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Digest

BTI 2014 LLC v Sequana SA

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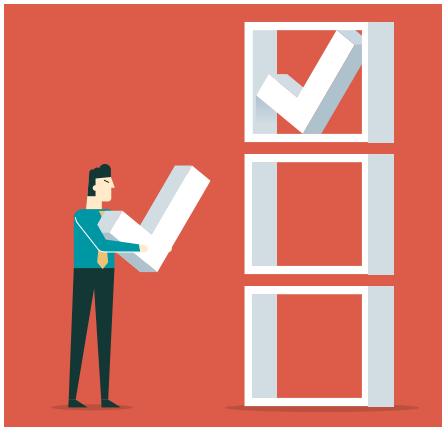

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Cover: King Charles III visits Gray's Inn, 23 November 2022. Credit Liz Isles Photography lizislesphotography.com 07772294329. Liz Isles is the recommended photographer for Gray's Inn and specialises in events, weddings, corporate and branded photography

SOUTH SQUARE

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From the editors

Marcus Haywood and William Willson

Welcome to the Christmas 2022 edition of the Digest! Another edition of the Digest brings another new Prime Minister. When the last edition of the Digest went to print in September, the UK had just got a new Prime Minister – its third in three years – Liz Truss. Since then, after only fifty days in office, Liz Truss stepped down amid a government and market crisis, making her the shortest-serving Prime Minister in the history of the United Kingdom.

Those fifty days saw a whirlwind of political and economic developments. On 23 September, Kwasi Kwarteng announced a controversial mini-budget encapsulating "Trussonomics", which proposed cutting taxation significantly, abolishing the 45% top income tax rate, cutting the basic rate of income tax, cancelling rises in national insurance contributions and corporation tax, abolishing the proposed Health and Social Care Levy, and cutting stamp duty, policies that were to be funded by borrowing.

The budget was poorly received by financial markets, blamed for a rapid fall in the value of the pound, and prompted a response from the Bank of England. The budget was criticised by the International Monetary Fund, US President Joe Biden, the Labour Party and many within Truss's party, including Michael Gove and Grant Shapps.

By 3 October, the abolition of the 45% income tax rate had been reversed. The cut in corporation tax was to go shortly after and Kwarteng was sacked and replaced by Jeremy Hunt on 14 October. Hunt subsequently reversed the vast majority of the remaining policies announced in the mini budget.

On 20 October, on her 45th day in office, Truss announced her resignation. She was succeeded by Rishi Sunak as Prime Minister on 24 October. Whilst the financial markets have calmed somewhat since then, many challenges remain ahead. Not least, on 3 November, the Bank of England warned that the UK is potentially facing its longest recession since records began, as it raised interest rates by the most in 33 years.

Against this background of economic decline, on 5 October 2022, the Supreme Court handed down its long-awaited judgment in *BTI 2014 LLC v Sequana SA*, the first case in which the Supreme Court has had the opportunity consider the existence, content and engagement of the so-called "creditor duty" (i.e. the duty of a director to consider the

interests of the company's creditors when the company is insolvent, or bordering on insolvency).

In this edition of the Digest, we have two articles covering differing aspects of this important judgment. Mark Phillips KC, Mark Arnold KC and Rabin Kok consider the history, rationale and scope of the duty following the Supreme Court's decision in *The Creditor Duty Comes of Age*. Meanwhile, Scott Atkins (Norton Rose Fulbright), Felicity Toube KC and Hilary Stonefrost focus on creditor protection, director liability and the impact on corporate restructuring of the decision in *The Interests of Creditors in the Zone of Insolvency.*

This edition of the Digest also sees the Insolvency Lawyers Association (ILA) reach an important milestone: the 1000th ILA Technical Bulletin. To celebrate this, we have an article prepared by members of the ILA Technical Committee (the ILA Committee which produces the Technical Bulletins) which looks back at where the ILA has been and ahead at what is to come. Chambers is proud of its long-standing association with the ILA and delighted to have this contribution to the Digest.

Coming fast off the back of the South Square / RISA Cayman conference and INSOL's third seminar in the British Virgin Islands (both attended by a number of members of Chambers), we also have two offshore articles. First, *Restructuring Repackaged in the Cayman Islands*, an article by Hamid Khanbhai of Campbells (Cayman) on the new restructuring regime known as the Restructuring Officers Proceeding or Restructuring Moratorium Proceeding which came into force in the Cayman Islands in August 2022. Second, *Bermudian Insolvency and Restructuring Law Update*, an article by John Wasty, Lalita Vaswani and James Batten of Appleby (Bermuda) which discusses three areas of recent development in Bermuda's insolvency and restructuring landscape.

Meanwhile, looking across the continent, Gemma Freeman and Luci Mitchell-Fry, of Dentons, review recent changes to the European Union (Preventative Restructuring) Regulations 2022 in *Your restructuring regime or mine?*

And in *The Excluded Asset Gap*, Matteo Clarkson-Maciel (Wilkie Farr & Gallagher) and Paul Fradley discuss when the proceeds of the sale of an asset, excluded from the scope of a floating charge, will be captured by that charge when sold by an insolvency practitioner.

In addition to these seven articles, we have our regular pieces including, as always, the Case Digests (which includes summaries of a number of important recent cases involving members of Chambers) and the South Square Challenge. We also have the next instalment of Simon Mortimore KC's history of Chambers, which in this edition reflects on the life of Muir Hunter, his family background, influences and early years.

Finally, in News in Brief, amongst other news there is a report of the visit of King Charles III to Gray's Inn on 23 November 2022, The King being a Royal Bencher of the Inn. A picture of the royal visit also appears on the front cover of this edition.

In other good news, Chambers welcomes Rabin Kok as a full member of chambers following the successful completion of his pupillage. Congratulations Rabin!

Many thanks to all our authors for their contributions. As always, views expressed by individuals and contributors are theirs alone.

We hope you enjoy this edition of the Digest. We wish all our readers an enjoyable festive season and happy New Year.

If you find yourself reading someone else's copy, or indeed have come across the Digest for the first time and wish to be added to the circulation list, please send an e-mail to kirstendent@southsquare.com and we will do our best to make sure you get the next and future editions.

It goes without saying that if you have any feedback to give us in relation to the Digest – positive or negative – we would be delighted to hear from you.

Marcus Haywood and William Willson

MARK PHILLIPS KC[1] **MARK ARNOLD KC** **RABIN KOK**

The Creditor Duty Comes of Age

A. Introduction

On 5 October 2022 the Supreme Court (Lords Reed, Hodge, Briggs, Kitchin and Lady Arden) gave long-awaited judgment in *BTI 2014 LLC v Sequana SA ("Sequana")*. *Sequana* raised important questions in relation to the director's duty to have regard to the interests of creditors when the company is in what is often called the "twilight zone", but it was the wrong case on its facts to resolve many of the more nuanced questions that fall to be determined. What the Supreme Court confirmed is that the "rule in *West Mercia*", so called after the Court of Appeal's decision in 1987 in *West Mercia Safetywear Ltd (in liq) v Dodd* [1988] BCLC 250, is part of English law, but the Supreme Court's decision says more about when the rule is not engaged rather than when it will be.

It held that the payment of a dividend when the company was neither insolvent nor on the verge of insolvency did not mean the directors had to have regard to the interests of creditors, even if there might be a risk of insolvency at some point in the future.

B. The Facts

On 18 May 2009, Arjo Wiggins Appleton Ltd ("AWA"), a UK registered company, made a distribution of nearly all its net assets to its parent company, Sequana SA. AWA had a long-term contingent environmental liability in respect of clean-up costs as a result of the pollution of the Fox River in Wisconsin[2]. AWA followed the statutory procedure in Part 23 of the 2006 Act for quantifying the amount that

1. *Mark Phillips was Counsel for the Liquidator in West Mercia Safetywear v Dodd.*

2. *BTI 2014 LLC v Sequana SA [2022] UKSC 25 ("Sequana (SC)")* at [115]; *BAT Industries plc v Sequana SA [2017] Bus. L.R. 82 (Sequana (HC))* at [5].

may be paid by way of distribution, including the preparation of relevant accounts, and made proper provision for its contingent liability. Some years after the distribution was made, it emerged that the contingent environmental liability, was much greater than originally estimated, and A Ltd became insolvent[3]. By then, however, AWA had already commenced proceedings against its directors for breach of duty, which it subsequently assigned to BTI 2014 LLC. The critical fact was that the distribution had been made some years before, at a time when Sequana was neither actually insolvent, nor imminently insolvent, nor in a position where insolvency was probable. The most that could be said at the time was that the estimate might turn out to be too little such that there was a real risk of insolvency.

Rose J at trial found that the distribution was lawfully made and that the risk of AWA's insolvency at the time of the distribution was not sufficient to trigger an obligation to consider creditors' interests. At the time of the distribution, AWA was not insolvent or likely to become insolvent. In her view, the Fox River liability was a long-term liability for which the directors had made their best estimate, and to hold them responsible for creditors' interests whenever there was a risk that the estimate would turn out to be wrong would be a significant, unprincipled, inroad into the normal way in which directors' duties applied.[4]

The Court of Appeal dismissed the appeal.[5] Judgment was delivered by David Richards LJ who held that the Court of Appeal was bound by the decision in *West Mercia* to hold that the directors owed a duty to consider the interests of creditors and that the authorities showed that the duty in relation to creditors was triggered when the directors knew or should have known that the company was insolvent.[6] In his judgment, the duty arose immediately prior to insolvency. Eschewing words suggesting that the test is that insolvency is imminent as they suggested a temporal test, however, he concluded that the duty arises when the directors know or should know that the company is likely to become insolvent, meaning that it will probably do so.[7] The company was not insolvent when the distribution was paid, and nor could it be said that it would probably become so. The duty did not arise simply because there was a real, and not remote, risk of insolvency.

An important question that the Court of Appeal left open – because it did not arise on the facts – was ***how much weight*** should be given to creditors' interests – were their interests paramount, or simply one factor among many for directors to weigh when faced with difficult business decisions? That said, David Richards LJ found it difficult to see how creditors' interests could be anything but paramount when a company was actually and presently insolvent, and said so.[8]

C. West Mercia – The Beginnings

Before *Sequana*, the existence of the 'creditor duty' in West Mercia was recognised (albeit obiter) in no fewer than five judgments at the highest level – including the Supreme Court's decision in *Bilta (UK) Ltd v Nazir (No. 2)*[9] and the Privy Council's decision in *Ciban Management Corp v Citco (BVI) Ltd.*[10]

It is perhaps surprising that the parties thought the existence of the rule was 'up for grabs', given how well established the *West Mercia* rule has become in common law jurisdictions and how readily the Justices have endorsed its existence, albeit in *obiter dicta* and while sitting as members of the JCPC. Nevertheless, the existence of the *West Mercia* rule was directly in issue in *Sequana*, and the court took the opportunity to conduct a root-and-branch examination of the origins of the rule.

West Mercia Safetywear Ltd was a subsidiary of AJ Dodd & Co Ltd. Mr Dodd, the director of both companies, transferred £4,000 from West Mercia's account to its parent's account, shortly before both went into liquidation. The parent having no assets available to enable it to repay, the liquidator of West Mercia sought an order that Mr Dodd repay the £4,000 instead. However, the first instance judge held that Mr Dodd had breached no duty to West Mercia because he was discharging a debt for West Mercia's benefit and, by extension, its shareholders.

The judge had found as a fact that both companies were not just distressed but insolvent when the £4,000 was paid.[11] So the question of whether there was a duty in the 'twilight zone' did not arise. The only question was whether Mr Dodd had breached any duty. The authorities on the topic were, it seems, in some disarray. The difficulty faced by counsel for the liquidators was that, in the *Multinational Gas* case, Dillon LJ had

3. *Sequana (HC)* at [6].

4. *Sequana (HC)* at [479].

5. *BAT Industries plc v Sequana SA* [2019] 2 All E.R. 784 ("Sequana (CA)").

6. *Sequana (CA)* at [217], and the preceding paragraphs.

7. *Sequana (CA)* at [218]-[221].

8. *Sequana (CA)* at [222].

9. [2016] AC 1, at [38] (Lord Mance).

10. [2021] AC 122 at [40] (Lord Burrows). See also *Stone & Rolls Ltd v Moore Stephens* [2009] AC 1391, Lord Mance at para 236; *MacDonald v Carnbroe Estates Ltd* [2019] UKSC 57, Lord Hodge at para 33; and *Byers v Chen* [2021] UKPC 4, Lord Kitchin at para 91.

11. *West Mercia Safetywear v Dodd*, 251g.

appeared to close off the path to the development of a creditor duty in English law, stridently declaring that:

"The directors indeed stand in a fiduciary relationship to the company, as they are appointed to manage the affairs of the company and they owe fiduciary duties to the company though not to the creditors, present or future, or to individual shareholders."[12]

In *West Mercia*, Dillon LJ was quick to point out that his words had been directed at ***solvent*** companies where the shareholders retained the economic interest. ***Insolvent*** corporations were a different matter. Here, Dillon LJ agreed with what Street CJ had said in *Kinsela v Russell Kinsela Pty Ltd*, an Australian authority that he had been referred to in argument:

"In a solvent company the proprietary interests of the shareholders entitle them as a general body to be regarded as the company when questions of the duty of directors arise…

But where a company is insolvent the interests of the creditors intrude. They become prospectively entitled, through the mechanism of liquidation, to displace the power of the shareholders and directors to deal with the company's assets. It is in a practical sense their assets and not the shareholders' assets…"[13]

That being so, the Court of Appeal had no difficulty in concluding that Mr Dodd caused the £4000 to be transferred in disregard of the interests of West Mercia's general creditors and was liable accordingly for misfeasance.

In Sequana, the court probed the historical origins of *West Mercia* more searchingly. Viewed against the long history of the common law *Kinsela* was an innovation, but Street CJ's pronouncement was far from being without any basis in authority. As Lord Reed recounts:

"29. A number of significant developments have occurred in relatively recent times. An early pointer was an influential dictum in the Australian case of Walker v Wimborne (1976) 137 CLR 1, where Mason J observed at p 7 that "the directors of a company in discharging their duty to the company must take account of the interest of its shareholders and its creditors," explaining that "[a]ny failure by the directors to take into account the interests of creditors will have adverse consequences for the company as well as for them."…

30. The idea that creditors' interests might be a relevant factor received more extended consideration in the New Zealand case of Nicholson v Permakraft (NZ) Ltd [1985] 1 NZLR 242 ("Permakraft"), where Cooke J expressed the view, obiter, that directors might owe a duty to the company to consider the interests of creditors "if the company is insolvent, or near-insolvent, or of doubtful solvency, or if a contemplated payment or other course of action would jeopardise its solvency" (p 249). He considered that such a duty might apply in respect of the interests of "current and likely continuing trade creditors" (ibid), but not other creditors. He stated that such a duty could be justified on the basis that "[i]n a situation of marginal commercial solvency such creditors may fairly be seen as beneficially interested in the company or contingently so" (p 249)…

31. That reasoning influenced the judgment of Street CJ in Kinsela v Russell Kinsela Pty Ltd (1986) 4 NSWLR 722 ("Kinsela"), a decision of the New South Wales Court of Appeal which heralded a more radical change in the way in which the law understands the concept of a company's interests…"

Lord Briggs went even further back, tracing the *"radical"* idea in *Kinsela* to the ancient recognition that debtors have duties to their creditors:

"[T]he company itself owes responsibilities to its creditors once it is insolvent, so that the directors as the custodians of the conscience of the company are duty bound to the company to see that it performs those obligations. The notion that insolvent persons have responsibilities to their creditors goes back to Roman law, in the Lex Paulina. This basic principle has long since been given effect to by statutory provision, both in England and Scotland …"[14]

Lady Arden, it should be noted, agreed that the seed of the idea recognised in *Kinsela* and thence in *West Mercia* was rooted in authority, though her survey was somewhat briefer.[15]

D. The West Mercia Duty in the Supreme Court

The Supreme Court acknowledged that the *Sequana* appeal raised questions of considerable importance for company law, but also noted that it was necessary to express provisional views about some issues which did not call for a final decision. It is important to note that the differences in reasoning, certainly among the four majority Justices, arose on matters which did not arise for decision. Still, this divergence will be a source of some uncertainty for directors and insolvency lawyers for some while to come.

The Supreme Court rightly held that there is no separate "creditor duty" i.e. a duty owed directly to creditors. That was not what *West Mercia* had held – the director's duty was a duty owed to the company as part of the director's fiduciary duties, specifically the duty to act in good faith in the interests of the company (now codified as the duty to promote the success of the company).[16] What changes is the content of that duty. When the company is insolvent or in the twilight zone that duty includes having regard to the interests of the creditors. As Lord Reed put it *"there are circumstances in which, for the purposes of the [director's duty to act in the interests of the company], the duty should be understood as including the interests of its creditors as a whole."* [17]

12. [1983] Ch 258, 288.
13. (1986) 4 NSWLR 722, 730.
14. *Sequana (SC)* at [129] and [146].
15. *Sequana (SC) at* [252]–[260].
16. Sequana *(SC)* at [112], [135], [261]–[277].
17. *Sequana (SC)* at [11].

The ratio of Lord Reed's judgment is contained in the following passage:

"Where the modifying rule applies – a rule which I shall describe as the rule in West Mercia, after the leading case ... the company's interests are taken to include the interests of its creditors as a whole. The duty remains the director's duty to act in good faith in the interests of the company. The effect of the rule is to require the directors to consider the interests of creditors along with those of members. The weight to be given to their interests, insofar as they may conflict with those of the members, will increase as the company's financial problems become increasingly serious. Where insolvent liquidation or administration is inevitable, the interests of the members cease to bear any weight, and the rule consequently requires the company's interests to be treated as equivalent to the interests of its creditors as a whole." [18]

In answering whether there is a "rule in *West Mercia*", Lord Briggs held:

"I am persuaded that the undertaking of that re-appraisal shows that the existence of a creditor duty at common law is sufficiently established, and sufficiently well-founded on principle, for it to be appropriate for this court to affirm it." [19]

Lord Kitchin agreed with Lord Briggs' majority judgment, as did Lord Hodge.

As for when the rule applies, Lord Reed said:

"I am satisfied that the rule in West Mercia does not apply merely because the company is at a real and not remote risk of insolvency at some point in the future. I therefore agree with the other members of the court that the appeal falls to be dismissed, and the claim fails."[20]

The rationale of the rule

Lord Reed explained the rationale of the rule in *West Mercia* as follows:

"It can be explained ... on the basis that, where the rule in West Mercia applies, the company's creditors have an economic interest in the company, based upon their entitlement to be paid the debts owed to them, ultimately enforceable against the proceeds of realisation of the company's assets, which is distinct from the interests of its members and requires separate consideration: something which can be taken to occur when the company is insolvent or bordering on insolvency, or where an insolvent liquidation or administration is probable, or where the transaction in question would place the company in one of those situations." [21]

"...where a company is insolvent or bordering on insolvency, the way in which the interests of the company are understood, for the purposes of the directors' duty to act in good faith in its interests, is extended so as to include the interests of the company's creditors as a whole as well as those of its shareholders. Where the company's interests have to be understood in that extended sense, it will be a breach of the directors' duty to the company for them to act in disregard of the creditors' interests." [22]

18. *Sequana (SC)* at [11].
19. *Sequana (SC)* at [138].
20. *Sequana (SC)* at [14].
21. *Sequana (SC)* at [12].
22. *Sequana (SC)* at [51].

Lord Briggs explained the rationale in similar terms: *"...it is not an abuse of language to describe creditors as having the main economic stake in the liquidation process which may be triggered by insolvency, and therefore as persons whose interests must be taken into account (albeit not necessarily as paramount) by the company's fiduciary managers, while still in control of the management of the insolvent company before the onset of liquidation."*[23]

Lord Hodge said at the outset: *"I am satisfied that the directors of a company which is insolvent or is bordering on insolvency owe a duty to the company to have proper regard to the interests of its creditors and prospective creditors."*[24] He put the rationale in the following two passages:

"When a company is insolvent or bordering on insolvency its creditors are recognised as having a form of stakeholding in the company, and its directors from that point must have a proper regard to the interests of the company's creditors as a body... I am satisfied that that remains good law. While the law in this area has remained in a relatively undeveloped and ill-defined state, I was not aware, until this appeal, of any serious challenge by company law practitioners to the existence of this fiduciary duty, which has been upheld by experienced commercial judges in a number of first instance decisions." [25]

"A company's creditors always have an economic interest in its continued solvency so that it can pay its debts to them. The relative importance of that economic interest or stakeholding as against the economic interest or stakeholding of the company's shareholders increases when a company is bordering on insolvency. It is this shift in relative economic interest or, in Lord Briggs' non- technical words, "skin in the game", that gives rise to the fiduciary duty to the company to give separate and proper consideration to the interests of a company's creditors." [26]

Lady Arden's judgment is difficult in places, not least because on some issues her reasoning was in the minority.

Lady Arden's description of the underlying rationale of the rule in *West Mercia* was, at times, consonant with Lord Reed's analysis.

She said: *"As Lord Reed explains... the rule in West Mercia applies when the economic position of the creditors changes: that analysis is an endorsement of the emphasis in the case law on the practical operation of the law in this field ... the rationale of the Rule in West Mercia is the need to ensure, so far as practicable, that creditors are not harmed by the asymmetry in governance following on from the shift in the economic interest which Lord Reed describes."* [27]

"It is only right that the fiduciary duties of directors should be qualified to provide appropriate protection to creditors and approving the Rule in West Mercia has the advantage of endorsing the high standards expected of directors." [28]

However, Lady Arden's primary focus was on showing that the duty was a negative duty, taking the form of one not to cause harm to creditors.

23. *Sequana (SC)* at [147].
24. *Sequana (SC)* at [207].
25. *Sequana (SC)* at [207].
26. *Sequana (SC)* at [246].
27. *Sequana (SC)* at [256].
28. *Sequana (SC)* at [258].

In her view, the rule was ultimately concerned to solve the 'principal-agent problem' that arises because creditors are not in the 'driver's seat' of a company prior to its insolvency and cannot control what the directors do:

"The correct analysis is that they may not exercise any of their powers so as to harm creditors' interests... [T]he purpose of the Rule in West Mercia is to redress the situation that creditors do not have any control over the management of the company at a time which is critical for the recovery of what is due to them. Given this purpose, the requirement of the Rule in West Mercia in practical terms is in my judgment a requirement on directors to consider creditors' interests at all material times and not to harm their interests." [29]

E. Sequana: Questions Answered

Turning to the questions considered and the answers provided:

The answer to question (1) – Does the rule in West Mercia even exist? Yes

Lord Reed held:

"This is the most fundamental question raised by this appeal. I answer it in the affirmative. It is clear that such a rule was recognised by the Court of Appeal and lower courts before the enactment of the 2006 Act. The existing law in this regard was preserved by section 172(3) of that Act, as this court has previously accepted in the cases of Bilta (UK) Ltd v Nazir (No 2) and MacDonald v Carnbroe Estates Ltd. I am satisfied that the rule has a sound legal basis...." [30]

Having debated the issues, Lord Briggs stated the answer to question 1 succinctly: *"I would resolve the first issue against the respondents".* [31]

The answer to question (2) – the content of the duty: It depends

Lord Reed held the rule modifies the director's duty:

"...the effect of the rule in West Mercia is to preserve the directors' duty to act in the interests of the company, but to modify the sense of the latter expression so that, where the rule applies, the interests of the company are no longer regarded as solely those of its shareholders but are understood as including those of its creditors as a whole." [32]

Lord Reed, agreeing with Lord Briggs,[33] approved the nuanced description of the duty by Lt. Bailiff Hazel Marshall QC in *Carlyle Capital Corp v Conway*, [34] a judgment of the Royal Court of Guernsey:
"I formulate the principle ...to take account of differences, according to particular circumstances, in what it may be reasonable and responsible for directors to do when they find that the company is in a sufficiently weak financial situation that a conflict of interest between its creditors and its shareholders appears to arise. The company is not - yet - in insolvent liquidation and remains under the management of the directors. Their duty is to decide what is in the extended best interests of the company in the particular case. It may well be that in some, possibly even most, situations, the company should thenceforth be run with regard to the best interests of its creditors alone, but that will not necessarily be true in all cases, and it is for that reason that I reject the word 'paramount'."

Lord Briggs emphasised that it is a fact sensitive question: *"...prior to the time when liquidation becomes inevitable and section 214 becomes engaged, the creditor duty is a duty to consider creditors' interests, to give them appropriate weight, and to balance them against shareholders' interests where they may conflict."* [35]

Lady Arden said that the rule in *West Mercia* is in two parts: *"The first part is the requirement for directors to consider creditors' interests. This arises whenever a company is financially distressed. By that I mean, ... the company is insolvent or bordering on insolvency, or an insolvent liquidation or administration is probable, or the directors plan to enter into a transaction in question would place the company in one of those situations."* [36]

Again, and unlike the other members of the Court, Lady Arden conceived of the rule as a 'harm prevention rule'. Her analysis, therefore, requires directors to think each action by the company through carefully, to consider if it would make creditors better off than in a liquidation:[37]

"If they consider in good faith, and having performed their duty of skill and care, that they can and should take action to promote the continued viability of the company, and that there is a way out of the company's financial difficulties, which will benefit shareholders and creditors, they are not obliged to treat the creditors' interests as the exclusive or primary determining factor in what they do next. However, since directors are obliged not materially to harm creditors' interests, they must be satisfied that the general body of creditors would be better off under that measure than if the company is immediately put into liquidation or equivalent process..."

Question (3) – when does the creditor duty apply? When insolvency is actual or imminent

The Supreme Court unanimously rejected the argument that the test should apply when there is a real rather than remote risk of insolvency or when insolvency is likely or even probable.

Lord Reed said that he was inclined to agree that it is sufficient if the company is "insolvent or bordering on insolvency"– in other words once the company has entered the so-called 'twilight zone' and insolvency is imminent:

"... the critical factor is whether, given where the economic interests lie, and the consequent

29. *Sequana (SC)* at [288].
30. *Sequana (SC)* at [76].
31. *Sequana (SC)* at [157]. The SC was unanimous on this point: see also Lord Hodge at [207] and [228], and Lady Arden at [250].
32. *Sequana (SC)* at [79].
33. *Sequana (SC)* at [82] and [171] respectively.
34. Judgment 38/2017 (unreported), 4 September 2017, set out in *Sequana (SC)* at [170].
35. *Sequana (SC)* at [176].
36. *Sequana (SC)* at [279].

distribution of risk, it continues to be appropriate to treat the interests of the company as equivalent to the interests of its shareholders alone." [38]

Lord Briggs described the principle as follows:

"The true principle ... is that creditors (or at least unsecured creditors) are not the main stakeholders in the company at any earlier date than when it goes into insolvent liquidation, at which point they acquire statutory priority in an entitlement to share pari passu in any distributions which that process may generate. It is that prospective entitlement which entitles them to have their interests considered, although not necessarily given paramountcy, when the onset of insolvency makes that prospect both much more likely and one which may be beyond the ability of the company to control, in the sense that insolvency immediately exposes a company to being wound up at the behest of any unpaid creditor." [39]

Lord Briggs then formulated when the duty applies: *"I would prefer a formulation in which either imminent insolvency (ie an insolvency which directors know or ought to know is just round the corner and going to happen) or the probability of an insolvent liquidation (or administration) about which the directors know or ought to know, are sufficient triggers for the engagement of the creditor duty. It will not be in every or even most cases when directors know or ought to know of a probability of an insolvent liquidation, earlier than when the company is already insolvent. But that additional probability-based trigger may be needed in cases where the probabilities about what lies at the end of the tunnel are there for directors to see even before the tunnel of insolvency is entered."* [40]

Lords Kitchin and Hodge agreed with this formulation.[41]

Lord Reed was *"inclined to agree"* with Lords Briggs, Kitchin and Hodge that the probability of an insolvent liquidation or administration would also suffice, but was *"less certain"* that it is essential that the directors *"know or ought to know"* that the company is bordering on insolvency.

Lady Arden said she would leave the question of knowledge open for full submissions. It may be that the 'twilight zone' is a state of affairs and should not turn on the director's state of mind.

Lady Arden said that *"the interests of creditors can only supplant the interests of shareholders altogether when the company becomes irreversibly insolvent, making insolvent liquidation or an administration unavoidable."*[42] *She agreed that "the test of a real and not remote risk of insolvency and the test of likelihood of becoming insolvent should be rejected."*[43]

Interaction with other provisions of the Insolvency Act 1986.

The Supreme Court was asked to consider the interaction of the rule in *West Mercia* with provisions of the Insolvency Act 1986, but, as the conclusion was that the provisions all work in different ways and none is incompatible with the rule in *West Mercia*, there is no need to elaborate here.

Interaction with the "ratification principle"

The Supreme Court recognised the interplay between the rule in *West Mercia* and what Lord Briggs referred to as the ratification principle (shorthand for the ability of shareholders, formally or informally, to authorise or ratify conduct that would otherwise constitute breach of duty on the part of the directors). Sensibly, the two cannot operate simultaneously, and it is accepted that the latter cannot operate when the company is actually insolvent, as Dillon LJ recognised in *West Mercia* itself. What falls to be determined more precisely another day is when – short of actual insolvency – that moment comes when the shareholders are deprived of that power, and whether on the facts of the case they have been. It sufficed for the purposes of decision in *Sequana* that the rule and the principle are not incompatible or irreconcilable such as to throw doubt on the existence of the rule itself; rather, the authorities show that the principle can *"readily adapt to the creditor duty on a principled basis"*.[44]

The Debate Surrounding the work of the Company Law Review Steering Group ("CLRSG")

There was a surprisingly lengthy debate about the effect of section 172(3) of the Companies Act 2006 and the views of CLRSG, which had recommended a statutory statement of the main fiduciary duties of directors and their duty of care and skill.

Lord Briggs said Parliament must be taken to have understood that *West Mercia* was binding law and section 172(3) had affirmed its existence:

"...the existence (although not the precise content and engagement) of the creditor duty was affirmed as existing at common law in section 172(3). That subsection needs to be interpreted in its historical context. It refers to "any enactment or rule of law" and makes the general duty set out in the rest of section 172 subject to it....Parliament must be taken to have understood the general state of the common law at that time, which by the binding Court of Appeal authority of the West Mercia case did clearly recognise a creditor duty, even if the precise content of that rule of law may have had fuzzy edges, and might thereafter be subject to further judicial development." [45]

Disagreeing with Lady Arden's analysis on this point, Lord Briggs agreed with Lord Reed that section 172(3) speaks for itself in sufficiently clear terms. He also agreed, however, with Lord Hodge's analysis of the legislative history.[46]

37. *Sequana (SC)* at [284].
38. *Sequana (SC)* at [87]. [88]: he considered that other phrases adopted in the authorities were *"broadly synonymous"*, all conveying *"a sense of imminence"*.
39. *Sequana (SC)* at [192].
40. *Sequana (SC)* at [203].
41. *Sequana (SC)* at [227].
42. *Sequana (SC)* at [306].
43. *Sequana (SC)* at [306].
44. *Sequana (SC)*, Lord Briggs at [149].
45. *Sequana (SC)* at [153].
46. *Sequana (SC)* at [154] and [204].

