brexit itself. Negotiations are supposed to start on 19th June, but it is difficult to see how, in any meaningful sense, they can. Plans for a hard Brexit are plainly not what the country wants; at least it is not clear that they are. Hopes for a strong base from which Mrs May could negotiate on our behalf

MIDDLE TEMPLE HALL

disappeared in the same puff of smoke in which her majority vanished. So what happens now? The government must surely go back to the drawing-board. But notice having been given, the clock is ticking, and time is no longer on our side.

The legal implications of Brexit will form a major topic for discussion at the International Insolvency Institute (III) Conference here in London, commencing on 18th June, jointly chaired by Mark Phillips QC and Tony Bugg. Following a day of debate over some nice sharp quillets of the law, a Legendary Dinner will take place in Middle Temple Hall, at which the III 2017 Outstanding Contributions Award will be presented to Michael Crystal QC, to whom we all send our heartiest congratulations.

Middle Temple Hall is a place where, having striven mightily as adversaries do in law, barristers eat and drink as friends. Shakespeare's Twelfth Night was first performed there for Queen Elizabeth I, in 1602. Extracts will be performed again at the Legendary Dinner. Shakespeare was obviously no stranger to Middle Temple. Its rose garden is famously the setting for the scene in Henry VI (Part 1, Act 2, Scene 4) when, with the plucking of a white rose and then a red, the rivalry between the Houses of York and Lancaster blooms and the Wars of the Roses begin. They will end – SPOILER ALERT – only on Bosworth Field after Richard III has tried, and failed, to swap his kingdom for a horse. At least according to Shakespeare from whom, according to Coleridge, we get our history (and our theology from Milton).

*'And do as adversaries do in law, Strive mightily, but eat and drink as friends'*

There is nothing fictional, however, about the other connections of which Middle Templars are rightly proud; not the least of which is that no fewer than five of their number were original signatories to the American Declaration of Independence, and seven signed the Constitution.

Shakespeare's admiration for lawyers is not as well-known, or indeed as evident, as it might be. True, the scene in the rose garden is attended by a lawyer; but she (or he: Shakespeare does not specify) does not say very much, and what she does say – although nicely caveated – is frankly not especially memorable. A prize for anyone who can spot her again, in Henry VI, Parts 1, 2 or 3. There is no reason to think Will subscribed to the views of Dick the Butcher in Henry VI, Part 2 (the first thing we do, let's kill all the lawyers **...**), however, as the context makes clear. I am deeply indebted to the Bard for all the otherwise unattributed, context-bereft but easily recognisable great lines in this piece, though it otherwise seem like the breath of an unfee'd lawyer.

For all the other great lines in this edition, read on. I draw your particular attention to the case digests which, as ever, have been carefully selected and prepared by South Square's excellent Juniors and edited by Hilary Stonefrost. Continuing the Brexit theme, Antony Zacaroli QC and I explore the possible consequences of Brexit for UK credit institutions in the insolvency context. It should not be forgotten, however, that Brexit (whatever form it takes) is still some way off and Europe remains highly relevant. Gabriel Moss QC looks at recent decisions of the CJEU, one concerned with the interrelation of a Dutch pre-pack and employment protection, the other with the meaning of "possession" or "control" in the context of the European financial collateral legislation. David Allison QC highlights the key changes introduced by the new European Insolvency Regulation, which will apply to insolvency proceedings opened from 26 June 2017.

Following his recent success in Gibraltar, David Alexander QC focuses on dishonesty in the context of two recent decisions on dishonest assistance in a breach of trust. Alexander Riddiford and Robert Amey have joined forces to unpack the recent decision of the Supreme Court in Waterfall 1, the latest step in the Lehman saga, which sees the demise of the so-called currency conversion claim (which, it transpires, never existed). Tom Smith QC and James Elliott of Harney Westwood & Riegels consider the divergence in approach adopted by the Cayman Islands courts to winding up petitions presented on grounds of "loss of substratum". William Willson reports on a recent decision of the English High Court as to the law of Jersey, which decides that claims against directors for breach of fiduciary duty are subject to a ten-year limitation period. Finally, Jeremy Goldring QC, John Briggs and Eduardo Lupi report on the recent INSOL and ILA Conferences.

Happy reading, and good luck with our barking South Square challenge. If you would like to be added to the circulation list (or your contact details have changed) please contact kirstendent@southsquare.com.

MICHAEL CRYSTAL QC

# Banking on Brexit

Antony Zacaroli QC and Mark Arnold QC analyse the potential impact of Brexit in the context of the insolvency regime as it relates to UK credit institutions[1]

With enterprise comes the risk of failure. Just as the one is to be encouraged, so the other must be managed, lest the failure of one should lead to the failure of others. As institutions, banks will inevitably be affected by insolvency at some stage. It will often be the insolvency of their customers or counterparties. Sometimes, however, it may be their own. The aim of this article is to analyse the potential impact of Brexit in the context of the insolvency regime as it relates to UK banks.

## The legislative framework

The relevant legislative framework comprises:

- Credit Institutions Reorganisation and Winding up Directive 2001/24/EC (*CIWUD*),
- Credit Institutions (Reorganisation and Winding up) Regulations 2004 (*2004 Regulations*, which implement CIWUD in the UK),
- Bank Recovery and Resolution Directive 2014/59/EU (*BRRD*),
- Banking Act 2009 (BA 2009), as amended by the Bank Recovery and Resolution Orders 2014/3329, 2014/3348 and 2016/1239 (which implement the BRRD in the UK).

*CIWUD and the BRRD: EU Member State credit institutions*

The purpose of CIWUD is to ensure mutual recognition of measures taken in relation to the reorganisation and winding up of credit institutions by the competent authorities of the Member State by which they are authorised to conduct business (the *home Member State*). With limited exceptions, it requires that measures which may affect third parties' existing rights be given effect by every other Member State regardless of the place in which any individual branch of the institution is located (the *host Member State*) or the law which governs the obligations which it has undertaken. CIWUD ensures that all assets and liabilities of the failing institution are dealt with in a single process in the home Member State. As appears below, CIWUD also applies to a decision involving the use of one of the resolution tools in respect of a failing institution introduced by the BRRD.

The BRRD was adopted in the wake of the financial crash of 2008. Its purpose is to

*1/. This article is based on part of a paper prepared by COMBAR on the possible consequences of Brexit for banks, in the insolvency context, to which both authors contributed (January 2017).*

THE OLD LADY OF THREADNEEDLE STREET

provide a minimum degree of harmonisation among EU Member States of the powers available to enable them to respond quickly and effectively to threats of that kind. The resolution authorities designated by each Member State (Art 3) are to have at their disposal a range of resolution tools and powers, which may adversely affect the rights of third parties, including shareholders and creditors.

CIWUD and the BRRD form part of an integrated set of European rules for dealing with failing financial institutions, under which measures taken by the home Member State are to be given universal effect throughout the EU, even in relation to obligations governed by foreign law.[2] In other words, it is for the home Member State to decide how to deal with a failing institution. Universal effect is achieved by CIWUD Art 3, pursuant to which reorganisation measures implemented in the home Member State are to be fully effective in every host Member State as soon as they become effective in the home Member State. Reorganisation measures for these purposes include the resolution tools and procedures provided for by the BRRD: CIWUD, Art 2. The CJEU has made clear that the definition of "reorganisation measures" is to be interpreted broadly: measures of a kind that do not fall within the scope of the BRRD can nevertheless constitute a reorganisation measure, with the consequences that flow from that.[3]

Similarly, recognition of measures taken

*2/. For an authoritative summary of the relationship between CIWUD and BRRD, see Guardians of New Zealand Superannuation Fund & others v Novo Banco SA; Goldman Sachs International v Novo Banco SA [2016] EWCA Civ 1092.*

*3/. Kotnik & Others v Državni zbor Republike Slovenije (Case C-526/14).*


ANTONY ZACAROLI QC

by the resolution authority of another Member State is expressly provided for in the BRRD, Art 66, which requires each Member State to ensure that the measures taken in the home Member State in respect of assets or liabilities in another Member State have effect in or under the law of the other Member State.

Universal effect throughout the EU is similarly achieved in relation to winding up proceedings (broadly defined) by CIWUD, Art 9. The law applicable to the reorganisation measures or winding up proceedings is generally that of the home Member State (CIWUD, Arts 3 and 10), subject to certain exceptions (Arts 20-27, 30-32). CIWUD (as amended by the BRRD) is incorporated into domestic law in the UK by the 2004 Regulations.

*CIWUD and the BRRD: Third Country credit institutions*

Both CIWUD (Arts 8, 19) and the BRRD (Art 67 and Title VI, Arts 93-98) make provision for Third Country credit institutions, which are incorporated into English law by Part 5 of the 2004 Regulations (Regs 36-38). For present purposes, a Third Country credit institution is one which has its head office outside the EU but which has set up a branch in a host Member State: CIWUD, Art 8; BRRD, Art 2(86). As incorporated into domestic UK law, it is a person which has permission under the Financial Services and Markets Act 2000 (FSMA) to accept deposits or to issue electronic money as the case may be, whose head office is not in the UK or an EEA State: 2004 Regulations, Reg 36(1)(b).

The provisions as they relate to Third Country credit institutions differ from those applicable to EEA institutions. The principal differences are addressed below.

## Pre-Brexit: the domestic UK position

UK banks for present purposes are those defined by the Banking Act 2009, s 2, namely UK institutions (with specified exceptions) which are authorised under Part 4A of FSMA to carry on the regulated activity of accepting deposits. The insolvency regime relating to UK banks is the Special Resolution Regime, for which the Banking Act 2009, Parts 1, 2 and 3 provide.

The Special Resolution Regime comprises:

- certain pre-resolution powers exercisable by the Bank of England: ss 3A and 3B, BA 2009;
- the five stabilisation procedures (BA 2009, Part 1, as amended and supplemented by the Bank Recovery and Resolution Order 2014/3329, which implements in part the BRRD), namely:
  - Transfer to a private sector purchaser
  - Transfer to a bridge bank
  - Transfer to an asset management vehicle
  - The bail-in option
  - Transfer to temporary public ownership;
- the bank insolvency procedure, which is based on a modified form of liquidation as

it applies to companies: BA 2009, Part 2; and

- the bank administration procedure, which is based on a modified form of administration as it applies to companies: BA 2009, part 3.

These powers and procedures fall to be exercised and implemented so as to ensure the continuity of banking services in the UK and other critical functions as well as other objectives set out in s 4 BA 2009 (see below).

The provisions of BA 2009 are supplemented by the 2004 Regulations, regulations 22 and 23-35. These provide that the general law of insolvency of the UK will apply to determine certain fundamental matters arising in the insolvency (the phrase used is "relevant winding up", but this extends to a UK CVA, administration, winding up or making of a stabilisation instrument: Reg 21(1)(b)), subject to certain exceptions (Arts 23-35). In substance, these provisions mirror those to be found in the Insolvency Regulations 1346/2000 (Arts 4, 5-15) and 2015/848 (Arts 7 and 8-18).

### Pre-Brexit: recognition within the EEA of the Special Resolution Regime applicable to UK banks

Where the UK is the home Member State, recognition in other Member States will be determined by reference to CIWUD, and the BRRD where applicable, and the domestic legislation by which the host Member State(s) concerned have given effect to the requirements of those directives. In summary:

*Reorganisation measures*

The UK's administrative or judicial authorities alone are empowered to decide on the implementation of one or more reorganisation measures in a credit institution, including branches in other Member States. Save as otherwise provided by CIWUD, the reorganisation measures will be applied in accordance with the laws, regulations and procedures applicable in the UK: CIWUD, Art 3.

It follows that such reorganisation measures are effective throughout the EU as soon as they become effective in the UK, and will be fully effective in accordance with UK law

*Pre-Brexit UK measures and proceedings are effective throughout the EEA...*

throughout the EU without further formalities, including as against third parties in other Member States: CIWUD, Art 3. Reorganisation measures for these purposes mean measures intended to preserve or restore the financial situation of a credit institution and which could affect third parties' pre-existing rights, and include the application of the resolution tools and the exercise of resolution powers provided for by the BRRD: CIWUD, Art 2. They would thus include (a) the five stabilisation powers and (b) bank administration, at least in some cases.

*Winding up proceedings*

The UK's administrative or judicial authorities alone are empowered to decide on the opening of winding up proceedings concerning a UK credit institution, including branches established in other Member States. A decision to open winding up proceedings taken by any court in the UK will be recognised without further formality, within the territory of all other Member States, where they will be effective as soon as the decision becomes effective in the UK: CIWUD, Art 9.

In such cases, the UK bank would be wound up in accordance with the laws, regulations and procedures applicable in the UK (CIWUD, Art 10), subject to certain exceptions (CIWUD, Arts 20-27 and 30-32). Whatever may be the precise nature of the procedure adopted as part of the Special Resolution Regime in respect of a UK bank, therefore, it will be automatically recognised and given effect throughout the EU, including in relation to its branches established in other Member States.

### Pre-Brexit: recognition in the UK of measures and proceedings relating to non-UK EEA credit institutions.

For completeness, as regards non-UK EEA credit institutions:

- reorganisation measures and winding up proceedings taken or opened in another Member State as the home Member State of the institution concerned will be recognised and take effect in the UK: Reg 5 of the 2004 Regulations;
- since 5 May 2004, such an institution (or any of its branches) cannot be wound up or put into administration or become subject to a company voluntary arrangement in the UK: Reg 3 of the 2004 Regulations; and
- schemes of arrangement may not be proposed or sanctioned if the institution (or branch) is already subject to a directive reorganisation measure or directive winding up proceedings unless the requisite notices have been given and no objections have been received: Reg 4 of the 2004 Regulations. In the absence of any such measure or proceedings, however, it follows that schemes of arrangement may be proposed and sanctioned in respect of EEA institutions, which are to be regarded as companies liable to be wound up under the Insolvency Act 1986 for this purpose: Reg 4(1) of the 2004 Regulations.

### Post-Brexit: the domestic position

As the domestic insolvency regime relating to UK banks is contained within domestic legislation (BA 2009), there is no reason why the domestic position should change post-Brexit, whether or not the UK remains an EEA State, with access to the Single Market, or becomes a Third Country (ie a non-EEA State). This will be so unless and until the Banking Act 2009 itself is revised, amended or repealed.

Whether recognition will be accorded elsewhere in the EU to the Special Resolution Regime applicable to UK banks, whatever form it may take, however, will depend on the UK's status following Brexit. This is addressed below.

### Post-Brexit: recognition within the EEA of the Special Resolution Regime applicable to UK banks

*Post-Brexit, if the UK remains within the EEA, there would be no change*

Much will depend on the UK's status following Brexit. If it were to remain within the EEA with access to the Single Market, CIWUD and BRRD would continue to apply as they do now with the result that the Special Resolution Regime applicable to UK banks would continue to be automatically recognised and given effect throughout the EU/EEA.

If the UK were no longer to be a member of the EEA, however, the position would be different: the domestic Special Resolution Regime applicable to a UK bank would no longer be the subject of, nor entitled to, automatic recognition throughout the EEA/EU because CIWUD, Arts 3 and 9 would no longer apply. In such circumstances, the UK would instead be a Third Country for the purposes of CIWUD and BRRD.

*BRRD: Third Country resolution proceedings*

In the context of resolution proceedings relating to a UK institution, the consequences of the UK being a Third Country under the BRRD would include the following:

- The Commission may submit proposals for the negotiation of an agreement with the UK as a Third Country regarding the means of cooperation between resolution authorities and the relevant UK authorities for the purpose of information-sharing in connection with recovery and resolution planning in relation to qualifying institutions and cooperation in carrying out tasks and exercising the powers referred to in Art 97 (considered below): BRRD, Art 93(1)-(3).
- Unless and until the Commission does so, Member States may enter into bilateral agreements with the UK in relation to such matters, but such arrangements must be consistent with BRRD provisions governing relations with Third Countries: BRRD, Art 93(4).
- Under BRRD Art 94, unless and until an international agreement is negotiated between the Commission and the UK, or if such an agreement (once concluded) does not extend to recognition and enforcement of UK resolution proceedings,


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arrangements relating to the recognition and enforcement of UK resolution proceedings where the UK institution or parent undertaking has subsidiaries or branches in relevant EEA States will be a matter for:

- the European resolution college established in accordance with BRRD Art 89 (if there is one), in which case national resolution authorities will be obliged to seek enforcement of the UK resolution proceedings, once they have been recognised by the college, in accordance with their national law;
- the same will apply where the UK institution has assets, rights or liabilities which are located in two or more Member States or governed by the law of those Member States;
- in the absence of a joint decision by the college, or if there is no college, the resolution authority of the Member State concerned, giving due consideration to the interests of each Member State where the UK institution operates.

■ The resolution authorities of relevant Member States would have certain minimum powers to (amongst other things) take their own resolution action in relation to:

- assets belonging to the UK institution which are located in their Member State or governed by its law; and
- rights or liabilities of the UK institution that are booked by the branch of that institution in their Member State or governed by its law, or where claims in relation to such rights and liabilities are enforceable in their Member State (BRRD, Art 94(4)).

■ In each such case, recognition and enforcement of UK resolution proceedings would be without prejudice to any normal insolvency proceedings under national law applicable (where appropriate) under the BRRD: Art 94(6).

*If the UK becomes a Third Country, a different regime will apply...*

- Recognition or enforcement may be refused in respect of any UK resolution proceedings in the circumstances set out in BRRD, Art 95. These include circumstances where the college or relevant resolution authority considers that the UK resolution proceedings would have an adverse effect on financial stability in the relevant Member State, if they think independent resolution action is necessary, or that the effects of such recognition or enforcement would be contrary to national law.
- The resolution authorities of the Member States concerned will have power to take unilateral action in relation to the branch of the UK institution located in those Member States if there are no applicable resolution proceedings in the UK or, if there are resolution proceedings in the UK, grounds to refuse recognition or enforcement have arisen under Art 95, if certain conditions are met: BRRD, Art 96.
- Unless and until an international agreement is negotiated between the Commission and the UK, or if such an agreement (once concluded) does not extend to co-operation with the UK in respect of the matters set out in BRRD, Art 97:
  - The European Banking Authority *(EBA)* may conclude general non-binding co-operation arrangements with the relevant UK authorities, but not so as to impose any legal obligations on Member States: BRRD, Art 97(2).
  - The EBA framework cooperation arrangements, if made, would establish processes and arrangements for sharing information necessary for, and cooperation in carrying out, various tasks and powers, including the development of resolution plans under UK law, and the application of resolution tools and the exercise of resolution powers exercisable under UK law: BRRD, Art 97(3).
  - It would be for the competent authorities or resolution authorities of individual Member States themselves to conclude non-binding cooperation arrangements with the relevant UK authorities in line with the EBA framework arrangements. However, this would not prevent any Member State from concluding a bilateral or multilateral arrangement with the UK, in accordance with Regulation (EU) No 1093/2010, Art 33: BRRD, Art 97(4), (5).
- Member States will be obliged to ensure that the exchange of confidential information with relevant UK authorities will be subject to strict requirements, the object of which will be to ensure that confidentiality is maintained: BRRD, Art 98.

It will be apparent from this summary that there can be no assurance that recognition and enforcement of resolution proceedings relating to a UK institution will be subject to the same regime as that which currently applies, nor that recognition and enforcement (if obtained) would have the universal effect currently required in other EEA States. The absence of certainty may have a material impact on the outcome of any UK resolution proceedings in those cases where the UK institution operates (whether through a branch or subsidiary) in another Member State, or has assets in, or rights or liabilities governed by the law of, a Member State, or enforceable in a Member State.

*...and there can be no assurance that UK measures and proceedings would be recognised and enforced in other EEA states*

*CIWUD: Third Country winding up proceedings*

CIWUD makes no provision for the recognition and enforcement in a Member State of winding up proceedings (widely defined) opened in a Third Country, nor for the prevention of the opening of such proceedings in relation to a branch or

subsidiary of a Third Country institution by the administrative or judicial authorities of the host Member State. On the contrary, CIWUD, Art 19 specifically contemplates that the relevant authorities of the host Member State may open winding up proceedings in relation to a branch of a Third Country institution. A similar position prevails in respect of reorganisation measures (CIWUD, Art 8), albeit this would be supplemented by the BRRD Third Country provisions outlined above.

In the context of winding up proceedings (widely defined to include a CVA or administration) in respect of a UK institution, therefore, recognition would depend on the conflict of laws rules prevailing in the relevant Member State unless that Member State has adopted the UNCITRAL Model Law. As matters stand, only four other Member States have done so (Poland, Greece, Romania and Slovenia). It is worth noting, however, that when adopting the UNCITRAL Model Law, countries can exclude credit institutions. Thus, for example, as adopted by the UK, the Model Law does not apply to a proceeding concerning a UK, EEA or Third Country credit institution: CBIR Sch 1, Art 1(2)(h) and (i). It is to be expected that other countries may do the same.

Enforcement will also depend on the conflict of laws rules prevailing in the relevant Member State. Even if the Model Law has otherwise been adopted by that Member State, its provisions do not currently extend to enforcement of judgments and orders made in another state.

## Post-Brexit: recognition within the UK of the resolution, reorganisation and winding up proceedings applicable to EEA institutions

The position as it relates to UK institutions, in the event the UK becomes a Third Country for the purposes of CIWUD and BRRD, is to be contrasted with the position as it would relate to banks and credit institutions formed and authorised in other Member States. Whether or not the UK remains an EEA State or qualifies as a Third Country, the 2004 Regulations would continue to apply to any non-UK EEA Institution (unless and until revised, amended or repealed as a piece of domestic legislation). That being so, the position in the UK in respect of such institutions would remain as it is at present, as summarised above[4].

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In consequence, there would be a structural imbalance and, depending on what (if any) arrangements are put in place between EEA States and the UK as a Third Country, an absence of reciprocity. Recognition and enforcement in an EEA State of resolution, reorganisation and winding up proceedings applicable to UK institutions will depend on the conflict of laws rules prevailing in that EEA State. These may not always be clear. Certainly the uniformity and predictability characteristic of the regime put in place by CIWUD and BRRD will be lacking, with potentially serious consequences for the UK institution itself, as well as those likely to be affected if it were to fail.

*4/. In addition, assistance would (if necessary) be available in the UK in respect of a credit institution from Ireland or Gibraltar, under s. 426 of the Insolvency Act 1986.*

# Supreme Court hands down judgment in Waterfall I

**Alexander Riddiford** and **Robert Amey** report on the recent Supreme Court decision in the long-running Lehman Waterfall litigation: *The Joint Administrators of Lehman Brothers Limited (Appellant) v. Lehman Brothers International (Europe) (In Administration) and others (Respondents)* [2017] UKSC 38

In September 2008, at the height of the worldwide financial crisis, various members of the Lehman Brothers group of companies entered insolvency proceedings around the world. The group's main trading company in Europe was Lehman Brothers International (Europe) ("LBIE"). Its shares were held by LB Holdings Intermediate 2 Ltd ("LBHI2") and Lehman Brothers Ltd ("LBL").

LBIE and LBL entered administration in September 2008, and LBHI2 entered administration in January 2009. The administration of LBIE has two unusual features. First, LBIE has sufficient assets to pay all its external creditors. It is therefore a solvent, distributing administration. This has given rise to a number of interesting and unusual legal questions as to what should be done with the surplus remaining after payment of proved debts. Secondly, LBIE was an unlimited company (apparently for tax reasons). This has given rise to complex questions as to the rights of creditors who are also potentially liable in their capacity as shareholders.

In February 2013, the administrators of LBIE, LBL and LBHI2 issued proceedings seeking directions from the Court on a number of questions relating to the administrations, in particular the order in which various liabilities of LBIE and its administrators should be paid. As a result, this application became known as the Waterfall application (consequent applications arising out of the Waterfall application have become known as the Waterfall II and Waterfall III applications).

More than four years after the Waterfall application was issued, the Supreme Court has now handed down its judgment on the seven issues concerned.

## Issue 1

Issue 1 concerned the ranking in the statutory waterfall of subordinated debt held by LBHI2. LBHI2 had advanced three subordinated loans to LBIE. Under the relevant contracts between LBHI and LBIE, the debt was expressed to be subordinated to LBIE's other Liabilities, defined very widely as

*"all present and future sums, liabilities and obligations payable or owing by [LBIE]*

*(whether actual or contingent, jointly or severally or otherwise howsoever)".*

The contracts provided that LBHI2 would have no remedy against LBIE other than as specifically provided by the contracts, and that the subordinated debt would not be paid unless LBIE was 'solvent' both at the time of and immediately after any payment. For these purposes, LBIE was deemed to be solvent if it was able to pay its Liabilities, disregarding "obligations which are not payable or capable of being established or determined in the Insolvency of [LBIE]".

LBHI2 accepted that subordinated debt must therefore rank below other provable liabilities. However, it contended that it ranked above statutory interest and non-provable liabilities. It provided two bases for this argument:

1./ Although non-provable liabilities are "Liabilities" under the relevant contracts, they are not "payable or capable of being established or determined in the Insolvency". Accordingly, when determining whether LBIE was 'solvent' (and therefore able to pay the subordinated debt), non-provable liabilities were to be disregarded.

2/. Statutory interest is not "payable or owing by [LBIE]", since statutory interest is payable by the administrator pursuant to Rule 2.88(7) rather than by the company. Accordingly, LBHI2 argued, statutory interest was not a "Liability", and since the subordinated debt was only subordinated to other "Liabilities" of LBIE, there was no reason for it to rank behind statutory interest. Alternatively, LBHI2 contended that statutory interest was not "payable or capable of being established or determined in the Insolvency", for the same reasons and with the same consequences as in the case of non-provable liabilities.

MORE THAN FOUR YEARS AFTER THE WATERFALL APPLICATION WAS ISSUED PERTAINING TO LEHMAN BROTHERS, THE SUPREME COURT (PICTURED BELOW) HAS NOW HANDED DOWN ITS JUDGMENT

ALEXANDER RIDDIFORD

The Supreme Court unanimously rejected LBHI2's arguments. Lord Neuberger commented that it was "hard to see any satisfactory basis" for the contention that statutory interest was not payable "in the Insolvency", since it arose as a result of (and was in fact only ever payable) in an insolvency process. On the plain wording of the contracts, statutory interest would therefore fall to be paid before the subordinated debt. Moreover, as Lord Neuberger noted, it was difficult to see any good commercial reason to construe the contracts as intending any different outcome.

Similarly, the Court rejected the argument that statutory interest did not fall within the definition of Liabilities, since it was not "payable or owing by [LBIE]". This argument was, however, slightly stronger, since the relevant statutory provisions are expressed in terms of there being an obligation on the officeholder to pay interest out of the estate, rather than there being an obligation on the company itself. However, the Court also noted that statutory interest will often replace a contractual entitlement to interest which existed prior to the insolvency. Moreover, if it could be argued that statutory interest was not a liability of the company, but was instead an obligation imposed on the officeholder, then the same argument might be applied to provable debts. This clearly would not be right: it could not be said that a provable debt did not fall within the definition of Liabilities in the relevant contracts.

In relation to the subordination of the subordinated debt to non-provable debts, the Court held that an officeholder who paid a non-provable liability of the company was making a payment "in the Insolvency". It did not matter that there was no express reference to non-provable liabilities in the legislation. The Court therefore found it unnecessary to resolve the difference of opinion between Moore-Bick and Briggs LJJ on the one hand and Lewison LJ on the other as to whether such liabilities were "established or determined" in the insolvency.

Lord Neuberger concluded his opinion on this issue by noting that the result the Court had reached was entirely consistent with what a reasonable reader would think upon perusing the relevant contracts. This is obviously right. Standing back from the precise language of the relevant clauses, and looking at the commercial scheme as a whole, the parties had clearly intended that the subordinated debt would indeed be subordinated to other liabilities in the event of LBIE entering administration, and it is entirely unsurprising that none of the nine judges who have looked at this in the three courts to consider the point reached a different conclusion.

