A REGULAR REVIEW OF RELEVANT NEWS, CASES AND ARTICLES FROM **SOUTH SQUARE BARRISTERS** NOVEMBER 2013

SOUTH SQUARE DIGEST

A little bit of luck?

Welcome to the November 2013 edition of the Digest. Well that blistering summer is now only a distant memory replaced by the more familiar English diet of grey sky and rain. And it all gets worse with the clocks going back and with us all being plunged into darkness in the middle of the afternoon. Oh well, luckily it will soon be Christmas.

Talking of luck, the economy seems to be having some of it. Whilst I am sure that George Osborne and Mark Carney would probably like to take all the credit – and who is to say they should not – the signs are all looking a bit more positive. Interest rates are to stay low they say. Help to buy is plainly helping. Giving away Royal Mail shares probably helps too. The London housing market just keeps powering ahead. The average price in the country as a whole has reached its highest-ever level. And the IMF has upped the UK's proposed growth figures for 2013 from July's estimate of 0.9% to 1.4% and for 2014 from 1.5% to 1.9%. Long may that trend continue.

So what else has happened over the last three months? Probably the biggest news was Syria. War was on the agenda. Then Cameron lost a vote. And the US didn't look like it wanted war either. But luckily the Russians came to everyone's aid and proposed that the solution was that Syria would give up all its chemical weapons. And everyone, including the US and Syria, agreed. Quite amazing really. Equally amazing is the fact that America was then closed for the first half of October, held to ransom by the Republicans and with a debt default looming that would not have been good for the world. Luckily for the rest of us the US just managed to pull itself back from the abyss at the last minute.

So what delights do we have for you in this edition of the Digest? Well there are lots of articles to enjoy. They start with a joint article by Michael Crystal QC, Adrian Cohen of Clifford Chance and Adam-Al-Attar on thwarting dissentient creditors, in the context of compromises and schemes of arrangement, from taking steps in foreign jurisdictions following the decision of the special tribunal in relation to Dubai World and its subsidiaries. We continue with our new offshore feature with an article on recent developments in Jersey and Guernsey which has been produced by Jonathan Speck and Jeremy Wessels of Mourant Ozannes.

There are also articles by Glen Davis QC on the Court of Appeal decision in Tambrook, by Christopher Brougham QC on insolvency and ancillary relief in family proceedings, and David Allison and Richard Fisher on the decision in Eurosail. In addition to all of that we have the usual Case Digests, this time edited by Hilary Stonefrost. And we have pieces on the INSOL Europe Annual Congress in Paris in September 2013, INSOL in Cayman in November 2013 and the latest Legal 500. As always we finish up with diary dates, news in brief and the South Square Challenge.

I hope you all enjoy this edition of the Digest. If you wish to be added to the Digest circulation list please send an email to kirstendent@southsquare.com. Similarly if your contact details have changed please let us know so that we can ensure you get the next edition of the Digest.

David Alexander QC - Editor

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Thwarting dissenting creditors

Michael Crystal QC, Adrian Cohen of Clifford Chance and **Adam Al-Attar** discuss enforcement of terms in the context of the recent decision in *Drydocks World LLC & Drydocks World - Dubai LLC v Monarch Master Funding Ltd*

Introduction

In what circumstances will a court that has sanctioned a compromise or arrangement take steps to restrain a creditor bound by that compromise or arrangement from acting contrary to its terms in a foreign jurisdiction? In what circumstances will such steps be recognised in that foreign jurisdiction?

This article examines each of the above questions in the context of the decision of Sir Anthony Evans, Michael Hwang SC and Sir David Steel, sitting as the special tribunal in relation to Dubai World and its subsidiaries (the Tribunal).

Discharge of debts under foreign law

A sovereign is sovereign only within its territory. A law is a sovereign act and so has effect only within that territory. English law choice of law rules, the rules by which foreign judgments are recognised, the rules which exclude foreign revenue, penal and other public laws, and the exceptional exclusion of foreign law on the ground of legal public policy are all rules premised upon a more fundamental rule derived from these principles, namely that an assertion or exercise of the sovereign right of a foreign state will not be enforced by an English court[1].

The decision of the Court of Appeal in *Gibbs & Sons v Société Industrielle des Métaux* (1890) 2 QBD 399 reflects this more fundamental rule. The court assumed that French law, the law applicable to the French liquidation of the defendant, purported to discharge the English law debt upon which the claimant sued. Lord Esher MR held that French law was irrelevant nonetheless because:

"[French law was] not a law of the country to which the contract belongs, or one by which the contracting parties can be taken to have agreed to be bound; it is the law of another country by which they have not agreed to be bound".

Gibbs is therefore treated as authority for the proposition that the discharge of a debt is governed by the law pursuant to which the debt was created. The result in *Gibbs* is however premised upon the more fundamental rule. It is only on the basis of that more fundamental rule that French law can have been held to have been irrelevant. Absent that more fundamental rule, the identification of English law as the law applicable to the question of discharge is not sufficient to justify the result in *Gibbs*. The question of why French law (or, for that matter, any other foreign law) should not have effect is otherwise unresolved.

So assessed, the rule in *Gibbs*, which is relevant to most cross border restructurings and is frequently the basis for a holdout by a dissenting creditor, is difficult to criticise. The propositions that a debt created by a particular law should be discharged by that law and that foreign law has no application in England unless a rule of English law says so are entirely unexceptional.

This is not to say *Gibbs* should be placed on a pedestal and treated as a charter for holdouts. The criticism that has been made by Professor Ian Fletcher[2] and others[3] is that a *further* rule of English law should be developed

1/. For judicial exploration of the principles underlying this more fundamental rule see *Government of India v Taylor* [1955] AC 491, HL, 511; *Attorney-General of New Zealand v Ortiz* [1984] AC 1, 21; and *Re State of Norway's Application (No. 2)* [1990] 1 AC 723, HL, 807-08.

2/. Insolvency in Private International Law (2nd edition, 2005) at 2.129.

3/. *Global Distressed Alpha Fund 1 Limited Partnership v PT Bakrie Investindo* [2011] Bus LR 970 at [25]-[26], in which Teare J said that there was much to be said for overturning the effect of Gibbs by the development of a further rule.

whereby, if one of the parties to the contract is the subject of insolvency proceedings in a jurisdiction with which he has an established connection, it should be recognised that the possibility of such proceedings must enter into the parties' reasonable expectations in entering their relationship, and as such may furnish a ground for the discharge to take effect under the applicable law.

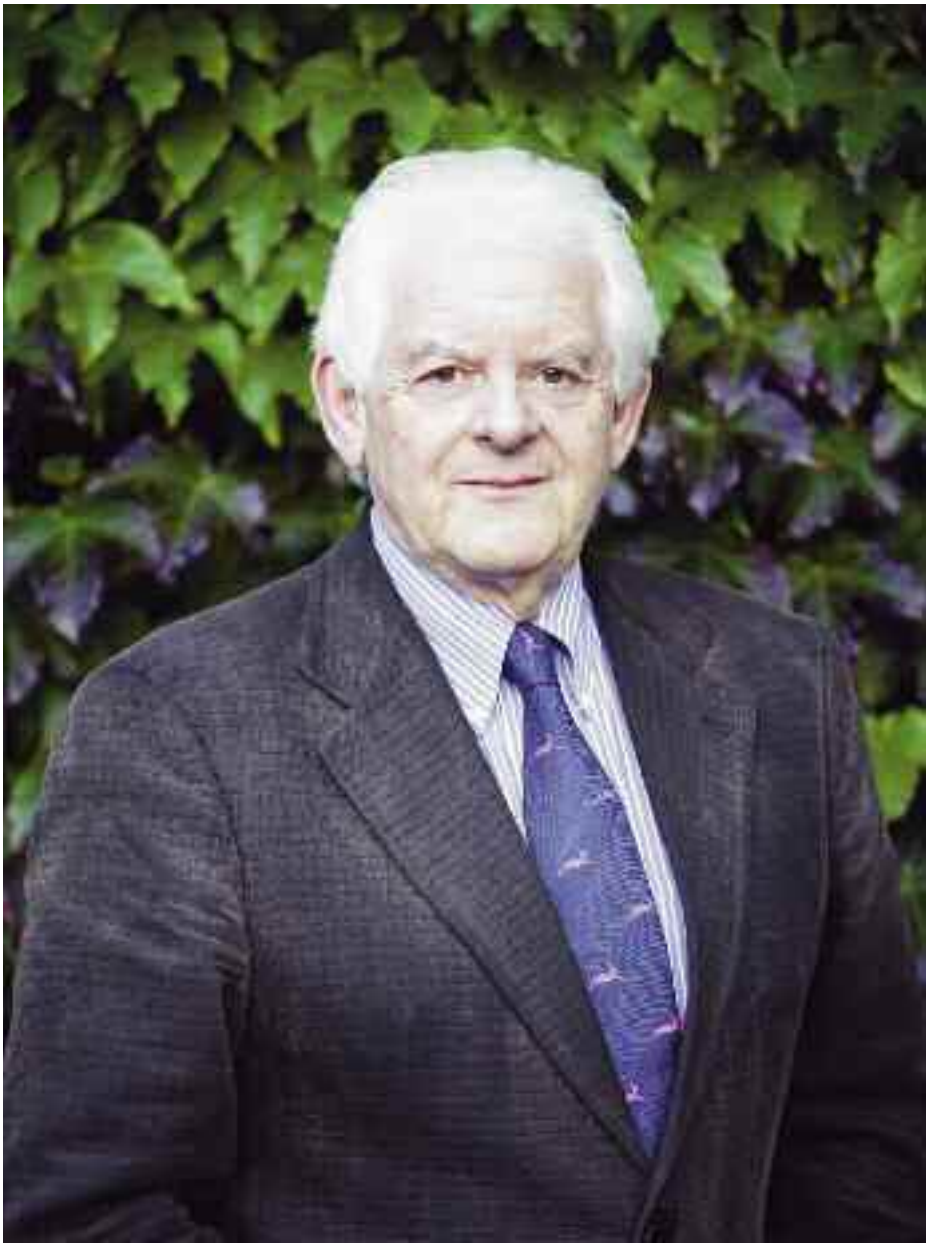
The development of such a rule is probably closed to any English court below the Supreme Court[4], and the reasoning of the majority in *Rubin v Eurofinance* SA [2013] 1 AC 236 suggests that the development of such a rule at common law will not be straightforward. In *Rubin*, the default judgments based upon avoidance provisions of US insolvency law were judgments *in personam*. The question Lord Collins asked, at [115], was whether as a matter of "*policy*" a different set of recognition rules should be developed with respect to *in personam* judgments in the *context* of insolvency. The Supreme Court declined to do so. Lord Collins said at [128]:

"There is a reason for the limited scope of the Dicey rule and that is that there is no expectation of reciprocity on the part of foreign countries. Typically today the introduction of new rules for enforcement of judgments depends on a degree of reciprocity. The EC Insolvency Regulation and the Model Law were the product of lengthy negotiation and consultation."

There is, likewise, no expectation of reciprocity on the part of the English court with respect to the discharge of foreign law debts under a compromise or arrangement *under English law*. The expectation is that a debt will be discharged under the law that gives rise to it.

In considering whether or not to develop a further rule to overturn the effect of *Gibbs*, any higher court is likely also to have in mind the following:

The justification to give effect to a foreign law *because* that law formed part of the parties' contractual expectations is difficult to apply to a debtor that has made a number of contracts over a period of time and in relation to an evolving business. In other words, parties' contractual expectations are necessarily fixed by reference to a particular contract at a specific time. If a further rule to recognise a discharge under the law applicable to a foreign insolvency proceeding is based upon a connection with the parties' contractual expectation, it is a rule unlikely to apply to all of the contracts made by the debtor. A heavy industry manufacturing business is a good



MICHAEL CRYSTAL QC

Parties' contractual expectations are necessarily fixed by reference to a particular contract at a specific time.

4/. This was certainly the view of Teare J in *Global Distressed Alpha Fund*. See also *Landsbanki Islands HF v Mills* [2013] UKSC 13 at [44], in which Lord Hope affirmed *Gibbs* as good (Scots) law.

DRYDOCKS WORLD – DUBAI, ABOVE, SPECIALISES IN VESSEL CONVERSION AND MODIFICATION.

example of a business in which there will likely have been complex contracts made in a number of jurisdictions over many years.

A solution to the problem described above is to recognise a discharge under a law relevant because of some other connecting factor, such as the centre or main interest (COMI), and not to rely on a direct connection with the parties' contractual expectations. This solution however necessarily gives rise to the prospect of a post-contractual re-ordering by a debtor of its affairs in order to secure a release of a particular debt under a friendly foreign law. It is the solution applicable in the EU because of the Insolvency Regulation made under the EU Treaty. A common law court may be reluctant to develop such a rule and judge that it is best left to the legislature.

Further, there are authoritarian states with substantial involvement in businesses either directly or indirectly through a close association of the political and business classes. An example highlighted by commentators in relation to *Rubin* is that of an oligarch domiciled and living in London with business interests in his home country via corporate entities. It is not so far-fetched that a liquidation might be initiated in his home country for the purpose of exporting default judgments to other jurisdictions in order to target that

A liquidation might be initiated abroad for the purpose of exporting default judgments to other jurisdictions in order to target an individual.

individual. It is clear that Lord Collins had a similar example in mind when he said at [130]:

"[T]he introduction of judge-made law extending the recognition and enforcement of foreign judgments would be only to the detriment of United Kingdom businesses without any corresponding benefit."

It cannot be said that all foreign states would be above opening a proceeding (ostensibly an insolvency proceeding) to secure the recognition abroad of debt forgiveness under the law of that state and on terms which might well discriminate against foreign creditors.

The desire to overturn the effect of *Gibbs* by a further common law rule does not, therefore, account for forum shopping (of the bad sort) or acts by a foreign state in the pursuit of its interests. To ensure acceptable results, any further rule common law rule would require the use by the courts of legal public policy to an extent hitherto unknown. The courts have always been reluctant to use legal public policy as a backstop because it involves a judge making an explicit judgement about a debtor's conduct or the acts of a foreign state. The latter is probably not even justiciable. For this reason, legal public policy has never played a significant role in relation to the recognition of foreign judgments. The traditional rules of recognition, affirmed in *Rubin*, avoid the need for difficult value judgements by a judge. By contrast, Section 426 of the Insolvency Act 1986 permits the application of foreign law because it is confined to former colonies and dominions whose legal heritage and values are assumed to be proximate to those of English law. The list of recognised territories is maintained by order and subject to review. A judge however can make no such distinctions and is bound to apply any further common law rule come-one-come-all.

Absent legislative intervention, *Gibbs* is therefore likely to remain part of the backdrop to any cross-border restructuring from some time to come.

The question then is how to extend the effects of a compromise or arrangement under foreign law to debts governed by English law. UNICITRAL provides an incomplete answer: if the desired relief is capable of expression in terms of a stay, the Model Law provides a solution practically equivalent to discharge for so long as a proceeding can be said to continue and thereby justify maintenance of the stay. There are also arguments that UNCITRAL might permit the application of foreign law. Such arguments sharply divide practitioners outside the US[5] and are beyond the scope of this article, which focuses on one aspect of the judgment of Lord Collins in *Rubin*. The extension of the law of submission in *Rubin* provides a further possible answer to the problem created by the absence of a further rule to deal directly with *Gibbs*.


ADRIAN COHEN OF CLIFFORD CHANCE

Submission and participation

Rubin affirmed in the context of insolvency the well-established rules for the recognition of a foreign judgment: presence and submission by appearance or by agreement. *Rubin* did, however, develop in one respect the circumstances to be treated as if a submission to the jurisdiction of a foreign court. Lord Collins said, at [165], that:

"In English law there is no doubt that orders may be made against a foreign creditor who proves in an English liquidation or bankruptcy on the footing that by proving the foreign creditor submits to the jurisdiction of the English court."

He cited *Ex p Robertson; In re Morton* (1875) LR 20 Eq 733, in which Bacon CJ had said:

"[W]hat is the consequence of creditors coming in under a liquidation or bankruptcy? They come in under what is as much a compact as if each of them had signed and sealed and sworn to the terms of it - that the bankrupt's estate shall be duly administered among the creditors. That being so, the administration of the estate is cast upon the court, and the court has jurisdiction to decide all questions of whatever kind, whether of law, fact, or whatever else the court may think necessary in order to effect complete distribution of the bankrupt's estate ... can there be any doubt that the appellant in this case has agreed that, as far as he is concerned ... the law of bankruptcy shall take effect as to him, and under this jurisdiction, to which he is not only subjected, but under which he has become an active party, and of which he has taken the benefit ... [The appellant] is as much bound to perform the conditions of the compact, and to submit to the jurisdiction of the court, as

5/. Chapter 15 of the US Bankruptcy Code implemented the Model Law on terms that did not allow access to avoidance actions under Chapter 11. The Second Circuit has construed the terms of the implementation as permitting access to foreign law avoidance provisions.

ADAM AL-ATTAR

if he had never been out of the limits of England."

In relation to the appeal in *New Cap*, he adapted this rule of English law to recognise the judgment of the Australian court. He said at [167]:

"It [the proving syndicate in *New Cap*] should not be allowed to benefit from the insolvency proceeding without the burden of complying with the orders made in that proceeding."

The justification for treating as if submission an act which involves no more than pointing out to a foreign representative that money is owed by the debtor and, if one is lucky, being paid is problematic in at least one respect. A winding up or bankruptcy is said not to change a creditor's rights and only the way in which those rights are to be enforced. This is a proposition asserted both as a matter of substantive law[6] and private international law[7]. On the basis of that proposition, it is difficult to justify the treatment of a payment, or of a demand for payment, as if an act of *submission* by appearance or by agreement. It is not sufficient pre-insolvency and should not be sufficient post-insolvency. The conclusion that the filing of a proof involves submission to all aspects of an insolvency proceeding, including the judgments of the foreign court seized of that proceeding, because that proceeding is a collective execution is, therefore, unsatisfactory. Execution, by judicial process or otherwise, may or may not involve submission to a foreign jurisdiction. If it does, it is for that purpose only, namely for payment. Aggregating that process to a collective process does not change the fact that a proving creditor seeks payment only. It is a leap of logic to assert that there is a submission by a creditor in *all* respects because a winding up or bankruptcy is for the benefit of *all* creditors of the debtor.

In this respect, the label submission may be unhelpful. Participation may be a better description of what occurs upon the submission of a proof. A proof permits the recognition of a claim against an estate, which estate, in part, may be supplemented by avoidance and other actions for the benefit of all creditors. Participation in *that* benefit may justifiably carry the burden of exposure to the jurisdiction of the court seized of the insolvency proceeding in certain circumstances. To say that proof should

6/. See, for example, Re *Dynamics Corpn of America* [1976] 1 WLR 757; Re *Lines Bros* Ltd [1983] Ch 1; and *Wight v Eckhardt Marine GmbH* [2004] 1 AC 147. The concept of collective enforcement is relied upon for the purpose of substantive law to distinguish the rules applicable to proofs of debt and distributions from the rules in relation to the enforcement of a judgment debt, specially from the doctrine of merger (in Wight) and from the rule requiring conversion to sterling as at the date of execution (in *Dynamics* and *Lines Bros*),

7/. Cambridge Gas Transportation Corporation v Official Committee of Unsecured Creditors of Navigators Holdings plc [2007] 1 AC 508, in which Lord Hoffmann borrowed the concept of collective enforcement developed for the purpose of substantive law to distinguish the rules of private international law applicable to judgments *in rem* and *in personam*.

8/. Cf Isis Investments Ltd v Oscatello Investments Ltd [2013] EWHC 75 (Ch) at [66] and [81], in which, in a different context, Asplin J considered that the filing of protective proofs did not amount to an election.

The concept of participation, as explained in Rubin, has created a mechanism by which the reach of a foreign restructuring might be extended.

carry that burden in all circumstances because of the equitable principle of benefit and burden is too general a proposition and thinly reasoned. The question has to be whether a particular benefit should carry a particular burden, relevantly the exposure of the person claiming to be a creditor to the jurisdiction of the foreign court. The reason for framing the question in this way is that it enables a distinction between the submission of a proof of debt and a payment on that proof. The mere submission of a proof should not be regarded as sufficient to justify exposure to the foreign court.[8] A proof might be submitted hastily or because if a proof were not submitted by a particular time any rights would be extinguished from the point of view of the foreign proceeding. The matter is different if a payment has in fact been made on a proof. Until the point of payment a proof might be withdrawn. After that time, there is a clear and meaningful participation in the foreign estate.

The question then is how far the concept of participation can be extended beyond payment on a proof in a winding up or bankruptcy. In relation to such distributive proceedings, the rule has a ready application. There may be difficult cases in relation to acts said to be equivalent to payment, such as set off or retainer, which occur either as a matter of law or because of an act of the foreign liquidator or trustee. In such cases, it may be that the quality of active participation is lacking[9].

Participation is, however, more complicated in relation to a compromise or arrangement, whether by a voluntary arrangement, a scheme or some other analogous proceeding. Such a proceeding is not necessarily distributive, and there is a well recognised distinction between a proof submitted for voting and for the purpose of distribution.

It was in this context that the Tribunal had to consider whether or not to make desist orders against a hedge-fund (Monarch Master Funding Ltd (Monarch)) that had secured an English judgment debt prior to the sanction of company voluntary arrangements (CVAs) under Dubai law (Decree No. 57 for 2009 which is derived from Chapter 11 of the US Bankruptcy Code, Part I of the Insolvency Act 1986 (English company voluntary arrangements) and Part 26 of the Companies Act 2006 (English schemes of arrangement)) in relation to Drydocks World LLC and Drydocks World - Dubai LLC (Drydocks). Drydocks are companies incorporated under the laws of the UAE, subject to the jurisdiction of the Tribunal and which principally carry on the business of ship construction and repair from Dubai. Monarch did not participate in the CVAs, either by voting/abstaining from voting at the creditor meetings approving the CVAs, attending the hearings before the Tribunal in relation to the CVAs or otherwise objecting to the CVAs; however, Monarch received payments under the terms of the CVAs, which it had sought to characterise as part payments in discharge of the English judgment debt and not as distributions under the CVAs.

The Tribunal relied on the payments received by Monarch as a justification for the Tribunal exercising its jurisdiction to make orders against Monarch requiring it to desist from executing against the assets of Drydocks in any jurisdiction. In this respect, the Tribunal relied on the analogous rule of English law cited by Lord Collins, at [165], and not the extension of that rule for the purpose of private international law, at [167].

Enjoining execution against assets situated abroad

The sanction attached to the desist orders was contempt of the Tribunal. Whether or not any other court would recognise the order of the Tribunal was irrelevant to the commercial reality that Monarch would be unable to do business in Dubai if it should have failed to comply with the desist orders. At the very least, to purge the contempt, the Tribunal could have sequestered future distributions from the CVA which would otherwise have been paid to Monarch. The case is, therefore, a useful illustration of the internal steps that a court can take to protect the integrity of a restructuring that it has sanctioned.

As regards any extra-territorial effect of the desist orders, the question was whether any foreign court would recognise and give effect to the orders of the Tribunal. It was in this respect that the extension in *Rubin* of what might amount to participation was significant. In Scotland (being one of the jurisdictions directly affected by Monarch's enforcement action) or elsewhere, there would, no doubt, have been argument as to how the payments received were to be characterised. *Rubin* however exposed Monarch to a real risk that the orders of the Tribunal would be recognised. In the light of that risk, a settlement was achieved.

The concept of participation, as explained in *Rubin*, has therefore created a mechanism by which the reach of a foreign restructuring might be extended. Conversely, it is a risk to which any creditor must be attendant, in particular, with respect to the terms of any post-restructuring receipts from the debtor.

9/. The appeal in *New Cap* did not grapple with this question in any detail. The decision is consistent with the proposition that the exercise of a right of retainer is equivalent to the payment of the amount withheld. It is not clear why a liquidator's decision to withhold payment should warrant the conclusion that a creditor has participated to an extent sufficient to justify exposure to the jurisdiction of the foreign court. Save for special facts, the most that can be said ordinarily is that, but for the retainer, the distribution *might* have been received. An automatic set off gives rise to a different question. It is because the set off is self-executing that there is no active participation.

