CHAPTER 3

THE EC REGULATION ON INSOLVENCY PROCEEDINGS

INTRODUCTION

3.1 Council Regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings ('the Regulation') came into force on the 31 May 2002. Being a Regulation it is self-enacting. It applies to insolvencies throughout the European Union and is directly applicable within all member states except for Denmark. Under the Protocol to the Treaty of Amsterdam of 1999, Denmark is excluded from the Regulation, though the Danish government is due to introduce domestic legislation to bring it in line with the Regulation.

3.2 It is to be noted that the Regulation has effect as primary legislation. Thus it has superseded any domestic rule of law which may have been inconsistent with its provisions. There was a hope that the Regulation would reduce, if not completely prevent, forum shopping. This occurs, for example, where a creditor chooses to litigate in a particular jurisdiction in order to prove his debt because the law in that jurisdiction is the most favourable for his claim, rather than because the jurisdiction is that most closely connected to the debt.

3.3 The terms of the Danish opt-out were considered in *Re Arena Corporation Ltd, Arena Corporation v Customs and Excise Commissioners*[1] and it was held that in accordance with recital 33 of the Regulation, Denmark was not to be considered a 'member state' for the purposes of the Regulation. Under the Regulation, an English court has no jurisdiction to make a worldwide winding-up order in relation to a company whose centre of main interests is in another member state but it was held that jurisdiction was not ousted by the Regulation even though the company's centre of main interests was in Denmark. This meant that an English court could exercise its traditional winding-up jurisdiction and wind up the company provided that it had sufficient connection with England, something which could not have been done had Denmark been a party to the Regulation.

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1 [2004] EWCA Civ 371, [2004] BPIR 415.

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EUROPEAN JARGON

3.4 The Regulation is, of course, legislation from Europe and, as such, is frequently expressed in a manner rather different from that to which English readers are accustomed. Sometimes its precise meaning will be seen to be open to different interpretations. It is thought, however, that the exact wording of the Regulation should usually be quoted in this commentary so that the reader can, at least, have before him the text that the court will have to interpret.

3.5 It is thus important not to try to read the Regulation like an English Act of Parliament. In *Re The Salvage Association*[2] Blackburne J said, in respect to the interpretation of the word 'court' in the Regulation:

> 'The answer lies, in my view, in avoiding a too-literal approach to the application of the definition of "court" in the Regulation and in understanding the reference in that definition to "other competent body of a Member State" as applying not merely to some organ of the state but, more widely, to any body recognised as competent in that Member State to resolve upon (i.e. "open") the insolvency proceedings in question.'

In other words a purposive and liberal interpretation should be adopted.

3.6 This itself is reflected in the Preamble to the Regulation. Paragraph 10 states:

> 'Insolvency proceedings do not necessarily involve the intervention of a judicial authority; the expression "court" in this Regulation should be given a broad meaning and include a person or body empowered by national law to open insolvency proceedings.'

3.7 The Regulation should surely be welcomed. While there will be difficulties in its interpretation, not least because of the way in which it is from time to time worded, it represents a vast improvement on the situation prior to its implementation.

THE AIM OF THE REGULATION

3.8 Despite the heading of this paragraph 'the aim of the Regulation' it is even more important at the outset to appreciate what the Regulation is *not* intended to do. There is no intention to harmonise the insolvency laws of the various member states of the European Union. Each will retain its own idiosyncratic procedures and remedies. For example, under IA 1986, s 238 a liquidator or an administrator in England can seek to set aside an undervalue transaction entered into by a company within the 2 years prior to the commencement of its winding up. Common sense dictates that there are bound to be similar procedures within other legal systems but that matters such as time-limits may be different. Such domestic idiosyncrasies will remain. Again

[2] [2003] BCC 504.

under IA 1986, s 273 a bankrupt within England may retain enough of his personal belongings to meet the basic needs of himself and his family. Within some legal systems a monetary limit is set upon those assets rather than leaving it to the discretion of the court to decide what is meant by 'basic'. Matters such as this will be unchanged under domestic law. In the same vein, bankruptcy is discharged in the UK one year from its commencement or such earlier time as the Official Receiver files with the court a notice that investigation of the conduct and affairs of the bankrupt is either unnecessary or concluded.[3] In some European states, bankruptcy lasts for longer periods of time. Such variations are bound to encourage forum shopping.