## Issue 2

Issue 2 concerned the rights of creditors whose debts had been denominated in a

foreign currency. Under the Rule 2.86 of the Insolvency Rules, foreign currency debts are converted for the purpose of proof into sterling at the date of the commencement of the relevant insolvency process. Accordingly, creditors who were owed a debt in (say) US dollars had that debt converted into sterling as at 15 September 2008. They were then paid the sterling equivalent of those debts. However, by the time they were actually paid, sterling had depreciated against the US dollar, with the result that those creditors received considerably less than their full entitlement when converted back into US dollars as at the date of payment.

The High Court and a majority in the Court of Appeal had held that those foreign currency creditors who had suffered as a result of the depreciation of sterling between the commencement of the administration and the date of payment had a "Currency Conversion Claim" for the unpaid portion of their debt, and that such a Currency Conversion Claim ranked as a non-provable debt.

One creditor, CVI, (who stood to gain from the existence of Currency Conversion Claims) argued that the Rule 2.86 mechanism for the conversion of foreign currency debts into sterling was concerned purely with the rights of creditors among themselves. For the purpose of pari passu distribution, it is important to have a single date by reference to which all debts are valued. However, CVI argued, once all debts were paid off in full with interest, there was no reason why any shortfall to foreign currency creditors should not be made up as a non-provable liability.

LBHI2 (which, as a subordinated creditor, had an interest in keeping the value of non-provable liabilities to a minimum) argued against the existence of Currency Conversion Claims on two bases. The primary, narrower basis, was that Rule 2.86 mandatorily converts the foreign currency debt into sterling, and renders the sterling equivalent of the debt provable in the administration, so that payment in full of the proved, sterling, sum, together with statutory interest, satisfies the claim of the creditor, who has no further claim against any surplus. The alternative, wider, basis for LBHI2's case was that payment in full of a proved debt, as assessed in accordance with any of the provisions of the Insolvency Rules, satisfies the underlying contractual debt.

*Overturning the decision of David Richards J at first instance and the majority decision of the Court of Appeal, the Supreme Court held that currency conversion claims do not exist*

Lord Neuberger, with whom Lord Kerr and Lord Reed agreed, considered that Currency Conversion Claims did not exist because rule 2.86 of the Insolvency Rules sets out in full the rights of creditors in respect of provable debts denominated in a foreign currency (LBHI2's primary, narrower basis). Lord Sumption also agreed with this part of the majority judgment.

Lord Neuberger then went on to consider the alternative, wider basis on which LBHI2 had argued against the existence of Currency Conversion Claims. Lord Neuberger (along with Lord Kerr and Lord Reed) was inclined to the view that payment in full of a proved debt satisfies the underlying contractual debt, and where a dividend of 100p in the £ was paid on a provable debt, that debt has no component which is capable of resurrection. According to the majority, this provided an additional reason to reject the existence of Currency Conversion Claims. Lord Sumption was inclined to disagree, while noting that his opinion on this point did not assist LBIE's foreign currency creditors, since he agreed with the majority on the primary, narrower basis for rejecting the existence of Currency Conversion Claims. Lord Clarke agreed with Lord Sumption on this point.

Lord Clarke gave a powerful dissenting judgment on Issue 2, agreeing with the majority judgments of Briggs and Moore-Bick LJJ in the Court of Appeal. His Lordship noted that although the 1986 insolvency legislation had made significant changes to the insolvency regime, it was not comprehensive, and important judge-made principles continue to be applicable. In particular, the 1986 legislation does not purport to deal with non-provable claims. Lord Clarke considered that the language of Rule 2.86, which required


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debts to be converted into sterling "for the purpose of proving" was simply a mechanism for calculating the amount to be paid out on a creditor's proof, and did not affect the creditor's underlying right to be paid the full amount of his foreign-currency claim. His Lordship concluded that it would be "wrong in principle" for shareholders to be paid, while foreign currency creditors had still not received their full contractual entitlement.

## Issue 3

The next issue, Issue 3, concerned whether a creditor of LBIE who had been entitled to, but had not been paid, statutory interest under rule 2.88(7) of the Insolvency Rules 1986 (as in force at the date of LBIE's entry into administration), can claim such interest in a subsequent liquidation.

Rule 2.88(1) provides that, when a company is in administration, creditors can only prove for contractual interest on their debts up to the date of administration, but para (7) provides for payment of interest at the rate specified in para (9) out of any surplus in the hands of the administrator, ie once all proving creditors have been paid in full. David Richards J held that, on the correct construction of rule 2.88(7), a creditor could not enforce any claim to unpaid interest under rule 2.88(7) in a subsequent liquidation. The Court of Appeal disagreed, holding that the surplus fund in the administrators' hands was charged with the obligation under rule 2.88(7) and that this position survived the transition into liquidation.

Lord Neuberger agreed with David Richards J, holding that on the correct construction of rule 2.88(7) a creditor could not claim any unpaid statutory interest under rule 2.88(7) in a subsequent liquidation, making it clear that he also shared the Judge's "*lack of enthusiasm*" in reaching that conclusion. His Lordship held (again agreeing with the Judge) that, where there was a lacuna such as this in the statutory regime, it is impermissible for the gap to be filled by some new Judge-made rule.

However, disagreeing with the Judge, Lord Neuberger concluded that the contractual right to interest for the post-administration period (to the extent that one existed) does not survive in favour of a creditor who has proved for a debt and been paid on his proof in a distributing administration.

This was because, according to Lord Neuberger, rules 2.88, 4.93 and section 189 of the Insolvency Act 1986 together provided a complete statutory code for the recovery of interest on proved debts. In particular, the decision of Giffard LJ in *In re Humber Ironworks* (1869) LR 4 Ch App 643, 647, on which the Judge had relied in this regard, was of no assistance in the context of this new statutory code for interest, not least because at the time of that decision (in

contrast to the 1986 Rules and Act) the applicable statutory regime gave no guidance as to how contractual interest was to be dealt with in a winding up.

The remaining 4 issues, Issues 4 to 7, all arose because LBIE is an unlimited company and so its members can be called upon to make contributions under section 74 of the 1986 Act to meet its liabilities if LBIE is in liquidation.

### Issue 4

Issue 4 was whether members' contributions under section 74 can be sought in respect of the liability for statutory interest and for non-provable liabilities of LBIE.

In disagreement with the Judge and the Court of Appeal, Lord Neuberger held that a contribution could not be sought under section 74 in respect of the liability for statutory interest, in particular because: (a) statutory interest was only payable out of the "surplus" after paying proved debts in full; and (b) section 74 could not be invoked so as to create a such a surplus from which statutory interest could be paid.

The Supreme Court was referred to observations of Lord Hatherley LC and Lord Chelmsford in *Webb v Whiffen* (1872) LR 5 HL 711, 718 and 724, which emphasised the broad scope of the power conferred by section 38 of the 1862 Act, but Lord Neuberger considered that these could not justify interpreting section 74 in a way which was inconsistent with the wording of the rule which is said to found the basis of the particular exercise of the power. In short, Lord Neuberger considered that the contention that a surplus could be created by a call under section 74 so that statutory interest might thereby become payable was a bootstraps argument and unsound.

By contrast, Lord Neuberger agreed with the Judge and the Court of Appeal that in section 74 the word "*liabilities*" was not restricted to provable debts and included non-provable liabilities. Accordingly, this conclusion leads to the counterintuitive outcome that a call may be made on members under section 74 to satisfy a company's non-provable liabilities, but cannot be made to satisfy the prior ranking liability to pay statutory interest. This outcome might make more sense if, on its proper analysis, statutory interest was not in fact the liability of the company at all, but rather the liability of the officeholder himself. Lord Neuberger speculated that this may indeed be the correct analysis, but refrained from deciding the point on the basis that it was not necessary to decide it.

*The Supreme Court held that a modified version of the contributory rule applies in LBIE's administration*

### Issues 5, 6 and 7

The other 3 issues arose because LBHI2 and LBL are creditors of LBIE as well as members of LBIE liable to contribute under section 74. In particular:

a) Issue 5 was whether LBIE could prove in the administration of LBHI2 and of LBL in respect of their contingent liabilities to make contributions in LBIE's prospective liquidation if they are called on to do so pursuant to section 150 of the Act.

b) Issue 6 was whether, if LBIE could not so prove, it could exercise a right of set-off.

c) Issue 7 was whether, if LBIE could not exercise such a right of set-off, it could invoke the so-called "contributory rule" which applies in liquidation, namely that a person cannot recover as a creditor until his liability as a contributory has been discharged.

As to issue 5 Lord Neuberger held, disagreeing with the Courts below, that the nature of the contributory's obligation under section 150 is such that it is incapable of being the subject matter of a proof unless the company concerned is in liquidation. His Lordship held that any money paid under section 74 forms a statutory fund which can only come into existence once that company is in liquidation. Accordingly, if that company is not in liquidation there is no existing person to be identified as a potential creditor, merely a possible future liquidator. Lord Neuberger also identified various practical difficulties which would flow from an administrator being able to lodge a proof in respect of a contingent claim against a

*The final 3 issues arose because LBH12 and LBL are creditors of LBIE as well as members of LBIE liable to contribute under 5.74*

contributory which also militated in favour of his conclusion on this issue.

As to issue 6 Lord Neuberger held, for essentially the same reasons, that prospective section 150 liabilities cannot be set off by the LBIE administrators.

As to issue 7 Lord Neuberger, again disagreeing with the Courts below, held that the contributory rule – a Judge-made rule applicable to liquidators to the effect that a creditor can recover nothing from the company until his obligations as a contributory have been discharged – should be extended to distributing administrations. Lord Neuberger was plainly aware that his approach to this issue was in tension with his decisions that the 1986 legislation amounted to a "complete code" for post-insolvency interest, with there being no room for Judge-made rules to fill any gaps in the statutory regime, and indeed with his rejection of the currency conversion claim. Lord Neuberger noted, at [176]: "*However, in this case, the course being contemplated does not involve inventing an entirely new rule. It involves extending an existing rule so that it can apply to what is an analogous, albeit not identical, situation to that to which it previously applied, and doing so in order to achieve precisely the same end for which it was conceived.*"

His Lordship concluded that the extension of the contributory rule to administrations would not conflict with the statutory regime, notwithstanding that at first sight it might seem to conflict with rule 2.69 (which requires debts to be paid in full unless the assets are insufficient to meet them) and rule 2.88(7) (which requires any surplus remaining after payment of the debts proved to be applied in paying statutory interest "*before being applied for any purpose*").

OF THE ELEVEN JUSTICES OF THE SUPREME COURT, FIVE WERE INVOLVED IN THE WATERFALL JUDGMENT: LORD NEUBERGER (CENTRE FRONT), LORD KERR (THIRD FROM RIGHT BACK), LORD CLARKE (THIRD FROM LEFT, BACK), LORD SUMPTION (SECOND FROM LEFT, BACK) AND LORD REED (RIGHT, BACK).

Lord Neuberger's answer to the argument that the contributory rule's extension to administrations would conflict with the statutory regime, lay in the fact that the contributory rule undoubtedly applies in a liquidation (see *per* Lord Walker in *Kaupthing (No 2)* [2012] 1 AC 804, para [20] and per Briggs LJ in the present case [2016] Ch 50, para [243]), and yet if the argument is correct the contributory rule could not apply in a liquidation either (since similar provisions to rules 2.69 and 2.88(7) apply in a liquidation also).

Lord Neuberger also responded to the practical objections of the Courts below to the extension of the contributory rule to distributing administrations. As Briggs LJ has noted: "*It would ... be a serious injustice to a solvent contributory to be disabled from ever proving in a distributing administration because, in the absence of a call, there was nothing which he could pay to free himself from the shackles of the rule. The company might (and usually would) distribute all its assets to its creditors without ever going into liquidation, leaving the contributory high and dry, even though its liability as a contributory might be very small, and its claim as a creditor very large - [2016] Ch 50, para 239*." Lord Neuberger's answer to this objection was a practical one: "*When making a distribution, the administrators should retain any sum which, if the Rule had not applied, would otherwise have been distributed to a contributory, in his capacity of a proving creditor. Thus, assuming a 100% dividend, if the administrator considers that a creditor's reasonable maximum potential liability as a contributory, A, is greater than his proved claim, B, then B must be retained. If A is less than B, then he can be paid (B-A), and A is retained. If the dividend is not 100% (as presumably almost by definition will be the case), then the position is a little more complex. The administrator would have to assess the likely level of dividend, C, and the same exercise would have to be carried out with (C x B) rather than B. Any such exercise would inevitably be speculative, and the administrator should be cautious but realistic. Any such retention would be kept safe and ready to be paid out appropriately when the final accounts were drawn up, and (save perhaps in these unusual days) the retained money would earn interest*."

*Although the Waterfall I application has reached its conclusion, it is not the end of the Lehman Brothers surplus litigation...*

Accordingly, there can be no doubt now that the contributory rule applies to distributing administrations. However, the implementation of the contributory rule in this context is likely, in light of Lord Neuberger's comments above, to give rise to certain practical complexities with which administrators will need to grapple carefully.

## Conclusion

Although the facts of the LBIE administration are highly unusual, and some of the issues addressed in the Waterfall application are unlikely to arise ever again, the judgment does contain some dicta of general application, in particular on the question of whether the insolvency legislation is a "complete code", and the manner in which it should be interpreted.

On one view, the insolvency regime consists of a complete legislative code supplemented in limited areas by judge-made gloss. On this view, the insolvency code must be construed literally, even if the result leads to undesirable consequences. On the opposing view, insolvency law consists of a series of fundamental principles which are expressed through (although not necessarily limited by) the legislation. On this view, the legislation is to be construed consistently with the underlying principles which it seeks to apply. The judgments in the present case fall somewhere in between the two extremes, Lord Neuberger arguably tending towards the former view, and Lord Clarke tending towards the latter.

Although the Waterfall I application has now reached its conclusion, this is not the end of the Lehman Brothers surplus litigation. The Waterfall II proceedings are currently before the Court of Appeal, and the Waterfall III proceedings are currently before the High Court.

# Dishonest Assistance – Two new decisions

**David Alexander QC** reports on recent dishonest assistance decisions from England and Gibraltar

As most lawyers know, there are four essential basic ingredients which it is necessary for a claimant to establish to found a claim for dishonest assistance: (1) that there is a trust, (2) that there is a breach of trust by the trustee of that trust, (3) that the defendant induces or assists that breach of trust, and (4) that the defendant does so dishonestly. The first three ingredients often do not cause much trouble: they are either obviously satisfied or they are not. The fourth ingredient, dishonesty, is historically the one which has caused the most trouble. In relation to dishonesty, three things tend to come to mind when one has to consider it.

Firstly there are the big three decisions: the decision of the House of Lords in *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 A.C. 378, the decision of the House of Lords in *Twinsectra Ltd v Yardley* [2002] UKHL 12; [2002] 2 A.C. 164 and the decision of the Privy Council in *Barlow Clowes International Ltd v Eurotrust International Limited* [2005] UKPC 37; [2006] 1 WLR 1476.

Secondly, that there are other decisions which have sought to interpret what was said in *Tan*, *Twinsectra* and *Barlow Clowes*: for example, at first instance in *Abou-Rahmah v Abacha* [2005] EWHC 2662 (QB); [2006] 1 All ER (Comm) 247 and by Arden LJ in the Court of Appeal in the same case [2006] EWCA 1492; [2007] 1 All ER (Comm) 827.

Thirdly, there is the question of whether there have been any recent decisions on dishonest assistance which might have a potential bearing on a claimant's case. The purpose of this article is simply to draw attention to two decisions this year in relation to financial institutions where the question of dishonest assistance has been considered. In one the financial institution was found not to have been guilty of dishonest assistance. In the other the financial institution was found to have been guilty.

The first decision is that in *Singularis Holdings Ltd v Daiwa Capital Markets Europe Ltd* [2017] EWHC 257(Ch) where the trial took place before Mrs Justice Rose in November and December 2016. Judgment was given on 16 February 2017. In these proceedings the Claimant was Singularis. It was a company incorporated in the Cayman Islands. It was wholly owned by Maan Al Sanea ("Mr Al Sanea"). By the time the proceedings were brought it was in official liquidation. In the proceedings a claim was made to recover US $204 million. It was alleged that in early June 2009 this sum was held by the Defendant stock broker, Daiwa, for the benefit of Singularis in a segregated account. The US $204 million was made up of two elements. US $124 million was surplus collateral that was left over when Diawa closed down (on 9 June 2009) a long standing secured relationship it had with Singularis. The remaining sum of about US $80 million had arrived into Singularis' account with Daiwa on 2 June 2009. Over the course of mid-June to mid-July 2009, Daiwa had paid out this money on the instructions of Singularis' sole shareholder, Mr Al Sanea. The payments were not made to Singularis. Instead they were made to bank accounts in the name of three other companies within the Saad Group. As a result the money had been lost to Singularis.

The liquidators' claim for recovery of the money from Daiwa was made on two grounds. First it was alleged that the employees of Daiwa who authorised the payments (there were eight payments in total ranging from US $1 million to US $180 million)

SINGULARIS OWNER MAAN AL SANEA

dishonestly assisted Mr Al Sanea's breach of fiduciary duty in removing the money from Singularis for the benefit of himself or companies in the Saad Group. Secondly it was alleged that Daiwa was in breach of the duty of care owed by a bank to its client by negligently failing to realise that Mr Al Sanea was committing a fraud on Singularis by misappropriating its monies when he instructed Daiwa to pay the money to third parties: see *Lipkin Gorman (a firm) v Karpnale Limited* [1989] 1 WLR 1340 and *Barclays Bank v Quincecare Ltd* [1992] 4 All ER 363.

In so far as concerned the dishonest assistance claim, Mrs Justice Rose held that this claim failed because the two individuals at Daiwa, a Mr Metcalfe and a Mr Hudson, were not dishonest when they approved the disputed payments. In so finding, among other things, Mrs Justice Rose said this:

"143 - The test for dishonesty in this context is that set out by the House of Lords in *Twinsectra v Yardley* **...** There Lord Hutton, with whom Lord Slynn of Hadley, Lord Steyn and Lord Hoffmann agreed, described the three possible standards which can be applied to determine whether a person has acted dishonestly. There is a purely subjective standard whereby a person is only regarded as dishonest if he transgresses his own standard of honesty even if that standard is contrary to that of reasonable and honest people; there is the purely objective standard whereby a person acts dishonestly if his conduct is dishonest by ordinary standards of reasonable and honest people, even if he does not realise this, and there is a combined standard:

"**...**which combines an objective test and a subjective test, and which requires that before there can be a finding of dishonesty it must be established that the defendant's conduct was dishonest by the ordinary standards of reasonable and honest people and that he himself realised that by those standards his conduct was dishonest".

144 - His Lordship having considered the test that had been applied by Lord Nicholls of Birkenhead in the earlier case of *Royal Brunei Airlines v Tan* **...** confirmed that dishonesty is a necessary ingredient of accessory liability and that (at paragraph 36):

"dishonesty requires knowledge by the defendant that what he was doing would be regarded as dishonest by honest people, although he should not escape a finding of dishonesty because he sets his own standards of honesty and does not regard as dishonest what he knows would offend the normally accepted standards of honest conduct."

145 - In *Barlow Clowes v Eurotrust* **...** Lord Hoffmann considered whether it must be shown that the alleged dishonest assister turned his mind to the ordinary standards of honest behaviour and whether his conduct fell below those standards. He held that it was not necessary. It


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was only necessary to show that the defendant's knowledge of the transaction rendered his participation contrary to normally accepted standards of honest conduct. He did not need to be shown to have had reflections about what those normally acceptable standards were.

146 - It is clear that wilful blindness will satisfy the test for dishonesty. An honest person does not "deliberately close his eyes and ears, or deliberately not ask questions, lest he learn something he would rather not know, and then proceed regardless": *Royal Brunei* per Lord Nicholls at 389F-G. It is therefore no defence for a defendant to say that he did not realise that he was acting dishonestly: *Starglade Properties Ltd v Nash* [2010] EWCA Civ 1314 at paragraph 32 and my judgment in *Goldtrail Travel Ltd v Aydin & Ors* [2014] EWHC 1587 at paragraphs 143-5.

147 - Mr Miles [QC, Leading Counsel for Singularis] accepted that Singularis has to show that a particular person within Daiwa was dishonest. There is an important difference between being incompetent – even grossly incompetent – and being dishonest. The person that Singularis identify as having been dishonest in relation to the payments of $180 million on 18 June 2009 and the payment of $5.2 million on 8 July 2009 is Mr Metcalfe. As regards all the payments except the £180 million payment on 18 June, Singularis also allege that Mr Hudson was dishonest.

148 - As regards Mr Metcalfe, Singularis submits that his conduct went beyond what an honest person would do in the circumstances. They say that in relation in particular to the $180 million payment, no honest person in his position, knowing what he did, would have approved the payment without asking further questions. The same is true of the $5.2 million payment. They say that this is a case where he turned a blind eye. He did not make the enquiries that would be obvious to any honest person because he did not want to know the answer. They point in particular to what Mr Metcalfe told Mr Roberts in his email of 18 June that Mr Weatherall had provided him 'with necessary documentation that ticked all compliance/legal boxes'. They submit that this was a dishonest statement because he knew that he had not properly explained the situation to anyone in the Compliance or Legal departments or got any formal approval.

149 - As to Mr Hudson, Singularis say that no honest person would have acted in the way he did, making the payments without asking a single question.

150 - I am satisfied on the evidence in this case that neither Mr Metcalfe nor Mr Hudson behaved dishonestly in approving the payments, even in the sense of turning a blind eye to what I regard as the very obvious shortcomings in the material provided to them. Rather they did not understand, despite Mr Wright's

THE JUDGE IN SINGULARIS, MRS JUSTICE ROSE (BELOW RIGHT), SAID THAT SOME DOCUMENTS HAD BEEN PRODUCED 'LIKE A RABBIT OUT OF A HAT'

email of 5 June 2009, what they had to do in order for Daiwa to fulfil its obligations to Singularis.

151 - So far as Mr Hudson is concerned, his evidence in the witness box was patently frank and open. Although he had seen Mr Wright's email, he was never told that something more was expected of him than to carry out the checks that he had always carried out as to whether the recipient was on the list of sanctioned or terrorist organisations. He could not be expected to know the scope of the legal duties incumbent on Daiwa in handling the money**...**

152 - **...** There is no basis for finding that he [Mr Hudson] was in any way dishonest in his handling of the approvals and I find that there was no dishonest assistance in relation to the payments which he approved.

153 - The position of Mr Metcalfe is more problematic. Again his evidence in the witness box was given with great clarity and openness and he resisted any temptation to embellish his evidence to excuse his own conduct. He frankly admitted that he should have been more sceptical about the documents Mr Weatherall provided to him to justify the payment of $180 million. But when it was put to him that he deliberately refrained from asking questions because he was turning a blind eye to an obvious fraud, he was emphatic that that was not true.

154 - I have already held that the Hospital Expenses Agreement was a sham document. It was probably created and signed by Mr Al Sanea shortly before it was sent to Mr Metcalfe in response to his request for some evidence of a legal obligation supporting the proposed payment of $180 million. Some of the factors that push me to that conclusion should have been obvious to Mr Metcalfe as well, in particular the fact that this agreement and accompanying invoice was produced like a rabbit from a magician's hat after the first explanation was rejected. But even on the slightly expanded concept of dishonesty

discussed in the authorities, I accept Mr McCaughran QC's submission on behalf of Daiwa that it is not enough to show that looked at objectively the documents provided to justify the payment were clearly bogus. Singularis have to show that Mr Metcalfe realised that the documents were very odd indeed.

155 - I am satisfied that Mr Metcalfe did not question the authenticity of

ADAM GOODISON, WHO ACTED FOR DAIWA IN SINGULARIS HOLDINGS LTD

the documents because he also was not properly instructed as to what he needed to do in response to Mr Wright's email. For some reason which no one was able to explain he was put in charge of authorising these payments despite being inexperienced in such matters and despite the fact that important considerations expressed by senior management were not passed on to him**...**

157 - I also take into account three other factors. First, Mr Metcalfe had worked with Mr Weatherall and other people at SFS over a number of years and had formed the view that they were honest and reputable people. He was slow to form suspicions that they would have a hand in a fraud of this kind. I consider he was rather naïve **...**[b]ut to be naïve is not the same as to be dishonest.

158 - Secondly I accept the point that Daiwa make which is that Mr Metcalfe had no possible motive for acting dishonestly in this situation **...**

161 - The third factor is that there was at least some attempt by Mr Metcalfe to involve other people in the decision whether to approve the payment or not **...** It is inconsistent for Mr Metcalfe to involve others in the approval of the payment."

There are three final matters to record in relation to the Singularis case. First, Mrs Justice Rose did find Daiwa liable to Singularis in negligence and breach of contract for the sum of US $203,741,900. Second Mrs Justice Rose held that such damages should be reduced by 25 percent to take account of Singularis' contributory negligence. Third, it is understood that the decision is being appealed.

Turning to the second of the decisions, *Edgar Lavarello and Adrian Hyde v Jyske Bank (Gibraltar) Ltd* ("Jyske"), a copy of the judgment in the case can be found at http://www.gcs.gov.gi/images/judgments/supremecourt/2017/edgar_lavarello_and_adrian_hyde_v_jyske_bank_gibraltar_ltd.pdf, It was a case in the Supreme Court of Gibraltar which arose against the backdrop of the fraud perpetrated by the Marrache brothers against clients of their Gibraltar law firm, Marrache & Co. The fraud led to the firm having a deficiency of £28 million. The Claimants (who were acting on behalf of certain clients of the Firm and/or as trustees for those clients) brought proceedings against Jyske, who had operated office and client accounts on behalf of the Firm, for dishonest assistance and knowing receipt. Jyske denied the claim in its entirety and the trial took place in February 2017.

Judgment was given by Jack J on 16 May 2017. In giving that judgment, Jack J said that the key issue in the case was whether Jyske were dishonest or not. He then said that the law on what constituted dishonesty was conveniently set out by Rose J in *Singularis*, quoting paragraphs 143-146 of it (i.e. as quoted above). The Judge then identified the only person at Jyske whom it was alleged by the claimants had been dishonest, namely Mr William Bishop. Mr Bishop was the account manager at Jyske charged with responsibility for the Marrache accounts between 2003 and 2010. Having then referred to other matters, the Judge turned to Mr

Bishop's knowledge and found that "the claimants had established at least blind-eye knowledge on the part of Mr Bishop". He then continued as follows:

"237 - I have considered whether I can go further and find that Mr Bishop was in fact aware of the monies being stolen. I have looked again at the authorities cited in *Re Wardour Trading Ltd* on burden and standard of proof. I am forced to the conclusion that he was aware monies were being stolen and that he knowingly assisted the Firm in its misappropriation of client monies. Many of the specific allegations against him, which I have outlined in detail above, were so egregious that in my judgment he simply must have been aware that client monies had gone missing, stolen by the Marrache brothers."

The Judge then listed various matters which in his judgment were sufficiently egregious to show dishonesty and said as follows:

"245 - **...** I conclude that Mr Bishop did knowingly and dishonestly assist the Marraches brothers to steal client funds. He was aware from at the latest mid-2004 that they had misappropriated client funds. His dishonest assistance continued until the Firm went under in 2010. Jyske are liable for his behaviour

JYSKE BANK IN GIBRALATAR

246 - The earliest losses sustained by clients represented by the claimants in the current action were those of Timeloft Ltd (now represented by Dr Serrero) in mid-2005. The losses therefore all post-date Mr Bishop's involvement in the Marrache fraud. Jyske are therefore (subject to an account and a point of limitation) liable to all of them for dishonest assistance"

Two final matters to record in relation to the Jyske case. First the Judge also found Jyske liable for knowing receipt. Second it is understood that Jyske propose to appeal Jack J's decision.