CASE DIGESTS

Edited by HILARY STONEFROST

On company law issues, the Court of Appeal has, unsurprisingly, upheld the decision of the Chancellor that a director even of a one-man company can be held liable to account for breaches of fiduciary duty which he commits against the company. The fact that a director is the directing mind and will of the company is not an answer to such a claim against directors; a rule of this kind would be contrary to the protection provided by the Companies Act 2006 (see *Jetivia SA v Bilta*). On corporate insolvency, the High Court has had the task of applying the *Eurosail* test of balance sheet insolvency in the context of an application to set aside a transaction at an undervalue. Mr Justice Warren, in his lengthy judgment, considers all the decisions on balance sheet insolvency from the first decision under the Insolvency Act 1986, namely *Byblo* (see *Carman v Bucci*). The administrators of MF Global sought directions on the relationship between a client's contractual rights and the right to prove in the client money pool (*Heis v Attestor Value Master Fund LP*) which decision is of significance to all failed companies holding client money. In the period since the last digest there have also been two decisions in respect of administration expenses, in one the Court of Appeal held that there was no jurisdiction to order fees owed to solicitors in connection with work defending a winding up petition be paid as an expense in the administration of Portsmouth Football Club Limited (*Neuman v Andronikou*) and in the other the Court refused to apply the *Lundy Granite* principle to elevate a claim that did not involve the use of a third party's property for the benefit of the insolvent estate (*Mackay v KSF*). Most recently, applying the test in *Hellas*, the court made an administration order in respect of Manches LLP combined with liberty to enter into a pre-packaged sale of the business to Penningtons Solicitors LLP.

HILARY STONEFROST

BANKING AND FINANCIAL SERVICES

Digested by WILLIAM WILLSON

WILLIAM WILLSON

John Spencer Harvey v Dunbar Assets PLC [2013] EWCA Civ 952
CA (Civ Div) (Longmore LJ, Black LJ, Gloster LJ), 30 July 2013

Bank guarantee – Co-sureties – Construction

The appellant ("A") appealed against a decision dismissing his appeal against a refusal to set aside a statutory demand served on him by the respondent bank ("R"). The statutory demand was based on a guarantee under which A had guaranteed the liabilities of a property development company. A contended that he was not bound because one of the intended co-sureties claimed his signature had been forged. The judge found that A was bound by the guarantee because one of the clauses provided that neither the obligations of a guarantor nor the rights, powers and remedies conferred on R in would be "*discharged impaired or otherwise affected by ... any failure to take or fully to take any security contemplated by or otherwise agreed to be taken in respect of the Principal Debtor's obligations*" to R. He concluded that the failure to take the security from one of the signatories did not discharge, impair or affect the obligations of the others. Held, that whether a signatory to a guarantee had assumed liability under it, in circumstances where other contemplated security had not been obtained, was essentially a question of construction of the guarantee against its

admissible factual matrix. If the form of the document showed that it was intended to be a joint composite guarantee, which assumed that it would be signed by all the sureties named as such in the document, then a starting point for construction purposes would be regarded as subject to the condition that the signatures of all sureties were necessary for its validity (*Capital Bank Cashflow Finance v Southall* [2004] EWCA Civ 817 applied). The guarantee was clearly a single composite document, prepared for signature by several persons as joint and several guarantors, which pointed to the likely conclusion that the signatures of all four were an essential precondition to liability. Nothing in the wording of the guarantee excluded that result. Accordingly, the statutory demand would be set aside.

Torre Asset Funding v Royal Bank of Scotland [2013] EWHC 2670 (Ch) ChD (Sales J), 3 September 2013

Loan participation – Duty of facility agent – Provision of information to lenders


JEREMY GOLDRING QC

The claimants sought damages from the bank alleging that the bank's failure to pass on information about a borrower caused them to retain a loan participation which, if the information had been provided, they would have realised before it became worthless. The claim was dismissed. The facility agent under an LMA standard-form loan agreement owes lenders only the duties to provide information set out in the contractual documents, properly construed, rather than any broader general duty to pass on relevant information arising out of its status as an agent. Nor could such a broad duty be implied into the contracts. Accordingly, the bank had not acted in breach of any obligations owed to the lenders. In any event, any loss suffered by the lender was neither caused by the bank, nor did it fall within the scope of the bank's duty: the fact that a lender might well wish to take account of information provided pursuant to obligations under the financing agreements when considering whether to invest further or remain invested in the transaction is a purely incidental effect of such obligations; it is not the object or purpose of those obligations to afford the lender that opportunity and to protect the lender against loss of such an opportunity. **[Jeremy Goldring QC]**

CIVIL PROCEDURE

Digested by ALEXANDER RIDDIFORD

Stylianou v Toyoshima [2013] EWHC 2188 (QB) (Sir Robert Nelson sitting as a Judge of the High Court), 24 July 2013

Service out of jurisdiction – Allocation of jurisdiction – CPR rr. 6.36, 6.37, PD 6B para 3.1(9)(a)


ALEXANDER RIDDIFORD

M, an insurer, applied to set aside an order granting permission for S, a British citizen and habitually resident in England, to serve a claim form out of the jurisdiction and sought an order for substituted service on T, the first defendant. S, on holiday in Western Australia, had been seriously injured in a car accident whilst traveling in a car driven by T. M was T's insurer. Permission to serve a claim form out of the jurisdiction under CPR r.6.36 and r.6.37 requires that one of the grounds set out in CPR PD 6B para.3.1 be established. In this case, the relevant ground under the latter provision was CPR PD 6B para.3.1(9)(a).
It was held that, in their natural meaning, the words "damage ... sustained within the jurisdiction" in CPR PD 6B para.3.1(9)(a) were wide enough to cover any kind of damage, direct or indirect. Therefore, economic loss or financial damage, such as loss of earnings or loss of care sustained in the United Kingdom, was in principle damage sustained within the jurisdiction, even though the initial injury causing direct physical harm occurred elsewhere. Accordingly, M's application to set aside the order granting S permission to serve the claim form out of the jurisdiction was dismissed.

Terra Raf Trans Trading Ltd v Assaubayev [2013] EWHC 2824 (Comm) (Judge Mackie QC), 5 August 2013

Address for service – Default judgments – Service – Setting aside

X applied for an order setting aside a default judgment obtained by T, who had commenced proceedings against X claiming damages for fraudulent and negligent misrepresentation and unjust enrichment arising out of a loan agreement and guarantee. The proceedings were served on X at an address in London and, with permission to serve out of the jurisdiction, at an address in Kazakhstan. T obtained a default judgment for over $5 million. When T later obtained a freezing injunction, served on X in London, X claimed that this was the first he knew about the proceedings. X argued that service of the proceedings had been defective because the London address had

been a rented apartment that he had not rented for three years, and the Kazakhstan address was a property owned by his mother that had been vacant for years.

X's application was granted since the court had to set aside the default judgment if the requirements for service had not been met. Moreover, the court could set aside a default judgment under CPR Pt 13 if the defendant had a real prospect of successfully defending the claim, as was the case in this instance.

Carr v Penman [2013] EWHC 2679 (QB) (Dingemans J), 2 September 2013

Service out of jurisdiction – Abuse of process – Applications without notice

P applied to set aside an order permitting C to serve proceedings on P in Australia claiming damages for libel and for a declaration that the court had no jurisdiction to try the claim.

C had issued the instant proceedings complaining about allegedly defamatory remarks made by P on two Australian websites. In particular, the extent of the publication in England was in issue. In support of his application to set aside, P argued, inter alia, that C had not made full and frank disclosure on his without notice application for permission to serve out of the jurisdiction.

The court, following the Court of Appeal decision in Jameel v Dow Jones & Co Inc [2005] Q.B. 946, held that it was required to stop as an abuse of process defamation proceedings which served no legitimate purpose. One of the two publications in question, which were published on websites in Australia, was linked to an English website but there had been no recorded downloads of this article in England. Further, the particulars of claim did not provide any details of publications or provide details of specific losses. Accordingly, on the basis that there had been a lack of full and frank disclosure and since the proceedings amounted to an abuse of process, the court set aside the order for service of the proceedings out of the jurisdiction and declared that it would not exercise its jurisdiction to hear the action.

Page v Hewetts Solicitors [2013] EWHC 2845 (Ch) (Hildyard J), 20 September 2013

Claim forms – Issue of proceedings – Limitation periods

As a preliminary issue, the court considered whether a claim for secret profits issued by P against H and F was brought within the limitation period. The events to which the claim related took place in 1999. The limitation issue turned on whether the claim had been "brought" within the relevant limitation period where the claimants' request to the court for the issue of the claim, submitted on the last possible day, had not been accompanied by the appropriate court fee. The appropriate fee for a money claim by way of damages or equitable compensation was £990. However, the claim submitted by P had included a non-money claim for an account of profits, with the result that the appropriate fee was the higher one of £1,390. Therefore, the fee provided was insufficient by £400. The shortfall of £400 was paid subsequently. However, P's failure to offer the appropriate fee at the relevant date meant that they had not done all that was required of them such that the claim had been "brought" in the relevant sense. Accordingly, since P had left it too late to correct the error, and since this was a risk they had unilaterally undertaken, it was held that the secret profits claim had not been "brought" within the relevant limitation period.

In the Matters of Atrium Training Services Limited, Kimberley Scott Services Limited and Connor Williams Limited (Birss J), 27 September 2013


DAVID ALEXANDER QC


LUCY FRAZER QC


STEPHEN ROBINS

Disclosure – List of Documents – Unless Order – Alleged Breach of Order

In proceedings making claims under Sections 213, 214 and 238 of the Insolvency Act 1986, the Liquidators of the above three companies had been ordered to conduct a search for documents falling within CPR 31.6 in compliance with the requirements set out in CPR 31.7 and to provide to the Respondents to the proceedings with a list of documents identifying the documents located as a result of that search in compliance with the requirements set out in CPR 31.10. In the first two sets of proceedings the Liquidators were to do that by 4pm on 28 June 2013 failing which their claims against the Respondents, said to be worth in the region of £45 million, were to be struck out without further order of the Court ("the Unless Order"). The Liquidators served lists of documents within the time period provided for by the Unless Order. However, the Respondents to two of the sets of proceedings alleged that the list served by the Liquidators was in breach of the Unless Order. They asserted that the list

did not include all relevant documents and the form of the list did not comply with the rules in that it did not include a short description so that each document could be identified. They sought judgment against the Liquidators. The Respondent in the third set of proceedings sought a further list on Unless Order terms.

The Judge decided that the Liquidators had carried out a search. However, through an error, relevant documents which the Liquidators had previously agreed would be disclosed by them in their June list, were not in the event disclosed. Whilst a Supplemental List was served by the Liquidators shortly before the hearing containing in the region of 600 additional documents running to some 7,000 pages of further documents, the Judge decided that the Liquidators were nevertheless not in breach of the Order. The Judge decided that the Liquidators had carried out a reasonable search and disclosed what that search had found. As regards the form of the list, whilst the documents had originally been hard copy documents, the Liquidators had uploaded them onto an e-disclosure platform with the knowledge of the Respondents. As a result, the Judge held that the Practice Direction 31B (which applies to the disclosure of electronic documents) applied in this case and the descriptions in the Liquidators' list were not in breach of those provisions. The Judge therefore dismissed the Judgment application and the application for a further list on Unless Order terms. The Judge then held that the Liquidators should conduct a review of documents in the lists which simply had single word descriptions like "transcript" or "email" with no other identifying information and use their best endeavours to fill in the blanks in the information.

[David Alexander QC, Lucy Frazer QC and Stephen Robins]

COMMERCIAL LITIGATION AND ARBITRATION

Digested by CHARLOTTE COOKE


CHARLOTTE COOKE

Foster v Action Aviation Ltd [2013] EWHC 2439 (Comm) (Hamblen J), 8 August 2013

Breach of contract – Misrepresentation – Aircraft

The Claimants brought an action for breach of contract and misrepresentation in connection with the purchase of an aircraft. The Claimants argued that one of the Defendants had told them that the aircraft had never been in an accident and that he had bought it new, but that was a fraudulent and/or negligent misrepresentation as the aircraft had been involved in an accident. The Claimants further argued that implied representations were made that the aircraft's manufacturer's warranty was a going concern, but that too was false as the manufacturer had filed for bankruptcy. It was held that it had been negligently misrepresented to the Claimants that the aircraft had not been involved in an accident, but that the other alleged misrepresentations had not been made.

Energy Venture Partners Ltd v Malabu Oil & Gas Ltd [2013] EWHC 2118 (Comm) (Gloster LJ), 17 July 2013

Contract – Commission – Implied agreement – Oil and gas

The Claimant sought payment of fees allegedly owed in relation to the sale of the Defendant's ownership interest in an oil prospecting licence for an oilfield in the waters of Nigeria. Under the agreement, the Claimant was entitled to retain as a fee any consideration received for the assets over an agreed price, but no agreed price was set. The Claimant claimed $200 million under the contract or by way of a quantum meruit. The Defendant's arguments that the agreement was a sham or had been terminated were rejected. Further, it was held an agreement that the Claimant would be paid a reasonable fee for its services in the event that it produced an offer which would have entitled it to commission under the agreement was to be implied from the parties' conduct. A reasonable fee was $110.5 million. A counterclaim to the effect that the Claimant was barred from claiming commission on the ground that a secret commission agreement had been entered into was dismissed.

Amlin Corporate Member Ltd v Oriental Assurance Corp [2013] EWHC 2380 (Comm) (Field J), 31 July 2013

Reinsurance – Shipping – Warranty

On 21 June 2008 the Princess of the Stars sailed into a typhoon and capsized; most of its passengers died. Reinsurers sought a declaration that the departure of the vessel from Manila to Cebu on 20 June 2008 constituted a breach of a warranty in a reinsurance contract entered into with the insurer who had agreed to indemnify the shipping

company concerned in respect of its liability for loss or damage to the vessel's cargo. The warranty in issue stated "*…it is expressly warranted that the carrying vessel shall not sail or put out of Sheltered Port when there is a typhoon or storm warning at that port nor when her destination or intended route may be within the possible path or the typhoon or storm announced at the port of sailing, port of destination or any intervening point.*" The declaration was granted. It was held that the object of the warranty was to protect the reinsurer from liability arising from typhoons that could travel at varying speeds and in directions that could not accurately be predicted. The reinsurer was right that if a vessel sailed from a port where there was a typhoon warning the warranty would be breached even though the port was not predicted to be in imminent danger from the typhoon.

Alpstream AG v PK Airfinance Sarl [2013] EWHC 2370 (Comm) (Burton J), 31 July 2013

Mortgage – Power of sale – Conspiracy

The Claimant companies brought a claim against a mortgagee for breach of duty in exercising its power of sale of the mortgaged property. Further claims were brought against an associated company of the mortgagee for procuring the mortgagee's breach of duty and against both Defendants for conspiring to cause economic loss by unlawful means. It was held that the transaction in issue was a sale to a connected party and therefore there was a heavy onus on the mortgagee to show that it had used its best efforts to obtain the best price reasonably obtainable. That onus could not be discharged on the facts. The Second Defendant was liable for procuring the mortgagee's breach, with both Defendants also being liable for conspiracy to cause economic loss by unlawful means.

COMPANY

Digested by **GEORGINA PETERS**

Re European Safety Vehicle Spain 1, S.A. (Henderson J), 24 June 2013

Scheme of Arrangement – Companies Act 2006, section 899 – Judgments Regulation – Foreign company – English law governed credit agreement


GEORGINA PETERS

A Spanish company sought and obtained an order under section 899 of the Companies Act 2006 sanctioning a scheme of arrangement with its lenders whose claims arose under a €395 million facilities agreement governed by English law and subject to the jurisdiction of the English courts. In broad terms, the scheme provided for the two facilities to be re-tranched and for their maturity dates to be extended. The fact that the relevant claims were governed by English law was considered to be a "sufficient connection" to the English jurisdiction for the purposes of the court exercising its jurisdiction in relation to the scheme. Two of the lenders were domiciled in England and the remaining lenders were domiciled in other Member States. The Court made no finding as to whether the Judgments Regulation applied to schemes of arrangement, as, even if it did apply, the Court had jurisdiction as a result of the jurisdiction clause in the facilities agreement. In considering whether the scheme was likely to have a useful effect, the Court had regard to expert evidence that the scheme would be recognised and enforced in Spain. **[Antony Zacaroli QC, Georgina Peters]**

Re Vietnam Shipbuilding Industry Group (David Richards J), 25 June 2013

Scheme of Arrangement – Companies Act 2006, section 899 – Judgments Regulation – Foreign company – English law governed credit agreement


TOM SMITH

A Vietnamese company proposed a scheme of arrangement with its creditors whose claims arose under a credit facility governed by English law and subject to the non-exclusive jurisdiction of the English courts. The company had no assets in England and no substantive links with the jurisdiction; however, the fact that the relevant claims were governed by English law was a "sufficient connection" for the purposes of the court exercising its jurisdiction in relation to a proposed scheme of arrangement. Certain of the lenders were domiciled in other Member States. Even if the Judgments Regulation did apply to schemes of arrangement (on which point there were contrary arguments), the Court had jurisdiction as a result of the jurisdiction clause in the credit facility. For these purposes, there was no difference between an exclusive jurisdiction clause and a non-exclusive jurisdiction clause. (The company had, in April 2013, obtained a stay of claims to enable the scheme to be put forward; see the decision of Blair J [2013] EWHC 1146 (Comm).) **[Tom Smith]**

Re Coroin Ltd; Patrick Gerard McKillen v Misland (Cyprus) Investments Ltd [2013] EWCA Civ 781 (Arden LJ, Moore-Bick LJ and Rimer LJ), 3 July 2013

Minority Shareholders – Shareholders' Agreement – Unfair Prejudice – Breach of Pre-Emption Provisions – Companies Act, section 994

The appellant shareholder ("McKillen") appealed against a decision dismissing his petition for relief against alleged unfairly prejudicial conduct under the Companies Act 2006, section 994. The shareholders' agreement contained pre-emption rights allowing McKillen to purchase the shares of other shareholders in prescribed circumstances, including if any shareholder security became enforceable, upon which the shareholder would be deemed to have given a transfer notice in respect of his shares and the pre-emption provisions would apply. The second respondent ("Quinlan") held shares in the company that were fully charged to secure debts which had been acquired by the Barclay interests. Upon Quinlan's resignation as a director of the company, he appointed a nominee of the Barclay interests as a director and also gave a power of attorney to a nominee of the Barclay interests to perform acts in relation to the company on his behalf.

McKillen submitted first, that the practical effect of the arrangements was that Quinlan had transferred his interest in his shares to the Barclay interests, or secondly, that there had been a transfer of a proprietary interest, such that the pre-emption provisions had been breached. The Court of Appeal rejected both grounds. The shareholders' agreement was specific about which transactions were prohibited, and mere transfer of control was not prohibited. Quinlan retained the equity of redemption and the arrangements were not irreversible. Nor did the arrangements involve the transfer of a proprietary interest, since on the facts, the making of an agreement between Quinlan and a company controlled by the Barclay interests for the sale of the shares had not completed. An interest in shares would not pass under a contract for the sale of shares which was subject to a true condition precedent until the condition precedent was fulfilled.

McKillen contended, thirdly, that the express obligation of good faith had been breached, which the Court of Appeal also rejected. Fourthly, it was argued that the provisions of the charges granted to the Barclay interests had become enforceable, enabling the directors to implement the pre-emption provisions in McKillan's favour. The Court of Appeal held that the first charge had not become enforceable, having regard to the conditions of the charge. The Court found that the second charge had become enforceable, but the relevant time period for a transfer notice to have been given in respect of the shares had expired. In the premises, McKillan had not been subjected to any unfairly prejudicial conduct.

Jetivia S.A. & URS Brunschweiler v Bilta (UK) Ltd (in liquidation) and Kevin John Hellard and David Anthony Ingram (the joint liquidators of Bilta (UK) Ltd) [2013] EWCA Civ 968 (Lord Dyson, Rimer LJ, Patten LJ), 31 July 2013

Ex Turpi Causa – Claim against Directors – Conspiracy to Defraud – Conspiracy to Injure – Fraudulent Trading – Companies Act 2006, sections 172, 239

The Court of Appeal upheld a decision that claims by a company in liquidation, the vehicle for a VAT fraud left unable to pay its liability to HMRC, for conspiracy and dishonest assistance against its former directors and overseas suppliers alleged to have been involved in the fraud, was not precluded by the principle of *ex turpi causa* or the decision in *Stone & Rolls Ltd v Moore Stephens (a firm)* [2009] 1 AC 1391 (HL). The liquidators' case as pleaded was that the object of the alleged conspiracy was to defraud and injure the company by depriving it of the money necessary to meet its VAT liabilities. Separately, claims for fraudulent trading were brought. The fraud had been orchestrated by the directors and sole shareholder, who were the only directors of the company. In relation to the common law claims, the appeal was brought by the overseas supplier and its director against the dismissal of applications for summary judgment on the basis of the ex turpi causa principle and the decision in *Stone & Rolls*. Patten LJ, in a judgment which considered the relevant authorities at some length, held as follows.

First, in order to engage the ex turpi causa rule the appellants had to establish that the law attributed to the company the unlawful conduct of its directors and sole shareholder, so that the company's actions against them and the appellants fell to be treated as an action between co-conspirators. The Court was bound by the decisions in *Belmont Finance Corp Ltd v Williams* [1979] Ch 250 and *A-G's Reference (No. 2 of 1982)* [1984] QB 624 to hold that even a director of a one-man company could be held liable to account for breaches of fiduciary duty which he committed against the company. The company was to be treated as the victim even though the loss which it suffered from the breach might be the compensation which it had to pay to a third party who had been damaged by the fraud. Although loss of that kind might be insufficient to prevent attribution under the principles in *Belmont and Re Hampshire Land Co* [1896] 2 Ch 743 when what was at issue was the company's own liability to a third party, there was no reason why it should have the same effect when the company

was the claimant and the fraudulent directors were the defendants. Secondly, the company was the intended and only victim of the conspiracy. In the context of a claim against the directors and the co-conspirator supplier company, the company was the victim regardless of whether its loss was consequential on that to a third party (HMRC). Thirdly, the sole actor rule applied in *Stone & Rolls* was not applicable to a claim by a company against its fraudulent directors that is based on a breach of duty under which directors always had a duty to consider the interests of creditors. It would directly contradict the protection given to creditors under the Companies Act 2006, sections 172 and 239, which applied regardless of whether the company was a one-man company or one in which there were innocent directors and shareholders. The sole director/shareholder owes to the company the fiduciary duties prescribed by section 172 and cannot use his control of the company to ratify his fraudulent acts against the company, particularly where the interests of creditors would be prejudiced; section 239(3) and *Franbar Holdings v Patel* [2009] 1 BCLC 1 considered. The Court was thus not bound by *Stone & Rolls* to apply the sole actor exception (that case being distinguishable on the basis that it concerned a claim against the company's auditors, not party to the fraud).

E-Clear (UK) Plc (in liquidation) v (1) Elias Elia (2) Ian Defty (as Trustee in Bankruptcy for the estate of Elias Elia (3) Mili Petrou Elia [2013] EWCA Civ 1114 (Patten LJ, Fulford LJ), 6 September 2013

Breach of Fiduciary Duty – Insolvency - Summary Judgment – Companies Act 2006, sections 170-177

The Court of Appeal allowed an appeal against a declaration made on an application for summary judgment, that the respondent company was the beneficial owner of 35.5 per cent of a property, and against an order for the sale of the property. The company, which processed credit card payments, had been profitable until the failure of two of its customers left it liable to cover certain chargebacks, resulting in its administration. Prior to that time, the appellant's son, a director and the beneficial owner of the company, had caused the company to make several payments partly funding the acquisition of the property. Subsequently, the director assigned his interest in the property to the appellant. The monies were said to be paid, in breach of his fiduciary duties under the Companies Act 2006, sections 170-177, to or for the benefit of the director and traceable into the purchase price via bank accounts in his name, giving rise to a proprietary claim in respect of the property. The director's principal defence was that the payments had been made in discharge of prior loans he had made to, and thus genuine liabilities of, the company. The Court held that the question whether the director had acted in breach of fiduciary duty was inextricably linked to the question of the company's solvency and the director's knowledge of its financial position, which should be investigated at trial. The judge had erred in finding that the company's insolvency was beyond reasonable doubt, and could not have been sufficiently certain that the company had been either insolvent, or on the brink of insolvency, at the time when the monies had been paid to the director, nor that the director had been aware of the pending insolvency at that time. Issues such as whether the contemporary management accounts were evidence that the company was in fact insolvent, and whether reliance could be placed on the survival of the company for a further year as evidence that it had the necessary financial support to continue which might have justified the director taking an optimistic view, were both issues for a trial.

