Nottingham Law School

Centre for Business and Insolvency Law

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Welcome to the Spring 2016 edition of the Bulletin. This issue covers a number of cross-border cases, touching on both the UNCITRAL Model Law and the EC Insolvency Regulation. Once again, the extra-territorial effect of section 263 of the Insolvency Act 1986 has been under scrutiny, only this time the *MF Global* decision has not been followed.

The *SeaFrance* case throws up an interesting point for competition lawyers and highlights the tension between doing a deal on insolvency that will preserve jobs and eliminating competition; in this case, the Supreme Court had to consider whether an "enterprise" or the company's "bare assets" had been acquired from the liquidator. The use of schemes of arrangement by companies with a tenuous link to England and Wales continues; although not an insolvency case, the *Jelf* case has been included for its discussion of what is an "arrangement".

There are several cases on liquidation which provide a useful refresher of the law on striking out winding up petitions. The *Power* and *Gagen Sharma* cases provide some interesting insights into the sentencing rules on contempt and the use of the illegality defence respectively.

For the first time the Bulletin has been written entirely by students studying on the LL.M programme. I would like to thank them very much for all their work and to congratulate them on their contributions. You can read their profiles at the back of the Bulletin.

It only remains for me to wish you all the very best for a lovely holiday over the Spring Break.

Paula

Paula Moffatt

In this Bulletin…

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CROSS-BORDER

Nordic Trustee ASA, OSX 3 Leasing BV v OGX Petroléo E Gás S A (EM Recuperação Judicial) and others [2016] EWHC 25 (Ch)

Executive summary

Where a party's only aim in seeking recognition of a reorganisation plan as a foreign main proceeding under the UNCITRAL Model Law was to obtain a stay of proceedings in order to prevent arbitration proceedings from taking place, that aim was an abuse of the process for recognition.

Facts

OSX 3 Leasing B.V. ("Leasing") was a company incorporated in the Netherlands. It had partly financed the construction of a floating production, storage and offloading vessel with a US$500m secured bond issue. The trustee for the bond issue was a Norwegian company, "Nordic".

In March 2012, Leasing entered into a charter agreement for the vessel with a Brazilian company, OGX Petroléo E Gás SA ("OGX") and shortly afterwards assigned its rights under the charter to Nordic. In October 2013, OGX experienced financial difficulties and its parent applied for a judicial reorganisation under Brazilian Bankruptcy Law. While this was happening, OGX and Leasing entered into negotiations to amend the terms of the charter and reduce the daily charter rates payable under the original charter. The parties subsequently entered into a new charter agreement.

The reorganisation plan (the "Plan") was approved both by OGX's creditors and the Rio de Janeiro Bankruptcy Court (the "Bankruptcy Court") in June 2014. Because the charter negotiations took place in parallel to the judicial reorganisation, the new charter agreement was not subject to the restructuring arrangements under the Plan.

The new charter was assigned by Leasing to Nordic. OGX acknowledged receipt of the relevant notice. The new charter expressly provided that all disputes under the charter should be subject to arbitration in the London Court of International Arbitration ("LCIA").

OGX subsequently failed to pay Nordic amounts due under the assignment and obtained an injunction from the Bankruptcy Court which unilaterally reduced the daily charter rates payable under the amended charter. Nordic and Leasing successfully applied to the Rio de Janeiro Court of Appeals to have the injunction declared null and void on the basis that the Bankruptcy Court had no jurisdiction to make the order as the new charter agreement fell outside the scope of the Plan. The matter was sent to the Brazilian lower court for determination and Nordic and Leasing applied to the LCIA to require OGX to discontinue the Brazilian proceedings.

The directors of OGX applied to the English court for an order for the Plan to be recognised in England as a foreign main proceeding under Article 2(i) of the UNCITRAL Model Law on Cross-Border Insolvency (the "Model Law"), in order to take advantage of the automatic stay of proceedings. OGX contended that its board of directors qualified as a foreign representative of OGX.

At the recognition hearing, the judge made an order for the Plan to be recognised as foreign main proceedings and for the arbitration to be stayed. At the same time, he gave permission for the counterparty to the arbitration to apply to have the stay lifted. Nordic and Leasing immediately did so contending that the judge had been misled or, that the order had been obtained by a material non-disclosure of the fact that the Plan for which recognition was sought did not apply to the claims in the arbitration under the new charter agreement.

Following a determination in Brazil that the Bankruptcy Court had no jurisdiction to order a reduction in the amounts payable under the new charter, the parties agreed to draft a consent order under which the automatic stay was to be lifted to permit the arbitration to continue.

Decision

The judge made the order lifting the automatic stay to enable the arbitration to continue, but delivered a judgment that addressed the wider importance of the issues for applications of this type. He expressed reservations about making an order that left the recognition of the Plan in place for no obvious purpose and in circumstances where it should probably not have been granted in the first place.

Comment

It was clear that in this case, OGX had been somewhat economical with the truth. The new charter was never subject to the terms of the Plan, but this had never been made explicit at the original recognition hearing. In that hearing, the judge had specifically asked counsel for OGX as to whether there were any matters to which his attention should be drawn which might lead to him not making the application sought. The rejection of the stay of proceedings was, therefore, more than a simple rejection.

Snowden J was particularly sensitive to the possibility of the abuse of the process for recognition of foreign proceedings. The argument brought up by OGX that it had provided sufficient evidence to comply with Articles 15 and 17 of the Model Law could be seen to be technically correct; OGX contended that its evidence did not address matters that were potentially relevant to the modification of the automatic stay as they were not necessary for the purpose of recognising foreign proceedings. The solicitor for OGX apologised to the court in the event that this was a mistaken approach.

The judge noted that where a foreign proceeding is recognised as a foreign main proceeding under Article 17 of the Model Law, the Article 20 stay operates automatically. Its operation is, however, limited so that any stay would only apply to the extent that a stay would apply had a winding up order had been made in relation to the company in England (Article 20(2)). The purpose of the automatic stay under section 130(2) Insolvency Act 1986 was to preserve the *pari passu* ranking of creditors and to prevent individual unsecured creditors from obtaining an illegitimate advantage over other unsecured creditors in collective proceedings. As the Model Law also applied only to collective proceedings, the judge considered that the stay could not work to prevent parties who were not subject to collective proceedings from pursuing their claims.

Here, the only reason for seeking recognition for the Plan was deliberately to frustrate the arbitration proceedings which dealt with claims not subject to the Plan. The judge held that this was inconsistent with the purpose of the Model Law and an abuse of the process for recognition of foreign proceedings. He considered that the disclosure made by OGX at the recognition hearing was "wholly inadequate" and that, had the judge at that hearing been aware of the omitted facts he would have been justified in refusing to grant recognition in the first place. He concluded his judgment by emphasising the importance of making foreign representative and their advisers aware that full disclosure must be made in recognition proceedings.

Miriam Carra
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Nike European Operations Netherlands/Sportland Oy [2015] EUECJ C-310/14 (15 October 2015)

Executive Summary

The Court of Justice of the EU ("ECJ") gave a preliminary ruling on the interpretation of Article 13 of Council Regulation (EC) 1346/2000 on Insolvency Proceedings (the "Insolvency Regulation").

Facts

A Dutch company, Nike European Operations Netherlands BV ("Nike") supplied goods to the Finnish retailer Sportland Oy ("Sportland") under a franchise contract governed by Dutch law. Sportland paid for the goods by ten instalments, amounting to a total of EUR 195,108. The final instalment was made shortly before the insolvency proceedings were opened.

In accordance with Paragraph 10 of the Finnish Law on Recovery of Assets, Sportland brought a claim before the Finnish court to get the payments annulled and receive restitution of the payments from Nike.

Nike sought dismissal of the claim on the grounds that Dutch law would be applicable under Article 13 of the Insolvency Regulation. Hence, the payments needed to be challenged under Article 47 of the Dutch Law on Insolvency and on that basis, the payments could not be challenged.