Lord Hodge, who, along with Lady Arden, was a member of the CLRSG said:

"In my view, in agreement with Lord Briggs, the words of section 172(3) of the 2006 Act point towards the purpose of preserving the commonlaw as it had been developed before the 2006 Act, particularly in [West Mercia]. That interpretation of the subsection is supported by a consideration of its historical origins..."[47]

Lord Hodge noted that *"it was recognised that directors were subject to other duties which were not included in the proposed codification."*[48] Like Lady Arden, Lord Hodge analysed the debate at the time but reached a different conclusion. Lord Hodge referred to the White Paper (which is admissible) which said:

"In doing so, it preserves the current legal position that, when the company is insolvent or is nearing insolvency, the interests of the members should be supplemented, or even replaced, by those of the creditors."[49]

That was a recognition of the existence of the rule in *West Mercia*. It was also recognised in the explanatory notes:

"314. It has been suggested that the duty to promote the success of the company may also be modified by an obligation to have regard to the interests of creditors as the company nears insolvency. Subsection (3) will leave the law to develop in this area."[50]

Lord Hodge's conclusion (with which Lords Briggs and Kitchin agreed) was:

"...the relevant background shows that the Government in introducing the Bill considered that it was preserving the then current legal position and, more significantly, that Parliament itself explained both that section 172(3) was a recognition that the section 172(1) duty is displaced on insolvency (para 313) and that the subsection allowed the common law to be developed by modifying the section 172(1) duty when a company nears insolvency..."[51]

Lady Arden's analysis of the history of the duty, and of the effect of section 172, is a minority view. Lords Reed, Briggs, Kitchin and Hodge all disagree with her. Lady Arden's commentary tilts at the proposition that there is a direct duty to creditors, but that was not how it had been articulated in *West Mercia* or in any of the subsequent cases. Lady Arden is also in a minority in saying that:

"What is said is that West Mercia brought into UK law principles about the duties of directors of insolvent companies which had been developed in the Antipodes, and so I will begin by considering the law from that source before I consider West Mercia. In my judgment, West Mercia only approves a limited part of the Antipodean approach."

It is respectfully suggested that this is to construe Dillon LJ's words in *West Mercia* as if it was a statute; whereas what Dillon LJ was really doing was applying the rationale of the antipodean authorities.

Lady Arden also highlighted that the other members of the *Permakraft* court had been reluctant to recognise a 'creditor duty' of any kind: *"If this Court is to move in that direction its decision to do so would need to be based on a thorough examination of the scheme and purpose of the companies' legislation. I prefer to leave that for a case where this question, itself a difficult amalgam of principle, policy, precedent and pragmatism, must be decided."*[52]

She then pointed out that Street CJ had hesitated: *"to attempt to formulate a general test of the degree of financial instability which would impose upon directors an obligation to consider the interests of creditors," citing the courts' traditional and proper caution about pronouncing on the commercial justification for a directors' decision (p 733).*

Lady Arden's analysis appears to have put more weight on the views held by members of the CLRSG (including those of the late and great Richard Sykes QC) than the language of section 172(3) itself and the decided cases. The thrust of Lady Arden's judgment is that *West Mercia* did not add to the pre-existing law on directors' fiduciary duties:

47. *Sequana (SC)* at [209].
48. *Sequana (SC)* at [210].
49. *Sequana (SC)* at [220].
50. Quoted by Lord Hodge in *Sequana (SC)* at [314].
51. *Sequana (SC)* at [222].
52. *Per* Richardson J and Somers J in *Permakraft* at 255, cited in *Sequana (SC)* at [393].

"Rightly or wrongly the view held at the time was that there was doubt as to the existence of the Rule in West Mercia."[53]

This is somewhat surprising given how radical the idea recognised in *Kinsela* and later in *West Mercia* was and, as Lord Hodge and Lord Briggs point out, that wasn't the view of Parliament. As the other Justices seem to have recognised in their survey, section 172(3) recognised the rule in *West Mercia*, which has now come of age.

F. Concluding Thoughts

Lord Reed recognised the practical need for clarity in this area of the law.[54] What, then, did the Supreme Court decide?

The Justices unanimously decided that a real rather than a remote risk of insolvency was not enough to trigger the rule in *West Mercia*, but the rule definitely exists and could apply in relation to a dividend otherwise lawfully made, just as Rose J and the Court of Appeal had previously decided.

Where the Supreme Court differed from the Court of Appeal was in rejecting the probability of insolvency as the trigger altogether, reverting instead (by a majority of four) to language requiring insolvency to be **imminent**, with the probability of insolvent liquidation or administration as an alternative, and (by a majority of three) that the directors know or ought to know that the company is in this position.

Such "imminent" language had previously been considered vague, and so it is. In circumstances where the enquiry must inevitably be fact specific, however, the Supreme Court must be taken to be satisfied that such language adequately conveys the general requirement – at least for the moment. Strictly speaking, the point may be open for further argument in a case on the facts of which the question actually falls to be determined.

In the meantime, directors must look to see whether there is "light at the end of the tunnel" and, if so, how bright it is, or whether insolvency is "just around the corner", taking some comfort, perhaps, from the Supreme Court's clear view that merely transitory insolvency doesn't count.

Having recognised the interplay between the rule in *West Mercia* and the ratification principle, and that the two cannot operate simultaneously, they can and must continue to adapt to each other on a principled basis. That's for another day.

Finally, how are directors to act when the rule in *West Mercia* is triggered? The guidance from the Supreme Court is that the weight to be attached to creditors' interests will depend on the circumstances of the case. But *Sequana* neither called for any deeper analysis of what might be expected of directors and, unsurprisingly, nor do the judgments provide one.

That too must wait for another day. ■

53. *Sequana (SC)* at [440].
54. *Sequana (SC)* at [87].

Diary Dates

South Square members will be attending, speaking and/or chairing the following events

22 – 24 February 2023

Fire Starters Global Summit

Conrad Hotel, Dublin, Ireland

16 & 17 March 2023

C5 Fraud Asset Tracing and Recovering Conference

Fairmont Grand Hotel, Geneva, Switzerland

21 April 2023

ILA Annual Conference

Linklaters, One Silk Street, London

17 – 19 May 2023

Thought Leaders 4: FIRE International

Anantara Hotel, Vilamoura, Portugal

Early June 2023

Moss Fletcher Lecture

The Pension Room, Gray's Inn, London. Further details to follow



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The Interests of Creditors in the Zone of Insolvency

Introduction

The long-awaited decision of the United Kingdom Supreme Court in *BTI v Sequana SA*[1] has generated renewed interest in corporate governance in an insolvency context, and the extent to which a best practice insolvency system can achieve an appropriate balance between creditor protection and managerial risk-taking. *Sequana* is the first occasion on which the United Kingdom's highest court has pronounced upon the nature and scope of creditors' interests as an incident of the duty of directors' to act in the best interests of the company.

Sequana is not a single judgment, but multiple judgments containing slightly different formulations. While some things are now clear beyond doubt, others are perhaps less clear than they were.

As a result, while the Court has now provided various different versions of the test to apply when the interests of creditors become material and suggesting what directors need to do to avoid breaching their duties in an insolvency context, considerable uncertainty remains for directors. Moreover, it is one thing to know what the 'test is' (or, perhaps, 'tests are'), but another thing to be able to assess, as a matter of commercial practice and without the benefit of the hindsight applied by a court, where a company sits on a sliding scale of insolvency in ever-changing economic circumstances, such as those that the world is currently facing.

Further, the expectation for directors accurately to weigh competing insolvency outcomes and to determine the probabilities of risks and returns across different creditor classes, especially in a corporate group context, might be said to be approaching the impossible. The risk is that directors' managerial prerogative is minimised, with the prospect of personal liability having a significant deterrent impact on directors' willingness to pursue a restructuring attempt that, inherently, has no guarantee of success.

This article examines these issues by way of a cross-jurisdictional analysis in the United Kingdom and Australia. It begins by outlining the approach to creditors' interests in an insolvency context in *Sequana* and the leading Australian authorities, before assessing the creditor protection/risk-taking balance and the impact on corporate restructuring.

The question that is posed in this article is whether, while the creditor protection objective is an important part of insolvency policy, it might be argued that it is better met by other actions conferred by insolvency law, such as voidable

transactions provisions and liability for insolvent and wrongful trading.

United Kingdom

In the United Kingdom, directors are required by section 172(1) of the Companies Act 2006 (UK) to act in a way which they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole. This is a codification of the corresponding equitable duty that directors have, as fiduciaries, to act in the best interests of the company.

The brief facts in *Sequana* were that the directors of a limited company, AWA, caused AWA to distribute a dividend of EUR 135 million to its sole shareholder, Sequana SA, in May 2009. When the dividend was paid, AWA also had a contingent liability relating to environmental clean-up costs for pollution. The value of the contingent liability was uncertain but it gave rise to a real risk of insolvency at some future point in time. The clean-up costs were later quantified as being significantly higher than first estimated, and AWA became insolvent 10 years after payment of the dividend. Proceedings were commenced, alleging the directors had breached their duty to consider the interests of creditors of AWA by paying the dividend notwithstanding the existence of the contingent liability and the risk of insolvency. This argument was rejected at first instance, and the decision was appealed to the Court of Appeal.

In the Court of Appeal, David Richards LJ (as he then was) held, with Longmore and Henderson LJJ agreeing, that while directors may at certain times be required to have regard to the interests of creditors as an incident of their duty to act in the best interests of the company, the interests of creditors are invoked not merely when there is a 'realistic prospect of insolvency', but rather when directors know or should know the company is or is likely to become insolvent. A risk of insolvency in the future, however real, was said to be insufficient unless it amounts to a 'probability'. However, the Court of Appeal made it clear that where the trigger point had been reached, the duty was owed entirely to the creditors.

In the factual circumstances, while at the time the dividend was paid there was a real prospect of future insolvency, AWA was not likely to become insolvent. This meant the requirement to take into account the interests of creditors was not engaged, and so the directors could not have breached their duties.

On appeal to the Supreme Court, Lord Reed (with Lord Hodge, Lord Briggs, Lady Arden and Lord Kitchin agreeing on the conclusion, although each writing separate, differing judgments) held that directors do not owe any separate duty to act in the best interests of creditors. Rather, the statutory and fiduciary duty remains to act in good faith in the best interests of the company, and 'there are circumstances in which the interests of the company' for the purpose of that duty 'should be understood as including the interests of the company's creditors as a whole'.[2]

According to Lord Reed:

"So long as a company is financially stable and is therefore able to pay its creditors in a timely manner, the interests of its shareholders as a whole ... can be treated as the company's interests for the purposes of the directors' duty to act in its interests. It is the shareholders whose interests are affected by fluc tuations in its profits and reserves, as they are the persons entitled to share in its distributions and its surplus assets ... [T]he creditors' interests do not require to be considered as a discrete aspect of the company's interests for the purposes of the directors' fiduciary duty to the company. It is sufficient for the directors to promote the interests of the shareholders in order for the company's business to be carried on over the long term and for the company's debts to be paid as part of the conduct of its business."[3]

However, the situation changes when the company is 'insolvent or bordering on insolvency'. In this case:

"As losses are incurred, and the company's surplus of assets over liabilities disappears, the company's creditors as a whole become persons with a distinct interest (possibly, depending on the gravity of the company's financial difficulties) in its affairs, as they are dependent on its residual assets, or on the possibility of a turnaround in its fortunes, for repayment."[4]

Lord Reed referred to the traditional view that creditors are 'responsible for the protection of their own interests', which 'casts upon creditors the risk of the company's failure'.[5] This is based on the underlying concepts of limited liability and the separate legal personality of the company, as well as 'the fact that the relationship between creditors and the company is usually contractual',[6] so that creditors 'can be expected to be the guardians of their own interests'.

However, Lord Reed observed that both company law and insolvency law have always recognised that creditors should not be 'bereft of legal protection' and:

"Acceptance of the need for limited liability to encourage entrepreneurial activity does not in itself justify the view that, even when a company is insolvent or in the vicinity of insolvency, the directors' duty to act in the interests of the company requires them to act solely in the interests of its shareholders."[7]

According to Lord Reed: *"To treat the company's interests as equivalent to the shareholders' interests in that situation encourages the taking of commercial*

1. [2022] UKSC 25.
2. Ibid, [11].
3. Ibid, [47].
4. Ibid, [48].
5. Ibid, [52].
6. Ibid.
7. Ibid, [53].

risks which are borne primarily not by the shareholders but by the creditors, who will recover less in a winding up if the company's assets have been diminished or if it has taken on additional liabilities. In economic terms, treating the company's interests as equivalent to the shareholders' interests in a situation of insolvency or near-insolvency results in the externalisation of risk: losses resulting from risk-taking are borne wholly or mainly by third parties."[8]

It follows that where directors are under a duty to act in good faith in the interests of the creditors, the shareholders cannot authorise or ratify a transaction which is in breach of that duty. The Court was unanimous in reaching this conclusion.

In terms of precisely when the interests of creditors are relevant, the Supreme Court held that a 'real risk' of insolvency is insufficient. That is because a real risk of insolvency 'is at one very large remove' and is 'simply too remote from the event which turns a creditor's prospective entitlement into an actual one'. Indeed, a real, but not probable, risk means that insolvency 'is by definition unlikely, and insolvent liquidation may only be a remote possibility'.[9] Rather, the need to take into account creditors' interests is invoked when directors know, or ought to know, that the company is insolvent or facing imminent insolvency, or that an insolvent liquidation or administration is probable.[10]

This timing issue meant that the requirement to take into account the interests of creditors was not invoked on the facts, and this was sufficient to reject the appeal. Nevertheless, by way of *obiter* comments, the Supreme Court elected to provide further guidance on what the duty to take into account the interests of creditors actually requires from directors in practice.

Lord Reed suggested that a careful balancing exercise is involved:

"Where the company is insolvent or bordering on insolvency but is not faced with an inevitable insolvent liquidation or administration, the directors' fiduciary duty to act in the company's interests has to reflect the fact that both the shareholders and the creditors have an interest in the company's affairs. In those circumstances, the directors should have regard to the interests of the company's general body of creditors, as well as to the interests of the general body of shareholders, and act accordingly. Where their interests are in conflict, a balancing exercise will be necessary…"

"[I]t can I think be said as a general rule that the more parlous the state of the company, the more the interests of the creditors will predominate, and the greater the weight which should therefore be given to their interests as against those of the shareholders. That is most clearly the position where an insolvent liquidation or administration is inevitable, and the shareholders consequently cease to retain any valuable interest in the company."[11]

In other words, there was a sliding scale where the interests of the creditors became more important, the closer that the company comes to insolvency. An otherwise lawful dividend (if made in accordance with the requirements of the Companies Act 2006 (UK)) could be made in breach of duty if the trigger point has occurred and the company's directors failed to act in accordance with their duties. However, Sequana was not such a case.

The Supreme Court did not express any conclusion as to whether the directors should be judged on whether they knew (or ought to have known) that the trigger point had been reached. This is a point that has been left open for submissions and consideration in future cases.

Finally, there was unanimity between all members of the Court that there is no conflict between the creditor duty and the prohibition against wrongful trading in section 214 of the Insolvency Act 1986 (UK).[12]

If matters had ended here, at least the test would have been clear(ish). But there are some notable differences in the judgments which, to put it at its lowest, make the position rather less clear.

Lord Briggs (with whom Lord Kitchen agreed) stated that the relevant duty would be engaged when insolvency is 'imminent' (i.e. 'just around the corner and going to happen') or when an insolvent liquidation or administration is 'probable'.[13] In contrast, Lord Hodge held that it was 'at or near the onset of insolvency'[14] or when the company is 'bordering on insolvency'.15 As we have already seen, Lord Reed considered it was when the company is 'insolvent or bordering on insolvency, or that an insolvent liquidation or administration is probable',[16] a formulation with which Lady Arden agreed, although she also added that it should also apply where 'the directors plan to enter into a transaction in question would place the company in one of those situations'.[17] There are circumstances where these different formulations will lead to different conclusions.

What about knowledge? The majority held that a director's knowledge or constructive knowledge (i.e. what they 'ought to know') was relevant to the onset of the duty. However, Lord Reed and Lady Arden left the question open.[18] As noted below, Lady Arden commented that because the progress towards insolvency may not be linear directors should stay informed of the company's financial position.[19]

What about the balancing exercise? Lord Briggs put the balancing exercise this way:

"Much will depend upon the brightness or otherwise of the light at the end of the tunnel; i.e. upon what

8. Ibid, [59].
9. Ibid, [193].
10. Ibid, [203].
11. Ibid, [81].
12. Ibid, [94], [97], [99], [122], [238], and [325].
13. Ibid, [203].
14. Ibid, [231].
15. Ibid, [238].
16. Ibid, [12].
17. Ibid, [279].
18. Ibid, [90] and [281].
19. Ibid, [303]-[304].

the directors reasonably regard as the degree of likelihood that a proposed course of action will lead the company away from threatened insolvency, or back out of actual insolvency. It may depend upon a realistic appreciation of who, as between creditors and shareholders, then have the most skin in the game; i.e. who risks the greatest damage if the proposed course of action does not succeed."[20]

In Lord Briggs' judgment, this happens at the point that section 214 of the 1986 Act also becomes engaged.[21] No other judge expressed a view as to whether this is correct. In any event, it could be said that the tunnel becomes rather dark when the outcome directors are being called on to assess may expose them to significant personal liability for their actions. Directors are required to assess a factual circumstance that is inherently fluctuating and changing.

As Lady Arden stated:

"The progress towards insolvency may not be linear and may occur not as a result of incremental developments but as a result of something outside the company which has a sudden and major impact on it."[22]

Where a company sits, on a sliding scale, particularly the 'bordering on insolvency' stage expressed as a critical marker by Lord Reed, will be difficult to estimate with precision. And yet so much depends on this answer – not only the extent to which the respective interests of shareholders and creditors are relevant, but just how relevant they are.

Even if a director is able accurately to pinpoint the company's financial condition on the sliding scale, they then face the further difficult task of determining multiple scenarios for shareholders and different sets of creditors, the likely return from each course of action, and the likely success (in terms of the impact on the prospects of company) of each course of action.

And even when the company is 'irretrievably insolvent', so that shareholders cease to retain any valuable interest in the company, directors face the unenviable task of needing to balance the competing interests of multiple creditor groups. This difficulty is captured in Lord Reed's comments that:

"...individual creditors may be in different positions, and may even have conflicting interests: that may be the position, for example, of secured creditors as compared with unsecured creditors. Secondly, the interests of the company cannot be confined to the interests of current creditors as at the time of a given decision by the directors, any more than they can be confined to the interests of current shareholders ... [T]he identities of the company's creditors constantly change so long as debts continue to be incurred and discharged."[23]

These observations do not provide much comfort to directors, and the fact they are obiter (with different interpretations possible in later cases) might be said to muddy the waters even more.

Australia

As in the United Kingdom, in Australia directors have a statutory duty under section 181(1)(a) of the *Corporations Act 2001* (Cth) to act in good faith in the best interests of the company, which corresponds with the same fiduciary duty recognised in equitable jurisprudence.

Australian courts have, in a long line of cases since the 1970s, held that the identity of the 'company' corresponds with the interests of creditors when the company is in financial difficulty. The exact time the interests of creditors are invoked has been variously expressed, ranging from when there is a 'real and not remote risk of insolvency',[24] or the company is operating in an 'insolvency context',[25] is facing 'financial instability',[26] or is 'insolvent or nearing insolvency'.[27] However, little elaboration has been provided.

The leading Australian authority which has dealt with directors' duties in an insolvency context and the scope of the obligation to creditors is *The Bell Group Ltd (in liq) v Westpac Banking Corporation (No 9)*.[28]

In that case, the Bell Group consisted of various Australian and United Kingdom subsidiaries with common directors. The initial operations of the Bell Group were financed by unsecured loans from six Australian banks and a non-Australian syndicate of 14 banks.

20. Ibid, [176].
21. Ibid, [176].
22. Ibid, [303].
23. Ibid, [48].
24. *Kalls Enterprises Pty Ltd (in liq) v Baloglow* (2007) 63 ACSR 557.
25. *Kinsela v Russell Kinsela Pty Ltd (in liq)* (1986) 4 NSWLR 722.
26. *Linton v Telnet Pty Ltd* (1990) 30 ACSR 465.
27. *New World Alliance Pty Ltd, Re; Sycotex Pty Ltd v Baseler* (1994) 51 FCR 425.
28. (2008) 70 ACSR 1.

Upon encountering financial difficulty, the existing bank loans were refinanced, so that the banks, among other things, took security over all significant assets of the Bell Group and obtained new guarantees from most subsidiaries, thereby obtaining priority over all existing and future creditors. Although the repayment dates for the loans were extended, the banks offered no new finance as part of this arrangement. After the refinancing, the financial position of the Bell Group worsened and liquidators and receivers were appointed to each company. The banks realised their securities and recovered AUD $282 million. In 1995, liquidators commenced proceedings against the banks and the Bell Group directors challenging the refinancing transactions. The action against the directors was discontinued at an early stage and the liquidators elected to continue solely against the asset-rich banks. However, it remained necessary to determine whether the directors breached their duties to the various subsidiary companies, as a positive answer was required to invoke *Barnes v Addy*[29] accessorial liability for the banks.

At first instance, Owen J held that, in approving the refinancing, the directors did breach their duties to the companies. At the time of the refinancing, the Bell Group companies were facing 'insurmountable endemic illiquidity' and imminent insolvency,[30] and this meant the interests of creditors corresponded with the identity of each subsidiary company that was indebted to them. The effect of the refinancing was that the subsidiaries had no additional working capital to meet their obligations and any future proceeds from the sale of assets would pass directly to the banks.[31] Also, in agreeing to the refinancing, the directors removed any prospect that the existing non-bank creditors of the companies could compete with the claims of the banks (who became secured following the refinancing) in the event of insolvency. The breach was said to be 'egregious' because the directors failed to make any enquiries to protect the interests of non-bank creditors of the companies.

Owen J held that directors do not owe any independent duty to creditors. However, the duty to act in the best interests of the company requires directors to take into account the interests of creditors when the company is operating in an 'insolvency context'.

According to Owen J, in assessing what is an 'insolvency context':

"A financial state short of actual solvency could be sufficient to trigger the obligation to take into account the interests of creditors ... Adversity might strike short of actual insolvency and might propel the company towards an insolvency administration. And that is where the interests of creditors come to the fore."[32]

While acknowledging the difficulty for directors in assessing the exact point at which the interests of creditors are invoked, Owen J said:

"I am not convinced that the consideration of other financial states, short of actual insolvency, as a practical test of directors' actions would necessarily cross the line from difficult to impossible... Judgesare paid to make difficult decisions. So too are company directors."[33]

Owen J's analysis in relation to the duty of directors to act in the best interests of the company was endorsed on appeal in *Westpac Banking Corporation v The Bell Group Ltd (in liq) (No 3)*.[34] In assessing when the interests of creditors correspond with the interests of the company, Drummond AJA said:

"I would prefer to say that if the circumstances of the particular case are such that there is a real risk that the creditors of a company in an insolvency context would suffer significant prejudice if the directors undertook a certain course of action, that is sufficient to show that the contemplated course of action is not in the interests of the company."[35]

Drummond AJA noted that the requirement to take into account the interests of creditors was a significant departure from earlier judicial attitudes

29. (1874) 144 ER 643.
30. Ibid, [1949].
31. Ibid, [992].
32. Ibid, [4445].
33. Ibid, [4449]-[4450].
34. (2012) 89 ACSR 1.
35. Ibid, [2046].

which left corporate decision-making largely to management.[36] However, this was said to be justified because:

"The impacts of corporate decision-making on a wider range of interests than shareholders are now being given more recognition. The need to ensure protection of those interests also I think serves to explain why modern company courts have become more interventionist, in reviewing the activities of directors than was traditionally the case."[37]

The only other decision since Bell which has considered in detail the nature of the interests of creditors as an aspect of directors' duty to act in the best interests of the company is *Termite Resources NL (in liq) v Meadows, Re Termite Resources NL (in liq) (No 2)*.[38] In that case, a claim was brought against the directors of Termite, a mining company. Termite was wholly owned by Outback Iron, itself owned by IMX Resources and Taifeng Yuanchuang International Development. The mining operations of Termite were funded by unsecured loans from IMX and Taifeng to Outback Iron, which then on-lent the funds to Termite.

After IMX encountered financial difficulty, its directors caused Termite to adopt and implement a distribution policy by which, subject to the retention of a reserve of AUD $3 million, all the surplus mining proceeds had to be distributed to IMX and Taifeng. The price of iron ore rapidly declined and the reserve of AUD $3 million was insufficient to pay Termite's liabilities.

Termite went into voluntary administration and then liquidation. It was held that the AUD $3 million reserve under the distribution policy was inadequate and that a reserve of at least AUD $10 million was needed for Termite to survive given the volatile iron ore market. White J in the Federal Court of Australia held that Termite's directors breached their duty to act in the best interests of the company, which had clearly been in a situation of doubtful solvency that invoked the interests of creditors.

The directors had, on the facts, preferred the interests of IMX and Taifeng to Taifeng's collective creditors. There was no analysis by management concerning the sufficiency of a reserve of AUD $3 million, taking into account the foreseeable changes in iron ore prices and their implications for the company's working capital.

White J held that the interests of creditors are invoked in circumstances broader than when the company is 'nearing insolvency' or of 'doubtful solvency'. It is not required for the actions of directors to be likely, on the balance of probabilities, to lead to the insolvency of the company. Rather, the interests of creditors are invoked simply when there is a 'real and not remote risk of insolvency' and when the 'objective circumstances require' consideration of the interest of creditors.[39]

This answers the question left open in *Sequana* as to whether the interests of creditors are invoked only when directors know or ought to know that the company is insolvent or facing imminent

36. Ibid, [2049].
37. Ibid, [2051].
38. (2019) 370 ALR 191.
39. Ibid, [209].

insolvency, or that an insolvent liquidation or administration is probable. Such knowledge is not required in Australia.

In terms of what directors are required to do to ensure they sufficiently take into account the interests of creditors, White J cited with approval academic commentary that:

"In summary, what directors must do to satisfy their obligation to consider the interests of creditors will vary according to the context. The steps required to be taken by directors will depend upon a number of factors, and these factors will vary from company to company. The factors will include the financial situation of a company (the closer the company is to insolvency, then the greater the weight that should be given by directors to the interests of creditors); the number of creditors the company has; the types of creditors the company has and the amount owed to each creditor; whether the company is part of a corporate group (the existence of a corporate group in the Bell Group litigation meant the directors faced a more complex task in relation to considering the interests of creditors); and the potential impact of any contemplated transactions being considered by the directors on the creditors."[40]

Analysis – The scope of director liability and the impact on corporate rescue

The current jurisprudence on when directors are required to take into account the interests of creditors in discharging their duty to act in the best interests of the company, and what is required of them in doing so, therefore might be said to raise more questions than answers. The delicate balancing exercise that directors must undertake, with reference to rapidly changing financial and economic conditions and a multitude of competing stakeholder interests, places them in a very difficult position in practice, and this may lead to a significant deterrent impact on the willingness of directors to pursue a corporate restructuring.

It is a hard task for directors to determine when a company is in fact insolvent to begin with, particularly in the current economic circumstances which see various levels of government support and loan and rental deferrals and fluctuating market expectations and financial forecasts by the day due to uncertainties in supply chains, levels of demand from customers, energy prices, and interlinked downside economic risks. There are also the uncertainties of an economy in transition, and how to quantify climate risk exposure based on principles yet to be settled by regulators domestically and internationally.

In light of that overarching difficulty, for directors to be expected to understand and apply a 'sliding scale' to assess when a company faces a 'real but not remote risk' of insolvency, or is more likely than not to be insolvent, or is sitting in a more generalised 'zone of insolvency', is necessarily also subject to imprecision and the potential for genuine, well-meaning error. If a claim for breach of duty is commenced against a director, the time at which the requirement to take into account the interests of creditors is invoked should not be, but will perhaps inevitably be judged, to some extent, with the benefit of hindsight.

Perhaps the argument put by the banks in *Bell* at first instance has even more resonance in today's economy:

"Directors do not have the opportunity in which to determine and categorise a series of variables in the financial position of the company at any given time. In the everyday world of commerce, companies' fortunes commonly fluctuate in a significant and rapid way. It is one thing to impose an obligation where a director forms a belief that a company is insolvent. It is quite another thing to impose an obligation where the company is in a financial state that is less than commercially desirable but does not amount to insolvency."[41]

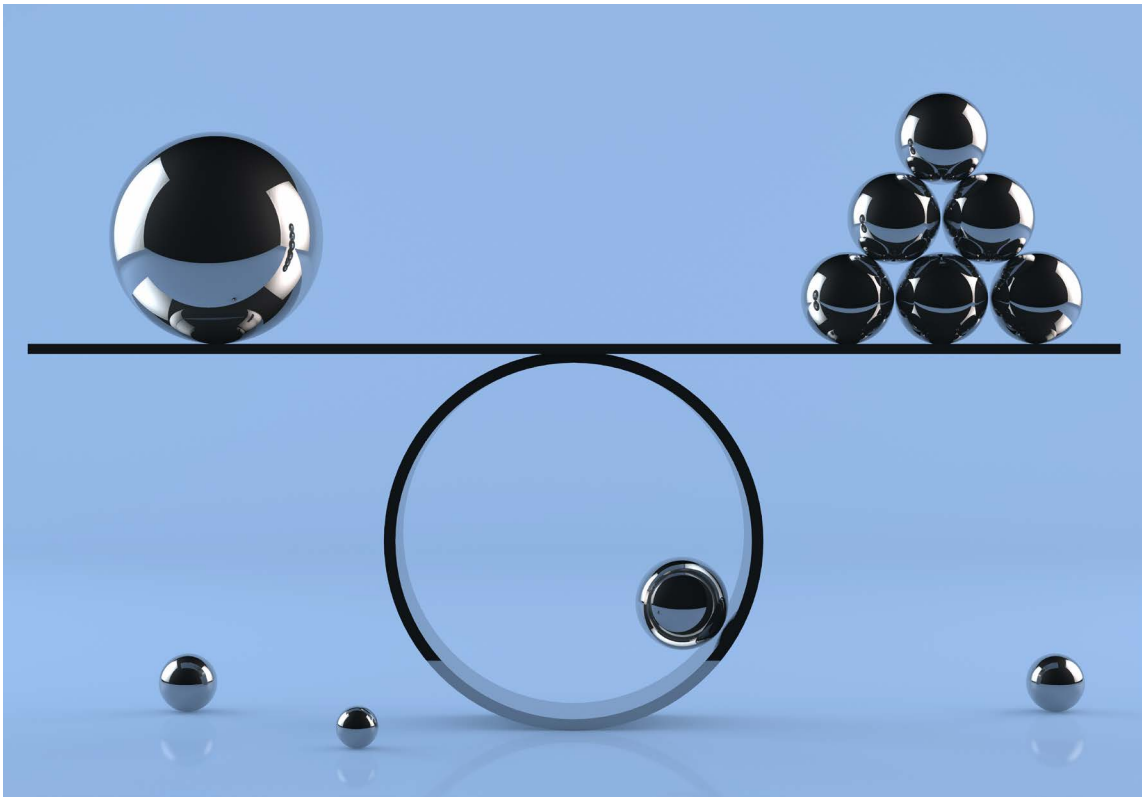
The recent decisions in the United Kingdom and Australia do not offer comfort or clarity to directors on precisely what needs to be done in fact to balance the interests of shareholders and creditors, and the interests of different sets of creditors, when the company is at various stages along the 'insolvency curve'.