HLC Environmental Projects Ltd; (1) Kevin Hellard (2) Devdutt Patel (joint liquidators of HLC Environmental Projects Ltd) v Horacio Luis de Brito Carvalho [2013] EWHC 2876 (Ch) (John Randall QC), 25 September 2013

Directors' Duties – Misfeasance – Companies Act 2006, section 172, 172(3) – Insolvency Act 1986, sections 123(1)(e), 123(2), 212

The Court found a director of the company to have breached his duty to act in the company's best interest under the Companies Act 2006, section 172, which included the duty to consider or act in the interests of creditors under section 172(3). The director had caused the company to make a number of payments, to (i) a parent company and the director personally, (ii) a company in which the director was investing, for his personal benefit, (iii) a mechanical engineer previously employed by the parent company, and (iv) a bank in discharge of its indebtedness. The insolvency threshold was satisfied, such that the company was found to be insolvent on both a cash flow and balance sheet basis at the relevant times. As such, the Court applied the principle that directors are not free to take action which puts at real risk the creditors' prospects of being paid, without first having considered their interests ahead of those of the

shareholders of the company. The Court confirmed the correct interpretation of the Companies Act 2006, section 172, as being that the duties owed are usually subjective, but that an objective test would apply (i) where there was no evidence of actual consideration of creditors' interests, in which case the test was whether an intelligent and honest man in the director's position could have reasonably believed that the transaction was for the benefit of the company, and (ii) where the interest of a creditor with a substantial claim was unreasonably overlooked. On the facts of the case, the Court found the general principle of subjectivity to have been displaced.

The payments fell, broadly speaking, into two categories. The first category constituted the payments to the director directly or for his personal benefit, and to the mechanical engineer who had never been employed by the company. The payments were held to be improper: the director had been unconcerned as to the company's liabilities, and his decision to make the payments was made without any consideration as to the company or its creditors' best interests.

The second category concerned the payments made to the parent company, and to the bank. Those payments were made in discharge of the company's genuine liabilities. The Court held that the director could nevertheless be held liable for breach of his duty under section 172, in circumstances in which he had not acted reasonably by failing to consider the interests of creditors or where he had a collateral purpose in reducing the parent company's exposure on a guarantee granted to the bank.

In this case, however, since those payments were made in discharge of the company's genuine liabilities, the Court applied Liquidator of West Mercia Safetywear v Dodd (1988) 4 BCC 30 in holding that an order against the director for payment to the company of those sums should be qualified by a proviso intended to prevent a windfall to creditors. The proviso was to the effect that, in distributing the company's assets to unsecured creditors, the debts due from the company to the parent and the bank should be notionally increased to what they would have been had the payments not been made, with any dividend attributable to the extra sum to be recouped to the director.

CORPORATE INSOLVENCY

Digested by ADAM AL-ATTAR


ADAM AL-ATTAR

Drydocks World LLC & Drydocks World - Dubai LLC v Monarch Master Funding Ltd Sir Anthony Evans, Michael Hwang SC and Sir David Steel, 15 July 2013

Dubai International Financial Centre, Special Tribunal in relation to Dubai World and its subsidiaries

CVA – Enforcement of terms – Injunction

The Tribunal had to consider whether or not to make desist orders against a hedge-fund, Monarch Master Funding Ltd ("Monarch") that had secured an English judgment debt prior to the sanction of company voluntary arrangements ("CVAs") under Dubai Decree No. 57 for 2009, which is derived from Chapter 11 of the US Bankruptcy Code, Part I of the Insolvency Act 1986 (English company voluntary arrangements) and Part 26 of the Companies Act 2006 (English schemes of arrangement), in relation to Drydocks World LLC and Drydocks World - Dubai LLC ("Drydocks"). Drydocks are companies incorporated under the laws of the UAE, subject to the jurisdiction of the Tribunal and which principally carry on the business of ship construction and repair from Dubai. Monarch did not participate in the CVAs, either by voting/abstaining from voting at the creditor meetings approving the CVAs, attending the hearings before the Tribunal in relation to the CVAs or otherwise objecting to the CVAs; however, Monarch received payments under the terms of the CVAs, which it had sought to characterise as part payments in discharge of the English judgment debt and not as distributions under the CVAs.

The Tribunal held that it had personal jurisdiction in relation to Monarch, which had been duly served out of the jurisdiction, and that it had jurisdiction in relation to the CVAs, which persisted, notwithstanding the issue of notices of completion, for the purpose of enforcing the terms of the CVAs against creditors such as Monarch who sought to act contrary to those terms. The legal basis for the injunction issued was the terms of the CVAs. The Tribunal was satisfied that it should act to protect the integrity of its proceedings by restraining a creditor from acting contrary to the terms imposed. The direct practical effect of the order was to permit the Tribunal to sequester further payments from the scheme and to expose Monarch to proceedings for contempt. The Tribunal also issued a letter of request to the Scottish court for assistance with respect to executions by Monarch prior to the hearing before the Tribunal. The Tribunal was not prepared to issue a mandatory injunction with respect to executions which had been completed in part prior to the hearing of Drydocks' applications. The case is discussed in this issue in the article "Thwarting Dissenting Creditors".

[Michael Crystal QC, Adam Al-Attar]

Neumans LLP (a firm) v Andrew Andronikou & Ors [2013] EWCA Civ 916 CA (Civ Div) (Mummery LJ, Rimer LJ, Underhill LJ), 24 July 2013

Administration – Expenses – Priority of payment under the statutory scheme – Guidance

Neumans LLP (the "Solicitors") acted for Portsmouth City Football Club Limited (the "Company") in connection with its opposition to a winding-up petition presented by HMRC. Administrators were appointed out-of-court by the floating charge holder and the winding-up petition was suspended. Eventually the Company went into liquidation. The Solicitors claimed priority for payment, as an administration expense, of their fees owed by the Company for work they did defending the winding-up petition as the liquidators had no funds.

A jurisdictional objection was successfully taken by the former administrators before Morgan J. The Solicitors appealed on the grounds that there were three ways in which their fees could be ordered to be paid as an expense in the administration: first, there was jurisdiction under section 51 of the Senior Courts Act 1981 to make an order for payment of the Solicitors' fees by the Company from assets in the hands of the administrators as an expense of the out-of-court administration; second, the court could direct the former administrators to treat the Solicitors' fees as if they were an expense of the administration; or, third, the court had jurisdiction under paragraphs 65 or 66 of Schedule B of the Insolvency Act 1986 or in its inherent jurisdiction to order that a claim which would not otherwise be regarded as an expense be paid as such.

The Court of Appeal followed the Lord Wilberforce in *Brumby v Milner* (1975) 51 TC 583 on "*appeals from impeccable judgments*". There was nothing wrong with the decision appealed or the reasons for it. The Court of Appeal was content to adopt, without reservation, the judgment of Morgan J.

The Court of Appeal summarised the legal position on expenses in twelve short points (paragraph 41 of the Judgment). The three principal points are: the matters listed as administration expenses in rule 2.67 of the Insolvency Rules 1986 are a complete list of the expenses allowed in the case of an administration and the Solicitors' fees do not fall within that list; and, the court has no power to direct the administrators to "treat" the Solicitors fees as an expense in the administration; and, the court has an inherent jurisdiction to give directions to administrators as officers of the court, but it would not be a correct exercise of that jurisdiction to direct the administrators to pay those fees as that would be inconsistent with the 1986 Rules listing those items that are payable.

[Hilary Stonefrost]

Bestrustees plc v Kaupthing Singer & Friedlander Ltd (in administration) [2013] EWHC 2407 (Ch) (Sir Terence Etherton), 31 July 2013

Administration - Proof of Debt - Trust

Bestrustees plc ("the Trustee") applied pursuant to rule 2.78 of the Insolvency Rules 1986 to reverse the decision of the administrators to reduce by £2 million the Trustee's proof of debt in the administration of Kaupthing Singer & Friedlander Ltd ("KSF") of £74,652,000 on the ground that the same amount had been paid to the scheme by KSF out of a trust account in which the scheme had a beneficial interest.

The Judge acceded to the application. First, there was no challenge by the administrators to the amount of the debt certified by the actuary under section 75 of the Pension Act 1995, including the figure for the assets of the scheme based on the audited accounts. Secondly, the relationship between the Trustee and KSF in relation to the £2 million deposit was never one of creditor and debtor. Subject to any particular conditions applicable to the operation of the trust account, it was only ever one of bare trust for the Trustee. The payment by KSF of the £2 million to the Trustee out of the trust account could not have discharged any part of the section 75 debt. The reasoning of the Chancellor can be contrasted with that of David Richard J in *MF Global (Shortfall Application)*, digested below.

[Tom Smith]

Carman (Liquidator of Casa Estates (UK) Ltd) v Bucci [2013] EWHC 2371 (Ch) (Warren J), 31 July 2013

Insolvency – Eurosail test applied

On an appeal from a decision of HHJ Purle QC on an application to a set aside a transaction at undervalue, the Court was required to consider the question of insolvency at the relevant time in the light of the decisions in *Cheyne* and *Eurosail*. The case is the first case to have done so on appeal since the decision of the Supreme Court in Eurosail.

HHJ Purle QC had applied the law as stated by Lord Neuberger MR and consider the question in terms of "*the point of no return*" test. That test was disapproved by Lord Walker in Eurosail and so Warren J had to consider the exercise afresh in the light of the test as explained in *Eurosail*.

The judgment is lengthy and considers each decision from *Byblos* to date in some detail. The key aspect of the judgment is at [81] and [89]-[91], in which the Judge seeks to state a practically workable formulation of the test in Eurosail in the context of avoidance actions. Of section 123 of the Act, Warren J said:

"*[T]he starting point must be that a company which has immediate liabilities which exceed assets is unable to pay its debts. Although, in the case of a winding-up petition, it is for the petitioner to establish to the satisfaction of the court that the case falls within s 123(2), the fact that a balance sheet shows a deficit is, by itself, enough to raise a prima facie case of insolvency; there is then an evidential burden on the company to show why it can, notwithstanding its balance sheet, reasonably be expected to meet its liabilities.*"

He continued:

"*Under s 240, the burden is the other way round in the case of persons connected with the company. [R]eading ss 123 and 240(2) together, it is necessary for [a connected person] to prove to the satisfaction of the court both (i) that the Company was at material times not unable to pay its debts as they fell due and (ii) that the value of the Company's assets equalled or exceeded the amount of its liabilities, taking into account its contingent and prospective liabilities…[T]he court has to make a judgment about whether it has been established that, looking at the Company's assets and making proper allowance for its prospective and contingent liabilities, it can reasonably be expected to meet those liabilities.*"

The case makes clear the potential difficulties for a liquidator in a claim against a person not connected with the company; however, the Judge emphasised that, even in that case, an arithmetic comparison of the balance sheet does place an onus on the respondent, if the comparison shows net liabilities.

Re Southern Pacific Personal Loans Ltd [2013] EWHC 2485 (Ch) (David Richards J), 8 August 2013

Liquidators – Personal Obligation – Data Protection Act

The liquidators of a company in the Lehman group applied for directions regarding data held by the company in relation to redeemed loans subject to the Data Protection Act ("DPA"). The active loans had been transferred to another company. The data in relation to redeemed loans was retained and was the subject of repeated requests for disclosure ("DSARs") by claim firms seeking to assess PPI and other mis-selling claims. A DSAR cost £10 to make and about £455 to comply with.

The Judge held that the liquidators were not data controllers but agents of the company in liquidation with respect to that data, and that the liquidators are not, therefore, personally responsible for compliance by the company with the DPA. The Court directed that the liquidators should dispose of all data in relation to the redeemed loans subject to two qualifications: first, the company must retain sufficient data to enable it to respond to DSARs made to the company before the disposal of the data; and second, the liquidators must retain sufficient data to enable them to deal with any claims that may be made in the liquidation.

Mackay v Kaupthing Singer & Friedlander Ltd (in administration) [2013] EWHC 2553 (Ch) (Martin Mann QC), 15 August 2013

Administration – Enforcement of security – Administration expenses

Kaupthing Singer & Friedlander Limited ("KSF") sought, amongst other things, permission under paragraph 43(2)(b) of Schedule B1 to enforce its security over the assets of UK Housing Alliance (North West) Limited ("UKHA") which in the circumstances explained below included a large number of properties ("Secured Properties"). UKHA also sought directions under paragraph 63 of Schedule Bl as to whether a tenant under an assured shorthold tenancy ("AST") in respect of one of the Secured Properties was entitled to a final payment ranking as an administration expense. The terms of the sale contract ("the Sale Contract")

provided for the remaining 30% (known as 'final payments') to be payable to the vendor at the end of the term of an AST (provided that the vendor had paid the rent and complied with the other covenants in the AST throughout the term) or sooner in the event of the vendor's death. With respect of UKHA's application, the Judge refused to apply Lundy Granite to elevate to an expense the right to a final payment. Lundy Granite was explained as a principle relevant only to the use of another's property for the benefit of the estate. In the present case, the rents under the ASTs were the property of UKHA, and the right to a final payment a mere personal right (as opposed to a right in fund held for the purpose of meeting the final payments) and which was not secured in any way. The Judge allowed KSF's application. The Secured Properties were in the nature of investments made by UKHA, and the purpose of the UKHA administration was to realise those assets for the benefit of the person entitled to them. UKHA accepted KSF was the only person with an interest in the Secured Properties and that should there be sales there would be a shortfall, leaving no surplus for the unsecured creditors.

Heis & Ors v Attestor Value Master Fund LP & Anr [2013] EWHC 2556 (Ch) (David Richards J), 16 August 2013

Administration – Contractual claim – Client money pool – Distribution

ANTONY ZACAROLI QC

The Court was asked to give directions to the joint administrators of MF Global UK Ltd (the "firm") as to the relationship of a client's contractual right against the firm and any right on the part of the client to prove for a shortfall in the satisfaction of its client money entitlement (a "CME") from the client money pool (the "CMP"). The application (the "Shortfall Application") therefore required the Court to consider:

(1) In what circumstances, if any, a client had a claim for a shortfall in the satisfaction of its CME?

(2) In respect of such a claim, whether it was provable alongside the client's contractual right against the firm?

(3) If so, whether the right of proof was limited in some, and if so what, way?

The Shortfall Application followed from the earlier application by the joint administrators, the Hindsight Application, in which the Court held that clients' CMEs were to be valued under Chapter 7 of the FSA's Handbook, the client assets sourcebook ("CASS 7"), without regard to hindsight and, in particular, the subsequent rise or fall in the value of derivative contracts open as at the date of the administration. That principle, however, applied with respect to unsecured claims against the general estate. In working out what claims were provable against the general estate, the Court, accordingly, had to grapple with the fact that a client's CME was derived from a contractual position against the firm and that a client's CME and the underlying contractual right might nonetheless have different values.

David Richards J held that:

(1) A client had a provable claim for a shortfall in the satisfaction of its CME from the CMP if and insofar as that shortfall was caused by a breach of trust by the firm. The mere fact of a shortfall did not justify a provable debt against the general estate.

(2) A client was barred by the rule against double proof to the extent that any claim for shortfall was in substance the same as a proof based upon the underlying contractual right. In practice, a client is able to prove only to the extent that its shortfall claim reflects the excess of its CME above its contractual claim by reason of a fall in the value of that contractual claim after the date of administration.

(3) A client's provable claim based on its underlying contractual position was to be reduced by payments actual or anticipated from the CMP. Actual payments discharged pro tanto the provable debt. In relation to anticipated payments, the debt was to be treated as "subject to" the contingency of discharge by reason of such payments from the CMP. The decision has wider significance because of the failure of other firms holding client money, notably Lehman, and because the Court gave a broad construction to the rule in special administration (which is identical to the rule under Insolvency Rules) regarding the quantification of debts subject to a contingency. Previously, that rule had been thought to apply only to debts the incidence of which may or may not occur and not to due debts the discharge of which was subject to a contingency. The reasoning of the Judge can be contrasted with that of the Chancellor in Bestrustees, digested above.

[Antony Zacaroli QC, Adam Al-Attar]

Rollings & Ors v O'Connell & Anr [2013] EWHC 2921 (Ch) (Warren) J, 26 September 2013

Administration – Sale of assets subject to security

The joint administrators of Musion Systems Limited (MSL) applied for an order under paragraph 71 of Schedule B1 to the Act to sell property subject to a fixed charge. The application was dealt with on an urgent basis over the course of two days. The company had limited funds to continue to trade and the purchaser had agreed a side letter which entitled it to withdraw if a sealed order was not obtained in advance of the quarter day.

In the course of the hearing, the Judge considered whether, in the exercise of his discretion, he should have regard to the right of a secured creditor to decide the timing of sale. The point arose because the charged property was intellectual

property the existence of which was disputed and subject to litigation. Although the joint administrators had entered into a limited sale agreement, the Judge was concerned that a resolution of the dispute at a later time might result in a substantially higher value. He, accordingly, invited submissions as to whether the wish of the fixed chargeholder to postpone a sale until after the litigation should be given effect to. Warren J did not decide the issue, finding, on the facts, that the litigation was not likely to be resolved imminently and that the balance was in of favour a sale. The litigation might have resulted in a nil value being ascribe to the IP assets. He, however, indicated that had he been required to decide the issue he would have taken the wish of the chargeholder into account in the exercise of his discretion, although he recognised the force of the submission that, unlike in a winding up, paragraph 71 of Schedule B1 to the Act had abrogated the right of a secured creditor to decide whether or not to sell and so it was not meaningful to ask when it wished to do so.

[Adam Al-Attar]

Re Arm Asset Backed Securities S.A. Chancery Division (David Richards J), 9 October 2013


FELICITY TOUBE QC

Provisional liquidation – Centre of main interests – EC Regulation

The company ("A") was incorporated under the laws of Luxembourg to issue bonds to investors. It did not obtain a licence from the Luxembourg regulator. Subsequently it became clear that such a licence was required, and A applied for one. However, the Luxembourg regulator refused to grant a licence. Accordingly, the business of A became paralysed and it was unable to issue any further bonds. The directors of A applied to the English High Court for the appointment of provisional liquidators ("PLs") to A. The petition was based on the 'just and equitable' ground. The directors contended that the centre of main interests ("COMI") of A was in the United Kingdom and that the English court had jurisdiction to appoint the PLs, notwithstanding the fact that A was incorporated in Luxembourg. The Judge held that the evidence in respect of the location of the A's head office functions was sufficient to rebut the presumption in Article 3.1 of the EC Regulation. Among other things, two of A's directors were resident in the UK and the third was resident in the Republic of Ireland. Further, A did not have any place of business in Luxembourg and it had never had any employees in Luxembourg. Re Eurofood IFSC Ltd (C-341/04) [2006] Ch. 508 applied. There remained, however, an issue as to whether the EC Regulation could apply to a petition based on the 'just and equitable' ground. It seemed arguable that the EC Regulation could apply only to petitions based on insolvency. That said, the evidence showed that A was insolvent and it was right to allow A to amend the petition to rely on insolvency. On this basis, the EC Regulation would apply and the English court would have jurisdiction to appoint PLs in respect of A.

[Felicity Toube QC, Stephen Robins]

Re Manches LLP (Asplin J), 14 October 2013


DAVID ALLISON

Administration application – Liberty to enter into pre-pack sale

The Court considered an application for an administration order in respect of Manches LLP and a request for liberty to enter into a pre-packaged sale of the business Penningtons Solicitors LLP. Liberty to enter into the sale was sought as the purchaser required that part of the purchase consideration was applied for the specific purpose of funding the repayment of partnership practice loans taken by partners to fund capital investments in the firm as opposed to forming part of the general estate for distribution to creditors of the firm in accordance with the respective priority of claims under the IA 1986. The Court made an administration order and gave the administrators liberty to enter into the pre-packaged sale. Asplin J was satisfied that the evidence displayed that the sale was the only real way forward (applying the test set out in Re Hellas Communications [2010] BCC 295) in view of the fact that (i) the next best offer was projected to realise a lesser sum for the general estate; and (ii) the evidence demonstrated that the collection of book debts in the course of an administration was likely to realise a lesser sum for the general estate, particularly in circumstances where the Solicitors' Regulation Authority would be likely to intervene in the absence of the pre-packaged sale.

[David Allison]

PERSONAL INSOLVENCY

Digested by MATTHEW ABRAHAM


MATTHEW ABRAHAM

Re Kapoor (In Bankruptcy) [2013] EWHC 2204 (Ch) (Penelope Reed QC), 25 July 2013

Bankrupt's duty to disclose information

The respondent was made bankrupt on 9 May 2012 and therefore, in accordance with s.279 of the Insolvency Act 1986, his discharge was due to take place on 9 May 2013. An application was made by the trustee in bankruptcy, pursuant to s.279(3) of the Insolvency Act 1986, to suspend the date of discharge of the bankrupt on the basis that the trustee suspected that the bankrupt had not disclosed relevant information relating to his assets. The trustee was late in bringing the application and as a result failed to comply with r.6.215(5) of the Insolvency Rules 1986 which requires evidence of the trustee to be served on the bankrupt at least 21 days before the date fixed for the hearing. Having gone through the case law in relation to s.279, including the case of *Bramston v Haut* [2013] 1 W.L.R. 1720, the Deputy Judge of the Chancery Division held that the purpose of an application under s.279 was both to penalise a non-compliant bankrupt as well as to aid in the trustee's collecting in, realising and distributing the estate of the bankrupt. The Deputy Judge found that there had been non-compliance on the part of the bankrupt. When determining whether to exercise her discretion the Deputy Judge found that the failure to comply with r.6.215(5) was not sufficient to militate against the Court exercising its powers under s.279. The case of *Chadwick v Nash* [2012] B.P.I.R. 70 was differentiated on the basis that, in that case, the trustee had done little to investigate the bankrupt's affairs during the course of the bankruptcy and the trustee was using the threat of applying to suspend discharge to obtain agreement to an income payments order from the bankrupt.

Times Newspapers Ltd v McNamara [2013] 1 All ER (D) 121 (Registrar Baister), 13 August 2013

Application for permission to inspect the court file

The applicant, Times Newspapers Ltd, applied, under r.7.31A(6) of the Insolvency Rules 1986, for permission to inspect the court file in bankruptcy proceedings concerning the respondent. The respondent was one of a number of Irish citizens who had sought relief from creditor pressure in the form of an English bankruptcy order. The bankruptcy order was made based on the evidence filed and without hearing the respondent. The applicant applied for sight of the court file, arguing that there was a strong public interest in discovering what security the banks had taken from the bankrupt before lending money to him, and what steps had been taken to prevent him dissipating his assets.

The Registrar granted the application holding that the administration of justice had to be open to journalistic scrutiny and that there were no factors to alter the default position. The Registrar drew five principles from the case of R (on the application of Guardian News and Media Limited) v City of Westminster Magistrate's Court [2012] EWCA Civ 420 when giving judgment: (a) that the administration of justice should be open, which includes openness to journalistic scrutiny; (b) that such openness extends not only to documents read in court but also to documents put before the judge and thus forming part of the decision-making process in proceedings; (c) that openness should be the default position of a court confronted with an application such as this; (d) however, there may be countervailing reasons which may constitute grounds for refusing access; (e) the court will thus in each case need to carry out a fact-specific exercise to balance the competing considerations. The Registrar also made it clear that r.7.31A was not limited to creditors or the official receiver.

McKinnon (Trustee in Bankruptcy of Richard David Graham) v Graham [2013] EWHC 2870 (Ch) (HHJ Behrens QC), 20 September 2013

Choice of law, Judicial Cooperation and Modified Universalism

The appellant bankrupt appealed against a District Judge's decision to apply Scottish law, under s.426(5) of the Insolvency Act 1986, in proceedings brought by the respondent trustee for the possession and sale of a property located in England. A sequestration order (bankruptcy) was made against the bankrupt in Scotland three years prior to the present application by the trustee in England. Under English law and Scottish law, property would revest in the bankrupt if no application was made to court within three years of the date of the bankruptcy. The two relevant statutory provisions differ in relation to a house occupied solely by the bankrupt. If a house is solely occupied by the bankrupt then there is no relief in Scotland (s.39A of the Bankruptcy (Scotland) Act 1985) but there is potential relief under English law if the house was his sole or principal residence (s.283A Insolvency Act 1986).

The appeal was dismissed on the basis that an appellate court would only interfere with the s.426(5) discretion if it was based on an error of law or if it was a decision

that no reasonable tribunal could have reached. The High Court Judge held that the District Judge had analysed the relevant law and had correctly concluded that the principle of modified universalism required him to apply Scottish law unless (a) it would be manifestly unfair or would offend against insolvency proceedings already taking place in England or against the general principle underlying insolvency law of fair distribution of assets amongst creditors; (b) it was otherwise against public policy. The High Court Judge found that this was not an exceptional case so as to exclude the principle of modified universalism and the District Judge's decision was not open to criticism. The decision in *Re HIH Casualty & General Insurance Ltd* [2008] UKHL 21 as explained in *Rubin v Eurofinance* [2012] 2 BCLC 682 was followed.