The Finnish court rejected Nike's position and the Helsinki Court of Appeal referred the following questions to the ECJ for a preliminary ruling on Article 13 of the Insolvency Regulation:

First, should Article 13 be interpreted to mean that its application is subject to the condition that the act at issue cannot be challenged on the basis of the law governing the act (*lex causae*), after taking account of all the circumstances of the case?

Second, in the event that the defendant relies on a provision of the *lex causae* under which the act can be challenged only in the circumstances provided for in that provision, which party is required to plead that those circumstances do not exist and to bear the burden of proof in that regard?

Third, whether the expression "does not allow any means of challenging that act…" applies, in addition to the insolvency rules of the *lex causae,* to the general provisions and principles of that law, taken as a whole?

Fourth, whether the defendant must show that the *lex causae*, taken as a whole, does not allow for that act to be challenged and whether a national court before which such an action is brought and where it considers that the defendant has adduced sufficient evidence, can consider that it is for the applicant to furnish evidence that a provision or principle of the *lex causae* exists on the basis of which that act may be challenged?

Decision

Question one: the ECJ held that when applying Article 13, the act in question cannot be challenged on the basis of the law governing the act, having taken into account all the circumstances of the case (the ECJ noting that the Finnish version of the Insolvency Regulation differed slightly from other translations).

Question two: it is up to the person who has benefited from an act detrimental to all the creditors to plead that those circumstances do not exist and to bear the burden of proof in that regard, so in this case, the defendant should bear the burden of proof.

Question three: the words "does not allow any means of challenging that act…" apply both to the insolvency rules of the *lex causae*, as well as the *lex causae*, taken as a whole.

Question four: consistent with the answer to question three, the ECJ held that it is for the defendant to prove that the act in issue cannot be challenged by 'any means'; in other words, the defendant must show that the *lex causae*, taken as a whole, does not enable that act to be challenged. If, however, the national court considers that the defendant has proven, in accordance with the rules generally applicable under its national procedural rules, that the act at issue cannot be challenged on the basis of the *lex causae*, the court may rule that it is for the applicant to establish the existence of a provision or principle of the *lex causae* on the basis of which that act can be challenged.

Comment

In this case, Nike wanted to demonstrate under Article 13 that the law of a Member State (here Dutch law) applied instead of the law of the Member State opening proceedings (Finnish law) as Dutch law would have enabled it to keep the payments it had received from Sportland. Although the ruling by the ECJ makes clear where the burden of proof lies in cross-border situations involving a transaction avoidance claim, it nonetheless contains some incongruities.

Article 13 aims to provide protection for the beneficiary of the detrimental act; as the ECJ explained, its purpose is to protect the legitimate expectations of a party who has benefited from a transaction governed by one law that it will continue to be governed by that law even after the proceedings have been opened. Finnish law (here, the *lex concursus*) cannot challenge the detrimental act if: (i) the act is subject to the *lex causae* (here, Dutch law), which differs from the *lex concursus*; and (ii) the issue cannot, in the relevant case, be challenged under the *lex causae*. If there is a possibility for the detrimental act to be challenged under the *lex causae*, the *lex concursus* will be applicable. Article 13 thus technically provides for cumulative application of the *lex causae* and the *lex concursus*, and therefore in theory provides protection in multiple ways. In case either judicial system makes it impossible to challenge the detrimental act, the detrimental act cannot be challenged.

In this case, the answers given by the ECJ lead to an unsatisfactory outcome. Since Dutch insolvency law states that it is up to the insolvency practitioner to provide proof for a transaction avoidance claim, the ruling leads to a reversal of the burden of proof. The defendant will need to provide proof of a negative fact. In this case, the ruling therefore effectively hollows out the protection Article 13 gives.

Tjalling Bosker

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Société Coopérative de Production SeaFrance SA ("SCOP") (Respondent) v The Competition and Markets Authority and another (Appellants) [2015] UKSC 75

Executive summary

The acquisition of the assets of an insolvent company constituted a "relevant merger situation" for the purposes of the Enterprise Act 2002 as it was necessary to look at the economic substance of the transaction rather than its form to determine whether an "enterprise" or the company's "bare assets" had been acquired.

Facts

SeaFrance SA was a subsidiary of the French state rail group SNCF which operated a ferry service between Dover and Calais until its liquidation in November 2011. Under French law, the liquidator was required to agree a job-saving plan with SeaFrance. One of the terms of the plan was that SNCF would pay up to €25,000 for each former employee re-employed on the SeaFrance vessels in operations similar to those carried on before the liquidation and the ships were placed in "hot lay-up".

The liquidator invited sealed bids for the SeaFrance assets and Groupe Eurotunnel SE ("GET") proposed to acquire them. An important part of GET's bid was that it would work with SCOP, which would provide crews and shore staff for the ferry service. The liquidator recommended the GET bid as it would safeguard the jobs of a substantial number of the workforce and, in July 2012 the acquisition was completed. By August 2012, ferry services had started to operate.

In October 2012, the Office of Fair Trading referred the acquisition of the SeaFrance assets to the Competition Commission (the "Commission"). The Commission found that a "relevant merger situation" existed which could substantially reduce competition in the cross-Channel ferry services market.

GET and SCOP challenged the decision and the case was remitted to the Competition and Market Authority ("CMA") which held that it was a "relevant merger situation". The parties appealed to the Competition Appeal Tribunal ("CAT") and ultimately the Court of Appeal, where the decision was reversed. The CMA appealed to the Supreme Court.

Decision

The Supreme Court unanimously allowed the appeal, holding that the economic substance of a transaction was more important than its legal form. Distinguishing between "bare assets" and assets amounting to an "enterprise" depended on first, defining what, over-and-above "bare assets" the acquiring entity obtained. To be an "enterprise" the acquirer must get more than it would have done by going to market and buying factors of production and the extra must be attributable to the fact that the assets were previously used in combination in the activities of the target enterprise. The shorter the interval between a target enterprise's cessation of trading and the acquisition of control of its assets, the more likely it is regarded as constituting an enterprise. It is not, however, a decisive criterion (para 39). In this case, the whole was greater than the sum of its parts, therefore GET acquired an enterprise.

Comment

On 31 July 2015, SCOP went into liquidation after the Supreme Court allowed the appeal. This case illustrates the tension that exists in trying to preserve jobs whilst at the same time, trying to maintain a competitive market. The deal between the SeaFrance liquidator and GET was highly political, the French State being shareholder of both enterprises. The job saving plan enabled the activities' economic continuity to be performed both before and after the acquisition of assets. The Supreme Court emphasised that a target enterprise whose activities are no longer actively carried on are to be widely assessed according to the period of time elapsed since the business was last trading and to the extent and cost of the actions that would be required in order to reactivate the business as trading entity. Nevertheless, the French Competition Authority cleared the deal because it was an economic and political decision taken by the State, thereby it was held to be a mere acquisition of bare assets of a defunct enterprise.

Conversely, the Supreme Court held that the CMA correctly assessed the acquisition of SeaFrance's assets as a relevant merger situation of two enterprises (Section 23(2)(a) Enterprise Act 2002) under the definition of enterprise provided in section 129(1) Enterprise Act 2002. In order to reach this conclusion, the Supreme Court focused on the acquired assets regarded as constituting an enterprise, which must give to their owner more than it might have acquired by going into the market and buying factors of production, and the extra must be attributable to the fact that the assets were previously employed in combination in the activities of the target enterprise (para 39).

This case is extremely important because it defines the requirements to be taken into account when assessing whether an enterprise acquires another one's assets or the bare assets of a defunct enterprise and whether an economic continuity exists between the actual assets and the previous business. When a merger situation exists, a purely legal analysis is no longer satisfactory when dealing with an acquisition of assets from a liquidated enterprise. If the embers of an enterprise are passed to the control of the acquiring enterprise, then the transaction is likely to be reviewed by the CMA (para 42).