3.9 That substantive insolvency law varies from state to state is acknowledged in para 11 to the Preamble:

> 'This Regulation acknowledges the fact that as a result of widely differing substantive laws it is not practical to introduce insolvency proceedings with universal scope in the entire Community. The application without exception of the law of the State of opening of proceedings would, against this background, frequently lead to difficulties. This applies, for example, to the widely differing laws on security interests to be found in the Community. Furthermore, the preferential rights enjoyed by some creditors in the insolvency proceedings are, in some cases, completely different.'

What the Regulation is intended to do is to ensure a mutual recognition throughout Europe of the office-holders and judgments of the courts of the member states. It is intended to foster co-operation between the member states within the European Union which should result in a more coherent approach to cross-border insolvencies at least with Europe itself.

3.10 Thus, for example, by Art 19:

> 'The liquidator's appointment shall be evidenced by a certified copy of the original decision appointing him or by any other certificate issued by the Court which has jurisdiction.'

(It will be seen that the term used to designate the office-holder is 'liquidator'. Quite why the draftsman of the Regulation should have chosen to refer to an office-holder as the liquidator is something of a mystery given that In English law the word 'liquidator' has a very specific meaning, namely a person who has been appointed to wind up the affairs of a company.)

3.11 Throughout the Regulation, as is provided by Art 2(b):

> '"liquidator" shall mean any person or body whose function is to administer or liquidate assets of which the debtor has been divested or to supervise the administration of his affairs. These persons and bodies are listed in Annex C.'

[3] IA 1986, s 279.

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Annex C then goes on to provide that a 'liquidator' within the UK, means a 'liquidator, supervisor of a voluntary arrangement, administrator, Official Receiver, trustee, provisional liquidator [and] judicial factor'.

Similarly by Art 16(1): 'Any judgment handed down by a Court of a Member State ... shall be recognised in all other Member States.'

3.12 Thus the aim of the Regulation is stated in para 8 to the Preamble to be to improve 'the efficiency and effectiveness of insolvency proceedings having cross-border effects'. The Regulation seeks to achieve this by introducing rules on the following matters:

- commencement of proceedings;
- concurrent proceedings in two or more member states;
- choice of law;
- applicability of local law;
- creditors' rights; and
- relations between office-holders.

Forum shopping

3.13 As stated above it is beyond doubt that one purpose of the Regulation was to prevent, or at least, discourage, forum shopping. This is the practice whereby a creditor chooses the jurisdiction which is most favourable to his claim rather than that which is the most connected with his claim. While clearly forum shopping can be of considerable assistance to the well-advised creditor, it may equally be detrimental to the body of creditors generally. Paragraph 4 to the Preamble expressly states:

> 'It is necessary for the proper functioning of the internal market to avoid incentives for the parties to transfer assets or judicial proceedings from one Member State to another, seeking to obtain a more favourable legal position (forum shopping).'

Perversely, however, it is possible that the Regulation encourages rather than discourages forum shopping in some instances. It is a prime aim of the Regulation that the decision to open insolvency proceedings in one member state must be recognised in the other member states, and it is naive to believe that this will have any effect other than to encourage forum shopping.

3.14 In *Hans Brochier Holdings Ltd v Exner*[4] there was a conflict between the interests of the directors of an insolvent company and its employee creditors. The directors made an extra-judicial appointment of administrators in the UK just 45 minutes before insolvency proceedings were commenced in Germany by the employee creditors pursuant to which a German administrator was also appointed. (It has to be said that the English administrators had acted in

[4] [2007] BCC 127.

complete good faith in accepting their appointment and genuinely believed on the information which they had at the time that the company's centre of main interests was in England.) The German insolvency procedure would have carried advantages for the employee creditors which were not available in the British administration. The administrators acted properly as officers of the court – a status given to them by the Insolvency Act 1986, as amended.[5]

3.15 Having said this, the English administrators acted with that sense of honour[6] which is to be expected of them as officers of the court[7] and recognised that the company's centre of main interests was in fact Germany. Accordingly their appointment was discharged.