OTHER CASES

Digested by HENRY PHILLIPS

Rawlinson and Hunter Trustees and ors v (1) Stephen John Akers (2) Mark MacDonald [2013] EWHC 2297 (QB) (Eder J), 26 July 2013

Third Party Disclosure – Privilege – Loss of confidentiality


WILLIAM TROWER QC


HENRYPHILLIPS

The Respondents are the joint liquidators of the Oscatello Group of companies, which operated under the umbrella of a trust in favour of Robert Tchenguiz and his children and remoter issue. The Oscatello Group of companies held positions in valuable assets by way of direct equity / debt investments and participated in large-scale derivatives and futures trading. Their investment activities were largely funded by Kaupthing hf. The Serious Fraud Office ("SFO") launched an investigation into the involvement of Robert and Victor Tchenguiz in Kaupthing's collapse. During the course of the SFO's investigations, the Respondents gave the SFO permission to read (but not take copies of) a number of reports which had been produced at the Respondents' request (the "Reports"). The Tchenguiz brothers were arrested in March 2009. On the same day, the SFO executed search warrants obtained in respect of properties used by the Tchenguiz brothers. The Reports had been relied upon by the police in order to obtain the search warrants. Notes of the contents of the Reports, but not the Reports themselves, had been exhibited to a witness statement produced for that purpose. As is now notorious, those search warrants were subsequently quashed in judicial review proceedings and the SFO ceased its investigation into the Tchenguiz brothers. The Tchenguiz brothers subsequently commenced proceedings against the Director of the Serious Fraud Office, alleging that the effect of the searches, arrests and investigation surrounding them was to cause extensive financial losses and reputational harm. The basis of those claims is that the SFO did not have reasonable grounds to suspect the Tchenguiz brothers of having committed a crime. During the course of the proceedings brought against the SFO, the Tchenguiz brothers made an application seeking third party disclosure of the Reports from the Respondents under CPR rule 31.17(3). The Respondents opposed the application on three main grounds i.e. (i) necessity/relevance (ii) litigation privilege; and (iii) discretion. The Judge held that the Reports were clearly necessary and relevant to the proceedings. As to litigation privilege, the Applicants contended that if the Reports had been subject to litigation privilege, the right to assert it had been lost because confidentiality no longer attached to the Reports as notes of their contents had been exhibited to a witness statement.The Judge was not satisfied on the evidence before him that the Reports had been produced for the dominant purpose of aiding actual or contemplated litigation, as opposed to having been produced for the purpose of assisting the Respondents in discharging their statutory duties as joint liquidators of the Oscatello companies. As to loss of confidentiality, even on the assumption that there was a loss of confidentiality in respect of the information contained in the notes of the Reports, it did not follow that there was a loss of confidentiality in the Reports themselves. The Judge held that the Reports were not in the public domain and that confidentiality still attached to them. However, the point was academic as the Reports had not, in any event, been created for the dominant purpose of aiding actual or contemplated litigation. The Judge exercised his discretion in favour of disclosure. **[William Trower QC; David Allison; Henry Phillips]**

Parvalorem SA v Oliveira & ors, Chancery Division, (Warren J), 2 October 2013

Freezing injunctions – Interim relief in aid of foreign proceedings – Business and legal expenses exceptions


BEN VALENTIN

In order to be allowed to spend monies subject to a freezing injunction, the respondent must satisfy the court that he has no other assets which he can use. It followed that an interim freezing injunction in aid of civil proceedings in Portugal, granted over sale proceeds from an auction of classic cars in England, should not contain the usual exception to allow payments in the ordinary course of business, where the court was able to infer on the existing evidence that there were sufficient free assets elsewhere from which those payments could be made. The usual exception for payment of legal expenses would also be omitted unless the respondent provided satisfactory evidence on affidavit that it had insufficient free assets elsewhere. **[Ben Valentin]**

Offshore Special: Jersey & Guernsey

Recent developments in the jurisprudence of the Channel Islands by **Jeremy Wessels** and **Jonathan Speck** of Mourant Ozannes.

JERSEY

Jersey has in recent years developed a significant reputation in two particular areas which I hope the reader will find of particular interest: firstly, as one of the leading lights in the development of jurisprudence in traditional chancery work; and secondly, as a destination for gourmets. And for those who consider neither of these especially appealing, they may find developments in relation to revenue collection, Foundations, litigation funding agreements and organs of the state of at least passing interest.

The Taxman Cometh

There has been much debate internationally about transparency so far as revenue matters are concerned. This has led to a proliferation of TIEAs (tax information exchange agreements) in particular between IFCs (international finance centres, the new name for offshore centres or, worse, tax havens) and so-called onshore jurisdictions. These agreements are beginning to be tested in the Courts of the IFCs, including Jersey. In the case of *Volaw & Larsen v The Comptroller of Income Taxes* [2013] JRC 095, the Royal Court considered for the first time the nature and extent of the duties operating on the relevant Jersey authority (the Comptroller of Income Taxes) when considering a request for assistance from a foreign revenue authority. The Comptroller issued a notice requiring a financial services business in Jersey to provide information. That business and the taxpayer appealed on the basis (*inter alia*) that there were no reasonable grounds for believing that the taxpayer may have failed to comply with the relevant domestic revenue law and that the exercise amounted to a fishing expedition. It was argued that the Comptroller had failed to approach his task with the requisite degree of rigour and that he had, in effect, abrogated his quasi-judicial, gate-keeper function in favour of adopting uncritically what the foreign tax authority asserted. The Court examined in some detail the particular transactions in which the foreign revenue authority was interested. The Court was firmly of the view that the Comptroller should look at the totality of the information available to him, but that it was not for him effectively to act as an adjudicator where there were conflicting assertions from the authority and the taxpayer. He was to be given a margin of appreciation in assessing whether he had reasonable grounds for issuing a notice.

The tax authority had provided considerable detail to the Comptroller. The transactions in question made little commercial sense. In the circumstances, the Court was satisfied that the Comptroller had very good grounds for believing that the tax authority's suspicions could be well founded. The allegation of a fishing expedition was unfounded and the Comptroller's issue of a notice was upheld.

At the time of writing, a decision is awaited from the Court of Appeal on appeal from this decision. Nevertheless, it is clear that the Comptroller is not able to permit simple fishing expeditions from foreign revenue authorities, and that the Court will carefully review his actions to ensure that the protections afforded by the Jersey legislation to taxpayers and local financial institutions are complied with.

The Jersey Foundation

Jersey has for many years had a reputation as a premier trusts jurisdiction. In 2009, it sought to expand the services

GOREY CASTLE, JERSEY

available in the Island by introducing the Jersey law foundation through the Foundations (Jersey) Law. The Royal Court had occasion, for the first time, to analyse the nature of a foundation in *In the matter of A Limited and the F Foundation* [2013] JRC 075. The sole remaining beneficiary of the Foundation was B, against whom substantial judgments had been taken in Russia by N. N sought to enforce against the assets of the Foundation in proceedings brought in Jersey. The Foundation was administered by a Council, which under Jersey regulations is required to have a qualified (in essence, a Jersey regulated financial services business) member, A Limited. A Limited applied to the Royal Court for directions as to how it should respond to the claim. The Court confirmed that it had a broad jurisdiction to grant relief to a council member in these circumstances, and in the circumstances of this case directed A Limited to adopt a neutral stance. This was not the same as Beddoe relief in the context of a trust, but more akin to the Court's general supervisory jurisdiction in relation to trusts and to assist in the blessing of momentous decisions as in *Public Trustee v Cooper*.

In analysing the nature of a foundation, the Court observed that there were significant differences between a foundation and a trust. A foundation probably owes no duties to its "*beneficiaries*" unless and until they become entitled to compel it to transfer to them some particular asset. The general duty that might be owed is a duty of care. The foundation's "*officers*" in the form of the council members owe duties to the foundation itself, not to the beneficiaries, which are articulated in the Foundations Law in a manner analogous to the duties owed by directors to their companies. In particular there is both a fiduciary obligation of loyalty whereby they must act "*honestly and in good faith with a view to the best interests of the foundation*" and a duty to exercise reasonable care, diligence and skill. Finally, it was clear that the regime which is to apply to foundations is radically different from that which applies to

It was clear that the regime which is to apply to foundations is radically different from that which applies to Jersey-incorporated companies when it comes to the Court's jurisdiction to intervene in their affairs.

Jersey-incorporated companies when it comes to the Court's jurisdiction to intervene in their affairs.

In conclusion, therefore, the position appears to be that a foundation is closer in nature to a company than it is to a trust, albeit that, unlike the position with a company, the council members of a foundation can take advantage of the wide-ranging jurisdiction of the Court to give directions and to bless momentous decisions.

Litigation Funding Agreements

In another important decision given by the Court in 2013, *Barclays Wealth Trustees (Jersey) Limited & anr v Equity Trust (Jersey) Limited & anr* [2013] JRC 094, litigation funding agreements have been upheld: they do not infringe the Jersey rules against champerty, nor will they offend against certain ancient rules of customary law which apply in Jersey to the effect that no contracts in relation to matters in litigation are permitted. In the case of Barclays, the new trustee was suing the former trustee in connection with its administration of a Jersey trust and had obtained funding from Harbour Litigation Investment Funding LP. The former trustee alleged that there was a blanket prohibition on contracting in relation to things or matters in litigation and that this included litigation funding arrangements. The funding arrangement was, they argued, therefore contrary to Jersey law and the proceedings amounted to an abuse of process. The Royal Court roundly rejected these arguments. The position on third-party funding is, therefore, now well established. The Jersey court is firmly behind the public policy objective of broadening access to justice and third party funding arrangements are key to that. Properly constituted funding arrangements where there is no assignment of the claim to the funder, where it is the party and not the funder who has control of the litigation and where there is proper provision made for the payment of adverse costs orders will not be champertous or otherwise improper. However, it is essential to ensure that such agreements are carefully drafted so as to comply with these requirements.

Mourant Ozannes' Advocate Justin Harvey-Hills acted for Barclays.

JONATHAN SPECK: MOURANT OZANNES' JOINT HEAD OF INTERNATIONAL TRUSTS & PRIVATE CLIENT TEAM IN JERSEY

The following members of South Square have previously acted in relation to Jersey cases.

Michael Crystal QC
Gabriel Moss QC
Simon Mortimore QC
Richard Sheldon QC
Richard Hacker QC
Robin Knowles CBE QC
Martin Pascoe QC
David Alexander QC
Glen Davis QC
Barry Isaacs QC
Felicity Toube QC
Mark Arnold QC
Jeremy Goldring QC
John Briggs
Adam Goodison
David Allison
Tom Smith
Stephen Robins
William Willson
Adam Al-Attar
Henry Phillips
Charlotte Cooke
Alexander Riddiford

The Rule in Hastings-Bass

Chancery practitioners will of course be familiar with this rule, which at least until recent decisions in the Supreme Court (see *Futter v Futter* and *Pitt v Holt* (2013)) allowed actions by trustees to be unwound in certain circumstances. The utility of the rule has now been substantially curtailed in England, but the good news in Jersey is that the legislature has amended the Trusts (Jersey) Law so as to maintain the remedy as previously formulated.

The new statutory provisions (which should come into force at about the time this Digest is published) cover the following four areas: (1) setting aside a settlor's transfer into a trust on the

ground of mistake; (2) setting aside an exercise of a fiduciary power in relation to a transfer into trust on grounds falling within the rule in Hastings-Bass; (3) setting aside an exercise of a power in relation to a trust on the ground of mistake; and (4) setting aside an exercise of a power in relation to a trust on grounds falling within the rule in Hastings-Bass.

In relation to Hastings-Bass, the requirements will be that the trustee or person exercising a power failed to take into account any relevant considerations or took into account irrelevant considerations, and would not have exercised the power, or would not have exercised the power in the way it was exercised, but for that failure to take into account relevant considerations, or but for that taking into account of irrelevant considerations. It will not matter whether the grounds occurred as a result of fault on the part of the trustee or person exercising the power or on the part of any adviser in relation to the exercise. This is different from the position in English law following the recent decisions of the Supreme Court referred to above.

In relation to mistake, the requirements will be that the trustee or person exercising a power made a mistake in relation to the transfer or exercise of the power, and would not have made the transfer or would not have exercised the power, or would not have exercised the power in the way it was exercised, but for that mistake, and the mistake is of so serious a character as to render it just for the court to intervene. The mistake may be as to the effect, consequences or advantages of the relevant exercise, and either as to law (including foreign law) or fact.

Recovery of costs from the trust fund by a non-trustee

The Royal Court gave a landmark decision on the ability of a person, other than a trustee, but acting as a fiduciary, to recover costs incurred in connection with the discharge of their fiduciary functions. In the case of *In the matter of the HHH Employee Trust* [2012] JRC 127B and [2013] JRC 021, a beneficiary of an employee benefits trust sought (*inter alia*) certain information from the settlor employer, which had certain fiduciary obligations. The Court considered that the issue of the extent of the settlor's obligation as a fiduciary to make disclosure to a beneficiary was a question which arose in the administration of the trust, and it was for the benefit of the trust estate that the question be determined. In these circumstances, the settlor was entitled to an indemnity for its costs out of the fund.

On analysis, the beneficiaries were bringing the proceedings in effect as a derivative action to recover funds for the benefit of the fund and therefore for the benefit of the trust estate.

Vulture Funds and Organs of the State: Piercing the Veil

Over the last couple of years, a good deal of publicity has attached to the efforts of so-called vulture funds, that is to say funds which acquire (often at a discount) debts of sovereign states, to collect on those debts against commercial operations owned by the state on the basis that they are organs of the state. One such case involved long-running litigation in Jersey, ultimately ending in the Privy Council, in the case of *La Generale des Carrieres et des Mines v FG Hemisphere Associates LLC* (2012). The Privy Council's decision was of particular importance as it went right to the heart of the rule that a company is a separate legal entity with limited liability and no responsibility for the debts of its shareholders. The question for the Privy Council was whether a different rule to that normally applicable to the lifting of the veil of a private company applied to state-owned companies. The Privy Council held that the rules were slightly different for state-owned companies, but that they were still stringent. The Court should consider the entity's constitution, control and functions, the nature of its activities and whether such activities were in themselves sovereign were of particular importance. The strong presumption was that a state-owned company's separate corporate personality would be respected, particularly where the entity had its own management and budget and where it had been set up for commercial or industrial purposes. The presumption would only be displaced in extreme circumstances where the entity had no effective separate existence from the state. This would require the creditor to prove that "*the entity and the State were so closely intertwined and confused that the entity could not properly be regarded for any significant purpose as distinct from the State*".

This decision is of considerable importance to those who transact with state-owned companies. Had the test for state-owned companies been made significantly lower than that of privately-owned companies, creditors of state-owned companies would have been placed at considerable risk. This would ultimately have made it much more difficult and expensive for such companies to undertake business. A lower test could also have had the unintended consequence of conferring sovereign immunity on those state-owned companies in certain circumstances. *Mourant Ozannes' Advocate Justin Harvey-Hills acted for La Generale des Carrieres et des Mines.*

Beddoe application by a beneficiary

The Royal Court considered for the first time, in In the matter of the X Trust [2012] JRC 171, an application by the principal beneficiaries of a trust for a direction that they may prosecute a breach of trust claim which they had brought against the continuing trustee, at the expense of the fund itself. On analysis, the beneficiaries were bringing

the proceedings in effect as a derivative action to recover funds for the benefit of the fund and therefore for the benefit of the trust estate. It was therefore a claim brought by the beneficiaries as if they were in fact acting as trustee. In these circumstances, the Court had inherent jurisdiction to grant relief to the beneficiaries so as to have the benefit of a pre-emptive order as to costs. This the Court did.
Mourant Ozannes' Advocate Bruce Lincoln acted for the trustee.

Jersey: the Perfect IFC?

Those professionals who advise their clients on which IFC to do business with are faced with an increasingly broad choice. Many will rightly have regard to such key factors as geographical location, governmental stability, the rule of law, the availability of expert professional services and so on. However, there are, for at least some professionals, three far more important considerations: (1) does British Airways fly there; (2) is the hotel accommodation sufficiently luxurious; and (3) will the dining experience be up to my exacting epicurean requirements. And the good news is that Jersey can answer a resounding Yes, Yes, Yes to all three.

The first question is an easy one. There are currently five BA flights daily from Gatwick, between 7.30am and 7.30pm. The flight takes only 35 minutes and there are liberal supplies of Champagne in Club Europe.

As for accommodation, this ranges from the luxurious and traditional Relais & Chateaux hotel, Longueville Manor, through the business-friendly and well-located Club Hotel & Spa, Royal Yacht Hotel and Radisson Hotel in St Helier, to the Hotel l'Horizon right on the beach in St Brelade's Bay and on to the Atlantic Hotel with fabulous views of, you've guessed it, the Atlantic Ocean and the other Channel Islands. There are many other quality hotels too numerous to mention in this article.

Remarkably, Jersey is blessed with no fewer than four Michelin-starred restaurants. The newest, Ormer by Shaun Rankin, is named after a rare shellfish (similar to an abalone) found in local waters, and is in the style of a French bistro. The cooking is, according to the inspectors, unfussy, refined and assured, and uses only the very best seasonal island produce. Bohemia (conveniently located immediately opposite the author's office) is a hotel restaurant with a chic bar and a stylish, candlelit dining room. The emphasis is on tasting menus, with fish featuring predominantly. The cooking is modern, vibrant and has a lightness of touch; original texture and flavour combinations feature, with charming, attentive service. The third is Tassili, at the Grand Hotel in St Helier, where if you feel so inclined you can watch on a screen footage from the kitchen hotplate. Again, the cooking is innovative and focuses on the best of local island produce. Finally, there is Ocean at the Atlantic Hotel. It boasts a traditionally elegant, well-run dining room, in a stunning position overlooking St Ouen's Bay. Local produce dominates again.

We truly are spoilt for choice!
Mourant Ozannes' Advocate Jonathan Speck regularly dines in these and other restaurants.

JEREMY WESSELS: MOURANT OZANNES' JOINT HEAD OF THE INTERNATIONAL TRUSTS & PRIVATE CLIENT TEAM IN GUERNSEY

GUERNSEY

Forum Selection Clause Fails to Take Centre Stage:- A Trip to Guernsey From Delaware

In *Carlyle Capital Corporation Ltd (in liquidation) and ors v William Conway Jr and ors* (5 March 2012), the Guernsey Court of Appeal determined that the appropriate forum for the trial of the entire action was Guernsey and not Delaware notwithstanding a forum selection clause (**FSC**) in an investment management agreement (**IMA**) between CCC and the Eighth Defendant, Carlyle Investment Management LLC.

In a multi-party dispute the fact that one party has the benefit of a FSC does not necessarily determine the proper jurisdiction for the whole dispute.

Brief facts

On 29 August 2006 CCC was incorporated in Guernsey. It was promoted by the Carlyle Group, one of the world's largest private equity firms, to invest in residential mortgage backed securities.

By July 2007 CCC had raised capital totalling US$945 million through a series of private placements and an initial public offering. It was listed on the Euronext Exchange in Amsterdam.

On 17 March 2008 CCC was placed into compulsory liquidation in Guernsey on the application of the Directors of CCC.

Between July 2007 and March 2008, when CCC was ordered to be wound-up, CCC's entire capital of $945 million was lost and CCC has a substantial deficit.On 7 July 2010 the Joint Liquidators issued protective proceedings in four separate jurisdictions: Guernsey, Delaware, District of Colombia and the State of New York. The proceedings were brought against CCC's de jure directors (**D1-D7**) and three corporate entities alleged to have been de facto or shadow directors of CCC (**D8-D10**).

On 7 July 2010 the Royal Court granted leave to serve out of the jurisdiction on each of D1-D6 and D8-D10, D7 being resident in Guernsey.

The Plaintiffs alleged that the Defendants acted in reckless breach of their fiduciary and other duties to CCC, were tainted by conflicts of interest and wrongfully traded so as to render CCC's insolvent liquidation inevitable.

The Plaintiffs also pursued statutory insolvency claims under the *Companies (Guernsey) Law* against each of the Defendants for misfeasance, wrongful trading and disqualification, together with non-statutory claims for breach of fiduciary and other duties for damages to be determined at trial exceeding US$1 billion.

By applications dated 28 February 2011, the non-resident Defendants applied to set aside the leave granted to serve out of the jurisdiction or, alternatively, for an order that proceedings be stayed pending the outcome of the proceedings in Delaware.

The Royal Court judgment

By judgment dated 22 July 2011, the Royal Court refused to set aside leave to the Plaintiffs to serve the Cause out of the jurisdiction, but ordered that the claims in the Cause be stayed pending a trial of any action against all the Defendants by the Plaintiffs in Delaware.

The Court of Appeal judgment

By judgment dated 5 March 2012, the Court of Appeal overturned the Royal Court's decision and determined that the appropriate forum for the trial of the entire action was Guernsey and not Delaware.

The reasons for the Court of Appeal's decision included:

- Only the Royal Court has jurisdiction to consider all the Plaintiffs' claims, in that only the Royal Court has jurisdiction over the Joint Liquidators' statutory insolvency claims.
- Guernsey law governs the majority of the Plaintiffs' claims and that it is "obvious beyond a peradventure that a Guernsey Court will be able to deal more directly, and shortly and cost effectively with such issues which are freighted by considerations of legal domestic policy, potentially particular to offshore jurisdictions".
- The place of incorporation will presumptively be the appropriate forum for the resolution of disputes internal to a company whose laws govern those issues and because of its ability to judge matters by its own standards of business conduct.
- The Defendants chose Guernsey as the place of incorporation of CCC, D1-D7 chose to take office as directors of a Guernsey company and chose Guernsey as the place for CCC's liquidation, such that they must have contemplated that they could face litigation in Guernsey.
- The logistical considerations relied upon by the Defendants as to location of potential witnesses and documents did not tilt the balance away from Guernsey.
- It was highly desirable that all heads of relief are determined in the same set of proceedings in a single jurisdiction and that "unless split hearings are required, they should be rejected as modus operandi".
- Despite the Defendants' reliance on the FSC described by the Court of Appeal as "the jewel in the crown of the Directors' submissions" there were strong reasons not to give effect to the Delaware FSC in the IMA in favour of D8, being the only Defendant with the benefit of the FSC in multi-party litigation which did not "fundamentally alter the nature of the Liquidators' pleaded case against the Directors in such a way that the IMA takes centre stage".

The Defendants' application for leave to appeal to the Judicial Committee of the Privy Council was dismissed on 30 May 2012.

This decision demonstrates that in a multi-party dispute the fact that one party has the benefit of a FSC does not necessarily determine the proper jurisdiction for the whole dispute. In this case, the existence of statutory insolvency claims that could only be brought in the Royal Court of Guernsey turned out to be the decisive factor in the determination that Guernsey was the proper forum for the resolution of the dispute.

Mourant Ozannes' Advocate Jeremy Wessels acted on behalf of CCC.

Guernsey Court of Appeal Upholds Grant of Anti Anti Suit Injunction

In the next stage of the proceedings in *Carlyle Capital Corporation Ltd (in liquidation) and ors v William Conway Jr and ors* (5 March 2012), the Guernsey Court of Appeal upheld the decision of the Royal Court of Guernsey to grant an

anti anti-suit injunction to restrain three of the Defendants ("the Carlyle Defendants") from seeking to rely upon the same forum selection clause (**FSC**) that had been considered in the hearing to determine the proper forum for the litigation in an effort to obtain an anti-suit injunction against the Plaintiffs before the Delaware Court.

Brief facts

In his judgment of 22 July 2011 the Deputy Bailiff stayed the proceedings in Guernsey on the basis that the Liquidators should litigate their non-statutory claims in Delaware and only thereafter litigate their statutory claims in Guernsey.

The liquidators pursued an appeal to the Court of Appeal but before that appeal was heard the Carlyle Defendants applied for summary judgment before the Delaware Chancery Court for an anti-suit injunction to prevent the pursuit of the claims against them including the prosecution of the appeal before the Guernsey Court of Appeal.

On 7 October 2011 an *ex parte* application was granted by Judge Finch in favour of the Plaintiffs restraining the Carlyle Defendants from pursuing the proceedings in Delaware. An application before Judge Finch to discharge the injunction was dismissed and the Carlyle Defendants appealed.

The Court of Appeal judgment

The Court of Appeal dismissed the appeal.

The reasons for the Court of Appeal's decision included:

- The paramount objective is the ends of justice. Insofar as discrete categories of cases in the granting of such an injunction have been identified, they are not exhaustive. Even within the category to which the greatest attention was paid in the present case, that is to say the restraint of vexatious or oppressive conduct, that too was a flexible concept.
- The Court of Appeal had gone significantly further than finding Guernsey to be *forum conveniens*, it had decided that the Guernsey court is the *only* court in which all the causes of action, common law and statutory, can be pursued.
- The overall interests of justice favoured the grant of the anti-anti-suit injunction. The FSC was not a trump card which overrides all other considerations because of the need to avoid fragmentation and inconsistent judgments.
- The Carlyle Defendants were seeking *"to re-litigate the same issues in Delaware, with a necessary concomitant of depriving the Royal Court of its jurisdiction in the matter notwithstanding the fact that an appellate court has determined that Guernsey is clearly and distinctly the appropriate forum for the trial of the Liquidators' claims (and the <u>only</u> available forum for the trial of <u>all</u> the Liquidators' claims).We would therefore, if necessary, characterise the purpose of the Carlyle Defendants' pursuit of the Delaware Anti-Suit Proceedings, and of this Appeal, as vexatious."*

The paramount objective is the ends of justice. ...the restraint of vexatious or oppressive conduct...was a flexible concept.