This judgment emphasised the caution which is required before an appellate court should consider overturning the economic judgments of expert tribunals such as the CMA and the CAT (see *British Telecommunications Plc v Telefónica and others [2014] UKSC 42; [2014] Bus LR 765; [2014] 4 All ER 907 at paras 46, 51*). This judgment may help to put an end to the uncertainty and delay that are liable to unsettle markets and damage the prospects of the business involved.

Victor Laplace-Builhé

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The Official Receiver v Norriss [2015] EWHC 2697 (Ch)

Executive summary

Section 236(3) of the Insolvency Act 1986 (the "1986 Act") was held to have extra-territorial effect, distinguishing the decision in *MF Global (UK) Ltd* [2015] EWHC 2319 (Ch).

Facts

Omni Trustees Ltd (the "Company") was the trustee of an Occupational Pension Scheme. In July 2014, the Company transferred £3.7m to a Hong Kong based scheme "SSAS". Mr Norriss was the principal trustee of SSAS.

In May 2015, the Secretary of State presented a petition to wind up the Company on public interest grounds. The Official Receiver was appointed as provisional liquidator and later became liquidator when the winding up order was made.

In a bid to find out what had happened to the £3.7m transferred by the Company to SSAS, the Official Receiver sought an order that Mr Norriss provide a witness statement and supporting documents relating to the transferred sum. As Mr Norriss was a person able to give information about the business, dealings and affairs of the Company, the application was made under section 236 of the 1986 Act. The Official Receiver did not seek to examine Mr Norriss in either England or Hong Kong.

Mr Norriss contended that the English court did not have jurisdiction to make the order under section 236 and, even if it did, the order went beyond the scope of what was permissible under that section.

Decision

The High Court held that section 236(3) of the 1986 Act had extra-territorial effect and an order could therefore be made for the documents requested to be produced. The order extended only to the production of information relating to the transactions from the Company to the SSAS Scheme.

Comment

In deciding that section 236(3) had extra-territorial effect, the judge expressly differed from the decision in *MF Global* where the extra-territorial effect of section 236(3) was denied. After careful analysis, he reached this conclusion on the basis of two substantial arguments brought forward by counsel for the Official Receiver.

Firstly, the judge considered the argument that the court in *MF Global* had not distinguished between requiring an individual resident abroad to be examined and requiring him to produce documents. The judge in *MF Global* (then David Richards J now LJ) had relied heavily on the ruling of *Re Tucker* [1990] Ch 148, which had concerned section 25 of the Bankruptcy Act 1914, the predecessor of the current section 236. In the present case, the judge concluded that section 236 was structured differently from its equivalent section in the Bankruptcy Act 1914 in that it separated the powers to order examination (section 236(2)) and to produce documents (section 236(3)). In contrast, the old legislation had provided a power of submission that was merely ancillary to, and dependent upon, the power to order examination. Since the old provision provided for both individual examination and for the production of documents without distinguishing between the two, the judge considered that *Re Tucker* should not have been an appropriate basis for the decision in *MF Global*. Consequently, he saw good reason not to follow the decision made in *MF Global*.

Secondly, the judge considered the case of *Re Mid East Trading Ltd* [1998] 1 BCLC 240 (which was not cited in *MF Global*), to be the authority that should be followed. *Mid East Trading* had also concerned the question as to whether the production of documents situated outside the UK could be ordered, albeit with the difference that the respondent had been physically present in the jurisdiction. The court had found that section 236(3) was to be interpreted as having extra-territorial effect, on the basis that applying section 236(3) did not involve an exercise in sovereignty but required merely an assertion of sovereignty which the legislature had intended the courts to make. The judge was therefore satisfied that the absence of Mr Norriss in the UK, which was the distinguishing factor with *Mid East Trading*, was irrelevant for the extra-territoriality of section 236(3).

The debate whether section 236 has extra-territorial effect has been a lingering one, but this case seems to settle it with regard to section 236(3), at least until it is heard in a higher court. The judge carefully and comprehensively explained why he did not agree with the decision made in *MF Global* and his reasoning sounds quite logical for the most part. Perhaps some questions can be asked regarding his "satisfaction" (para 14) that the argument of counsel for the Official Receiver is correct as to whether section 236 is structured differently from section 25 under the old legislation. If one closely reads sections 236(2) and (3), one may still argue the latter is ancillary to the former, seeing as it reads "any such person as is mentioned in subsection (2)(a) to (c)", which explicitly relates to persons the court "may summon to appear before it". In this light, some further explanation by the judge would have been welcome. However, as noted by Lawford and Merritt, whereas under the 1914 Bankruptcy Act it was expressly stated that the Bankruptcy Rules could not extend the jurisdiction of the court, the opposite is true under the 1986 Act.[1] This could enable the extra-territorial effect of section 236(3) even if it is similar to section 25.

On another note, the judge seems to have easily overlooked the fact that the court in *MF Global* had based its decision not only on the authority of *Re Tucker*, but also expressly on "the presence of what is now section 237(3)" (para 32 of that judgment), which might

[1] Mark Lawford and Lindsay Merritt, 'Section 236, extra-territorial effect and a way forward following Re MF Global UK Ltd and Re Omni Trustees Ltd', European Restructuring Watch 10 February 2016, available at http://www.lexology.com/library/detail.aspx?g=34729c7e-6c43-4022-83b9-bfde43095431, last accessed 04-03-2016; cf Rule 12A.20 of the Insolvency Rules 1986.

imply a relation or hierarchy between sections 236 and 237 that would justify a lack of extra-territoriality of the former.

Nevertheless, in the light of judgments such as *Mid East Trading* and also *Re Casterbridge Properties Ltd* [2002] BCC 453, where the partial extra-territoriality of section 236(2) was asserted in the way that examinations could always be ordered to take place in the jurisdiction of presence, this judgment can be welcomed as both clarifying and answering the question of extra-territoriality of section 236 further in the affirmative. It will be interesting to see whether in the near future section 236(2) too will be deemed to have (full) extra-territorial effect.

Matthijs van Schadewijk
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SCHEMES OF ARRANGEMENT

***Re Public Joint-Stock Company Commercial Bank "Privatbank" and in the Matter of the Companies Act 2006* [2015] EWHC 3299 (Ch)**

Executive summary

A Ukranian bank had a sufficient connection with England for the court to sanction a scheme of arrangement since it had a representative office in England and all the relevant finance documents were governed by English law.

Facts

Privatbank was one of the largest banks in the Ukraine. It also operated in Cyprus and Latvia and carried out administrative functions in the UK and China. Due to a political crisis and the strong depreciation of the Ukrainian currency, the bank faced financial difficulties in 2015.

To avoid being put into temporary administration in the Ukraine, Privatbank proposed to restructure its loan notes, which were heavily subordinated and unlikely to be repaid in administration. The notes had an aggregate nominal value of US$ 220 million.

Privatbank applied to the court to sanction a scheme of arrangement under the Companies Act 2006 for the purpose of restructuring the notes. The existing notes were to be cancelled and new notes issued on broadly the same terms with a deferred maturity date. As the notes were held in global note form, the noteholders were not creditors of the bank, so the bank entered into a deed poll agreeing to be directly liable to the noteholders.

In deciding whether or not to sanction the scheme, the court had to consider whether Privatbank had sufficient connection with England to establish its jurisdiction.

Decision

The court was satisfied that Privatbank had a sufficient connection with England on the basis that the loan note agreements and trust deeds were expressly stated to be governed by English law. In addition, they gave jurisdiction to the English courts or submitted disputes to arbitration with a London seat. Additionally, the bank's representative office and assets were in England so that, in the event of insolvency, Privatbank would be likely to be wound up in England, albeit in practice as an ancillary liquidation to an insolvency process in Ukraine.

Jente Dengler

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Re Codere Finance (UK) Ltd [2015] EWHC 3778 (Ch)

Facts

Codere SA was incorporated in Spain and was the ultimate parent of a group specialising in gaming activities in Latin America, Italy and Spain. It financed its activities through the issue of loan notes by its subsidiary, Codere Finance (Luxembourg) SA. The notes were governed by New York Law and guaranteed by various group companies and were also subject to an English law inter-creditor agreement.