3.16 Warren J agreed that the company's centre of main interests was indeed in Germany. Although the company's registered office was in England, it had no branches in England, had never traded in England, had its main bank accounts in Germany and had over 700 employees in Germany. Warren J stated:

> 'I should mention some of the benefits that are perceived as accruing if the main proceedings are in Germany ... There is a large advantage in relation to German social security law, which will give the employees a significant advantage as compared with an English administration. The vast majority of the company's employees are located in Germany and are subject to German employment and social security laws and it is clear...only an experienced German insolvency administrator will be able adequately to address those rights and interests.'

3.17 Thus a just conclusion was reached in this case; but its history illustrates well the dangers of a precipitate race to commence legal proceedings which will often and inevitably be based upon an inadequate knowledge of the facts.[8]

PROCEEDINGS SUBJECT TO THE REGULATION

3.18 Article 2(a) states that the Regulation applies only to 'collective insolvency proceedings' which, in the words of para 10 to the Preamble 'entail the partial or total divestment of a debtor and the appointment of a liquidator'. In other words proceedings falling under the Regulation must be judicial in nature. Having said this, the term 'judicial' is given the fullest possible meaning. The Preamble to the Regulation states that 'Insolvency proceedings do not necessarily involve the intervention of a judicial authority'. For this reason:

> 'the expression "court" in this Regulation should be given a broad meaning and include a person or body empowered by national law to open insolvency proceedings. In order for this Regulation to apply, proceedings (compromising acts

[5] IA 1986, Sch B1, para 5.
[6] This brings into play the so-called rule in *Ex parte James* (1874) 9 Ch App 609.
[7] A status enjoyed by all administrators in the UK, regardless of whether their appointment is judicial or extra-judicial: IA 1986, Sch B1, para 5.
[8] See Doyle and Keay *Insolvency Legislation, Annotations and Commentary* (Jordan Publishing Ltd, 4th edn, 2014).

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or formalities set down in law) should not only have to comply with the provisions of this Regulation, but they should also be officially recognised and legally effective in the Member State in which the insolvency proceedings are opened and should be collective insolvency proceedings which entail the partial or total divestment of the debtor and the appointment of a liquidator.'

3.19 For this reason it is almost certainly the case that a creditors' meeting in a corporate voluntary arrangement, a creditors' voluntary winding up or an individual voluntary arrangement is 'a person or body empowered by national law to open insolvency proceedings'.[9] Likewise an extra-judicially appointed administrator falls within the Regulation because his appointor is regarded as 'the judicial body or other competent body of a Member State empowered to open insolvency proceedings'.[10] On the other hand, a receivership is generally not a 'collective' insolvency proceeding and so does not therefore fall within the scope of the Regulation. The receiver is usually a contractual appointment made by a secured creditor, and once the receiver has recovered and handed over sufficient funds to repay that secured creditor he must vacate office.[11]

TYPES OF PROCEEDINGS

3.20 The Regulation covers three types of insolvency proceedings, main, secondary and territorial. In brief, main proceedings are commenced within the territory where 'the centre of a debtor's main interests' is to be found. The significance of main proceedings is that the office-holder enjoys cross-border authority. Paragraph 12 to the Preamble provides that 'these proceedings have universal scope and aim at encompassing all the debtor's assets'. Once main proceedings have been commenced then secondary proceedings may be commenced within another member state, but such secondary proceedings are limited to those assets of the insolvent within the member state where the secondary proceedings are being commenced.

3.21 If main proceedings have not been commenced and there are assets within a state other than that where the centre of the debtor's main interests is to be found then territorial proceedings can be commenced. These again are limited to assets within the state where the proceedings are commenced. Paragraph 17 to the Preamble explains territorial proceedings:

> 'Prior to the opening of the main proceedings, the right to request the opening of insolvency proceedings in the Member State where the debtor has an establishment should be limited to local creditors and creditors of the local establishment or to cases where main proceedings cannot be opened under the law of the Member State where the debtor has the centre of his main interest.'