The Carlyle Defendants' application for leave to appeal to the Judicial Committee of the Privy Council was dismissed on 30 May 2012.

The decision illustrates the ability of the Court to fashion relief to suit the justice of the case before it. Having decided that Guernsey was the only forum in which the Plaintiffs claims could all be pursued in one forum, and that the statutory insolvency claims could only be tried before the Guernsey Court, the Court upheld an in junction designed to ensure that the Plaintiffs proceedings could indeed be heard before the Guernsey Court. Again, the forum selection clause was not determinative and, had it been applied, would have led to the fragmentation of proceedings and deprived the Plaintiffs of statutory claims vested in them as a result of the liquidation of CCC.

Mourant Ozannes' Advocate Jeremy Wessels acted on behalf of CCC.

Guernsey: The following members of South Square have previously acted in relation to Guernsey cases

Michael Crystal QC
Simon Mortlmore QC
Richard Sheldon QC
Richard Hacker QC
Robin Knowles CBE QC
Martin Pascoe QC
Glen Davis QC
Barry Isaacs QC
Felicity Toube QC
Mark Arnold QC
Jeremy Goldring QC
Lucy Frazer QC
Lloyd Tamlyn
David Allison
Tom Smith
Stephen Robins
William Willson
Adam Al-Attar
Henry Phillips

Guernsey Court of Appeal Clarifies the Law in Relation to External Restraint Orders

In its judgment in *HM Procureur v King & HSBC Trustee (Guernsey) Limited* the Court of Appeal ruled that the discretionary power given to the Royal Court to discharge or vary a restraint order in support of "external proceedings" did not permit it to consider allegations of undue delay in those proceedings. The Court of Appeal reversed the decision at first instance and ordered the restraint order, originally made in June 2006, should continue, despite there being no prospect of a trial in the South African proceedings in the foreseeable future.

The prosecuting authority of any country may request the assistance of Her Majesty's Procureur to restrain assets in support of criminal proceedings, including investigations. The decision in *HMP v King* represents the first time the Court of Appeal has considered the

discretionary power to discharge a restraint order granted in support of such external proceedings. Neither the Guernsey provision nor its equivalent in the United Kingdom have previously been the subject of detailed judicial consideration.

The Court of Appeal held the starting point was that a valid restraint order had been made. A material change in the circumstances would provide an opportunity for review. However, so the Court of Appeal held, "delay" did not fall within the parameters which the Royal Court, in making the restraint order, ought to have had in mind in undertaking such a review. The Court of Appeal noted the need to give due respect to courts of sovereign jurisdictions and found that consideration of such delays should not play a part in the exercise of a general discretion.

The decision of the Court of Appeal significantly restricts the scope of the discretionary power to discharge restraint orders made in support of external proceedings. The Court of Appeal said the approach taken "*does not deprive the Guernsey framework of practical effect*" and that circumstances may arise which permit the variation or discharge of a restraint order. However, the Court of Appeal's view is such circumstances are restricted to those in which there has been a "*change in circumstances*" from that which existed at the time the restraint order was made and which, expressly or impliedly, were the basis upon which the order was made.

The decision demonstrates the strength of the public policy considerations applied by Guernsey courts in support of criminal proceedings in other jurisdictions. Despite an equivalent order over the trust's English assets being discharged by the Southwark Crown Court (although under a different statutory regime) the Court of Appeal took a narrow view of the discretion under Guernsey law.

The decision also brings into focus the potentially lengthy and costly exposure facing those holding assets when these external restraint orders are made. Delay will not be a ground for discharge, and trustees, banks and custodians will be caught holding and managing restrained assets for an indefinite period while criminal proceedings (to which they are not a party) make their way through foreign courts.

Mourant Ozannes' Advocates Christopher Edwards and Abel Lyall acted on behalf of the Trustee, HSBC.

Note on the Decision in Ben Nevis and Anor v Commissioners for HM Revenue & Customs – Court of Appeal [2013] EWCA CIV 578

End of the revenue rule?

It is a well-established and almost universal principle that courts of one country will not enforce the revenue laws of another country. The *"revenue rule"*, as noted in England by the House of Lords decision in *Government of India v Taylor*, has been widely recognised for many years.

However recent years have seen substantial moves away from the revenue rule through the use of international agreements. Many bilateral and multilateral tax assistance treaties now include provisions for the collection and recovery of taxes. In many cases these treaties have been introduced by way of protocols which amend existing double taxation agreements.

Changes to such existing tax conventions brings into focus how far back authorities can reach to recover tax debts which were, until those changes, unenforceable. In its decision in *Ben Nevis Holdings Limited and Anor v HMRC* the English Court of Appeal has considered this question in the context of the Tax Convention between the UK and South Africa. The Court of Appeal held that not only did the 2010 Protocol permit recovery of taxes assessed prior to its introduction but also taxes prior to the commencement of the 2002 Convention it amended. In theory, authorities in South Africa could use the 2010 amendments to the Tax Convention to recover all tax debts irrespective of their age, subject only to any limitation periods.

Ben Nevis is a BVI company owned by a Guernsey Trust, and held various assets including interests in South Africa. In 2002 Ben Nevis was assessed by the South African Revenue Service (**SARS**) for taxes for the years 1998, 1999 and 2000. Ben Nevis appealed the assessments but in October 2010 was ultimately determined to be liable for a total sum of 2.6 billion Rand or approximately £222 million. At each of the relevant tax years, the date the tax assessment was issued and the date of the ultimate determination of the appeals against the tax assessment there was no provision permitting the enforcement of South African revenue debts in the UK. It was not until October 2011 that a protocol amending the UK/South Africa Tax Convention was introduced providing for mutual assistance in the collection of taxes (the **Protocol**).

Following the introduction of the Protocol SARS approached HMRC for assistance to recover the taxes owed by Ben Nevis in South Africa. Ben Nevis resisted the proceedings commenced by HMRC *inter alia* on the basis that the debts to which the enforcement was sought predated the Protocol and the Convention.

At first instance the High Court found that the Convention as amended by the Protocol applied to the tax debts notwithstanding that those debts are due in respect of years of the assessment prior to the coming into force of the Convention. On appeal by Ben Nevis, the Court of Appeal upheld this decision.

Article 27 of the Convention provided an "entry into force" provision which stated that the Convention entered into

Recent years have seen substantial moves away from the revenue rule through the use of international agreements.

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The Court of Appeal expressed the view that the Revenue Rule did not exist for the "benefit or protection" of tax payers but rather was created for the protection of the sovereign power of State.

force on 17 December 2002 and that the Convention had application in respect of South African taxes from January 2003. The Protocol introduced Article 25 (a) to the Convention. The only temporal limit stated in the Protocol was that it shall have effect in respect of requests for assistance made on or after the date that the Protocol came into force.

The Court of Appeal held that the Protocol of itself contained an "*entirely sensible and workable*" provision for assistance in the collection of taxes and it was unnecessary to resort to Article 27 of the Convention to impose a temporal limitation. The Court contrasted this with the Double Tax arrangements which it considered needed to be delineated in time such that a party knew whether the arrangements were covered by the Convention or earlier treaty. The Court also held that the presumption that applies against legislation having retrospective effect had no application in this case as the application of the Protocol to taxes arising prior to the Convention did not involve any "*objectionable*" retrospective effect.

The Court said that it does not change the relevant law, does not confer on any person a power to act with retrospective effect and does not alter the legal incidence of a transaction or other conduct affected before its commencement. In effect, the Court of Appeal was of the view that Ben Nevis became subject to liability to pay South African taxes and that liability was not changed by the Protocol. In the view of the Court there is "*no unfairness*" in permitting the enforcement of pre-existing tax liability. The Revenue Rule prohibited the enforcement of foreign tax liabilities in the UK however that Rule was always liable to be set aside by Treaty. As such Ben Nevis could have no "*legitimate expectation*" that the revenue rule would not be abrogated in the future.

Looking more broadly, the Court of Appeal expressed the view that the Revenue Rule did not exist for the "*benefit or protection*" of tax payers but rather was created for the protection of the sovereign power of State.

The Court of Appeal decision demonstrates clearly that companies can no longer rely on the revenue rule to safeguard English based assets against claims by foreign revenue authorities. The increasing number of mutual assistance

conventions now including assistance with revenue enforcement means the absence of a present enforcement provision will not avoid the imposition of a liability in the future. Companies and trustees which hold UK assets while undertaking business in other countries will need to be mindful of future enforcement risks should a tax liability be incurred.

There are no signs at present that Guernsey proposes to sign up to similar agreements under its mutual assistance arrangements. However should such enforcement provisions become a new international standard, the pressure from the UK and elsewhere may become overwhelming.

Guernsey Court Refuses SEC Permission to Join Proceedings

The US Securities and Exchange Commission (**SEC**) has failed in an attempt to join interpleader proceedings in Guernsey dealing with substantial assets claimed to be the proceeds of a fraud alleged against Nikolai Battoo and the BC Capital Group.

In *The United States Security and Exchange Commission v EFG Private Bank (Channel Islands) Limited & Ors* (18 July 2013) the Royal Court held that the SEC had failed to establish a sufficient interest in the interpleader relief and that it would not be "just and convenient" for it to be joined.

The interpleader proceedings were commenced by EFG Bank on 23 March 2013 in the face of competing claims to assets it held as custodian by the BVI liquidators appointed to various "Battoo" hedge funds and Receivers appointed by the US Court at the request of the US Commodity Futures Trading Commission (**CFTC**). The SEC, which along with the CFTC had obtained injunctive relief in the US Courts against Nikolai Battoo and his related entities, applied to join the Guernsey interpleader proceedings.

The Court had to consider whether the SEC met the test in the decision of *Gresh v RBC Trust Company (Guernsey) Ltd and HM Revenue and Customs [2009-2010] GLR 239*. In *Gresh*, HMRC successfully applied to join an application to set aside a distribution to beneficiaries under the *Hastings-Bass* principles. The Court noted that in order to join proceedings a party must demonstrate that:

1/. There is a question or issue between the joinder applicant and a party to the action;

2/. The question or issue arises out of, or relate to, or be connected with any relief or remedy claimed in the proceedings;

3/. It is just and convenient to determine that issue in the proceedings.

Applying the first limb of the *Gresh* test, the Court held that there was a question or issue between the SEC and other parties to the interpleader proceedings. In particular, the Court noted the SEC asserted the assets in Guernsey represent the proceeds of crime and cannot be claimed by the BVI liquidators and the "Battoo" hedge funds.

The Court however was not satisfied that the second and third limbs of the test had been met. It noted that the SEC did not assert any direct claim to the assets but rather that it had "an interest in what happens" to them. Such an interest in the Court's view was "too far removed" from the issues or questions in respect of the relief sought by EFG Bank.

Even if it was wrong on the second limb, the Court was of the view that it was not "just and convenient" to determine whether the assets held by EFG Bank represent the proceeds of crime in the interpleader proceedings. In doing so the Court acknowledged that this was a balancing exercise, but was particularly mindful of the effect that joinder would have on the timetable of proceedings which had begun some months prior. In light of evidence that a number of proceedings in relation to these issues were already underway in other jurisdictions, the Court placed lesser emphasis on the need to avoid a multiplicity of proceedings than might normally be the case. It was also noted that there was a degree of alignment between the interests of the SEC and the Receiver. The Receiver was appointed by the same court which granted asset freeze orders to the SEC and the appointment of the Receiver at the request of the SEC's "sister agency" the CFTC. Unlike in *Gresh*, where HMRC wanted to raise arguments which would not be made by other parties, the Court considered there was a degree of concession that the SEC would be able to assist the Receiver without being made a party and that the arguments to be advocated and the evidence to be led would be closely aligned.

The decision reinforces the need for parties who wish to be heard in civil proceedings in Guernsey to ensure they can establish a direct or substantive interest.

The decision gives further helpful guidance on application of the test for joinder and provides that those wishing to join proceedings will need to show more than just an interest in the proceedings. The fact that the interests the SEC represented were, in substance, the same as those represented by the Receiver appears to have been decisive in the present case.

The *Gresh* decision which opened the way to HMRC joining *Hastings-Bass* applications in Guernsey originally caused significant concern, however experience since suggests such interventions will be rare. Where they occur, the above decision may give those opposing such intervention some useful ammunition to resist joinder.

Finally, the decision reinforces the need for parties who wish to be heard in civil proceedings in Guernsey to ensure they can establish a direct or substantive interest. Where a freezing order has been obtained elsewhere, this would most readily be done by obtaining a "mirror" order in in this jurisdiction.

TAMBROOK JERSEY: There but for the grace...

When a decision by Mann J threw into doubt the English Court's jurisdiction to make an administration order in respect of a Jersey company, Felicity Toube QC led Stephen Robins on an urgent and successful appeal. **Glen Davis QC** reflects on the English Court of Appeal's decision in ***Re Tambrook Jersey Limited*** [2013] EWCA Civ 576

The Bailiwick of Jersey – a British Crown Dependency consisting of the island of Jersey, together with two groups of smaller islands – nestles off the coast of Normandy in the English Channel. Jersey is a picturesque island with a benign climate, an even more benign tax regime, and an airport which (in my experience) tends to be prone to fog. Interest in the tax advantages outweighing potential travel inconvenience, Jersey is frequently the domicile of choice for single purpose vehicles for property developments and other investments in the UK.

Jersey is constitutionally separate from the UK, with its own legal system, ruled today, as it has been ruled for a thousand years, by the Duke of Normandy (nowadays, the English Queen wearing one of her other crowns). As Lord Maugham explained in the Privy Council in 1936[1]:

"…the Island of Jersey is not a colony, or, to use the old phrase, 'a plantation.' It is part or parcel of the ancient Duchy of Normandy, which came into the possession of William, Duke of Normandy, in A.D. 933, and remained attached to the English Crown when Philip II of France conquered the rest of Normandy from King John. It has its own constitution, and is governed by its own laws."

It is well-known that Jersey has relatively undeveloped insolvency laws. A form of compulsory liquidation (and a personal insolvency equivalent) is available under the graphically-named Bankruptcy (Désastre) (Jersey) Law 1990, and a procedure broadly similar to an English creditors' voluntary liquidation may be commenced by resolution of the shareholders under the Companies (Jersey) Law 1991. When a company is en désastre, its assets are in effect sequestered and vest in the Viscount, an official of the court, to be sold subject to any security interests.

There is no direct equivalent in Jersey to administration under the English Insolvency Act 1986 or the US Chapter 11 regime; Jersey has yet to embrace the "rescue culture" in that sense. There is a process which the Jersey Court has said is in some senses similar[2], under the *Loi (1839) sur les Remises de Biens*,which establishes a process by which a debtor can surrender his assets into the control of the court whereby he hopes to achieve a more orderly administration of his estate for the benefit of ordinary creditors, and possibly for his own benefit as well.

For some years, over a number of cases, a well-trodden path to address this lacuna has become established where the significant assets are in the UK. The creditor asks the Jersey Court to seek the assistance of the English Court under section 426 of the Insolvency Act 1986 ("the 1986 Act") and the making of an English administration order. For a fateful fortnight in April of this year, it seemed an inconvenient decision of Mr Justice Mann[3] in the Companies Court in London might throw a spanner in the works, but fortunately our Court of Appeal moved swiftly to confirm the correct analysis, and normal service has been resumed. As a by-product, we have a further useful appellate authority on the proper construction of, and approach to, section 426 of the 1986 Act.

Section 426 is a very helpful statutory provision, where it applies, but in some respects it is a discriminatory and therefore rather odd one to find in a modern insolvency statute. It has its roots in section 122 of the Bankruptcy Act 1914[4], which required and therefore

1/. Renouf v Attorney-General for Jersey [1936] AC 445 at 460.

2/. [2011] JRC 232A at [15].

3/. Re Tambrook Jersey Ltd [2013] EWHC 866 (Ch), [2013] 2 WLR 1249.

4/. in England, "bankruptcy" refers only to personal as opposed to corporate insolvency.

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enabled, "*The High Court, the county courts, the courts having jurisdiction in bankruptcy in Scotland and Ireland, and every British court elsewhere…*" to "*severally act in aid of and be auxiliary to each other in all matters of bankruptcy…*".

This was an imperial measure, passed on the eve of the First World War and at the zenith of Britain's powers, just as the imperial sun was beginning to set. The expression "British court" was as much a political as a legal term: as Lord Denning MR put it in 1976: "*…the word "British" in that Act was there used in the same sense as it was often used at that time in the phrase "British Empire," see Roberts-Wray, op. cit., pp. 19-22. It meant any part of Her Majesty's dominions outside Great Britain and Ireland. It included colonies and protectorates.*"[5]

In 1980, in the first case of a request from Jersey under section 122 of the 1914 Act to come to the English Court[6], Goulding J rejected an argument that the Royal Court of Jersey was not a "British court" for these purposes.

The position nowadays is beyond doubt. Section 426(4) of the 1986 Act provides:

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 other part of the United Kingdom or any relevant country or territory.

And Jersey, being one of the Channel Islands, is in a privileged position as one of the relevant countries or territories: section 426(11) provides:

In this section "relevant country or territory" means—

(a) any of the Channel Islands or the Isle of Man, or

(b) any country or territory designated for the purposes of this section by the Secretary of State by order made by

'British court' was as much a political as a legal term.

5/. In re James (an Insolvent) (Attorney-General intervening) [1977] Ch 41; however, the majority of the Court of Appeal in that case disagreed with Lord Denning that the courts of Rhodesia, which had unilaterally declared independence, continued nonetheless to qualify as "British" courts for this purpose.

6/. In re a Debtor (Order in Aid No 1 of 1979), ex parte Vicount of the Royal Court of Jersey [1981] Ch 384.

The Jersey court confirms for itself that that the company is insolvent and could apply to have its property declared en désastre.

statutory instrument[7].

From the point of view of the Jersey Court, there is no statutory jurisdiction to make a request to the English court, but the Jersey Court does so in its inherent jurisdiction. This was asserted in the *OT Computers* case[8], and considered in more detail in 2011 in the *REO (Powerstation)* case, in which the Deputy Bailiff said[9]:

As to the inherent jurisdiction of the Court it is perhaps apt to refer to two decisions of the Court of Appeal. The first is the Finance and Economics Committee-v-Bastion Offshore Trust Company Limited [1994] JLR 370, at page 382 where Sir Patrick Neill J A said this:-

"Practitioners in these courts and in the courts of Guernsey are familiar with the maxim "la cour et toute puissante" and "the court is master of its own procedure."

The better known a proposition is, the harder it is to find authority for it and so it turns out if one seeks judicial statements of these two maxims (though in Guernsey the Court of Appeal relied on the second maxim in Cherub Invs. Limited-v-Channel Islands Aeroclub (Guernsey) Limited).

Both maxims are expressions of the inherent jurisdiction of the court.

The Deputy Bailiff then went on to say:

16. All these considerations, however, go to support these two propositions:-

(i) The Court does lend its assistance in an appropriate case to a process by which formal proceedings against a debtor can be suspended in order to achieve an orderly realisation of the debtor's assets;

(ii) In insolvency matters generally, the Court has in the past exercised an inherent jurisdiction in a number of different respects.

17. We have gone into some detail in relation to the matter because although in the First Orion Amber case this was described as a well trodden path, it appears to us that this was perhaps something of an overstatement and that in the event that objection might be taken in the High Court to the application for an administration order, it was right that we should deal in some detail with the question of our own jurisdiction to make a request. Furthermore, the fact that the companies have not appeared to object to the exercise of any jurisdiction, notwithstanding that they were put on notice, also suggests that perhaps there is no dispute that the jurisdiction exists.

The procedure which has now been established over a series of cases is that an application is made either by the Jersey company itself[10] or by substantial creditors[11] on notice to the company. The application is accompanied by an affidavit setting out the evidential background, and supported by an Opinion of English leading counsel confirming that the English court is likely to accede to the request.

The Jersey court confirms for itself that the company is insolvent and could apply to have its property declared *en désastre* pursuant to the Bankruptcy (Désastre) (Jersey) Law, 1990 or for a winding up pursuant to the Companies (Jersey) Law, 1991, and then considers whether, against that background, it is in the interests of the creditors to issue a Letter of Request to the English Court, notwithstanding the absence of any insolvency proceedings in Jersey. If it does, it issues the Letter, which is then brought before the English Court[12].

In the *REO (Powerstation)* case, the Deputy Bailiff said[13]:

It seems to us that the Court should be prepared to contemplate issuing a letter of request if it is in the interests of the creditors, or if it is in the interests of the debtor or if it is in the public interest. In relation to the latter of these three considerations, the public interest obviously includes, indeed we think as a matter of priority, a satisfactory methodology for dealing with the interests of the creditors and the debtor. Subordinate to these considerations in relation to the public interest is also the interests of the Island in terms of its reputation outside these shores. Public

The point Mann J considered insuperable was jurisdiction.

7/. The original list of relevant countries or territories was set out in 1986 in the Co-operation of Insolvency Courts (Designation of Relevant Countries and Territories) Order 1986 (SI 1986/2123). These were: Anguilla, Australia, the Bahamas, Bermuda,Botswana, Canada, Cayman Islands, Falkland Islands, Gibraltar, Hong Kong, the Republic of Ireland, Montserrat, New Zealand, St Helena, Turks and Caicos Islands, Tuvalu and the Virgin Islands. Malaysia and South Africa were added in 1996 (SI 1996/253) and the list was extended to Brunei in 1998 (SI 1998/2766).

8/. In re OT Computers [2002] UR 29 at [4].

9/. [2011] UR 232A, at [12].

10/. as in the OT Computers case.

11/. examples are Re First Orion Amber Limited and First Orion Amber Nominees Limited [2009] UR 126 and Re REO (Powerstation) Ltd [2011] UR 232 A.

12/. on an urgent application, this can be done almost immediately.

13/. at [18].

policy considerations do not overtake the requirement to do justice as between those who are directly affected, and in our view is therefore subordinate to those interests when it comes to exercising a discretion in a matter of this kind, but we can have regard, at the edges of our discretion, to the fact that a major insolvency of a Jersey company, causing extensive damage to creditors and debtor alike is not in the best interests of the Island, and this can operate as an additional reason to exercise the discretion to issue a letter of request.

Examples of cases in which this procedure has been followed[14] include: OT Computers Limited in 2002, where the company manufactured computer hardware ("Tiny" brand computers) and sold them through some 160 High Street stores, and was expected to lose its banking facilities within a couple of days – a purchaser of material parts of the business had been identified, but was said only to be prepared to complete a sale from an independent insolvency practitioner; the *First Orion* cases in 2009, where the principal asset of the insolvent companies was a substantial charged leasehold property in London; the *St John Street Limited* case in 2010, involving a property development again in London where the company had defaulted on a £30.5 million loan and the secured creditor had appointed receivers, but it was nonetheless considered desirable to appoint administrators under the 1986 Act with their wider powers; the *REO (Powerstation) Limited* case in 2011, in which the main assets were again said to be real estate in London.

So when the application by HSBC for administrators to be appointed in the *Tambrook Jersey* case was brought by junior counsel before the Companies Court in London on 12 April 2013 on a Letter of Request granted by the Royal Court of Jersey on 28 February, there was every expectation that the application would be granted, and it was something of a shock when it was not[15].

GLEN DAVIS QC

Mann J was satisfied that, apart from one point, the case before him would be an appropriate one for the appointment of administrators. The point he considered insuperable was jurisdiction. He was aware that similar orders had been made in some five previous cases[16], but was concerned that:

In none of the English cases is a reasoned decision recorded. The only thing that is known about the hearing at which the order was made is its date and (in most but not all cases) the judge making it.

The mistaken view the Judge took of the English court's jurisdiction under section 426 was that he thought the English could only assist if there were

14/. The present author was involved as English counsel in a number of them.

15/. Mann J's decision is [2013] EWHC 866 (Ch) available on BAILII and reported at [2013] 2 WLR 1249.

16/. the Judge refers to an online article by Paul Omar, Section 426 of the Insolvency Act 1986 : Extending Rescue to Foreign Debtors on a 'Passporting Basis' (http://www.iiiglobal.org/component/jdownloads/viewcategory/647.html) in which the cases were "gathered and considered".

some insolvency proceedings on foot in the foreign court. As he put it[17]:

The problem in the present case lies in the fact that it is not possible to see how the Royal Court is "assisted" for these purposes. The English court is not empowered to act merely because a foreign court invites it to do so. The foreign court has to be an insolvency court (which I accept the Jersey court is) and the English court has to be invited to "assist" that court. In my view that requires that the foreign court be assisted in its functions as an insolvency court. That in turn presupposes that the foreign court is doing something, or perhaps planning to do something, which the English court can, and is invited to, assist. That is what the plain words seem to me to mean.