In August 2015, the group found itself in financial difficulties with almost EUR 1.5 billion worth of debt. Codere SA proposed to restructure the debt using a scheme of arrangement under Part 26 of the Companies Act 2006 (the "2006 Act"). Under the scheme, the existing notes in issue would be cancelled and exchanged for shares and new notes. In December 2015, creditors representing 98.78% of the total indebtedness, voted in favour of the scheme.

In order to establish a connection with England so that the English court could sanction the proposed scheme, Codere SA acquired an English subsidiary, Codere Finance (UK) Ltd, and made it a co-obligor as regards the financial obligations under the loan notes. Soon afterwards Codere Finance (UK) Ltd applied for an order sanctioning the scheme under Part 26 of the 2006 Act.

Decision

Although the judge noted that the facts of the case illustrated "quite an extreme form of forum shopping" he held that there was a sufficient connection with England for the court to sanction the scheme. The connection was demonstrated by the existence of the English law inter-creditor agreement, evidence that a significant percentage of the noteholders were domiciled in England and the fact that the trustees performed their duties from offices in London. In view of the creditors' support and the losses that they would suffer if the scheme did not proceed, the court had no good reason to decline the application.

Comment

In *Drax Holdings* [2004] 1 WLR 1049, Collins J stated that the English courts should not sanction a scheme applied for by a foreign debtor unless a "sufficient connection" with England could be shown. Subsequent case law has demonstrated that the courts have shown a degree of leniency as regards the use of schemes by companies incorporated outside England and Wales. The courts have allowed a "sufficient connection" to be established solely because the contractual rights of the scheme creditors were governed by English law or because there was a jurisdiction clause in favour of the English courts (*Re Rodenstock GmbH* [2011] EWHC 1104 (Ch)), factors which proved relevant in the present case.

A few months prior to the *Privatbank* case, Snowden J pleaded in the *Van Gansewinkel Groep BV* [2015] EWHC 2151 (Ch) judgment for greater scrutiny to be given to foreign debtors seeking to benefit from using English law schemes of arrangement. It did not, however, prevent him from further expanding the forum shopping opportunities as *in casu* the presence of only one creditor in England sufficed to assert jurisdiction. In particular, he emphasised that the support of an overwhelming majority of the scheme creditors does not permit the courts to act as a rubber stamp.

In the two cases in issue the role of creditor support undeniably still has a considerable role to play. As the position of creditors significantly improves in cases where a restructuring takes place under the auspices of an English scheme, the relevance of the "sufficient connection" condition seems to shift to the background. Moreover, in the *Codere* case, Newey J was right to state that when a debtor aims to achieve the best possible outcome for its creditors, we should not speak of forum shopping nor deny a debtor the sanction of a scheme due to a lack of a "sufficient connection". Conclusively, it is a comforting thought that English courts hold on to their tendency of dealing constructively with scheme applications by foreign debtors.

Jente Dengler

In the matter of the Companies Act 2006 and in the matter of Jelf Group PLC [2015] EWHC 3857 (Ch)

Executive summary

Even if the company's only function is to amend the register of members of the company, which was a purely administrative function, such a function sufficed to fall within the definition of 'arrangement' as it has come to be interpreted for the purpose of the Companies Act 2006 (the "2006 Act").

Facts

Jelf Group plc ('Jelf') was a UK insurance broker which provided its services to UK SMEs. MMCAL sought to acquire Jelf using a scheme of arrangement under Part 26 of the 2006 Act (the "Scheme"). At the Scheme meeting ordered by court, the required consenting majority had been obtained by a vote of well over ninety percent.

At the Scheme sanction hearing, the court considered its jurisdiction to sanction the Scheme by assessing whether the proposal fell within the scope of Part 26 of the 2006 Act as an "arrangement … between a company and … its members".

Decision

The Companies Court sanctioned the Scheme as it concluded that, in all the circumstances and notwithstanding that it might be thought to be stretching the concept of an "arrangement … between a company and … its members" to apply it to a case such as the present, the existence of authority and reliance on that authority for decades meant that the facts of the present case fell within the definition of 'arrangement', as it had come to be interpreted for the purposes of the 2006 Act.

Comment

Although this case is not a case involving an insolvent company, it is interesting for its analysis of what constitutes an "arrangement" and re-affirms the flexibility of the process (most often seen in insolvency cases in the context of establishing the jurisdiction of the English court).

As a starting point, it is essential to note that, whilst schemes have a statutory basis in Part 26 of the 2006 Act, the provisions themselves are particularly brief. Section 895 of the 2006 Act requires that the scheme proposal constitutes an "arrangement" (or "compromise") "between" the company and its creditors or members. However, the legislation contains no details regarding the meaning of these terms. Instead, it has been up to the courts to determine its ambit, jurisdiction and procedural rules, and they have been very flexible in doing so. From the basis of its ordinary commercial meaning, the courts have generally sought to construe the concept of "arrangement" as widely as possible (*Re Savoy Hotel* [1981] Ch.351). It is, however, required that the arrangement involves some form of "give and take" and the company must be party to the arrangement. In the judgment concerned, due regard is given to both limitations.

Of particular significance is the citation from Lowe ACJ in *Re International Harvester Co. of Australia Proprietary Limited* [1953] VLR 669, which is generally referred to when the jurisdiction of Pt 26 CA 2006 is concerned (see para 8). It seems to me that, in defining the ambit of schemes, focus has shifted to an *argumentum a contrario* approach in that "almost any arrangement otherwise legal which touches or concerns the rights and obligations of the company or its members or creditors" would be permissible unless the arrangement concerns *ultra vires* acts or if the company's intention is to evade a statutory procedure or restriction.

Regarding the concept of an "arrangement" as involving "give and take", Mann J appears to struggle with the legacy of the nature of schemes as they have come to be interpreted for the purpose of the 2006 Act. In particular, the decreasing role of the company provided a hurdle for the judge as he analysed the function of the company in the scheme document and "exposed" the arrangement to be not far from a "contractual sale of shares to a purchaser in which the company has what seems to be purely administrative functions" (see para 4). What is it that made this arrangement more than just that? The answer is case law.

In the course of time, the term "arrangement" has gradually evolved from a more restrictive interpretation (*Re General Motor Cab Co Ltd* [1913] 1 Ch 377: synonymous with "compromise") to an approach in which it is construed more broadly. The courts have sanctioned schemes in which the rights of creditors and/or members are varied as against the company, as well as between creditors and members. Likewise, the principle of "give and take" requires some form of accommodation on each side and consideration has to be given for the relinquishment of rights (*Re NFU Development Trust* [1972]) that may take place between the members and a party that is not the company. Consequently, the role of the company will remain only marginal. Members' schemes such as that in *In re Savoy Hotel Ltd* and *Re T&N Limited (No. 3)* [2006] EWHC 1447 (Ch) show that, even if the company's (Jelf's) only function is to register the transfer of shares and thereby terminate the existing members' status as members, this is considered "sufficient" to make the arrangement one between the company and its members.

This case provides a nice illustration of the merits as well as the pitfalls of the UK scheme of arrangement, in particular as it pertains to the way in which courts consistently and increasingly construe terms very broadly, therewith maximizing jurisdiction. The court provides additional clarity of the "between the company and its members/creditors" requirement, recognising that the role of the company may be reduced to a minimal, *de facto* administrative function, and still suffice to fall within section 895. I am of the opinion that this judgment is both convincing and comprehensible. It is clear that the courts will continue their liberal approach in defining the ambit of schemes, stretching the concept of an "arrangement between the company and its members".

Selina Backus

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LIQUIDATION

Coilcolor Limited v Camtrex Limited [2015] EWHC 3202 (Ch)

Executive summary

The Court granted an injunction restraining the presentation of a petition to wind up the Company in circumstances where the petition was requested for the purpose of putting pressure on the Company to pay its debts when there was a *bona fide* dispute as to whether the money was owed.