The prospect of a workout attempt, whether informal or via formal reorganisation processes, offers no guarantees of success. But if it is successful, a workout will enhance returns for all creditors, and the collective benefit of all creditors aligns with a fundamental intention of insolvency law. The decision on whether to pursue a rescue attempt for a financially-distressed company involves a strong degree of business judgment – based on relationships with creditors, the context and history of the business, and an assessment of future prospects. In determining a breach of duty based on hindsight, arguably the risk-taking prerogative of directors is displaced.

Directors are effectively required to place percentage values on the likelihood of a rescue attempt succeeding, compared to other insolvency alternatives, and to also estimate a range of expected returns in a multitude of scenarios, the outcome of which rapidly changes by the day in a volatile economy. This becomes somewhat onerous especially in a corporate group situation. At first instance in *Bell*, Owen J held that the directors were required to take into account the interests of 'direct and indirect creditors of individual Bell Group companies'[42] and, in a group situation such as this, the duty:

"demanded a tracing exercise to ascertain the effect on creditors of [the refinancing transactions]. In this respect 'creditors' includes indirect creditors, that is, creditors of debtor companies and debtors of creditor companies

40. Ibid, [208].
41. (2008) 70 ACSR 1, [4446].
42. Ibid, [9743].



within the group ... The directors did not do that tracing exercise. They did not ascertain the extent of external creditors of individual companies and nor did they consider how those creditors would be affected by what was proposed."[43]

This tracing exercise across potentially thousands of creditors in different jurisdictions is an exercise of immense complexity – and ultimately requires a significant element of commercial judgment and an element of risk-taking. Yet that judgment call is not reflected in an express defence to personal liability for directors specifically in an insolvency context such as this, although the normal 'honest and reasonable' defence will no doubt be raised by directors in these circumstances.

While creditor protection is a legitimate and important policy objective of insolvency law, a careful balance is required between creditor protection and commercial realities which necessitate the exercise of risk taking. One might ask whether the creditor protection objective is already sufficiently met through other core provisions of an insolvency regime – voidable transaction provisions enabling the recovery of uncommercial transactions and unfair preferences, as well as insolvent and wrongful trading provisions.

If those provisions were left to operate – without also imposing a duty for directors to act in the best interests of creditors as the relevant identity of the 'company' in an insolvency context – then the decision to pursue a restructuring attempt might be able to be left as a commercial judgment for directors, subject to a lack of good faith or preferential treatment for particular groups of stakeholders.

Such an alternative formulation of directors' duties could strike a better balance and increase the incidence of corporate rescue for viable entities, at a time when it is very much needed (given the current economic climate) to ensure economic and financial stability, and to preserve jobs, livelihoods and communities. Indeed, the creation of incentives to enhance the incidence of corporate restructuring has been called for by the World Bank[44] and the International Monetary Fund[45] as a way to navigate the economic difficulties the world is now facing.

Alternatively, the common law duties might play a valuable role in covering circumstances where a company does not enter insolvency, but where there is nevertheless a loss caused by its actions when it was in a perilous time, or for other areas where insolvency actions are not available.

Is the purpose of the common law duties to encourage directors to consider the financial position, and to act with care and caution?

It is hoped that this article will serve as a conversation starter in assessing the complexity of corporate governance in an insolvency context, and considering how to strike the right balance to incentivise restructuring outcomes for viable entities, where restructuring outcomes are likely ultimately to be in the best interests of creditors, the broader community, and the economy.■

43. Ibid, [6064].
44. World Bank, *Finance for an Equitable Recovery* (2022), Chapter 3: Restructuring Firm and Household Debt.
45. International Monetary Fund, *Policy Options for Supporting and Restructuring Firms Hit by the COVID-19 Crisis* (2022).

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Restructuring Repackaged in the Cayman Islands

A new restructuring regime known as the Restructuring Officers Proceeding or Restructuring Moratorium Proceeding has been in force in the Cayman Islands since 31 August 2022. There is much continuity with the past in terms of substantive law, but the statutory scheme has important changes to procedural law. Officeholders may also have increased flexibility in using differences between jurisdictions, in order to achieve a successful outcome.

Sections 91A to 91J of the Companies Act (2022 Revision) establish the new regime, and court rules have been introduced as Order 1A of the Companies Winding Up Rules. In broad outline:

- A company may petition for the appointment of Restructuring Officers ("RO", "RO Petition"), who are officers of the Court;
- The only ground is that the company (a) is or is likely to become unable to pay its debts, and (b) intends to present a compromise or arrangement to its creditors;
- It may be intended for the compromise or arrangement to be presented by way of scheme of arrangement under Cayman Islands law, or pursuant to a foreign law, or by way of consensual restructuring;
- Unless otherwise directed, the RO Petition will be heard within 21 days of filing, having been advertised not more than 7 business days after filing and not less than 7 business days before hearing;
- ROs may be appointed on an interim basis, on an ex parte application by the company, prior to the hearing of the RO Petition;
- On the RO Petition being filed at Court, an automatic and worldwide stay prevents the commencement or continuation of claims or proceedings against the company or the presentation of a winding up petition against the company, without leave of the Court; and
- Secured creditors may enforce their security without leave of the Court, notwithstanding the RO Petition or the appointment of ROs.

ROs by any other name

One of the key reasons behind the legislative reform was to decouple both the language and the process from any form of liquidation.

Prior to the reform, a moratorium would arise only if provisional liquidators were appointed on a restructuring mandate, following the presentation of a winding up petition. Clients were reluctant to file and advertise a winding up petition seeking an order that the company be wound up, with a view to seeking the appointment of liquidators who (if appointed) could shepherd the debtor through a restructuring. The words 'winding up', 'provisional liquidation', and 'provisional liquidators' had the ring of the chophouse.

In addition, there was always a risk that the Court refused to appoint provisional liquidators and instead heard the winding up petition which, once advertised, could not be withdrawn without leave. Even if provisional liquidators were appointed, the hearing of the winding up petition was merely adjourned, pending discharge of the officheolders, with the result that the debtor's fate continued to hang in the balance until a compromise was approved by the Court.

Restructuring in the Cayman Islands now has a standalone proceeding and does not need the wrapper of a provisional liquidation in order to stay creditor action against the debtor. No winding up petition is filed. The originating process is a petition filed under section 91B of the Companies Act, seeking the appointment of ROs. Only qualified insolvency practitioners can be appointed as ROs, who are officers of the Court, so the same individuals will take appointments as ROs who might have been appointed as restructuring provisional liquidators.

If the RO Petition is dismissed, the Court is not automatically tasked with hearing a winding up petition in default of appointing the ROs. In reality, if a creditor opposes the appointment of ROs and prevails, it likely will have been on the basis that the company is irretrievably insolvent and that a winding up order should be made instead. In order to obtain a winding up order, however, the creditor would need to present its own winding up petition – and can do so only with leave of the Court, if an RO Petition has already been presented.

Easier for Debtor to File

A second impulse for legislative reform was the procedural difficulty that companies previously faced, when seeking to restructure debt with the benefit of a moratorium, which required the filing of a winding up petition.

Unlike in England, the rule in Re Emmadart [1979] Ch 540 had not been cured by statute in the Cayman Islands. A Board of Directors could not resolve to file a winding up petition, unless authorized expressly by (i) the company's Articles of Association or (ii) special resolution.

When those options were not available, a practice had developed whereby the company would find a 'friendly creditor' to present a winding up petition, only so that the company could then make its application for the appointment of restructuring provisional liquidators. That never had a proper basis in rules of court, since a company's application for the appointment of restructuring provisional liquidators expressly could be made only on the company's own petition (Order 4 rules 1 and 6 of the Companies Winding Up Rules).

Under the new regime, the company is the only legal person entitled to file an RO Petition. Section 91B(2) also makes clear that the petition may be presented by the debtor company, acting by its directors, without a resolution of its members or an express power under its Articles of Association.

Section 91B(1) provides that the RO Petition must be presented by the company on the ground that:

"(a) The company is or is likely to become unable to pay its debts within the meaning of section 93; and (b) Intends to present a compromise or arrangement to its creditor (or classes thereof) either, pursuant to this Act, the law of a foreign country or by way of a consensual restructuring"

Sub-section (1)(b) contemplates not only a court-supervised restructuring under Cayman Islands law, using schemes of arrangement, but also situations in which the proceeding in the Cayman Islands is ancillary: the restructuring may be proposed under the laws of a foreign country or may require no court approval at all (i.e. a consensual restructuring).

If ancillary, the main benefit of the Cayman Islands proceeding is likely to be the automatic stay.

Earlier Automatic Stay with Extraterritorial Scope

On filing the RO Petition, an automatic stay arises under Section 91G. The stay prevents the commencement or continuation of suits, actions or other proceedings against the company. It also prevents any person from presenting a petition against the company for its winding up, without leave of the Court.

As a matter of Cayman Islands law, the stay has extraterritorial effect. That will prevent, for example, investment funds incorporated or registered in the Cayman Islands from taking enforcement action in foreign jurisdictions. It remains to be seen how foreign courts approach the extraterritoriality of the stay, with respect to claimants or applicants that are not resident or domiciled in the Cayman Islands.

These features are a departure from the law as it previously stood. A stay would arise only once a Court had made an order appointing restructuring provisional liquidators, which left a company vulnerable to enforcement action between filing and the hearing of an appointment application. The stay was also not expressed to be extraterritorial before, but few Cayman Islands companies and partnerships likely chose to bring proceedings abroad under the old regime, given the Cayman Court's personal jurisdiction over them.

Depending on whether a proceeding is a restructuring or a winding up, the automatic stay on claims against the company will be different. If a winding up petition is presented against a company, it remains the case that no stay arises until a winding up order is made; and it is not expressed to be extraterritorial.

The Cayman Court will be careful to prevent abuse. If a creditor presents a winding up petition, a company might choose to file an RO Petition in order to stay the winding up proceeding – at least temporarily.

Cross-Jurisdictional Possibilities

The statute expressly refers to the possibility of an RO Petition being filed in the Cayman Islands in support of restructuring efforts intended to be promoted in a foreign proceeding.

Officeholders may therefore take advantage of certain features of other regimes, such as a Chapter 11, with a reduced risk of satellite litigation on forum. This is a welcome development because jurisdictions have distinct tools which may be used in combination. Different treatment of creditors across jurisdictions can also afford leverage in negotiation with stakeholders.

Distinct Tools

The success of a restructuring may depend on or benefit from seeking to avoid or subordinate a secured creditor's claim. That may be capable of being achieved in an adverse proceeding filed within a Chapter 11 which pleads, amongst other things, 11 USC §510(b) of the US Bankruptcy Code, which (if applicable) operates mandatorily to subordinate a secured creditor's claim even if found to be valid. By contrast, (i) secured creditors fall outside the scope of the Cayman Islands restructuring regime and the automatic stay, and may continue to enforce their contractual security; (ii) there is no equivalent of 11 USC §510(b) of the US Bankruptcy Code in Cayman Islands law; and in any event (iii) it is rare for officeholders in the Cayman Islands to be granted powers to bring litigation, within the context of a restructuring.

Different Treatment

Consider also a situation in which the creditors of a company include claimants under US securities laws. They would be subordinated to other unsecured creditors in a US Plan, which is a powerful tool (or stick for negotiation) that could be used by Cayman Islands ROs. In a Cayman Islands scheme, by contrast, those litigants may be indistinguishable from holders of unsecured bonds, for example, when identifying what rights are to be varied or released against the company, assuming the hypothetical comparator is a liquidation. If a class action is on foot, the number of litigants may be large or unknown. Additionally, the value of the bond debt would be easily ascertainable, but there cannot be the same confidence in the pleaded value of the litigants' damages. This may make a pure scheme of unsecured debt hard to achieve or at the very least unpredictable, given both (i) the headcount requirement and (ii) the difficulty in offering different percentages of recovery, by way of scheme consideration, to each of the groups of unsecured creditor who would, subject to adjudication of claims, recover *pari passu* in a hypothetical liquidation.

No *Gibbs* short-cut

Some have suggested that a new feature of the regime is that it will be easier to compromise or vary English-law debt. That may not be the case.

Section 86 of the Companies Act continues to set out legislative provisions about the presentation of a compromise or arrangement to creditors or members of a company, the Court's power to order meetings and (if statutory majorities are achieved) sanction a scheme, and its binding effect if so approved. Those provisions do not form part of the insolvency law of the Cayman Islands. New Section 91I replicates those same provisions but within the context of the Restructuring Officer Proceeding. In particular, section 91I(2) provides that *"... the compromise or arrangement shall, if sanctioned by the Court, be binding on all the creditors or class of creditors..."*

Some practitioners and commentators consider that the purpose of such duplication is to allow ROs appointed in the Cayman Islands to apply, under section 426(4)-(5) of the Insolvency Act 1986, for assistance from the English Court. The English Court would be invited to apply Cayman Islands insolvency law, *viz.* Section 91I. They argue that it would therefore no longer be necessary to present a parallel scheme in the English Court, if a Cayman Islands scheme of arrangement was approved which purported to vary or compromise debts governed by English law.

That may not be the correct analysis and, if so, the rule in *Gibbs* (1890) 25 QBD 399 will continue to require a parallel scheme in England. The Restructuring Officer Proceeding may not be treated as part of Cayman Islands' "insolvency law" for the purposes of an application under section 426, given the express and exclusive definition in that statutory provision.

- Section 426(4) of the Insolvency Act 1986 provides that *"The courts having jurisdiction in relation to insolvency law in any part of the United Kingdom shall assist the courts having the corresponding jurisdiction in ... any relevant country"* and section 426(5) refers to any request made *"to apply, in relation to any matters specified in the request, the insolvency law which is applicable by either court in relation to comparable matters falling within its jurisdiction".*
- The term "insolvency law" for these purposes is defined by section 426(10) in an exclusive manner. In relation to any relevant country, such as the Cayman Islands, insolvency law is that part of the Cayman Islands law that "corresponds" to the specific Acts and provisions referred to in section 426(10)(a)-(c), in relation to England & Wales, Scotland and Northern Ireland.
- None of the UK Acts or provisions referred to in section 426(10)(a)-(c) include provisions that correspond to the Restructuring Officer Proceeding (or section 91I specifically), which find their closest analogue in Part 26 or Part 26A of the UK Companies Act 2006.

Other Features

There are two features of the new regime which may become clearer through judicial decision-making.

Interim ROs

There is scope under section 91C, *"where it is in the interests of the company to do so"*, for the company to make an *ex parte* application for the appointment of ROs on an interim basis, pending the hearing of the RO Petition.

The test itself will need to be glossed by judicial interpretation. However, it means that in some situations, ROs may be in office sooner than 21 days after filing.

But the need for such a provision is elusive. The company has initiated the proceeding and so already seeks a restructuring to save the company. The intended ROs might already be involved, on an informal basis, in negotiations with key stakeholders. Why should they formally be appointed on an interim basis, on an *ex parte* application?

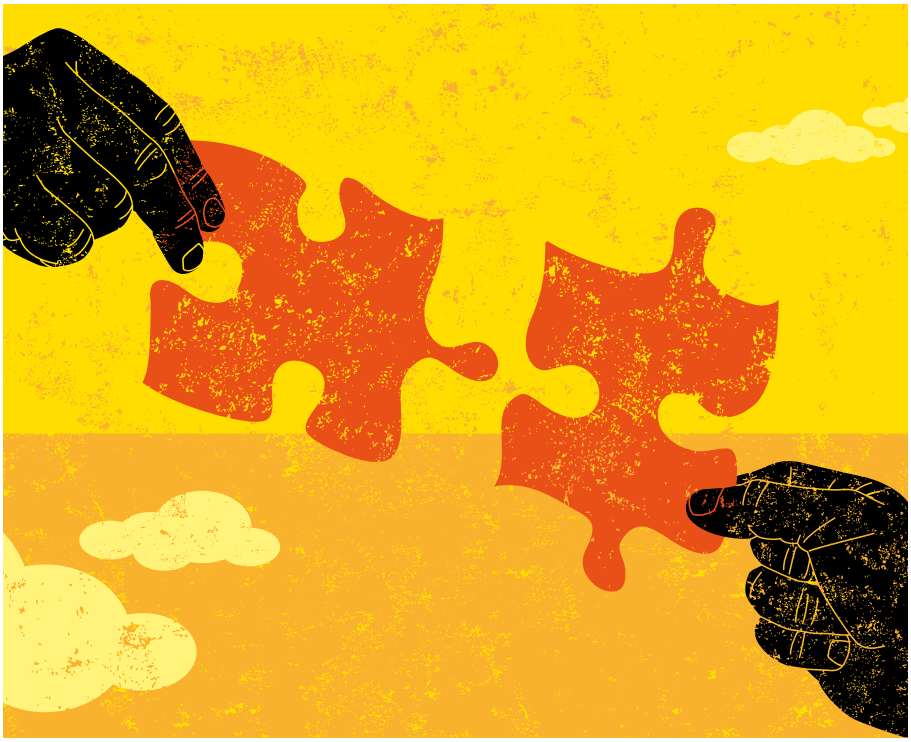
If there are creditors that seek a winding up order, they are prevented from presenting or continuing a petition without leave of the Court because of the automatic stay that arose on filing the RO Petition.

Members' Schemes

The only ground on which an RO Petition may be presented is one of insolvency:

"91B(1)(a) The company is or is likely to become unable to pay its debts within the meaning of section 93; and (b) Intends to present a compromise or arrangement to its creditor (or classes thereof) either, pursuant to this Act, the law of a foreign country or by way of a consensual restructuring"

Members-only schemes likely therefore fall outside of this regime altogether. Such cases may have less need for a moratorium on claims against the company, in any case. A compromise or arrangement only with members may therefore be presented by filing a scheme petition under section 86 of the Companies Act. It should be noted that for members' schemes in the Cayman Islands, the necessary statutory majority is now 75 per cent by value approving the scheme in any given class, without any separate headcount requirement.



Nevertheless, section 91I is entitled *"Power to compromise with creditors and members within restructuring officer proceeding"* and section 91I(3) sets out the statutory majority required for members. This may be intended to cover a situation in which the terms of a debt restructuring also involve an alteration to the rights of members, such that it involves a compromise or arrangement also with members.

Conclusion

In terms of substantive law, the manner in which debt may be restructured in the Cayman Islands within a court proceeding has not changed.

- Schemes of arrangement continue to be the principal tool under Cayman Islands law and the mechanics of schemes have not been altered. Unlike the relatively new regime under Part 26A of the UK Companies Act, for example, there is no possibility of cross-class cramdown.
- Secured creditors fall outside scope and may continue to enforce their contractual security, unlike in a Chapter 11 proceeding.
- For the restructuring of the debt of a group of companies, the debt of each company still needs to be considered individually. There is no scope for 'substantive consolidation'.

As a matter of procedural law, however, there are important changes.

- The establishment of a standalone regime reflects the fact that companies may seek judicial assistance specifically with a restructuring in mind – restructuring is not a reaction to the presentation of a winding up petition. In the same vein, the language is now consistent with the expectations of clients and the reality of what is to be undertaken and, hopefully, achieved.
- The initiation of a restructuring proceeding is simpler, which benefits companies in financial trouble seeking quick relief.
- The relief provided by way of an automatic stay on claims against the debtor by being immediate, upon filing, and extraterritorial in scope.

There is now also express reference to a Cayman Islands proceeding being used to support restructuring efforts to be promoted in a foreign proceeding. Officeholders may therefore take advantage of tools available only in other regimes, and differences of treatment of creditors between jurisdictions, in order to achieve the best outcome for the debtor and all stakeholders. ■

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Bermudian Insolvency and Restructuring Law Update

Bermuda's insolvency and restructuring landscape is distinct in a number of ways. In this article, we discuss three of those areas with recent developments:

- Bermuda has developed a rescue culture without statutory provisions in support of rescue procedures;
- Bermuda's approach to directors is notably friendlier than many other jurisdictions; and
- Bermuda strives to enable, through regulation, novel corporate activity and structures.

First however, we will begin with a brief overview of the key aspects of Bermuda's insolvency regime.

Bermuda is an overseas territory of the United Kingdom. Its legal system is based on the English common law but, over the years, Bermuda has developed its own distinct jurisprudence in many areas, including insolvency and restructuring.

The principal statutory provisions governing corporate insolvency and restructuring are contained in Part XIII of the Companies Act 1981 (the Companies Act) and are supported by the Companies (Winding-Up) Rules 1982 (the Winding-Up Rules). The Companies Act is based on the English Companies Act 1948 and the Companies Winding-Up Rules are based on the English Companies (Winding-Up) Rules 1949. No substantive changes have been made to Part XIII of the Companies Act and the Winding-Up Rules since they were enacted, although there have been minor amendments. The following insolvency and restructuring processes are available in Bermuda:

- Members' voluntary liquidation;
- Creditors' voluntary liquidation;
- Compulsory winding up by the Court;
- Provisional liquidation; and
- Schemes of arrangement.

Pari passu treatment of unsecured creditors is central to the Bermudian insolvency regime. Secured creditors are unaffected by insolvency proceedings in Bermuda and may enforce their security in accordance with the terms of the governing security instrument (although they have standing to present winding-up petitions).

The Companies Act allows liquidators to challenge certain transactions executed by insolvent companies through avoidance or claw-back provisions.

This includes the avoidance of preferential payments to creditors and transactions at an undervalue. The Companies Act also provides remedies for fraudulent trading and dispositions of company property after the commencement of the winding-up.

Bermuda's Rescue Culture

Bermuda enjoys a strong rescue culture. Provisional liquidation in Bermuda is the appointment of a liquidator other than for the immediate winding up of the company. A provisional liquidator will be nominated by one or more of the parties. The court must accept the credentials of any nominees who, by custom and practice, will be insolvency practitioners with an accounting background and at least one of whom must be resident in Bermuda.

There are two circumstances an order for the appointment of a provisional liquidator will be made:

- where it is necessary for the court to appoint an officer to protect and prevent a dissipation of the company's assets in the intervening period between the filing of a petition and the making of a winding-up order; or
- where there is a prospect of 'rescuing' an insolvent company through restructuring either with or without the displacement of some or all of the board's executive functions.

The first type of appointment given above mirrors the English jurisdiction for appointment of provisional liquidators and, like in England, is one of the most extreme tools at the Court's disposal, deployed only in exceptional circumstances where an urgent need to preserve assets justifies the immediate appointment of liquidators; it will be unlikely the Company recovers.

The second type of provisional liquidation is a distinct feature of Bermuda's restructuring landscape. Accordingly, where a company is insolvent, instead of making a winding-up order to liquidate the company, the Bermuda court often appoints provisional liquidators with certain, limited powers, known as 'light-touch' powers. This appointment is by far the most common form of provisional liquidation in Bermuda.

The Court of Appeal for Bermuda has recently addressed the law on this second kind of provisional liquidation. On 30 September 2022, the Court of Appeal for Bermuda (the Court) handed down its reasons for making a winding-up order, overturning the Bermuda Supreme Court, in *Hong Kong and Shanghai Banking Corporation Ltd v NewOcean Energy Holdings Limited* [2022] CA (Bda) 16 Civ *(re NewOcean)* (discussed in further detail below).

In a light-touch liquidation, a company may continue its business operations as usual, pending implementation of a plan for the restructuring the company's debt. Usually, the court must be satisfied that a restructuring will produce a better result than a winding up for creditors. As explained by Kawaley CJ in *Z-OBEE Holdings Ltd* (2017) Bda LR 19:

> *"[Section 170 of the Companies Act 1981 (Power of Court to appoint liquidators)] has for almost 20 years been construed as empowering this Court to appoint a provisional liquidator with powers limited to implementing a restructuring rather than displacing the management altogether pending a winding-up of the respondent company."*

The Bermuda court has used provisional liquidation as a tool to restructure the affairs of a company, preserve value in a business and provide a platform for distressed companies to recover – which together promotes the sustainability and success of cross-border business.

A key feature of provisional liquidation is the stay of proceedings against the company triggered by the appointment of provisional liquidators. Creditors are protected, given the independent oversight of provisional liquidators who, as officers of the court, are under a duty to act in the best interests of creditors.

Provisional liquidation is often used together with a scheme of arrangement to effect debt restructurings. It has been said that it is unprecedented for an insolvent scheme to be promoted other than by provisional liquidators. The Scheme of Arrangement requires a double majority: 75% in value and a majority of those voting in each class.

Class composition is broadly in line with other common law jurisdictions and there is no cross-class cram down in a Bermudian scheme.

Companies have often sought the shelter of light-touch provisional liquidation in response to a creditor's petition. The Court must then consider whether to adjourn the creditor's petition and appoint JPLs or to make an immediate winding up order,

dismissing the application for light-touch provisional liquidation.

This was precisely the situation in *re NewOcean* when the case was heard before the Supreme Court of Bermuda in December 2021 on a creditor's petition. NewOcean Energy Holdings Limited (NewOcean) is a Hong Kong listed, Bermuda incorporated, holding company for a Chinese energy, real estate and shipping group.

In 2020, NewOcean found itself in financial difficulties. It owed upwards of USD $800m to a number of banks. NewOcean entered into negotiations with over 30 bank creditors and tried to restructure its debt by way of parallel schemes of arrangement in Hong Kong and Bermuda. Those schemes were ultimately unsuccessful, having failed to win sufficient support of creditors. On 22 October 2021 the Hong Kong and Shanghai Banking Corporation Ltd (HSBC), one of the bank creditors, presented a petition for NewOcean's winding up.

NewOcean had failed to respond to a statutory demand served by NewOcean and so was deemed insolvent. The first default to HSBC was on 2 September 2020, and so by the time the petition was heard at the end of 2021, NewOcean was clearly cash-flow insolvent as a matter of fact. NewOcean accepted this in its evidence but claimed that it was balance sheet solvent, i.e. that despite its current liquidity issues the values of its assets exceeded its liabilities.

Relying on this fact, amongst others, NewOcean asked the Court to adjourn the petition and appoint JPLs on a light-touch basis. The Court did so, adjourning the petition. JPLs were appointed on 14 December 2021 and the petition was adjourned on a number of occasions thereafter. By the end of March 2022, the extent to which creditor sentiment had hardened against NewOcean was very clear. 64.8% of bank creditors opposed any further adjournment and supported an immediate winding-up order. In order to secure its restructuring, NewOcean needed 75% of its creditors to approve its proposed scheme.

On 9 May 2022, the petition was adjourned again for reasons given by Mussenden J in a written judgment dated 31 May 2022. In that judgment, the Court held that four exceptional

circumstances that were relied upon by NewOcean were still in existence:

1. NewOcean had come before the Court in relation to a scheme previously, showing early engagement with its financial difficulties;

2. There was a restructuring plan that could be pursued by NewOcean with the JPLs' assistance;

3. As a listed company with a number of licences issued by the Chinese Government, an immediate winding-up order would be value destructive; and

4. NewOcean was a balance-sheet solvent company praying for a short adjournment to attempt a restructuring.

The 31 May 2022 judgment, in particular the decision to adjourn, was appealed by HSBC as the petitioning creditor. The appeal was heard on 25 July 2022 and on 26 July 2022, the Court allowed the appeal making a winding-up order against NewOcean. The Court's reasons were handed down on 30 September 2022.

The following key points of principle can be derived from the Court of Appeal's judgment:

1. The interests of the creditors are paramount and it will be a truly exceptional case where the views of the majority are disregarded by the Court, although the Court will not approach this from a strictly arithmetic point of view.

2. The percentage of creditors opposed or in support of the winding-up petition takes on even greater significance when the restructuring plan prayed in aid of an adjournment requires 75% in favour. Where it is clearly unlikely that majority will be achieved, an adjournment should not be granted.

3. The absence of creditors opposed to the winding up should be sufficient in most cases to justify an immediate winding up.

4. The maintenance of a light-touch provisional liquidation calls for complete transparency and cooperation from the company and non-disclosure of material matters is a strong factor in favour of an immediate winding-up.

Sir Christopher Clarke P, delivering the judgment of the Court of Appeal found that in the decision adjourning the petition dated 31 May 2022, the judge had failed to take into account (sufficiently or at all) a number of relevant considerations including:

a. The size of the majority required to restructure the company's debt. NewOcean required 75% of creditors in favour but had nearly 66% of creditors against. The prospect of the requisite majority being met and therefore of a restructuring succeeding was remote.

b. The fact that so many creditors were opposed to the adjournment. The creditors were experienced bankers and best placed to judge their own interest with no evidence that any creditors were likely to change their mind.

c. The absence of a majority of creditors opposing the making of a winding up order.

d. That the proposal was an adjournment for time to liquidate assets and that liquidations should be supervised by liquidators.

e. The history of the case, including the time since the defaults and previous failures to implement similar schemes.

This judgment clarifies the circumstances in which an order for provisional liquidation will be made and when the Court should instead make an immediate winding-up order. The Court of Appeal has reaffirmed that the views of creditors take precedence over other considerations and made clear that those seeking to appoint provisional liquidators, must cooperate with them. The decision is however subject to an outstanding appeal.

Provisional liquidators may also be appointed with full powers for the purpose of restructuring, in which case they displace the board of directors which becomes defunct. Although not common, this form of appointment has taken place where there is a lack of confidence in the Company's management and there is a likelihood that creditors may receive a greater recovery than in a liquidation scenario. In *FDG Electric Vehicles Limited* [2020] SC (Bda) 32 Com. In the *FDG* case, the Supreme Court chose to order the removal of the existing Joint Provisional Liquidators who had been appointed with *"light touch powers"* and replace them with new JPLs with full powers.

The Court found that one of the directors of the company had a conflict of interest and that the Board of Directors had engaged in questionable transactions. The Court accordingly ordered that new JPLs be appointed with full powers which effectively displaced the Board of Directors as that appointment was both in the best interests of the company and its unsecured creditors.

Director-Friendly Approach

There are a number of features of the Bermudian landscape that could lead one to conclude Bermuda is a director-friendly jurisdiction. Examples include:

1. The availability of a defence to a breach of statutory directors' duties on the basis that the director has relied on, *inter alia*, the report of an attorney, accountant, engineer, appraiser or other person whose profession lends credibility to a statement made by him (section 97(5A) of the Companies Act 1981).

2. Bermuda requires shareholders who wish to bring a derivative action to demonstrate that an exception to the rule in *Foss v Harbottle* applies: a high bar requiring a fraud on the minority with the wrongdoers in control of the Company.

3. The ability of companies to indemnify directors and hold them harmless in respect of liabilities incurred by directors to the Company.

This last feature of Bermudian corporate law provides considerably protection against claims for breaches of directors' duties than is available in other jurisdictions (for instance in the United Kingdom under section 232of the Companies Act 2006). The standard Bermudian indemnity from a company to its officers (usually contained in the bye-laws) will prevent the Company from bringing an action against a director except in cases of fraud or dishonesty.

In *Peiris v Daniels* [2015] BDA LR 16, heard before the Bermuda Supreme Court, directors of a company omitted to obtain compulsory insurance against workplace injury.

The failure by the directors to obtain this compulsory insurance amounted to a strict liability criminal offence. One of the company's employees was injured in the course of his employment.