Even the best Judges sometimes make mistakes. The Applications List in the Companies Court at the Rolls Building in London, which is where the application came to be heard, is a busy one, and in the course of a sitting day the Judge hearing that list deals with a range of different applications of varying complexity. It is interesting to note that in the same list there was apparently an application for recognition under the Cross-Border Insolvency Regulations 2006, which implement in England the *UNCITRAL Model Law on Cross-Border Insolvency*, and it is an important distinguishing feature that for such an application to be brought, there must be insolvency proceedings on foot in the foreign jurisdiction. Perhaps it was this which led Mann J astray.

The vagaries of litigation can sometimes mean that an inconvenient decision on a point of principle nonetheless stands uncorrected, but fortunately in this case an appeal was urgently brought before the Court of Appeal, which heard it on 1 May 2013 and gave considered reasons on 22 May[18]. Davis LJ, with whom Longmore and McFarlane LJJ agreed, makes clear that the English court can assist a foreign court under section 426 of the 1986 Act, whether or not there are insolvency proceedings on foot in the foreign jurisdiction.

Davis LJ was in no doubt that Mann J had erred in his construction of section 426(4).

Davis LJ traces section 426 back to its origins in section 122 of the 1914 Act, and the view expressed in the Cork Report, the precursor to the 1986 Act, that it should be the paramount objective of each of the insolvency systems of the United Kingdom, the Channel Islands and the Isle of Man that "so far as practicable, there should be only one insolvency administration of any insolvent person subject to the jurisdiction of any of them". He says that the provisions of s.426 as enacted are designed to accord with what Lord Hoffmann had described in the course of his judgment in *HIH Casualty and General Insurance Limited*[19] as the "principle of modified universalism".

Davis LJ also considers two well-known background cases which were cited to the Court of Appeal. The first was *re Dallhold Estates*[20], in which Chadwick J granted an English administration order to preserve the value of a lease in England on a Letter of Request from the Australian court. Davis LJ observes that *Dallhold* shows the English court applying a purposive approach to the interpretation of sections 426(4) and (5), and also highlights that administration was being sought in *Dallhold* as an alternative to an Australian winding-up order; under the terms of the lease, there could have been a forfeiture on a winding-up, in which event the value would have been lost. He notes that *Dallhold* had been approved by the Court of Appeal in *Hughes v Hannover*[21], and that in *Rubin v Eurofinance*[22], Lord Collins had referred to *Hughes v Hannover* among other authorities indicating that section 426 "has been given a broad interpretation.

The second case considered by Davis LJ was *Television Trade Rentals*[23], an unreported decision of Lawrence Collins J in which there had been no insolvency proceedings on foot in the Isle of Man but the Manx Court had recognised an appointment of English provisional liquidators and then issued a Letter of Request asking the English Court to apply the provisions of Part 1 of the 1986 Act (relating to company voluntary arrangements), which the English Court had done although, as Davis LJ noted, if the reasoning and approach of Mann J in *Tambrook* had been correct, *Television Trade Rentals* would also seem to be a case where the court had no jurisdiction.

Davis LJ was in no doubt that Mann J had erred in his construction of section 426(4) and in his approach to its application. Although the Judge's reasoning "could not have been more clearly and lucidly put"[24], his interpretation and approach were "unduly and unnecessarily restrictive"[25]. Davis LJ gives four reasons for his conclusions.

17/. at [10].

18/. [2013] EWCA Civ 576.

19/. [2008] UKHL 21, [2008] 1 WLR 852.

20/. re Dallhold Estates (UK) Pty Limited [1992] BCLC 621.

21/. Hughes v Hannover Rückversicherungs Aktiengesellschaft [1997] 1 BCLC 497.

22/. **Rubin** v Eurofinance SA [2012] UKSC 46, [2013] 1 AC 236.

23/. Re Television Trade Rentals Ltd [2002] EWHC 211 (Ch).

24/. at [21].

25/. at [35].

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First, section 426(4) is not applicable to courts *exercising* jurisdiction in relation to insolvency law: it is by its wording applicable to courts *having* jurisdiction, or the corresponding jurisdiction, in insolvency law[26]. "Having" is not the same as "exercising": there is no need for insolvency proceedings to be on foot in the requesting jurisdiction.

Second, sections 426(4) and (5) are to be given a broad interpretation: there is neither linguistic necessity nor purposive compulsion to adopt a narrow and restrictive approach[27]. This is in line with previous authority, and will be helpful in any future cases where the scope of section 426 is in issue.

Third, freedom to request or make orders under section 426 where insolvency proceedings are not on foot in the requesting jurisdiction is in accordance with "modified universalism" (and the desirability of there being only one insolvency administration where that is practicable)[28].

Fourth, Davis LJ did not accept the Judge's propositions that the English court was not being asked to assist the Jersey court "in any endeavour", or that the Jersey court was not "exercising the corresponding jurisdiction in relation to insolvency law[29]. He considered that the Jersey court *was* engaged in an endeavour:

The endeavour was to further the interests of this insolvent company and its creditors and to facilitate the most efficient collection and administration of the Company's assets. In that regard, the Company had itself resolved that it should seek to be placed in administration in England: and the Royal Court had (before making its order that a Letter of Request be issued) itself duly considered the interests of the creditors. Indeed, the whole insolvency flavour of what was being done here is yet further illustrated by the request contained in the Letter of Request to give priority to Jersey creditors in accordance with Jersey insolvency law. All of this is the very stuff of insolvency; and there is no good reason, in my opinion, to refuse to acknowledge it as an exercise of insolvency jurisdiction simply because formal proceedings for an (unwanted) désastre order had not been issued or contemplated.

In short, it was clear to Davis LJ reviewing the Jersey authorities cited to him that making a request in such a context is considered to be part of, and the exercise of, Jersey insolvency law, and it had been appropriate for the Jersey court to have made the statement in the first paragraph of its Letter of Request that "This court is a court exercising jurisdiction relating to insolvency law in Jersey".

As the Judge himself had accepted

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that it would have been appropriate to accede to the request if there was jurisdiction to do so, and as the Court of Appeal was satisfied that the English Court had jurisdiction, the Court of Appeal therefore made the administration order when the appeal was allowed (and confirmed that the previous five orders were orders which the court had had jurisdiction to make)[30].

So inconvenience has been avoided, normal service can be resumed, and for all those jurisdictions which enjoy a gateway to the English Court under section 426, there is further Court of Appeal authority as to the liberal breadth of the provisions.

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26/. at [37].

27/. at [38].

28/. at [39], and Davis LJ also prayed in aid in this context the well-known comments of Lord Hoffmann in Cambridge Gas Transportation v Official Committee of Unsecured Creditors [2006] UKPC 508, [2007] 1 AC 508 at paragraph 22 by reference to s 426(5): But the domestic court must at least be able to provide assistance by doing whatever it could have done in the case of a domestic insolvency. The purpose of recognition is to enable the foreign office holder or the creditors to avoid having to start parallel insolvency proceedings and to give them the remedies to which they would have been entitled if the equivalent proceedings had taken place in the domestic forum.

29/. at [41].

30/. at [46].

Insolvency and ancillary relief in family proceedings

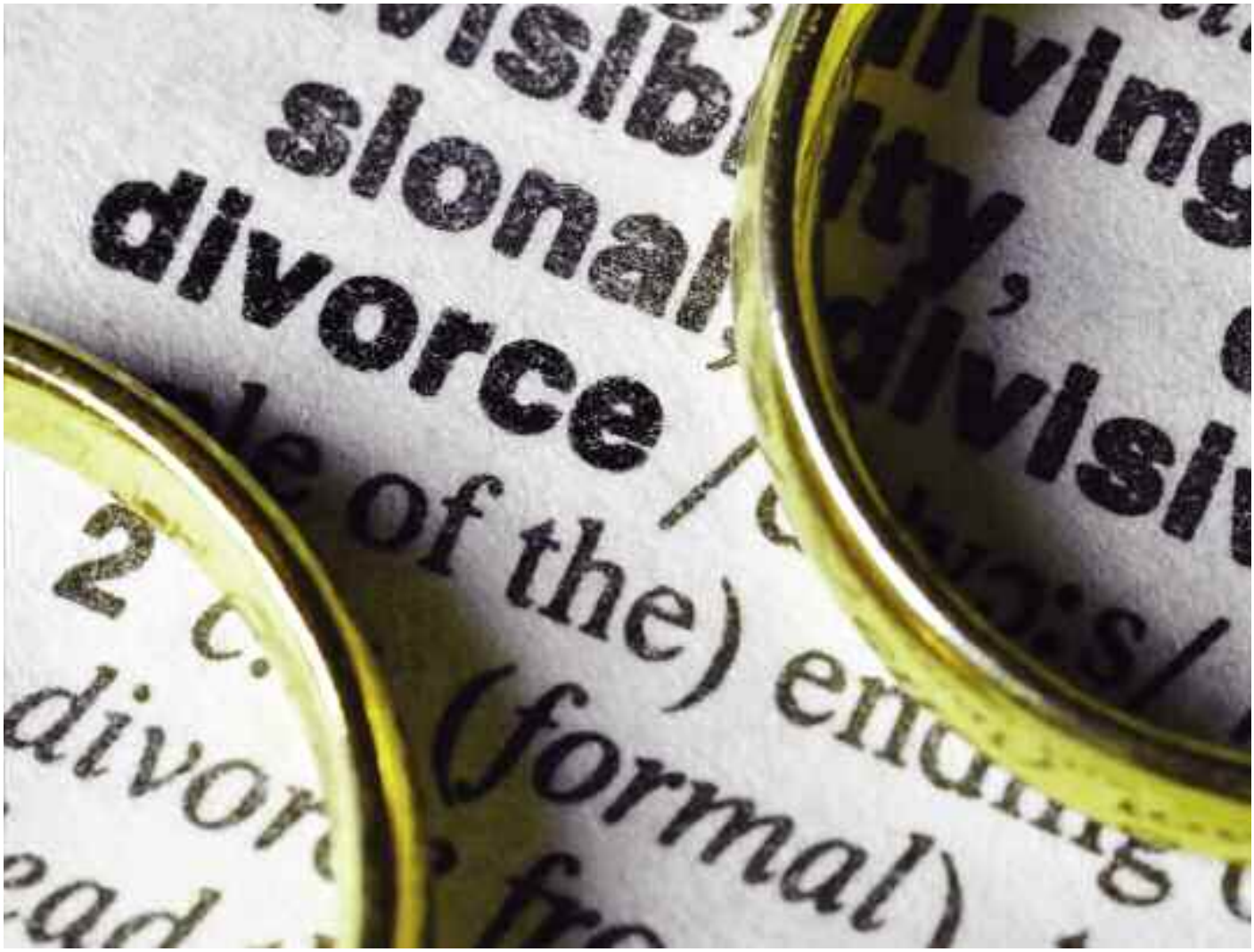
Christopher Brougham QC discusses the effect of the Insolvency Act and Rules 1986 in relation to ancillary relief in family proceedings and comments on *Arif v Anwar* and *Prest v Petrodel Resources Ltd*.

Introduction

The Insolvency Act and Rules came into force at the end of 1986. They raised at least three questions of importance in relation to orders made in family proceedings, none of which was resolved until well into this century, and one only very recently. In their order of resolution they were (a) the reason why an obligation to pay a lump sum or costs arising under an order made in family proceedings, which had been provable under the Bankruptcy Act 1914 (*Curtis v Curtis* [1969] 1 WLR 422, CA), was made not provable by IR, r.12.3(2)(a); (b) the relationship between the transactions at an undervalue provisions of IA 1986, s.339, and property adjustment orders made under the Matrimonial Causes Act 1973; and (c) the circumstances in which the bankruptcy court would direct, under IA 1986, s.281(5), that on his discharge a bankrupt be released from a bankruptcy debt arising under an order made in family proceedings. This article discusses the resolution of those questions and then refers to the novel ancillary relief case of *Arif v Anwar* [2013] EWHC 624 (Fam); [2013] B.P.I.R. 389 and to *Prest v Petrodel Resources Ltd* [2013] UKSC 34; [2013] 3 WLR 1.

Why was an obligation to pay a lump sum or costs made no longer provable?

Under the Bankruptcy Act 1914 and previous bankruptcy legislation, claims for arrears of, or future, periodical payments were not provable in bankruptcy (*Linton v Linton* (1885) 15 QBD, 239, CA; *Kerr v Kerr* [1897] 2 QB 439, DC; *James v James* [1964] P 303, DC). The justification for this was that the family court had the power to remit arrears or vary future payments, so that the debt was not capable of being fairly estimated; the debt being not provable, the bankrupt was not released from it on his discharge. (Consequently it is probable that such debts are, aside from IR, r.12.3(2)(a), not provable under IR, r.12.3(3) as being not provable under 'a rule of law'). On the other hand, claims for unpaid lump sums and costs, not being capable of remission or variation, were provable debts (*Curtis v Curtis*, above) and on his discharge the bankrupt was released from them. IR, r.12.3(2)(a) in its original form made 'any obligation arising under an order made in family proceedings' not provable, but on his discharge the bankrupt was not released from such an obligation 'except to such extent and on such conditions as the court may direct' (IA 1986, s.281(5)). In *Woodley v Woodley (No.2)* [1994] 1 WLR 1167, CA, the appellant submitted that the rule, in so far as it applied to lump sums, was *ultra vires.* In rejecting this submission, Balcombe LJ confessed that he did not know whether it was the intention of those who drafted the Insolvency Rules to bring about the change and invited the Insolvency Rules Committee 'to consider whether a lump sum order made in family proceedings should be provable in bankruptcy as it was before the Rules of 1986 came into force'. Despite a further such invitation from Sir Donald Nicholls VC in *Re Mordant* [1996] BPIR 302, nothing happened for a number of years. This notwithstanding that nobody, not even members of the Rules Committee at the relevant time, could explain the change. It seems that it was, as was suggested by Balcombe LJ, 'unintentional'. However, the error was not rectified until the Insolvency (Amendment) Rules 2005 came into force, amending the above words quoted from IR, r.12.3(2)(a), so as to insert '(other than an obligation to pay a lump sum or to pay costs)' after 'obligation', the amendment having



THE INSOLVENCY ACT ADDS YET A FURTHER DIMENSION TO THE KNOTTY PROBLEM OF DIVORCE

been drafted by the author of this article. The amendment, however, applies only in relation to bankruptcies commencing on or after April 1, 2005.

Transactions at an undervalue and property adjustment orders

Under the Matrimonial Causes Act 1973, s.24, the family court can order one party to a marriage to transfer to the other party such property as may be specified in the order. An important question arising from the undervalue provisions of the IA 1986 was whether, once such a property had been transferred, any consideration had been given by the transferee for the property. For if not, the transfer would inevitably be a transaction at an undervalue within IA 1986, s.339(3). In *Jackson v Bell* [2001] EWCA Civ 387; [2001] B.P.I.R. 612 (an application for permission to appeal) the Court of Appeal put the question the other way round and stated that a point of principle, fit to be considered by it, was whether a 'property adjustment order normally granted by the Family Division [can] be a transaction at an undervalue, even though certain aspects of it may appear to be somewhat gratuitous … [The] dividing line between the Family Division, on the [one] hand, and the insolvency regime on the other, should be considered in this respect'. *Jackson v Bell* settled and the appeal was not heard.

Once a property had been transferred, had any consideration been given by the transferee?

Then in *Hill v Haines* [2007] EWCA Civ 1284; [2008] Ch 412, the judge at first instance concluded that 'for the purposes of considering the applicability of section 339 to a case such as this, the position is the same whether the matrimonial court makes an order following a contested hearing or following a compromise agreement – in neither case does the receiving party give, nor the paying party receive, consideration'. The author of this article criticised this decision in the next release of *Muir Hunter on Personal*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Insolvency on the basis that, if correct, it would mean that, in all but the most exceptional cases, a spouse or civil partner would lose the benefit of any property adjustment order that took effect within two years before the presentation of a petition leading to the bankruptcy of the other spouse or civil partner; that period would increase to five years, unless the benefiting spouse or civil partner could prove that the (prospective) bankrupt was solvent immediately after the order took effect. The Court of Appeal, however, subsequently allowed the wife's appeal:

> '[I]t is … self-evident that the ability of one spouse to apply to the court for one or more of the orders referred to in [MCA 1973] ss. 23 to 24D is a right conferred and recognised by the law. Further it has value in that its exercise may, and commonly does, lead to court orders entitling one spouse to property or money from or at the expense of the other. That money or property is, prima facie, the measure of the value of the right.' (at [29])
>
> 'If one considers the economic realities, the order of the court quantifies the value of the applicant spouse's statutory right by reference to the value of the money or property thereby ordered to be paid or transferred by the respondent spouse to the applicant. In the case of such an order, whether following contested proceedings or by way of compromise, in the absence of the usual vitiating factors of fraud, mistake or misrepresentation the one balances the other. But if any such factor is established by a trustee in bankruptcy on an application under s.339 then it will be apparent that the prima facie balance was not the true one and the transaction may be liable to be set aside.' (at [35])
>
> 'Finally, as to policy, it would be unfortunate in the extreme if a court approved, or even (an a fortiori case) a court determined property adjustment order would be liable, in practice, to be undone for up to five years because the husband goes bankrupt within that period. That could even encourage such bankruptcy on the part of a disaffected husband. Although a collusive agreement by a divorcing husband and wife to prefer the wife and children over creditors and thus dishonestly to transfer to her more than his estate can truly bear, if his debts were properly taken into account, and thus more than her ancillary relief claim could really and knowingly be worth, is no doubt susceptible to section 339 relief despite the existence of a court order in her favour … : nevertheless, in the ordinary case, where there is no dishonest collusion, and where a court approves or determines the sum or property to be transferred, it would be entirely foreign to the concept of a "clean break" if the husband's creditors could thereafter seek to recover, in bankruptcy, the property transferred or its value. However, … it would require the overthrow of long-established

"…the ability of one spouse to apply to the court for one or more of the orders referred to…has value."

jurisprudence, the re-interpretation of section 39 [MCA 1973], the misunderstanding of the doctrine of consideration, and an assault on current views of the statutory entitlement to ancillary relief, to arrive at that unhappy and unnecessary situation.' (at [82])

In what circumstances will the court direct that a bankrupt be released from a bankruptcy debt arising under an order made in family proceedings?

Under IA 1986, s.281(5), upon his discharge a bankrupt is not released from any bankruptcy debt which arises under an order made in family proceedings 'except to such extent and on such conditions as the court may direct'. Surprisingly, it is only very recently that there has been any authoritative guidance as to the circumstances in which the court might so direct.

In *Hayes v Hayes* [2012] EWHC 1240 (Ch); [2012] B.P.I.R. 739, the deputy Chancery judge dismissed an appeal from the bankruptcy registrar's order dismissing an application by a discharged bankrupt for an order under IA 1986, s.281(5)(b), releasing him from an obligation arising under an order for costs made in family proceedings. The registrar had correctly observed that the case law and academic commentary gave no specific guidance as to how the discretion whether or not to make such an order was to be exercised. The judge held that there was no time limit post-discharge for the making of such an application but the length of any delay was a consideration to be taken into account by the court in exercising its discretion whether or not to make the order sought. The judge went on to consider what other factors were relevant to the exercise of the court's discretion:

> 'One factor … is obvious from the statutory provisions … The default position established by the statutory material is that family orders as defined within [IA 1986, s.281] are required to survive the discharge of a bankrupt and are to remain enforceable. The policy behind this approach … probably stems from the desirability of ensuring that family liabilities are not avoided by a bankruptcy procedure that is now much foreshortened by reforms contained in the Enterprise Act 2002 that were enacted to assist those with entrepreneurial interests to return to business following a bankruptcy'. (at [15])
>
> '[T]here are a number of factors that have to be borne in mind aside from the factors to which I have already referred. First and foremost, if an order is made discharging this debt, then the consequence will be that the debt will become unenforceable. It follows that if, contrary to the appellant's current expectations, he is able to resume significant income earning, or if for some other reason he receives substantial funds, none of those funds will be payable to the respondent in discharge of this long outstanding debt. That is a factor which is of importance because it is likely to mean that discharge of the debt will be a disproportionate step to take unless the court can be confident that the applicant for relief under [IA 1986, s 281(5)(b)] will never be in receipt of income or capital which will enable the debt to be discharged. This is always likely to be a significant factor in the exercise of discretion and in combination with the default position established by the statutory material is likely to be one which is going to provide an answer in many if not most cases'. (at [21])

"The default position established by the statutory material is that family orders…are required to survive the discharge."

A further factor identified by the judge was the risk of the respondent to the application using the fact of the obligation (if not released) to harass the applicant, for example by bringing new and abusive bankruptcy proceedings calculated to restrict the applicant in building a new life.

In *McRoberts v McRoberts* [2012] EWHC 2966 (Ch); [2013] 1 WLR 1601, Hildyard J, in dismissing an application for an order under the same subsection, agreed that all the factors outlined in *Hayes*, above, should be taken into account:

> '[T]he ultimate balance to be struck is between (a) the prejudice to the respondent/obligee in releasing the obligation if otherwise there would or might be some prospect of any part of the obligation being met and (b) the potential prejudice to the applicant's realistic chance of building a viable financial future for himself and those dependent upon him if the obligation remains in place.
>
> In striking that balance I consider that the burden is on the applicant; unless satisfied that the balance of prejudice favours its release the obligation should remain in place: that follows from the fact that continuance is the default option, and from the rationale of excluding such obligations from automatic discharge …
>
> [T]he purposes for which the discretion is conferred do not include review of the merits or overall fairness of the underlying obligation …
>
> Further … in the case of an obligation imposed in matrimonial proceedings, that is so, even if circumstances have changed such as might suggest that the obligation might fairly be reviewed or modified … [A]ny such review or modification … should be reserved to the matrimonial courts in the exercise of its [*sic*] jurisdiction to do so (if any) conferred by the Matrimonial Causes Acts'. (at [24]-[27])

Arif v Anwar

Since *F v F* [1994] 1 FLR 359, in which Thorpe J, sitting in the Family Division,

A striking variation on this theme is Arif v Anwar, and the subsequent history of that case.

annulled a husband's bankruptcy (based on his own petition), there have been further reported cases of annulments ordered by the Family Division where the court has been satisfied that the bankrupt was not in truth insolvent (e.g., *Couveras v Wolf* [2002] 2 FLR 107; *Paulin v Paulin* [2009] EWCA Civ 221; [2010] 1 WLR 1057). It has not always been clear whether jurisdictional technicalities had been complied with. However, in *Forder v Forder* [2002] EWCA Civ 1527, where a wife had applied in the Family Division to annul the husband's bankruptcy and the family judge had adjourned the application and stayed the bankruptcy until the conclusion of the wife's ancillary relief application, the Court of Appeal described the judge's order as 'essentially a case management decision' and 'a sensible and pragmatic solution to the problem which confronted him'.

A striking variation on this theme is *Arif v Zar* [2012] EWCA Civ 986; [2012] B.P.I.R. 948, and the subsequent history of that case. In *Arif v Zar* the Court of Appeal allowed an appeal by a husband against an order of the family court transferring the wife's application for the annulment of the husband's bankruptcy from the Chancery Division to the Family Division, after a bankruptcy registrar had refused to order such a transfer. The Court held that the family court had had no jurisdiction to interfere with the registrar's refusal: the wife should have appealed to a judge of the Chancery Division under IA 1986, s.375(2). The wife subsequently discontinued her annulment application but continued with her application for financial relief in the family court. The assets of the husband were, of course, vested in his trustees in bankruptcy. The husband asserted that the former family home was owned by himself and his son by a previous marriage in equal shares and that the son was a substantial creditor in his bankruptcy, with the consequence that there was no prospect of a surplus being available from which to provide the wife with financial relief. The wife disputed these assertions and also the validity of a substantial claim by another, unrelated, creditor, and on the wife's application, Eleanor King J (a judge of the Family Division) ordered that there be an *OS v DS* ([2004] EWHC 2376 (Fam); [2005] 1 FLR 675) hearing, an exploratory preliminary hearing, before a judge of the Chancery Division sitting in the

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Family Division to investigate these issues (*Arif v Anwar* [2012] EWHC 3435 (Fam)). The *OS v DS* hearing duly took place before Norris J (a judge of the Chancery Division) and after extensive cross-examination by the wife's counsel of the husband, the son and the unrelated creditor on their evidence adduced for the purposes of the hearing, the judge ordered that there be a trial of the two issues of the ownership of the family home and the indebtedness of the husband to the son, with the son as claimant and the husband, wife and trustees as respondents (*Arif v Anwar* [2013] EWHC 624 (Fam); [2013] B.P.I.R. 389). As regards the unrelated creditor, the judge concluded that although his debt appeared to require further investigation, any such investigation should be carried out in the bankruptcy, and not the family, proceedings. Notwithstanding opposition on behalf of the husband and son, Norris J permitted the trustees' legal representatives to be present throughout the hearing. In effect, the trustees had the benefit of a private examination, under IA 1986, s.366, of the bankrupt, his son and the unrelated creditor, paid for by the wife.