Facts

Coilcolor Limited (the "Company") had purchased steel coils from Camtrex Limited ("Camtrex") intermittently since 2004. In April 2015, the Company identified several defective steel coils for which it claimed compensation and suspended the payment of the relevant invoices. After various attempts to solve the issue amicably, Camtrex served the Company a statutory demand for £344,304.64. The Company declared itself available to pay part of the amount but disputed the balance of £100,633.12 and, in September 2015, filed an application for an injunction restraining the presentation of a winding up petition. In particular, the Company claimed to be entitled to set-off or cross-claim on the basis of defective supplied goods.

Camtrex contended that the cross-claim was formulated for the mere purpose of delaying the payment of the invoices and, further that Company had not fulfilled the necessary contractual requirements relating to the supply of defective goods. The Company rejected this argument.

The case also raised the question as to whether the Companies Court represented the correct forum for the adjudication of the disputed contractual matters whilst it dealt with the application to restrain the presentation of a winding-up petition.

Decision

The Company's application for an injunction restraining the presentation of a winding up petition was awarded. Hildyard J noted that Camtrex's true objective was not that of making use of the winding up petition as a class remedy against an insolvent debtor, but rather to put pressure on a solvent company for the payment of disputed debts.

Although the cross-claim appeared to be contrived, it raised issues which were different from the inability to pay and which were unsuitable for adjudication by the Companies Court. The judge therefore concluded that the Company deserved to be given the benefit of doubt on the substantiality of the cross-claim and that the relevant issues, concerning the application, interpretation and variation of contractual terms, should be dealt with in an ordinary process without any of the parties being subject to the threat of winding up. To do otherwise would result in an abuse of process.

Comment

The Coilcolor case allowed the Companies Court to confirm the well-established case law on the conditions upon which an injunction to restrain the presentation of a winding up petition will be granted by the Court, for the purpose of preventing an abuse of process.

In particular, Hildyard J recalled that, on the basis of *Mann v Goldstein* [1968] 1 WLR 1091, *Bryanstone Finance Ltd. V De Vries (No. 2)* [1976] Ch. 63 and *Charles Forte Investments Ltd. V Amanda* [1964] Ch. 240, an application for an injunction of such nature may be successful only if the winding up petition would be an abuse of process and/or would be bound to fail. Those conditions are deemed to be fulfilled if the applicant can provide evidence of the fact that the debt for which a winding up petition may be presented is *bona fide* disputed on substantial grounds and/or that the applicant is entitled to cross-claim for amounts exceeding the debt, on genuine and substantial basis. The *ratio* for such rule is clear: there is no interest in granting the petitioner a winding up petition, if the cross-claim is established and would entitle the liquidator to claim back the relevant assets or amounts.

The Court also reiterated the point that the presentation of a winding up petition is meant to be a class remedy, which can be used by anyone who can stand as a creditor, in favour of the entire class, whether or not this is appreciated by the other creditors. Lack of such standing leads to the dismissal of the petition. It was also thereby restated that the use of such a tool as a means of putting pressure for the payment of *bona fide* disputed debts, and avoid an ordinary proceeding, represents an abuse of process, as better illustrated in *Re a Company* (No 0012209 of 1991) [1992] BCLC 865.

However, in this regard, Hildyard J further underlined that it is not enough for the applicant to state, although in good faith, that he is entitled to cross-claim; the debtor shall provide evidences sufficient to persuade the Court that the defence is well grounded and susceptible of succeeding. Reference was made to *Re a Company* (No 6685 of 1996) [1997] BCC 830, where it was acknowledged that the Court shall not be bound to grant the injunction if the evidence supporting the cross-claim is not credible.

Hildyard J also took the opportunity to clarify that the status of solvent or insolvent company is not conclusive for the purpose of granting or restraining the grant of a winding up petition. Such a statement leads to two significant considerations: (i) the debtor, although in financial distress, cannot be wound up if the unpaid debt is challenged or disputable; that is to say that, the lack of the chance, for any reason, to dispute a debt which is substantially disputable does not entitle the creditor to request the liquidation of the debtor, if the latter is still entitled to challenge the debt; and (ii) the good financial standing of the debtor does not prevent the winding up of the same, if it fails to pay any undisputable debt. As acknowledged in *Cornhill Insurance Plc v Improvement Services Ltd* [1986] 1 WLR 114, the solvency of large companies cannot be used by them as a defence, i.e., as a shield against petitions, allowing them to delay payments limitlessly.

In light of the above, it is possible to conclude that the Coilcolor case confirms that the Court may grant an injunction to restrain a winding up petition each time the debtor, regardless from being solvent or insolvent, is entitled to cross-claim with prospect of success. In particular, the Companies Court should do so to prevent the use of such *forum* as an abusive alternative to the RSC Ord 14 procedure.

In the present case, the Company was experiencing some financial difficulties but no evidence was provided to show that it was insolvent; in addition, it disputed the debt claimed by Camtrex. Thus, the analysis focused on the genuineness or substantiality of the cross-claim formulated by the Company. In this regard, the judge stated that the defence formulated by the Company and based on the alleged defects appeared to be contrived; moreover, it was noted that if Camtrex's defence was grounded, as to the integration of its standard terms and conditions into the agreement, those terms would, at a first glance, prevent the Company from bringing forward any cross-claim. The judge found that Camtrex had succeeded in providing strong evidence that its terms and conditions were incorporated.

This evidence was not sufficient to defeat the Company's defence, since the Company was also challenging the interpretation of the terms and conditions or, alternatively, whether they had been varied or waved. Therefore, the Court acknowledged that in order to assess the soundness of the Debtor's defence it was necessary to engage in factual inquiries concerning contractual interpretation and statutory control which exceeded the scope of action of the Companies Court. Consequently, the Court decided to give the Company the benefit of the doubt, making the injunction and referring the solution of the abovementioned issues to the Chancery Division. Such conclusions were achieved on the basis of the fact that, in line with the case law, the Companies Court does not deem itself to be the appropriate *forum* for the adjudication of similar issues, and wishes to discourage the use of winding up petition as an abusive alternative to the ordinary proceeding.

It is worth it underlining that in the illustration of the legal principle supporting the decision, the judge appeared to slightly diverge from the case law, widening the requirements upon which a restraining injunction may be adopted. In particular, having stated that only if the debtor's defence is genuine and substantial and presents solid prospect of success, the injunction may be made, he granted the application observing that the defence appears to be equivocal, contrived and, if analysed in depth, likely to lack sufficient substance (paras. 43, 47, 65). As already clarified, the injunction is granted since the debtor's defence is based on a number of factual issue which require a complex analysis to be carried out in a different *forum*, however, such elements are deemed sufficient to give the debtor the benefit of the doubt as to the genuineness of the cross-claim, and make the injunction. Should we thus infer that the beam for the grant of an injunction restraining a winding up petition has been lowered, making it possible to obtain it although the cross-claim is not *prima-facie* credible or substantial? The future case law will bear the burden to answer this question.

Priscilla Conti
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Free of Tie Leases Ltd. v Raymond Court Hampton [2015] EWHC 3974 (Ch)

Executive Summary

A winding-up petition shall be struck out where it was disputed on substantial grounds and the petitioner had omitted to follow the correct procedures in relation to presenting and pursuing the winding up petition.

Facts

Free of Tie Leases Limited (the "Company") applied the Court to strike out a winding-up petition presented against it by the Petitioner and to restrain the advertisement of the winding up petition.

The Petitioner had served a statutory demand on the Company in October 2015 and subsequently presented a winding up petition. The Petitioner claimed costs he had incurred under a lease agreement which he had been induced to enter into as a result of alleged fraudulent misrepresentation by the Company. The Petitioner notified the Company's bank of the winding up petition.

The Company claimed that the petition should be struck out as an abuse of process for three reasons. First, because the Petitioner had publicised the winding up petition despite knowing that that Company had applied to court to prevent him from doing so; second because the money demanded was not presently due and payable; and third because the alleged debt was disputed on substantial grounds.