*Adam Goodison acted for Daiwa in Singularis Holdings Ltd.*
*David Alexander QC acted for the claimants in Edgar Lavarello and Adrian Hyde v Jyske Bank (Gibraltar) Ltd.*


(FOREGROUND) DAVID ALEXANDER QC AND RICHARD SAUNDERS (RIGHT) OF MOON BEEVER LEAVING THE SUPREME COURT IN GIBRALTAR

# Case Digests

The case digests cover diverse issues in this edition. There is a summary of the decision of Blair J to award summary judgment against Ukraine for non-payment of US$3 billion due under Eurobonds held by an English Claimant on trust for the Russian Federation (see the Commercial Litigation section) and of the Court of Appeal's decision to remit to the Judge the claim brought by a footballer's agent against Bolton Wanderers and others for the Judge to assess whether the agent had a claim for loss of a chance (see Sport).

Of particular note in the context of the many claims that have been and are being brought against banks, is the successful claim brought against Jyske Bank (Gibraltar) Ltd by the liquidators of a firm of solicitors for dishonest assistance and knowing receipt (see Property and Trusts).

There have been a number of decisions of note on company law and corporate insolvency issues. The Court of Appeal has produced an analysis of the scope of section 21 of the Limitation Act as applied to breaches of fiduciary duty by directors (see Company law). The Chancellor has sanctioned a shareholders' scheme of arrangement in circumstances where the Chairman disallowed the votes of 434 individual shareholders who had each acquired the shares as a gift from the transferor in circumstances where, had the votes been allowed, the requisite majority would not have been achieved (Company law). For those readers who have a particular interest in the Lehman – Waterfall cases there is a summary of the decision of the Supreme Court (which, together with the article by Alexander Riddiford and Robert Amey, will also be of considerable assistance to those who think they ought to know how the issues were analysed but would prefer not to have to read the judgment (Corporate Insolvency)).

HILARY STONEFROST

On a more practical note, the Court has also considered, in the context of Burnden Group Ltd, the circumstances in which a liquidator, against whom a successful application has been made, can be made personally liable for costs.

*Hilary Stonefrost*

# BANKING AND FINANCE

Digested by TOBY BROWN


TOBY BROWN

## Macris v Financial Conduct Authority [2017] UKSC 19 (Lord Neuberger PSC, Lord Mance, Lord Wilson, Lord Sumption, Lord Hodge JJSC, 22 March 2017)

*JP Morgan Chase Bank - warning notices – identification of third parties*

The FCA issued warning, decision and final notices to JP Morgan Chase Bank NA notifying it that the FCA had decided to impose substantial penalties as a result of $6.2bn of losses incurred in a trading portfolio managed by the bank. This followed a £137m regulatory settlement agreed with the FCA.

The Claimant was head of the bank's Chief Investment Office. He alleged that by the notices referring to "CIO management", he had been "identified" such that the FCA was required under s. 393 FSMA 2000 to give him third party rights, in particular to serve the notices on him and give him the opportunity to make representations to the FCA. He relied on the fact that 5 months previously a US Senate committee had published a report on the bank's losses which referred to his role by name. The Claimant was successful at first instance in the Upper Tribunal, and the FCA's appeal was dismissed.

The Supreme Court allowed the appeal in a majority decision given by Lord Sumption (with whom Lord Neuberger and Lord Hodge agreed; Lord Mance dissented on the law but not the disposal of the appeal; Lord Wilson dissented fully).

Lord Sumption commented that the question of whether the Claimant had in fact been identified "*may look like a small point but…has significant implications*" in relation to the FCA's investigatory and disciplinary functions. In his view, a person is identified in a FCA notice under s. 393 if they are identified by name or by a synonym, such as by their office or job title. As to a synonym it must be apparent from the notice itself that the reference could only apply to one person, which person is identifiable from information either in the notice or that is publicly available. Resort to public information would only be permissible where it enables one to interpret, rather than supplement, the language of the notice. What is not permissible is to resort to additional facts about the person described in the notice, such that if the additional material and notice are placed side by side, it becomes apparent they refer to the same person.

The real question here was whether the terms of the FCA notice would have conveyed to a reasonable member of the public without extrinsic information that the references to "CIO management" were a synonym for the Claimant. On the facts Lord Sumption concluded that "*plainly it would not*". The Claimant was therefore not a "third party" for the purposes of s. 393.


ADAM GOODISON

## Singularis Holdings Ltd v Daiwa Capital Markets Europe Ltd [2017] EWHC 257(Ch) (Rose J, 16 February 2017)

*Banker's duty of care – fraud by director – dishonest assistance*

The claimant Singularis was a Cayman incorporated company, now in official liquidation. It was wholly owned and controlled by Maan Al Sanea, who also owned the Saad Group based in Saudi Arabia. The defendant Daiwa is a London based subsidiary of the Japanese investment bank and brokerage company.

Singularis, acting by Mr Al Sanea, instructed Daiwa as paying broker to execute payment instructions to pay on behalf of Singularis a total of US$204m to other companies within the Saad Group. Daiwa executed the various payments, making inquiries as regards some payments, and no inquiries as regards others. About a month after the last payment, Singularis went into liquidation. The liquidators of Singularis alleged that Mr Al Sanea had acted in breach of his duties as a director because the company had been insolvent or was of doubtful solvency, and that Daiwa had dishonestly assisted Mr Al Sanea in making the payments.

Alternatively, it was alleged that Daiwa breached its duty of care owed as a bank to its customer under Barclays Bank v Quincecare [1992] 4 All ER 363.

Rose J held that Mr Al Sanea was in breach of his duties but found on the evidence that that employees of Daiwa had not dishonestly assisted. However, the judge had "no hesitation" in finding that Daiwa had breached its duty of care because any reasonable banker would have realised there were many obvious

signs that Mr Al Sanea was perpetrating a fraud on the company and was clearly using the funds for his own purposes. In making the disputed payments without proper or any inquiry, Daiwa was negligent and liable to repay the monies.
Rose J rejected Daiwa's defence that Mr Al Sanea's fraud was to be attributed to Singularis as a "one man company", because this would denude the Quincecare duty where it was needed most. The judge also rejected the defence of illegality, holding that the wrongdoing of Mr Al Sanea was not to be attributed to Singularis. Rose J, however, assessed Singularis' contributory negligence at 25 percent.
An appeal has been lodged by Daiwa against the negligence judgment. Briggs LJ has granted permission to appeal, and the Court of Appeal case will therefore concern questions of attribution, duties owed by a paying broker when following the instructions of the sole shareholder and controller of the customer, and the interplay between duties owed for the benefit of members or creditors and the provisions under the Insolvency Act 1986 which protect creditors. **[Adam Goodison]**

# CIVIL PROCEDURE

Digested by ALEXANDER RIDDIFORD

## Takhar v Gracefield Developments Ltd [2017] EWCA Civ 147, Court of Appeal (Patten, King, Simon LJJ, 21 March 2017)


ALEXANDER RIDDIFORD

*Abuse of process – due diligence – res judicata*

K appealed against the Court's refusal to strike out a claim brought by T as an abuse of process.
For relevant purposes, the dispute centred on whether a joint venture agreement had been entered into between T and K. T denied that she had signed the joint venture agreement and claimed that she had not seen it until the dispute arose, and that the Court's judgment, which had been entered against her on the basis of this joint venture agreement, should be set aside on the basis of fraud.
T obtained evidence from a handwriting expert, expressing the view that she had not signed the agreement. Relying on that evidence T issued the instant claim, seeking to have the judgment set aside.
The Judge determined, as a preliminary issue, that the new action did not amount to an abuse of process and should be allowed to proceed to trial. He found that T had a real prospect of satisfying the conditions set out in *Royal Bank of Scotland Plc v Highland Financial Partners LP* [2013] EWCA Civ 328, [2013] 1 C.L.C. 596 for setting aside a judgment for fraud.
The issue was whether T had to satisfy the additional test set out in *Ladd v Marshall*, namely establishing that the evidence of forgery had not been available to her at the time of the trial and could not have been discovered with reasonable diligence.
The Court of Appeal allowed K's appeal:
a) It was noted that the starting point in relation to res judicata and the policy considerations governing abuse of process was that parties to litigation were required to bring forward their whole case and not to seek subsequently to raise issues which could have been decided in the earlier litigation.
b) T would not be able to re-litigate the issue of the terms of the joint venture agreement unless she could rely on evidence that she could not with due diligence have produced at the trial. The fact that fraud was alleged did not mean that the reasonable diligence condition did not apply.
c) Because the issue of the authenticity of the joint venture agreement had not been raised or decided at the trial, the questions of res judicata or issue estoppel did not arise.
d) However, the court was concerned with the wider policy considerations embodied in the rule in *Henderson v Henderson*. Those policy considerations were engaged whenever a litigant sought to challenge an earlier decision of a competent court, whether directly or indirectly, by commencing new proceedings in which the same issues arose or sought to appeal against a decision on the basis of new evidence.
e) The real question in cases such as this was whether the challenge to the Court's earlier judgment amounted to an abuse of process if the success of the action depended upon evidence which could with reasonable diligence have been produced at the earlier trial. In this regard, there was no distinction between applications to set aside previous judgments for fraud and applications to re-litigate issues on the basis of new evidence: the reasonable diligence condition applied in both cases.

## Glaxo Wellcome UK Ltd (t/a Allen & Hanburys) v Sandoz Ltd [2017] EWCA Civ 227, Court of Appeal (Floyd, Moylan LJJ and Sir Timothy Lloyd, 6 April 2017)

This was an appeal against a decision refusing the appellants' application to join two companies as defendants to their passing off action against the respondents.
The Court of Appeal held that:
a) Liability as a joint tortfeasor would arise where a party had assisted the commission of a tort by another person, pursuant to a common design with that person to do an act which was or turned out to be tortious, *Fish & Fish Ltd v Sea Shepherd UK* [2015] UKSC 10 followed.
b) The appellants had made out a sufficiently arguable case of liability on the part of the two companies jointly with the respondents for their primary acts of passing off.
c) An accessory was liable not for his acts of assistance, but for the primary actor's tortious act, *Sea Shepherd* followed. Accordingly, no cause of action accrued against the two companies until late 2015 when the relevant product was first promoted and sold in the UK by the respondents.
d) The same limitation period applied to the claim against the two companies as to the claim against the respondents. It followed that limitation provided no justification for refusing to join them as additional defendants. Accordingly, the two companies were added as defendants to the claim, and the case was remitted for consequential case management directions.

## Apex Global Management Ltd v Global Torch Ltd [2017] EWCA Civ 315, Court of Appeal, (Gloster, Black LJJ and Sir Christopher Clarke 28 April 2017)

*Delay – judgments and orders – relief from sanctions – stay of execution*

The parties were shareholders in a joint venture company. A third party had purchased shares in the company under a share purchase agreement (SPA). The entirety of the purchase monies was paid to the appellants. Both parties subsequently issued unfair prejudice petitions under the Companies Act 2006 s.994. Each relied upon a version of the SPA which the other said was forged. The appellants' petition was ultimately struck out after repeated failures to comply with Court orders.
Two weeks after judgment was handed down, the appellants sought the stay of execution on the basis that (a) the respondent's version of the SPA contained an exclusive jurisdiction agreement in favour of the courts of Saudi Arabia and (b) the Judge should therefore have declined jurisdiction. The judge refused a stay on the basis that the application was too late.
The Court of Appeal dismissed the appeal against the Judge's decision. It was possible to make a late application for a stay of proceedings in certain circumstances. Such an application would be treated as an application for relief from sanctions. As a result, whether a stay should be granted fell to be determined in accordance with the principles in *Denton v TH White Ltd* [2014] EWCA Civ 906. The Court had no doubt that the application of those familiar principles clearly resulted in the refusal of a stay. The appellants' failure to make the application at the earliest opportunity was serious and significant. They should have sought a stay when first aware of the terms of the respondent's version of the SPA.

## Emmott v Michael Wilson & Partners Ltd [2017] EWCA Civ 367, Court of Appeal, (Simon, David Richards, Hickinbottom LJJ, 19 May 2017)

*Judgment debts – payment into Court – third party debt orders*

A judgment debtor appealed against a decision granting the respondent judgment creditor's application under CPR 72.10 for the payment out to him of monies standing to the appellant's credit in Court.
The judgment debtor had paid the monies into Court in connection with unrelated litigation and they had stood to its credit following a Court of Appeal order in its favour. However, a subsequent freezing order in that litigation covered those sums. The judgment creditor had sought payment out of the monies to satisfy an unpaid arbitration award which had been made in his favour as against the judgment debtor. The judgment debtor had argued that the monies in court were not its asset because it was subject to a charge in favour of a company to which the judgment debtor was indebted. The judgment creditor had challenged the authenticity of the loan documentation between the judgment debtor and that company.

The Court below had held that CPR 72.10 was to be treated as separate to the other provisions in CPR Part 72 and that, whatever their prior status, once sums had been paid into Court, they were sums available to a judgment creditor.
The Court of Appeal held that CPR 72.10 simply prescribed how an application was to be made where a judgment creditor sought to obtain an order for payment of a sum owed by a judgment debtor from sums in court. It was not a free-standing regime as described by the judge. If an issue in relation to the judgment creditor's right to an order under CPR 72.10 was made, the Court had to decide whether to make the order taking into account the other provisions in CPR Part 72. Money in Court was not immune from other claims, and the Court was not bound to make an order in favour of the judgment creditor.
As the Judge had reached his decision by the application of the wrong principles, it fell to the instant Court to exercise its own judgment as to whether to grant the order sought, and it held that the order should not be made.
**[Matthew Abraham]**

# COMMERCIAL LITIGATION

Digested by MADELEINE JONES

## Marathon Asset Management LLP v Seddon [2017] EWHC 300 (Comm); [2017] I.R.L.R. 503 Queen's Bench Division (Commercial Court) (Leggatt J, 22 February 2017)


MADELEINE JONES

*Damages – loss – confidential information*

Two former employees of an investment management company had copied electronic files containing confidential information, in breach of their employment contracts and the implied duty of fidelity owed by an employee, before leaving the company. The Claimant company had not suffered any financial or other loss as a result of the theft, nor had the Defendant employees profited from it.
After assessing the extent of the Ds' liability, the acts which had constituted breaches, and the nature of the duties breached, Legatt J went on to consider the principles governing quantum of damages.
Leggatt J rejected C's contention that the appropriate measure of damages was the amount of money which would reasonably have been agreed in a hypothetical negotiation between a willing seller in the Claimant's position and a willing buyer in the position of the defendants to release the defendants from the duties to the Claimant of which they were in breach. Not only was such a measure hard to quantify (expert evidence was adduced but the estimates ranged from US$200,000 and £39.4m), but it was wrong in principle.
Damages could not be awarded by analogy with conversion of goods because copying the data did not deprive C of anything. Nor could damages be awarded for the risk of loss to which C was exposed and the corresponding opportunity of gain achieved by the Ds. English law does not award damages for risk of loss or order the surrender of hypothetical benefits.
The various evidential rules which assist claimants where the level of loss is uncertain (for example, estimation of the value of damage that has certainly been suffered but is hard to quantify, and a presumption in favour of the claimant where the defendant has destroyed or wrongfully prevented or impeded the claimant from adducing relevant evidence) do not enable the court to conjure facts out of the air and apply only where evidence is not reasonably available.
Leggatt J examined two circumstances in which there may be compensation without financial loss. The first is where the defendant is in breach of a fiduciary duty owed to the claimant.
The second is where a defendant's wrong consists in using the claimant's property for the defendant's own purposes. In such a case damages may be awarded representing the value of such use to the defendant. This "user principle" applies to intellectual as well as physical property. Cases where this principle applies fall into two main types – *Wrotham Park* damages (so called after *Wrotham Park Estate Co Ltd v Parkside Homes Ltd* [1974] 1 WLR 798) where the claimant has lost its right permanently, and 'licence fee' cases, in which the defendant has availed himself of the claimant's right temporarily.
In these cases, quantum of damages is assessed in one of three ways. In the first instance the court asks what value the claimant could expect to obtain the licence for in the open market. Where there is no such market, the court estimates the licence fee that could reasonably have been charged. Where such a licence would not have been sold, the court should assess the amount of profit made by the wrongdoer which is fairly attributable to its wrongful use of the claimant's property. This may be by way of an account of profits or by the awarding of the percentage of the profits that are attributable to the defendant's wrongful acts.

However, the instant case did not fall into any of the exceptions under which damages could be awarded in the absence of loss. Accordingly, the claimant was awarded only nominal damages.

## Law Debenture Trust Corp Plc v Ukraine [2017] EWHC 655 (Comm) (29 March 2017, Blair J)

*International law – justiciability – capacity – duress*

Mr Justice Blair granted summary judgment against Ukraine for non-payment of US$3 billion due under Eurobonds held by the English Claimant company on trust for the Russian Federation.

Ukraine argued that Russia had pressured it into accepting financial support from Russia rather than entering into partnership with the EU (as it alleged the Ukrainian people would have preferred), by the use of trade restrictions, the threat of force, and the use of force, in the invasion of Crimea and the support of military action in eastern Ukraine. It relied upon this pressure as a justification for its non-payment under the bonds, and put forward a number of arguments to this end.

Ukraine said that it had no capacity to enter into the bonds as a matter of Ukrainian law. However, Blair J ruled that even if the state's entry into the bonds had been illegal as a matter of national law, this did not mean the state did not have capacity to enter the agreement as a matter of English law. Under the "Lotus principle" (a principle of international law accepted by the English courts) states have the right to do whatever is not prohibited by international law. This capacity is recognized by the English courts.

Ukraine's case that the requisite authority to enter into the contract was not given (as the approval of the Minister of Finance was said to be required) could not succeed since as a matter of English law, a principal is bound by the acts of an agent with ostensible authority, even if that agent does not have actual authority.

The court accepted that Russia had applied measures restrictive of trade which were more than simply economic but of profound consequence to Ukraine. However, these could not be relied on for the contractual defence of duress. This was because under the foreign act of state doctrine, recently set out by the Supreme Court in *Belhaj and others v Straw and others [2017] UKSC 3* the English courts decline to adjudicate on the lawfulness of the extraterritorial acts of foreign states in their dealings with other states or the subjects of other states.

Russia's use of force against Ukraine did not constitute a public policy exception to the foreign act of state doctrine. The cases established that the making of war and peace by states were not justiciable by the English courts, and the international law crime of aggression did not form part of English law.

It was also not possible to imply a term into the notes to the effect that they would not be repayable if Russia frustrated Ukraine's ability to repay as a result of its military intervention. This is because the notes are tradeable instruments and the implication of terms into such instruments was limited because transferees or potential transferees have to be able to ascertain the nature of the obligation they are acquiring (or considering acquiring) from within the four corners of the relevant contracts. Otherwise, the scope of transferability would be severely limited, and the market thereby compromised.

The English court's lack of jurisdiction over international law matters also meant that it could not rule that the Ukrainian refusal to pay was a proportionate response to Russia's military intervention. Accordingly, there was no justiciable defence to the repayment and therefore no other compelling reason for a trial. Summary judgment was granted.

## Plantation Holdings (FZ) LLC v Dubai Islamic Bank PJSC [2017] EWHC 520 (Comm) (Picken J, 24 March 2017)

*Reasonable opinion – damages*

The Claimant property developer acted as surety for a debt restructuring agreement with the Defendant bank. Repayment was to be in instalments set out in the agreement. C granted the bank a conditional assignment of the lease to the land for whose development the money had been borrowed. The agreement provided that D could give notice where, in its reasonable opinion, there had been an event of default; such a notice opened the way to D to perfect the assignment.

D gave notice to C that it was in breach of contract and various local laws, and perfected the lease assignment. D sought further to rely

on the fact that C had stopped paying or was unable to pay its debts, which would constitute an event of default. Picken J found that the allegation that C had violated contractual provisions or local laws so as to give rise to an enforcement event was not made out.

Regarding the question of an event of default, the contractual requirement that D have formed a 'reasonable opinion' required D to have had subjective knowledge and to have relied on this knowledge at the time. The fact that the notice did not refer to an insolvency event showed that D did not have it in mind, so that the test was not met.

As to damages, Picken J rejected a claim in conversion on the ground that a lease is land, and land cannot be made subject to a claim in conversion. He considered instead the question of what damages would compensate C. This involved considering what would have happened but for the breach. In fact, an enforcement event would have occurred, so that D would have become entitled to perfect the assignment. The property was making a loss at the time notice was given and until the next repayment date, at which C would have defaulted. Accordingly, C was entitled to nominal damages only.

## Wood v Sureterm Direct Ltd [2017] UKSC 24 (Lord Neuberger PSC, Lord Mance, Lord Clarke, Lord Sumption, Lord Hodge JJSC, 29 March 2017)

*Contractual construction*

The Supreme Court considered an indemnity clause in a share sale and purchase agreement. The clause provided that the Respondent seller would indemnify the Appellant buyer in respect of costs arising from legal proceedings or fines following "claims or complaints" registered with the FSA or other regulator in respect of mis-selling or suspected mis-selling.

After the agreement was entered into, employees of the company alleged that it had mis-sold products. A informed the FSA, and the FSA directed it to pay compensation to customers. A relied on the indemnity to recover the cost of this compensation from the seller. However, the Supreme Court upheld the decision of the Court of Appeal, that because A had referred itself to the FSA, the losses could not be said to stem from a claim or complaint to the FSA, and therefore were not covered by the indemnity.

Lord Hodge JSC gave the unanimous judgment of the Court.

He considered the question of whether the CA had fallen into error by reliance on counsel's submission that the Supreme Court in *Arnold v Britton [2015] AC 1619* had "rowed back" from the guidance on contractual interpretation in *Rainy Sky SA v Kookmin Bank [2011] 1 WLR 2900*. Lord Hodge rejected this submission, and took the opportunity to clarify the relationship of *Arnold* and *Rainy Sky*. The latter was not a recalibration of the former. They were saying the same thing.

The court's task is to ascertain the objective meaning of the language which the parties have chosen to express their agreement. This is not a literalist exercise but the court must consider the contract as a whole. Depending on the nature of the contract it may give more or less weight to elements of the wider context in reaching its view as to the objective meaning. This was the approached summarized in *Rainy Sky* and all the justices in *Arnold* confirmed the approach in *Rainy Sky*. Sophisticated and complex agreements negotiated and prepared with the assistance of skilled professionals may well be interpreted by mainly textual analysis. Contracts which are informal, brief or drafted without professional assistance may be interpreted with greater emphasis on the factual matrix. However, even sophisticated professional contractual negotiators may fail to achieve a logical and coherent text because of various extraneous matters, so that provisions in detailed contracts may be unclear and fall to be interpreted by reference to the factual matrix.

Lord Hodge held that the construction favoured in the instant case had been reached mainly by a careful examination of the language which the parties have used, rather than by an appeal to business common sense. This was because "*in the tug o' war of commercial negotiation, business common sense can rarely assist the court in ascertaining on which side of the line the centre line*
*marking on the tug o' war rope lay, when the negotiations ended*."

# COMPANY LAW

Digested by EDOARDO LUPI

## *First Subsea Limited v Balltec Limited & others* [2017] EWCA Civ 186

**(Patten, Kitchen, Briggs LJJ, 30 March 2017)**

EDOARDO LUPI

*Limitation – constructive trusts – directors*

Following the trial on liability at first instance, the Second Defendant, a former director of the Claimant, was held liable for various breaches of fiduciary duty and was ordered to account or pay compensation to the Claimant. Norris J held that breaches of duty relating to the preparation and making of bids for contracts in competition with the Claimant through a newly formed rival company, the First Defendant, formed by the Second Defendant and his associates for that purpose, were made out.

The appeal was heard by Patten, Kitchen and Briggs LJJ, and was concerned primarily with limitation. The relevant breaches of duty had all taken place more than six years before the claim form was issued. The appeal required their Lordships to consider the much-litigated provisions of s. 21 of the 1980 Act (the "1980 Act"), when applied to 'constructive trustees'. In general, a breach of fiduciary duty by a director falls either under s. 21 (3) of the 1980 Act, to which a 6-year limitation period applies, unless it falls within s. 21 (1) of the 1980 Act, which disapplies any statutory limitation period in the case of fraud (21 (1)(a)) or where trust property is in the possession of the trustee or converted to the trustee's use (21 (1)(b)).

By way of relevant legal background, as was confirmed in *JJ Harrison v Harrison* [2002] BCLC 162 directors are treated as Class 1 fiduciaries within the well-known classification set out by Millett LJ in *Paragon Finance plc v D B Thakerar & Co* [1999] 1 All ER 400. In *Paragon Finance* itself a distinction was drawn between, on the one hand, a constructive trustee who owes pre-existing duties in respect of property pre-dating any breach of duty (a Class 1 constructive trustee) and, on the other, a constructive trustee who only becomes such by virtue of having committed some wrongdoing (a Class 2 constructive trustee). The reason directors are treated as Class 1 fiduciaries is that the law views them as holding company property on trust from the outset.

The issue before the Court of Appeal was, in essence, whether a fraudulent breach of duty committed by a director as a Class 1 fiduciary but which breach does not involve misappropriation of company property, would nevertheless fall within s. 21(1)(a) of the 1980 Act. The Second Defendant's contention was that s. 21(1)(a) has no application to a breach giving rise to a Class 2 constructive trust even where the breach is committed by a Class 1 fiduciary. The sub-section is limited to cases where the fiduciary misappropriates or misuses property already vested in him or under his control.

The key paragraphs of Patten LJ's judgment on this difficult issue were [58] to [63]. The definition of 'trust' and 'trustee' under s. 38(1) of the 1980 Act requires the words to be given a consistent interpretation where they occur under s. 21. Thus, if a defendant is a constructive trustee for the purposes of s. 21(3) it follows that he is also one under s. 21(1), the only difference being that under section 21(1) the trust property remains in the trustee's possession (or has been converted to his use) or his breach was fraudulent. Even where a director does not fall under s. 21(1)(b) because he has not misappropriated or received pre-existing company property because, say, he has received a secret profit, the director nevertheless remains a Class 1 fiduciary at all times.

Accordingly, if a director is a trustee for the purposes of s. 21, the phrase 'breach of trust' must encompass any breach of his fiduciary duties, even if a breach does not involve misapplication or misappropriation of company property. According to Patten LJ, the question is one of status which is determined by the nature of office which a director lawfully holds, such that a director is for all purposes a Class 1 fiduciary for the purposes of s. 21 of the 1980 Act.

On the facts of the case, the judge had sufficient evidence before him properly to decide that the Second Defendant's breaches were fraudulent. Accordingly, the Second Defendant fell within s. 21 (1)(a) such as to prevent time running under s. 21 (3).

## Power Adhesives Limited v Stephen Sweeney & others [2017] EWHC 676 (Ch) (Chief Master Marsh, 31 March 2017)

*Rule in Hastings-Bass – issue of shares*

The Claimant sought a declaration that the decision by its directors to issue 490,000 B shares (the "Shares") was taken in breach of their fiduciary duties, was voidable and should be set aside. Prior to the Shares being issued, the Company's issued share capital comprised 10,000 ordinary shares. Chief Master Marsh granted the declaration sought.

Before the issue of the shares, concern had been mounting among the directors regarding the size of the loan account of one their number, P, which had reached £600,000 and would become payable (they thought, perhaps erroneously) immediately upon P's death. P then became terminally ill. The Company passed a number of resolutions which led to the Shares being issued to P, to extinguish the Company's liability to him in respect of the loan account, which liability had by then been reduced to £490,000. The problem with the debt to equity swap was that the Company was a successful concern and the effect of allotting the Shares to P was that the other shareholders were significantly diluted as a result. Further, it became apparent upon P's death that the allotment of the Shares created a potential for significant inheritance tax and capital gains charges.

The Claimant's application was based on the rule in *Re Hastings-Bass*, the rule applying to decision-making by fiduciaries which is analogous to the test of Wednesbury unreasonableness in the realm of decisions by public bodies.