Prest v Petrodel Resources Ltd

Prest v Petrodel Resources Ltd is probably principally important as a helpful in-depth analysis of the long-standing concept of 'piercing the corporate veil'. It also has specific importance as regards ancillary relief proceedings and the family court's then notion of what constituted a party's property for the purposes of such proceedings. It was this notion that was largely responsible for the case's unfortunate history and its unusual resolution in the Supreme Court. As mentioned above, under MCA 1973, s.24(1)(a), the court may order one party to the marriage to transfer to the other 'property to which the first-mentioned party is entitled, either in possession or reversion'. Under s.25(2)(a), in considering what, if any, ancillary relief to grant, the court has to have regard to the 'income, earning capacity, property and other financial resources which each of the parties to the marriage has or is likely to have in the foreseeable future'. It was the practice ('the Practice') of the family court to conflate these two provisions, so that where property was owned by a company that one of the party's controlled to the extent that he or she could procure the property's transfer, that property was treated as a financial resource of the party and therefore 'property' for the purposes of s.24(1)(a). Mr Prest controlled companies which were the legal owners of a number of properties which Mrs Prest wished to have transferred to her under s.24(1)(a). Mr Prest had been uncooperative throughout the proceedings, failing to provide full and frank disclosure of his financial position, and the companies (joined as parties) had failed to file a defence or comply with orders for disclosure. Mrs Prest put her case in three separate ways: (a) that the court should 'pierce the corporate veil' and treat the properties as properties of Mr Prest; (b) the court should apply the Practice with the same consequence; (c) that the properties were beneficially owned by Mr Prest, and so were in truth his property. The judge at first instance declined to pierce the corporate veil, because there had been no relevant impropriety on the part of Mr Prest. He did, however, apply the Practice and ordered the transfer of the properties to Mrs Prest. He declined to grant a declaration that Mr Prest was the beneficial owner of the properties, as he thought that if he were to do so there would be 'potential tax consequences'. The Court of Appeal allowed Mr Prest's appeal (Thorpe LJ, who supported the Practice, dissenting) on the basis that the Practice was wrong. Patten LJ referred to the Family Division as having developed 'an approach to company-owned assets in ancillary relief applications which amounts almost to a separate system of legal rules unaffected by the relevant principles of English property and company law'. Unfortunately for Mrs Prest, the Court took the view that the judge below had rejected her claim that Mr Prest was the beneficial owner of the properties.

The judge at first instance declined to pierce the corporate veil, but applied the Practice.

Mrs Prest appealed to the Supreme Court, which confirmed that the Practice was wrong. As Lord Sumption JSC put it, s.24(1)(a) 'is invoking concepts with an established legal meaning and recognized legal incidents under the general law. Courts exercising family jurisdiction do not occupy a desert island in which general legal concepts are suspended or mean something different. If a right of property exists, it exists in every division of the High Court and in every jurisdiction of the county courts. If it does not exist, it does not exist anywhere'. He also pointed out that the recognition of the Practice 'would cut across the statutory schemes of company and insolvency law'. The unusual denouement of the case was that the Court, being satisfied that the judge had not actually rejected the claim that the properties were beneficially owned by Mr Prest, was itself able, on the limited material available to it, to make a finding to that effect. So Mrs Prest's appeal succeeded on the most straightforward of the three bases of her claim. Had the judge not applied the Practice but made an order on the basis that Mr Prest was the beneficial owner of the properties, the case might well have ended there and have never been considered by the Court of Appeal, let alone the Supreme Court.

"If a right of property exists, it exists in every division of the High Court and in every jurisdiction of the county courts."

The meaning of Section 123(2)

David Allison and **Richard Fisher** on the continuing search for the meaning of Section 123(2) of the Insolvency Act 1986 and the Supreme Court decision in Eurosail.

Key Points

- The Supreme Court found that section 123(2) requires the petitioner to satisfy the Court, on a balance of probabilities, that a company has insufficient assets to be able to meet all its liabilities, including prospective and contingent liabilities.
- The Supreme Court expressly rejected any suggestion that section 123(2) requires the company to have reached the point of no return.
- The Supreme Court did not provide any guidance on how contingent and prospective liabilities should be taken into account as a matter of practical reality when conducting the balancing exercise required by section 123(2).
- There must be doubt as to whether the section 123(2) is ever an appropriate trigger in a finance document in view of the fact that it requires a fact sensitive and potential complicated enquiry, taking into account all relevant circumstances.

Introduction

This article considers the recent decision of the Supreme Court in BNY Corporate Trustee Services Ltd v Eurosail-UK 2007-3BL PLC [2013] 1 WLR 1408 on the meaning of section 123(2) of the Insolvency Act 1986 ("the Act") and its possible future implications.

The *Eurosail* case is important as it represents the first time that the UK's highest court has considered the interpretation of section 123(2) since its introduction onto the statute book a quarter of a century ago.

Section 123(2) sets out one of the circumstances in which a company is to be deemed to be unable to pay its debts. It plays a key role as a jurisdictional gateway relevant to a large number of remedies made available under the Act. Moreover, it plays an important role in finance documentation where it is commonly included by the draftsman as an event of default which operates as a gateway to the acceleration of the sums owed by a debtor and the enforcement of the security held by or on behalf of the lenders.

The correct interpretation of the provision arose for determination in the *Eurosail* case by reason of the fact that the Notes provided for an event of default potentially to occur in circumstances where the Issuer was unable to pay its debts within the meaning of section 123(2).

Section 123 of the Act

Section 123 is one of the four main sections in Chapter VI of Part IV of the Act which is concerned with the grounds and effect of winding up petitions.

Chapter VI commences with section 122 which is headed "*Circumstances in which company may be wound up by the Court*". Section 122(1)(a)-(g) identify those circumstances. One of the circumstances in which a company may be wound up is that the company is unable to pay its debts: see section 122(1)(f).

Section 123 (headed "*Definition of inability to pay debts*") then elaborates on the preconditions for the exercise of the statutory power granted to the Court in section 122(1)(f), by providing a definition of inability to pay debts. The key provisions of section 123 are sections 123(1)(e) and 123(2):

(1) A company is deemed unable to pay its debts-

(e) if it is proved to the satisfaction of the court that the company is unable to pay its debts as they fall due.

(2) A company is also deemed unable to pay its debts if it is proved to the satisfaction of the court that the value of the company's assets is less than the amount of its liabilities, taking into account its contingent and prospective liabilities.

Lord Walker's judgment contains a careful treatment of the case law and the legislative history leading to the enactment of section 123 of the Act in its

current form: see [25]-[37]. These matters are beyond the scope of this article, but are the subject of detailed consideration in an article by Dr Peter Walton, "Inability to pay debts: beyond the point of no return" [2013] Journal of Business Law 212.

The test found in section 123(1)(e) is commonly known as the "cashflow test". This provision was the subject of detailed consideration in *Re Cheyne Finance plc (No. 2)* [2008] Bus LR 1562, where Briggs J concluded that the test contains an element of futurity such that it is concerned not only with whether the company is able to pay debts that are immediately payable, but also with those that would be payable in the future.

The test found in section 123(2) is commonly known as the "balance sheet test". There must, however, be a serious question as to whether this remains an appropriate label following the decision of the Supreme Court.

Section 123(2) requires the Court to strike a balance between the value of assets and the amount of liabilities of a company, taking into account not only debts which are immediately due and payable, but also its contingent and prospective liabilities. In *Stonegate Securities v. Gregory* [1980] 1 Ch 576, Buckley LJ described a contingent creditor as a "*creditor in respect of a debt which will only become due in an event which may or may not occur*" and a prospective creditor as a "*creditor in respect of a debt which will certainly become due in the future, either on some date which has been already determined or on some date determinable by reference to future events*".

The relevance of the definition of an inability to pay debts set out in section 123 is not confined to the consideration of whether the jurisdictional pre-condition to the existence of the discretion to make a winding-up order has been satisfied. The provision plays an important role throughout the fabric of the Act. To give two examples:

(1) The provision plays a key role in the administration regime. Save for an application by a holder of a qualifying floating charge, the Court must be satisfied on an application for the appointment of administrators by the Court that the company is or is likely to become unable to pay its debts: see paragraph 11 of Schedule B1 of the Act.

(2) An inability to pay debts within the meaning of section 123 is a necessary pre-condition to a successful claim by an officeholder to avoid an antecedent transaction as a preference under section 239 of the Act or an undervalue under section 238 of the Act: see section 240(2) of the Act.

Factual background to the decision

It is important to set out a brief summary of the factual background to the *Eurosail* case as it may offer some clues to the reasons for the approach taken by the Supreme Court and, in particular, the reason why the Supreme Court did not provide any detailed guidance in relation to the conduct of the balancing exercise required by section 123(2).

The Transaction

The Issuer is a special purpose company that acquired a portfolio of Sterling denominated mortgage-backed loans all relating to UK residential properties. This purchase was funded by the issue of notes in a number of separate classes with different priority and interest entitlements. The notes were denominated in three currencies – Sterling, Euros and US$. The notes had long stop dates for payment as late as 2045, but in practice it was expected that they would be discharged at a much earlier date as the underlying mortgages were redeemed.

The Issuer entered into various currency and interest rate hedging transactions with a US Lehman entity to hedge its obligations under the notes. These agreements were terminated following the collapse of the Lehman group in circumstances where the Issuer was unable to purchase replacement hedging arrangements. The lack of hedging caused heavy losses to the transaction as foreign exchange rates moved significantly against the Issuer. This had the consequence that the non-sterling notes

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were being paid down at a much slower rate (and using more of the Sterling generated by the mortgage portfolio) than originally anticipated.

Two key points should be noted about the ranking of the different classes of notes under the payment waterfall contained in the trust deed prior to the service of an enforcement notice by the Trustee:

(1) The principal sums due in respect of the notes would be paid sequentially to the noteholders, having regard to the different rankings of the sub-classes of Notes. In other words, the Issuer was obliged to repay the A1 Notes in full first, then the A2 Notes, then the A3 Notes etc.

(2) The junior Notes (i.e. the B Notes, C Notes, the D Notes and the E Notes) would continue to receive payments of interest from available funds on each Interest Payment Date.

This state of affairs would materially alter under the payment waterfall that would apply following the service of an enforcement notice by the Trustee. Three key points should be noted:

(1) All the notes would become immediately repayable;

(2) The sums available for payment to the Noteholders would be paid sequentially in order of the seniority of the Notes disregarding the sub-classes. In

In view of the large deficiency in net assets, the A3 Noteholders argued that it could not sensibly be contended that the Section 123(2) trigger had not occurred on any interpretation of Section 123(2).

other words, the A1 Notes would rank *pari passu* with the A2 Notes and the A3 Notes for all payments of principal and interest.

(3) The junior Notes would not receive any further payments (whether in respect of principal or interest) unless and until all prior ranking classes of notes had been repaid in full.

The aim of the A3 Noteholders

The A3 Noteholders were concerned that there would not be sufficient collateral to meet the principal due on their notes as and when they fell due for payment. The Issuer's audited and management accounts indicated that there would be a significant shortfall in this regard: the management accounts presented a net liability position of in excess of £120 million. Accordingly, faced with the prospect of such a shortfall but in circumstances where monies continued to be paid to lower ranking notes, the A3 Noteholders wished to trigger a change in the priority of payments so that all A Notes ranked *pari passu*.

In the first instance, the A3 Noteholders sought to achieve their aim by purporting to direct the Trustee to serve an enforcement notice as they held more than 25% of the A Notes as a whole. This attempt proved to be unsuccessful, Sales J finding that the conflict between the interests of the A1 and the A2 Noteholders on the one hand and the A3 Noteholders on the other meant that any such direction was ineffective unless given by each of the sub-classes of the A Notes which were in conflict: see [2009] EWHC 513 (Ch).

The A3 Noteholders then changed tack and sought to rely on the trigger set out Condition 9(a)(iii) of the Notes:

The Issuer…being unable to pay its debts as and when they fall due or, within the meaning of Section 123(1) or (2) (as if the words "it is proved to the satisfaction of the court" did not appear in Section 123(2)) of the Insolvency Act 1986 (as that Section may be amended from time to time), being deemed unable to pay its debts.

A breach of Condition 9(a)(iii) would not automatically give rise to the service of an enforcement notice by the Trustee. The clause additionally required a direction by the Noteholders or the exercise of the Trustee's discretion and the requirement that the Trustee certify to the Issuer that the event was, in the Trustee's sole opinion, materially prejudicial to the interests of the Noteholders.

Post-enforcement call option ("PECO")

The Eurosail structure also included a PECO which, in certain circumstances, entitled OptionCo (a company associated with the Issuer) to acquire the entirety of the notes for a nominal consideration.

The option was conferred pursuant to clause 3.1 of the PECO:

In connection with the issuance of the Notes, the Trustee on behalf of the Noteholders, but without any personal liability on its part, hereby grants, and the Issuer hereby acknowledges, an option (the "Option") exercisable by OptionCo, permitting OptionCo to acquire all (but not some only) of the Notes (plus accrued interest thereon) in the event that the Security for the Notes is enforced and the Trustee, after the payment of the proceeds of such enforcement, determines that the proceeds of such enforcement are insufficient, after payment of all claims ranking in priority to or pari passu with the Notes pursuant to the Deed of Charge, to pay in full all principal and/or interest and any other amounts whatsoever due in respect of the Notes. The Trustee shall promptly after the Security is enforced and the proceeds of such enforcement are paid, make a determination of whether or not there is such insufficiency. If the Trustee determines that there is such an insufficiency the Trustee shall forthwith give notice (the "Insufficiency Notice") of such determination to OptionCo and the Issuer."

Whilst it is a rather lengthy provision, the key point to note is that its commercial effect would be to protect the Issuer from the risk of being wound-up as the notes would find their way into the hands of a friendly entity.

Clause 3.2 of the PECO enabled the option to be exercised by notice at any time after an Insufficiency Notice had been given. The key point in this regard is that such a notice could only be given following the enforcement of the security in circumstances that led to a deficiency of assets to meet the claims of the Noteholders.

Summary of the arguments

There were two main planks to the argument of the A3 Noteholders that the section 123(2) event of default had been triggered:

(1) They relied on the fact that all the financial information available in relation to the Issuer indicated that it was unable to pay its debts within the meaning of section 123(2). For example, the latest audited financial statements revealed that the Issuer had net liabilities of around £75 million. As noted above, the management accounts demonstrated an even larger deficiency. If reduced to present values, the amount of liabilities exceeded the value of assets and therefore the Issuer was deemed unable to pay its debts within the meaning of Section 123(2). The A3 Noteholders contended that the statutory balance sheet was the beginning and the end of the enquiry, subject to any necessary modifications to include assets and liabilities not otherwise recorded on the statutory balance sheet. In view of the large deficiency in net assets, the A3 Noteholders argued that it could not sensibly be contended that the section

123(2) trigger had not occurred on any interpretation of section 123(2).

(2) They further contended that the existence of the PECO was entirely irrelevant to the section 123(2) issue as the Notes were full recourse obligations of the Issuer at all times prior to the exercise of the PECO and, critically, that they remained so as at the point at which the assessment of whether Section 123(2) was satisfied was conducted.

The Issuer contended that there had been no breach of the section 123(2) trigger. It relied, in broad terms, on three distinct arguments:

(1) Despite the large sum of net liabilities shown in its financial statements, the Issuer was not unable to pay its debts within the meaning of section 123(2) of the Act. It contended that the exercise required by Section 123(2) of the Act was materially different to that required for the drawing up of the balance sheet in accordance with relevant accounting standards and that, in respect of prospective and contingent liabilities, the phrase "taking into account" meant that the exercise involved a more refined consideration of whether a company could be expected to pay such debts rather than simply requiring their inclusion (at some value) in the balance sheet.

(2) It contended in the alternative that the section 123(2) event of default should be seen as having a special meaning, different to the ordinary meaning of the statute, when viewed in the overall context of the transaction.

(3) In any event, the PECO precluded a determination that the Issuer was unable to pay its debts within the meaning of section 123(2) as it was impossible for the Issuer's liabilities to exceed its assets, because the PECO's practical effect was to make the Notes limited in recourse to the value of the Issuer's assets.

The Chancellor [2011] 1 WLR 1200 and the Court of Appeal [2011] 1 WLR 2524 determined that the Issuer was not unable to pay its debts within the meaning of section 123(2). They also determined that the PECO would not have assisted the Issuer had it otherwise been unable to pay its debts within the meaning of section 123(2).

Findings of the Supreme Court

The Supreme Court (Lord Walker delivering a judgment with which each of the other members of the Court agreed) held that the Issuer was not unable to pay its debts within the meaning of section 123(2).

Lord Walker emphasised that the exercise required by Section 123(2) differs from the preparation of a company's statutory accounts. He found that section 123(2) requires a petitioner to satisfy the court, on the balance of probabilities, that a company cannot reasonably be expected to meet, or has insufficient assets to be able to meet, all its liabilities, including prospective and contingent liabilities: see [42] and [48], and also the subsequent application of *Eurosail* by Warren J in *Re Casa Estates (UK) Ltd* [2013] EWHC 2371 (Ch) at [34] – "*can the company reasonably be expected to meet its liabilities?*"

Lord Walker emphasised that the exercise required by Section 123(2) differs from the preparation of a company's statutory accounts.

Lord Walker further noted that the starting point in a case where the liabilities of the Issuer were not repayable for a further 30 years and it was meeting its debts as they fall due, was that the Court should proceed with the greatest caution: see [42]. Lord Walker then considered the impact of the fact that the movements of foreign exchange and interest rates over this period were incapable of prediction with any confidence: see [49]. He concluded that this meant that the Court could not be satisfied that there would eventually be a deficiency of assets to meet the Issuer's future liabilities under the Notes as and when the Notes matured. Lord Walker therefore found that the A3 Noteholders had failed to discharge the burden of proof of demonstrating that the Issuer was unable to pay its debts within the meaning of s123(2): see [49].

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In view of this conclusion, the Supreme Court did not finally determine the alternative argument of the Issuer that the section 123(2) trigger in Condition 9(a)(iii) should be seen as having a special meaning different to the ordinary meaning of the statute when viewed in the overall context of the transaction. As noted by Lord Walker (at [50]), this would have been a very difficult argument for the reasons given by the Supreme Court in *Enviroco Ltd v Farstad Supply A/S* [2011] 1 WLR 921 in view of the fact that Condition 9(a)(iii) expressly cross-referred to the statutory provision, thereby *prima facie* incorporating its ordinary meaning into the contract.

In view of the finding of the Supreme Court on section 123(2), there was no need for it to consider in any detail whether, on the assumption that section 123(2) had been triggered, the PECO would have come to the Issuer's rescue

It is this notion of "taking into account" that, in the context of a company with large prospective and contingent liabilities, requires the Court to do more than simply value and compare the asset and liability position.

and prevented an event of default from occurring. Transactional lawyers will be interested to note that Lord Hope did, however, take time to answer this question. Lord Hope concluded that the Chancellor and the Court of Appeal were correct to find that the PECO would not have assisted the Issuer.

Lord Hope found that the relevant provisions of the Notes and the PECO meant that the Issuer's obligation to pay the Noteholders' principal and interest on their claims remained full recourse obligations until (i) the security had been enforced by the Trustee; (ii) the collateral had been realised and distributed with a deficiency to the Noteholders; and (iii) OptionCo had exercised the PECO and acquired the notes. In other words, the liability of the Issuer to the Noteholders should not be characterised as amounting to a limited recourse liability prior to the service of an Enforcement Notice: see [61].

Lord Hope rejected the argument of the Issuer that this conclusion would amount to the triumph of legal form over commercial substance. He cited the decision of the Supreme Court in *Rainy Sky SA v Kookmin Bank* [2011] 1 WLR 2900 and agreed that the Court should adopt the more, rather than the less, commercial construction where competing interpretations were available. He found that this principle did not assist the Issuer as the wording of the PECO was not open to doubt: see [62]-[64].

Guidance given by the Supreme Court

First, the Supreme Court expressly rejected certain labels used by Lord Neuberger MR in the Court of Appeal: see [42] and [48]. Lord Neuberger MR had characterised the meaning of section 123(2) as requiring an answer to the question of whether the company had "*reached the point of no return*" or whether it was a company which should "*put up the shutters*". The use of these labels had the potential to give rise to serious issues. This can be illustrated by three short examples:

(1) The use of such labels gave rise to a serious risk of conflating the test for an inability to pay debts found in s123(2) and the test for wrongful trading found in section 214 of the Act which requires the Court to be satisfied "*that there was no reasonable prospect that the company would avoid going into insolvent liquidation*". Practitioners will be well aware that this is a test that can be very difficult to satisfy as a matter of evidence as highlighted by the low number of successful wrongful trading claims.

(2) The classic way in which creditors can enforce the duty of the directors of an insolvent company to act in the best interests of its general body of creditors is to commence insolvency proceedings. A test which equated section 123(2) with whether a company had reached the "*point of no return*" would have imposed a very high hurdle for a contingent or prospective creditor to discharge when exercising the class right to petition for the winding-up of the company. There is normally no question of disclosure on a winding-up petition so it is difficult to see how creditors could have questioned an apparently credible assertion by the directors that the company had not yet reached the point of no return.

(3) The labels used by the Master of the Rolls were already giving rise to practical difficulties in the context of claims by officeholders to avoid antecedent transactions. An inability to pay debts within the meaning of section 123 is a necessary pre-condition to a successful claim by an officeholder to avoid an antecedent transaction as a preference under section 239 of the Act or an undervalue under section 238 of the Act: see section 240(2) of the Act. Defendants to undervalue and preference claims were becoming quick to assert that the company had not reached the "*point of no return*" at the time of the transaction.

It is to be welcomed that the Supreme Court has expressly rejected this gloss on the language of section 123(2) although, it may be questionable to what extent, in practice, balance sheet insolvency based in large part on prospective or contingent liabilities will ever be capable of being demonstrated short of such a case.

Second, the Supreme Court expressly approved *Cheyne Finance (No.2)* (referred to above) in which Briggs J found that the cashflow test in s123(1)(e) contains an element of futurity: see [34]. Lord Walker noted, however, that once the Court has to move beyond the reasonably near future any attempt to apply a cashflow test will become completely speculative, and that s123(2) then becomes the only sensible test for determining whether a company is unable to pay its debts: see [37].

Third, Lord Walker confirmed that the assessment of whether a company is unable to pay its debts within the meaning of s123(2) may differ from a company's statutory balance sheet prepared in accordance with the requirements of the Companies Act 2006. In particular, the test may require the Court to take in to account contingent assets or contingent liabilities that are not reflected on the statutory balance sheet: see [1].

Fourth, it is this notion of "*taking into account*" that, in the context of a company with large prospective and contingent liabilities, requires the Court to do more than simply value and compare the asset and liability position. Despite what some might consider to be relatively clear language in Section 123(2), and the fact that (1) the exercise of "*taking into account*" is directed to be done for the purpose of assessing whether the amount of liabilities exceeds the value of assets i.e striking a balance; and (2) a shortfall of assets as against liabilities under Section 123(2) is expressed as deeming a company

unable to pay its debts, it is clear that a negative balance sheet may not be enough to satisfy section 123(2). A further aspect of the required analysis is to consider whether the company can reasonably be expected to meet those prospective and/or contingent liabilities in the future.

Potential future issues

It is appropriate to conclude by highlighting four potential future issues arising from the decision.

First, it is perhaps unfortunate that the Supreme Court did not provide any guidance on how contingent and prospective liabilities should be taken into account as a matter of practical reality when conducting the balancing exercise called for by section 123(2). Lord Walker informs us that there is a need to discount for "*contingencies and deferment*" (at [37]) and agrees with the view of Toulson LJ in the Court of Appeal that there is a need to make "*proper allowance*" for contingent and prospective liabilities (at [42]), but does not comment further on the methodology to be adopted when undertaking the discounting exercise. The simple answer may be that this is a fact-sensitive question that depends on the nature of the liability in question, but it is a point which is likely to generate litigation in the future. It would have been helpful to know whether the Court should adopt the methodology set out in the Insolvency Rules 1986 for the valuation of contingent debts (rule 4.86) and prospective debts (rules 4.94 and 11.13) or whether there is some other basis for "*taking into account*" contingent and prospective liabilities under section 123(2). The issue of the valuation of contingent liabilities may give rise to additional difficulties in the future following the Supreme Court's recent decision in *Lehman/Nortel* [2013] UKSC 52 that expands the matters that are capable of giving rise to contingent liabilities under rule 13.12.