(By way of a defence to allegations of poor proofreading, the editors would point out that sometimes the Regulation refers to the centre of the debtor's

[9] See para 10 to the Preamble to the Regulation.
[10] Article 2(d) of the Regulation.
[11] See also 3.26.

'main interest' (as in para 17 to the Preamble quoted above) and sometimes to the centre of the debtor's 'main interests' (as in Art 3). This chapter uses the terminology as it appears in the part of the Regulation in which it appears. A common law judge would traditionally say that where different terminology is used in different places in a statute, Parliament must have intended them to be interpreted differently. This is, however, almost certainly not the case in the interpretation of European legislation.)

3.22 Thus it will be appreciated that there can be more than one set of insolvency proceedings running concurrently for a single debtor. This will result in a plurality rather than a unity of proceedings. However, to reduce the risk of conflict there is a hierarchy established for the different sets of proceedings which may be running concurrently, with main proceedings occupying the dominant position.

3.23 Thus to add further to the complexity, main proceedings, secondary proceedings and territorial proceedings apply to different types of insolvency proceedings. This will now be considered.

MAIN PROCEEDINGS

3.24 As we have seen, the Regulation applies only to 'collective insolvency proceedings which entail the partial or total divestment of a debtor and the appointment of a liquidator'. (We should remind ourselves that the term 'liquidator' is used generally in regard to main proceedings to refer to any insolvency office-holder other than a receiver.)

3.25 Annex A states that main proceedings are limited, in the case of the UK, to:

> '• Winding up by or subject to the supervision of the court,
> • creditors' voluntary winding up (with confirmation by the court),
> • administration, including appointments made by filing prescribed documents with the court,
> • voluntary arrangements under insolvency legislation,
> • bankruptcy and sequestration.'

3.26 The requirement for confirmation of the court was implemented in the UK by the Insolvency (Amendment) Rules 2002, SI 2002/1307 and is to be found in IR 1986, rr 7.62 and 7.63. There is no corresponding secondary legislation for an extra-judicial administrator, but it is thought that such an office-holder is covered by the Regulation since para 5 of Sch B1 to the Insolvency Act 1986 provides that such an appointee is an officer of the court. Moreover, the Virgos-Schmidt Report on the draft EU Convention on Insolvency Proceedings assumed that such office-holders fell under the Regulation. While the Report was not agreed by all EU members and has no official standing, it is nevertheless of persuasive authority. In spite of this, it might be sensible in any administration having an international flavour to

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CHAPTER 6

DUTIES OF THE LIQUIDATOR

PRELIMINARY DUTIES

6.1 Within 14 days of his appointment, the voluntary liquidator must publish notice of his appointment in the *Gazette* and file the notice with the Registrar of Companies.[1] He should also ensure that a copy of the winding-up resolution is duly filed with the Registrar of Companies within 15 days[2] and published in the *Gazette* within 14 days.[3] In the case of a compulsory winding up, the Official Receiver becomes the liquidator of the company and remains the liquidator until some other person is appointed in his place.[4] Three sealed copies of the winding-up order must be sent by the court to the Official Receiver who, in turn, must send one copy to the registered office of the company (or its principal or last known principal place of business) and one copy to the Registrar of Companies.[5] In addition to the standard contents the notice must state that a winding-up order has been made in respect of the company and the date of the order.[6] The Registrar must publish in the *Gazette*, notice of his having received the copy of the winding-up order.[7] This is official notification for the purposes of the Companies Act.

6.2 Where a liquidator is appointed by a creditors' or contributories' meeting, or by a meeting of the company, he must, on receiving his certificate of appointment, give notice in such manner as he thinks appropriate.[8] Formerly there was a requirement that the notice of appointment had to be given in the *Gazette*. It is, however, now for the liquidator to decide where to give notice as he thinks fit. The expense must initially be borne by the liquidator but he is entitled to be reimbursed from the assets of the company as an expense of the liquidation.[9] In the case of a compulsory winding up, the liquidator must still