Chief Master Marsh applied the rule following the summary of the law in relation to directors by John Randall QC sitting as a Deputy Judge of the High Court in *Hunter v Senate Support Services Limited* [2004] EWHC 1085 (Ch). Chief Master Marsh held that it was plain from the detailed evidence before him that the directors had not understood the effect of the transaction they approved and, had they understood it, they would not have passed it. More particularly, the directors had failed to take into account relevant considerations like the massive dilution of the value of the ordinary shares and the potentially serious tax consequences flowing from the transactions.

The one outstanding issue related to the role of the Company's professional advisers and whether, by relying on their advice, the directors had fulfilled their fiduciary duties. The master concluded that the directors had failed to use all proper care and diligence in obtaining advice about the consequences of the transaction, such that the advice they had obtained did not negate their breaches of duty in the circumstances of the case.

## Re Dee Valley Group Plc [2017] EWHC 184 (Ch) (Sir Geoffrey Vos, Chancellor of the High Court, 8 February 2017)

*Schemes of arrangement – sanction – share splitting*

The case concerned the pre-conditions under s. 899(1) CA 2006 that engage the court's discretion to sanction a scheme of arrangement. Specifically, the case was concerned with the requirement that there must be a majority in *number* of the class of members present and voting.

The issue before the court arose in the context of the Company's application for the sanction of a scheme of arrangement in respect of it by which the Company's entire issued share capital was to be sold to another company. The issue was whether the chairman of a class meeting had been right to disallow the votes of some 434 individual shareholders opposing the scheme. Each of the 434 shareholders had acquired one share by way of gift from the same transferor. By disallowing the votes, the scheme was approved and *prima facie* met both pre-conditions under s. 899(1). Had the individual shareholders' votes been allowed, the requisite majority would not have been reached, such that there would have been no basis on which the scheme could have been considered for sanction by the court.

The Chancellor noted that it appeared to be the first such case where a share-splitting exercise had been undertaken to defeat a scheme of arrangement.

By way of background, one opposing shareholder had acquired three tranches of shares after the court had directed that the class meeting be held for the purposes of voting on the scheme. The dissentient then delivered valid stock transfer forms to the Company's Registrars, and the Company subsequently registered the 434 new shareholders. For the sake of completeness, an order was obtained from Registrar Derrrett giving permission to the chairman of the meeting to reject the votes of these particular shareholders.

The first issue concerned the proper

approach to determining the validity of the members' votes. Again, there was little authority directly in point, so the Chancellor proceeded from first principles. The Chancellor's starting point was that a class meeting summoned by the court is under the control of the court. Subsequently, at the sanction stage, among the things the court considers are (i) whether the statutory pre-requisites have been fulfilled; (ii) whether the class attending the meeting was fairly represented by those attending the meeting; and (iii) whether the statutory majority were acting *bona fide* and not coercing the minority in order to promote interests adverse to those of the class they purport to represent. It is by reference to the factors considered by the court at the sanction stage that one receives a clue as to what members are supposed to be doing when they vote at the class meeting. The test is whether the class members at the court meeting have voted in the interests of the class and not to promote interests adverse to the class they purport to represent.

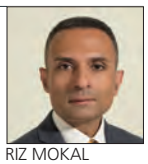
The Chancellor acknowledged that it would only be in a very unusual case that an attempt could be made to challenge the motives of the opponents of a scheme, because evidence necessary to do so is rarely available. In the case before him, however, the Chancellor held that the chairman had been justified to reject the votes as not having been cast for the purpose of benefitting the class as a whole: the only possible explanation for the conduct of the 434 shareholders was to further a share manipulation strategy to defeat the scheme by ensuring that the statutory pre-requisites were not met. The individual shareholders can only have joined the class of voting members with the pre-conceived notion of voting down the scheme. Sir Geoffrey said at [58]: "*Both the Chairman and the court could and should…take these matters into account in considering whether the votes of the Individual Shareholders were valid. In my judgment, they were not. The Chairman was entitled to protect the integrity of the Court Meeting against manipulative practices such as the share-splitting that would frustrate its statutory purpose.*"

Having been satisfied that the statutory pre-requisites were met in the case before him, the judge went on to sanction the scheme in respect of the Company.

# CORPORATE INSOLVENCY

Digested by RYAN PERKINS & RIZ MOKAL


RYAN PERKINS


RIZ MOKAL

## Akers v Samba Financial Group [2017] UKSC 6; [2017] 2 WLR 713 (Lord Neuberger PSC, Lord Mance, Lord Sumption, Lord Toulson, Lord Collins JJSC, 1 February 2017)

*Section 127 – trusts*

The liquidators of a company contended that shares in various Saudi banks were held on trust for the company. The shares had been transferred to the defendant after the commencement of the liquidation, and the liquidators sought a declaration that the transfer was void under section 127 of the Insolvency Act 1986. The Supreme Court held that the transfer did not involve a "disposition" of the company's assets within section 127, and refused to grant the relief sought by the liquidators. In particular, the Supreme Court held as follows: (i) a trust can be created over assets situated in a jurisdiction which does not recognise trusts in any form; (ii) accordingly, the fact that the shares were situated in Saudi Arabia did not prevent them from being held on trust for the company; (iii) further, the company's beneficial interest in the shares constituted "property" within section 436 of the Act; but (iv) there was no "disposition" of the company's property, since all that had been transferred was legal title to the relevant shares, whereas the company *prima facie* retained its beneficial interest in the shares after the transfer occurred; and (v) even if the company's beneficial interest in the shares was destroyed as a result of the transfer (e.g. due to the priority rules under the *lex situs*), this did not constitute a "disposition" within section 127.


DANIEL BAYFIELD QC

## Re Dalnyaya Step LLC [2017] EWHC 756 (Ch) (Mrs Justice Rose, 10 April 2017)

*Cross-Border Insolvency Regulations 2006 – recognition of foreign insolvency proceedings – security for costs*

The company's Russian liquidator obtained an order recognising the Russian liquidation as a foreign main proceeding under the Cross-Border Insolvency Regulations 2006 (implementing the UNCITRAL Model Law on Cross-Border Insolvency). After recognition was granted, three former managers of the company

applied to set aside the recognition order. The managers had not been served with the recognition application, and the liquidator had failed to disclose a significant public policy issue between the managers and the Russian authorities. In these circumstances, the managers applied for an order requiring the liquidator to give security for the managers' costs of their application to set aside the recognition order. The liquidator resisted the application for security on three alternative grounds: (i) that there was no "claim" or "proceeding" within CPR 25.12; (ii) that the managers were not the "defendants" of the supposed "claim"; and (iii) that the Court should not exercise its discretion to award security (even if, which was denied, the Court had jurisdiction to do so). The Court rejected the liquidator's arguments and granted security for costs. *Held*: (i) the recognition application brought by the liquidator was a "claim" or "proceeding" within CPR 25.12; (ii) the managers should be treated as the "defendants" of the claim, on the basis that Court should have been informed of the public policy issue affecting the managers (which would, in turn, have resulted in an *inter partes* hearing between the liquidator and the managers as to whether recognition should be granted); (iii) the application to set aside the recognition order was part and parcel of the underlying recognition "claim"; such that (iv) the Court had jurisdiction to order security in favour of the managers. Further (v) the liquidator had no assets in the UK against which costs could be enforced if the managers were successful; (vi) the managers had a real prospect of succeeding on their application to set aside the recognition order; and (vii) the facts were exceptional and granting security would not open undesirable floodgates to many similar applications, such that (viii) the Court should exercise its discretion to award security. The Court recognised that security will rarely be awarded against a liquidator, but declined to apply this rule in the context of a foreign representative.

**[Daniel Bayfield QC]**

## Rosesilver Group Corp v Paton [2017] EWCA Civ 158 (Henderson LJ and Sir Christopher Clarke, 24 May 2017)


BARRY ISAACS QC

*Breach of fiduciary duty – double employment*

Where a solicitor acting for the buyer of a property also acts in a very limited way for the seller, this does not automatically create a conflict between the solicitor's duties to the buyer and the seller. An actionable conflict must be real, rather than merely theoretical. In any event, the seller had given his informed consent to any conflicts that might in theory have arisen. Accordingly, there was no breach of fiduciary duty, or breach of the double employment rule.

**[Barry Isaacs QC, Ryan Perkins]**

## Joint Administrators of LB Holdings Intermediate 2 Ltd v Joint Administrators of Lehman Brothers International (Europe) [2017] UKSC 38 ('Waterfall I') (Lord Neuberger, Lord Kerr, Lord Clarke, Lord Sumption, and Lord Reed JJSC, 17 May 2017)


ROBIN DICKER QC


WILLIAM TROWER QC


RICHARD FISHER

*Administration – ranking of subordinated claims of those contributing toward financial firm's regulatory capital – currency conversion claims – whether payment in full of proved debt fully discharges debtor's indebtedness – whether statutory interest in administration claimable in subsequent liquidation – contributory's liability toward statutory interest and unprovable liabilities – whether company in administration may prove in contributory's insolvency proceedings – whether liability qua contributory may be set off against contributory's claim qua creditor – whether the contributory rule applies in distributing administration*

The Supreme Court decided seven issues in the litigation between 'LBIE', the unlimited company that was the main European trading entity in the Lehman Brothers investment banking group, and its immediate parents, 'LBHI2' and 'LBL', each of which is in administration. In doing so, the Court also considered the fundamental nature and effect of the winding-up regime.

The first issue concerned LBIE's indebtedness to LBHI2 for a sum of £1.254bn under three subordinated loan agreements on standard terms provided by the Financial Services Authority. Under the Basel framework, these funds formed part of the 'gone concern' layer of LBIE's regulatory capital, colloquially so called in recognition of its intended role of protecting other creditors in the event of a financial institution's failure. Those creditors had been paid

in full for the sums for which they had proved in LBIE's administration, and the question was how LBHI2's subordinated claims ranked, in payment out of the substantial funds remaining in the estate, against (a) statutory interest pursuant to Insolvency Rule 2.88(7) and (b) non-provable liabilities whose discharge is required under common law principles before anything may be paid to the company's members. Lord Neuberger, with the concurrence of Lords Kerr and Reed, held that (a) statutory interest is payable and owing by LBIE in its insolvency even though LBIE could not have been sued for it and the liability is only imposed on its administrators in relation to any surplus after full payment of proven claims. (b) As to non-provable liabilities, the payments the administrator makes towards them are also made in the insolvency, notwithstanding the absence of any statutory machinery for doing so. It followed, on the terms of subordinated loans, that LBHI2's claims rank below the payment of both statutory interest and non-provable liabilities. Also as a matter of construction of the loan agreements, LBHI2 could lodge a proof for these claims only once it was clear that payment in full on these claims, including payment of any statutory interest on them, would not prevent non-provable liabilities from being met in full.

The second issue concerned so-called currency conversion claims. LBIE owed substantial debts payable in foreign currencies, which under Insolvency Rule 2.86 were to be converted into the sterling equivalent as at the commencement of administration. Sterling having depreciated against some relevant currencies since that date, it was argued on behalf of '**CVI**' representing such creditors that payment in full of the sterling equivalent of their proved claims would leave them with a shortfall as against their contractual entitlement, which should be recoverable as non-provable debt. According to CVI, the statutory regime for the proof of debts, of which Rule 2.86 is part, is geared merely towards ensuring equitable and orderly treatment of creditors inter se, but does not affect the underlying debt. It follows that when prior ranking claims and statutory interests thereon have been paid in full and a surplus remains, foreign currency claimants should be able to assert a currency conversion claim to the full extent of their contractual entitlement. Basing himself on the considered views of the Law Commission and the Cork Committee, Lord Neuberger rejected this argument as a matter of construction and intended effect of Rule 2.86. Significantly, his Lordship was also attracted, albeit tentatively, by the wider proposition that payment in full of a proved debt discharges the underlying contractual (and, it may be presumed, other) obligations. This entailed recontextualising well-established dicta to the contrary in the Court of Appeal and the Privy Council and giving them a narrower reading than they had previously borne. It is worth noting that in an otherwise concurring judgment, Lord Sumption gave powerful reasons for his view, also said to be provisional, that the winding-up regime in itself has a merely administrative effect and nothing short of payment in full or (said his Lordship, presumably by oversight) dissolution of the corporate debtor discharges the latter's underlying indebtedness. Also in an otherwise concurring judgment, Lord Clarke accepted CVI's arguments in favour of the existence of currency conversion claims.

Third, Lord Neuberger held that Rule 2.88(7) only applies while an administration is in existence and is to be understood as a direction to the administrator to pay statutory interest from any surplus after payment of provable debts. There can be no other use of the Rule. In particular, found his Lordship expressly without enthusiasm, it cannot be the basis for claiming any unpaid interest in a subsequent liquidation.

The fourth question was whether the liability of contributories of an unlimited company under sections 74(1) and 150(1) of the Insolvency Act to contribute towards its "debts and liabilities" extended to statutory interest and non-provable liabilities. Lord Neuberger held that the phrase "debts and liabilities" included non-provable liabilities but excluded statutory interest. The conclusion involves the apparent paradox that contributories must pay toward a category of liability (non-provable liabilities) that lies below another (statutory interest) towards which contributories need pay nothing. Lord Neuberger dismissed any concern on this account on the basis that his conclusion causes neither practical nor conceptual difficulty.

Fifth and following from the previous point, LBIE's administrators argued that LBIE was entitled to prove in the administrations of LBHI2 and LBL for the latter companies' contingent liabilities as contributories under section 150 of the Insolvency Act. Lord Neuberger rejected this argument. Only a liquidator on behalf of the court may make calls under Section 150, hold the resulting funds separately from the company's general estate, and apply them solely toward the company's statutory liabilities in winding-up. LBIE not being in liquidation, there was no one with the standing to press a claim in LBHI2's and LBL's administrations or to ensure that the resulting funds would be put to the stipulated use.

Sixth, LBIE's administrators argued that they could set off the prospective section 150 liabilities of LBHI2 and LBL against these companies' subordinated claims. LBHI contested

this argument firstly on the basis of the fairly widely accepted proposition that only provable claims may be the subject of insolvency set-off. Lord Neuberger rejected this on the basis that nothing in the statutory language (in this instance, of Insolvency Rule 2.85) governing insolvency set-off supports this requirement. His Lordship nevertheless found that no set-off was permissible in this case for the reasons relevant to the previous issue, that is, that only a liquidator may make a section 150 call and may only do so in order to satisfy the company's liabilities in liquidation.

Seventh and finally, however, Lord Neuberger acceded to the LBIE administrators' argument that they could invoke the 'contributory rule' to refuse to pay anything to LBHI2 and LBL qua creditors until the latter had fully discharged their liabilities qua contributories. His Lordship approved the analysis provided by *McPherson's Law of Company Liquidation* that the rule is one manifestation of a general equitable principle qualifying distributions under the Insolvency Rules. In practical terms, this meant that the administrators should segregate and retain any sum that would have been distributed to the contributory qua creditor in the absence of application of the contributory rule. This sum may be paid out upon the taking of final accounts.

**[Robin Dicker QC, William Trower QC, Barry Isaacs QC, Daniel Bayfield QC, Richard Fisher, Stephen Robins, Charlotte Cooke]**

## Re Central A1 Ltd [2017] EWHC 220 (Ch) (Mr Registrar Jones, 14 February 2017)

*Creditors' voluntary liquidation – jurisdiction to assess reasonableness and necessity of expenses incurred pre-liquidation – relevance of time costs to fixed fees – trust of funds in client account*

The Applicant was engaged by 1,796 companies to undertake the work required to put each of the companies into creditors' voluntary liquidation. A fixed fee was agreed for the work of £6,000 for each of the companies but this fee would not be paid if the relevant company did not have sufficient assets. The substantial majority of the companies had less than £2,000 realisable assets and some of the companies had less than £1,000. The aggregate fee payable pursuant to the agreement was £2,875,017; an average of £1,600 per company. The Liquidators refused to agree payment of the fees. The Applicant made an application to Court pursuant to section 112 of the Insolvency Act 1986 for a declaration that the fees were payable on the grounds that the amount was reasonable for the work that was necessary to put the companies into creditors' voluntary liquidation.

There were a number of preliminary issues decided by the Court. The Court decided that:

(1) The expenses incurred in the preparation of statements of affairs and in connection with the convening of the section 98 creditors' meeting should only be paid where they are reasonable and necessary pursuant to section 115 of the Insolvency Act 1986 and rules 4.38 and 4.62 of the (applicable) Insolvency Rules 1986.

(2) While the Rules do not expressly refer to the expenses of the members' meeting, the court could direct payment of these expenses if they were properly incurred; following *Re A V Sorge & Co Ltd* (1986) 2 BCC 99,306 and *Re Sandwell Copiers Ltd* (1988) BCC 227.

(3) These pre-liquidation expenses are governed by the priority set out in rule 4.218(3) of the Rules and are necessary disbursements (m) if they do not fall within (k) as payments to a person employed to prepare the statement of affairs.

(4) The monies held by the Applicant in its client account were not held on trust or subject to security in favour of the Applicant.

(5) The Liquidators were wrong in their argument that the Court is required to investigate the time spent by the Applicant to comply with the judicial and professional guidance on the assessment of fees in circumstances where the Applicant had agreed a fixed fee (in keeping with standard practice for this work) and did not intend to rely on the hours actually spent in addressing the issue as to whether the agreed fee was reasonable.

There is a further hearing listed for the Court to determine the reasonable fee for the work done by the Applicant.

**[Hilary Stonefrost]**

## DP Holding SA [2017] Lexis Citation 19 (Mr Registrar Baister, 23 February 2017)

*BVI provisional liquidation – BVI court's request for assistance – request to order private examination – procedural irregularities in applications to English court*

DPH, a Swiss-incorporated company, had been placed in provisional liquidation in the British Virgin Islands at the behest of creditors seeking to enforce a substantial arbitral award. The BVI court requested assistance from the English court, and on an urgent ex parte application under section 426 of the

Insolvency Act, the English court permitted the provisional liquidators to issue a section 236 application for the private examination of the respondents. The respondents in turn applied to set aside the section 426 order on the basis that the provisional liquidators had failed to comply with their commitments to the BVI court, failed to disclose those commitments to the English court, and had committed other procedural irregularities. While accepting that several such irregularities had occurred, the Registrar nevertheless refused to set aside the section 426 order since there remained a good basis for assisting the BVI court and discharging the order would be wasteful and disruptive of the provisional liquidation. As to the section 236 application, the Registrar noted that the company was seeking in the BVI court to set aside the provisional liquidation order. If it succeeded, the English court would be functus; otherwise, the respondents were in any case willing to cooperate voluntarily in providing information, so the order was not necessary.

## Re Burnden Group Lt [2017] EWHC 406 (Ch) (His Honour Judge Stephen Davies, sitting as High Court Judge, 2 March 2017)


JOHN BRIGGS

*Liquidator's personal liability for costs*

The applicants had successfully appealed the decision of the respondent, the liquidator of a company, to reject their proof of debt. They now applied for an order directing the liquidator personally to pay their significant costs in circumstances where the company had no assets to meet them. They argued that the liquidator had vigorously contested the appeal not in exercise of his quasi-judicial power to adjudicate the validity of a proof but instead as a necessary precondition to bringing a misfeasance claim against the applicants. The court held that the liquidator was obliged to make a decision on the validity of a submitted proof, and on the facts, had been justified in rejecting the proof as originally submitted. Further, while there was undoubtedly a connexion between the liquidator's handling of the proof of debt and the contemplated misfeasance action, the connexion was not so close nor the liquidator's conduct in relation to the proof so inextricably linked to the misfeasance issue, as to make it appropriate for the court to render the liquidator personally liable. In the result, 80% of the applicants' costs were ordered to be regarded as expenses of the liquidation.

**[John Briggs]**

## Kean v Lucas [2017] EWHC 250 (Ch) (Mr Registrar Briggs, 3 March 2017)

*Creditors' voluntary liquidation – requisite majority of creditors requesting meeting to consider liquidator's removal – whether court has jurisdiction to direct that no meeting be called*

The requisite majority of the creditors of a company had requested a meeting to consider the liquidator's removal, which, given creditor views, was said to be a foregone conclusion. The liquidator resisted and the Applicant, a creditor who was also the company's former director and shareholder, applied to the court to direct him to hold a meeting. By way of his own application under section 112 of the Insolvency Act for a direction that a meeting not be called, the liquidator argued that the applicant was motivated by the ulterior purpose, namely, to forestall investigations into her management of and dealings with the company in the period leading up to the liquidation. After an extensive review of the authorities, the Registrar held that, in relation to a creditors' voluntary liquidation, an applicant under section 112 must demonstrate that the determination of the question or exercise of power sought by the applicant would, on an objective consideration of class interests, be just and beneficial to the winding-up. If this test is met, the court has discretion but not a duty to make an order or direction. On the facts, the liquidator had failed to establish that a direction that the meeting not be called would be just and beneficial to the winding-up. There was no evidence of an active ongoing investigation by the liquidator, the viability of any claims arising from such an investigation was merely speculative, and it had not been established that a new liquidator would stymie their pursuit. Even if the liquidator had established that the court had jurisdiction under section 112, the Registrar would have refused to exercise it in his favour in deference to a proper request by creditors, the absence of any evidence of abuse or impropriety or that a new officeholder would act improperly and the liquidator's failure to demonstrate that restraining a meeting would be in the creditors' class interests.

**[Andrew Shaw]**

# PERSONAL INSOLVENCY

Digested by MATTHEW ABRAHAM


MATTHEW ABRAHAM

## Willmont v Elm International Ltd [2017] EWHC 428 (CH)

*Permission to serve proceedings out of the jurisdiction and interim injunctive relief*

This case arose out of an ex parte application for two heads of relief. First, for permission to serve out of the jurisdiction a claim form which was issued on 5 January 2017 against three defendants and subsequently amended to include two additional defendants with a further amendment on the day of the hearing to add a further Defendant. The second application was for proprietary injunctions and associated relief against all the five original defendants.

The claim was brought by the trustees in bankruptcy of Mikhail Shlosberg who was discharged on 29 November 2016. The claimants do not accept that Mr Shlosberg gave full disclosure of his assets in his bankruptcy, still less vested those assets in his trustees. The claimants claim (by way of 9 claims) that each of the defendants holds assets which are beneficially owned by Mr Shlosberg.

The principal assets which the claim targets are two pieces of real estate in England valued at £40 million or thereabouts. The first and second defendants are respectively the registered proprietors of those assets, which are two residential properties in London. The claimants put the application to serve the claim form out of the jurisdiction on two alternative bases: firstly, under rule 12A.20 of the Insolvency Rules 1986 and paragraph 6.6 of the Practice Direction for Insolvency Proceedings; and secondly, under CPR 6.36 and 6.38.

In relation to the first ground the Court was not satisfied that the claims in the claim form and developed in the Particulars of Claim were insolvency proceedings. The Court found that the claims were not brought under any provision of the Insolvency Act 1986 or the Insolvency Rules and that they were brought against third parties to the bankruptcy. In particular, the Court held that the fact that the claims are brought by trustees in bankruptcy for the purposes of getting in the bankrupt's estate does not make the claims insolvency proceedings. The Court did however find that it had jurisdiction under the CPR and granted permission to serve out save in respect of one of the 9 claims which was for declaratory relief in relation to unidentified property.

In relation to the injunctive relief the Court granted a modified form of the relief sought.

## Oraki v Bramston [2017] EWCA Civ 403 (Sir Terence Etherton MR, McCombe, David Richards LJJ, 24 May 2017)

*Professional Negligence claim against a Trustee in Bankruptcy*

The appellants, Dr Sheida Oraki and her husband Mr Ardeshir Oraki, brought an action for damages against the respondents as successive trustees in their respective bankruptcies. The respondents were alleged to have acted in breach of duty to the appellants in their conduct of the bankruptcies in a significant number of respects, but in particular it was said that they had prolonged the administration of the bankruptcy estates and had frustrated the appellants' attempts to annul their bankruptcies. Following a seven-day trial, Proudman J dismissed the action. This appeal was brought with permission granted by the judge both on issues of fact and law.

As regards the factual basis for the claims, two grounds of appeal were advanced by the Appellants. First, that the judge was wrong not to find that the trustees had unnecessarily prolonged the bankruptcies, by failing to use the liquid funds available to them to pay the debts, costs and expenses of the estates. Secondly, that the judge was wrong not to find that the trustees had unnecessarily prolonged the bankruptcies, in particular by actively opposing the applications by the appellants for the annulment of their bankruptcies. Prior to dealing with the two grounds of appeal on the facts the Court helpfully went through the law governing the annulment of a bankruptcy at paragraphs 52 to 63.

Following a review of the facts of the case the Court held that the appeal failed on its facts. As a result it was not necessary for the Court to reach conclusions on the legal issues that would otherwise have arisen. That said the Court made obiter comments in relation to the legal issues that arose. The legal issues arose as a result of the first instance judge accepting that (i) the duties of a trustee in bankruptcy to the bankrupt are governed exclusively by section 304 of the Insolvency Act 1986 and that no duties are owed at common law, (ii) in any event, the effect of a release of the trustee under section 299 of the Insolvency Act 1986 is to preclude any claim save under section 304, and (iii) again in any event damages were not recoverable for mental distress. In relation to section 304, while noting that this was not the

case to deal specifically with the legal issue, the Court noted that the section cannot be read as excluding any liability on the part of a trustee to a bankrupt, save as expressly provided by the section and so it does not exclude the possibility a duty in respect of loss caused to the bankrupt personally. In relation to the effect of section 299 the Court raised doubt with the finding of the first instance Court however made it clear that it did not propose to deal with its effect as it was unnecessary on the facts of the case.

**[John Briggs]**

# PROPERTY & TRUSTS

Digested by ANDREW SHAW


ANDREW SHAW


MARCUS HAYWOOD


HENRY PHILLIPS

## Lavarello & Hyde v Jyske Bank (Gibraltar) Ltd, Supreme Court of Gibraltar (Jack J), 17 May 2017

*Dishonest assistance - knowing receipt - section 85 Solicitors Act 1974*

Three brothers in a firm of solicitors in Gibraltar, Marrache & Co ("the Firm"), stole monies from the firm's client accounts, the total deficit of the Firm being in excess of £28 million. The three brothers were sent to prison in Gibraltar for between 7 and 11 years following the longest criminal trial in the history of Gibraltar.

On 17 March 2010, Edgar Lavarello and Adrian Hyde were appointed as liquidators of the Firm. They brought proceedings against Jyske Bank (Gibraltar) Limited ("the Bank") on behalf of the defrauded clients of the firm. The claims made were in dishonest assistance in a breach of trust and knowing receipt. The trial of the proceedings took place between 6 and 28 February 2017.

By his judgment dated 17 May 2017, Jack J found the principal account manager for the Firm at the Bank, Bill Bishop, to have been guilty of both dishonest assistance and knowing receipt. Jack J concluded that Mr Bishop had, at least, blind-eye knowledge. However he then went on to consider whether Mr Bishop was in fact aware that monies were being stolen from clients of the Firm. He concluded that Mr Bishop was aware and that this was so from at the latest mid-2004 and that his dishonest assistance continued until the Firm went under in 2010. The Judge held that Jyske were liable for his behaviour and that Section 85 of the English Solicitors Act 1974 (as imported into Gibraltar) did not provide the Bank with any defence in such circumstances.

The Judge then said that, since the earliest losses sustained by clients represented by the claimants occurred in mid-2005, Jyske was liable for all of those losses on the basis of dishonest assistance and knowing receipt. He ordered that these losses be determined by the taking of an account.

**[David Alexander QC, Marcus Hayward and Henry Phillips]**

# SPORT

Digested by ROBERT AMEY


ROBERT AMEY

## McGill v Sports and Entertainment Media Group [2017] 1 WLR 989 (Lord Justice Lloyd Jones, Henderson J, 4 November 2016)

*Football Agents Regulations – contract between player and agent not complying with Regulations – rival agent allegedly procuring a breach of contract*

The claimant, M, had entered into an oral agreement with G, a professional footballer, under which M was to act as G's exclusive agent in finding him a new club and in negotiating contractual terms with that club. M asserted that he had negotiated a deal for G's transfer to Bolton Wanderers. However, before the deal was concluded, the defendant (SEM) was instructed by Bolton Wanderers to find a player. G subsequently joined Bolton Wanderers on essentially the same terms that M had previously negotiated. SEM was then paid a fee of £300,000.