Second, the judgment of Lord Walker contains language that requires an enquiry as to whether a company could reasonably be expected to meet contingent and prospective liabilities as and when they fall due. For example, Lord Walker relies on the fact that the Court "*cannot be satisfied that there will eventuality be a deficiency*": see [49]. This language appears much closer to the cashflow test found in section 123(1)(e) as opposed to the balancing of assets and liabilities required by section 123(2). It is difficult to discern the need for such an enquiry from the wording of section 123(2) and the practical utility of such a test must be uncertain in view of Lord Walker's recognition that a cashflow test is difficult to apply beyond a point in the reasonably near future. Warren J in *Re Casa* (above) went as far as saying that there is no rigid demarcation between the two tests, and that they feature as part of a single exercise focusing on whether a company is unable to pay its debts.

LORD WALKER OF GESTINGTHORPE

Third, the application of the *Eurosail* test to transaction recovery actions (such as transactions at an undervalue) is not entirely without difficulty. Some assistance can now be derived from *Re Casa*, in which Warren J suggested that a negative balance sheet based on current assets and liabilities is sufficient to give rise to a *prima facie* case that Section 123(2) is satisfied, such that (at least in the context of a petition) there is then an evidential burden on the company to show why it can, notwithstanding its balance sheet position, reasonably be expected to meets its liabilities (see [81]). But officeholders will still need to be wary that, in actions against unconnected persons, they will carry the burden of demonstrating balance sheet insolvency in the sense described in *Eurosail* (see [89]).

Fourth, it is perhaps time for the draftsman of finance documents to give serious consideration as to whether section 123(2) is an appropriate trigger to include as an event of default in circumstances where the test requires much more than a cursory glance at the balance sheet of the company. As illustrated by the *Eurosail* case, the fact sensitive enquiry required by section 123(2) seems a long way from the certainty that is required in the context of determining whether an event of default has occurred under a finance document.

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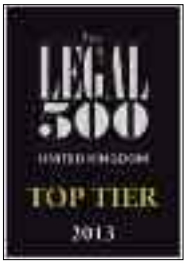
2014 Legal 500 Guide



The recently released 2014 Legal 500 guide to the UK Bar highlights South Square's depth of expertise across a range of practice areas. As you might expect, our commercial work, including all aspects of international trade, finance and commerce, with particular emphasis on banking, insurance, reinsurance and 'city' work, is recognised as a particular strength. But the diversity of Members' practices, including sport, international arbitration and civil fraud, is also emphasized. We are also delighted that our clients also praise our 'extremely responsive, accessible, and very professional clerks'. We bring you some highlights from the Legal 500 below.

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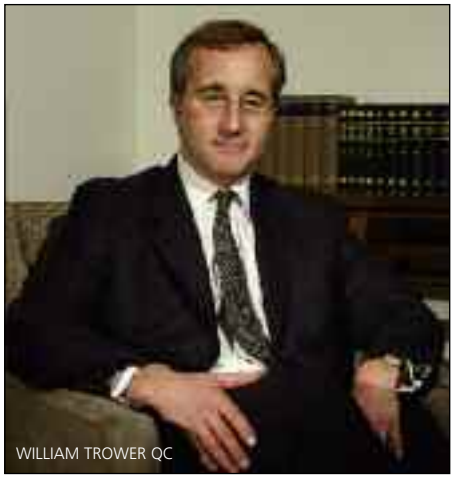
Daniel Bayfield
Tom Smith
Richard Fisher
Stephen Robins
Joanna Perkins
Jeremy Goldring QC is noted as a New Silk in this field.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Michael Crystal QC
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Robin Knowles QC
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Glen Davis QC
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Daniel Bayfield
Tom Smith


ANTHONY ZACAROLI QC

Insolvency

South Square provides 'a world-class service', and is 'the best set at the Bar for insolvency matters'. We are delighted that our clients are enthusiastic about the work we undertake both at silk and junior level in this field. Our Members continue to be involved in almost every major insolvency, including Administrators of Heritable Bank plc v Winding-up Board of Landsbanki Islands HF, BNY Corporate Trustee v Eurosail, and Re Nortel GmbH, all in the Supreme Court in 2013.
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David Alexander QC
Antony Zacaroli QC
Glen Davis QC
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John Briggs
Adam Goodison
Hilary Stonefrost
Lloyd Tamlyn
Ben Valentin
David Allison
Daniel Bayfield
Tom Smith
Richard Fisher
Stephen Robins.
Listed as New Silks in this field are Mark Arnold QC, Jeremy Goldring QC and Lucy Frazer QC.


JEREMY GOLDRING QC


BEN VALENTIN


LUCY FRAZER QC


DANIEL BAYFIELD


RICHARD SHELDON QC


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The complex cases regularly handled by the barristers at South Square often include elements of insurance, reinsurance and professional negligence.
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Fidelis Oditah QC is recommended as a leading Silk for International Arbitration.

Media, entertainment and sport

Recommended as a leading Silk is **Mark Phillips QC**, who handles high-profile Formula 1 cases (advising and representing Formula 1 teams and drivers in connection with competition law issues) and heavyweight football disputes. He regularly leads recommended junior **Daniel Bayfield**, who acts for the FA Premier League and the Football League.


MARK PHILLIPS QC

INSOL Europe Annual Congress

Report by John Briggs

The conference was billed as giving delegates an exciting programme showing "the full cabinet of horror that officeholders may experience in their profession, from bad banks to the shipping industry in the perfect storm, and a Fraud-European tour 2013, failing of restructuring, the personal risk and liability of directors and administrators, to real estate which cannot be sold, valuation issues where there is no value and fights between shareholders, junior creditors and senior creditors".

As it turned out, the conference, which was well attended by over 400 delegates from most EU jurisdictions, and particularly Germany, the Netherlands and Ireland, raised most frequently the spectre of lack of judicial trust and confidence between jurisdictions, and the lack of cooperation and trust between officeholders from different jurisdictions and between local creditors and foreign officeholders. Localism is still too often alive and well! Questions from delegates all too often raised the issue of the failure of one State's courts to communicate with those of another, or local creditors failing to understand the practices and procedures in a different jurisdiction. This was particularly the case in debate following the session on "Secondary proceedings" on the second day of the conference.

The Break-out- session "Turnaround Wing: Why do restructurings fail?" gave the not-unexpected answer that promoters and directors of companies are over-optimistic about its business and prospects. Anyone familiar with directors disqualification proceedings in the UK will be only too aware of this phenomenon!

PARIS REVEALED A LACK OF JUDICIAL TRUST AND CONFIDENCE BETWEEN JURISDICTIONS

The delights of Paris, good weather, fine wine and good food, was somewhat offset by the gloomy and disorganised interior of the Hyatt Regency, the Congress Hotel, adjacent to the Palais des Congrès, at Porte Maillot. Notwithstanding the gloomy interior of this hotel, the Welcome Drinks Reception and Congress dinner, morning welcome coffees and coffee breaks afforded a marvellous opportunity to meet delegates and speakers from the UK and Europe.

Unlike some international conferences, the Break-out sessions were well attended and particularly interesting was the "Anti-Fraud Forum: Fraud – European Tour 2013" chaired by David Ingram of Grant Thornton UK, with a panel of speakers from France, Germany and Cyprus. The use of liquidation proceedings as an asset tracing exercise in the common law jurisdictions is well- known, liquidators are not risk averse and have powers at their disposal to obtain information not generally available in ordinary civil proceedings. However, it quickly became apparent during the session that the same possibilities do not exist in a number of Continental jurisdictions. Officeholders are under the control of the supervising judge, CFAs are not possible, even illegal in some jurisdictions, and recovery of costs limited. Cultural differences also exist, since traditionally matters of fraud or suspected fraud are referred to State prosecuting authorities who run the proceedings at public expense (usually in a dilatory and unsatisfactory manner), with the officeholder attending or actively participating, with a view to eventual combined criminal and civil sanctions.

The Programme of events finished off with a boat trip down the Seine including dinner and entertainment, which was delightful.

Lastly, it should be mentioned that the programme was preceded by an Academic Forum in which our own Professor Ian Fletcher gave an eminent and well received lecture to fellow academics.

INSOL International Cayman Islands

MARRIOTT BEACH RESORT GRAND CAYMAN

INSOL International is holding a one day seminar at the Marriott Beach Resort on Grand Cayman in association with Recovery and Insolvency Specialists Association (Cayman) Ltd (RISA). South Square continues its close partnership with INSOL and is a Gold Sponsor of the event.

The programme covers cross-border insolvency and restructuring topics, with a particular focus on the offshore jurisdictions. Topics to be covered include Offshore Restructuring in the region, directors and insolvency proceedings, ISDA and the lessons to be learnt from Lehman, law enforcement and insolvency and developments in international insolvency law. In addition the programme has a slot for a series of presentations by rising stars which looks as if it is going to be like X Factor (it is certainly billed as that) with the delegates picking the winner. The seminar involves restructuring professionals from across the region and is designed to be interactive and to allow attendees to discuss and debate practical issues with the speakers.

South Square will be well represented at the INSOL International seminar as the following are currently planning to attend: Richard Hacker QC, David Alexander QC, Glen Davis QC, Felicity Toube QC, Hilary Stonefrost, Stephen Robins, Marcus Haywood and William Willson. But these will not be the only members of South Square in the Cayman Islands during the course of that week. Richard Hacker QC will also be appearing that week in the Cayman in the Court of Appeal in Re Cybernaut Growth Fund L.P. in circumstances in which a Cayman exempted limited partnership may be wound up on the just and equitable ground (including whether a petition presented by a limited partner is liable to be stayed in favour of a foreign arbitration). Michael Crystal QC, Gabriel Moss QC, Tom Smith and Stephen Robins are also scheduled to be in the Court of Appeal later in the week in Irving H Picard (as Trustee for the Liquidation of Bernard L.Madoff Investment Securities LLC) & Anor v Primeo Fund (in Official Liquidation) where the issue concerns the ability of the Cayman to apply foreign law or Cayman law transaction avoidance provisions in support of a foreign insolvency. So it looks as if quite a few members of South Square will be in Cayman at the same time. If you are there, look out for them!

RICHARD HACKER QC

WILLIAM WILLSON

MARCUS HAYWOOD

NEWS in brief

South Square hits the heights at Bar Awards

SOUTH SQUARE'S BARRY ISAACS QC AND LLOYD TAMLIN WITH CRIMINAL BARRISTER, CLIVE ANDERSON.

Members of Chambers gained two prestigious awards at the 2013 Bar Awards at a glittering ceremony at the Hilton Hotel in Park, hosted by television personality (and barrister) Clive Anderson. Barry Isaacs QC was named Silk of the Year in Insolvency and Corporate Restructuring, after just two years as a QC.

Barry was praised by the judges for his important work in insolvency and as "accessible, sharp, commercial and user friendly".

Lloyd Tamlyn was named Junior of the Year. He was described as "exceptionally bright, he grasps issues very quickly and is great to work with". Very many congratulations to both Barry and Lloyd.

UK insolvency judgement recognised in Russia

Like the case described in page 55 of the August 2013 edition of the South Square Digest, this case also arises out of the collapse of the property empire of Sean Quinn, now Ireland's largest bankrupt. A Quinn company, Demesne Investments Limited ('Demesne') by a series of purported assignments dated 4th April 2011 was alleged to have parted with claims against a series of Russian entities for many millions of dollars in return for a price of US$100 for each claim. The purported assignee was a Belize company called Galfis. The dating on the assignments of 4th April 2011 was highly suspicious as the accounts of Demesne continued to show the purported assigned claims as belonging to Demesne. Even the purported US$100 per assignment was not paid. Subsequently, documents were obtained by proceedings in Belize which showed that the assignments could not have been executed on 4th April 2011. Apart from anything else, Galfis itself was only taken off the shelf on 6th July 2011. The significance of the dating was that whilst Sean Quinn was a Director of Demesne on 4th April 2011, he ceased to be such after 14th April 2011. By July 2011 he had no power or authority to execute any assignment. Not surprisingly therefore the High Court Judge hearing the matter in Northern Ireland McCloskey J, concluded that the assignments were null and void for lack of authority. In the alternative he found that the transactions were unlawful on the ground that Sean Quinn was acting in blatant disregard of his fiduciary duty to Demesne and that Galfis had actual constructive knowledge of the material facts. In the further alternative, the Judge found that the assignments were void under the Northern Irish equivalent of Section 423 of the Insolvency Act 1986, which gives the court power to avoid transactions at an undervalue entered into for the purpose of putting assets beyond the reach of Demesne. The assignments here were plainly at a substantial undervalue. On 8th October 2013, the Russian Supreme Arbitrazh Court recognised the order of the Northern Irish Court. The relevant Russian attorney was Andrey Zelenin, a partner in Lidings in Moscow. Gabriel Moss QC acted as Lead Counsel in Northern Ireland and advised on English law in relation to the recognition application in Russia.

GABRIEL MOSS QC

South Square supports Africa round table in Lusaka

South Square's Fidelis Oditah QC, SAN and Glen Davis QC joined legislators, lawyers insolvency practitioners, bankers, judges, policymakers and academics from some 15 countries across Africa (as well as Bermuda, the United States, UK and Holland) in Lusaka, Zambia on 11-12 October for the latest Africa Round Table organised by Insol International and the World Bank Group under the theme: "Building Africa's Credit Environment for Growth: How insolvency regimes can improve the cost and availability of credit". South Square was one of the sponsors of this year's event, and Fidelis and Glen both moderated panels.

The Africa Round Table initiative was conceived at a meeting during the INSOL Dubai conference in 2010. The inaugural meeting was held in Abuja, Nigeria in September 2010. The second ART took place in Cape Town, South Africa, in 2011, and the third in Nairobi, Kenya, last year.

Giving the keynote address, the Hon Wynter Kabimba, Zambia's Minister of Justice, noted that there are currently fewer insolvency reforms across Africa than in any other region of the world. "The skills of stakeholders, including the Judiciary and insolvency practitioners, need to be developed, and countries need to focus on both institutional and infrastructural reforms that will seek to preserve value in financially distressed businesses".

FIDELIS ODITAH QC

ABOVE: THE RADISSON BLU HOTEL, LUSAKA.
BELOW: WYNTER KABIMBA GIVES HIS KEYNOTE SPEECH

DIARY DATES

30 October-2 November 2013.
Atlanta, Georgia, USA.
NCBJ Annual Conference.

6 November 2013.
London, Natural History Museum.
Insolvency Lawyers Association Annual Dinner. Preceded by Lecture by Mr Justice David Richards: "Evolution: the role of the judge in insolvency."

7 November 2013.
Cayman Islands.
INSOL International Offshore Seminar. (Sponsored by South Square)

14 November 2013.
London.
TMA UK Annual Conference.

2014
14-16 May 2014
Tivoli Marina,
Villamoura, Portugal.
R3 Annual Conference.

Halsbury's Laws

The new edition (the 5th edition) of Halsbury's Laws, Vol 3(2) (Bankruptcy and Individual Insolvency) is due to be published shortly. **Felicity Toube QC** and **Richard Sheldon QC** are the Consultant Editors.

RICHARD SHELDON QC

FELICITY TOUBE QC

New member arrives at South Square

South Square is pleased to announce that Matthew Abraham has become a member of Chambers following the successful completion of his pupillage here. Matthew joined Chambers after obtaining a first class law degree from University College London and the BCL from Oxford University. Matthew was called to the Bar at Lincoln's Inn in 2012 as a Lord Mansfield Scholar and was awarded the Megarry Award and the Buchanan Prize for his performance on the BPTC. For the year between his undergraduate and postgraduate degrees Matthew worked as a judicial assistant in the Supreme Court of India.

Matthew also carried out an internship at Shook Lin & Bok LLP in Singapore and Malaysia working on restructuring and insolvency matters as well as commercial arbitrations. As a result of this year Matthew developed strong ties within the Indian, Singaporean and Malaysian Bar.

During his BPTC, Matthew was a tutor in company law at St Catherine's College Oxford and King's College London. Matthew continued to tutor company law for the Oxford Law Faculty during his pupillage year.

- ***Called to the Bar, Lincoln's Inn, 2012***
- ***Pupillage at South Square, 2012-2013***

MATTHEW ABRAHAM

NEWS in brief

City Equities Limited - Special Administration

At 17.24pm on Friday 11 October 2013, at an urgently convened hearing, Mr Justice Roth at the Rolls Building, London granted a special administration order in respect of an investment bank, City Equities Limited.

The directors of the brokerage house had wanted originally to appoint administrators out of court, but had been advised this was not possible because of the special investment bank administration regime imposed by the Investment Bank Special Administration Regulations 2011 / 245 ("the IBSAR"). The Financial Conduct Authority required an expedited hearing as a matter of policy so as to protect the client monies and client assets.

This case follows on the previous work from South Square on investment banks, brokerage houses, and FCA or other regulated entities. This was only the 5th-ever case under the IBSAR, the previous cases in London being MF Global UK Ltd (represented on the application by **Martin Pascoe QC** of South Square), Worldspreads Ltd (represented on the application by **Glen Davis QC** of South Square). There have also been two small cases outside London, Pritchard Stockbrokers Ltd and Fyshe Horton Finney Ltd.

Adam Goodison of South Square acted for the directors of City Equities Ltd. A review is being undertaken for HM Treasury on the statutory regime of administration for investment banks.

ADAM GOODISON

Professor Ian Fletcher QC

In August 2013, Professor Ian Fletcher QC delivered a paper at the International Law and Arbitration Conference, conducted jointly by the Federal Court of Australia and the Law Council of Australia. His paper, in a session devoted to cross-border insolvency, was titled: "Tomorrow's World – Current and Future Prospects for International Cooperation in Insolvency Matters". The paper will be published in a book of the collected papers from the conference. On 26 September 2013 at the conference of the Academic Forum of INSOL Europe in Paris Professor Fletcher delivered the 2013 Edwin Coe Lecture. The title was: "Spreading the Gospel: The mission of insolvency law, and insolvency lawyers, in the early 21st century".

Insolvency levels down

UK corporate insolvency levels are on a downward trend. The overall business insolvency rate fell to 0.08% in July 2013 from 0.09% in July 2012. Nine out of eleven regions in the UK saw the insolvency rate drop in July 2013 by comparison to July 2012.

The exceptions were London and the South East. Yorkshire and the West Midlands saw the greatest decreases in insolvency levels.

The trend continued into August 2013 where levels fell from 0.09% in August 2012 to 0.08% in 2013.

The largest fall in August was in the North East and London posted its first decrease since March 2013.

Top earners pay lion's share of tax

In mid-2012 the UK population was estimated to be 63.7 million. As at 2010-2011 HMRC said that there were about 29 million individual tax payers. Whilst there is a slight mismatch in the years, it seems that under half of the population pays any tax at all.

Of those who do pay tax about 4.3 million apparently pay the higher rate and about 290,000 pay the top rate (formerly 50% but now 45%).

HMRC receive £150 billion a year in respect of income tax. People in the top 1% - for which it is said you need to earn £160,000 - pay almost a third of that sum. For in 2013-2014 the best paid 1% will contribute 29.8 per cent of all income tax. That is up from 1997 when they paid 20% of all income tax. And up from 2007 when they paid 24.4%.

Appointments and retirements

In the last two issues of the Digest news in brief has recorded a significant number of new appointments to the bench. This time there are more appointments as well as retirements.

At the top tier, The **Rt Hon Patrick Stewart Hodge** was appointed as a Justice of the Supreme Court with effect from 1 October 2013. He joins Lord Reed as the Scottish members of the Court. Lord Hodge replaces Lord Hope following the latter's retirement after 17 years of service in the House of Lords and the Supreme Court.

Moving to the Court of Appeal, two well-known former Chancery judges have retired. **Lord Justice John Mummery**, who was called to the bar in 1964, became a High Court judge in the Chancery Division in 1989 and was appointed to the Court of Appeal in 1996, retired on 6 September 2013. **Lord Justice Timothy Lloyd**, who was called to the bar in 1970, took silk in 1986, became a High Court judge in the Chancery Division in 1996 and was appointed to the Court of Appeal in 2005 retired on 1 October 2013.


LORD HODGE

On to the next tier in the judiciary, **Lord Justice Leveson**, who became a household name after being put in charge of the inquiry into media practices, became President of the Queen's Bench Division with effect from 1 October 2013. He succeeds **Sir John Thomas** who has become Lord Chief Justice. There have also been more appointments to the High Court bench. **Geraldine Andrews QC**, **Stephen Philips QC** and **Nicholas Green QC** were appointed with effect from 1 October 2013 and have been assigned to the Queen's Bench Division. **Christopher Nugee QC** was also appointed with effect from 1 October 2013 and has been assigned to the Chancery Division. **Ingrid Simlar** has been appointed with effect from 28 October 2013 and will sit in the Queen's Bench Division.

After the recent of judicial appointments to the Chancery Division over the course of the last year, and leaving aside the Chancellor, the current make-up of the Chancery Division is as follows (in order of seniority): Sir Peter Smith, Sir David Richards, Sir Anthony Mann, Sir Nicholas Warren, Sir Lancelot Henderson, Sir Paul Morgan, Sir Alistair Norris, Sir Gerald Barling, Sir Philip Sales, Dame Sonia Proudman, Sir Richard Arnold, Sir Peter Roth, Sir Guy Newey, Sir Robert Hildyard, Dame Sarah Asplin, Sir Colin Birss, Dame Vivien Rose and Sir Christopher Nugee.


LORD JUSTICE LEVESON

Hourly rates under attack

The President of the Supreme Court, Lord Neuberger has said that "slow and ignorant" lawyers are using hourly charging rates to unjustly inflate their bills.

Speaking during a lecture at Freshfields Bruckhaus Derringer, Lord Neuberger is reported to have said "where the service is legal advice or representation, there is a public interest in keeping the charge as low as possible.

"In this connection the centrality of the hourly rate appears to me to be malign. As a matter of principle, it confuses cost with value.

"It encourages inefficiency or worse: if a lawyer is short of work, it can be surprising how much time a particular task takes. The hourly rate rewards the slow and ignorant lawyer at the expense of the speedy and knowledgeable lawyer".

Lord Neuberger called for an overhaul of legal fees to reduce the sums paid.


LORD NEUBERGER

South Square Challenge

Welcome to the November 2013 South Square Challenge. It is the usual format. All you have to do is look at eight pairs of picture clues, work out what they are clues for and then identify the link between the eight answers. As usual for the winner (drawn from the wig tin if there is more than one correct entry) there will be a magnum of champagne and a South Square umbrella. Please send your answers by email to kirstendent@southsquare.com or by post to Kirsten at the address on the back page. Entries by 10 January 2014 please! Good luck. *David Alexander QC*

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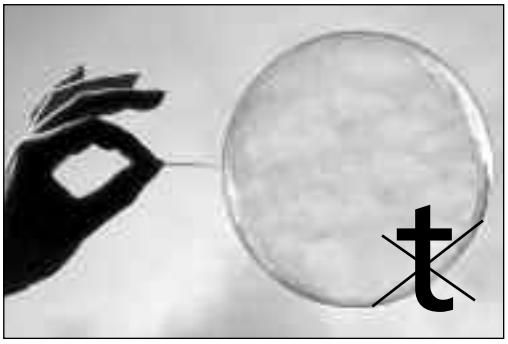

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9 And the connection is?

AUGUST CHALLENGE

The correct answers to the August 2013 South Square Challenge were: (1) Somerset's Case (2) Bushel's Case (3) Carlill v Carbolic Smokeball Company (4) Salomon v Salomon (5) Associated Provincial Picture Houses v Wednesbury Corporation (6) British Airways v Laker Airways (7) Rylands v Fletcher (8) Factortame. The most important missing case that seemed to be obviously missing from the list was Donaghue v Stevenson. There were a number of correct answers. But the winner drawn from the wig tin is Neil Dooley of Hogan Lovells to whom go our congratulations together with a magnum of champagne and a South Square umbrella

SOUTH SQUARE

"A VERY HIGH-QUALITY GROUP OF BARRISTERS WITH A WONDERFUL BLEND OF SKILLS."

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Christopher Brougham QC
Gabriel Moss QC
Simon Mortimore QC
Richard Adkins QC
Richard Sheldon QC
Richard Hacker QC
Robin Knowles CBE QC
Mark Phillips QC
Robin Dicker QC
William Trower QC
Martin Pascoe QC
Fidelis Oditah QC
David Alexander QC

Antony Zacaroli QC
Glen Davis QC
Barry Isaacs QC
Felicity Toube QC
Mark Arnold QC
Jeremy Goldring QC
Lucy Frazer QC
John Briggs
Adam Goodison
Hilary Stonefrost
Lloyd Tamlyn
Ben Valentin
David Allison

Daniel Bayfield
Tom Smith
Richard Fisher
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Hannah Thornley
William Willson
Georgina Peters
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