The Company entered insolvent liquidation and proceedings were brought by the liquidator pursuant to section 247 of the Companies Act 1981 (power of court to assess damages against delinquent officers) alleging that the directors' actions constituted misfeasance and wilful default.

The Court found that the breach of duty constituted a misfeasance but not a wilful default for the purpose of the indemnity. The Plaintiff's action was dismissed. The directors were therefore saved only by their indemnity from this wilful default in the performance of their duties. Notwithstanding Bermuda's relatively director-friendly approach, Bermudian courts have applied English decisions in some contexts, particularly where there is little Bermudian authority. One such area is in relation to the creditor duty owed on the eve of insolvency.

Corporate and dispute resolution lawyers have been reflecting on the potential impact of *BTI 2014 LLC v Sequana SA* [2022] 3 WLR 709, since its release last month. While directors enjoy significant protections in Bermuda, are acutely aware of and consider themselves bound by the duties they owe to their companies. *BTI v Sequana* has therefore already had an influence in Bermudian boardrooms, as we find ourselves able to give clearer and more definitive advice on the timing and nature of the creditor duty.

Cutting-edge Corporate Forms

Bermuda has played a leading role in the creation of novel corporate structures, principally in support of the insurance industry but that may be of wider applicability in the fullness of time. The Segregated Account Companies Act 2000 and the Incorporated Segregated Account Companies Act 2019 create two different forms of company: the Segregated Account Company (SAC) and the Incorporated Segregated Account Company (ISAC).

In July of this year, in *Ivanishvili v Credit Suisse BM* [2022] SC 57, the Chief Justice described the nature of SACs:

"The concept of a segregated accounts company is that the company, as a separate legal entity, may create segregated accounts such that the assets and liabilities of each segregated account are separate from the assets and liabilities of each other segregated account. A segregated accounts company comprises (i) a general account containing assets and liabilities which are separate from the assets and liabilities of other segregated accounts; and (ii) the segregated accounts. A fundamental feature of a segregated accounts company is that assets linked to the segregated account may only be used to discharge

liabilities which are linked to that segregated account. This fundamental feature is reinforced by a number of provisions set out in the SAC Act."

ISACs operate in a similar fashion, save that each segregated account is itself, a corporate entity.

These novel corporate forms will continue to pose interesting questions as the Courts grapple with the practical implications of these structures. A liquidator may be appointed in respect of a SAC or an ISAC but, if the Court is invited to consider a petition against a SAC or ISAC, any assets or liabilities linked to the segregated accounts must be disregarded when considering with the SAC or ISAC is solvent. Conversely, a segregated account may not be wound up by order of the Court.

The Court is instead limited to appointment of receivers over those accounts. A receivership order may direct that the business and assets and liabilities of an ISAC, a segregated account or an incorporated segregated account shall be managed by a receiver specified in the order for the purpose of:

a. the orderly management, sale, rehabilitation, run-off or termination of the business of, or attributable to, the ISAC, the segregated account or the incorporated segregated account; or

b. the distribution of the assets and the payment of the liabilities of the ISAC, the segregated account or incorporated segregated account to those entitled thereto.

This is perhaps reasonably clear in the context of a straightforward insurance company but a power exists to grant SAC or ISAC status to non-insurance companies and insurance itself is becoming increasingly complex in Bermuda, with insurance as an investment or as a component of commercial lending becoming increasingly common. That is to say nothing about the insurtech movement that is sprouting up on the island, encouraged by the Bermuda Monetary Authority's innovation hub and sandbox initiatives for novel insurance models that are not yet ready for a full insurance licence.

While we wish these businesses taking advantage of novel structures every success, as litigators we are curious to see how the courts would face some of the challenges that would be posed by their failure.

Conclusion

Bermuda will continue to thrive as a restructuring destination, offering a suite of flexible options for organisations considering restructuring, supported by courts, lawyers and insolvency practitioners who have a sophisticated understanding of cross-border complexities.

Bermuda remains a jurisdiction with a vibrant and evolving insolvency and restructuring scene. Through the appointment of provisional liquidators with soft touch powers and the Court's broad discretion to determine the allocation of powers and responsibilities between provisional liquidators and company directors, the Court continues to create lifelines for a healthy recovery of distressed companies and for the protection of creditor interests.

The last year has seen interesting developments and we look forward to whatever the next year will bring. We believe that Bermuda will remain committed to its rescue culture, its director-friendly approach and its innovative approach to questions of corporate structure and regulation. ■

Case Digest Editorial

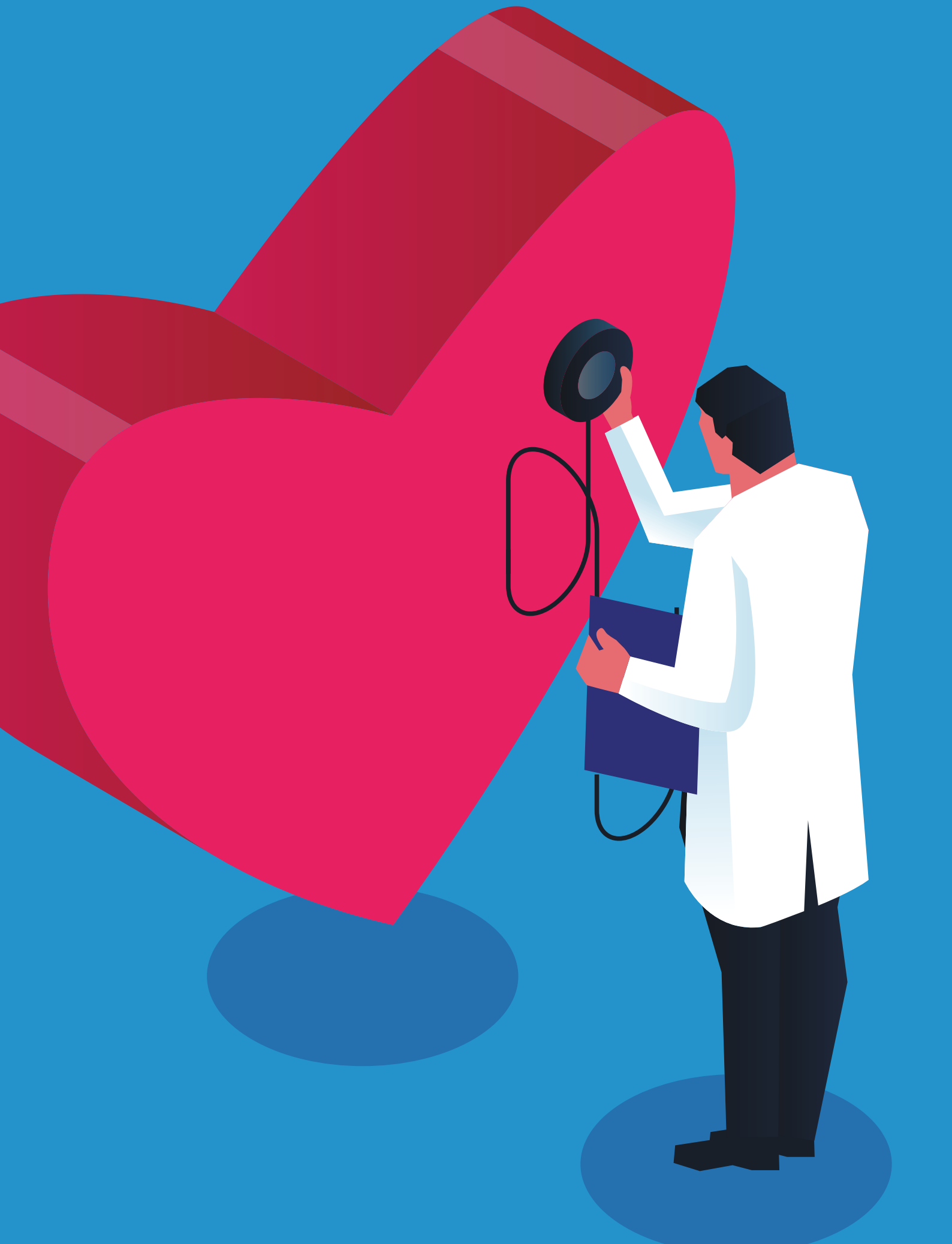
by Martin Pascoe KC

A doctor has been reported as advising that a man is born with a definite but limited number of heartbeats and it would be a mistake to waste any in a gymnasium. The same might be said of getting over-energetic in pre-action correspondence. What may have felt satisfying at the time of sending rarely has the desired effect, and may eventually produce positively undesirable results.

And what may have looked good at the time seldom seems the same when it comes to be read by a judge some months or years later. As the unsuccessful defendants in *Pisante & Ors v Logothetis* found to their (indemnity) cost when their excited response to a measured letter before action came before Mr Justice Andrew Baker on argument about the appropriate basis of assessment of costs.

The latest instalment in the Lehman administration has had to grapple with the rare situation encountered where an administration has succeeded in paying all debts, of every kind, with interest and costs and everything else, such that the company is fully restored to solvency and is to be returned to the hands of the directors on termination of the administration. This raised the question of what was meant by a "continuing" event of default – a question not addressed in the ISDA Master Agreement, and thereby the fate of payment obligations under interest rate swaps that had been suspended while an insolvency event of default was "continuing". In *Grant v FR Acquisition Corp (Europe) Ltd* Mr Justice Hildyard held that the relevant question was whether the state of affairs that constituted the event of default are continuing and not whether the effects on creditors' rights are continuing or irreversible. Thus the non-defaulting counterparty's payment obligations would revive when the administration came to an end and LBIE restored to its directors. The decision may well have ramifications for other suspended payment obligations where positions have matured in the meantime, and deserves careful study.

Finally, reverting to the important issue of heartbeats, one or two discreet retired trustees may have experienced a rise of a point or two in their resting heart-rates when considering the Privy Council decision in *Equity Trust v Halabi*. There, a 7-strong Board held, by the narrowest of margins, that a former trustee's proprietary right of indemnity out of the trust assets does not enjoy priority over the rights of a later trustee, and held that current and former trustees' rights of indemnity out of the trust fund must rank *pari passu* where the fund is insufficient to pay them all in full. As Rabin Kok notes, this decision may well have ramifications for trust creditors as well as retired trustees.



Case Digests

Banking and Finance

DIGESTED BY STEFANIE WILKINS

Bitar v Bank of Beirut SAL

[2022] EWHC 2163 (QB) (Freedman J)
15 August 2022

Bank accounts • Contract terms • Lebanon • Transfer of monies

The claimant, who was domiciled in the UK, sought repayment of the balance on accounts which he held with the defendant bank in Lebanon. The contracts between the claimant and the bank were governed by Lebanese law. The English court had jurisdiction under sections 15A–15E of the Civil Jurisdiction and Judgments Act 1982, which provides that a consumer may bring proceedings against the other party to the consumer contract in the courts of the place where the consumer is domiciled, subject to requirements which were met in the present case.

The case was brought against the backdrop of the Lebanese economic crisis; its severity led to the Association of Banks in Lebanon advising its members in November 2019 to impose restrictions on international transfers, to avoid a collapse of the Lebanese banking system.

The claimant maintained that the defendant had been under an obligation to accede to his requests to make international transfers to a bank outside Lebanon. The bank contended that there was no contractual right or custom to make an international transfer as requested, and that the economic crisis in Lebanon was sufficient under Lebanese statutory law to establish an acceptable or legitimate reason not to make an international transfer.

The court held that there was a contractual obligation to effect international transfers, which was established by the terms of the contracts; the correspondence between the parties; the bank's website; and the fact that, prior to the economic crisis, the bank had routinely acceded to international transfer requests. There was also a Lebanese banking custom to effect international transfers.

The obligation could not be vitiated by fear of a bank run or the economic crisis, but only by specified categories of reasons such as lack of funds, insufficient information, or regulatory restraints.

Accordingly, the court ordered specific performance of the obligation to make an international transfer in an amount equal to the balance on the claimant's accounts, together with interest at 9% per annum.

Barry Isaacs KC

Civil Procedure

DIGESTED BY ANNABELLE WANG

Correia v Williams

[2022] EWHC 2824 (KB) (Garnham J)
11 September 2022

Witness statements prepared for foreign language speakers

A Portuguese claimant in a personal injury case had filed a witness statement in English, which set out that he was not wholly fluent in English but was able to give the witness statement in English because his solicitors spoke fluent Portuguese. The claimant's solicitor had signed a statement at the end of the witness statement setting out that he was proficient in English and Portuguese and had translated the statement and read it back to the claimant in Portuguese.

At trial, the judge had refused to allow the witness statement to be admitted, as it did not comply with the relevant requirements set out in Practice Direction 32, that it must be drafted in the witness's own language and translated into English, with the translation being filed alongside a copy of the foreign language witness statement with the court. The judge noted that the purpose of those requirements is to ensure the court can have confidence that the statement comprises the witness's own evidence, rather than the evidence of the drafter.

The claimant appealed the judge's decision not to admit the witness statement, arguing that there was no evidence that he did not understand its contents or did not believe they were true. On appeal, the court upheld the decision of the trial judge on the basis that the failure to comply with the requirements of PD32 amounted to defects of substance, rather than merely form and the judge had been entitled to exercise his discretion to refuse to admit the statement.

Turner & Ors v Thomas & Anor (Costs)

[2022] EWHC 1944 (Ch) (Zacaroli J)
26 July 2022

Costs • Costs of an appeal • Costs against a non-party

The claimant brought a successful action against a company and an individual. The defendant company unsuccessfully appealed and was subject to an order for costs. The individual had not appealed, and the issue then arose as to whether the appellant company or both defendants should be liable for the costs of the appeal.

The individual argued that he should not be liable for costs, as he did not participate in the appeal.

The judge held that the mere fact that the individual was a co-defendant to the original action was not a sufficient reason to make a costs order against him. The correct approach was to apply by analogy the principles derived from cases where costs orders are sought against non-parties.

Applying those principles, the court considered that the individual was in fact the "real party" to the action, as he was the director and sole shareholder of the company, as well as the person responsible for managing a farm on behalf of the company. He would therefore have benefitted from a successful appeal, as it would have enabled him to continue conducting farming the land via the company. It was not a bar to making a costs order that the individual had not funded the appeal from his personal resources.

Pisante & Ors v Logothetis & Ors

[2022] EWHC 2575 (Comm) (Andrew Baker J)
13 October 2022

Indemnity costs • Pre-action correspondence

The claimants, having been successful in the action, applied for costs on the indemnity basis. The court rejected the submission that there was a presumption that successful fraud claimants should be awarded their costs on the indemnity basis, as a successful allegation of dishonest wrongdoing does not, without more, make it appropriate that a claimant's costs should be recoverable though disproportionate.

However, the court determined that the conduct of the defendants did amount to unreasonable behaviour that went beyond the norm. The relevant conduct included providing highly contrived evidence, improperly redacting material evidence during disclosure, failing to be candid with the court, and notably, responding to a "serious and measured" letter before action in "wholly inappropriate, polemic terms, calculated to intimidate".

In their response to the letter before action, the defendants had baselessly suggested that the claimant's claims were obviously vexatious, scurrilous, and ill-founded, and threatened complaints of professional misconduct and applications for costs against the claimants' solicitors and counsels. The court held that the award of indemnity costs was "the mildest of responses" to defendants who "sought to bully the claimants as to the merits of their claim".

Commercial Litigation

DIGESTED BY JAMIL MUSTAFA

ABT Auto Investments Limited v Aapico Investment Pte Limited & Ors

[2022] EWHC 2839 (Comm) (Richard Salter KC, sitting as a Deputy High Court Judge)
14 November 2022

Commercial law • Loan Agreements • Security • Financial Collateral Arrangements • Enforcement

For the first time, the High Court considered what was required for a collateral taker to comply with the requirement to value collateral in a 'commercially reasonable manner' under Regulation 18 of the Financial Collateral Arrangement Regulations 2003 (the "FCARs").

The claimant and defendant had been party to a joint venture which was to be carried out by a joint venture company in which both the claimant and the defendant held shares. Under the joint venture the defendant had provided monies under two loan agreements, one agreed in 2017 and another in 2018. At the time of the second loan agreement, the claimant provided a charge over its shares in the joint venture company in favour of the defendant(the "Share Charge") to secure the amounts due under both the 2017 and 2018 loan agreements. It was common ground that the Share Charge was a security financial collateral arrangement and so subject to the FCARs.

The joint venture was ultimately unsuccessful. The defendant demanded repayment from the joint venture company of amounts due under the two loan agreements. No payment was forthcoming. The defendant then demanded payment of the outstanding amounts from the claimant under guarantees which the claimant had provided. The claimant did not pay and therefore the defendant exercised its rights under the Share Charge to appropriate the claimant's shares in the joint venture company, ascribing their shares a value of USD 27m.

The claimant brought proceedings challenging the appropriation by the defendant on two bases: (i) the appropriation was invalid because it was not in accordance with the requirements of the Share Charge and/or the FCARs because it did not provide for a valuation in a commercially reasonable manner; and (ii) alternatively, because the claimant's valuation was not commercially reasonable, the Court should determine the value of the charged shares. The judge rejected both of these challenges and entered judgment in favour of the defendant.

First, the judge rejected the argument that the Share Charge was ineffective to confer a legally valid power of appropriation because it did not provide for a method of valuation that was commercially reasonable. The judge considered that it did. Further, and in any event, the judge did not consider that the FCARs required a valuation in a commercially reasonable manner as a precondition of a legally valid appropriation. The remedy for a non-compliant valuation under the FCARs, after an appropriation, was to ask the Court to set aside that valuation and substitute a compliant one.

The judge further rejected the claimant's alternative case that the valuation carried out was not conducted in a commercially reasonable manner as required by the FCARs. In his judgment, he outlined the principles to be applied, and made clear that, in the context of the consideration of the valuation required by the FCARs, there was no requirement for the collateral taker to act in good faith or any basis to imply and equitable or other duties associated with the English law of mortgages. It was, however, clear from the FCARs that the duty of valuation lay upon the collateral taker, who was therefore responsible for any third-party valuation, which must be carried out in a commercially reasonable manner. In this respect, it was the way in which the valuation was carried out that had to be commercially reasonable, not the result, and whether the valuation was commercially reasonable was an objective question and fact-sensitive. Applying these principles, the judge rejected the challenges brought by the claimant to the valuation of the defendant (undertaken by a third-party valuer) and the claimant's claim was dismissed.

Tom Smith KC and Ryan Perkins

Transworld Payment Solutions UK Limited (in liquidation) and Anor v First Curaçao International Bank N.V. and Anor

[2022] EWHC 2742 (Ch) (Freedman J)
31 October 2022

Jurisdiction challenge • Natural forum • Case management stay • Assignment of fraudulent trading claims

The judge rejected a jurisdiction challenge brought by the first defendant, FCIB, and an application for a case management stay brought by the second defendant, Mr Deuss. The claimants had commenced proceedings against the defendants in England for fraudulent trading, dishonest assistance, contribution and breach of fiduciary duty. The underlying facts related to an alleged missing trader intra-community fraud. The fefendants are alleged to have assisted English companies (now in liquidation) in committing fraud by providing banking services to them. The first defendant had commenced proceedings in Curaçao claiming a negative declaration that they are not liability and raising a defence based on a settlement agreement. These proceedings were still at the jurisdiction stage in Curaçao.

The judge held that broadly the issues were more closely connected with England than Curaçao – the alleged fraud related to VAT, the claimants were based in England, key meetings were in London, and the companies alleged to be engaged in the underlying fraud were largely English companies. The construction of the settlement agreement was not the sole or predominant question in the English proceedings because the fraud was not admitted. The judge considered it was "highly material" that the Curaçao proceedings were for negative declarations and that Mr Deuss was not a party to them. The judge also considered that the possibility of inconsistent decisions had significantly less weight given that it was the first defendant's choice to commence proceedings in Curaçao. The judge took account of the claimants' delay in bringing proceedings as a factor, but felt its significance was greatly reduced by the fact that substantive proceedings have not yet commenced in Curaçao.

The judge also rejected the second defendant's application for a stay. The judge noted that "there are closely intersecting factors" with the first defendant's application. Given he had concluded that the natural forum was in England, he did not consider it appropriate to stay the English proceedings pending the determination of the claims in Curaçao.

However, the judge did hold that the claimants were not entitled to bring assigned fraudulent trading claims. The purportedly assigned claims did not fall within the statutory provision which enabled such assignments because the relevant liquidations (of the assignor companies) were commenced before the provision came into force. The Judge considered he was therefore bound to follow Re Oasis Merchandising Services Ltd (In Liquidation) [1998] Ch 170. The statutory provision did not affect this decision and it was clearly the intention of the legislature that the provision should only apply where the relevant liquidation was commenced after 1 October 2015.


Tom Smith KC and Paul Fradley

Grant v FR Acquisition Corp (Europe) Ltd

[2022] EWHC 2532 (Ch)

Interest rate swaps • ISDA Master Agreement • Interpretation • Schemes of Arrangement

The High Court considered the interpretation of a number of standard form provisions of the 1992 and 2002 ISDA Master Agreements upon a directions application made within the administration of Lehman Brothers International Europe ("**LBIE**").

LBIE was party to two swap transactions with FR Acquisitions (Europe) Ltd and JFB Firth Rixson Inc (together "**Firth Rixson**") governed by 1992 and 2002 form ISDA Master Agreements respectively. Other counterparties to similar derivatives transactions with LBIE had closed out their transactions with LBIE following its entry into administration. Firth Rixson was 'out of the money' (i.e., owed LBIE money) under both of these swap transactions. But for more than a decade, Firth Rixson had declined to close out the swap transactions, and pay monies over to LBIE, in reliance on section 2(a)(iii) of the ISDA Master Agreement, the effect of which, as held by the Court, was that the payment obligation of the non-defaulting party to a derivatives transaction was suspended for as long as the relevant Event of Default was continuing (*Lomas v JFB Firth Rixson Inc* [2012] 1 CLC 713).

However, after a decade in administration, the joint administrators of LBIE were working towards bringing its administration to an end and return the company to the control of its directors. The joint administrators of LBIE argued that once this had happened, no Event of Default or Potential Event of Default (as defined under the ISDA Master Agreement) was continuing in respect of LBIE and therefore the suspension of payment under section 2(a)(iii) would be lifted. Firth Rixson challenged this position on the bases that: (i) LBIE had become subject to a number of additional Events of Default, by reason of the sanction of a scheme of arrangement in respect of it and the recognition and enforcement of that scheme under the US Bankruptcy Code; and (ii) the original Events of Default, namely LBIE's failure to make payments when due under the swaps, its admission in writing of an inability to pay its debts and entry into administration (which it was common ground were Events of Default), and the subsequent Events of Default, would be "*continuing*" even after the termination of the administrators' appointment and were incapable of cure.

Both of these challenges gave rise to questions of interpretation of the ISDA Master Agreement.

The central issue in the case was, however, whether the scheme of arrangement was an *"arrangement…with or for the benefit of [LBIE's] creditors"* within the meaning of section 5(a)(vii)(3) of the ISDA Master Agreement and therefore an Event of Default. The judge held that it was not. The word *"arrangement"* had to be interpreted in its context and was concerned with a process entered into and designed to operate in circumstances of financial distress which affected the credit risk of the defaulting party. That was not the context or effect of the scheme of arrangement which only affected the surplus in the administration while at the time of its sanction LBIE was solvent and remained solvent. It followed therefore that by virtue of it being a solvent scheme of arrangement, its recognition and enforcement in the US was also not an Event of Default. As regards, the meaning of the word *"continuing"*, the judge held that the test was whether the event or state of affairs giving rise to the Event of Default was continuing, not whether the creditor's rights were permanently altered or continued to be affected. Accordingly, the judge held that all of the Events of Default to which it was common ground that LBIE had been subject would no longer be continuing upon the termination of LBIE's administration and confirmation of its ability to pay its debts.




The late Robin Dicker QC, Daniel Bayfield KC, Henry Phillips and Ryan Perkins

Company Law

DIGESTED BY PETER BURGESS

In the matter of Seahawk China Dynamic Fund Ltd

(FSD 23 of 2022 (DDJ)) (Doyle J) (Cayman Islands)
9 August 2022

Cayman Islands • Dismissal of winding up petition based on the just and equitable ground • Solvent open-ended investment fund • Quasi-partnership • Legitimate expectation of participating in management • Need for an investigation • Alternative remedies

A winding up petition brought by a substantial investor against a solvent open-ended hedge fund was dismissed by the Grand Court of the Cayman Islands. The two main protagonists were LCS, the investor and petitioner, and HL, the hedge fund manager and the owner of the fund's voting shares. The investor had invested over $200 million in the fund, and the fund manager had generated very significant returns. The relationship between the investor and the fund manager had nonetheless deteriorated.

The investor brought a petition for the winding up of the fund on the just and equitable basis. He claimed that the fund had been established as a quasi-partnership and that he had had a legitimate expectation of being involved in management. The petitioner had previously been a director of the fund but had been removed by the fund manager. Prior to the hearing of the petition, the petitioner successfully applied for the appointment of provisional liquidators over the fund.

The petitioner claimed that changes to the fund's share structure and governing documents relating to the payment of performance fees made by HL, and the allocation of $20 million of performance fee to HL, were unauthorised and dishonest. He also claimed that certain trades undertaken by HL had been done to deliberately and dishonestly cause loss to the fund.

As a result of these two courses of conduct, the petitioner claimed that the relationship of mutual trust and confidence had irretrievably broken down and that he had lost confidence in the fund manager due to a serious lack of probity. He also claimed that his removal as director was an unjustified exclusion from management and that there was an urgent need for an investigation.

The judge rejected all of the petitioner's grounds and discharged the appointment of the provisional liquidators. He remarked that it is a very serious step to make an order winding up a solvent company. He was not satisfied that the fund was a quasi-partnership; the relationship was one between an investor and a fund manager.

He found no evidence of dishonesty on the part of the fund manager. The allegations of dishonesty were at the core of the petitioner's case; shorn of dishonesty, and in the particular context of the fund, the allegations were not sufficient to justify the court taking the drastic step of winding up a solvent company.

Even if the petitioner had established his alleged grounds, the court would not have ordered winding up. Since the fund was open-ended and solvent, there was a reasonable alternative remedy available to the petitioner, namely redemption of his shareholding pursuant to the terms of the fund. The petitioner had unreasonably failed to pursue his alternative remedies.

Tom Smith KC and Peter Burgess

Barclay-Watt v Alpha Panareti Public Ltd

[2022] EWCA Civ 1169 (Males, Phillips, Andrews LJJ)
19 August 2022

Negligent advice • Director's liability • Limited liability

The claimants were investors who alleged that the company, APP, had made or was responsible for misrepresentations and negligent advice in relation to investments in the development of luxury properties in Cyprus. The judge had found that APP was liable to the claimants because it had failed to warn the claimants of the foreign currency risks when extolling the benefits of a mortgage which involved a loan denominated in Swiss francs with the anticipated rental income being in Cyprus pounds or sterling. However, the director of APP and the driving force behind the marketing was under no personal liability.

APP appealed the finding of liability against it, while the claimants cross appealed on the basis that the judge should have found the director personally liable as an accessory to the wrongdoing of the company.

On liability, the Court of Appeal considered that it had been a central issue at the lengthy trial before the judge and it was impossible to say that the judge was not entitled to reach the conclusions he did.

On the director's liability, the claimants submitted that the director was liable as an accessory to the tort committed by the company, having dropped a submission that he was a primary tortfeasor. The claimants relied on the principles set out by the Supreme Court in Fish & Fish Ltd v Sea Shepherd UK [2015] UKSC 10, [2015] AC 1229.

The Court of Appeal reviewed the authorities and emphasised that the question of whether a director or senior manager should be held personally liable as an accessory to a tort committed by a company is a fact-sensitive question. The question is a difficult one that requires the courts to strike a balance between the principle that individuals can limit their liability by incorporating a company as a distinct legal entity to carry on their business and the principle that a tortfeasor should be liable for his tortious acts and not escape liability merely because he is a director or officer of a company.

In the context of the present case, the business of developing and marketing the properties was APP's business, not the director's. APP entered into contracts, not the director. The director had not himself committed any tortious act and the judge had found that it would not have occurred to any of the claimants that the director had assumed any responsibility towards them. If the director in this case were to be personally liable, the Court considered it would be difficult to see why any director or senior manager who is heavily involved in a company's marketing of an unsuitable investment would not incur personal liability for a negligent but non-fraudulent failure to warn of the risks of that investment. This would drive a coach and horses through the concept of a limited liability company.

Re Compound Photonics Group Ltd

[2022] EWCA Civ 1371 (Snowden, Carr, Newey LJJ)
21 October 2022

Unfair prejudice petition • Shareholders' agreement • Good faith clause

This was an appeal of a decision in an unfair prejudice petition under section 994 of the Companies Act 2006 in which the majority shareholder appellants had been ordered to buy the shares of the minority shareholder petitioners in the company.

The essence of the minority shareholders' petition was that they had been unfairly prejudiced when two minority shareholders were removed from office as directors and thereby excluded from any continuing role in management. However, since it was common ground that the company was not a quasi-partnership, the decision was reached on the basis that the majority shareholders had breached the terms of a shareholders' agreement.

The judge had found that the shareholders' agreement and the Company's articles comprised a "constitutional settlement" under which: (i) certain minority shareholders were entrenched in office as directors; and (ii) even though the majority had 93% of the shares, if they voted in favour of removing the minority shareholders from office or sought to obtain control of the board, that would be a breach of contract. There were no express terms of the shareholders' agreement to that effect so this was derived from the clause in the agreement under which the shareholders undertook to act "in good faith" to each other and to the company in relation to the matters contained in the agreement.

The majority shareholders appealed on the basis that the judge interpreted the "good faith" clause in the shareholders' agreement far too widely; the clause did not mean that the majority had given up the right to vote to remove the minority shareholder-directors or take control of the management of the company.

The Court of Appeal agreed with the majority shareholders and allowed the appeal. In principle, the judge had been correct to approach the case on the basis that, in the absence of a quasi-partnership, the only grounds for constraints upon the majority shareholders were to be found in the shareholders' agreement. However, the Court of Appeal disagreed with the judge's interpretation of the good faith clause in that agreement. The concepts of good faith relied upon by the judge were derived from cases and commentary on US contract law and in Australia in relation to commercial contracts. The structure of a limited company and the relationship between its shareholders was a very different context. Minimum standards of good faith derived from other contexts should not be imported and the concept of adherence to the spirit of the agreement supports only the common purpose of the parties, objectively ascertained. In this case, the common purpose of the articles and the shareholder agreement was not to remove all power from the majority regarding the management of the company. In the Court of Appeal's view, the duty of good faith imposed only a core requirement that the parties should act honestly towards each other and the company and not to act in bad faith.

Corporate Insolvency

DIGESTED BY DANIEL JUDD AND PAUL FRADLEY

Re Allied Wallet Limited

[2022] EWHC 1877 (Ch) (ICCJ Burton)
19 July 2022

Electronic Money Regulations 2011 • Payment Services Regulations 2017 • Costs of administration and liquidation

The business of Allied Wallet Limited ("AWL") included processing electronic payments for online businesses, and issuing electronic money in the form of prepaid cards. It was subject to the Electronic Money Regulations 2011 ("EMR") and the Payment Services Regulations 2017 ("PSR"), and was required to safeguard monies received from these activities. The FCA was concerned that AWL had not complied with those obligations, appointed provisional liquidators, and wound up AWL. There were insufficient monies available to meet the claims against AWL. The liquidators applied for directions in relation to how AWL's remaining assets should be applied. A number of the issues on which the liquidators sought directions had been resolved by the decision of the Court of Appeal in Re Ipagoo LLP (in administration) [2002] EWCA Civ 302. The judgment of ICCJ Burton gives guidance on three additional issues.