M sued G for breach of contract, and settled that action for £50,000. M then brought proceedings against SEM, Bolton Wanderers and others alleging that the defendants had induced a breach of the contract between M and G. M also alleged a conspiracy to injure, a conspiracy to use unlawful means, unlawful interference and unjust enrichment.

At first instance, the court found that SEM had clearly induced G to breach his contract with M. However, at the relevant time, the Football Agents Regulations required contracts between players and agents to be in writing, and M accepted that he would not have been entitled to receive commission had his contract with G not been reduced to writing. The trial judge found as a fact that G would not have agreed to sign a written contract. Accordingly, although M had established wrongdoing on the part of SEM, that wrongdoing had not caused M any loss. M appealed.

Allowing the appeal, the Court of Appeal held that M was entitled to damages for the loss of a chance that G might have entered into a written contract with him which would have satisfied the Football Agents Regulations, thereby entitling M to commission. The case was remitted to the judge for him to assess the percentage likelihood that G would have entered into a written agreement.

## Aljaž Bedene v International Tennis Federation (Charles Hollander QC sitting as sole arbitrator, 2 March 2017)

*Slovenian-born athlete acquiring British nationality – whether eligible to represent Great Britain in the Davis Cup – EU freedom of establishment – irrationality*

The International Tennis Federation (ITF) organises the annual Davis Cup competition, in which different national teams compete against each other. The ITF manages the Davis Cup in accordance with the Davis Cup Regulations, which (among other things) set out the eligibility criteria of participants both in terms of the nations that may enter and the players who are eligible to compete for a nation.

In around September 2013, the ITF became concerned with the ease with which players could switch nationalities in order to become eligible to compete in the Davis Cup. Under the Davis Cup Regulations in force at the time, an athlete could switch nationalities and play for his new country, provided that he had lived in his new country for 24 consecutive months, and had not played for any other country in the preceding 36 months. At the 2014 AGM of the ITF, it was resolved to amend the Davis Cup Regulations to insert a new Regulation 35, providing that a player could only ever represent one nation at senior professional international level, unless the Davis Cup committee agreed to make an exception.

Mr Bedene was born in Slovenia in 1989, and represented Slovenia at u14, u16 and u18 levels. He moved to the UK in 2008, but continued to represent Slovenia in international tennis, competing for Slovenia at the 2010, 2011 and 2012 Davis Cup tournaments. In 2015, Mr Bedene acquired British citizenship. At the time Mr Bedene submitted his application for British citizenship, the Davis Cup Regulations had not yet changed. Mr Bedene had lived in the UK for 7 years, and had not played for Slovenia for nearly 3 years. Accordingly, under the regime as it was at the time, Mr Bedene would have been eligible to play for Great Britain in the 2015 Davis Cup. However, as a result of the rule change in 2014, Mr Bedene was obliged to apply to the Davis Cup Committee for an exemption. That application was refused, and Mr Bedene commenced arbitral proceedings to challenge the refusal.

Mr Bedene's challenge was put on three bases. First, it was said that Regulation 35 breached Mr Bedene's EU right of freedom of establishment. Secondly, it was said that even if Regulation 35 is justifiable in general, the refusal to grant an exemption to Mr Bedene was discriminatory and disproportionate. Thirdly, it was said that the decision not to grant an exemption was unfair and/or irrational.

The tribunal accepted that Mr Bedene had genuinely settled in the UK, and was not merely adopting British citizenship as a 'flag of convenience'. It also noted that the effect of Mr Bedene's defection was to "burn bridges" with the Slovenian Tennis Federation. The tribunal expressed "the greatest sympathy" for Mr Bedene, who through no fault of his own had found himself unable to play for either Great Britain or Slovenia, as a result of a rule change that came "at precisely the wrong time for him". However, the tribunal rejected all three bases on which Mr Bedene challenged the decision.

First, while EU freedom of establishment rules apply to the employment of athletes in the same way that they apply to any other type of employment, the Court of Justice of the European Union has long recognised the right of sports governing bodies to exclude athletes from a national team on the basis of nationality. The tribunal considered that Regulation 35 did indeed engage Mr Bedene's EU law rights, but that the ITF was able to justify the restriction placed on Mr Bedene's freedom of establishment.

Dealing with the second and third bases together, the tribunal noted that the ITF did not provide any reasons for its decisions, and so there was no ground for saying that the ITF's decision-making process was defective. Mr Bedene's contention was essentially that any decision to refuse him an exemption was necessarily unlawful. The tribunal noted that it should be slow to interfere with the decision of a specialist decision-making body, and yet Mr Bedene's case invited the tribunal to usurp the ITF Board entirely. Accordingly, Mr Bedene's second and third bases of challenge failed.

The tribunal therefore dismissed the application, while expressing hope that if Mr Bedene applied for an exemption at some point in the future, the ITF might change its mind.

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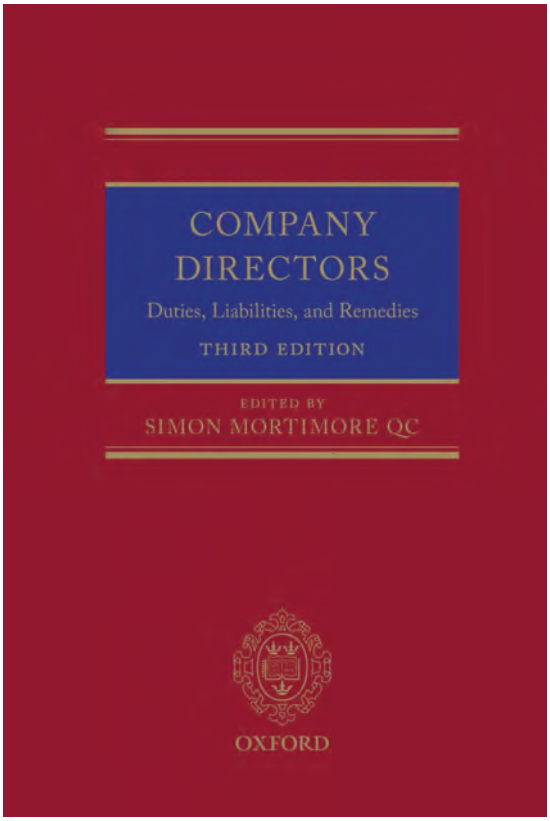


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# Winding up investment funds for "loss of substratum" – the end of the road?

**Tom Smith QC** and **James Elliott**, of Harney Westwood & Riegels, consider the approach taken by the Cayman Islands Courts to winding up petitions presented on grounds of "loss of substratum"

A Cayman Islands company is one of the favoured vehicles for setting up an investment fund. Since the original enactment of the Mutual Funds Law in 1993, very substantial numbers of investment funds have been established as exempted companies or segregated portfolio companies under the Cayman Islands Companies Law. However, the remedies available to investors in such funds – who are typically issued with non-voting shares – are often limited to the "nuclear remedy" of presenting a winding up petition.

An ongoing issue that the Cayman Courts face is in what circumstances an investor should be entitled to have a fund wound up and liquidators appointed. This issue often arises when an investment fund has ceased to carry on business in the way envisaged in its offering documents. This might arise where a fund has ceased to accept new investments, has suspended redemptions and gone into a "soft wind down".

### Historical position – the English approach

Petitions presented for the winding up of Cayman funds have typically been those seeking a "just and equitable" winding up on the ground that the company has "lost its substratum". The existence of this ground was first recognised in England in *Re Suburban Hotel Co* (1866-67) LR 2 Ch App 737. There, Lord Cairns stated that if it was shown that "the whole substratum of the partnership, the whole of the business which the company was incorporated to carry on, has become impossible", then this might justify the making of a winding up order.

The rationale has historically been that majority shareholders ought not to be entitled to compel the minority to continue to commit capital for an enterprise which has become entirely different from that which was originally contemplated. In *Re Diamond Fuel Company* (1879) 13 Ch D 400 the Court of Appeal upheld a decision to make a winding up order on this basis. In doing so, James LJ stated: "The ground for the order seems to me to be this, that the company had, to all intents and purposes, come to an end without the slightest hope or prospect of ever being resuscitated".

The "impossibility" argument was then developed in *Re German Date Coffee Company* (1882) 20 Ch D 169. There, the company had been formed for the purpose of exploiting a specific patent to manufacture a partial substitute for coffee made from dates. The patent was not granted and the company could not carry on the business for which it had been formed. Baggally LJ stated that "...if you have proof of the impossibility of carrying on the business contemplated by the company at the time of its formation, that is a sufficient ground for winding up the company. Therefore the question arises in the present case, is there an impossibility of carrying out the objects of the company?"

This updated rationale was later endorsed by Jenkins J in *Re Eastern Telegraph Co Ltd* (1947) 2 All ER 104: "... if a shareholder has invested his money in the shares of the company on the footing that it is going to carry out some particular object, he cannot be forced against his will by the votes of his fellow shareholders to continue to adventure his money on some quite different project or speculation". [see also *Re Kitson & Co Ltd* (1946) 1 All ER 435].

### The position under Cayman Islands law

The principles summarised above reflect the present state of the law in England and in other common law jurisdictions. However, in a series of


TOM SMITH QC

cases in the Grand Court, a different approach has been taken in relation to open-ended investment funds.

*Re Belmont Asset Based Lending Limited* [2010] (1) CILR 83 concerned an open-ended corporate mutual fund which had attracted investors for the purpose of investing in a portfolio of asset-based lending and related strategies. As a result of market conditions following the liquidity squeeze in and around September 2008, it was accepted by the fund's management that it was no longer able to pursue its investment objective or viable as a mutual fund.

Mr Justice Jones considered some of the above English authorities and widened the "impossibility" test, making clear that in respect of open-ended corporate mutual funds it could be said to be just and equitable to make a winding up order "if the circumstances are such that it has become impractical, if not actually impossible, to carry on its investment business in accordance with the reasonable expectations of its participating shareholders, based upon representations contained in its offering document".

The sentiments underlying this decision can readily be understood: why should an investor who invested funds on the basis of an investment approach set out in the offering documents be locked into a fund which is no longer carrying on that business, has suspended redemptions and is in an informal "wind down" but under the control of its existing management rather than a liquidator?

*Re Matter of Wyser-Pratte Eurovalue Fund Ltd* [2010] (2) CILR 194 concerned an open-ended mutual fund and a feeder fund in a typical master-feeder structure. In September 2008, the company suspended redemptions of its shares. In March 2010, the company distributed a "wind down plan" to investors. Jones J held that the company had ceased to be a viable open-ended mutual fund by the time the petition had been presented, stating that: "By definition, a company cannot be said to be carrying on business as an open-ended mutual fund if its ability to redeem shareholders in cash and its ability to accept new subscriptions has been terminated permanently".

The loss of substratum ground was subsequently considered by the High Court of the British Virgin Islands in *Aris Multi-Strategy Lending Fund Ltd v Quantek Opportunity Fund Ltd* [BVIHCOM 2010/0129] which concerned another open-ended mutual fund operating as a feeder fund. The company suspended redemptions and proceeded with the winding down and distribution of its assets. Refusing to make a winding up order, Mr Justice Bannister considered both the English authorities above, before turning to *Belmont and Wyser-Pratte*. The BVI Judge noted that the reasoning of Jones J was confined to open-ended investment funds, but held that there could not be a separate principle applying to a

particular type of business. He also rejected the concept of "viability" as the touchstone for determining loss of substratum because it was too uncertain. Instead, he reverted to the English test of impossibility, and in doing so dismissed the petition.

Further consideration was given in the Cayman Islands case of *Re Heriot African Trade Finance Fund Limited* [2011] (1) CILR 1. There, the fund had received redemption requests from a majority of its investors, had suspended redemptions and had stated its intention to permanently cease investment operations, liquidate its assets and repay investors. In winding up the company, Jones J followed his earlier decision in *Belmont* and identified the question as being whether it had become "practically impossible" to carry on its investment business in accordance with the reasonable expectations of its participating shareholders based upon the representations contained in the relevant offering document.

In *ABC Company (SPC) v J & Company Limited* [2012] (1) CILR 300 the Cayman Islands Court of Appeal overturned the first instance decision of Jones J [Unreported, 1 August 2011] dismissing an application to strike out a petition presented on grounds of loss of substratum as a result of the company having temporarily suspended the calculation of the NAVs of 18 of its segregated portfolios (***SPs***). The Court of Appeal determined that there was no reasonable prospect of establishing that a suspension of the minority of the SPs meant that the company itself had ceased to carry on business in accordance with the reasonable expectations of its shareholders. In doing so, Chadwick P recognised the conflicting Cayman and BVI authorities at the time, stating:

JAMES ELLIOTT

"It must be anticipated that an appeal will come before this court in which it will be necessary to choose between the approach of Jones, J. in *Belmont* and *Heriot* on the one hand, and that of Bannister, J. in *Aris v Quantek* on the other hand: or, perhaps, to decide that the true approach in this jurisdiction should lie somewhere between the approaches respectively adopted in those cases. But this is not that appeal".

## Where are we now?

Both the English and Cayman tests were considered in *Re Harbinger Class PE Holdings (Cayman) Ltd* [FSD 80/2015], a case relating to the Harbinger hedge fund run by Philip Falcone.[1] An investor sought the winding up of the company, again alleging loss of substratum.

The company was initially incorporated as a subsidiary of a feeder fund in a master-feeder structure. Investors subscribed for shares in the feeder fund, whose sole asset was in turn shares in the master fund. As a result of the financial crisis, the feeder fund received substantial redemption requests which could not be met. In response, the master fund (which had back-to-back redemption obligations to the feeder) created a new class of shares to which it allocated certain private equity-type investments (***Investments***) from within its managed portfolio. The new shares were subsequently used to satisfy in part the redemption claims by way of an in specie redemption.

The principal allegation made by the petitioner in the *Harbinger* case was that the company had stated in a supplement to the confidential offering memorandum of the feeder fund, issued in December 2008, that it would use "commercially reasonable efforts" to complete the redemption of shares by the end of 2010, but had failed to do so.

Mr Justice Clifford adopted the English "impossibility" test and dismissed the petition. In doing so, the Judge looked beyond the wholly general objects clause of the company and found on the evidence that the principal object for which the feeder fund was formed was limited to holding the shares issued by the master fund and receiving net available cash flow from the realisation by the master fund of the Investments, for onward payment to shareholders. The company was fulfilling this purpose and continued to do so.

The decision in *Harbinger* illustrates the Grand Court's demarcation between the recent line of Cayman authority (made up of cases decided after the financial crisis involving open-ended mutual funds) and the English test applied by Clifford J here.

Most recently, Mrs Justice Mangatal considered another Cayman winding up petition in *Re Washington Special*

*1/. Tom Smith QC and Harney Westwood and Riegels acted for Harbinger Class PE Holdings (Cayman) Ltd.*

PHILIP FALCONE, WHO FOUNDED HARBINGER CAPITAL PARTNERS IN 2001

*Opportunities Fund Inc* [FSD 151/2015], presented on grounds including an alleged loss of substratum. Both the fund and its manager opposed the petition, arguing that, amongst other things, the fund was continuing to fulfil its purpose, despite being in "soft wind down". The petitioner cited *Belmont*, to support its case that the fund was in "soft wind down", that it was non-viable and that a winding up order should be made.

Mangatal J found that there was no loss of substratum, since there was insufficient evidence that the fund had actually failed in the pursuit of its commercial objectives:

"I am of the view that neither on the Belmont line of authority, nor on the more traditional impossibility test, is there room for properly finding that this Fund has lost its substratum or that it is non-viable. This is not a fund in respect of which it could properly be said, as Jones J. said of the fund in *Heriot* that it had "failed commercially". In other words, on the evidence, it has not been demonstrated that it is either actually impossible, or impracticable for the Fund to carry on its business in accordance with the reasonable expectations of its investors".

## Conclusion

There are a number of points which can be made in conclusion. The first is that, whatever test is applied for assessing loss of substratum, as a matter of Cayman Islands law, the Court will determine the purpose for which the company was formed by reference to all the evidence of the expectations of the shareholders, and not merely by reference to the objects clause in the memorandum of association. This seems a sensible approach, during times when objects clauses are typically entirely general.

Beyond that, there could be said to be a divergence in approach in the Cayman Islands depending on the type of corporate entity at issue. In relation to open-ended corporate funds which have issued shares to investors on the basis of offering documents, the test arguably remains whether it has become impractical for the relevant company to carry on its investment business as advertised in its offering documents. In relation to other companies, the test appears to be whether it has become impossible for the company to achieve the purpose for which it was formed. It remains to be seen whether this amounts to a genuine distinction in practice, or whether the Courts will find an opportunity in due course to create a unified test for all cases.

# Limitation periods for Jersey Law Directors' Duties claims

**William Willson** on an important recent decision in relation to directors' duties claims brought under the laws of Jersey

## Introduction

What is the applicable limitation period for claims against directors under Article 74 of the Companies (Jersey) Law 1991?

Remarkably, for a jurisdiction where the financial services sector is the dominant sector in the local economy and where so many are employed as professional directors, this is a question in relation to which there is no decisive Jersey law authority. Indeed, Jersey does not even have a limitation law statute.

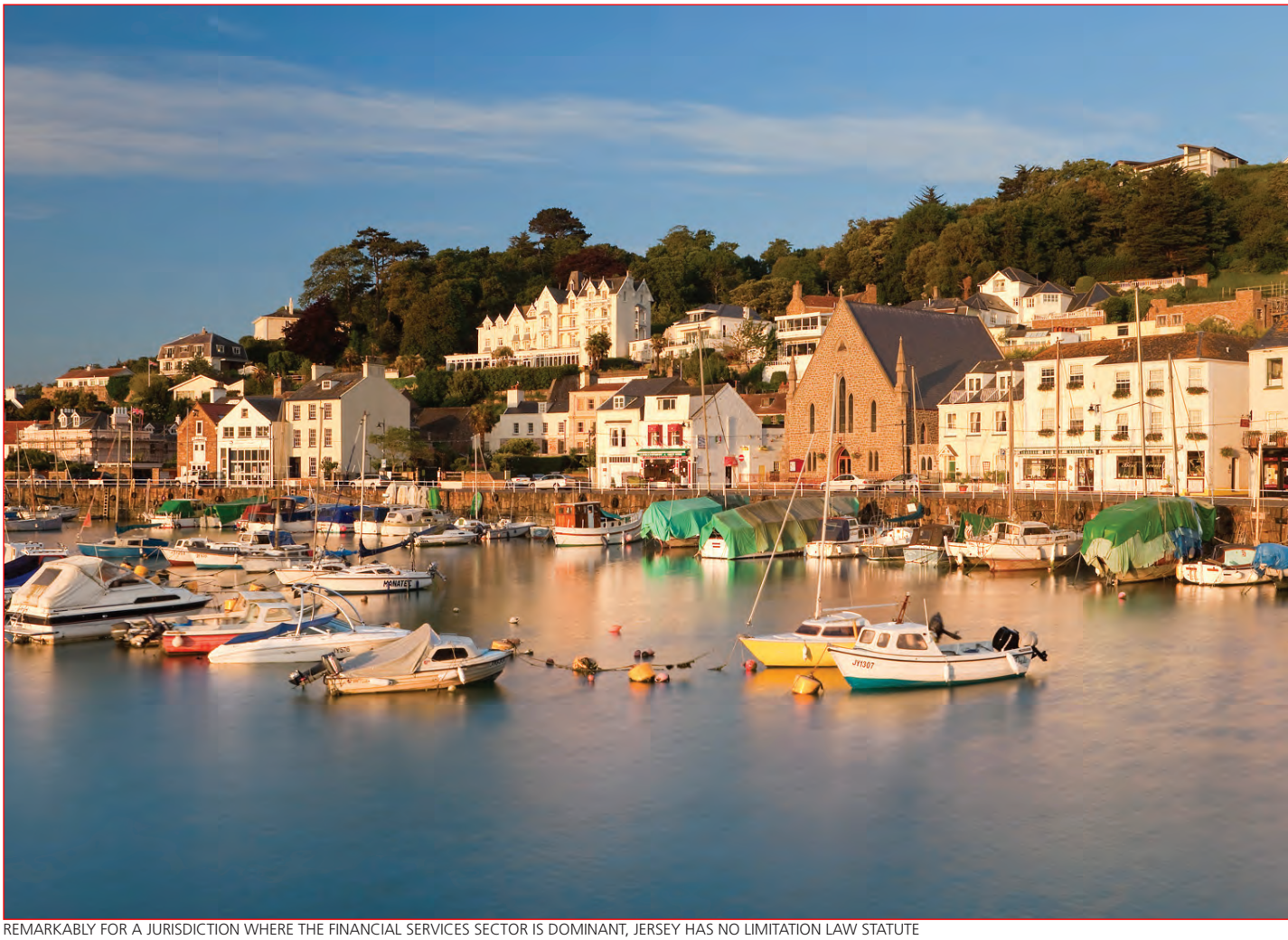
However, in the recent decision of *O'Keefe & Or v Caner & Ors* [2017] EWHC 1105 (Ch), the English High Court (HHJ Keyser QC) concluded that, as a matter of foreign law, the applicable limit in relation to both limbs of Article 74 is 10 years, not 3 years. Though not binding on the courts of Jersey, the decision is persuasive authority, and therefore likely to provide some considerable weight on this issue unless and until the question is resolved by legislation.

## Background

The applicants were the joint official liquidators ("**the Official Liquidators**") of Level One Residential (Jersey) Limited ("**Level One**") and Special Opportunity Holdings Limited ("**Special Opportunity**") (together, "**the Companies**"). The Companies were incorporated in Jersey, but their centre of main interests was in England, and they were put into administration in England in 2008 on the basis of High Court orders, and subsequently into liquidation in 2012.

The first respondent was the ultimate beneficial owner of the Companies and was at all material times a director of the Companies. The second to fifth respondents were each professional directors of one or both of the Companies. The sixth respondent, Capita Trustees Limited ("**Capita**"), was a professional trust company that provided services to the Companies, including the appointment of the second to fifth respondents as professional directors.

The applicants issued proceedings against all of the respondents under section 212 of the Insolvency Act 1986 ("**IA86**") seeking declarations that the respondents were guilty of misfeasance and breach of duty in respect of various payments made out of the Companies in the 18-month period before the administration orders, and for an order for the payment of the equivalent sum of the payments ("**the Special Opportunity Litigation**"). In particular, their case was that between 10 April 2007 and 10 June 2008 payments of some €16 million from Level One's bank account and of some €18 million from Special Opportunity's bank account were made to or for the benefit of the first respondent or companies owned by him; that the payments were not made in good faith or for a legitimate commercial purpose; that they were not made for any or any adequate



REMARKABLY FOR A JURISDICTION WHERE THE FINANCIAL SERVICES SECTOR IS DOMINANT, JERSEY HAS NO LIMITATION LAW STATUTE

consideration; that throughout the relevant period the Companies lacked sufficient reserves; and that in causing or permitting the payments the first to fifth respondents acted in breach of their duties as directors of the Companies and did not (a) act honestly and in good faith with a view to the best interests of the Companies or (b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

The specific duties relied upon in relation to the directors' duties claims against the first to fifth respondents are set out in Article 74 (1) of the Companies (Jersey) Law 1991 ("**the Companies Law**"), which provides that:

"*A director, in exercising the director's powers and discharging the director's duties, shall –*

*(a) Act honestly and in good faith with a view to the best interests of the company; and*

(b) *Exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances*".

The first to fifth respondents denied the allegations.

A central part of their defence was that the limitation period for the claims against them as a matter of Jersey law was 3 years, as being the relevant time period applicable for claims for both breach of trust and tort under Jersey law, and that the claims were therefore time-barred.

The applicants contended that the applicable limitation period was 10 years as being the default period applicable to personal claims under Jersey law.

The issue of the applicable limitation period in relation to claims under Article 74 (1) therefore became the subject of a preliminary issue, which was tried over 6 full days of evidence and argument before HHJ Keyser QC ("**the Judge**") in the Chancery Division during March 2017.

It was common ground amongst the parties that the issue of limitation fell to be determined according to Jersey law. This was because:

NORTHWIND YACHTS LTD [2005] JLR 137 CONSIDERED THE ISSUE OF THE APPLICABLE PRESCRIPTION PERIOD FOR DIRECTORS' DUTIES CLAIMS, BUT OBITER

(a) The duties of the first to fifth respondents fell to be determined in accordance with the laws of Jersey, being the place where the Companies were incorporated: see *Base Metal Trading Ltd v Shamurin* [2005] 1 WLR 1157.

(b) Where a cause of action is governed by the law of a foreign jurisdiction, the limitation period applicable to the cause of action is governed by the same foreign law: see section 1 (1) of the Foreign Limitation Periods Act 1984.

(c) Section 212 of IA86 is a procedural mechanism whereby an office holder may vindicate a cause of action vested in the company, so that the relevant limitation period is that applying to the company's cause of action: see *Re Eurocruit Europe Ltd* [2008] Bus LR 146.

It was also common ground that there was no authoritative decision of the Jersey courts that was determinative of the preliminary issue.

*It was common ground between the parties that there was no authoritative decision of the Jersey courts determinative of the preliminary issue*

Since the content of the law of Jersey is a matter of fact, which must be proved by expert evidence, the court was therefore assisted by evidence from three experts, each of whom were Jersey lawyers and solicitor-advocates. As the Court of Appeal explained in *Macmillan Inc v Bishopsgate Investment Trust plc* [1999] CLC 417, at [23]-[24], the function of expert evidence as to foreign law is: (1) to inform the court of the relevant contents of the foreign law, identifying statutes or other legislation and explaining where necessary the foreign court's approach to their construction; (2) to identify judgments or other authorities, explaining what status they have as sources of foreign law; and (3) where there is no authority

directly in point, to assist the English judge in making a finding as to what the foreign court's ruling would be if the issue was to arise for decision there.

## Arguments, Analysis and Conclusions

As the Judge made clear at the start of his judgment, there is no decisive Jersey authority on the matter. To date, the issue of the applicable prescription period for breach of director's duty under Article 74 (1)(a) and (b) has been considered obiter and in relatively short form in two Jersey cases, *In the matter of Northwind Yachts Ltd* [2005] JLR 137 and *Alhamrani v Alhamrani* [2007] JLR 44, and in even shorter form in a case management decision by a master in *CMC Holdings Ltd v Forster* [2016] JRC 149.

Nor does Jersey have a statute of limitation. The starting point is that where there is no specific period, the default period is 10 years save where another period is by analogy clearly more applicable (*Re Esteem Settlement* [2002] JLR 53). In relation to application by analogy, the Judge clarified that:

"*the dicta in those cases [Northwind and Alhamrani] indicate that the judges of the Jersey courts have not understood analogous application of prescriptive periods to involve mere comparison of causes of action but have had regard to considerations involving the coherence of the law and the practical convenience of departing from the 10-year default period in any given case. Such considerations seem to me to be quite different from the sort of policy considerations – for example, an opinion that in society a shorter or longer period is more desirable – that are properly the preserve of the legislature*".

The Judge analysed the competing arguments by reference to the different nature of the duties

WILIAM WILLSON

contained in Article 74, those that were fiduciary in nature (Article 74 (1)(a)) and those that could broadly be described as a duty of care and skill (Article 74 (1)(b)).

Article 74 (1)(a)

The respondents argued that:

(a) As directors' duties in Jersey law are statutory, breach of them must *ipso facto* constitute the tort of breach of statutory duty to which Article 2 of the Law Reform (Miscellaneous Provisions) (Jersey) Law 1961 (**"the Reform Law"**), which prescribes a 3-year limitation period, applies directly or by way of analogy (**"the Statutory Duty Argument"**); alternatively the duty was essentially of a tortious nature, so that Article 2 applies directly or by way of analogy (**"the Tortious Argument"**).