Decision

The court granted the Company's application and struck out the winding up petition. The judge held that the Petitioner did not have the necessary standing to present a winding up petition and this alone was sufficient for the petition to be struck out. Even if the petition had been properly served (which the judge was not sure was the case) the Petitioner had wholly disregarded the rules relating to the advertisement of a winding up petition which require seven clear days to elapse between the presentation of the petition and its advertisement. This meant that the petition could also be struck out as an abuse of process.

Comment

The case at hand offered the Companies Court a new chance to rule on the conditions upon which a winding up petition may be struck out by the Court.

With specific reference to the main findings upon which the Court adopted the decision, as better illustrated above, it is worth clarifying that: (i) the petition was an abuse of process because the Petitioner publicised it to the Company's bank in full knowledge that the latter was taking steps to prevent him from doing so; and (ii) the petition was not served properly, as per the witness statements provided by the Company, and the debt concerned unliquidated damages, not due or payable until liquidation has occurred.

The court acknowledged that the substance of the Petitioner's claim concerned issues raised by the Company through proceedings for possession of a pub (i.e., the premises for which the lease was entered into by the Petitioner) commenced, earlier that year, against both the Petitioner and the previous tenants. Such proceedings, where no allegations of fraudulent misrepresentation were formulated by the Petitioner, resulted in an order for possession, for forfeiture of the lease, a money judgement and a conviction to pay the costs of the action against the Petitioner. The Court clearly stated that if any claim for misrepresentation against the Company was to be raised by the Petitioner, then it should have been formulated in answer to the proceeding for possession. However, the Petitioner did not choose to do so (para. 35). It was also noted that the allegations supporting the statutory demand were not "*properly particularised … and mostly directed against the former tenant of the premises*" (para. 37); while no evidence had been served in answer to the Company's application.

Moreover, the Court took the opportunity to recall that, as clarified in *Tallington Lakes Ltd v Ancasta International Boat Sales Ltd* [2012] EWCA Civ 1712, the winding up petition may be filed only if the petitioner has the unchallenged standing of creditor; if the debt is disputed on substantial grounds then the petitioner lacks the necessary standing and the petition shall be struck out.

It appears clear that the facts provide several reasons to strike out the petition, thus, doubts may arise as to whether all those conditions shall be fulfilled in order to have the petition struck out. Fortunately, the decision answers such question pointing out that: (i) on the sole basis of the debt being substantially disputed, the petition could have been struck out; and (ii) also the fact that the Petitioner has consciously disregarded the procedures set out by the law to serve and advertise a winding up petition, would alone entitle the Court to strike out the petition as an abuse of process.

Priscilla Conti
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Harvey v Dunbar Assets Plc [2015] EWHC 3355 (Ch)

Executive summary

It would be contrary to the public interest to allow a debtor to challenge a second statutory demand by raising the same point he relied upon in his application to set aside a previous statutory demand in circumstances where the point was adjudicated against him and he had abandoned it in successive appeals.

Facts

The Appellant, Mr Harvey, had executed a joint and several guarantee along with three of the directors of the Company in favour of the respondent, Dunbar Assets Plc (the "Bank"). The guarantee was given in respect of the liabilities owed by the Company to the Bank under a facility agreement. The Appellant had no connection with the Company but had given the guarantee at the request of the Company and the Bank.

The Company failed and the Bank served a statutory demand ("the first statutory demand") on the Appellant for the payment of sums due under the guarantee.

The Appellant disputed the statutory demand on the basis that he had only consented to the guarantee after an employee of the Bank had assured him that his personal guarantee was just a formality for the loan to get approved by the Bank and that he had been assured that the bank would never enforce it against him. On this basis, he argued that the bank was estopped from enforcing the guarantee (the "promissory estoppel point"). The District Judge refused to set aside the first statutory demand on the grounds that the evidence submitted by the Appellant did not establish a case of promissory estoppel.

Subsequently, the Appellant abandoned the promissory estoppel point and was allowed to appeal on a different ground to the High Court and then to the Court of Appeal, where he argued that the signature by one of the co-guarantors, Mr Lenney, was a forgery with the result that the guarantee agreement was not valid. The Court of Appeal agreed and set aside the first statutory demand on that ground.

However, subsequent to the Court of Appeal's decision, the Bank launched proceedings in the High Court against Mr Lenney to enforce the guarantee against him. Norris J made a factual finding, confirming that Mr Lenney's signature was authentic and the guarantee was enforceable. At no stage in the proceedings had the Appellant pursued the promissory estoppel point.

Following the finding that the guarantee was enforceable, the Bank served a second statutory demand on the Appellant who disputed it on the promissory estoppel point.

The District Judge held that the Appellant could not rely on promissory estoppel point for the second time as the point was already adjudicated against him and he had abandoned the point on his appeal to the High Court and in the Court of Appeal.

Decision

The High Court upheld the decision of the District Judge. It held that debtor could not rely on the promissory estoppel point again as in the instant case, there were no special or exceptional circumstances which would warrant the re-arguing of the estoppel point. The new evidence as adduced by the appellant to support his case was immaterial and he had willingly chosen to abandon the promissory estoppel point on appeals to High Court and Court of Appeal. In effect, he was simply re-litigating the same point on the same substantial material and relying on the same arguments as before. All of this was contrary to public interest.

Comment

The Court recognised that the issue raised by the appeal was a novel one, there being no definite authority on the point. Although the case is based on a personal matter, there is no reason to think that the same principle established in this case would not arise in the context of a corporate insolvency. Here, counsel for the Appellant argued that there was no issue estoppel or *res judicata* that prevented the Appellant from arguing the same point as he had previously argued. The successful appeal in the Court of Appeal trumped the estoppel, despite being based on a different point (that of the alleged forged signature). Counsel for the Bank argued that this was a classic case of issue estoppel or *res judicata*. Hence, regardless of Mr Harvey's rights in the hearing of petition served against him by the Bank, he should not be allowed to set aside the second statutory demand on the same point he relied upon in the disputing the pervious statutory demand.

The majority of the case authorities cited to the Court dealt with a situation where the debtor whose application to set aside the statutory demand was rejected, raised the same point at the hearing of the petition for bankruptcy. The judge considered these authorities and helpfully identified important principles applicable to bankruptcy proceedings (para 34 – 36). The Court emphasised that these principles had equal application throughout the bankruptcy process, including applications to annul the bankruptcy and to invoke the court's jurisdiction under section 375(1) of Insolvency Act 1986 to review its order. Most importantly, the Court held that same principles were relevant to the present case despite its novel status.

The main principle on which the Court relied upon to make its decision was the *Turner* principle, following *Turner v Royal Bank of Scotland*, which asserts that a court will not entertain the same point which had been raised by the debtor at the application to set aside the statutory demand at the petition hearing unless there was a change of circumstances or other special reasons. It was made abundantly clear by the Court that the *Turner* principle was based on protecting public interest, that is, to allow the Appellant to re-litigate the same point which had been decided against him would be a waste of court's valuable time and parties' resources, in addition to being against the purpose of the statuary scheme. It would lead to unnecessary delays for the first-time litigants presenting their case to the court. Only in special or exceptional circumstances, the Appellant would be justified in re-arguing the same point, however, what these special circumstances are, the court did not say.

The case should prove to be useful to insolvency practitioners as the judgment conveniently lists important principles extracted from a large number of authorities relating to bankruptcy proceedings.

Muhammed Furqan Haider
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Power and others v Hodges, Hodges and others [2015] EWHC 2931 (Ch)

Executive Summary

The court had to consider the appropriate sentences for four directors all of whom were in contempt of court for failing to comply with a disclosure order under sections 235-237 of the Insolvency Act 1986.

Facts

The applicants were the Liquidators of a Company and the four main respondents were its Directors. The Liquidators alleged that the Directors had acted in breach of their fiduciary duties and/or misfeasantly in transferring or disposing of the Company's assets to four respondent companies when the Company was insolvent for little or no consideration.