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1 IA 1986, s 109.
2 IA 1986, s 84(3) and CA 2006, s 30, formerly CA 1985, s 380.
3 IA 1986, s 85.
4 IA 1986, s 136(1) and (2).
5 IR 1986, r 4.21.
6 I(A)R 2010, Sch 1, para 152.
7 CA 2006, s 1078.
8 IR 1986, r 4.106A(1) and (2).
9 IR 1986, r 4.106A(5) and (6).

give notice in the *Gazette*;[10] he must also give notice to the Registrar of Companies.[11] He may also advertise his appointment in such other manner as he may think fit.[12]

6.3 The liquidator should ensure that the company is described as 'in liquidation' on all letter headings, invoices and orders; a like statement must also appear on all the company's websites.[13]

6.4 It is important to note that the giving of notice of a winding up in the *Gazette* is not notice to the world that the company is in liquidation. In *Official Custodian for Charities v Parway Estates Developments Ltd*,[14] a lease contained a provision that the landlords could re-enter the property and forfeit the lease if the company went into liquidation. A winding-up order was made against the company and notification of the order and of the appointment of a liquidator was duly given in the *Gazette*. For over a year the landlords, unaware of the winding-up order, continued to accept rent. Upon discovering that the company was in liquidation they refused to accept any further rent and sought by action to forfeit the lease. The company contended that the acceptance of the rent amounted to a waiver of the right to forfeit the lease. The Court of Appeal held that in accepting the rent the landlords had neither actual nor imputed knowledge of the liquidation, notwithstanding that notice had been given in the *Gazette*. Therefore there had been no waiver of the right to forfeit.

DUTY TO MAINTAIN LIQUIDATOR'S RECORD

6.5 Throughout the course of winding up the liquidator must maintain the statutory record prescribed by the Insolvency Practitioners Regulations 2005.[15] This is a record of proceedings during the winding up and is distinct from the duty to maintain books and accounts. The record begins with the date of commencement of the liquidation and ends with the final meetings, filing of final returns and dissolution of the company; Sch 3 to the 2005 Regulations sets out the form of the record. It must be available for inspection by the competent authority or professional body which authorises the liquidator to act as an insolvency practitioner, or its duly appointed representative, and the Secretary of State (or his representative), on reasonable notice. When the record is kept in a non-documentary form, on computer, for example, legible copies should be available for inspection. Each record which is maintained must be kept in such a way as to be capable of being produced by the insolvency practitioner separately from any other record. The liquidator must retain the record for a

10 IR 1986, r 4 106A(2)(a).
11 IR 1986, r 4.106A(4).
12 IR 1986, r 4 106A(2)(b).
13 IA 1986, s 188.
14 [1984] 3 All ER 679.
15 Insolvency Practitioners Regulations 2005, SI 1990/439, rr 16–20.

period of 6 years from the date on which the security or caution maintained in respect of that estate expired or from the date of his release or discharge, whichever is the later.

DUTY TO TAKE POSSESSION OF PROPERTY

6.6 The company's property does not vest in the liquidator. The property remains vested in the company. This is in sharp contradistinction to the immediate vesting of the bankrupt's estate in his trustee in bankruptcy.[16] Perhaps curiously there is no general statutory duty requiring a liquidator to carry out the winding up in a proper manner. Nevertheless there are duties both at common law and equity requiring him to apply the company's assets as provided by legislation. As such the liquidator is under a duty to get in all the company's property, including books, papers and records, into his custody. To this end if any person has in his possession or control any property, books, papers or records to which the company appears to be entitled, the court may, on the application of the liquidator, require that person forthwith to surrender up such items to the liquidator.[17] In *Re Coslett (Contractors) Ltd*[18] it was said that an application for recovery under this provision must be commenced in the name of the office-holder and not that of the company.

6.7 In *Re London Iron & Steel Co Ltd*,[19] Warren J held that on an application under s 234 the court had jurisdiction to determine whether or not the company was entitled to the property in respect of which an order was sought. In *Euro Commercial Leasing Ltd v Cartwright and Lewis*[20] the court dealt under this provision with a solicitor's lien. Similarly in *Re Cosslett (Contractors) Ltd*,[21] s 234 was applied in considering a lien over plant on a construction site. However, in *Re Leyland DAF Ltd*,[22] the Court of Appeal held that this did not put the office-holder seeking the s 234 order is a better position than the company itself. This case concerned a dispute as to the ownership of property where the dispute was due to be settled by a Dutch court. In these circumstances, the English courts had no power to settle the matter.