(b) Article 57 of the Trusts (Jersey) Law 1984 **("the Trusts**

*In the absence of a statute for prescription under Jersey Law, the default period of limitation for an action personelle mobilière applies*

**Law")** in relation to breach of trust applies either directly or by way of analogy to breach of a director's duty (**"the Trusts Law" Argument**").

The applicants argued that the default 10-year period for an *action personnelle mobilière* (a 'personal action') applies, and there is no other period that applies either directly or by way of analogy

The Judge rejected all of the respondents' arguments.

First, in relation to the Statutory Duty Argument, the Judge concluded that: the Jersey law authorities relied on do not support the conclusion that if an actionable duty exists by virtue of a statutory provision then breach of that duty is *ipso facto* a tort; if (as was accepted) the law of Jersey and England are the same in relation to breach of statutory duty, then there are plenty of examples of statutory duties that are not tortious in nature (e.g. the duties of a trustee under the Trustee Act 2000); critically, fiduciary duties and tortious duties are fundamentally different in their nature; and the Jersey case law shows that what are formerly fiduciary duties remain fiduciary duties notwithstanding that they have been given statutory form.

RYAN PERKINS, WHO ACTED TOGETHER WITH ANTONY ZACAROLI QC AND WILLIAM WILLSON FOR THE OFFICIAL LIQUIDATORS IN THE SPECIAL OPPORTUNITY LITIGATION

Second, as for the Tortious Argument, it was common ground that the duty under Article 74 (1)(a) is a fiduciary duty in the sense explained by Millett LJ in *Bristol and West Building Society v Mothew* [1998] Ch 1, and that these observations represent the modern law of Jersey and that the modern law of Jersey on fiduciary duties was imported from and is substantially the same as English law (*In the Matter of E, L, O and R Trusts* [2008] *JRC 150*; *Vilsmeier v AI Airports International Ltd* [2014] JRC 257). However, as the Judge pointed out, fiduciary duties do not give rise to causes of action in tort and, moreover, there are several obvious differences between fiduciary duties and tortious duties e.g. fiduciary duties arise in equity whereas tortious duties arise at common law, the remedies for breach of fiduciary duty are primarily restitutionary or restorative, whereas the principal remedy in tort is damages, and damage *per se* is not even a necessary requirement for a claim based on breach of fiduciary duty. The Judge therefore dismissed the argument that breach of fiduciary duty is a tort under Jersey law on the basis that there was no Jersey case to that effect, and that Jersey law is in effect the same as English law on this point.

Third, in relation to the Trusts Law Argument, the respondents relied upon Article 57 (2) of the Trusts Law, which states that "*where paragraph (1) does not apply, the period within which an action founded on breach of trust may be brought against the trustee by a beneficiary is 3 years from – (a) the date of delivery of the final accounts to the beneficiary; or (b) the date on which the beneficiary first has knowledge of the breach of trust, whichever is the earlier*". The Judge concluded that that as a matter of construction of the Trusts Law, Article 57 (2) has no direct application to an action based on breach of directors' duties under Article 74 (1). In particular, he concluded that: English directors are not by virtue of their office trustees of the company's property, because a company is the legal and beneficial owner of its property and the directors do not *qua* directors hold the company assets (relying on dicta in *Bairstow v Queen's Moat Houses plc* [2001] 2 BCLC; *JJ Harrison (Properties) Ltd v Harrison* [2002] 1 BCLC 162; and *Gwembe Valley Development Co Ltd v Koshy (No 3)* [2004] 1 BCLC 131); and Article 57 could not have direct application to company directors, not least because the very precise definitions of terms such as "*breach of trust*", "*trust*" and "*existence of a trust*" in Article 1 only apply to trusts in the strict sense.

Finally, in relation to whether Article 57 applies by way of analogy, the applicants argued that claims against wrongdoer trustees under the Trusts Law arise not only through Article 57 (2) – which relates to "beneficiaries" – but also by

Article 57 (3B) – which relates to claims by successor trustees. The weight of the expert evidence was that there was no relevant analogue in relation to directors' duties claims to claims by successor trustees: in particular, successor directors do not have rights of action; nor, significantly, do they have the same duty of investigation into the conduct of their predecessors. Further, to apply only Article 57 (2)(b) would be to impose the relatively short period of 3 years from the date when knowledge of the breach of duty can first be attributed to the company, without however making a provision for the availability of a longer period to reflect later investigation by an incoming officer by analogy with Article 57(3)(B). This means that the headline 3-year period is not in fact applied similarly for the two cases. The Judge concluded that these are powerful objections that rest not on the mere verbal difficulties but also on the substantive effect of Article 57 in the context in which it directly applies so that the Trusts Law does not apply by way of analogy.

Article 74 (1)(b)

The respondents argued that:

(a) The claim under Article 74 (1)(b) is tortious in nature and the 3-year period for tort in Article 2 of the Reform Law applies.

(b) Alternatively, the claim is founded in breach of statutory duty and is therefore a claim for tort so that the 3-year period under Article 2 (1) of the Reform Law applies directly, alternatively that the cause of action, if not for breach of statutory duty, is nevertheless tortious, so that Article 2 (1) applies directly; and as a further alternative that the limitation period for torts applies by way of analogy.

Again, the applicants argued that the 10-year period for an *action personnelle mobilière* applies; and that if, on the contrary, any other period were to apply by way of analogy, it would be the 10-year period for quasi-contractual claims (since before the enactment of the Companies Law a claim based on a director's duty of care would have been quasi-contractual).

*The best way to resolve the conflicting points of principle that have arisen in this case is through legislation*

Again, the Judge rejected the respondents' analysis and accepted the arguments of the applicants.

First, the Judge concluded that there was no evidence of any Jersey case law to support the proposition that the duty of care under Article 74 (1)(b) is tortious, nor was he shown any authority that before the Companies Law came into action Jersey law treated breach of the director's duty of care as a tort. Rather, the duty of care was an equitable one: though the distinction between the common law duty of care and the specific equitable duty of care is a fine one, it is nonetheless clear and intelligible (*Base Metal Trading v Shamurin*, per Tuckey LJ).

Second, and alternatively, the Judge agreed that the director's duty of care is best otherwise seen as a *sui generis* duty arising out of the relationship between the director and his company. The duty is most naturally akin to quasi-contract, on the basis that it arises from a particular relationship, brought about by lawfully permitted acts, which generates mutual rights and obligations quasi ex contract though not in fact by contract.

Finally, the Judge rejected the argument that the limitation period for torts applies by of analogy. He concluded that although the statutory duty is similar to the duty in the tort of negligence, it is also likely to be similar to a contractual duty of care: and that the duty has an analogy with, if it is not strictly identical to, the duty of care that arises as a matter of quasi-contract.

On this basis, the Judge concluded that the there was no good reason to apply a period other than that normally applying to personal actions.

## Commentary

The Judge therefore concluded that the prescriptive period for both causes of action under Article 74 is 10 years (not 3 years).

The decision has not been the subject of an application for permission to appeal the Special Opportunity Litigation has subsequently been compromised): and as things stand it is by far the most detailed authority on this issue, even if not strictly binding in Jersey.

It has, however, been the subject of great interest in Jersey – given its far-reaching practical consequences, most obviously for professional directors who are the subject of potential litigation, but also in other areas e.g. D&O insurance (where there will need to be increased premiums to cover potential long-tail claims).

Though the decision appears to have both its supporters and critics, the one clear area of consensus is that this critical (but still uncertain) area for the island' economy is best addressed through legislation and the enactment of a limitation statute by the States of Jersey.

*William Willson acted in the Special Opportunity Litigation for the Official Liquidators with Antony Zacaroli QC and Ryan Perkins*

# EU/EEA LAW UPDATE

GABRIEL MOSS QC

**Gabriel Moss QC looks at EU/EEA developments outside the UK**

# PRE-PACKS UNPACKED

**Federatie Nederlandse Vakvereniging v Smallsteps BV (Case C-126/16) – Advocate General's Opinion of 29 March 2017[1]**

The Court of Justice of the European Union is for the first time considering the interrelation of pre-packs and employment protection. The reference to the CJEU was made by the District Court for the Central Netherlands at the instigation of a Dutch union federation. The case concerned a Dutch prepack.

The Dutch method is to appoint a *proposed* insolvency practitioner and a *proposed* supervising "judge" before the opening of insolvency proceedings, with a view to the administrator and "judge" being formally appointed after they had studied the proposed pre-pack and immediately selling/approving the sale to the new entity. The question that arose was whether such a prepack sale was subject to the employee protections laid down by European law or whether it fell within the exception for insolvency proceedings. In particular, did the contracts of employment that employees had with the debtor migrate automatically to the purchaser, or was the administrator entitled to sack all the employees, with a view to the ones that were required to continue the business being employed on new employment contracts by the purchaser?

The Advocate General's opinion recognises that pre-packs can be a good thing and can save businesses or parts of businesses. The question was how to balance this aim with the protection of employees guaranteed by EU law.

The current Directive is Directive 2001/23, which in general terms, provides three types of protection for employees. Firstly, and perhaps most importantly, it automatically transfers contracts of employment from the debtor to the transferee of the undertaking, under Article 3 of the Directive. Secondly, under Article 4, the transfer of an undertaking "does not in itself constitute grounds for dismissal by the transferor or the transferee". However, the Directive makes clear that this provision is not an obstacle to the ability to dismiss employees for economic, technical or organisational reasons requiring changes in the workforce. Thirdly, Article 7 lays down the obligations on the part of the transferor and the transferee to inform and consult workers' representatives.

Article 5 of Directive 2001/23 provides an exception from the applicability of Articles 3 and 4:-

"Unless Member States provide otherwise, Articles 3 and 4 shall not apply to any transfer of an undertaking, business or part of an undertaking or business where the transferor is the subject of bankruptcy proceedings or any analogous insolvency proceedings which have been instituted with a view to the liquidation of the assets of the transferor and are under the supervision of a competent public authority (which may be an insolvency practitioner authorised by a competent public authority)."

The debtor in this case was Estro Groep, the largest childcare company in the Netherlands, with numerous branches in the country. After consensual discussions with creditors failed, it embarked on the aptly-named "Project Butterfly" under which a significant part of the group would continue business under new ownership, keeping most of the employees. The only potential buyer contacted was a related company. We are not told whether any marketing took place before the pre-pack.

In terms of formal steps, on 5th June 2014, the debtor submitted an application to the Amsterdam District Court for the appointment of a *prospective* insolvency administrator, who was appointed as such on 10th June 2014. On 20th June 2014 a Newco was created to take over a large part of the business of the debtor. On 4th July 2014 the debtor applied to the court for a suspension of payments. The next day, on 5th July 2014 the application was amended to become an application for a declaration of insolvency and that declaration was made the same day.

Further on the same day, the pre-pack contract of sale was signed by the insolvency administrator and the Newco under which the Newco purchased the business of most of the establishments of the debtor and agreed to offer employment to most of the employees. On 7th July 2014 the administrator dismissed all the debtor's employees and the Newco offered a new contract to most of them, but over 1,000

employees remained dismissed. A Netherlands trade union organisation and four applicants who had not been offered new contracts of employment brought an action seeking a declaration that Directive 2001/23 applied to the pre-pack that had been concluded and put into effect. They sought a declaration that the individual applicants should be regarded as working for Newco as of right with the same conditions of employment.

The Advocate General set out his interpretation of the Directive on the basis of the previous case law, which he said the Directive reflected. In order to see whether the Article 5 exception applied, the court had to look at both the *objective* of the insolvency procedure in question and the *form* of that procedure, whilst having regard to the purpose of the Directive, namely to protect employees' rights. On the basis of the previous case law, exclusion from protection by means of the exception in Article 5 "*…* is justified only if the aim of the procedure at issue, having regard to its objectives in its form, is the liquidation of the undertaking's assets. On the other hand, if, having regard to its objectives in its form, the aim of the procedure at issue is the continuation of the undertaking's business, its economic and social objective does not justify a situation where, in the event of the undertaking being transferred, its employees lose the rights which the Directive confers on them". (paragraph 53).

The Advocate General thus distinguishes between insolvency proceedings which are initiated to liquidate the transferor's assets and those which were not initiated to liquidate the transferor's assets but to ensure the continuation of the undertaking.

At paragraph 57, the Advocate General takes the view that "in general" a transfer is to be regarded as being part of a procedure, the aim of which is the continuation of the undertaking, where that procedure is designed or applied specifically in order to preserve the operational character of the undertaking or of its viable units, in such a way as to make it possible to retain the value which stems from the uninterrupted continuation of its operation.

By contrast, procedures for the liquidation of assets are not created specifically to pursue such a goal but are concerned solely with maximising the payment of the creditors' collective claims.

At paragraph 58, the Advocate General accepts that "there may be some overlap" between the objective of preserving the operational character of the assigned part of the undertaking and that of maximising the payment of the creditors' collective claims. He accepts that the value of an undertaking which is operating normally is, in general, much higher than the value of its assets taken separately or the value which that undertaking would have if its serious financial distress was publicised. He does, however, purport to distinguish the two types of situation as follows:-

"However, in procedures where the aim is the continuation of the undertaking, preserving that continuation is the central feature, the ultimate goal of the procedure itself, or the application of that procedure *in concreto*. On the other hand, in liquidation procedures, preservation is a purely functional aspect of the payment of the creditors' claim." (paragraph 58).

The Advocate General goes on to consider the operation of pre-packs as they have developed in practice in the Netherlands. The Advocate General describes two phases, being a preparatory phase, before the declaration of insolvency, and a phase simultaneous with or immediately following the declaration of insolvency. In the preparatory phase, which is always opened on the initiative of the debtor, it asks the court to appoint a prospective insolvency administrator and a prospective *juge-commissaire* (supervisory judge). The idea behind this advance appointment is to enable the prospective insolvency administrator to gain information about the undertaking and to examine its financial circumstances and the possible solutions envisaged, so that he is able to make a speedy request to the supervisory judge after the declaration of insolvency, in order to implement the pre-pack transfer: see paragraph 68. The prospective insolvency administrator contacts the undertaking, reviews its accounts and other relevant data and receives information on possible solutions. In this preparatory phase, the pre-pack is prepared down "to the last detail". Once the declaration of insolvency is made, the court appoints the prospective insolvency administrator as the actual insolvency administrator and the prospective supervisory judge becomes the actual supervisory judge. The insolvency administrator then asks for and receives authorisation from the supervisory judge for the pre-pack transfer.

The Advocate General points out that the aim of the structure of this procedure is to avoid the disruption that would result from a sudden cessation of the undertaking's activities at the point of declaration of insolvency, since that would lead to a significant loss of value of the undertaking or the viable parts being transferred: see paragraph 72. The Advocate General also points out that the preparatory phase "is not regulated by law" and formally speaking neither the insolvency practitioner nor the supervisory judge has any power at this preliminary stage: paragraph 73.

The Advocate General has no doubt that the objective of the Netherlands procedure, taken as a whole, "is aimed at transferring the undertaking (or its still viable units) in order to restart the business without any interruption, immediately after the declaration of insolvency". (paragraph 75).

At paragraph 76 of his opinion, the Advocate General considers that the Netherlands proceedings "*…* are not real insolvency proceedings *…*" but are rather "technical insolvency proceedings": paragraph 76.

The Advocate General further points out that the procedure is frequently used for the purposes of restructuring and is "not aimed at liquidating the undertaking": paragraph 77.

In the light of his analysis, the Advocate General concludes that in view of the objective of the Netherlands form of pre-pack proceeding, although it may in part be conducted as part of an insolvency procedure, the Netherlands pre-pack cannot be regarded as a bankruptcy procedure or any analogous insolvency proceedings instituted with a view to the liquidation of the assets, "for the purposes of Article 5(1) of Directive 2001/23". Accordingly the

Netherlands pre-pack procedure does not fall within the exception to employee protection set out in that Article.

### Comment

The question of whether the employee protections apply, and in particular whether contracts of employment are automatically transferred, may well be critical for the success of a pre-pack. The Advocate General's distinction between the main propose of a proceeding being to save the viable parts of the business on the one hand and liquidating the debtor's assets for the benefit of creditors on the other is a difficult one. In a normal pre-pack the aim is both to save the viable parts of the business and to liquidate the debtor's assets i.e. realise them for the best price reasonably available for the benefit of creditors. The Advocate General accepts that there can be an overlap between the two types of purpose, but cannot give a bright line distinction between them. It all depends on the type of proceeding, its purpose and how it works in practice. The Dutch pre-pack turns out fundamentally to be about saving the viable parts of the business and not liquidating the debtor's assets for the benefit of creditors, in the Advocate General's dichotomy. The same could be said of most pre-packs.

We will now have to see what the CJEU makes of all this: while they follow the Advocate General's view most of the time, there are a number of cases where they do not.

*I am grateful to Kon Asimacopoulos of Kirkland & Ellis International LLP for drawing this case to my attention.*

# COLLATERAL DAMAGED

**Private Equity Insurance Group SIA v Swedbank AS (Case C-156/15)**

This appears to be the first case involving the Financial Collateral Directive 2002/47 which has come before the Court of Justice of the European Union (CJEU).

The debtor's predecessor, a Latvian company, opened an ordinary current account with the defendant bank. The terms of opening contained a financial collateral clause under which all monies in the current account were to be held as security for all liabilities from the accountholder to the bank. After the commencement of insolvency proceedings, the bank debited a sum of money from the current account of the debtor as maintenance commission in respect of a period prior to the opening of the insolvency proceedings against the debtor client. The debtor brought a claim in Latvia for recovery of the amount on the basis of a requirement under Latvian law that all creditors should be treated equally in insolvency proceedings. The question of the validity of the financial collateral security in terms of the Directive was referred by the Latvian Supreme Court to the CJEU for a preliminary ruling.

The key question of whether the monies were subject to the "possession or control" of the security-taker had been dealt with by two cases in England: *Re F2G Realisations Limited, Gray v GTP Group Limited* [2011] 1 BCLC 313 (the *Gray* case) and in *Re Lehman Brothers International (Europe) (In Administration) (No. 5)* [2014] 2 BCLC 295 (the *Lehman Brothers* case). In the *Gray* case, it had been held that (i) "possession" had no sensible application to intangibles and (ii) there could be no control where, pending crystallisation of a floating charge, the collateral provider had the legal right to require the collateral-taker to deal with the deposited money at the collateral provider's direction.

Following widespread criticism, pointing out that this approach severely restricted the ability of a floating charge to amount to sufficient possession or control, even though floating charges were expressly mentioned in the Directive, an amendment was made to the implementation of the Directive in England as follows:-

"For the purposes of these Regulations "possession" of financial collateral in the form of cash or financial instruments includes the case where financial collateral has been credited to an account in the name of the collateral-taker or a person acting on his behalf (whether or not the collateral-taker, or person acting on his behalf, has credited the financial collateral to an account in the name of the collateral-provider on his or that person's books) provided that any rights the collateral-provider may have in relation to the financial collateral are limited to the right to substitute financial collateral of the same or greater value or to withdraw excess financial collateral."

This appears to give meaning to the notion of "possession" in relation to intangibles used as security but limits the scope of "possession" to a situation where the collateral-provider had very restricted rights in relation to the collateral. As Briggs J. put it in the *Lehman Brothers* case, the amendment limited the recognition of "possession" in relation to intangibles "...to the narrow circumstances in which full legal control in the collateral-taker was only subjected to rights of substitution and the withdrawal of excess collateral".

In the *Lehman Brothers* case, Briggs J. considered that even without the amendment it was wrong to limit "possession" so as to exclude any application to intangibles.

Otherwise, however, he agreed with the *Gray* case and held that "possession or control" "**...** requires something much more than mere holding by, or delivery or transfer to, the collateral-taker". He also agreed with *Gray* that the control had to be legal rather than merely administrative control. Such control or possession had to amount to a "dispossession" of the collateral-provider. He considered that even on this basis, some floating charge situations would qualify e.g. cases where there was a right of substitution.

The UK Government made submissions during the hearing before the CJEU. In the Advocate General's opinion, the *Gray* and *Lehman Brothers* cases are referred to with

apparent approval at paragraphs 45, 46, 48 and 49. In particular, the Advocate General appears to have accepted that "control" has to be legal and not merely administrative control. The requirement of possession or control "would become entirely ineffective if it were interpreted as covering a situation where the collateral-provider is able to continue to dispose of it freely". (At paragraph 49).

The CJEU was of the same view. With regard to the particular facts in that case, the Court stated at paragraph 44:-

"It follows that the taker of collateral in the form of moneys lodged in an ordinary bank account may be regarded as having acquired "possession or control" of the moneys only if the collateral-provider is prevented from disposing of them."

On the facts of that case, the bank had a further problem: the monies debited by the bank were deposited in the account only after the date on which the insolvency proceedings were commenced. The CJEU held at paragraph 45 that the Directive does not protect financial collateral if it was provided after the commencement of insolvency proceedings.

On the facts of that particular case, therefore, the answer was relatively straightforward: the Directive and its protections against insolvency law did not apply because (i) the terms of the collateral arrangement did not contain any clause preventing the collateral-provider from disposing of the monies deposited in the current account and (ii) the monies in question were deposited in the current account subject to financial collateral terms after the commencement of the insolvency proceedings. The judgment however also deals with one or two interesting arguments raised by the parties.

One argument was that the Directive was only intended to apply to monies deposited in accounts which were used in payment and security settlement systems. This was rejected by the Court as being too narrow, at paragraph 35.

Although the Court did not attempt any comprehensive definition or description of "possession" or "control" for the purposes of the Directive, it did state that the criterion must be given an autonomous and uniform


PRIVATE EQUITY INSURANCE V SWEDBANK THE FIRST CASE INVOLVING THE FINANCIAL COLLATERAL DIRECTIVE

interpretation throughout the Union, taking into account the wording, context and objective: see paragraph 39.

The Court also dealt with the concern of the Latvian courts to the effect that the enhanced protection given to takers of financial collateral by the Directive, breached the fundamental principle of equality of creditors.

The Court referred to the principle of equality of creditors as an example of the more general principle of equality before the law, now set out in Article 20 of the Charter of Fundamental Rights of the European Union: paragraph 49. This is described as:-

"...A general principle of EU law which requires that comparable situations should not be treated differently and that different situations should not be treated in the same way, unless such different treatment is objectively justified. A difference in treatment is justified if it is based on an objective and reasonable criterion, that is, if the difference relates to a legally permitted aim pursued by the legislation in question, and it is proportionate to the aim pursued by the treatment..." (Paragraph 49).

The Court goes on to hold that the financial collateral regime, whilst it confers an advantage on financial collateral by comparison with other types of security, such advantage is based on an objective criterion relating to the legitimate aim of the Directive, i.e. to improve the legal certainty and effectiveness of financial collateral in order to provide stability in the financial system. (See paragraphs 50 and 51). Such special treatment is not disproportionate to the aim being pursued: see paragraph 52. The Court ties in this point to the fact that the Directive is interpreted as only applying to collateral provided before the insolvency proceeding is commenced: see paragraph 52. In the same paragraph the Court also makes the link between the principle of proportionality and the requirement of "dispossession", which severely limits the scope of the special status of financial collateral.

To sum up, it seems that the approach taken in the *Lehman Brothers* case by Briggs J. (as he then was) has in effect been followed by the CJEU and, whilst the UK remains in the EU, is binding on all UK courts. For there to be either possession or control sufficient for the purposes of the Directive, there must be a "dispossession" of the collateral-provider. A security arrangement such as a typical floating charge situation, which allows the collateral-provider generally to withdraw monies or securities from the possession or control of the security-taker would not seem to create sufficient possession or control for the purposes of the Directive.

# Recast EU Insolvency Regulation: the key points

**David Allison QC** provides an overview of the key changes that will apply to insolvency proceedings opened after 26 June this year

## Introduction

The EU Insolvency Regulation (Regulation 1346/2000) ("Regulation") came into force in 2002. It introduced a uniform set of conflict of laws rules to determine insolvency jurisdiction as between Members States (Art 3) and the applicable law in relation to insolvency proceedings (main, territorial or secondary) according primarily to where they are opened (Art 4) subject to some important exceptions (Arts 5-15). It also made provision for the recognition of those insolvency proceedings in all other Member States (broadly Arts 16-26), as well as a framework for the co-ordination of parallel proceedings opened in relation to the same debtor in more than one Member State (Arts 27-38).

The Recast EU Insolvency Regulation (Regulation 2015/848) ("RR") will apply to insolvency proceedings opened after 26 June 2017. As with its predecessor, RR applies to all Member States with the exception of Denmark. While the RR is a good deal longer than its predecessor, it very largely adopts the same approach as the Regulation. The purpose of this article is to provide a high level overview of the key changes.

## Scope

The Regulation focuses only on insolvent debtors. The scope of RR covers insolvent debtors, but also extends to proceedings which promote the rescue of economically viable but distressed businesses and which give a second chance to entrepreneurs: see Recitals (10), (11) and (17) and Art 1(1). In this regard:

- Recital (10) provides that RR extends to proceedings which provide for the restructuring of a debtor at a stage where there is only a likelihood of insolvency, as well as to proceedings which leave a debtor fully or partially in control of its assets and affairs.
- Recital (11) provides that RR applies to procedures which grant a temporary stay on enforcement actions brought by individual creditors where such actions could adversely affect negotiations and hamper the prospects of a restructuring of the debtor's business.
- Recital (17) provides that RR extends to proceedings which are triggered by situations in which the debtor faces non-financial difficulties, provided they give rise to a real and serious threat to the debtor's actual or future ability to pay its debts as they fall due. The example given is a case where a debtor has lost a contract which is of key importance to it.

There are two points which are particularly noteworthy on the limitations of the scope of RR:

- First, the relevant insolvency proceedings which fall within RR are those exhaustively identified in Annex A. If they are not there, they are not covered by RR: see Art 1(1), Art 2(4) and Recital (9).
- Second, Annex A does not mention the English law scheme of arrangement. Although many in Europe wanted the English scheme to become subject to RR, this has been successfully resisted by the UK. While its absence from Annex A would be sufficient to exclude it from the scope of RR, Recital (16) further explains that although RR should apply to proceedings based on laws relating to insolvency, those based on general company law not designed exclusively for insolvency situations should not be considered to be based on laws relating to insolvency.

THE RECAST REGULATION CONTAINS A CODIFICATION OF THE METHOD OF DETERMINING COMI

It should also be noted that RR codifies existing principles derived from the authorities which confer jurisdiction on the courts of the Member State within the territory in which main insolvency proceedings have been opened for any action which derives directly from the insolvency proceedings and is closely linked with them, such as avoidance actions: see Art 6. Recital (35) serves to highlight the distinction between avoidance actions and actions concerning obligations which arise in the course of the insolvency proceedings (where jurisdiction is conferred on the courts of the Member State in the main insolvency proceedings) and actions for the performance of the obligations under a contract concluded by the debtor prior to the opening of insolvency proceedings (where matters are governed by the Recast Judgments Regulation).

## International Jurisdiction: COMI and forum-shopping

As noted above, a key purpose of the Regulation was the introduction of a uniform set of rules to determine insolvency jurisdiction as between Member States. This was achieved by the imposition of jurisdictional gateways as follows:

- COMI: the jurisdictional requirement to be satisfied if main proceedings are to be opened. For the courts of a Member State to open main proceedings, the debtor's COMI must be situated within the territory of that Member State.
- Establishment: the jurisdictional gateway to be satisfied if secondary (or territorial) proceedings are to be opened. For the courts of a Member State to open secondary (or territorial) proceedings, the debtor must have an establishment in that Member State and its COMI in another Member State.