The Liquidators were granted orders under sections 235-237 of the Insolvency Act 1986 to access the company books and records, as well as electronic disclosure by requiring the Directors to disclose their usernames and passwords. The disclosure order was not followed nor was a further disclosure order granted at a later date.

The Liquidators claimed that the overall conduct of the Directors in providing incorrect information or failing to disclose relevant information seriously prejudiced the Liquidators' ability to perform their obligations. The Liquidators issued a committal application for the Directors' contempt of court.

The Directors accepted that they were in breach of their duties and the disclosure order and admitted that they were in contempt of court.

Decision

Two of the Directors were fined £1,800 and £4,500 respectively. The fines took into consideration mitigating circumstances. Both the other Directors were given prison sentences, one of four, the other of six months. Both sentences were suspended pending compliance with certain conditions.

Comment

This was a very clear, well-structured judgment delivered by HHJ Baker. The sentencing of the four defendants was broken down very well. The Directors' various levels of blameworthiness were analysed and the judge clearly explained why certain defendants received certain punishments. It is a model judgment to view the interaction of insolvency and criminal law.

The judge concisely set out the relevant principles. Contempt of court may be described as knowingly defying a judicial order (para 58). The only purpose of contempt proceedings is "to ensure justice is done" (para 56). They are a "last resort" (para 57), which shows the importance of this case. The case also provides an insight into the behaviour of the defendants and how matters reached this stage. Issues of intention and understanding of the breach are taken into account in terms of both mitigation and aggravation (para 58). The purposes of the offence are punishment, deterrence and coercion (*JSC BTA Bank v Solodchenk (No. 2)* [2012] 1 WLR 350). The maximum punishment is two years imprisonment under the Contempt of Court Act 1982. The judge clearly set out the legislation, as well as relevant case law, including the *Solodchenk* case.

The judge also set out the sentencing guidelines for contempt relating to non-compliance of disclosure orders as explained by the Court of Appeal in *JSC BTA Bank v Ablayazov (No. 8)* [2013] 1 WLR 1331. These included that a substantial breach normally merits imprisonment, however a fine may be sufficient in the circumstances and that continuing failure may warrant a sentence at the upper-end of the scale. He also gave a list of various factors which should be taken into account (para 67), relying on the first instance decision in *Solodchenk* ([2010] EWHC 2843 (Ch)). These factors include the prejudice caused to other parties, duress, intention and degree of culpability. Very importantly, it was recognised that guilty pleas are hugely important in mitigation and attract reductions of between 10% and 33%, depending on the stage of the trial. HHJ Baker set out the principles of this area very clearly well and provided an easy thread to follow through to the individual sentencing.

Two of the Directors avoided custodial punishment. One of them received the lightest sanction of the four. He was handed a £1,800 fine following the 10% reduction. The court felt that his breach was caused by the conduct of others. It was not accepted that he acted under duress and it was unlikely that he did not appreciate the importance of the order. However, he was of good character and he gave a genuine guilty plea. The other Director who escaped a custodial sentence did not have as strong a mitigation; he never attempted to make an arrangement and failed to engage with the Liquidators. He too was of good character. A fine of £4,500, taking into account the reduction, was deemed appropriate.

The contempts of the other two Directors were "in an altogether different category" (para 81). These two Directors were brothers and very much took the lead in that they received legal advice and they were well-placed to formulate a viable proposal. The first of them had no rational basis for believing that he was in a financial position to comply with the terms that he and his brother had proposed. His breach was "deliberate and…a conscious disregard" of the order and the law (para 82). His eventual compliance was not viewed as much of a mitigating factor. The court found that he was of good character and that he quickly accepted that he was in contempt. Very little weight was attached to the contention that he was a subordinate to his brother by virtue of being the younger brother. HHJ Baker would have given him a 12 month sentence, split equally between coercion and punishment/deterrence. However, he felt that the coercive element no longer applied and that six months was appropriate, reduced to four due to the early guilty plea.

His brother's offence was viewed by the court as the most serious of the four. He was overtly blasé about his court-ordered obligations, shown by the continued failure to comply, instead diverting his attention to another of his businesses. The judge felt that he was a person who would be prepared to say anything (namely, agreeing to proposals with which he knew he could not comply) for his own personal benefit. Though he pleaded guilty, it was at a late stage. This was deemed only to match the aggravation. He was thus handed a six month sentence, without reduction.

The judge deemed, however, that it was appropriate to suspend both sentences. Firstly, as the liquidation of the Company was ongoing, it would not be in the best interests of the liquidators for the brothers to be in prison while it lasted. Secondly, it would further emphasise the deterrent element of the punishment, in the public interest, as well as the private interest of this case.

The judgment is extremely well-written. It is easy to follow the judge's line of thought throughout. The principles he enunciates and the formulae he utilises to calculate the appropriate sanctions are very clear. It is suggested that this would be a model judgment for anyone involved in insolvency who may not be as familiar with the criminal aspects. It could be of benefit to any reader, from students studying this area, to academics and practitioners. Even those familiar with the criminal implications of insolvency can use this modern case as a refresher.

Paul Barry

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Gagen Sharma (as former Liquidator of Mama Milla Limited) v (1) Top Brands Limited (2) Lemione Services Limited (3) Barry John Ward (as Liquidator of Mama Milla Limited) [2015] EWCA Civ 1140

Executive Summary

An insolvency practitioner who fails to exercise the standard of care expected of an ordinary skilled insolvency practitioner when dealing with a company whose activities prove to be fraudulent, can only rely on the illegality defence in circumstances where the illegality caused the loss claimed.

Facts

Mama Milla Limited ("MML") carried on business as a supplier of toiletry products until entering into creditors' voluntary liquidation in September 2011. Prior to the company entering liquidation, £548,074.56 (the Sum) was paid by MML'S principal purchaser, "SERT", to MML. Upon the freezing of MML's account the full Sum was transferred into the account of the appointed liquidator (the "Liquidator"). As a result of a fraudulent assertion made over a trust by a party claiming to be SERT, the Liquidator wrongfully authorised the payment of the Sum to numerous recipients at varying amounts between November 2011 and April 2012.

In October 2012 the two creditors of MML (two of the three respondents) commenced proceedings against the Liquidator contending, *inter alia*, misfeasance under section 212 IA 1986 for wrongly paying away the sum belonging to MML. In January 2014 the third respondent replaced the Liquidator and subsequently found that the business conducted through MML involved VAT acquisition fraud with the VAT lost to HRMC amounting to no less than £1.5 million.

HHJ Barker found the Liquidator's actions to be in breach of the duty implicit in section 107 IA 1986. Further liability arose for negligence with the judge concluding that the Liquidator failed to act in accordance with the "standard of care expected of an ordinary, skilled insolvency practitioner", amounting to misfeasance pursuant to section 212 IA 1986 (para 21).

The Liquidator raised the illegality defence at trial which was subsequently refused on the basis that the illegal business conducted by MML was peripheral to the court's examination of the case concerned. Accordingly, the Liquidator was ordered to contribute £548,074.56 to MML by way of compensation.

The Liquidator appealed to the Court of Appeal. She contended first, that the sole business conducted through MML was VAT fraud and therefore, if an inextricable link between the relief claimed and the illegality of MML's business was satisfied, the illegality defence should apply; second, that the recovery of the Sum would have the effect of condoning illegality; and third, that the claim made under section 212 to recover the Sum was for criminal property as defined by section 340(3) of the Proceeds of Crime Act 2002 ("POCA").

Decision

The Court of Appeal unanimously dismissed the appeal, upholding the decision of the High Court. The Court of Appeal held that there was no inextricable link between the relief claimed and the illegal conduct. The scope of the defence was limited to circumstances where the claimant needed to rely on the facts which revealed the illegality. The "reliance test" was not satisfied here. The illegality of the business conducted through MML had no causal link to the loss claimed since the MML had already ceased trading by the time the Liquidator was involved; the Sum could not have been used for illegal activities. Furthermore, HHJ Barker QC made no finding that the creditors and SERT conspired to commit VAT fraud using the Sum.