The first issue was the scope of the "costs of distributing the asset pool", referred to in the EMR at regulation 24(2) and the PSR at regulation 23(15), for the purpose of reimbursing officeholders for their work done. The court held that these words should be interpreted broadly to include work related to reconstituting or distributing the asset pools. That may include work to identify, investigate, and realise the company's assets, including liaising with the FCA and reporting to the court. However, it did not extend to all of the costs of provisional liquidators or liquidators in performing their functions.

The second issue was the applicable date for valuing assets and liabilities in foreign currency, where a company was subject to the EMR and PSR.

The Judge concluded that the claims of creditors against the asset pool were analogous to unsecured claims. On that basis, rule 14.21 of the Insolvency Rules 2016 should apply, and the liquidators must convert all debts into sterling at a single exchange rate for each currency, by reference to the exchange rate prevailing when the company entered liquidation. Even if the claims were regarded as analogous to secured claims, it would nevertheless be appropriate for the court to select this same date as a workable solution in this case.

Finally, where a company is obliged to safeguard funds under two regulations (each requiring a separate asset pool), the court considered how the available assets should be applied as between monies safeguarded under the EMR and PDR regimes. In the absence of other identifiable principles, the court applied the maxim "equality is equity", and held that the assets should be applied rateably. The assets available to reconstitute the asset pools should be divided between the asset pools rateably by reference to the shortfall suffered by each asset pool.

Richard Fisher KC and Andrew Shaw

Re Rhino Enterprises Properties Limited

[2022] EWCA Civ 824 (Newey LJ)
21 June 2022

Contractual interpretation • Claims against administrators • Settlements • Releases • Third party rights

This was an appeal about the interpretation and effect of a settlement agreement which appeared to release claims against the "Affiliates" of the parties to the settlement agreement.

Certain companies within the same group had entered into loan facilities and interest rate hedging agreements with Barclays Bank (the "Bank"). The Bank appointed administrators to those companies following non-payment. The group companies made claims that the Bank mis-sold swaps to them, and that it had made dishonest representations relating to LIBOR. The administrators considered those claims against the Bank with the assistance of a firm of solicitors. Those proceedings were settled by a settlement agreement in 2015. The settlement agreement provided that the "Parties' Affiliates" could enforce the settlement in accordance with the Contracts (Rights of Third Parties) Act 1999, and that the settlement was in "full and final settlement of all Claims any Party has or may have against any other Party or against any other Released Party". In 2019, the same group companies claimed misfeasance against the administrators, and also brought claims against the firm of solicitors. Both the administrators and the solicitors applied to strike out the claims on the basis that they had been released by the settlement agreement. In the High Court, the claims were struck out in their entirety against the administrators, and against the solicitors in so far as the claim alleged a breach of duty whilst acting as an agent. The group companies appealed, and the solicitors cross-appealed.

The Court of Appeal dismissed the appeal and allowed the cross-appeal. The group companies' claims were therefore struck out in their entirety.

The evidence relied upon by the group companies, to the effect that it was not intended that the settlement agreement should release claims against the administrators, was inadmissible. Newey LJ reiterated that it was not permissible to rely on evidence of subjective intention to interpret the settlement agreement, nor to rely on pre-contractual communications or negotiations in order to draw inferences about what the contract should be understood to mean. There was no relevant doubt as to the aim or purpose of the settlement agreement.

As a matter of contractual construction, the Court of Appeal rejected the argument that the settlement agreement should be interpreted such that claims by a party's own affiliates were excluded, i.e. that a party was in effect purporting to release itself. This ran contrary to the natural meaning of the words used. There was a reason to think that the Bank would seek the maximum possible protection in order to avoid exposure to "ricochet" and contribution claims. Further, the defendant administrators, and the solicitors they appointed, were properly to be regarded as "Affiliates" of the group companies. Once the defendants were a "Released Party" under the settlement agreement, they were released from all claims against them – not just claims in their capacity as agents.

The Court of Appeal also agreed with the Judge that the former administrators were not precluded by the rule in Ex p James from relying on the release in the circumstances, noting that the administrators did not instigate the settlement, which was entered into with the benefit of legal advice, and that it was apparent from its terms that the settlement provided for wide releases which third parties would be able to enforce.


Tom Smith KC and Hannah Thornley

Re Galapagos SA

[2022] EWHC 1633 (Ch) (Bacon J)
30 June 2022

Winding-up • Jurisdiction • EU and Retained Insolvency Regulations • COMI shifting

In this case, English insolvency proceedings had been issued, following a series of steps to shift the Company's COMI to England. However, after this, a group of noteholders exercised their rights to replace the Company's board with a sole German director. The Company then commenced insolvency proceedings in Germany and the English proceedings were stayed. The German Court made a preliminary reference to the CJEU on the issue of whether the German proceedings were 'main proceedings' within the EU Insolvency Regulation. The CJEU held that court of the Member State within the territory of which the debtor's COMI is situated at the time of the initial request to open insolvency proceedings retains jurisdiction to open those proceedings if the debtor subsequently moves its COMI to another Member State after lodging the request but before the proceedings are opened.

The English Court held that the German proceedings were not validly opened and so could not be characterised as 'main proceedings' for the purposes of the EU Insolvency Regulation (as it has effect under transitional provisions). The CJEU had unambiguously determined that the court of the member state first seised had exclusive jurisdiction to open main proceedings. The Court did not need to wait for the German court to implement the effects of the CJEU's ruling. As a result, the EU Insolvency Regulation no longer governed the jurisdiction of the Court on the facts.

The Court was satisfied that the policy considerations underpinning the CJEU's approach to the EU Insolvency Regulation (namely to prevent forum shopping) still applied to the Retained Insolvency Regulation. COMI therefore needed to be assessed at the time the request to commence insolvency proceedings was made. The Judge determined that prior to the English insolvency proceedings being commenced the Company's COMI had properly been shifted from Luxembourg to England – the core management team had been relocated, meetings either took place or were organised from England, and the changes were notified clearly to third parties.

Finally, the Judge determined it was appropriate to exercise the Court's discretion to make a winding-up order. There was a sufficient connection with England, and it would be incongruous to take account of the subsequent COMI shift to Germany. The winding-up order would end a protracted period during which the company has been unable to pay its substantial debts and had no source of income.



David Alexander KC, Daniel Bayfield KC, and Ryan Perkins

Harrington & Charles Trading Limited v Ors

[2022] EWHC 2960 (Ch) (Edwin Johnson J)
15 August 2022

Freezing injunctions • Discharge • Failure to disclose • Shadow directors

The defendants applied to discharge a worldwide freezing order in the sum of US$932 million. The claimants' case was that each of the defendants were complicit in a US$1 billion fraud whereby the proceeds of bullion advanced to two companies were misappropriated, laundered and concealed through multiple layers of corporate entities, with the vast majority of the proceeds said to have ended up in entities owned and/or controlled by the defendants. The claimants (now in liquidation) were said to have been used as vehicles in the alleged fraud, as one layer of the corporate entities through which the proceeds of the alleged fraud are said to have passed. The defendants contended that the claimants, in obtaining the freezing order, had breached their duty of fair presentation, and that none of the causes of action advanced by the claimants had a good arguable case. The judge dismissed the discharge application and agreed to continue the freezing injunction.

In so doing, he held *(inter alia)* that it was well arguable that section 212(1)(c) of the Insolvency Act 1986 applied to shadow directors (c.f. the Supreme Court decision in *Paycheck Services* [2010] UKSC 51 at [22]), and that the claimants had good arguable case that they are entitled to claim repayment, or restoration, or an accounting or contribution from each of the respondents pursuant to section 212.

William Willson

Re Discovery Yachts Ltd; PSV 1982 Ltd v Langdon

[2022] EWCA Civ 1319 (Lewison, Asplin, and Arnold LJJ)
12 October 2022

Directors' liabilities • Reuse of company names • Section 217 of the Insolvency Act 1986

The Court was required to determine preliminary issues in the course of a claim that a director of a company was personally liable for its debts and liabilities. The Court held that the effect of section 217 of the Insolvency Act 1986 was that, once liability was established in proceedings against a company, a director who breached section 216 was automatically liable for that liability. Section 216 prevents the reuse by company directors of the names of companies which have gone into liquidation or similar names. Asplin LJ, giving the judgment of the Court, considered this was apparent from the ordinary and natural meaning of the statute. The Court noted that the principal target of sections 216 and 217 was 'phoenix syndrome', i.e. the continuation of the activities of a failed company by those responsible for the failure using the vehicle of a new company.

Asplin LJ also held that it would be surprising if Parliament had intended that a creditor who had to establish a liability in proceedings against the company would have to prove that liability again. Parliament would not have intended creditors to be put to the expense of proving the underlying liability twice. To the extent that there was a risk of any injustice to the director, Parliament intended the risk of injustice to be on the director who breached section 216 rather than the creditor. Moreover, the Court held that a director was liable in respect of a breach of contract which occurred at the time the director was in breach of section 216, even where the contract was entered into at a time when there was no breach.

Doran & Anor v County Rentals Ltd (t/a Hunters)

[2022] EWCA Civ 1376 (Asplin LJ)
24 October 2022

Winding-up petitions • Inability to pay debts • Coronavirus test • Preliminary hearings

This appeal was concerned with the "coronavirus test", applicable to winding-up petitions presented from 27 April 2020 until 30 September 2021, and the enquiry which the court was required to engage in when this issue was raised at a preliminary hearing. The test required petitioning creditors to show reasonable grounds for believing either that coronavirus has not had a "financial effect" on the company, or that (if it had) that the company would have been insolvent and unable to pay its debts in any event.

In this case, the petitioner appealed against the dismissal of a winding up petition on the basis that the court should have confined itself to considering the effect of coronavirus on the company's solvency, taking the petitioner's evidence at its highest, and that the court should not have considered at that stage potential grounds for disputing the underlying debt. The court had drawn inferences regarding whether the company was unable to pay its debts within the meaning of section 123(1)(e) of the Insolvency Act 1986, including by reference to the company's evidence that it believed that it had been paying pre-pandemic debts, but where payment was mistakenly made to the wrong account, and where the company was unaware of this alleged indebtedness until the after pandemic supervened.

The Court of Appeal dismissed the appeal and upheld the court's dismissal of the winding up petition. It was important to stand back and consider the entirety of the temporary regime introduced by the Corporate Insolvency and Governance Act 2020, which was put in place to seek to ameliorate the effects of the pandemic on companies facing winding up. For the coronavirus test to come into play at all, the company must first be deemed to be "unable to pay its debts as they fell due". As a matter of common sense, this required the court to be satisfied that the substantive ground for presenting the petition applied, in order to then be able to satisfy itself that the ground would still apply even if coronavirus did not have a financial effect on the company. At the preliminary hearing stage, the court was required to consider whether it was likely that a winding up order would be made, taking into account the effects of the pandemic. In doing so, the court was entitled to conclude that no such order would be made on the basis that there were genuine and substantial grounds for disputing the debt. In any event, when considering the evidence at the preliminary hearing, the court was not required to make any assumptions in the petitioner's favour. The court was entitled to draw inferences on the evidence available, and to conclude in this case that the non-payment of pre-pandemic debts did not discharge the petitioner's onus of showing that the company was "unable to pay its debts as they fell due" before the pandemic.

Frasers Group PLC v The Official Receiver & Ors

[2022] EWHC 3028 (Ch) (Sir Paul Morgan)
29 November 2022

Amendments to pleadings • Section 164 of Insolvency Act 1986

In the proceedings the appellant, Frasers, seeks declarations that a Claims Release Deed, alternatively certain of its provisions, are illegal or unenforceable, alternatively that it is void or voidable (and has been avoided). Frasers appealed against the decision of the ICC judge refusing it permission to amend its points of claim to advance new allegations that each of the respondents had committed an offence under Section 164 of the Insolvency Act 1986. Section 164 provides that "*a person who gives, or agrees or offers to give, to any member or creditor of a company any valuable consideration with a view to securing his own appointment or nomination of some person other than himself, as the company's liquidator is liable to a fine*". The ICC judge refused permission on the basis that it was not for the ICC to determine whether or not someone had committed a criminal offence. On appeal, the court concluded that the ICC judge was wrong in law in this regard. However, the court went on to consider the respondents' Respondent's Notices, which asked the appeal court to uphold the order on different and additional grounds. In relation to the first ground, the respondents contended that the relevant person in Section 164 must be someone capable of being appointed as a liquidator, and that the acts of a "*person*" only came within the section if they were done "*with a view to securing his own appointment*" or "*preventing the appointment....of some other person other than himself*" and that, in the case of "*securing....the appointment...of some person other than himself*", this referred to a case where the appointment was of some other person as a co-appointee. The court concluded that Frasers had a real prospect of defeating this argument, and that it was not "*obviously right*". He also dismissed the respondents' other additional grounds. He allowed the appeal and granted permission to amend accordingly.




Tom Smith KC, Lloyd Tamlyn, William Willson and Charlotte Cooke

Personal Insolvency

DIGESTED BY LOTTIE PYPER

Lyubov Kireeva (as bankruptcy trustee of Georgy Bedzhamov) v Georgy Bedzhamov

Bedzhamov [2022] EWHC 2676 (Ch) (Falk J)
27 October 2022

Bankruptcy • Forgery • Fraud • Common law recognition

Mr Bezhamov ("B") was made bankrupt and Ms Kireeva ("T") was appointed as bankruptcy trustee in Russia on 2 July 2018. The bankruptcy order was made on the basis that B had granted a guarantee to support a loan facility given to his sister and did not pay under the guarantee when it was called, resulting in a judgment in favour of the lender ("VTB"). T sought common law recognition of the bankruptcy in England.

The matter had already been heard before Snowden J and the Court of Appeal, and this hearing was a trial to determine the issues of whether, as B contended, (1) the guarantee was a forgery, (2) that the judgment in favour of VTB was a fraud and that (3) common law recognition should accordingly be denied. In light of B's evidence, Falk J was not persuaded that the guarantee was a forgery, which resolved all three issues in T's favour.

William Willson

David Bacci, Michael Boyle, Paul Mundy, Marek Zwiefka-Sibley (by way of an assignment by the Joint Administrators of Fundingsecure Limited) v Matthew Green

[2022] EWCA Civ 1393 (Newey, Males, Arnold LLJ)
25 October 2022

Bankruptcy discharge • Fraud • Enforcemen • Pensions

This case considered to what extent a fraud claim which survived a bankrupt's discharge from bankruptcy could be enforced against the bankrupt ("G")'s occupational pension scheme. Under the pension scheme, G had the power to revoke his "enhanced protection" and thereby obtain a lump sum payment of £1.6 million after tax. The question was whether the court had jurisdiction under section 37(1) of the Senior Courts Act 1981 to require G to revoke his "enhanced protection" given that, as G contended, the "enhanced protection" was not itself a property right or tantamount to ownership. The Court of Appeal held that there was jurisdiction to make such an order, and noted that other circumstances in which the court could have made such an order included an order ancillary to an appointment of receivers or as part of injunctive relief. They also held that there was no public policy basis not to make such an order, and the fact that the order occasioned a tax liability was not a bar to making it. G's appeal was dismissed.

Property and Trusts

DIGESTED BY RABIN KOK

Equity Trust (Jersey) Ltd v Halabi; ITG Ltd v Fort Trustees Ltd

[2022] UKPC 36 (Lord Reed, Lord Briggs, Lady Arden, Lord Stephens, Lady Rose, Lord Richards, Sir Nicholas Patten, Lord Richards)
13 October 2022

Trustee's right of indemnity

This appeal concerned a number of issues relating to a trustee's right to be indemnified out of trust assets. First, did the right of indemnity confer on a trustee a proprietary interest in trust assets? The Board held that the right did create a proprietary interest in favour of the trustee.

Second, did a trustee's proprietary interest survive the transfer of trust assets to a successor trustee? The Board held that the proprietary interest did survive the transfer. The trustee's right of indemnity was to payment out of the trust fund and the court would enforce it by an order for payment out of the fund. It was the consequence of that right that the trustee had a proprietary interest in the trust property.

Third, did a former trustee's proprietary interest take priority over the equivalent interests of successor trustees? As between equitable proprietary interests, the default rule was that the first in time should prevail. However, The majority of the Board held that current and former trustees' rights of indemnity rank pari passu. While the "first-in-time rule" was an established rule of equity, equitable remedies were ultimately flexible ones which could be fashioned and adapted to meet new problems. Equity would recognise trustees' rights as ranking equally because the trustees had suffered a shared misfortune. It did not matter that the pari passu rule was now part of a statutory code – the principles in the insolvency legislation emerge from the general law. There was inherent justice in equal division, or, in the case of an inadequate fund, in equal sharing in a common misfortune.

Fourth, did a trustee's indemnity extend to the costs of proving its claim against the trust if the claims to indemnity exceeded the value of the trust fund? A trustee's right of indemnity extended to costs incurred in proceedings brought by or against a trustee in its capacity as trustee, provided that there was no misconduct on the trustee's part. There was no basis for suggesting that that principle did not apply to the costs of proceedings brought by a trustee to establish a right to indemnity in respect of particular liabilities, or for suggesting that it did not extend to such costs incurred after the trustee's replacement.

Sport

DIGESTED BY ROSEANNA DARCY

AC Sports Wiltshire LLC v Swindon Town Football Company Limited

[2022] EWHC 2071 (Ch) (Deputy ICC Judge Baister)
25 July 2022

Football • Winding-up Petitions • Sham Agreements • Abuse of process

A winding up petition was presented by AC Sports Wiltshire LLC ("AC Sports") against Swindon Town Football Company Limited ("Swindon Town") based on an alleged debt of £109,094.52 pursuant to a loan agreement. Swindon Town disputed the debt asserting that (i) the loan agreement was a sham, and (ii) the petition was presented for a collateral purpose and so amounted to an abuse of process.

For an agreement to be a sham it is necessary to show that it was intended to give the appearance of creating, as between the parties, legal rights and obligations which different from those (if any) which the parties truly intended to have effect (Snook v London and West Riding Investments Ltd [1967] 2 QB 786). As to an abuse of process, there will only be an abuse where the petitioner (i) does not really want to obtain the liquidation of the company but instead issues the proceedings to put pressure on the company to take some action which the company is otherwise unwilling to take, and (ii) does want the achieve the relief sought but this is not within the interests of creditors as a whole (Maud v Aabar Block Sarl [2015] BPIR 819).

In reaching a decision, the Judge did not consider that there was any abuse of process. The evidence presented was thin and it could not be said that AC Sports was acting other than in the interests of the general body of creditors. Similarly the Judge did not consider that the loan agreement was a sham and the points taken by Swindon Town were described as "scraping the bottom of the barrel".

However, based on the facts of the case, it became clear that the particulars of the petition were incorrect. A subsequent oral agreement suspended the obligation to repay for a period of time, with the loan being treated differently over time. This resulted in a lack of clarity concerning the petition debt and its true contractual basis. The Judge suspected that further facts might emerge if full and proper disclosure were given and witnesses were cross-examined. Swindon Town were entitled to properly test AC Sports' case which it could not do in a summary proceeding. The debt was therefore capable of being disputed on grounds of sufficient substance to dismiss the petition.

Re Cardiff City Football Club (Holdings) Ltd

[2022] EWHC 2023 (Ch) (Adam Johnson J)
29 July 2022

Football • Unfair prejudice

A minority shareholder in the holding company of Cardiff City Football Club petitioned for relief under s.994 of the Companies Act 2006 asserting that the company's affairs had been conducted in a manner which had caused him unfair prejudice. In particular, an offer of shares made in 2018 resulted in the majority shareholder (and first respondent) being the only shareholder to take up the offer, which in turn increased his shareholding whilst reducing the petitioner's. The petitioner asserted that the majority shareholders had been the chief orchestrator of the offer and had acted out of personal animosity to him, rather than for a proper business purpose. The majority shareholder rejected this, relying on his offer for the shares improving the company's balance sheet as he had also agreed to write off approximately £67 million which the company owed him, an amount he had publicly committed to reducing.

The petition was dismissed. Whilst Adam Johnson J accepted that the majority shareholder had mixed motives in orchestrating the offer, it nevertheless made commercial sense and it made good on the majority shareholder's pledge to reduce the company's indebtedness to him. Also, and significantly, the conduct of the majority shareholder did not amount to unfair prejudice. S.994 will only be engaged where "the company' affairs are or have been conducted" in an unfairly prejudicial manner (emphasis added). Applying Re Unisoft Group Ltd (No 3) [1994] BCC 766, there is a distinction between the conduct of a company and the conduct of a shareholder in their private capacity. Only the former will be within s.994. As the majority shareholder had acted in his private capacity as a shareholder his conduct could not amount to unfair prejudice, even if he had been motivated by vindictiveness towards the petitioner.

New Member of Chambers

South Square is delighted to welcome Rabin Kok as a full Member of Chambers following successful completion of his pupillage here.

Rabin joined South Square as a pupil in October 2021. He topped his year at Cambridge University and subsequently graduated with a First Class degree in Law and as a Senior Scholar of Peterhouse. He went on to read for the Bachelor of Civil Law at Oxford, graduating with a Distinction. He won several mooting titles while in Cambridge – including the Oxford vs Cambridge Intervarsity Advocacy Cup and a 2nd place at the Willem C Vis Moot 2018.

Rabin is developing a practice in insolvency, civil fraud, company and financial disputes – both in England & Wales and offshore. His current and recent led instructions include: defending a Middle Eastern financial institution against conspiracy, fraudulent trading and UAE law claims by the administrators of NMC Healthcare (exceeding US$700 million), acting for ISAM Group entities in the IS Prime v Think litigation, placing the sanctioned UK airline CargoLogicAir into administration, and in an ICDR arbitration over a billion-dollar joint venture.

As a pupil, Rabin assisted with a number of cases notable for both their facts and legal complexity, including *Croxen & Ors v GEMA* [2022] EWHC 2826 (Ch) on the interaction between unjust enrichment and the energy regulatory regime; *Vneshprombank LLC and Kireeva v Bedzhamov* [2022] EWHC 1166 (Ch) which related to a £1.34 billion proprietary freezing order and established that a trustee in bankruptcy has an arguable proprietary claim to a bankrupt's assets; and the US$440m *Softbank v Credit Suisse* litigation.

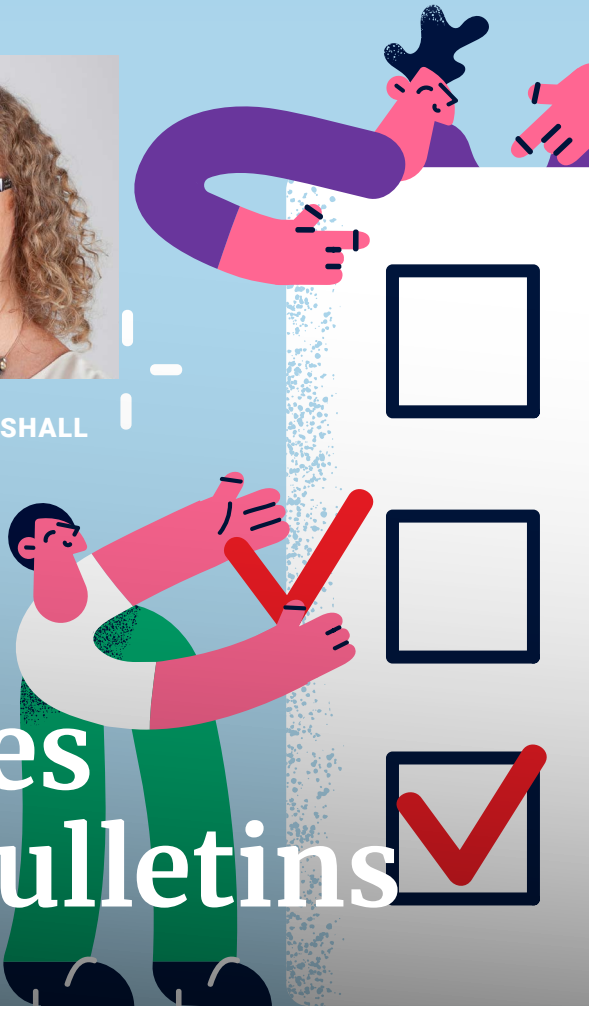
Rabin is also comfortable appearing as sole counsel in the English courts. He regularly appears in the Insolvency and Companies Court in London, in the District Registries of the Business and Property Courts, and the County Court.

He currently acts unled advising on a claim for an equitable interest in foreign property, and has full rights of audience in the Astana International Financial Centre (AIFC).

PROFESSOR SARAH PATERSON
LSE

INGA WEST
COUNSEL
ASHURST

JENNIFER MARSHALL
PARTNER
ALLEN & OVERY



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MARK PHILLIPS KC, PAST PRESIDENT OF THE ILA

It is a strange but incontrovertible fact that many of us are drawn to round numbers. In a recent podcast Adam Alter, a professor of marketing and psychology at New York University, described them as 'very powerful' and 'very visible'.[1] And so it is that the publication of the Insolvency Lawyers' Association (ILA) 1,000th Technical Bulletin seemed a worthy occasion to look back and celebrate where the ILA has been and to look ahead and celebrate what is to come.

The *Concise Oxford English Dictionary* defines 'an Association' as an 'organised body of persons for a joint purpose'. When the Insolvency Lawyers' Association ("**ILA**") was formed in 1989, its founding members were part of an institutional structure which would have supported, and given substance to, this idea of joint purpose. Although law firms competed, competition was relatively genteel. By and large, clients still selected their 'house' solicitors and instructed them on most, if not all, of their matters, and solicitors built up close relationships with members of the Bar whom they regularly instructed. Retiring partners passed a good portfolio of clients to new partners, and senior barristers

1. Christopher Intagliata (Host), 9 April 2015, '10, 50, 100: Why Do We Find Comfort in Round Numbers' thepulse WHYY PBS https://whyy.org/segments/10-50-100-why-do-we-find-comfort-in-round-numbers/.

were able to pass work to their junior colleagues. In other words, firms and barristers were secure in their sphere of influence.

At the same time, many firms' clients raised finance in a tightly knit clearing bank market. A significant number of large companies relied on syndicated or club loans as a principal source of external finance. The 1990s was the era of the 'London Approach',[2] which comprised a set of principles that set out how banks were expected to behave to facilitate the successful restructuring of financially distressed companies. It was developed by the Bank of England following the experience of the secondary banking crisis in the 1970s and relied for its enforceability in the 1980s on the metaphorical 'Governor's eyebrows'. However by the time the Association was formed the Bank of England was stepping back from this role. Nevertheless, the 'London Approach' continued to dictate market practice in the tight financing world of the time because bank lenders feared exclusion from future syndicates if they did not play by the customary rules. This meant that, for the first decade of the Association's life, large corporate restructuring in England was a largely informal affair, negotiated around the table with the 'London Approach' providing the stick to motivate bargaining and agreement. If a restructuring could not be agreed, then resort was usually had to a formal insolvency procedure. It was common to trade the business in insolvency, and generally the aim was to achieve a sale of the business and assets as a going concern. Insolvency practitioners developed their own close ties with the leading clearers and could be assured of a regular flow of work from their relationship bank.

> "Congratulations to the ILA, what an amazing organisation you are and a huge thanks to the Technical Committee and the Presidents (past and present) for what you have selflessly created and the contribution to insolvency and restructuring: onwards and upwards!"
>
> **RITA LOWE, PAST PRESIDENT OF THE ILA**

At the smaller end of the market, relationship banking continued to flourish. It was likely that a smaller business relied on a single bank for working capital support and had a bank relationship manager who acted as the first port of call at signs of trouble. As a result, the bank was motivated both to try to retain its client and to preserve its own public reputation and deals were frequently struck to buy debtors more time.

Overall, then, this was a relatively simple world. But dramatic organisational and institutional change was afoot. New entrants into the finance market, notably distressed debt traders, had different incentives and the 'London Approach' largely lost its force. Lenders became more diverse and harder to locate, and restructuring, as well as insolvency, often required a legal process. The idea of the leveraged capital structure began to gain real traction in the UK so that large financially distressed clients now had complex capital structures made up of layers of debt with equally complex legal documentation governing them. And small business banking became steadily less profitable and more challenging. In the non-financial corporate world the shareholder value revolution, the development of executive compensation designed to align directors' and shareholders' incentives and promotion by merit rather than longevity have revolutionised the world of work.

2. For an excellent overview, see Pen Kent, 'The London Approach' (1993) Q1 Bank of England Quarterly Bulletin 110.

It is not surprising that these changes in the proximate fields of the financial and corporate markets have had a profound effect on the legal world, with increasing levels of specialisation, greater employment mobility between firms, client loyalty no longer a given, and fierce competition on price.

All of which means that the world in which we now work is profoundly different from the world when the ILA was founded. There is much to be celebrated in this new world: some of the biases of the past have fallen away; clients may achieve a better financial deal; and the world of work is undoubtedly intellectually stimulating and financially rewarding. But it poses challenges too. Indeed, the practice of law is a 24/7 endeavour with less space for outside interests, including civic and charitable interests; to use the words of the sociologist Richard Sennett negotiation can feel like 'aggressive opinion-pushing rather than real give-and-take discussion';[3] and the work itself is more complex giving rise to a greater potential for serious error in an increasingly litigious world.

And growing complexity does not stop there. Insolvency law is immeasurably more complex now than it was in 1989. Precisely because most financially distressed debtors were able to reach accommodations with their syndicate or relationship bank through contract, in 1989 insolvency law was largely reserved for cases where the debtor was considered unviable or where there had been a complete breakdown of trust between banker(s) and customer. This arguably began to change in in the early 2000s and it is no surprise that that is when ILA Technical Bulletins began, with one of the first emails to members covering the landmark decision on directors' duties in *Continental Assurance* in 2001.[4] Since then, insolvency and restructuring practice has changed considerably and professionals have continued to adapt (and in some cases ingeniously contort) insolvency and, increasingly, restructuring law to serve their clients' interests.

The law which has emerged from this process of adaptation is complex, fragmented and, arguably, in some places lacking in coherence. Back in 1989 the confident practitioner could enter the meeting room armed only with their edition of Sealy and Milman's annotated guide,[5] and be reasonably confident that they were suitably equipped for the challenge ahead. Since then, numerous government consultations have resulted in multiple pieces of primary and secondary legislation and a sprawling field has emerged which it is exceptionally difficult to stay on top of. In an article in 2006, John Armour and Adrian Walters commented that:

'… insolvency law has developed in the haphazard manner of a medieval building, with new parts being added to existing ones without much concern for the coherence of the resulting edifice or whether the foundations will take the weight.'[6]

If this description was true in 2006, it has only become more apt in the nearly 2 decades which have followed. Crown preference has gone and returned;[7] Britain has been part of the European Insolvency regime and has left it;[8] transaction avoidance claims have been limited to liquidators and become capable of being brought by administrators and of being assigned;[9] creditor meetings have been all but abolished;[10] and creditors have gained significantly more say in insolvency practitioners' remuneration.[11] We could go on (and on). Suffice to say that the relatively straightforward legislative landscape of 1989 has been replaced by something considerably more mountainous and difficult to navigate. The reforms of the Corporate Insolvency and Governance Act 2020 (the "**CIGA**") scarcely did anything to smooth the way and recent consultation on changes to cross border insolvency law, to which the ILA submitted a substantive response,[12] suggests that this highly dynamic field is unlikely to receive a legislative pause any time soon.