The Regulation provides no guidance on the question of COMI, save that Recital (13) said that COMI should correspond to the place where the debtor conducts the administration of its interests on a regular basis, in a manner ascertainable by third parties. In the case of companies or other legal persons, there is currently a rebuttable presumption that it is the place of its registered office. In the case of individuals, there is currently no presumption at all

While RR does not change the jurisdictional gateways for the opening of insolvency proceedings, it provides significantly more guidance


DAVID ALLISON QC

on the question of COMI. For example, what was in Recital (13) is now to be found in Art 3(1), and Recitals (28), (30) and (32) summarise the guidance on the question of COMI given by the CJEU in cases such as *Eurofood IFSC Ltd (Case C-341/04)* [2006] Ch 508 and *Interedil Srl v Fallimento Interedil Srl (Case C-396/09)* [2012] Bus LR 1582 (e.g. each debtor needs to be considered separately; all relevant factors must be reviewed comprehensively; special weight is to be attached to creditors' perceptions etc).

Art 3(1) RR also makes significant changes to the operation of the presumption in relation to COMI:

- The COMI presumption only applies to companies if the registered office has not moved to another Member State within three months prior to the request to open insolvency proceedings.
- The COMI presumption is extended to individuals carrying on independent business or professional activity, in which case there is a rebuttable presumption that it is that individual's principal place of business, unless it has moved within three months prior to the request to open insolvency proceedings.
- The COMI presumption is extended to ordinary individuals, in respect of whom there will be a rebuttable presumption that their COMI is their habitual residence, unless it has moved within six months prior to the request to open insolvency proceedings.

It is apparent from the Recitals that the principal reason for the new time limits is to reduce the scope for abusive forum-shopping. To be clear, that is forum-shopping "*to the detriment of the general body of creditors*" (now clarified by Recital (5), which adds these important words to what was Recital (4) of the Regulation).

Indeed, it is expressly stated in Recital (29) that RR should contain a number of safeguards aimed at preventing fraudulent or abusive forum-shopping. These include the time limitations placed on the COMI presumptions identified above; the guidance given as to when the COMI presumptions may be rebutted: see Recitals (30) and (31); a requirement for creditors to be informed of the new location from which the debtor is carrying on activities or making it public by other means (Recital (28)); and, in cases of doubt, requiring the debtor to submit additional evidence and/or permitting creditors the opportunity to present their own views on the question of jurisdiction (Recital (32)). In addition, Recital (33) records that unless the court is satisfied COMI is established in its Member State, it cannot open main proceedings; Art 4 emphasises that the court asked to open insolvency proceedings must examine whether it has jurisdiction of its own motion, and must specify the grounds on which it is based; and Art 5 expressly states that the debtor or any creditor may challenge the decision opening main proceedings on grounds of international jurisdiction (see also Recital (34)).

## Applicable law

The provisions which address the applicable law (Arts 7-18, which replace Arts 4-15) are very largely the same as before. As regards the applicable law, the general rule is that it is the law of the Member State where the insolvency proceedings are opened. That is so whether the proceedings are main, territorial or secondary (Arts 7 and 35).

There are specific exceptions to this rule contained in Arts 8-18, but they are the same as before. The changes to be noted are as follows:

- Art 11(2) clarifies that in relation to contracts relating to immoveable property, the court which opened main insolvency proceedings shall have jurisdiction to approve the termination or modification of such contracts where (i) the law of the Member State applicable to those contracts requires that such a contract may only be terminated or modified with the approval of the court opening insolvency proceedings; and (ii) no insolvency proceedings have been opened in that Member State.
- Art 13 clarifies that the courts of the Member State in which secondary proceedings may be opened retains jurisdiction to approve the termination or modification of employment contracts even if no insolvency proceedings have been opened in that Member State. This feeds into other changes made in respect of secondary proceedings, largely with a view to avoiding them, which are addressed below.
- Art 18 clarifies that the law which governs the effect of insolvency proceedings on pending lawsuits or arbitral proceedings, which concern an asset or a right of which the debtor has been divested, is that of the Member State in which the lawsuit is pending or in which the arbitral tribunal has its seat.

## Secondary proceedings

The proliferation of insolvency proceedings can lead to practical difficulties. Experience over the past few years shows that secondary proceedings may, in practice, hamper the efficient administration of the insolvency estate, even more so if (as is currently the case) secondary proceedings must be winding-up proceedings regardless of the nature of the main proceedings. RR expressly recognises the scope for such conflict and seeks to address this (Recital (41)).

First, secondary proceedings are no longer confined to liquidation proceedings, but can be any of those mentioned in Annex A. This change has been effected simply by the deletion of the offending sentence in Art 34 (previously Art 27).

Secondly, RR emphasises the need for co-ordination of insolvency proceedings. The Regulation currently contains provisions which require officeholders in the respective proceedings to co-operate and communicate with each other: see Art 41. In addition, the English courts have recognised in recent years duties on the courts themselves to communicate and co-operate with each other, and other similar duties as between officeholders and the courts.

RR introduces detailed provisions requiring communication and co-operation all-round: see Arts 41-44 and Recitals (48)-(50). These bear some similarity to the co-operation provisions of Cross Border Insolvency Regulations 2006, Arts 25-27. Indeed, Recital (48) specifically states that insolvency practitioners and courts should have regard to best practices for cooperation, including in particular the UNCITRAL guidelines.

Thirdly, RR emphasises the need for the avoidance of secondary proceedings, save where necessary. In England, the court has already adopted the stance that secondary proceedings should be opened only when it is demonstrated (by the applicant) that they will serve a useful purpose: see e.g. *Re Nortel Networks SA* [2009] BCC 343. This is the approach favoured by RR as highlighted by the wording "*may open*" in Art 34 rather than "*shall permit*" currently to be found in Art 27 of the Regulation.

Fourthly, RR makes use of another means of avoiding secondary proceedings adopted in England whereby an officeholder has been permitted to undertake that the rights of local creditors will be recognised and protected as if secondary proceedings had been opened elsewhere, although not opened in fact: see, for example, *Re Collins & Aikman* [2007] 1 BCLC 182 and *Re Nortel Networks SA* [2009] BCC 343. The undertaking method of avoiding secondary proceedings is introduced into RR by Recitals (42)-(44) and Arts 36 and 38. In summary, it will enable secondary proceedings to be avoided where the undertaking is approved by a qualified majority of local creditors (Art 36(5)) and the local court is satisfied that it adequately protects the interests of local creditors (Art 38(2)).

Fifthly, certain Articles make provision for the stay of the opening of secondary proceedings in appropriate cases: see Art 38(3) and

**The Recast Regulation provides for increased co-operation and communication all round**

## The Recast Regulation introduces a framework for group insolvency proceedings, something which was notably absent in the original Regulation

Recital (45) which permit a three month stay where there are negotiations between the debtor and its creditors, provided creditors' interests are protected in the meantime. The stay may be lifted by the court of its own motion if satisfied its continuation would be detrimental to the interests of creditors: see Art 38(3).

Finally, even once secondary proceedings have been opened, as before the process of liquidation or the realisation of assets may be stayed for up to 3 months (which may be extended), on the application of the officeholder in the main proceedings, provided that the interests of local creditors are adequately protected: see Art 46 (previously Art 33).

### Groups of Companies

A notable absence from the Regulation is any provision concerned with insolvency proceedings relating to more than one company in the same corporate group. RR makes two key changes.

- First, it contains detailed provisions for co-operation and communication between officeholders, between courts, and between officeholders and courts, with a view to facilitating the effective administration of the proceedings: see Arts 56-60.
- Second, it introduces of a new regime of group coordination proceedings (Arts 61-77). These provisions are considered below.

It should be noted that the provisions relating to groups are not intended to limit the ability of one court to open separate insolvency proceedings for several companies in a single jurisdiction, appointing the same officeholders, if satisfied that their COMI is located in that member state: see Recital (53). That means that current restructuring practice of migrating COMI to one Member State in appropriate cases, with a view to opening coordinated insolvency proceedings in respect of all group companies in that Member State, can continue.

### Group coordination proceedings

Group coordination proceedings are proceedings opened by the court of a Member State having jurisdiction over insolvency proceedings relating to any member of the group: see Art 61. They involve the appointment of a group coordinator, who must outline recommendations for the coordinated conduct of the insolvency proceedings affecting the members of the group; and propose a group coordination plan, recommending a comprehensive set of measures aimed at the resolution of the group members' insolvencies: see Art 72(1). The plan may contain proposals for measures to re-establish the economic viability of the group (or any part of it); settlement of intra-group disputes; and agreements between the officeholders of the group members: see Art 72(1)(b). The group coordination plan must not, however, include recommendations as to the consolidation of proceedings or insolvency estates: see Art 72(3).

The group coordinator may not only participate in the insolvency proceedings relating to any individual member of the group, but can also request a stay of up to six months of the proceedings opened in respect of any member, provided that this is necessary for the proper implementation of the plan and would be to the benefit of the creditors in the proceedings for which the stay is requested: see Art 72(2)(e).

The application to open group coordination proceedings may be made by an officeholder in insolvency proceedings opened in relation to any member of the group: see Art 61(1). It seems the officeholder may apply to any court having jurisdiction over the insolvency proceedings; but in practice, it seems likely that the application would be made to the relevant court in their own Member State. Where a number of such applications are made, the court first seised wins and the others must decline jurisdiction: see Art 62. That said, where at least 2/3 of all officeholders appointed in insolvency proceedings of the members of the group agree that a court of another Member State having jurisdiction is the most appropriate court for the opening of group proceedings, then that court will have exclusive jurisdiction: see Art 66(1).

Art 63(1) provides that the relevant court must be satisfied in respect of the following matters before giving notice of the request to open group coordination proceedings:

- group coordination proceedings are appropriate to facilitate the effective administration of the insolvency proceedings relating to the different group members: see Art 63(1)(a);
- no creditor of any group member anticipated to take part is likely to be financially worse off by inclusion of that member: see Art 63(1)(b); and
- the proposed group coordinator is (i) a person eligible to act as an insolvency practitioner under the law of a Member State but (ii) is not one of

the officeholders appointed in respect of any of the group companies and (iii) has no conflict of interest: see Art 63(1)(c) and 71.

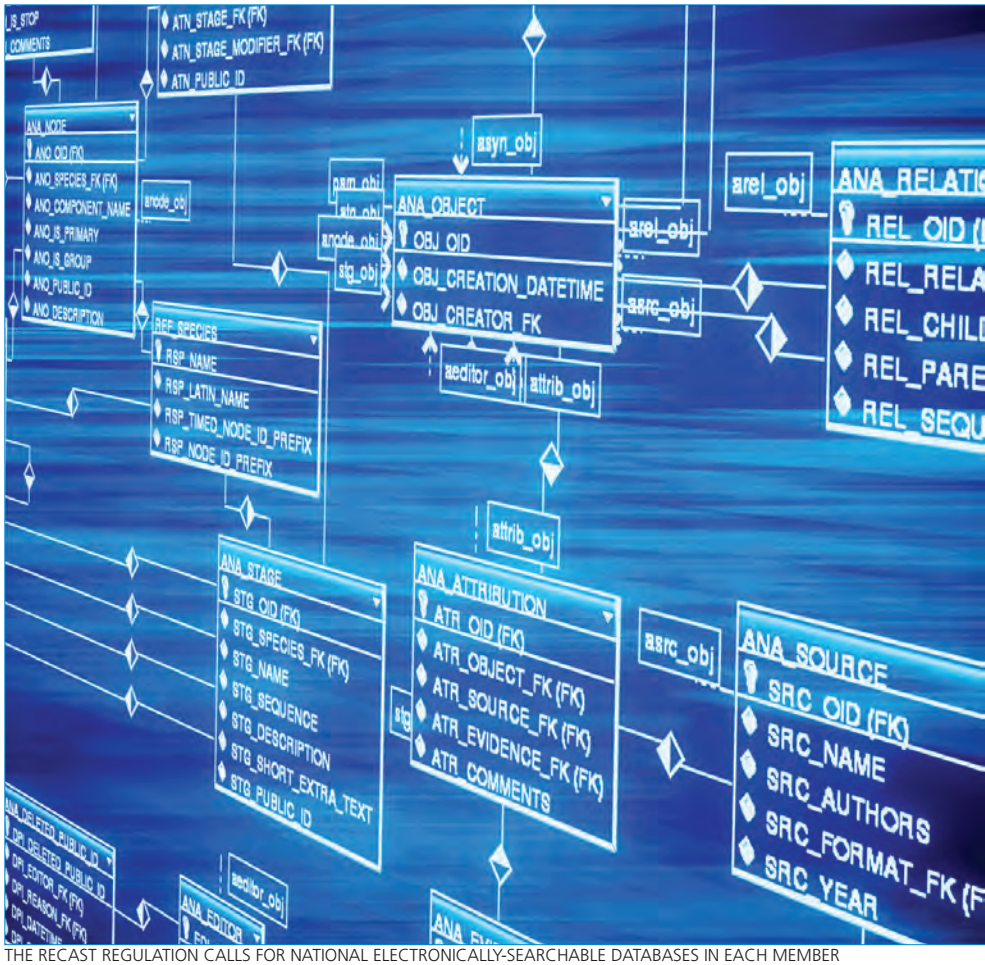
When satisfied in relation to the above matters, the court gives notice of the request to open proceedings to the officeholders appointed in relation to the members of the group: see Art 63(1). The officeholder of any member of the group is then given the opportunity to object within 30 days of receiving the notice, either to (i) inclusion of their company in the group coordination proceeding; or (ii) to the person proposed as coordinator: see Art 64.

If the objection is made to participation, the company concerned will not be included in the group coordination proceedings: see Art 65(1). If the objection is made to the proposed coordinator, the court may decline to appoint that person, and invite alternative nominations: see Art 67.

Otherwise, after the 30 days have elapsed, the court may open group coordination proceedings, and shall appoint a coordinator, decide on the outline of the coordination and decide on the estimated costs and how they are to be shared by members of the group: see Art 68(1).

The participation in group coordination proceedings is a voluntary act at the option of the officeholder of the relevant member of the group. In circumstances where (i) the officeholder has initially objected and then changes their mind and wants to join the proceeding; or (ii) new insolvency proceedings are opened with respect to a member of the group after the opening of the group coordination proceedings and the officeholder wishes to join the proceedings, then the group coordinator may accede to the request where (Art 69(2)):

- the group coordinator is satisfied that inclusion would be appropriate to the achievement of the purpose of the proceedings, and no creditor of any participating group member would be financially worse off as a result of the inclusion of that member; or
- all the officeholders of the other participating group members agree, subject to the conditions in their national law.



THE RECAST REGULATION CALLS FOR NATIONAL ELECTRONICALLY-SEARCHABLE DATABASES IN EACH MEMBER STATE, LINKED VIA A CENTRAL E-JUSTICE PORTAL

It should be noted that participation in the group coordinated proceedings does not mean that participation in the plan is compulsory. While the officeholders of individual participating group members are obliged to consider the group coordinator's recommendations and the group coordination plan itself, they are not obliged to follow either the recommendations or the plan, in whole or in part; although they must give their reasons for not doing so: see Art 70.

## Information for creditors

RR makes provision for the establishment of insolvency registers in Member States, in which information relation to insolvency proceedings is to be published for the general benefit of creditors; and the Commission is to establish by 26 June 2019 a decentralised system for the interconnection of insolvency registers, composed of the insolvency registers themselves and the European e-Justice Portal: see Arts 24-27.

In addition, more detailed provision is made for the communication of information to creditors and for the procedure for lodging claims: see Arts 54-55.

# 'Embracing change' down under

**Edoardo Lupi** reports from INSOL International's 10th World Congress in Sydney, Australia.

INSOL International's 10th Quadrennial Congress in March was once again well attended by members of South Square. Among the 1000 delegates converging on the International Convention Centre in Sydney's picturesque Darling Harbour were Gabriel Moss QC (one of a panel of experts covering 'hot and heating' topics), William Trower QC, Fidelis Oditah QC (who spoke on a panel addressing the issue of rescue capital for companies in distressed situations), David Alexander QC, Tom Smith QC and Edoardo Lupi.

GABRIEL MOSS QC

Despite the insolvency gods decreeing record-breaking rainfall for the month of March in Sydney, the congress was a great success, combining excellent technical content with seamless organisation, and providing a relaxed setting for delegates to meet old friends and make new acquaintances.

### Offshore Ancillary Meeting

The third offshore ancillary meeting took place one day before the start of the main congress. Chaired by Hugh Dickson of Grant Thornton, the programme for the offshore meeting consisted of sessions with a distinctly cross-border flavour, including '*East meets West – Restructuring offshore entities with onshore Asian Operations: practical considerations*', but also saw discussions on more industry specific issues, such as '*Restructuring and insolvency of extractive industries*'.

Perhaps the standout session of the day was a lively debate on the motion '*Universalism is Dead*'. Notwithstanding developments following the *Cambridge Gas* case, not least the Privy Council's latest contribution in this area in *Singularis v PwC*, and the numerous limitations set out in that case by the majority

INSOL'S 10TH CONGRESS WAS HELD AT SYDNEY'S RECENTLY-OPENED INTERNATIONAL CONVENTION CENTRE

of the Board on the court's powers of assistance at common law, delegates voted overwhelmingly against the motion, despite the valiant efforts of the motion's proponents Arabella di Iorio (Maples) and Rebecca Hume (Kobre & Kim).

## The Congress

Following a welcome reception generously sponsored by BDO LLP the previous evening, the congress itself kicked off with a much needed continental breakfast sponsored by South Square. In addition to pastries and coffees, delegates were treated to hard copies of last quarter's edition of the South Square Digest – an invaluable companion for a hangover and the rest of the conference.

## Keynote Speakers

The keynote address on the first day was given by David Gronski, an eminent figure in the Australian business world. Chairman of both the ANZ Banking Group Ltd and Coca-Cola Amatil Limited, Mr Gronski provided practitioners with his perspective on the shifting challenges he has faced as a company director over the decades. Mr Gronski's address tackled issues ranging from the pitfalls of social media in the modern age to the under-representation of women on company boards across the world.

A subsequent keynote speaker was Kevyn Orr (Jones Day), who was interviewed by

SOUTH SQUARE SPEAKERS INCLUDED FIDELIS ODITAH QC (LEFT) AND GABRIEL MOSS QC (FAR LEFT)

EDOARDO LUPI

Robert Hertzberg, a past president of INSOL International. Mr Orr acted as the Emergency Manager for the city of Detroit between March 2013 and December 2014, before being appointed Special Counsel for the Emergency Manager for Atlantic City. Under Mr Orr's supervision, the city of Detroit filed for bankruptcy under Chapter 9 of the US Bankruptcy Code, thus becoming the largest municipality to enter such proceedings in US history. Mr Orr spoke candidly about the magnitude of the challenges he faced in restructuring the city's $18 billion debt, whilst at the same time seeking to deliver improved public services and maintain public order.

## Case Study

A case study entitled '*Oil on Troubled Waters*' provided an overarching problem for delegates to get their teeth stuck into on the first day of the congress.

The study was introduced by an excellent film (complete with cameos from INSOL Fellows) which depicted a fictional oil company coming to grips with a Deepwater Horizon-style failure of one of its rigs. The film follows the machinations of the company's board members, who are eventually forced to confront the reality that the company's debt obligations need to be restructured, in circumstances where each debt is governed by the law of a different jurisdiction.

Various breakout sessions then dealt with the different issues raised by the scenario. The issues ranged from the board's duties in such situations to the restructuring options available to the company in England, the US and Canada. At a concluding plenary session delegates armed with clickers were torn between voting for a US Chapter 11 and an English scheme of arrangement as the most suitable restructuring tool for the oil company.

During the remainder of the congress, a number of recurring themes emerged as being of particular interest to speakers and delegates alike. Two of those themes are picked up on below.

## Brexit

Inevitably, Brexit was a topic raised frequently with the UK delegates at the congress. The impact of Brexit was addressed in a panel session entitled '*The Good, the Bad and the Ugly: National and Regional Insolvency Law Reforms*'. Alongside panellists considering developments in the US, the EU and Singapore, Mark Craggs (Norton Rose Fulbright) discussed UK developments, noting that the Insolvency Service's 2016 consultation, 'A Review of the Corporate Insolvency Framework' had rather taken a back seat following the outcome of the Brexit referendum.

In discussion after the panel had concluded their contributions, certain delegates considered that there were pressing questions concerning the post-

Brexit status of the EU Insolvency Regulation, and issues involving the future prospects of European officeholders receiving assistance from the English courts. Delegates were generally sanguine, however, with some noting that at the very least foreign officeholders would still be able to rely on the UNCITRAL Model Law as incorporated by the CBIR 2006 and (in some cases) s. 426 of the Insolvency Act 1986, whatever the outcome of the Brexit process.

## Singapore

Another prominent theme at the congress was new legislation coming out of Singapore (addressed in last quarter's edition by Smitha Menon and Stephanie Yeo (WongPartnership) with Mark Arnold QC and Matthew Abraham). Just before the congress, the Singaporean Parliament passed the Companies (Amendment) Bill 2017, to which the President gave his assent following the INSOL congress. Many of the legislation's key elements are not yet in force.

The new legislation was a major talking point at a number of sessions, including one entitled '*A Hitchhiker's Guide to Forum Shopping*' chaired by the Hon. Judge Jim Peck (retired) with contributions from Patrick Ang (Rajah & Tann), who summarized the significant elements of the Singaporean legislation, and later in *The Good, the Bad, and the Ugly* session, where Sushil Nair (Drew & Napier, and a member of the 'Committee to strengthen Singapore as an international debt restructuring centre') tackled the background to the committee's recommendations.

In addition to incorporating the UNCITRAL Model Law, the new legislation takes elements from the debtor-friendly US Chapter 11 regime and the more creditor-friendly English scheme jurisdiction. Key questions raised by the delegates related to how the extraterritorial stay under the new legislation in aid of schemes of arrangement would operate in practice, as well as issues concerning the recognition of Singaporean schemes where the debt being adjusted is governed by a foreign law. How these questions will be addressed both by the Singaporean courts and foreign courts confronted by Singaporean schemes of arrangement remains to be seen.

NEW LEGISLATION COMING OUT OF SINGAPORE WAS A MAJOR TALKING POINT

## Future Events

Before the gala dinner wrapping up proceedings, the final panel saw a discussion by an eminent selection of judges from Australia, Hong Kong, the US and the UK, with the latter being represented by Mr Justice Norris. The panel addressed topical issues like forum shopping, COMI shifts and cross-border assistance.

The congress was greatly enjoyable and well worth the round-the-world-trip. I am sure many of us are already pencilling 2021 into our diaries for the next world congress in San Diego, California.

# Insolvency Lawyers Association Annual Conference

April 2017 brought with it the Insolvency Lawyers Association Conference, this year sponsored by GLAS at the Royal College of Physicians in London, the theme "All Change? The future of English restructuring and insolvency law". **Jeremy Goldring QC** reviews the technical programme.

A large group, including many from South Square, gathered for an excellent Saturday, admiring views of Nash's timeless Regency architecture, talking with old friends and listening to the latest news and debate from the world of restructuring and insolvency.

As so often, Brexit was to the fore, but not, thankfully, the exclusive focus. For this, much was down to Leon Zwier, as Conference Chair, who provided a welcome Australian perspective as an antidote to parochialism. Other welcome non-English perspectives (some measured, some less so) came from Hon James M. Peck, former US Bankruptcy Judge for the Southern District of New York and Alexandra Bigot of the Paris Bar, who (with Chris Howard) participated in a debate, chaired by Tony Bugg called "*Clashing patriotic viewpoints: Why my system is best*". As can be imagined, all was sweetness, light and compromise, all participants gracefully acknowledging the strength of other systems and the weaknesses (if any) of their own.

JEREMY GOLDRING QC

Another welcome feature of the day was a series of presentations about current trends in economic performance. Trevor Williams, former Chief Economist at Lloyds' Bank Corporate Markets, talked entertainingly about the UK macro-economic outlook, focusing on various challenges including the impact of Donald Trump, Brexit, Russian adventurism and the slowdown in China. John Disson (of Standard Bank), Will Wright (of KPMG) and Mike Jervis (of PwC) dealt with business sectors, viz. oil & gas, retail and healthcare.

THE ROYAL COLLEGE OF PHYSICIANS - VENUE FOR THE INSOLVENCY LAWYERS ASSOCIATION CONFERENCE

None was entirely optimistic, but the position in elderly care services was particularly gloomy, with estimates of a funding gap of more than £2.6 billion; some explanation for the political debate about the so-called 'dementia tax' ongoing as I write.

As always at the ILA conference, the broad themes were accompanied by a series of technical legal sessions.

Linton Bloomberg reflected on the impact of the pre-pack reforms, and Patrick Corr on whether directors' duties are ripe for reform. Chambers' David Allison QC and Adam Al Attar provided an update on schemes of arrangement, giving attention to the impact of the Recast Judgments Regulation on the English Court's jurisdiction to sanction a scheme and vote splitting at scheme meetings. After lunch, Ken Baird chaired a panel on cross-border recognition of insolvency proceedings post-Brexit. Kay Norley helpfully explained the EU's proposals on harmonizing insolvency laws, including its new so-called Chapter 15. Our own Barry Isaacs QC considered whether the EU regulation would continue to have any application post-Brexit and, if not, whether any EU member states would recognize English insolvency proceedings or vice versa. James Douglas, having extolled the virtues of the New Zealand restructuring process, provided an upbeat assessment of the continuing relevance of English schemes in the international market for restructuring. Louise Hutton had the unenviable, but important, task of explaining the new Insolvency Rules, which she did admirably, reading them all so (I hope) we do not need to.

All-in-all a stimulating way to spend a Saturday, and many thanks must go to the ILA Committee for organizing it. And who knows what will have happened by the time the ILA Conference comes around in April 2018. Jeremy Corbyn as Prime Minister? Mike Pence as US President? At least we can be fairly sure that Nash's terraces around Regent's Park will still be there.

# ILA Academic Forum

reviewed by John Briggs

This proved a most interesting and entertaining day. The event was chaired by Prof Andrew Keay and the five talks were each led by an Academic and accompanied by a Practitioner as "Commentator". Since law is a practical subject this approach proved a novel (at least for me) and very successful formula. In my view, this stimulated interest, generating lively debate from the floor. Again, a mix of delegate academics and practitioners and well-attended.

Some of the Academics presented uncompleted research projects or the genesis of draft articles, so testing their ideas and perceptions with the audience. For instance, Dr Richard Williams on "Directors' Liabilities" and Dr John Wood "Painting over the cracks" a study on the regulatory framework for deterring opportunistic behaviour.

Closer to home for me was the bare bones of a research project on Debt Relief Orders (DROs") by Prof Iain Ramsay of Kent University and whether DROs achieve their object of rehabilitation of consumers with persistent debt problems and no assets and very little surplus income. I was invited to commentate on this topic and after a brief reminder of how English bankruptcy law has developed over recent centuries into a compassionate regime, I contrasted DROs and their operation with IVAs and bankruptcy.

From the floor, on this topic there was a general cynical feeling promoted by Chris Garwood, a fellow Deputy Bankruptcy Registrar of mine, that what was dressed up by the Insolvency Service as addressing the real needs of consumer debtors was, in reality, a cost-cutting measure introduced by the Government to avoid the expense of unnecessary work by the Insolvency Service. Indeed, Prof Ramsay told us that the statistics showed that the Insolvency Service was actually making a profit from this administrative procedure!

The final two sessions turned to a presentation on cross-border insolvency by Prof Irit Mevorach and then, finally, a panel discussion on Brexit led by Prof Horst Eidenmuller. The latter very much a hot topic.

Prof Mevorach's presentation was ably commented upon by David Chivers QC, whose all-round contribution to the day's discussions was impressive. What I got out of this cross-border session was the overriding "localism" of European jurisdictions outside

JOHN BRIGGS

the ambit of the European Insolvency Regulation and their reluctance to engage in co-operation even if reciprocity is offered. No instinct for modified universalism there, unless treaty driven.