6.8 In *Re La Senza Ltd, Uniserve Ltd v Croxon*[23] the company was in administration. The administrators had entered into a contract to sell certain goods to a third party. However, the goods were held by the claimants in the

16 IA 1986, s 306.
17 IA 1986, s 234. This power for an office-holder to apply to the court extends beyond liquidators; it also applies to administrators, administrative receivers and also provisional liquidators.
18 [1998] Ch 495.
19 [1990] BCC 159.
20 [1997] BCC 724.
21 [1998] Ch 495.
22 [1994] BCC 166.
23 [2012] EWHC 1190 (Ch).

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case who sought an order permitting them to sell the goods themselves[24] since they had a contractual lien over them. It was held that it was the claimants who should be permitted to sell the goods. The terms of the contract made by the administrators did not afford sufficient protection of the rights of the claimants under their lien.

6.9 In *Re Oakwell Collieries Co*[25] it was said that the precursor to this provision created a summary procedure for recovering property, books papers and records from any person. However, in *Re First Express Ltd*,[26] Hoffmann J held that it was generally wrong for a s 234 application to be heard ex parte:

> 'It is a basic principle of justice that an order should not be made against a party without giving him an opportunity to be heard. The only exception is when two conditions are satisfied. First, that giving him such an opportunity appears likely to cause injustice to the applicant, by reason either of the delay involved or the action which it appears likely that the respondent or others would take before the order can be made. Secondly, when the court is satisfied that any damage which the respondent may suffer through having to comply with the order is compensatable under the cross-undertaking or that the risk of uncompensatable loss is clearly outweighed by the risk of injustice to the applicant if the order is not made.'

The provision applies only to tangible property. In *Welsh Development Agency Ltd v Export Finance Co*[27] it was held that it did not extend to the improper seizure of choses in action.

DUTY AS TO BANK ACCOUNTS

6.10 In a voluntary winding up the liquidator must pay any surplus funds held on behalf of the company into the Insolvency Services Account (ISA) of the Bank of England at the expiration of the first 6 months of his appointment and every following 6-month period. Such funds include any unclaimed or undistributed dividends or assets, together with monies held by the company on trust as a debt owing to any member or former member. The liquidator is entitled to retain a sufficient amount to pay for immediate costs arising in the course of the liquidation.[28] In a compulsory winding up the liquidator has to pay all money received by him into the ISA without deduction.[29] When money has been paid into the ISA to which someone else claims to be entitled, that person may ask the Secretary of State for the repayment of the requisite amount.[30] An appeal lies to the court against any decision as to such entitlement.[31] If a voluntary liquidator wishes to draw any moneys held in the

[24] Under IA 1986, Sch 43(3)(b).
[25] [1879] WN 65.
[26] [1991] BCC 782.
[27] [1992] BCC 270.
[28] Insolvency Regulations 1994, SI 1994/2507, reg 5(2).
[29] Insolvency Regulations 1994, reg 5(1).
[30] Insolvency Regulations 1994, reg 32(1).
[31] Insolvency Regulations 1994, reg 32(2).

ISA, he must first apply in writing to the Secretary of State who will authorise such payments only for the purposes of distributions or expenses incurred in the liquidation. Payments may be authorised directly to the liquidator or by way of cheques in favour of the payees for delivery to them by the liquidator.[32] Dividends in a compulsory winding up are paid by payment instruments prepared by the Department for Business, Innovation and Skills and transmitted to the liquidator for distribution amongst the creditors.[33]

6.11 Where, in the liquidator's opinion, the amount held to the company's credit in the ISA is greater than that required in the immediate conduct of the liquidation, he may request the Secretary of State to invest the surplus in government securities.[34]

6.12 Funds held to the company's account in the ISA earn interest at the rate of 4.25% per annum.[35]

6.13 The liquidator can continue to use the company's existing banking facilities, either in the name of the company 'in liquidation' or in his own name. He should take over all cheque books and send to the bank a copy of the resolution appointing him, with instructions to stop all cheques which are still unpaid.