"The thing that always struck me about the Association was the collegiality and friendship among members of Council and across the wider membership and I think this was and has always been the glue that has helped the Association achieve all that it is today. No egos, ready to have a laugh but always with sleeves rolled up."

PHILLIP HERTZ, PAST PRESIDENT OF THE ILA

3. Richard Sennett, Together: The Rituals, Pleasures and Politics of Cooperation (2012).

4. Technical Bulletin 1. All Technical Bulletins referred to are available in the members' section of the ILA website ilauk.org

5. Sealy & Milman: Annotated Guide to the Insolvency Legislation now in its 25th edition and co-authored by Professor David Milman and Peter Bailey.

6. John Armour and Adrian Walters, 'Funding Liquidation: A Functional View' (2006) 122 LQR 295.

7. Abolished by the Enterprise Act 2002, s 251 and 252 and reintroduced by the Finance Act 2020, s 98 and 99.

8. Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast) which largely ceased to apply in Britain at the end of the Brexit transition period.

9. Small Business, Enterprise and Employment Act 2015, s 117-119.

10. Ibid., s 122.

11. Part 18 of Insolvency Rules 2016 which replaced the Insolvency (Amendment) Rules 2015.

12. ILA.6.10.22.UNCITRAL_Consultation_Response_FINAL(402620081_.1)_.pdf (ilauk.com).

"The 1994 Annual Conference organised by Peter Totty set a formidable standard. For me, the highlight was Gabriel Moss QC speaking on the subject of fixed charges on book debts and sparking a three-way debate between himself, Sir Peter Millett and Professor Roy Goode which left most of us gasping for air!"

HAMISH ANDERSON, PAST PRESIDENT OF THE ILA

This world of complex legislative change has been matched by equally seminal moments in the case law. Of course, the collapse of Lehman gave us a raft of crucial cases on everything from the boundaries of scheme jurisdiction,[13] to the interpretation of crucial provisions in the ISDA Master Agreement,[14] and the Lehman cases still continue. In a series of important judgments, the contours of the scheme as a corporate restructuring tool took shape.[15] Dramatic determinations on cross border insolvency were made in case law.[16] And the capacity to restructure selected liabilities in a Company Voluntary Arrangement finally received judicial attention after many years of market development.[17]

As all these adaptations have occurred, the ILA has continued to adapt and evolve. The idea of "associating" can play a vital role in mitigating some of the challenges in the new world of work; in other words, associating is more relevant today than it has ever been. Associating can provide us with a vital sense of solidarity, and it can remind us of the sheer pleasure of the company of others with similar interests and concerns to our own. It can be both a strategic tool in a rapidly changing and complex world and an end in itself. The ILA annual conference has gone from strength to strength, paused only briefly for the pandemic; adapted rapidly to be delivered virtually in the changed world; and adapted back, with equal speed, to an in-person event at which lawyers could meet and share ideas just as soon as that was possible. The annual dinner has remained an equally important place of "association" but has also adapted and evolved: from a black-tie event; to a "smart" event; to this year's more flexible format.

The Association plays an equally important role in responding to the many consultations which foreshadow legislative reform. It worked with The City of London Law Society Insolvency Law Sub-Committee to respond to the consultation on the proposed legislative reforms in 2018/2019 which preceded the CIGA reforms.[18] Just recently, it has been able to voice considerable concern in the profession about the impact of the National Security and Investment Act 2021 for restructuring and insolvency cases. It took a significant thought leadership role in the pandemic on what has come to be known as 'light touch administration', producing an influential paper on the contours of the technique,[19] and working to promote the protocol developed by a team at South Square which sought to operationalise it.[20] And it has responded to the potentially ground-breaking proposals for the future of insolvency regulation.

13. Technical Bulletin 229.
14. Technical Bulletin 420.
15. Technical Bulletin 220.
16. Technical Bulletin 222.
17. Technical Bulletin 951.
18. ilauk.com/docs/Joint_ILA_and_CLLS_issued_paper_on_legislative_reforms.Feb_2019_.pdf (ILA members' access only).
19. Insolvency Lawyers' Association, 'Changing the Narrative Around Administration' 2 April 2020 available at: https://www.ilauk.com/news-events/news-view/changing-the-narrative-around-administration.
20. Technical Bulletin 1000.

The Association's work on consultations, and its own thought leadership papers, are published on its webpage but may not always be at the top of members' inboxes. This is surely not true of the Technical Bulletins which continue to play such an important role in providing comment on evolving case law. These bulletins provide members with much more than a summary of the facts of the case and the decision. It is the comment section which has come to be seen by many in the market as vital in the complex, fragmented, perhaps occasionally incoherent, and certainly constantly changing landscape within which we now practice restructuring and insolvency law. There have been bulletins on all of the Lehman and other pivotal decisions referred to above as well as on Rubin and New Look CVA. The ILA has also published bulletins on the first UK restructuring plan, the first contested restructuring plan and the first restructuring plan to deal with landlord claims.

> "Having a forum to discuss complex legal and market developments with like-minded people, without the pressures of having to impress or "market" clients, has been invaluable – as has been getting to know, at a social level, other members of the profession."
>
> **JENNIFER MARSHALL, PAST PRESIDENT OF THE ILA**

All of these bulletins are available to members in the members' section of the website. As such, the bulletins archive charts a historical path through insolvency case law and provides an invaluable resource tool. The ILA's 1,000th bulletin covered the important decision in *Re Houst Limited*,[21] which both begins to draw out how very different the English law approach to cross-class cram down is from the US approach and perhaps also charts a path for smaller and medium-sized enterprises to make use of the new Part 26A restructuring plan tool. And a bulletin on the decision in *BTI 2014 LLC v Sequana SA and Ors*[22] will soon be published. It seems extraordinarily fitting that the focus is on directors' duties once again, 20 years after that first bulletin on *Continental Assurance*.

It is true that associating is a more complex endeavour in the twenty-first century than it was in 1989, but that strengthens rather than diminishes the need for, and the role of, the ILA in 2022. This is an Association run by restructuring and insolvency lawyers for restructuring and insolvency lawyers. It provides a space for the members of the community to come together; to support each other; and, quite simply, to reinforce the pride and privilege we all share in working in this crucial area. It continues to represent members' interests when legislative change is on the horizon and is at the forefront of commenting on and highlighting new developments. And, at the beating heart of the Association are all those technical bulletins with perceptive, often prescient, comment on each one. The arrival of the 1,000th bulletin in members' inboxes is truly a landmark for the ILA. We look forward to the next 1,000 bulletins to come.■

21. [2002] EWHC 1961 (Ch). Technical bulletin 1000.

22. [2022] UKSC 25.

"I have always thought that lawyers practising in the world of insolvency and restructuring are very lucky to have the ILA as their professional organisation. Ever since its foundation over 30 years ago, it has provided countless opportunities to improve our understanding of the many developments in our chosen specialism, and it has done so with great learning and panache. The atmosphere of collegiality, and the ability to spend time discussing problems with other like-minded professionals in a forum which has traditionally eschewed all but the most subtle of marketing activity, is one of its great strengths. The technical bulletins are a fine example of the type of work that the ILA does so well. I have no doubt that they will continue to be produced by members who can rest assured that their quality is much appreciated by the many practitioners for whom they are an invaluable resource."

MR. JUSTICE TROWER

GEMMA FREEMAN
COUNSEL
DENTONS (DUBLIN)

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DENTONS (LONDON)

Your restructuring regime or mine?

In July 2021, we put forward many reasons why we see Ireland as an obvious contender for collaboration with the UK in cross-border restructurings in our previous Digest contribution [*Everybody needs good (restructuring) neighbours*]. The case for this is now stronger given the recent changes to the Irish regime under the European Union (Preventative Restructuring) Regulations 2022 SI 380/2022 (the **Regulations**), which bring further similarities with the UK restructuring regime than ever before.

Before the implementation of the Regulations, Ireland already had a number of tried and tested restructuring tools which were broadly in line with the key elements of the Regulations (i.e. a debtor in possession remedy, the ability to implement a cross-class cram-down and the concept of a "relevant alternative" for the purposes of analysing unfair prejudice). These have been utilised in a number of large-scale complex cross-border restructurings to date.[1] Some of the changes made are not radical to these concepts embedded in the Irish examinership regime, which is more than 30 years old. However, we can expect a more streamlined interpretation and approach to the case law between the UK and Ireland when determining issues in our respective processes.

Ireland is the only EU jurisdiction that can avail itself of statutory recognition in the form of foreign recognition assistance under section 426 of the Insolvency Act 1986 to achieve inbound recognition in the UK. This will no doubt be helpful to UK practitioners who, in light of Brexit, are forced to consider other regimes in Europe to overcome recognition issues in other jurisdictions.

While the Regulations are not implemented in England, the addition of the restructuring plan to the UK's restructuring toolbox has aligned its insolvency regime with many of its European neighbours, whilst also maintaining the UK's status as an international restructuring hub. Since its introduction by the Corporate Insolvency and Governance Act 2020 (**CIGA**), there have been 11 restructuring plans sanctioned, and one declined, giving rise to a body of precedent dealing with issues such as treatment of out-of-the-money creditors

and valuation issues in the context of the "relevant alternative" comparator.

Ireland – what has changed?

A detailed explanation of Ireland's restructuring regime is set out in our previous Digest contribution [*Everybody needs good (restructuring) neighbours*]. On 29 July 2022, the European Union (Preventative Restructuring) Regulations 2022 were signed, bringing into effect Directive (EU) 2019/1023 and leading to a number of changes to the examinership legislation under the (Irish) Companies Act 2014 (the **Irish Companies Act**)[2] including the introduction of a "best-interests-of-creditors" test and amendments to voting rights for "out-of-the-money" creditors.

By virtue of the Regulations, the Irish examinership regime now incorporates a "best-interests-of-creditors" test which needs to be considered at two key stages of the examinership process: (i) in preparation for and on petitioning for examinership; and (ii) when seeking confirmation of the examiner's proposals for a scheme of arrangement. While not defined in the Irish Companies Act (or in the Regulations), the best-interests-of-creditors test is defined in the Directive as one which is "*satisfied if no dissenting creditor would be worse off under a restructuring plan than such a creditor would be if the normal ranking of liquidation priorities under national law were applied, either in the event of liquidation, whether piecemeal or by sale as a going concern, or in the event of the next-best-alternative scenario if the restructuring plan were not confirmed*" (emphasis added).

The "best-interests-of-creditors" test is very similar to the "no worse off" test which is part of the cross-class cram-down statutory mechanism under the UK restructuring plan.[3] As in Ireland, when a court is tasked with sanctioning an examiner's proposals for a scheme of arrangement, the English court may exercise its power to sanction a restructuring plan, notwithstanding that it has not been approved by the requisite majority in each meeting of creditors or members. This is provided that the court is satisfied that none of the members of the dissenting class would be any worse off than they would be in the event of the relevant alternative.

Before the Regulations, a petition for Irish examinership needed to be accompanied by an opinion from an independent expert (being either the relevant company's auditor or another person qualified to be appointed as an examiner or liquidator of the company) covering: (i) the reasonableness of a company's prospects of survival; and (ii) whether an attempt to continue the company (in whole or part) "*would be likely to be more advantageous to the members as a whole and the creditors as a whole than a winding-up*" of that company (emphasis added).

By virtue of the Regulations, however, the independent expert must now opine on whether an attempt to continue the undertaking "*meets the best-interest-of-creditors test and would be likely to be more advantageous to the members as a whole than a winding-up of the company*" (emphasis added)[4]. In doing so, the independent expert is now mandated not to limit his or her analysis to a benchmark liquidation scenario, but to broaden this to include a next best alternative scenario for dissenting creditors in the event that the proposals are not sanctioned.

As we have seen from the recent body of Part 26A cases, the relevant alternative is whatever the court considers would be most likely to occur in relation to the company if the restructuring plan were not sanctioned (similar to the "next best alternative scenario" definition in the Directive). The court need only be satisfied as to that alternative scenario on the balance of probabilities (*Virgin Active*[5]). While there is no requirement for an independent expert's opinion to accompany an application under Part 26A, the cases to date have established the critical importance of having thorough valuation evidence to withstand careful interrogation of the relevant alternative before such an application is made.

Alternative scenarios

In contested Part 26A cases, we have seen valuation evidence being filed by dissenters and financial advisers being cross-examined (Virgin Active). What the relevant alternative is will be a question of fact and, as determined by cases in both Ireland and England, it is not necessarily liquidation (as in *DeepOcean*[6]). Other relevant alternatives have included a pre-pack administration sale (*PizzaExpress*[7]), trading insolvency and sale (*Virgin Active*), managed wind-down (*Hurricane*[8]), a receiver controlled workout (*McInerney Homes Limited*[9]) and could include other consensual outcomes e.g. an accelerated M&A. As to the requirement to reflect "*the normal ranking of liquidation priorities under national law*", in the recent case of *Re Houst* we saw the English court held that a departure from the usual priority rule is not, of itself, "*fatal to the success of the plan*"[10].

These are issues with which the examiner typically grappled at sanction stage to show that the proposals were not unfairly prejudicial to any interested party. However, as the independent expert is now obliged to opine on whether the "best-interests-of-creditors" test has been met, this would appear to be a heavier burden than previously existed. A robust next-best-alternative analysis for dissenting creditors at the petition stage may not be possible, or may be purely hypothetical. This could give rise to further challenge about how nuanced this analysis ought to be, which of course will depend on information available to the independent expert at that stage in the process.

Creditors' voting rights

The Regulations have also made significant changes to the way in which creditor voting rights in an Irish examinership have worked to date.

1. *Mallinckrodt plc, Norwegian Air, Cityjet and Re Weatherford Group.*
2. Not all of which will be covered in this article.
3. Section 901(G) CIGA.
4. Amending section 511(3)(g) of the Irish Companies Act.
5. In *Re Virgin Active Holdings Ltd and others* [2021] EWHC 1246 (Ch).
6. In *Re DeepOcean 1 UK Ltd and others* [2021] EWHC 138 (Ch).
7. In *Re PizzaExpress Financing 2 plc* [2020] EWHC 2873 (Ch).
8. In *Re Hurricane Energy Plc* [2021] EWHC 1759 (Ch).
9. In *Re McInerney Homes Limited* [2011] IESC 31.
10. *Re Houst Ltd* [2022] EWHC 1941 (Ch) [30].

Previously, the court could confirm proposals for a compromise or scheme of arrangement if: (i) the proposals were accepted by a simple majority of one class of creditors whose rights would be impaired by the implementation of the proposals; (ii) the court was satisfied that the proposals were fair and equitable in relation to any impaired dissenting class of members or creditors; and (iii) the proposals are not unfairly prejudicial to the interests of any interested party.

The Irish Companies Act now expressly provides that unimpaired creditors cannot vote on an examiner's proposals for a scheme of arrangement.[11] Additionally, while it remains the case in an examinership that approval of only one class of impaired creditors is required (requiring a simple majority in number and value of that creditor class), the examiner cannot count any creditor vote where any such creditor *"would not receive any payment or keep any interest in a liquidation scenario"*.

The position under the Irish Companies Act is similar in scope to Condition B to the cross-class cram-down mechanism under a restructuring plan, requiring an "in-the-money" class to vote in favour. This is a significant departure from the previous position under Irish examinership whereby "out-of-the-money" impaired classes would typically vote in favour of the proposals (and could therefore be the single class relied upon for sanction purposes) by virtue of receiving some dividend, however small, under the proposals. In the UK, the position of "out-of-the-money" creditors goes even further in that, where the court is satisfied that a class of creditors or members has no genuine economic interest in the company, the court may order for that class of creditors or members to be excluded from the plan meeting(s).[12]

This change with respect to "out-of-the-money" creditors' voting rights is likely to lead to greater scrutiny on behalf of both the examiner, when formulating his or her proposals, and the court on issues of class composition. In this specific context, some wariness on behalf of the English courts has been shown on the issue of class manipulation and engineering classes in such a way so as to create an artificial class group of "in-the-money" creditors to vote in favour of a plan (for example, with a group of creditors who would have been prepared to enter into a consensual arrangement to restructure their rights). In Re Houst, the court warned against the temptation of plan proponents to artificially "create an in-the-money class for the purposes of providing an anchor to activate the cross-class cram-down power ...".[13]

11. *Section 540(4A) of the Irish Companies Act.*

12. *Section 901(C) CIGA.*

13. *Re Houst Ltd [2022] EWHC 1941 (Ch) [20].*

Potential for further valuation and disclosure battles?

At the heart of restructurings is a valuation analysis that the company is worth more continuing as a going concern than being liquidated.

In the case of restructuring plans under Part 26A, the burden is on the plan proponent, typically the company, to establish the "no worse off" test on the balance of probabilities. In Irish examinership, the examiner formulates proposals, having undertaken an investigation of the company on its viability and sought out bids for investment. The examiner has the burden of proving that the proposals do not unfairly prejudice the interests of creditors. As an independent officer of the court, the examiner is under a duty to consider all external bids. Even where the senior lenders and the company have reached a consensual deal to restructure the company's debts, or where that class has otherwise established a plan for the enforcement of its security, the examiner must still consider any bids received from third parties during the process and decide, using his or her commercial judgement, which is the optimum bid to ensure the company's survival and pass the legal thresholds for creditor and court approval.

Questions of valuation and the "next best"/ "relevant" alternative are critical to the sanction of any scheme or plan which imposes a cram-down. Valuation issues also come into focus where active members or creditors want greater scrutiny and disclosure on where value breaks to prove potential recoveries in alternatives in order to have a seat at the table for negotiating and ultimately voting power in respect of the proposals. The courts in each jurisdiction have, through a number of cases, given guidance for opposing creditors and plan proponents on how valuation disputes and disclosure issues that arise during the process will be dealt with. For example:

- While there is a balancing exercise to ensure that "...the potential utility of Part 26A is not undermined by lengthy valuation disputes", it is clear that "the protection for dissenting creditors given by the 'no worse off' test (and the Court's general discretion) must be preserved" (Virgin Active).[14]

- Opposing creditors or members should raise issues at the convening stage rather than postpone their objection to sanction stage for tactical reasons and act expediently to request any financial information, if seeking to deploy such information in expert evidence (Smile Telecoms[15]).

- With regard to disclosure issues, plan proponents should "co-operate in the timely provision of information". Where the information is commercially sensitive, confidentiality undertakings are usually provided (Virgin Active).

  It has been acknowledged in the context of restructuring plans that "it would be most unfortunate if Part 26A plans were to become the subject of frequent interlocutory disputes".[16] However, the English courts have demonstrated that the practicalities of providing information in a compressed timeframe can be overcome. In Virgin Active, the court ordered the submission of witness evidence, response evidence, a pre-trial hearing and a sanction hearing to take place over a bank holiday weekend so as not to disrupt an ambitious plan timetable.

- Given the very short statutory timeline (currently up to 150 days) in Irish examinership within which the examiner must present his or her proposals to court for sanction, as a practical matter, interlocutories and other pre-trial procedures such as discovery must be pragmatically dealt with. While an examinership deadline is tight, the importance of cross-examination, particularly where there are wildly conflicting versions of facts deposed to on affidavit, has been underlined by examinership case law (*Re McInerney Homes*). On seeking further information from an examiner on materials which are already before the court, to date the examiner, as an officer of the court, has been entitled to rely on his or her commercial judgement on whether this should be provided. Unless such a decision falls foul of the Edennote utterly unreasonable/ absurd standard, it is unlikely to be interfered with (*Re Ladbrokes (Irl) Ltd*).[17]

Ipso facto clauses

Another important harmonious development between the two jurisdictions is the introduction in Ireland of a ban on creditors withholding, terminating, accelerating or modifying an executory contract when a company is in examinership, solely because the company is in examinership. The ban is not limited to an "essential executory contract" and remains in place for as long as the company is in examinership and under court protection.[18] Prior to the Regulations, a party was allowed to terminate or modify contracts upon the occurrence of certain events of default, such as a counterparty's insolvency or examinership.

Under English law, a new section 233B of the Insolvency Act introduced by CIGA similarly restricts a supplier of goods or services to a company in a formal rescue or other insolvency procedure (but not schemes of arrangement) to vary or terminate the contract by virtue of that company's entry into a formal process. As in Ireland, the supplier is prohibited from demanding payment of outstanding pre-insolvency liabilities as a condition of continuing supply. If the supplier was entitled to terminate before the company went into an insolvency process, it cannot exercise that right during such process.

14. *Re Virgin Active Holdings Ltd and others [2021] EWHC 1246 (Ch) [130].*

15. *Re Smile Telecoms Holdings Ltd [2022] EWHC 740 (Ch).*

16. *Re Virgin Active Holdings Ltd and others [2021] EWHC 1246 (Ch) [131].*

17. *Re Ladbrokes (Irl) Ltd & Ors [2015] IEHC 381.*

18. *Section 520A(1) and 520A(2) of the Irish Companies Act.*

However, unlike the position in Ireland, termination in England is possible if the company or an insolvency office holder agrees, or the court finds, that continuation of the contract would cause the supplier "hardship". Section 233B supplements the pre-existing regime under section 233A which provides that an insolvency-related termination of contract for the supply of "essential goods or services" ceases to have effect when a company enters administration or CVA, where suppliers are able to demand a personal guarantee from the officeholder for post-insolvency charges.

While there is a corresponding prohibition on an examiner from terminating a contract solely because the company is in examinership, it remains to be seen to what extent the ban on ipso facto clauses will be successfully challenged by counterparties. Underpinning the ban is a policy of corporate rescue being implemented throughout Europe. It is emboldened by another example of a derogation from the principle of contractual freedom in the Irish examinership regime, namely the company's power to repudiate executory contracts during the process.[19] In order for a company to avail itself of the power to repudiate in an examinership: (i) the contract must be executory (i.e. one where some element of performance other than the payment of money remains); and (ii) the company needs to establish that the repudiation is necessary in order to formulate proposals for a scheme of arrangement or the survival of the company as a going concern. In essence, the company must be in a position to prove that its survival will be prejudiced if the repudiation is not effected.

Given that a company's right to repudiate a contract under the examinership legislation has previously survived challenges based on, among other things, an infringement of property rights (*Re Linen Supply Ireland Ltd*[20]), we expect that Regulation's introduction into Irish law of a ban on ipso facto clauses to similarly survive any such challenge.

Directors' duties on insolvency or likely insolvency

The Regulations have introduced into the Irish Companies Act a new statutory duty on directors who "believe" or who have "reasonable cause to believe" that a company is or is likely to be unable to pay its debts (under both an as-they-fall-due test or balance sheet insolvency test).[21] Under Irish law, such directors are required to "have regard to", among other things, "*the interests of creditors*" and "*the need to take steps to avoid insolvency*". This duty is expressed to be owed by directors to the company "*and the company alone*" and is enforceable in the same way as any other fiduciary duty owed to a company by its directors (e.g. by derivative action). Before now, a duty to have regard to creditor interests in a company's insolvency or likely insolvency existed at common law only and as to whom precisely this duty was owed was not as clear.

In English law, the general duties owed by a director to the company are codified in sections 171 to 177 of the Companies Act 2006, based on certain common law rules and equitable principles relating to directors. Section 172(1) of the Companies Act requires directors to act

19. *Section 537 of the Irish Companies Act.*

20. *In Re Linen Supply Ireland Ltd [2010] IEHC 28.*

21. *Section 22A of the Irish Companies Act.*

in the way that they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole. Section 172(3) makes the duty under section 172(1) "*subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company*". At common law, directors are required, as part of their fiduciary duties to the company, to consider, and in some cases prioritise over shareholder interests, creditor interests under what is known as the "creditors' interests duty" or the rule in *West Mercia*.[22]

The existence of the "creditors' interests duty", its trigger point and scope was recently considered by the Supreme Court in Sequana.[23] The Supreme Court confirmed that the "creditors' interests duty" arises when directors know or ought to know the company is insolvent or bordering on insolvency, or insolvent liquidation or administration is probable. Where the "creditors' interests duty" is triggered, directors must give consideration and weight to creditor interests in a manner that is appropriate or proportionate to the circumstances of the company. This must be balanced against other stakeholders, including members. However, once insolvency is inevitable, creditors' interests are paramount.

In both jurisdictions, the subjectivity of a director's knowledge or belief of a company's insolvency or likely insolvency will invariably raise issues, as will the question of what giving "consideration to" or "having regard to" actually means in the context of creditors' interests. Recent case law in Ireland has attempted to answer the latter (albeit in a different context) finding that "*having regard to implies looking at the matter concerned and factoring in its relevance, if any, and weight, if any, as those matters appear to the decision-maker*" and that "*expressions like consider, take into account and have regard to all mean the same thing*".[24]

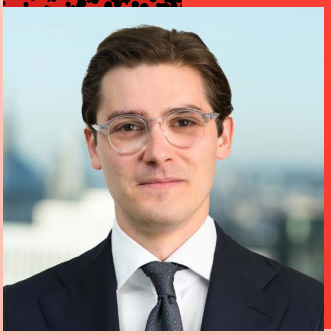
Neighbourly cooperation

England and Ireland are common law English-speaking jurisdictions with highly regarded judicial systems and specialist practitioners on both sides of the Irish Sea. The sophistication of our respective restructuring regimes has been borne out by a considerable body of significant cross-border restructuring cases in recent years. For UK processes, a parallel process with a European jurisdiction may be required in order to secure pan-European recognition. An Irish insolvency process is the only European process that can avail of statutory recognition in the UK under section 426(4) of the Insolvency Act 1986. The similarities between and robustness of our respective processes should give ample scope to working together in troubling times. ■

22. *West Mercia Safetywear Ltd v Dodd [1988] BCLC 250.*

23. *BTI 2014 LLC v Sequana SA [2022] UKSC 25.*

24. *Cork County Council v Minister for Local Government, Planning and others [2021] IEHC 683.*



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The Excluded Asset Gap: Why floating charges capture realisations of unsecured assets

Introduction

Will the proceeds of the sale of an asset, excluded from the scope of a floating charge, be captured by that charge when sold by an insolvency practitioner? The answer turns upon the "Excluded Asset" definition in the floating charge and poses a key normative question with practical consequences for lenders, insolvency officeholders and other creditors. If the proceeds from the realisation of an excluded asset are captured by the floating charge and distributed to the debenture-holder, the value of their security will be significantly enhanced, and the effect of the exclusion of assets from the charge will be reduced considerably in insolvency. By contrast, unsecured creditors will lose out.

We suggest that there exists a poorly understood lacuna which, in principle, could entitle debenture-holders to the proceeds of assets, even where excluded from the scope of a floating charge, when sold by insolvency practitioners (the "**Excluded Asset Gap**"). Professional advisers should consider the Excluded Asset Gap when designing and drafting security packages. To understand how the Excluded Asset Gap arises in many security agreements, a hypothetical scenario will be posed. Using this scenario as the backdrop, this article will consider the law of floating charges and the interaction between floating charges and company assets following (i) crystallisation and (ii) an insolvency process. Both factors will be crucial in understanding why a floating charge can capture the sale proceeds of an excluded asset.

The Scenario

Suppose a company, "**NewCo**", has entered into a debt financing arrangement with its lender (the "**Lender**").

1. *Re Yorkshire Woolcombers* [1903] 2 Ch 284.

2. *See Holroyd v Marshall* (1862) 10 H.L. Cas. 191 for floating charges over future property.

The Lender requires a security package as collateral, and the parties enter into an English law-governed debenture (the "**Debenture**"). The Debenture purports to create a floating charge over all or substantially all of NewCo's assets "*both present and future (including assets expressed to be charged under the Debenture)*" (the "**Floating Charge**"). The parties agree to exclude from the scope of the Floating Charge certain assets, such as shares held by NewCo in a joint venture company (the "**Shares**"). NewCo enters administration. NewCo's administrators implement a transaction resulting in the sale of the Shares to a third party (the "**Realisation**"). The Shares are not captured by the terms of the Floating Charge over NewCo's assets and are defined as Excluded Assets under the security agreement. Does the Floating Charge nevertheless catch the proceeds of the Realisation?

Floating Charges: Post-Crystallisation Receipts

A floating charge captures assets within a class of assets[1] (both present and future)[2] and allows the security provider to use those assets in the ordinary course of business.[3] A floating charge will cover property within a specified class even if assets within the class are acquired after the appointment of an administrator or where the charge has crystallised. The charge "floats above" the class of assets, allowing individual assets within that class to come and go within the scope of the charge without encumbrances.[4] Unlike a fixed charge, which binds to the underlying asset itself, it is the *class* of assets that remains subject to the floating charge; in the ordinary course of business, the underlying assets can be disposed of free of the floating charge.

It is also tolerably clear that floating charges over all or substantially all of a company's assets will capture property acquired even after crystallisation of the floating charge (and the appointment of insolvency officeholders), provided that the property falls within the class of assets as defined by the charge.[5] Crystallisation affects who has control over the disposal of the assets free of the charges, and not whether the charge captures new, future assets.

The Excluded Asset Gap

A clause in a debenture which appears to limit the assets over which a floating charge applies will not capture the proceeds of a realisation unless the terms of the debenture extends specifically to the proceeds of any realisation, regardless of whether the realisations were made before or after the administration. When charged assets are realised, they are not necessarily treated in the same way in the security package perimeter as was their progenitor. An asset not subject to a floating charge (because it falls outside the class of assets to which the charge applies) will, when converted or exchanged so that the new asset falls within the class of assets, fall within the scope of the floating charge.

By way of example, in a grain warehousing business subject to a floating charge, the floating charge will capture purchased grain delivered to the warehouse, even where the charge has crystallised. This would be the case even though the cash used to acquire the grain came from a bank account and was excluded from the floating charge's scope. The substantive effect would be that the effective value transfer – from cash into grain – has resulted in a net gain for the floating charge holder at that given time.

This proposition is supported by authority. In *N.W. Robbie & Co Ltd v Witney Warehouse Co Ltd*, after the appointment of a receiver and manager, a company sold £1,251 worth of goods on credit to the defendants (and £852 worth of goods from the defendant's subsidiary). It was held that the debt "*belonging to the company became thus assigned in equity to the debenture-holders, at times when the defendants had no cross-claim of any kind against the company and consequently no right of set-off*".[6] The High Court of Australia followed the decision in *Ferrier & Australian Factors (Qld) Pty v Bottomor* (1972) 126 CLR 597;Menzies J accepting the proposition "*that a deed creating a floating charge upon present and future assets does operate to charge assets coming to the company after the debenture has crystallized*".[7] Thus, any cash received in the administration by NewCo will be captured by the Floating Charge even if the Floating Charge crystallised on the appointment of the administrators.

So, then, does administration change the nature of the sale of the Shares (and the receipt of cash in exchange) such that the Floating Charge is precluded from capturing the cash? In *Mineral & Chemical Traders Pty Ltd v T Tymczyszym Pty Ltd*, the Supreme Court of New South Wales addressed this question head on.[8] The defendant company had given a floating charge over its assets and undertaking to the plaintiff. The defendant sold part of its business in return for shares,

3. See *Ashborder BV v Green Gas Power Ltd* [2004] EWHC 1517 (Ch).

4. This remains the case post-crystallisation where a company is in administration: see Insolvency Act 1986, Schedule B1, paragraph 70.