This does not augur well for Brexit and the panel discussion on Brexit case studies with various scenarios and alternatives of using the Hague Convention or the continuing possibility of using the Rome Convention fed more pessimism. I got the impression that some of the Continental jurisdictions may welcome seeing the back of UK competition for European insolvency work and English Schemes operating across European borders. The Germans may welcome us out, no doubt seeing an opportunity to dominate the European insolvency law sector.

The venue for the conference was at the Royal College of Physicians on the edge of Regent's Park. It was in all respects a great venue, and with good food and refreshments which is disappointingly not always the case with these large conferences. Smoothies included on the breakfast bar and a fantastic range of desserts and cheeses to finish off lunch.

The weather helped and we were all outside on the terrace for drinks at the end of the afternoon. A pleasure in these events is the opportunity to meet new people and old friends and contacts. In my case, my then very young company law tutor at KCL, Prof Harry Rajak, now at Sussex University. Not only is he a great guy and we enjoyed discussing college days, other tutors and student contemporaries but he also complimented me on being one of his brightest students and said my year group was his brightest ever. Welcome praise indeed!

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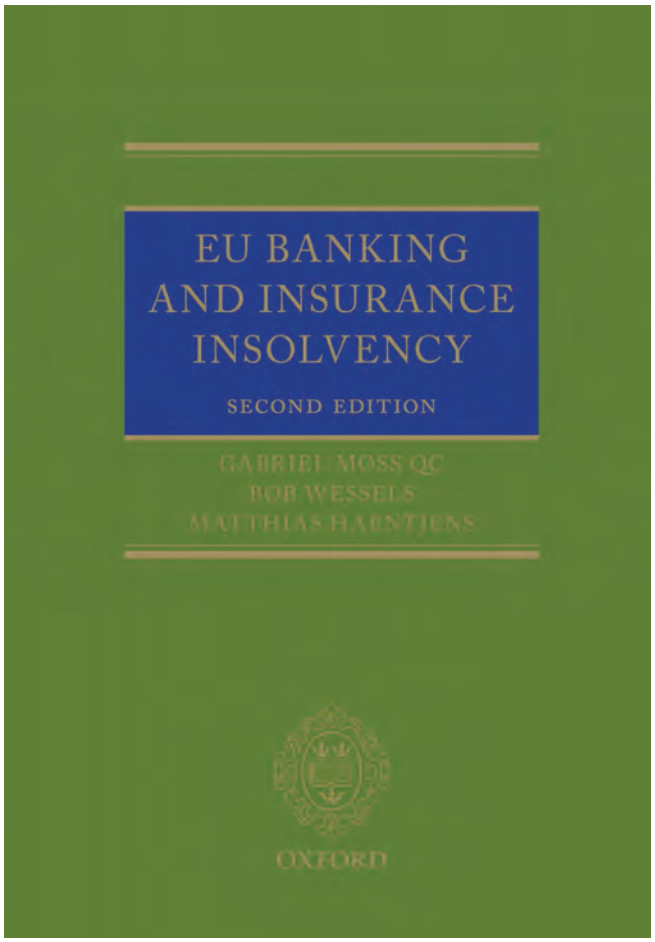


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# South Square at Spencer House

The South Square Spring reception was held in glorious weather on Thursday 25 May. Members and staff were once again delighted to welcome Chambers' clients and friends to Spencer House, one of London's finest surviving eighteenth-century town houses, overlooking Green Park.

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# NEWS in brief

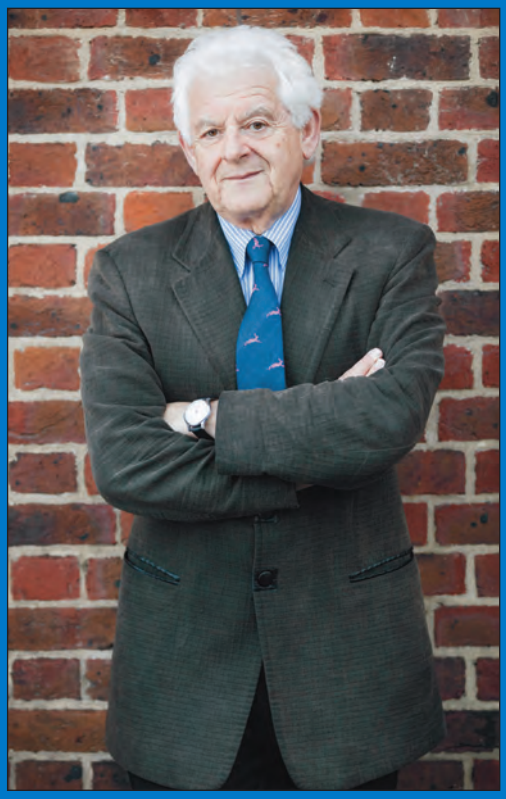
## Michael Crystal QC to receive the III 2017 Outstanding Contributions Award

**We are delighted that Michael Crystal is to be honoured with the International Insolvency Institute's 2017 Outstanding Contributions Award at the III Annual Conference to be held in London later this month. This award honours a person who reflects prominent, distinguished and exceptional service to the field of insolvency and to the insolvency community, and Michael is only the second English lawyer to receive the award in its 14-year history.**

**Michael has been at the forefront of insolvency law for over 40 years. Mark Phillips QC, who is co-chair of the London conference, remarks that "Michael's energy and vision are extraordinary, if not tiring to keep up with! Through many of the world's leading cases in which he appeared, he created solutions to pressing problems that became standard practice both in England and across the world. Not only is he a Master of the Bench, he is the Master of the English Insolvency Bar".**

Past III Outstanding Contributions Honorees include:

***2016 - Hon. Allan Gropper, U.S. Bankruptcy Court (Ret.), New York. 2015 - President Luciano Panzani, Court of Appeals, Rome. 2014 - Prof. Jay L. Westbrook, University of Texas, Austin. 2013 - Richard Gitlin, Gitlin & Company, LLC, Delray Beach. 2012 - John Barrett, Norton Rose Fulbright, Houston. 2011 - Hon. Burton R. Lifland, U.S. Bankruptcy Court, New York. 2010 - Lucio Ghia, Studio Legale Ghia, Rome. 2009 - Lord Leonard Hoffman, House of Lords, London. 2008 - Dr. Manfred Balz, Lazard, Frankfurt. 2007 - Hon. James M. Farley, Ontario Superior Court of Justice (Retired), Toronto. 2006 - Dr. Gerold Herrmann, Past Secretary, UNCITRAL, Vienna. 2005 - Dr. Shinjiro Takagi, Past Chair, Industrial Revitalization Corporation of Japan, Tokyo. 2004 - Prof. Geoffrey Hazard, Immediate Past Executive Director, The American Law Institute, San Francisco.***



MICHAEL CRYSTAL QC

## 80,000 businesses at risk from interest rate rises new R3 research reveals

One in 25 UK businesses, nearly 80,000 enterprises, would struggle to handle an increase in interest rates of as little as a quarter of a percentage point, according to research by the Association of Business Recovery Professionals, R3.

The figure is four times as many as in R3's previous survey and is the clearest sign yet of the fragile state of corporate balance sheets.

It is thought that some 79,000 businesses would be unable to repay their debts if rates were to rise.

The research, part of a long-running survey of business distress by R3 and BDRC Continental, also found that 96,000 firms (five per cent) were only paying interest on their debts.

Andrew Tate, spokesperson for R3, says: "This is the first increase in the number of businesses worried they would be unable to cope with an interest rate rise since 2014, and it coincides with a period of slower than expected growth and a small rise in corporate insolvency numbers.

"UK firms have faced a challenging 2016 and early 2017: the sharp fall in the pound has made things difficult for importers, while a rising National Living Wage and the roll-out of pensions auto-enrolment have added to businesses' running costs."

# New Deputy High Court Judges appointed

**South Square is delighted that Professor Sarah Worthington QC, FBA, has been appointed as a section 9(4) Deputy High Court Judge.**

**Sarah is an academic member of South Square, the Downing Professor of the Laws of England and Director of the Cambridge Private Law Centre.**

**Sarah's appointment was announced, along with 20 others, on 23 May 2017 by the Lord Chief Justice of England and Wales, the Right Honourable The Lord Thomas of Cwmgiedd, and she will serve for a single, fixed four-year term.**

**The appointment under section 9(4) of the Senior Courts Act 1981 is aimed at putting lawyers and legal academics with no previous judicial experience directly on to the High Court's benches, thus broadening the pool of talent from which the judiciary is drawn. Announcing the initiative in 2015 Lady Justice Hallett said "We fear we may be missing out on a pool of talent for whom the traditional route is not an option – top-flight solicitors and barristers, general counsel, academics and many more."**

**All solicitors and barristers with at least seven years' post-qualification experience are eligible to apply if, during that time, they have been engaged in law related activities, as defined under section 52 of the Tribunals, Courts and Enforcement Act 2007.**

# Bar placement week

We are pleased to be taking part once again in the Bar Council's Bar Placement Week, which is open to academically gifted Sixth Form students from non-traditional backgrounds (such as those who will be the first in their family to attend university) who have an interest in law and, particularly, a career at the Bar. The week in July forms part of the Bar Council's ongoing commitment to improving social mobility within the profession and will see more than 60 students from across the capital participate in this year's event.

During the week the students are introduced to the variety of careers available in the profession, see what becoming a barrister entails by shadowing a Member of Chambers for work experience, learn the various pathways they could take to the profession and attend a day of advocacy training including a mock trial.

The Bar Council organises a series of Bar Placement Weeks each year in London, Birmingham, Leeds, and Manchester, with London being the largest and most established.

# London Legal Walk

Members, pupils and staff were proud to take part in the London Legal Walk in support of the London Legal Support Trust, on Monday 22 May 2017. This is an annual event where thousands of judges, barristers, solicitors, staff and legal students cover a 10km route around London, raising much-needed funds through sponsorship to support free legal advice centres. The money raised enables the centres to offer help to the homeless, housebound elderly, victims of domestic violence and people trafficking and many more. This year's event was the largest yet with over 12,000 walkers. Donations can still be made through the following website: http://www.londonlegalsupporttrust.org.uk

## Online Courts Hackathon

**A 24-hour hackathon is being held to help to design online courts. The event is being organised by Legal Geek in association with Professor Richard Susskind, OBE, the President of the Society for Computers and Law.**

**Professor Susskind says, "Online courts are likely to be the most significant development in our court system since the nineteenth century, enabling far greater and affordable access to justice. This is a great opportunity to contribute to the design of online courts".**

**Interested individuals or teams are invited to join the event, to be held at a secret London location over July 1 and 2. Fuelled by pizzas and prizes it is hoped they will produce designs, solutions and systems for the online courts service.**

## US Westinghouse files Chapter 11

**Westinghouse, Toshiba's US nuclear unit, has filed for US bankruptcy protection.**

**The US firm has struggled with hefty losses that have thrown its Japanese parent into a crisis, putting the conglomerate's future at risk.**

**Westinghouse has suffered huge cost overruns at two US projects in Georgia and South Carolina.**

**Toshiba said the bankruptcy would not affect Westinghouse's UK operation, which employs more than 1,000 workers.**

**However, the firm warned that the writedown of its US nuclear business could see Toshiba's total losses last year exceed 1 trillion yen ($9.1bn; £7.3bn), almost triple its previous estimate.**

# Clothing retailer Jaeger falls out of fashion

Administrators for British high-street retailer Jaeger have announced it has gone into administration.

This puts Jaeger's 46 stores, 63 concessions, its logistics centre and its head office in London under threat of closure.

The appointment of administrators, AlixPartners, was made by Jaeger's directors after the company was unable to attract suitable offers despite an extensive process to try to sell the business.

Founded in 1884, Jaeger provided clothing for Ernest Shackleton's Antarctic expedition and was famous for dressing film stars such as Audrey Hepburn and Marilyn Monroe, but the company has struggled in the past few years to stand out in a increasingly competitive fashion retailing market.

# Brexit QC backs cameras in UK courts

Lord Pannick QC has gone on the record supporting the widespread introduction of cameras in court.

Arguably the most publicised case of 2016 was that of Gina Miller — the fund manager who took the government to court over its Brexit strategy, and won.

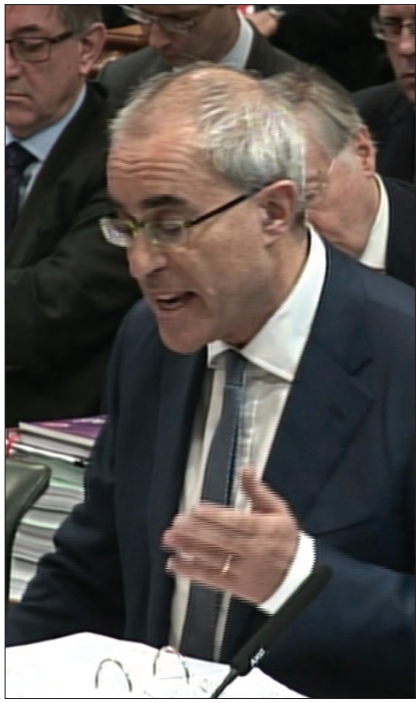
Unlike in the lower level courts, Supreme Court proceedings are filmed and livestreamed, meaning thousands of people were able to tune in and out of the hearing at their leisure.

Leading Miller to victory, Lord Pannick became an unlikely Twitter star when his constitutional law advocacy skills were broadcast to the world.

"Broadcasting of crown court trials would make a substantial contribution to understanding of the legal process," said Lord Pannick

"To impose a general prohibition on broadcasting, preventing members of the public from being able to watch any part of any criminal trial from their homes, is indefensible.

"The criminal justice system should not continue to exclude the most popular means of mass communication. Open justice should be open to the cameras."



TV STAR LORD PANNICK QC

# UK Court backs Azeri Bank IBA's petition over creditors

**International Bank of Azerbaijan (IBA), the energy exporting country's biggest lender, said on Wednesday 7 June 2017 that a London court had supported its request to prevent creditors pursuing legal action in the United Kingdom, giving it time to restructure its $3.3 billion (£2.5 billion) debt. A similar decision was made by a U.S. court last month. The state-controlled bank said last month that it was suspending payments on some liabilities and seeking creditors' support to restructure more than $3 billion of debt, mostly owed to foreign creditors, to tackle bad loans left over from an oil price slump.**

JAHANGIR HACIYEV: JAILED FOR 15 YEARS

**IBA presented a restructuring plan to its creditors on May 23 in London and informed them that they could swap its debt for sovereign bonds, but that some would suffer losses and would have to wait longer to be repaid. "Foreign creditors won't be able to pursue legal actions against the bank's assets and liabilities without the court's permission," IBA said in a statement published on its website**

**The bank's former chairman, Jahangir Haciyev, is serving a 15-year term in prison after being convicted for embezzlement and abuse of office in 2016. Haciyev, a relative of former National Security Minister Eldar Mahmudov, denied the charges.**

# A first for the Insolvency Service

In early April Leicester Crown Court imposed the first ever Serious Crime Prevention Order obtained by the Insolvency Service on Scott Kidd, also known as Scott Sheffield-Kidd and Scott Carrington, of Leicester.

He was arrested on 9 November 2016 in a joint operation with Leicestershire Police, with assistance from the East Midlands Special Operations Unit, and appeared at Leicester Crown Court on 7 December 2016 where he pleaded guilty to two offences of acting in the management of a limited company whilst a disqualified director and two offences of fraud by false representation.

The order runs for five years from his date of release from prison and ensures that over the next five years Mr Kidd must report all his financial and business dealings to the investigators, with the aim of preventing him reoffending.

He will need to report any bank account he opens or has access to, any credit obtained, and premises purchased.

He must detail what businesses he is involved in and must not again use an alias name. Contravention of the order could lead to five years imprisonment and an unlimited fine.

# Karen Millen declared bankrupt

Fashion designer and retailer Karen Millen was declared bankrupt by the High Court at the end of March over a demand for £6 million in unpaid tax. Millen was worth an estimated £35 million when she sold the clothing stores (which she set up with her business partner and former husband Kevin Stanford) that bear her name in 2004.

KAREN MILLEN: BLOCKED FROM STARTING AGAIN

The 2008 collapse of the Icelandic bank Kaupthing, which had financed the buyer who bought the clothing business, wiped-out much of her and Stanford's fortunes. Whilst Millen and Stanford had divorced in 2001 they had maintained the commercial interests they had together, including many in high-street clothing chains. Millen had also invested in a tax avoidance scheme called Round the World which was successfully challenged by the tax man in 2010. In a further blow, she lost a High Court trademark battle last year over her right to start using her name again for a new homewares and lifestyle business.

Ms Millen said she was "deeply devastated" and insisted that she had been a victim of a fraud carried out by Kaupthing.

# CAT orders Law Society to pay up to £230,000 to Socrates

The Competition Appeal Tribunal (CAT) has hit the Law Society with a costs order of up to £230,000 after finding it breached competition law. The CAT ruled that by requiring law firms to buy anti-money laundering (AML) and mortgage fraud training from it, rather than others, as a condition of maintaining their Conveyancing Quality Scheme Accreditation, the Law Society had abused its dominant position in the legal training market.

The claimant, Socrates Training, which provides online AML training packages, alleged that the Law Society's actions were anticompetitive and sought an injunction as well as damages and costs. Its approved costs budget was £230,000.

The CAT ruled that the Law Society must now pay Socrates' costs and damages. Socrates sought £112,500 damages in its claim form. The quantum of damages, however, will be determined at a later hearing.

THE LAW SOCIETY - HIT WITH TRIBUNAL COSTS

# Retail Acquisitions declared insolvent

**Retail Acquisitions, the company through which Dominic Chappell bought BHS from Sir Philip Green for £1, has been wound up.**

**The High Court ruling formally handed down on 16 May, shed light on the amount of cash Chappell extracted from BHS prior to its collapse – amounting to around £9m.**

**Retail Acquisitions' assets will now be scrutinised and BHS administrators Duff & Phelps can begin reclaiming funds for BHS' creditors. According to the ruling, after incorporation, Chappell's business took out a loan of £6.2m from BHS. Then, shortly after buying BHS, it took another £2.8m from the retailer.**

**The money was given to Retail Acquisitions' directors, or companies owned by the directors, City AM reported.**

**The business also took out a loan of £3.5m from Green's retail group Arcadia.**

**The application for permission to appeal by Chappell was refused by Registrar Briggs. Chappell was given 21 days to renew his application to a High Court judge.**

**Former high street stalwart BHS collapsed last year with a £571m black hole in its pension scheme.**

**Earlier this month, the Institute of Directors called for new governance rules for large private companies to avoid a repeat of the BHS pensions scandal.**

# DX under investigation

DX Exchange has, for the past 42 years, been a favoured next-day delivery provider for solicitors and barristers. However, on 9 June the group told investors "The board of DX announces that it has been notified by the City of London police economic crime directorate of an allegation that has been made against the company, which has resulted in the commencement of a preliminary investigation centred on the DX Exchange operations".

As well as servicing the legal sector, DX Exchange is also used by central and local government, banks, building societies and accountants among others.

DX earlier this week won the backing of activist investor Gatemore Capital Management after it revised terms for the proposed merger between DX and John Menzies' distribution division. The board of John Menzies now say that they are considering their position and will make an announcement "when appropriate".

DX: ALLEGATION AGAINST DX EXCHANGE OPERATIONS

## Supreme Competition for the South Square Challenge!

**The Supreme Court has launched its own competition, and in contrast to our own Challenge the victor will win tea with an-as-yet-unnamed Supreme Court Justice and a £100 book voucher.**

**Judged by a Supreme Court justice, the writing competition asks Year 12 and 13 students to submit 1,000-1,500 word answers to one of the following questions:**

*** Has the law reached a fair balance between protecting the rights of individuals, whilst still safeguarding society against crime and terrorism?**

*** Has the law successfully adapted to combat discrimination or are there areas where it needs to go further to protect minorities?**

*** Is it justifiable that public interest can override an individual's right to privacy?**

**Helpfully, the Supreme Court lists useful cases for each question and, in words of the Supreme Court, entering the competition "will look great on your UCAS form"**

# HMRC to reach for the stars

**At the end of April HMRC deployed 180 officers across the UK and France to raid the offices of several football clubs, including Newcastle United and West Ham. A press release by HMRC stated that "HMRC has arrested several men working within the professional football industry for a suspected £5m income tax and national insurance fraud."**

**Whilst no further details were given, speculation is that the tax fraud is linked to the abuse of image rights, and the involvement of the French authorities highlights that this is a cross-border problem.**

**Image rights have an established place in the contracts between players and clubs, enabling them to commercialise various aspects of a player's identity. These rights have a potentially significant value to the individual over and above their earning potential from a particular profession.**

**Whilst historically the majority of litigation around image rights focuses on celebrities protecting their pictures, signatures and the like from exploitation without consent, the new HMRC arrests are thought to centre on concerns that image rights payments might be used to shelter income from tax authorities.**

**The concern is that a large proportion of salary can be disguised as an image rights payment, and therefore enjoy the tax breaks that such payments offer if a player's image rights company is established outside the UK.**

# SOUTH SQUARE CHALLENGE

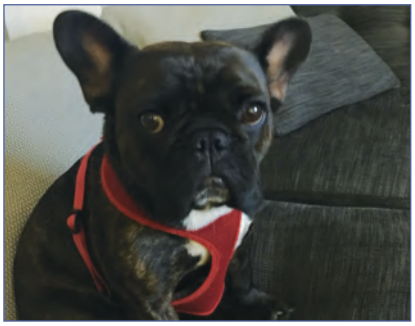
As a light-hearted Challenge this June we have decided to hold a 'match the dog to its owner' competition. If the urban myth that dogs and their owners tend to look alike, the results could be pawsitively fascinating. Below we have a selection of the dogs owned by Members and, on the facing page, their dogglegangers! In a twist to our usual rules, in the unlikely event that there are no completely correct entries the winner (drawn from the wig tin if necessary) will be the entrant with the greatest number of correct matches. As always the prize is a magnum of champagne and a much-coveted South Square umbrella. Please send your entries to Kirsten by 1 September 2017 either by post to the address on the back page, or by e-mail to kirstendent@southsquare.com.

LARKIE'S OWNER IS?.....

HOBBES' OWNER IS?.....

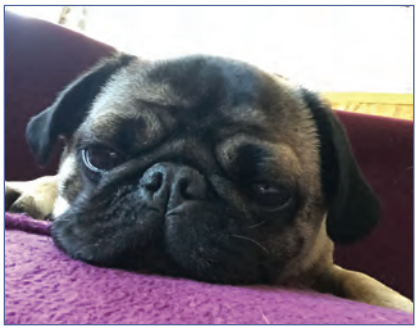
DYLAN'S OWNER IS?.....

RUM'S OWNER IS? .....



COCO'S OWNER IS?.....

COBY'S OWNER IS?.....



BRUCIE'S OWNER IS? .....

CONCHITA'S OWNER IS?.....


MARK PHILLIPS QC


JOHN BRIGGS


EDOARDO LUPI


GABRIEL MOSS QC


FELICITY TOUBE QC


DAVID ALLISON QC


GLEN DAVIS QC


MARTIN PASCOE QC

## MARCH CHALLENGE

*The correct answers to the March 2017 Challenge were:*
*1/. The Paper Chase. 2/. To Kill A Mocking Bird. 3/. Miracle on 34th Street. 4/. Kramer v Kramer. 5/. Philadelphia. 6/. My Cousin Vinny 7/. A Man For All Seasons. 8/. Judgment at Nuremberg.*
*The connection was that they were all Oscar-winning films with a legal slant.*
*We had many correct entries but the winner, drawn from the wig tin, is Robert Tiffen of Birketts LLP, to whom go our congratulations, a magnum of Champagne and a South Square umbrella.*

# Diary Dates

**Members of South Square will be attending, speaking at and/or chairing the following events:**

**International Insolvency Institute 17th Annual Conference**
18-20 June 2017- Rosewood Hotel, London

**Chancery Bar Association Summer Conference 2017- Litigation Issues in Modern Chancery**
26 June 2017 - Royal College of Surgeons, Lincoln's Inn Fields

**INSOL International/INSOL Europe joint conference**
27 June 2017 - Tel Aviv

**INSOL International Channel Islands Seminar**
13 September 2017 - Duke of Richmond Hotel, Guernsey

**ILA Annual Dinner**
26 September 2017 - Guildhall

**Litigation Forum 2017 (co-hosted by South Square and Mourant Ozannes)**
27 September 2017 - 200 Aldersgate, London

**INSOL Europe Annual Congress**
5 October 2017 - Warsaw

**RISA Conference 2017 (in association with South Square)**
28 November 2017 - Grand Cayman

South Square also runs a programme of in-house talks and seminars – both in Chambers and onsite at our client premises – covering important recent decisions in our specialist areas of practice, as well as topics specifically requested by clients. For more information contact events@southsquare.com, or visit our website www.southsquare.com

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# Butterworths Insolvency Law Handbook

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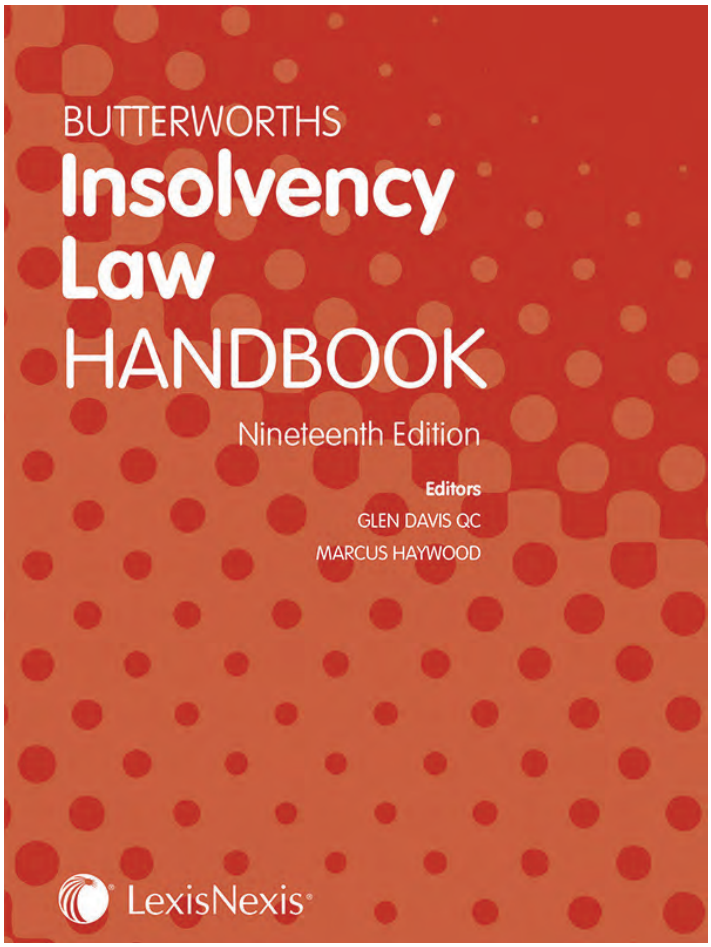
Now in its 19th edition, this essential reference source for lawyers, accountants, insolvency practitioners, regulators and students is fully brought up to date to 6 April 2017 to include all recent amendments and new legislation:

- Substantial amendments to the Insolvency Act 1986 (applying in relation to England and Wales) made by the Small Business, Enterprise and Employment Act 2015 which came into force on 6 April 2017;
- The Insolvency (England and Wales) Rules 2016 (as amended by the Insolvency (England and Wales) (Amendment) Rules 2017) which apply from 6 April 2017;
- The Disqualified Directors Compensation Orders (Fees) (England and Wales) Order 2016 and the Disqualified Directors Compensation Orders (Fees) (Scotland) Order 2016;
- Various amendments made by the Insolvency (England and Wales) Rules 2016 (Consequential Amendments and Savings) Rules 2017
- New Scottish Regulations including the Bankruptcy (Scotland) Regulations 2016, the Bankruptcy (Applications and Decisions) (Scotland) Regulations 2016, and the Protected Trust Deeds (Forms) (Scotland) Regulations 2016.

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