In addition, the Sum did not fall within the meaning of section 340(3) POCA and even if it had, it would be of no benefit for the Liquidator, in the context of civil action for negligence and breach of duty.

Comment

The case is relatively clear in relation to the fact that the liquidation was conducted without due diligence. The inadequate steps taken to ascertain MML's state of affairs contributed to a distorted overall perspective of MML's true obligations which ultimately led to the wrongful payment of the Sum. There is little concern with the statutory breach of duty under section 107. What is less clear is the scope and applicability of the illegality defence which is currently, in a state of flux. Excluding the "reliance test" in *Tinsley v Milligan*

[1993] All ER 65 endorsed by Lord Browne-Wilkinson, with whom Lord Jauncey and Lord Lowry agreed, there are numerous approaches adopted in case-law.

The "inextricable link" test contended by the appeal echoes the approach in *Tinsley* where both Lord Goff and Lord Keith agreed that the threshold for satisfying such test is the existence of "an immediate and necessary relation" between the relief claimed and the alleged misconduct (para 43). This approach has been endorsed in several cases, including *Hounga v Allen* [2014] UKSC 47, [2014] 1 WLR 2889. Following *Hounga*, the Court of Appeal in the present case discerned that the nexus between the illegality and the claim was so loose that the alleged fraud was no more than a "collateral" to the creditors' claim (para 46). The respondents did not rely on anything illegal in order to found their claim against the Liquidator.

However it must be noted that Lord Wilson, Baroness Hale, and Lord Kerr in *Hounga* approached the illegality defence through the lens of public policy, acknowledging that allowing the claim would lead to projecting a tolerance for an illegal conduct. *Les Laboratories Servier v Apotex Inc* [2014] UKSC 55, [2014] 3 WLR 1257 supports this approach (para 49). The Court of Appeal in the present case emphasised the flexibility of the "public policy" approach in that it is fact sensitive. There is no fixed formula laying out whether one policy outweighs another (para 52). In the given case, the public policy inherent within sections 107 and 212 IA 1986 which imposes a duty on the liquidator to collect and distribute the company's property accordingly, outweighed the policy of avoiding giving an appearance of condoning an illegal conduct (para 54). In winding up MML, preferential creditors were not a matter that needed consideration and thus it was solely the case of the liquidator distributing monies properly and equally (para 20). Given the backdrop of the non-causal link between the fraudulent business conducted by MML and the Liquidator's breach of duty, the public policy within sections 107 and 212 IA 1986 must triumph.

On the flip side, Lord Hughes and Lord Carnwath in *Hounga* focused on applying the "sufficiently close connection" test by requiring a close link between the illegality and the claim made (para 43).

In the present case, the different tests relating to the establishment of an illegality defence were analysed, but none of them assisted the Liquidator. She could not use the illegality defence to avoid returning funds to MML which would subsequently be made available to pay the debts to its creditors including the claimants and HMRC. As acknowledged by Lord Neuberger in *Bilta (UK) Ltd v Nazir (No.2)* [2015] UKSC 23, [2015] 2 WLR 1168 and in the present case, the illegality defence is in need of further clarification by the Supreme Court (para 38).

Kazuhisa Deguchi

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Selina Backus

As a postgraduate student on the Dual LL.M. in Insolvency Law at Radboud University Nijmegen and NTU, I am currently studying here in Nottingham. I welcomed the opportunity to write for the Bulletin as I am of the opinion that one of the many interesting features of insolvency law is the continued interdependence between academic research and practice. It is for this reason that I am considering both practice and pursuing a PhD as an option for my future career. After writing my dissertation, I will begin a traineeship with one of the Netherlands' leading law firms and I am very much looking forward to both experiences.

Priscilla Conti

I completed my Combined Bachelor and Master of Science in Law at Università L. Bocconi, in Milan (IT), with a major in Company Law. I had the chance to focus and develop a real interest in Insolvency Law working for almost four years in the corporate and restructuring department of Ashurst LLP's Milan office. Meanwhile, I qualified as a lawyer in both Italy and Spain. At present, I am studying for an LLM in Corporate and Insolvency Law to widen my awareness of the corporate rescue instruments available outside the Italian jurisdiction and gain confidence in providing advice to foreign clients. My personal

Miriam Carra

I studied law at the University of Montpellier, France where I obtained a bachelor in private law and an honourable bachelor (Master 1) in Law, focusing on corporate and patrimonial law. I then spent an Erasmus year at Radboud University in Nijmegen after which I chose to study on the Dual LL.M in Insolvency Law programme with NTU and am currently based at NTU. I wish to continue learning about European Insolvency Law and am considering studying for a PhD with a view to undertaking legal practice in this field.

Victor Laplace-Builhé

I obtained an LLB in France, an LLM in the Netherlands and I am currently studying for a Dual LL.M in Insolvency Law at Radboud University and NTU. I am specialised in European and Corporate law and I developed a great interest for pre-packaged administration. I would like to work in a corporate and restructuring department of an international law firm.

Matthijs van Schadewijk

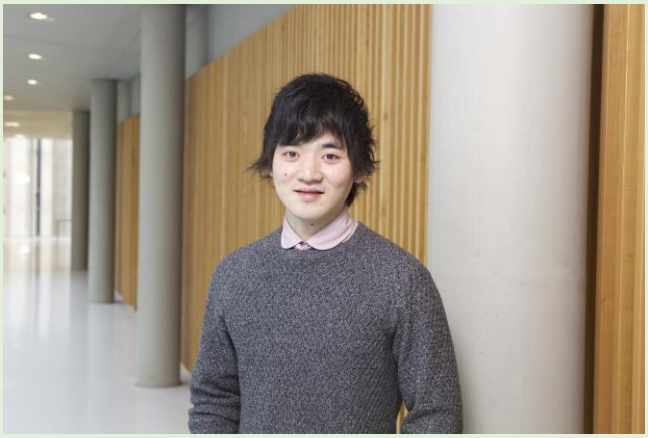
I studied European and Dutch law at Radboud Universiteit Nijmegen, The Netherlands, before coming to Nottingham to complete the Dual LL.M in Insolvency Law. My main interests lie with European law, in particular the way it affects corporate enterprises. I hope to do a PhD and/or work in this field in the future.

Jente Dengler

During my masters at the University of Ghent last year, I got my first experience of insolvency law in a European context. Intrigued by this interesting field of law, I chose to do the Dual LL.M in Insolvency Law at Radboud University Nijmegen and NTU to get a better understanding of global restructuring techniques and their implications for practice. After completing my LL.M degree I hope to work in an international law firm, advising and rescuing companies in financial distress.

Tjalling Bosker

I have completed an LLB and LLM in Dutch Law at the University of Groningen. Currently, I am studying for a Dual LL.M in Insolvency Law at Radboud University Nijmegen and NTU. My interest in insolvency law was sparked during my studies at Groningen, and naturally, I wrote my dissertation on this topic as well. I have a particular interest in the role of financiers with regard to the rescue of troubled companies. In the future, I would love to work in the field of Restructuring & Insolvency/Banking & Finance at either a law firm or a bank.



Kazuhisa Deguchi

I studied for my LLB at Keele University with one of my modules in the final year being Company Law. I am now studying for an LLM in Human Rights Law at Nottingham Trent University and I hope to work for the UN in the future. I have maintained my interest in company law by undertaking a free-standing elective in Corporate Rescue.

Muhammad Furqan Haider

I studied law Nottingham Trent University and am now studying for an LLM in Corporate and Insolvency Law at Nottingham Trent University. My interest in corporate insolvency law was sparked by studying it briefly at undergraduate level. In future, I would like to practise in the field of corporate law.

Paul Barry

I completed my primary BCL (Law and Irish) degree in University College Cork, graduating with a first class honours degree with a high first in the Company Law module. I am currently studying for an LLM in Sports Law and have a particular interest in the relationship between insolvency law and football clubs in the UK and Ireland. I have previously worked as a paralegal in a commercial law firm in Cork. Next year, I will begin a traineeship with Arthur Cox, one of Ireland's leading law firms.