5. See *Lightman & Moss on The Law of Administrators and Receivers of Companies* (6th ed), at paragraph 3-100; and *Gough: Company Charges* (2nd ed), at paragraph 6.22.

6. [1963] 1 WLR 1324 at 1338.

7. Ibid, para 17 at p.610.

8. (1994) 15 ACSR 398.

and the terms of the charge were then varied so that the charge would not extend to the shares. The defendant later entered liquidation, and the liquidator sold the shares.

The plaintiff claimed that the proceeds of the sale came within the floating charge. Santow J agreed: the terms of the charge expressly included future property and it was well established that "*such a charge may cover future assets which come into existence after crystallisation*".[9]

Three propositions can be drawn from the above case law. First, a floating charge will capture future assets whose description falls within its defined scope. Second, where an excluded asset is sold in exchange for consideration within a floating charge's scope, the consideration will become subject to the floating charge. Finally, a floating charge will capture the proceeds of an asset within its scope even after administration has commenced.

In the scenario identified above, an Excluded Asset Gap is inherent in a floating charge. An excluded asset will necessarily be excluded from the security package, but the proceeds of the realisation of that asset will, in principle, fall within the scope of the security.

Should Insolvency Change the Position?

As a matter of law, the insolvency of NewCo does not change the scope of a floating charge. Criticisms that the Floating Charge should not capture the proceeds are related to the nature of floating charges; it is insufficient to suggest that cash mixed into a general bank account would remain an Excluded Asset simply because, at some time, its value was converted from an Excluded Asset. The temporally-related argument that any proceeds of Excluded Assets sold in insolvency ought to remain excluded relies on the idea that the occurrence of the administration changes the treatment of Excluded Asset proceeds. This does not reflect the law of floating charges. The actions of the NewCo administrators have – on the surface – increased the return to secured creditors at the expense of the returns provided to unsecured creditors. The secured creditors may be regarded as having received a windfall, while the unsecured creditors are deprived of an asset they reasonably considered to be unencumbered. An administration does not affect the ability of a floating charge to capture new assets acquired or exchanged in the administration. What is it, then, about administration which might change the treatment of proceeds?

In our example, as the Shares are Excluded Assets, one argument is that they should not form part of the 'bucket' used to pay secured creditors. This assumes that assets which will be used to fill those buckets have crystallised – i.e. if an asset is unsecured at the time of administration, it can only be used to satisfy unsecured creditors. No actions by the administrators can result in that asset being re-characterised and becoming subject to a floating charge. The proceeds of a secured asset realised by the administration should remain 'ear-marked' for secured creditors so that any underlying Excluded Assets remain excluded from the security.

Yet this is doctrinally incorrect. The obligation to distribute proceeds of a secured asset to the debenture-holder depends on the proprietary rights a charge holder has in the assets. Fixed Charge assets do not form part of the estate.[10] Where a creditor has a proprietary interest in an asset, and the asset is sold by an insolvency practitioner with the

9. See *Ashborder BV v Green Gas Power Ltd* [2004] EWHC 1517 (Ch).

10. This remains the case post-crystallisation where a company is in administration: see Insolvency Act 1986, Schedule B1, paragraph 70.

express permission of the secured creditor, that creditor is entitled to an account of the realisations made in respect of the asset because of their proprietary rights.[11] By contrast, the unsecured creditors hold no proprietary interest in the Shares, and their disposal does not require consent nor do their proceeds demand ear-marking. If the parties had intended to exclude *proceeds* from a floating charge, they would need to maintain the cash in a separate bank account, segregated from the company's funds.[12]

Which assets will be used to 'fill' the different 'buckets' for creditor classes must be determined at the distribution stage, rather than at the administrator's appointment. The fact that a floating charge may continue to operate in administration suggests that the proper time for assessing the proverbial 'shape' of the relevant buckets is a matter of contractual interpretation taking place at the end or after administration, i.e. the relevant time for determining the contents of the floating charge is tallied on declaring a final dividend to creditors since the floating charge's scope remains subject to the priority waterfall.[13]

For interim dividends, where the Shares are sold after the interim dividend, but before final distribution, their proceeds would be subject to the floating charge despite not being subject to the floating charge at the interim stage. The floating charge would, in theory, continue until the floating charge creditor's claim (or the prescribed part) was fully satisfied. In the same way, the practical effect will be that any realisations by an insolvency officeholder's actions of so-called 'Excluded Assets' would be captured by a floating charge.

Addressing the Excluded Asset Gap

Many English law security agreement precedents do not account for the Excluded Asset Gap and result in proceeds of Excluded Assets becoming caught by the Floating Charge. Unless an Excluded Asset definition includes words indicating the contrary, the proceeds of an Excluded Asset can – and indeed should – form part of the security interests of a lender. For instance, some debentures are defined to include "related rights" of an Excluded Asset within the class of "excluded assets" but to exclude "related rights" only insofar as they require third-party consent. That is, for the reasons discussed above, insufficient.

Given this, what should parties do to ensure their intentions are appropriately reflected when formulating security packages? Crucially, parties need to ensure that they have fully considered the consequences of insolvency on the scope of Excluded Assets. Insolvency is, after all, when that security package will matter most. If parties truly intend for assets and their proceeds to be excluded from the security package, then it will be crucial to ensure that the Excluded Asset definition is defined correctly. A good draughtsman would specify that Excluded Assets include: (i) the Shares specifically and their proceeds *irrespective* of whether the Shares require third-party consent; and (ii) any Excluded Asset realisations are paid into a specific, designated bank account which is itself defined as an Excluded Asset. Invariably, the secured lender will want the proceeds of the sale of an Excluded Asset to be caught by a floating charge, and it should therefore be incumbent upon the lender's lawyers to ensure the definition of Excluded Assets is drafted with the default position under the general law firmly in mind.

Unsecured creditors will be anxious to give Excluded Assets a broad meaning, and an unclear definition will lead many to gauge credit risk incorrectly.[14] Unsecured creditors of NewCo may argue that the sale proceeds are 'related rights' of an Excluded Asset, and therefore the proceeds of the Excluded Asset would also be excluded. It might also be said that the proceeds of Excluded Assets realised in insolvency should remain earmarked only for unsecured creditors. This is particularly so given that the publication of security packages on the Company's Register is "*intended for the protection of the creditors of an insolvent company*" by providing "*persons dealing with a company the opportunity to discover [...] whether its assets were burdened by [...] charges which would reduce the amount available for unsecured creditors in a liquidation.*"

Insolvency practitioners should seek to assess the scope of the Excluded Asset definition at the distribution stage. Given that the Excluded Asset Gap will affect the quantum earmarked for both secured and unsecured creditors, they should consider this in advance. Along with their legal advisors, insolvency practitioners will want to understand the impact of the definition on distributions to creditors, given that their actions may disproportionately benefit the unsecured creditors *pro-rata* at the direct expense of the secured creditors who benefit from the floating charge.

Conclusion

The "*Excluded Assets*" wording in English-law security agreements often suffers from an Excluded Asset Gap: they do not always capture the proceeds of Excluded Assets. An Excluded Asset definition that does not consider the location of the proceeds of the asset will likely result in the Excluded Asset Gap occurring, which will directly benefit the lenders. Parties to security agreements and insolvency practitioners alike should closely scrutinise the drafting of the Excluded Assets definition to ensure minimal disruption when distributions occur following an insolvency event.

Insolvency practitioners should make this assessment before the distribution of the estate. If an insolvency practitioner incorrectly assumes that the proceeds of an Excluded Asset remain excluded their decision may give rise to a claim by secured creditors regarding the loss incurred by their actions. Lenders, too, should be weary of insolvency practitioners intuitively believing that proceeds of Excluded Assets remain excluded. This will likely result in material losses in recovery by the lenders. ■

11. See *Lightman & Moss on The Law of Administrators and Receivers of Companies* (6th ed), at paragraph 3-100; and *Gough: Company Charges* (2nd ed), at paragraph 6.22.

12. [1963] 1 WLR 1324 at 1338.

13. Ibid, para 17 at p.610.

14. (1994) 15 ACSR 398.

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Muir Hunter,

His family background, influences and early years

SIMON MORTIMORE KC

Muir Vane Skerrett Hunter (1913–2008) was called to the Bar in 1938 and joined Cyril Salmon QC's chambers at 3 Paper Buildings in 1954, after moving from 3 King's Bench Walk, which he had joined shortly before the outbreak of World War II.

He became head of chambers in 1959 and remained head for about 25 years. He remained a member of chambers, actively involved in insolvency law, for many years after the chambers moved to South Square in 1989. This article describes Muir's family background, early life, political activity, the start of his career at the Bar, and his war service in India. It ends in 1946 when Muir returned to England to resume his career as a barrister.

Muir's career as a barrister and a legal reformer, with a deep concern for due process, truth, fairness, and justice was heavily influenced by his family background; his education; his involvement in the politics of the 1930s at Oxford, as aid worker in the Spanish Civil War, and as a Labour Party candidate; and by his wartime service as a military judge in India dealing with bribery and corruption cases. From these influences came the single-minded passion to fight his case and the drive to right what he saw as injustices, whether in individual cases or more generally by reforming the law. Muir was not just a barrister who specialised in bankruptcy law and who came to national attention through his work on the Poulson case (*Digest* March 2021, pages 80–95 and July 2021, pages 90–105).

His practice as a barrister was the springboard for his work as a reformer of the law (notably through his membership of the Cork Committee, whose report influenced the reforms brought into effect by the Insolvency Act 1986); his work to bring justice to the disadvantaged (establishing in North Kensington the first neighbourhood law centre); and his work in trials overseas for Amnesty International and Justice.

Muir Hunter's family background

Muir was immensely proud of his parents and their families. He grew up in a home which valued literature, languages, social justice, and equality, and which took an active interest in politics and world affairs. Muir took his first name from his paternal grandfather, John Muir Hunter (1844–1920), who was a lieutenant-colonel in the Bombay Staff Corps of the Indian Army and was made a Companion of the Star of India. Muir proudly displayed the Star of India in his room in 3 Paper Buildings. Muir's father, Hugh Stewart Hunter (1880–1960) seemed destined to follow his father in a military career. He won a Military Exhibition to Wellington College, where he excelled in languages. Although he was entered for Sandhurst, he did not go there. Instead, in 1903 Hugh Hunter joined the civil service in London; first in the Inland Revenue's Estate Duty Office, from 1911 in the National Health Insurance Commission, and from 1921 in the Ministry of Health, where he was a principal clerk and later head of the Intelligence Department. During the two world wars, doubtless because of his skill with languages, Hugh was deployed as chief organiser of the Prisoners of War Bureau set up by the War Office.

Muir took his third name from his maternal grandmother's family, the Skerretts of County Clare, one of the Fourteen Tribes of Galway, who had lived on the west coast of Ireland since the thirteenth century. Muir's maternal great-grandfather, William Joseph Skerrett (1818–78), lived at Finavara House, an imposing late eighteenth-century house overlooking Muckinish Bay, from where he farmed 2,000 acres and hunted. He was a Justice of the Peace and Deputy Lieutenant of County Clare. He and his wife did their best to secure the continuation of the Skerrett family line; there were ten sons and four daughters. But the males died young, and the last male grandchild, a monk, died in a monastery in Belgium in 1936. Meanwhile Finavara and the land had long-since been sold or abandoned. Muir's maternal grandmother, Matilda Anne (1849–1928) was

Hugh Hunter is seated 2nd right in Wellington College, house photograph, 1898

William Joseph Skerrett's seventh child. She was brought up by her aunt, who had been unable to have children, in Florence. It was there, in 1868, that Matilda Anne met Muir's maternal grandfather, George Douglas Williams (1839–1910), a journalist employed by the Reuters news agency.

George Douglas was the son of George T Williams, a gentleman of leisure who loved the classics and could speak French, Italian and Spanish. Although George T Williams obtained a law degree, became a member of the Inner Temple, and acquired chambers in the Temple, which he retained until his death, he did not practice as a barrister. He used his chambers as a convenient place to entertain friends with oysters and porter after a visit to the theatre.

George Douglas joined Reuters' City office at the age of twenty. He was sent to Florence, where he reported on steps towards the reunification of Italy, and then to Paris, where he witnessed the Franco-Prussian war, the signing of the Treaty of Versailles, and the brief Communard take-over of Paris. In 1874, he returned to Reuters' City office, where he became chief editor; a post he held until he retired in 1902.

George Douglas and Matilda Anne Skerrett married in a Roman Catholic Church in Dublin in 1871 and spent most of their married life in the Notting Hill area of Kensington, which was where Muir's mother, Matilda Ann (1877–1960), was born. Matilda Ann, who called herself Bluebell, became an independent-minded "New Woman" of the type depicted by her friend HG Wells in his novel *Ann Veronica*. Determined to make her own way in the world, Bluebell established an office in Bloomsbury where she and other women provided a typing service for writers including WB Yeats and George Bernard Shaw.

In September 1905, Hugh Hunter married Bluebell at a ceremony in a Roman Catholic Church in North Kensington. They had four daughters and one son, Muir, who was born on 19 August 1913 at 1 Mitcham Park, Lower Mitcham in Greater London. By this stage Bluebell had given up the typing office. Instead, she wrote serials for women's magazines and became one of the most widely read of all serial writers. Her earnings from writing provided a valuable supplement to the family budget. In 1919, the Hunter family moved to Kensington, where Hugh and Bluebell would remain for the rest of their lives.

Bluebell was always close to her younger brothers, Valentine (1883–1946) and Douglas (1892–1975), who followed their father into journalism. At the beginning of World War I, they were accredited correspondents reporting from the front line in Flanders; Valentine for the Daily Mail and Douglas for Reuters. They both joined up, were wounded in battle, and were awarded the Military Cross for gallantry. After the War, they returned to journalism. Douglas became chief editor of Reuters, the position his father had held; but after a couple of years as editor, he moved to New York as America correspondent for Reuters and, later, for the Daily Telegraph. Valentine left the Daily Mail in 1922 to pursue a more varied career. This included some reporting; he was the first person to report the discovery of Tutankhamun's tomb, he interviewed Presidents Coolidge and Roosevelt, and in 1937 he reported on the coronation of George VI for American radio. But his main activity was writing novels ("shockers" as he called them). His first novel, written when he was recovering from war wounds, was *The Man with the Clubfoot*, about Dr Adolph Grundt, a perfidious and cunning German, whose evil designs are thwarted by Desmond Okewood, a young British officer. His many novels included more Clubfoot stories and others featuring such characters as Baron Alexis de Bahl (The Fox)

and the Savile Row tailor and amateur detective, Mr Treadgold. He also wrote radio plays, in some of which he acted with his wife, and film scripts, including the script for the film *A Dispatch from Reuters*, which was released in the United States in 1940 and starred Edward G Robinson as Baron de Reuter.

Muir at Westminster School

In September 1925, at the age of 12, Muir went to Westminster School as a weekly border in Rigaud's house. Westminster was, and is, a school with strong connections with the Abbey and the monarchy. It had been re-founded by Queen Elizabeth I in 1560. The School's regulations provided that religious instruction should be "*in accordance with the doctrine and formularities of the Church of England*" and that all boys should attend Abbey for a short service every weekday morning, unless exempted by the headmaster. In addition, in accordance with a proviso to the Act of Uniformity 1662, once every week, all boys attend Latin Prayers, which were spoken or sung in Westminster Latin, a form of medieval English scholastic pronunciation, which satisfied Queen Elizabeth I's command that Latin should not be spoken in the monkish fashion. During Muir's time at Westminster, the headmaster was The Reverend Dr Harold Costley-White, who was appointed Chaplain to George V in 1932. When Muir was at the school, boys wore top hats and tails.

Muir excelled at classics, the core subject at the school, and won several prizes for classics and poetry. In July 1929, as Muir was approaching his sixteenth birthday, his father wrote to Christ Church College, Oxford, to enter Muir for the examination for a Classics Scholarship. To confirm Muir's enthusiasm for the classics, Hugh Hunter reported that Muir was reading Aristophanes' *The Frogs*, Sophocles' *Oedipus Tyrannus* and Virgil's *Bucolics*. Another work that apparently engaged Muir's interest was Cicero's *In Verrem*; speeches made in 70 BC during the trial of Gaius Verres, the former governor of Sicily, on charges of corruption and extortion (vices that Muir would encounter during his career as a lawyer). On the application form, Hugh Hunter said that Muir intended a career at the Bar. Muir's housemaster informed Christ Church that Muir "*has good wits and should do well at Oxford*". In December 1931, Muir duly won a Classics Scholarship to Christ Church. Even in later life, Muir felt that his academic achievements at Westminster were undervalued by the headmaster, because he was a Catholic.

Muir at Christ Church

Muir arrived at Oxford to read classics in October 1932. In November 1933, Muir was admitted to Gray's Inn so that he could start eating the dinners required for him to be called to the Bar. In February 1936, Muir won a Slade Exhibition, a classical scholarship in philosophy and ancient history. That summer, he took a second-class degree in his finals, which was perhaps not the glorious result for which his father might have hoped.

There were too many distractions at Oxford for Muir to devote himself exclusively to studying the classics. He immediately joined the Oxford Union, as did Peter Pain (1913-2003), his contemporary at Westminster and Christ Church, who would become a barrister, specialising in industrial relations cases, and a High Court judge. Whereas Peter Pain immediately involved himself in the Union, regularly speaking at debates – always supporting the left-wing viewpoint – and, in June 1933, becoming a member of the Union's standing committee under the presidency of Michael Foot (the future leader of the Labour Party), Muir proceeded more cautiously. This may have been because Muir had arrived at Oxford as a supporter of Liberalism, which, after the collapse of Lloyd George's government in 1922, was an unfashionable viewpoint. In debates in November 1932 and January 1933, the Union endorsed motions asserting that socialism offered the only solution to the country's problems, and that there was no future in British Liberalism.

On 9 February 1933, during Muir's second term, the Oxford Union held its *King and Country* debate, in which the motion "*this House will in no circumstances fight for its King and country*" was passed by 275 votes to 153. This vote in support of pacifism caused outrage in traditional circles. A black box containing 275 white feathers was sent to the president of the Union. The following week, without meeting any resistance from Union officers and members, some 30 or 40 undergraduates, who objected to the Union being sullied by the record of the offending resolution, ripped the resolution from the minute book and tore it into 30 pieces. Prince Leonid Lieven, who witness the scene, was dismayed: "*Although you may not have been willing to fight for King and country, I think you might have fought for the society's minute book.*"

Westminster School, Little Deans Yard

The resolution of 9 February was re-written into the minute book. The following month, Lord Stanley and Randolph Churchill moved that the resolution of 9 February be expunged, but their motion was lost by 138 votes to 612.

In a well-attended debate on 12 October 1933, at the beginning of his second year, Muir spoke in support of the motion that "*the revival of liberalism offers the only safeguard against dictatorship and war in Europe*". Peter Pain spoke against the motion which was lost by 251 votes to 281. By then Muir was exploring the full range of progressive politics: he supported and involved himself in the efforts of the League of Nations Union and New Commonwealth Society to secure peace through collective security and disarmament. On the domestic and economic front, he was attracted by the moderate proposals for social and economic reform promoted by the Next Five years Group and Lloyd George's Council of Action. Towards the end of his time at Oxford, Muir joined the Labour Party and started his move towards the political left.

On leaving Oxford, Muir's ambition was to follow the familiar twin paths of the Bar and politics. He decided to delay his start at the Bar to pursue a political opportunity; but first he would travel to China, where his mother was researching a series of novels.

Bluebell's novels and Muir's visit to China

Towards the end of the 1920s, Bluebell moved from writing magazine articles and serials to writing more substantial novels. She appreciated, no doubt reluctantly, that she stood a better chance of being recognised if she adopted a male nom de plume. She used the names "Boris M Hunter", "John Guildford", and, for two books on which Muir collaborated, "George Lancing". Since the George Lancing books became popular successes, she used that name for her subsequent novels written without Muir's collaboration. While Muir was at Christ Church, Bluebell used to come to his rooms to write.

The themes of the two books written by George Lancing in Christ Church – *Infamous Conduct* (1934) and *Fraudulent Conversion: A Romance of the Gold Standard* (1935) – reflect Muir's interests in law, economics and politics, and his enthusiasm for curing injustices. Indeed, Muir described himself as co-author of *Fraudulent Conversion*, and adopted the persona of George Lancing when he wrote letters to the Daily Herald to protest about the plight of the unemployed in the north of England that he had witnessed and to advertise a short play he had written about the Spanish Civil War.

Infamous Conduct concerned the power that the General Medical Council held over the private lives of members of the medical profession. If it came to the notice of the GMC that a doctor had committed adultery or eloped with a patient, he would be charged with infamous conduct in a professional respect and, if the charge were proved, his name would be erased from the register of practitioners without right of appeal and he would be professionally ruined, unable to practice in Britain and the Empire. In the early 1930s, there were several such cases, but the most notorious of these cases, and the one which probably inspired George Lancing's book, was the case of the gynaecologist Dr Harold Burt-White who was charged with maintaining a secret and improper relationship with a patient against the wishes of her husband who was a well-known solicitor, Harold Bevir (described in my article in the *Digest*, July 2019). In George Lancing's book, a young female doctor fell in love with the husband of one of her patients. The case did not reach the divorce courts, but it came to the attention of the implacable GMC. The reader's sympathy is with the female doctor and the object of her love, a thoroughly admirable King's Counsel (who like Muir was the son of a well-to-do civil servant and had been brought up in Kensington), who had the misfortune to be married to a woman who is portrayed as unattractive and hysterical. Reviews of the book ranged from "*one of the most outstanding books of fiction produced this year*", "*excellently written and expertly developed*" to dismay at Mr Lancing's "*tawdry style*".

In March 1935, The Times advertised the publication of *Fraudulent Conversion* as an important novel by the author of *Infamous Conduct*, with a commendation from the literary critic of the Daily Herald, who described it as "*an original, well-planned and continually interesting novel*". The novel was a satire about the gold standard and capitalism and a commentary on the policies of Major CH Douglas concerning paper money and social credit (a national dividend for all citizens to supplement earnings), which inspired the short-lived Green Shirt Party for Social Credit, whose members wore green shirts as party uniform until political uniforms were outlawed by the Public Order Act 1936.[1] The novel features Professor Ambrose Worlidge, an unworldly medieval historian and expert in the Plantagenet period, who is struck on the head by a falling branch as he walks through Hyde Park after attending a lecture by a speaker who promoted Major CH Douglas's policies. While the Professor is lying in a daze, a little man in green reveals to him the secret of making gold sovereigns from beech leaves. The catch is that the sovereigns must be spent within 12 hours. With his newly found powers, the Professor ends wage slavery and poverty and causes economic mayhem. One reviewer called the book stimulating, another called it "*an engrossing and extremely well-written novel … An admirable story deftly handled*", but another, while finding the book "*very amusing and instructive*", thought it would divide readers between those that thought it very good and those that thought it a "*coarse and common book*".

Bluebell's next literary project was a series of novels about the life of the Empress Dowager T'z-hsi (or Cixi), who controlled the Chinese government from behind the curtain for 47 years between 1861 and her death in 1908. Although the years of her rule are regarded as reactionary and marred by decadence, corruption and cruelty, the Empress Dowager would have appealed to Bluebell. She was a strong-willed woman who had made use of her charms, brains, and literacy to exercise power in a male-dominated world.

1. CH Douglas (1879-1952) developed his ideas in three books: *Economic Democracy* (1920), *Credit-Power and Democracy* (1920) and *Social Credit* (1924, revised 1934). His ideas were influential in Canada, Australia, New Zealand, and Japan.

The main source of information about the life of the Empress Dowager, available in England in the 1930s, which Bluebell read, was *China Under the Empress Dowager* (1910) by Sir Edmund Backhouse, a British oriental scholar and Sinologist, and JOP Bland, a Times journalist. The authors claimed that their book was based on the diary of Ching-shan, a senior official in the Imperial Household, which Backhouse had found when he had rented the house where Ching-shan had lived until he was murdered by his son who pushed him down the well in the courtyard of the house. Since then, it has been conclusively proved that the alleged diaries are forgeries created by Backhouse, whose account of life at the Empress Dowager's court cannot be relied upon.[2]

Bluebell was not to know that Backhouse and Bland's book was based on forged diaries. At all events, Bluebell decided that she must go to China to see Peking (Beijing) for herself and conduct her own research. At the end of November 1935, Bluebell travelled by ship to Shanghai with her youngest daughter Roseanne, who was then aged fifteen. Bluebell pursued her research in Peking with great thoroughness. She visited the Empress Dowager's private apartments in the Summer Palace, met surviving members of the royal family, and built up a detailed picture of the late Manchu Imperial court with the help from "*gifted Chinese friends*", who introduced her to the Chinese histories and romances, which provided the historical detail deployed in her books and the source of her characters and dialogue.

At the end of July 1936, having finished his last term at Oxford, Muir travelled by ship to join his mother and help her with her research. While in Peking, he took the opportunity to meet HH Kung (Kung Hsiang-hsi), who was then Minister of Finance and Governor of the Central Bank of China, and other Kuomintang (Nationalist Party) leaders. For Muir there would have been much to discuss and learn about economic policies and the rising tensions with Japan, which already controlled Manchuria and would attack Peking and other Chinese cities the following year.

After a few weeks, Muir returned to England by way of the USSR and the trans-Siberian railway. He was home by the end of October.

The first of George Lancing's novels about the Empress Dowager, *Lotus Blossom*, was published in 1939 and received favourable notices in The Times and Daily Mirror. Publication of the four other novels about the Empress Dowager (*Imperial Motherhood, The Mating of the Dragon, Dragon in Chains, and Phoenix Triumphant*) was delayed until after the end of the War.

The Labour Party candidate for the Petersfield constituency

In the spring holidays before his last term at Oxford, Muir presented himself as a potential Labour Party candidate for the Petersfield constituency. He could be considered a local man, since his parents had a cottage at Headley within the constituency. The disadvantage of the seat was that it was a Conservative Party stronghold. It had returned a Conservative Member of Parliament at every election since 1892 and would go on doing so until 1983, when it became the East Hampshire constituency, another safe Conservative seat. At the general election held in November 1935, when the Conservative dominated National Government had won a majority of 245, the Conservative candidate, Major Reginald Dorman-Smith had defeated the Labour Party candidate, Lionel Birch, in a straight fight by 79.1% to 20.9% of the vote. After suffering such a massive defeat, Birch declined to fight the next election for the Labour Party. It would take a miracle to unseat Major Dorman-Smith, the president of the National Farmers Union, in his rural constituency. Muir took to the challenge with his usual vigour; after all he was concerned for the disadvantaged farm workers who outnumbered the farmers. Even if Muir failed to win the seat, he would at least establish a toehold in national politics.

Between April and July 1936, Muir made speeches and answered questions at several Labour Party meetings in the constituency. His knowledge of politics and economics and his plans

2. Bluebell acknowledged this source in the preface to Lotus Blossom. In 1936, William Lewisohn, a British journalist in Peking, published an article exposing flaws in the diaries: they were historically inaccurate or incredible, they included pastiches of published material and, most compellingly, Ching-shan was known to be stone-deaf and could not have heard the conversations apparently transcribed in his diaries. In 1991, Lo Hui-min, an academic, published clear proof that the diaries were forgeries. By then Backhouse's reputation as a scholar was in tatters; see Hugh Trevor Roper's *The Hermit of Peking* (1976), which exposed Backhouse as a serial fraudster and fantasist.

to galvanise support for the Party so impressed the local Party that in August 1936, it adopted him as its official candidate for the constituency at the next general election, which was expected to be held in 1939 or 1940. He was described as a "*young man with a brilliant record*" who intended to practice at the Bar. The Party released a photograph of Muir: he looks confident and studious, with his black-rimmed glasses and dark swept back hair. He wears a heavy dark suit with wide lapels, a white shirt and sober tie.

In September 1936, shortly before Muir returned from his trip to China, an event occurred that might transform his electoral prospects. Mrs Muriel Grace Whinfield, the formidable wife of a retired colonel, a breeder of prize-winning silver foxes, and the long-serving chairman of the Alton Women's Branch of the East Hants Conservative and Unionist Association, announced her resignation from the Association. She could no longer supported the Government and had joined the Fascist Party, founded by Sir Oswald Mosley in 1932. At the beginning of December, the Fascist Party announced that Mrs Whinfield was its prospective Parliamentary candidate for Petersfield. This raised the prospect of a split in the vote of the right between the Conservatives and Fascists, which would enable the Labour Party, with its attractive policies for peace and for improving conditions for agricultural workers, to emerge as the winner. That at least was the optimistic opinion of the vanquished Lionel Birch, who was impressed by Muir's ability as a candidate.

Muir's first meeting with constituents after his return from China took place in Headley on 5 December. It was attended by two distinguished members of the Labour movement. One was Lord Passfield (formerly Sidney Webb), a local resident, one of the first members of the Fabian Society and a minister in Ramsay MacDonald's Governments. The other was DN Pritt KC MP (Claude Duveen's pupil-master, *Digest* July 2019) who earlier in the year had represented John Marchbank, a trade union official, at the trial of a libel action brought by Mosley at which the jury expressed its contempt for Mosley by awarding him one farthing in damages. Both Passfield and Pritt were enthusiastic supporters of Stalin's rule in the USSR. With his wife, Beatrice Webb, Passfield had written *Soviet Communism: a new civilisation?* (1935). In August 1936, Pritt had attended the trial in Moscow of Zinoviev, Kamenev and fourteen others on charges of conspiring to kill Stalin and other members of the Soviet Government. The defendants had made fulsome confessions, were found guilty and executed. On his return to England, Pritt published *The Zinoviev Trial* in which he defended the fairness of the proceedings from ill-informed and "*frankly unscrupulous*" criticism. At the meeting in Headley, both men wisely kept off the subject of the USSR, which would not win any votes in Petersfield. Lord Passfield, who took the chair at the meeting, opened the proceedings by criticising the constituents in Headley for being politically backward, since there were too many army officers and retired people (who took a long time dying), but ended by predicting a bright future for the Labour Party in southern England. DN Pritt spoke about the situation in Spain, where supporters of the Government were fighting for democracy against fascism. Muir also spoke about Spain and then outlined his plans for a big campaign in the villages in the spring. The meeting raised £3 for a fund which would send a food ship to the Spanish people.

At a meeting of the Petersfield Labour Party in February 1937, Muir spoke against the Government's policy of re-armament to deal with the threat from Germany, encouraged the Government to support France, warned against the threat of Fascism in England

(Mrs Whinfield being a prime example), and encouraged the middle-class to join working people in building a free and prosperous country. He ended by assuring the meeting he stood for "*all the interests of the people that really mattered, not the squires, the professional politicians, the Riviera crowd or the financiers, but the interests of every patriotic, sincere and hardworking person who produced the wealth of this great country of ours*".

The Spanish Civil War

Like many on the left, Muir saw the issue in the Spanish Civil War, which had begun in the summer 1936, as a simple fight between democracy and fascism. He volunteered to go to Spain to undertake humanitarian work for the National Joint Committee for Spanish Relief (NJCSR), which had been established in December 1936 by the Duchess of Atholl and others as a non-political organisation to co-ordinate humanitarian aid for the people of Spain. It arranged for buses, lorries, food, and money to be sent to Spain.

On 13 March, Muir left England for Perpignan, on the French side of the border with Spain, to act as liaison officer between the NJCSR and the Spanish Medical Aid Committee, which ran a relief camp at Perpignan. By May, Muir was driving a lorry, with "*for the women and children of Spain from the people of England*" emblazoned on its side, in convoys delivering food to Barcelona, Valencia and Madrid and evacuating women and children from the war zones. In Barcelona, people appeared to him to be well-turned out and happy, despite bread and milk queues and the city being subjected to shelling by Italian warships and bombs being dropped on residential areas. He visited the headquarters of the International Brigade, where he found the men cheerful and courageous, despite losing comrades and relations in the fighting. By the end of June, Muir was back in England. He remained confident that the Republicans would prevail unless Nationalists received more troops and weapons from Germany and Italy, or they resorted to poison gas. George Orwell, who was in Barcelona at the same time, took a more jaundiced view of Republican prospects. He thought that the revolutionary spirit was fading as people were tiring of the war and noted "*an atmosphere of suspicion, fear, uncertainty, and veiled hatred*".

A citadel for the people

Over the next year or so, Muir fully engaged himself in promoting the cause of the Labour Party in Petersfield, while at the same time studying for his Bar examinations. He spoke at numerous meetings and debates in the constituency. A regular theme was peace and the threat of war from Nazi Germany and Japan. He remained an advocate of the League of Nations and collective security and did not believe that Neville Chamberlain's Munich Pact had secured "*peace in our time*". Instead, in his view, Great Britain, France, Russia, and Czechoslovakia should take a collective stand to compel Germany to disarm and, with Italy, withdraw from Spain.


Sir Oswald Mosley

Another subject to which Muir kept returning was agriculture. He supported the Labour Party policy that there should be national control of agricultural land and agricultural prices. To further his participation in agricultural issues, Muir became editor of Country Standard, a political monthly journal, founded in 1935 and sold for one penny, which circulated in agricultural districts and promoted peace and socialism in the countryside. It's banner proclaimed: "*Sharpen the sickle! The fields are white; 'tis the time of the harvest at last.*"

On the broader economic front, Muir explained that the National Government's policies were not working; unemployment was still too high, at 1.5 million; and the Government's only policy for avoiding a slump was by boosting arms production. He supported the Labour Party's programme of reconstruction, which involved nationalising the Bank of England (the fount of the nation's credit), the land (the source of the nation's food), coal, electricity, and gas (the sinews of national industry), and transport (the means of distribution).

On 13 October 1938, at the invitation of Mrs Whinfield, Sir Oswald Mosley gave a speech on the policies of the British Union Party, as the Fascist Party was then called, at the Petersfield Town Hall. He attracted the largest audience ever assembled in that hall. The atmosphere was highly charged and there were constant interruptions and scuffles during his 90-minute speech. Mosley said that the Prime Minister had been courageous to go to Germany, but the fault, which had humiliated the country, had been in getting involved in a dispute between nations which was not our concern. Britain should concentrate on becoming able to feed itself from its own agriculture and trade with the Empire. He favoured returning to Germany its former colonies that had passed to Britain under the Treaty of Versailles, provided Germany did not use them for military purposes. During one scuffle, two men were ejected from the room and, as the audience rose to its feet to see what was going on, Muir shouted: "*Fascist bullies, that is what you are!*" When it came to questions, Muir had so many that Mosley refused to take any more from him, saying:

"You will not have any further answers from me tonight." The meeting ended with the National Anthem and the members of Mosley's Party giving their salute.

To Muir the political future looked bright and exciting. The Labour Party had attractive and sensible policies while the right was split and bereft of answers. Looking to the future, on 25 October 1938, Muir announced that Alton would have a Labour Hall, a modern building, which would be used by the Labour Party, trade unions, the Women's Co-Operative movement, and the Left Book Club. He said: *"We feel that now people are awakening and confronted on all sides by loss of liberties and rights, they must have a citadel where they can rally. Alton Labour Party is providing them with that citadel – a citadel for the people of Alton."*

The Bar and marriage

In July 1938, Muir passed his Bar exams with 2nd class honours. Gray's Inn awarded Muir a valuable Holker Senior Scholarship, worth £200 pa for three years, and gave him a grant of 100 guineas to pay for his pupillage with Charles Erskine Simes, the Recorder of Banbury and a specialist in local government cases, who had chambers at 3 Temple Gardens. In November 1938, Muir was called to the Bar. He joined the Western Circuit, perhaps because it included the Petersfield constituency in Hampshire. In May 1939, Muir joined the chambers of Victor Aronson at 3 King's Bench Walk in the Temple. Aronson was an expert in bankruptcy law, the subject to which Muir would devote his professional career.

In June 1939, Muir became engaged to Dorothy (usually called Dorothea) Verstone (1909-86), the eldest daughter of Philip Eason Verstone, a newspaper proprietor and fellow of the Institute of Journalists. Muir had met Dorothea through their common membership of PEN (poets, essayists, and novelists), the organisation formed in 1921 to support human rights and the freedom of expression of writers throughout the world.

Dorothea's first career was as an actress. In 1927, she obtained a Diploma at RADA and the following year appeared in a leading role in Cyril Campion's *Dope*, which drew "*capital audiences*" at its twice nightly performances at the Grand Theatre, Fulham and then toured provincial theatres for forty weeks. At the end of the following year, Dorothea appeared in *The Lash*, which had a short run in the provinces. By the time she met Muir, Dorothea had changed her career. After taking a course in social administration at the London School of Economics, she became an administrator in social and public services and worked as an almoner at St Mary Abbot's Hospital, Marloes Road, Kensington.


Muir Hunter in uniform

Because it was thought probable that the general election would be held in the autumn of 1939, the wedding was brought forward and the couple were married on 29 July 1939 at Our Lady of the Victories, the Catholic Church in Kensington High Street. The couple lived in a flat in Holland Road, Kensington and at Muir's parents' house at Headley Down.

Dorothea took a keen interest in Muir's practice. She shared his passion for justice and in helping the individual in a battle with the establishment. She often accompanied Muir to court, including trips to foreign courts, and would tell him how she thought the case was going, which points were working, and which were not. At home in the evening, Muir would discuss his cases with Dorothea. An oil portrait of Dorothea looked down on Muir as he worked in his room in 3 Paper Buildings.

The political door closes

Shortly after returning from honeymoon, on 19 August, Muir hosted his second annual Labour Party garden party at Headley Down. It was a happy occasion for over 300 guests.

Muir made a short speech to fire up the Party for the anticipated general election. He introduced his new wife and said that the Women's Section would find Dorothea "*a very able and powerful ally*". After the speeches, the Headley Branch of the East Hants Labour Association presented the Hunters with a tea service.

A fortnight later, on 3 September, Great Britain declared war on Germany. The general election was postponed until after the war was over. By the time it took place in 1945, Muir was still on active service in India and had to withdraw from the contest. The war also brought changes to the fortunes of Sir Reginald Dorman-Smith, who by then was Minister of Agriculture, and Mrs Whinfield. In May 1940, when Churchill became Prime Minister, Dorman-Smith was sacked as a minister and the following year was appointed Governor of Burma (just before it was invaded by the Japanese). Later in May 1940, Mrs Whinfield was interned under Regulation 18B of the Defence (General) Regulations 1939, along with other notorious opponents of the war and sympathisers with Nazi Germany, including Sir Oswald Mosley and Archibald Ramsay MP, the founder of the secret Right Club, whose object was "*to oppose and expose the activities of Organised Jewry*".

A brief start at 3 King's Bench Walk

Muir seems to have got off to a quick start to his career in bankruptcy work. These cases are seldom newsworthy but one, in January 1940, attracted the attention of several regional newspapers. This was a case where Muir obtained a discharge from bankruptcy for a former stockbroker who was serving in the army. He had run debts trying to keep up with the demands of his American wife who had left him, and he had then been caught by the fall in the stock market. The discharge was suspended for 18 months, but, at least, the bankrupt was not required to pay anything to his creditors.

A newly qualified barrister has little if any choice in the clients he is asked to represent. In May 1940, Muir found himself in the Fulham Police Court, before Sir Gervaise Rentoul KC, defending a client who seemed to have had a deep loathing for the Labour Party. James Smith, an unemployed insurance broker,

King's Bench Walk

was charged with unlawfully and wilfully writing in chalk on the front wall of Fulham Town Hall words which were a gross insult to, and intended to vilify, the Labour-controlled Council; namely "*Labour Party rats, J Smith and FEUDL*". Those letters apparently signified the Fulham Employed and Unemployed Defence League. Muir was relieved to discover that the accused denied writing the offending words and claimed that he was set up by one of his enemies. There were two difficulties about this defence. One was that a Council worker apprehended Smith just after he had used a piece of chalk to write the letters FEUDL on a window box at the Town Hall; and the other was that Smith had more pieces of chalk in his pockets. Muir valiantly cross-examined the prosecution witnesses and suggested, as were his instructions, that someone else had done the chalking to frame Smith. Sir Gervaise had no doubt that Smith was the perpetrator of an obvious nuisance and thought "*the whole thing is very silly*". He fined Smith 10 shillings.

In August 1940, Muir joined the Royal Armoured Corp (Royal Tank Regiment) as a private and passed into Sandhurst. In October, before he was immersed in military training, Muir made his first appearance in the Court of Appeal in *Pollock v Charles Burt Ltd* [1941] 1 KB 121, a case about the common law doctrine of common employment. Muir stood in for David Turner-Samuels, who was on military service. David was five years' younger than Muir, had also been to Westminster School, and had married Dorothea's younger sister Norma. Muir and David would be life-long friends and Muir never forgot that David's absence on military service provided him with his first appearance in the law reports. Muir was led in the case by Moss Turner-Samuels, David's father, who had been the junior counsel for the successful plaintiff in the leading House of Lords case of *Radcliffe v Ribble Motor Services* [1939] AC 215. In the words of Lord Denning, Moss Turner-Samuels was "*a hardened warrior*" who "*took every point, good or bad, usually bad*", but in the *Pollock* case there enough good points to deploy without resorting to the bad ones.

In 1937, the common law doctrine of common employment celebrated its centenary. Its function was to protect employers from being sued by an employee for damages for personal injury caused by the negligence of another employee, even though the employer would have been liable to non-employees for the same negligence. In *Priestley v Fowler* (1837) 3 M&W 1, Lord Abinger, siting in the Court of Exchequer, was confronted with a novel case, in which a butcher's servant sued his master for damages. The servant had broken his leg when he was thrown from an overloaded cart driven by a fellow-employee. In holding that the servant had no claim against his master for the fault of his fellow-employee, Lord Abinger summoned up a nightmare vision of what would happen if the law were otherwise. A servant would be able to sue his master for compensation if he was injured by the negligence of another of the master's servants: e.g., a drunken coachman, a chambermaid who puts damp sheets on the bed, an upholsterer who instals "*a crazy bedstead*" which collapses in the night, or a cook who fails to clean the copper vessels or who serves rotten meat. Lord Abinger could not be accused of holding progressive views. As Sir James Scarlett KC MP, he vigorously opposed the Great Reform Bill, as an experiment which would "*effect a great alteration in the nature and character of [the House] and endanger every other institution of which Englishmen had reason to be proud*", by which he meant the Monarchy and the Aristocracy in the House of Lords. Moreover, as the owner of thirty slaves on an estate in Jamaica, until they were emancipated in 1836 and for which he received £626 2s 2d in compensation, he was unlikely to favour a servant's claim against his master.

Twenty years later, in 1858, Chief Baron Pollock enthused that there "*was never a more useful decision, or one of greater practical and social importance in the whole history of the law*". In the same year, the House of Lords confirmed that the doctrine was part of the laws of England and Scotland, when it denied claims for damages brought by dependents of miners who had been killed when the cage in which they were being brought to the surface overturned due to the negligence of the man in charge of the operation. By the end of century, the doctrine was recognised in legislation.[3] It had its critics, most notably the great jurist Sir Frederick Pollock, who called the doctrine "*one of the great mistakes of the Common Law*". In the *Radcliffe* case in 1939, Lord Atkin said that the doctrine was much criticised and unloved but accepted that it was too well-established to be overthrown by judicial decision. Instead, he and the court narrowed the scope of the doctrine so that it only applied if the injured employee and the negligent co-employee were engaged in the same common work, were fellow labourers in the same work, or were engaged in the same departments of duty. This narrowing of the doctrine led to fine distinctions which had little to do with the justice of the case. Indeed, the House of Lords itself vividly illustrated the absurdity of the doctrine as explained in *Radcliffe*. In that case a bus driver succeeded in his claim against his employer for injuries suffered in an accident caused by the negligence of another driver employed by the same company, since, at the time of the accident, the drivers were not driving on prescribed routes, but were making their way back to the depot by routes of their choice. Eight years later, the House of Lords held that a tram company had a defence of common employment to a claim for damages brought by one of its drivers who was injured in a collision caused by the negligence of another of its drivers, since both were travelling on tramlines, which were prescribed routes.[4]

In Muir's case, the plaintiff, Mr Pollock was the manager of the Watford branch of Charles Burt Ltd, furniture dealers. Because the salesman was away, head office instructed Pollock to take his place visiting potential customers in a car driven by one of the head office's drivers. Due to the driver's negligence, there was a collision and Pollock was injured.

He claimed damages from Charles Burt who denied liability because Pollock was in common employment with the driver; they were employed by the same company, participating in company

3. *Vose v Lancashire and Yorkshire Railway Co* (1858) 2 H&N 728; *Bartonshill Coal Co v Reid* (1858) 3 Macq 266; *Bartonshill Coal Co v McGuire* (1858) 3 Macq 300; Employers' Liability Act 1880; Workmen's Compensation Acts 1897-1943.

4. *Graham v Glasgow Corp* [1947] AC 368.

business, and were sitting side by side in the car. At the trial at the end of September 1940, Mr Justice Hilbery accepted that defence and dismissed Mr Pollock's claim. Within one month of that decision, the parties were in the Court of Appeal. Moss Turner-Samuels, leading Muir, persuaded the Court of Appeal, that there was no common employment. Applying the *Radcliffe* guidance, the Court found that the men had come together for a particular task which was outside their normal employment and which they performed in different departments of duty. When Mr Pollock was engaged as branch manager, he could not have imagined he would be driven to visit customers by a driver from head office.

Dealing with defences of common employment would not be a fertile area of practice for Muir when he returned to the Bar from war service, because the defence was abolished by the Law Reform (Personal Injuries) Act 1948. In moving the bill, Sir Hartley Shawcross, Attorney-General, described common employment as "*a notorious and ill-favoured doctrine of common law*".

War service

In May 1941, Muir was commissioned at Sandhurst as a 2nd Lieutenant with the 2nd Royal Gloucestershire Hussars. In September 1941, he passed his examinations at Sandhurst with distinction. By this stage the Royal Gloucestershire Hussars had long since gone to Libya and Egypt to form part of the 22nd Armoured Brigade. In that theatre of war, the regiment suffered such heavy casualties that it was disbanded, and the survivors redeployed in other regiments. Instead, Muir was granted a commission in the 7th Battalion of the King's Own Yorkshire Light Infantry, which in August had sailed to Bombay. This battalion became the 149th Regiment in the Royal Artillery Corp and formed part of the 50th Indian Tank Brigade. Muir joined the regiment while it was undergoing training at Poona. In April 1942, the regiment moved from Poona to Ahmednagar in Maharashtra. In July it moved on to Ranchi in West Bengal in readiness for jungle warfare on the Burma front against the Japanese.

At some stage in 1942, Muir suffered a serious leg injury in an accident when he was riding a military motorbike. He was hospitalised and later transferred from the Tank Brigade to GHQ in New Delhi, where he joined General Staff Intelligence as a captain and undertook legal work. Muir's work seems to have impressed his superiors, because in April 1944, at the age of 30, Muir was promoted to lieutenant-colonel. This rank would give him the appropriate status to sit as a military judge with two civilian judges on special tribunals in Lahore, Rawalpindi, and Karachi, which tried offences of bribery, corruption, and fraud in Government contracts and on the State railways. As Muir explained in a letter to Lord Passfield, the tribunal had "*considerable powers of jurisdiction and protection from appeal, so that we are able to deal out some fairly effective punishments to the parasites who prey upon the Government*". Major Watts was such a parasite. He had bought three Buick cars in India for sale to customers in Persia at a handsome profit for himself. Using his military office and falsely claiming that the cars were for military use, rather than

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for his personal profit, Watts obtained Government petrol for the cars and got the Government to pay for them to be transported by rail from Quetta to Persia. Muir's tribunal sentenced Watts to one year's "*rigorous imprisonment*" and a fine. Muir's work on this tribunal had a lasting effect on him. He would always react strongly to the slightest hint of corruption.

Muir remained in India throughout 1945 and so was unable to take part in the general election of that year in which the Labour Party won a majority of 145 seats. Shortly before the election, Muir met Pandit Nehru and astonished him by confidently predicting a Labour victory. The outcome of the election would have pleased Muir enormously. His disappointment at not being able to take part would have been mitigated by seeing that Petersfield had again returned a Conservative MP.

Return to England

At the beginning of 1946, Muir was finally demobbed, with the right to use the rank lieutenant-colonel.

He returned to family life in England and to resume his career at the Bar at 3 King's Bench Walk. The next article will describe how Muir became a specialist in bankruptcy law at 3 King's Bench Walk, his move to Cyril Salmon QC's chambers at 3 Paper Buildings in 1954 and the history of those chambers after Salmon, Duveen and Potter had all become judges and Muir became head of chambers. ■

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The Times Archive

Who Was Who

Wikipedia

News in Brief

South Square wins Company/ Insolvency Set of the Year

We were absolutely delighted to win once again Company/Insolvency Set of the Year at the Chambers UK Bar Awards, held at Old Billingsgate on the evening of 17 November 2022.

The awards are based on the Chambers UK Bar's research over the past 12 months. We are enormously grateful to all our clients and friends who have supported us once again.

A Royal Visit

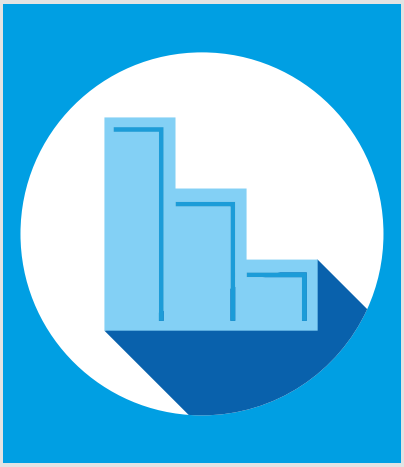
On 23 November 2022 The Honourable Society of Gray's Inn was delighted to welcome their Royal Bencher, His Majesty King Charles III. On arrival, The King was greeted by tenants, staff and residents of the Inn (one of whom was joined by a corgi). His Majesty then met with some of the Inn's Members and staff, including students pursuing a career at the Bar, practising barristers, judges and Benchers. His Majesty was appointed Royal Bencher in 1975.

Photographer: Liz Isles © The Honourable Society of Gray's Inn

First Cayman restructuring officer appointment

On 11 November 2022, Mr Justice Kawaley ordered the first appointment of a restructuring officer (RO) in Re Oriente Group Limited (FSD 231 of 2022) under the new Cayman Islands restructuring regime.

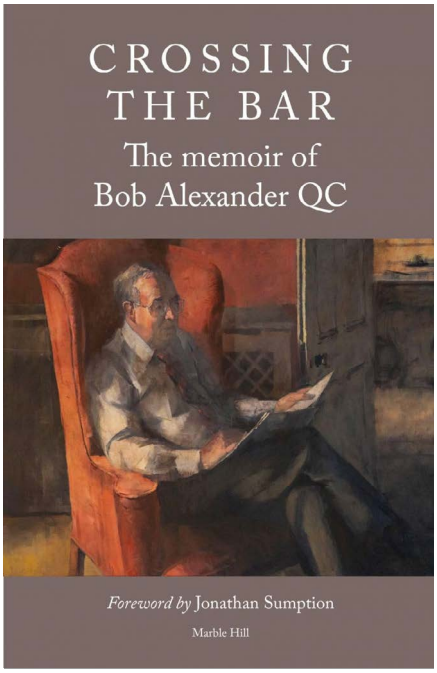
Oriente Group, a Hong-Kong headquartered financial services company, filed the RO petition on 21 October after two of its creditors presented a winding up petition against it. The judge's order granted the appointed ROs (Andrew Morrison and David Griffin of FTI Cayman Islands, and Ken Fung of FTI Hong Kong) powers typically granted in a winding up order, including the power to liaise with legal advisers and creditors, and the power to seek recognition in foreign courts. The order also imposes an initial 28-day reporting deadline for the ROs, with updates to then be filed every three months thereafter, and sets a case management conference four months after the date of the order for the court to assess progress.



Crossing The Bar: Book Launch

The memoir of Lord Alexander of Weedon QC are to be published by Marble Hill in January 2023.

Bob Alexander, a former joint Head of Chambers at South Square, was described by Lord Denning as "*the best barrister of his generation*". A self-made man from the Potteries, Bob's career spanned over a quarter of a century at the Bar, during which time he acted for Kerry Packer against the Test and County Cricket Board, for Geoffrey Collier, the City of London's first convicted insider trader, and for Ian Botham, whom he represented in fighting a suspension from Somerset for bringing cricket into disrepute. Perhaps his most famous case was representing Jeffrey Archer in one of the most sensational libel cases of the last quarter of the 20th century. But Bob Alexander's life also took him from the law to being chairman of the Takeover Panel and NatWest Bank at a critical time when the impact of 'Big Bang' demanded huge changes from many staid financial institutions. Add to that his passion for cricket, his appointment as chairman and then president of the MCC, his chairmanship of the Royal Shakespeare Company, together with his elevation to the peerage, and you have the extraordinarily full life of a man who rose to the very top of the British establishment.



Details of how to purchase Lord Alexander's memoir will appear in the next issue of The Digest.

A Legal Cover Story

The Bar Council report into the state of court buildings in England and Wales revealed that a barrister needed to shelter under an umbrella during a court hearing at Snaresbrook Crown Court, in Greater London, thanks to a leaking roof. It also highlighted a court in Wales where they had only just managed to get rid of an infestation of fleas when the roof caved in.

The report, entitled "Access Denied" also notes that the 239 court closures since 2010 have led to 65 per cent of Parliamentary constituencies without a working court, and therefore without decent access to justice. One barrister told of a litigant who walked for two days to get to court for a family proceeding.

The Bar Council report claims that the ramifications of continuing cuts to the justice system leaves "*a workforce that is tired, cynical and increasingly looking for other sources of employment*".

Islands in the sun

On 8 November South Square was delighted to host our sixth Cayman Islands conference, in association with RISA. The conference comprised three expert panels dealing with sanctions, mediation and the new Cayman Islands restructuring law.

The following week saw Members of Chambers attend the third INSOL seminar in the British Virgin Islands.

It was particularly good to meet friends and colleagues from across the seas in person, rather than via Zoom/Teams: our last visits as a set of Chambers were in November 2019, just a matter of weeks before the Covid pandemic struck.

News in Brief

JCPC sits in Cayman for the First Time

The Judicial Committee of the Privcy Council ('JCPC') sat in the Cayman Islands from 15 to 18 November 2022. This is the first occasion on which the JCPC have sat in an Overseas Territory of the United Kingdom.

The JCPC is the final appellate court for the Cayman Islands and hears appeals of the greatest public or constitutional importance.

The hearings took place in a specially appointed Court (Courtroom 9), a new state-of-the-art courtroom which was in use for the first time.

Cases heard by the JCPC were FamilyMart China Holding Co. Ltd. (Respondent) v Ting Chuan (Cayman Islands) Holding Corporation (Appellant) (Cayman Islands), in which South Square's Hilary Stonefrost appeared; Justin Ramoon (Appellant) v Governor of the Cayman Islands (Respondent); and HEB Enterprises Ltd. and another (Respondents) v Bernice Richards (as Personal Representative of the Estate of Anthony Richards, (Deceased) (Appellant) (Cayman Islands).

In addition to the hearings the Justices engaged in several information-sharing initiatives including a "Court Users" meeting attended by a cross-section of legal practitioners; and a meeting with senior high-school-aged students from University College of the Cayman Islands (Dual Enrolment programme), Cayman Prep. High, and St. Ignatius High, who participated in the JCPC's "Ask a Justice" session.

Onion Defends Right to Parody

Long-running satirical American publication, The Onion, has filed a very real amicus brief with the US Supreme Court to urge it to take on a case centred on the right to parody.

It concerns Anthony Novak who, in 2016 was arrested (but then acquitted) for making a Facebook page that parodied the local police force in Parma, Ohio. Following his acquittal he sued the police department, arguing it was retaliating against him for using his right to free speech.

In May of this year a US appeals court backed the police, a finding which Novak's lawyer said set a dangerous precedent in undermining free speech. The case would be heard next year if the Supreme Court opts to consider it.

In true Onion style, the filing describes the publication as having a readership of 4.3 trillion and "*the single most powerful and influential organization in human history.*"

And the winner is … Manchester!

Lord Reed, President of the Supreme Court, has announced it will be sitting in Manchester in March 2023.

This marks the first time that the court has sat outside one of the four UK capital cities (London – where it has its permanent home, Cardiff, Belfast and Edinburgh).

In his announcement Lord Reed said *"As the final court of appeal for the United Kingdom, we hear cases of profound importance to everyone across the country. My colleagues and I strongly believe that the experience of attending a court hearing in person should not be limited to those able to get to London"*. As with all its hearings, the cases in Manchester will also be live streamed.

Croydon Council Bankrupt Again

Croydon Council has been forced to declare bankruptcy for the third time, issuing a Section 114 notice declaring it cannot balance its budget in the next financial year, with the current mayor – Jason Perry, who gained control of the council in May 2022 – blaming '*toxic historic management*'. The authority first declared bankruptcy in 2020 and was given a £120m bailout loan by central government to balance the books.

Since the first bankruptcy filing, the council has made £90m in savings and £50m in asset sales and has proposals to save £44m during the 2023-24 financial year. It also has about £100m in proposed asset disposals in the coming years.

Joules Files for Insolvency

Joules Group Plc is set to file for insolvency after the British retailer failed to secure bridge financing or raise equity, putting around 1,600 jobs at risk. The clothing chain, known for its colourful coats and Wellington boots, has appointed Interpath Advisory as administrators to protect the interest of creditors.

SOUTH SQUARE CHALLENGE

Welcome to the South Square Challenge – as traditional at this time of year as the Sunday Times Christmas Crossword.

We had no completely correct answers to our previous challenge so it is a roll-over, with the prize being two magnums of champagne and two South Square umbrellas! Your task on this occasion is to correctly identify what the following images represent, and work out the common thread that binds them. Once again, in the event of multiple correct answers the winner will be drawn from the wig tin. Good luck!

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Please send your answers to Kirsten either by e-mail to **Kirstendent@southsquare.com**, or to the address on the back cover, by 31 January 2023.

The correct answers to our September 2022 challenge were:

1. The Children Act, Field Court entrance to Gray's Inn Square
2. Bridget Jones' Baby, Middle Temple Lane
3. Shakespeare in Love, Middle Temple Hall
4. The DaVinci Code, Temple Church, Inner Temple
5. Wonder Woman, Old Square, Lincoln's Inn
6. Suffragette, Entrance to New Square, Lincoln's Inn
7. Poirot, Chapel Undercroft, Lincoln's Inn
8. Pirates of the Caribbean On Stranger Tides, Middle Temple Lane
9. Silk, outside Temple Church, Inner Temple
10. Mary Poppins Returns, Gate 5 to Essex Street, Middle Temple

1.

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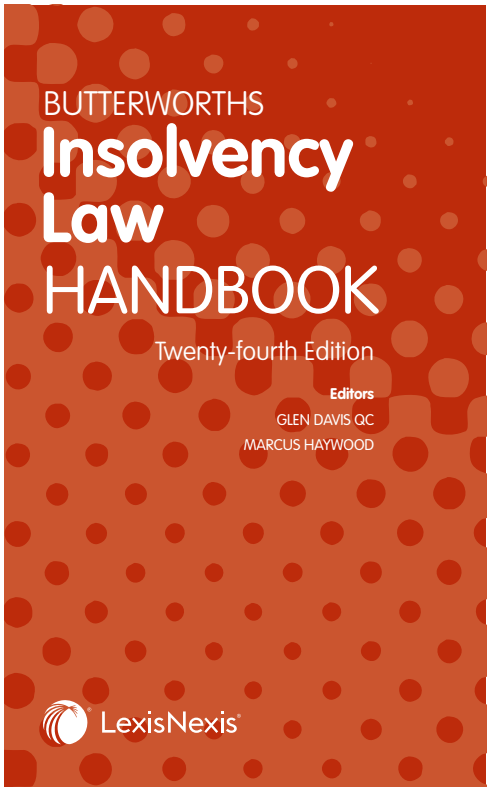
10% discount

Butterworths Insolvency Law Handbook

Twenty-fourth Edition Edited by Glen Davis KC and Marcus Haywood

Butterworths Insolvency Law Handbook is the most comprehensive single collection of statutory source material and practice directions relating to insolvency law in England, Wales and Scotland. It is the essential reference source for lawyers, accountants, insolvency practitioners, regulators and students.



Why Insolvency Law Handbook?

- Have it all covered with the most important statutes, statutory instruments and European legislation
- Advise clients with confidence as legislation is printed as currently in force with all amendments, repeals and revocations
- Save time with detailed, technical annotations regarding commencement as well as cross-references to other legislation, commencement tables and forms tables
- Work more efficiently with a user-friendly, chronological and industry recognised layout

What's New?

The 24th edition of the Handbook incorporates important changes to the insolvency regime in England and Wales, and in Scotland, including:

- Commercial Rent (Coronavirus) Act 2022
- Payment and Electronic Money Institution Insolvency Regulations 2021
- Payment and Electronic Money Institution Insolvency (England and Wales) Rules 2021
- Relevant provisions of the National Security and Investment Act 2021
- Amendments made to the Insolvency (England and Wales) Rules 2016 by the Insolvency (England and Wales) (No 2) (Amendment) Rules 2021 in connection with the moratorium procedure in Part A1 of the Insolvency Act 1986
- Amendments made to the Co-operative and Community Benefit Societies and Credit Unions (Arrangements, Reconstructions and Administration) Order 2014 made by the Co-operative and Community Benefit Societies (Administration) (Amendment) Order 2021
- Amendments made to Company Directors Disqualification Act 1986 by the Rating (Coronavirus) and Directors Disqualification (Dissolved Companies) Act 2021
- Amendments made to the Corporate Insolvency and Governance Act 2020 by the Governance Act 2020 (Coronavirus) (Amendment of Schedule 10) (No 2) Regulations 2021
- The new Temporary Insolvency Practice Direction Supporting the Insolvency Practice Direction

Publication details:

Publication scheduled: May 2022
Formats available:

- Print (paperback): ISBN: 9781474321051 – Price: ~~£252.99~~ £227.69
- Ebook: ISBN: 9781474324212 – Price: ~~£252.99~~ £227.69
- Print + Ebook: ISBN: Z000050926509 – Price: ~~£316.99~~ £285.29

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