6.14 In the case of a compulsory winding up, all receipts and payments must as a general rule pass through the ISA. Any money received must be paid into the account once every 14 days or immediately if more than £5,000 is received.[36] The liquidator must apply to the Secretary of State if he wishes a payment to be made out of funds held in the company's name. The application is made on a form obtainable from the Department for Business, Innovation and Skills or on a form which is substantially similar.[37] Payments into the account must be accompanied by a form available from the Department or, again, a form which is substantially similar.[38]

6.15 If the compulsory liquidator intends to carry on the business of the company, he may apply to the Secretary of State for permission to open a local bank account, though it should be noted that he can only carry on the business so far as necessary for the beneficial winding up of the company with consent of the court or the liquidation committee in a compulsory liquidation.[39] Before granting such permission, the Secretary of State must be satisfied that an administrative advantage is to be gained from having such an account.[40] Where

[32] Insolvency Regulations 1994, reg 8(3).
[33] Insolvency Regulations 1994, reg 8(1).
[34] Insolvency Regulations 1994, reg 9(1).
[35] Insolvency Regulations 1994, reg 9(6).
[36] Insolvency Regulations 1994, reg 5(1).
[37] Insolvency Regulations 1994, reg 5(4).
[38] Insolvency Regulations 1994, reg 5(4).
[39] Insolvency Regulations 1994, reg 6(1). See also IA 1986, s 168(3) and Sch 4, Part 1 and para 5 of that Schedule to that Act.
[40] Insolvency Regulations 1994, reg 6(2).

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a local bank account is opened, it must be specifically dedicated to the company in liquidation.[41] When such an account is opened, the Secretary of State will fix an upper and lower limit on the payments which can be made into and from the account.[42] As soon as the carrying on of the business ceases, the liquidator must close the local account and pay the balance to the ISA as provided by reg 5.[43]

6.16 As in the case of a voluntary winding up, balances held to the company's account in the ISA earn interest at 4.25% from the date when the liquidator gives notice that the excess is not immediately required.[44]

DUTY TO SETTLE LIST OF CONTRIBUTORIES

6.17 The term 'contributory' is defined in s 79 as meaning every person liable to contribute to the assets in a winding up, including an alleged contributory but excluding anyone liable to contribute under s 213 (responsibility for company's fraudulent trading) and s 214 (wrongful trading). An unanswered question is whether a person who has been ordered to make a payment to a company by reason of his having been the recipient of an undervalue transaction[45] or a preference[46] might be a contributory. It is suggested that he may well be, on the application of the expressio unius est exclusio alterius[47] rule of construction. The definition includes a holder of fully paid shares since every member is under a primary liability to contribute, qualified only by the provisions of s 74(2)(d) that a member's liability shall not be greater than the amount unpaid on his shares. A former member who held partly paid shares ceases to be liable on those shares one year after he has ceased to be a member,[48] and his liability ceases if the existing holder of the shares is able to satisfy the contributions required to be made by him.[49]

6.18 In this regard it is to be noted that in some ways the term 'contributory' is misleading. Semantically, and in common sense, it means someone who is liable to contribute to the assets of a company. Yet it is quite clear from cases such as *Re Anglesea Colliery Co*[50] and *Re Phoenix Oil & Transport Co*[51] that it also includes current members of the company even where they hold fully paid shares. A past member is not liable to contribute if he ceased to be a member more than one year before the commencement of the winding up.[52] Moreover, he is not liable to contribute unless it appears to the court that the

41 Insolvency Regulations 1994, reg 6(3).
42 Insolvency Regulations 1994, reg 6(2).
43 Insolvency Regulations 1994, reg 6(8).
44 Insolvency Regulations 1994, reg 9(6).
45 Contrary to IA 1986, s 238.
46 Contrary to IA 1986, s 239.
47 Sometimes expressed as expressum facit cessare tacitum.
48 IA 1986, s 74(2)(a).
49 IA 1986, s 74(2)(c).
50 (1866) 1 Ch App 555.
51 [1958] Ch 560.
52 IA 1986, s 74(2)(a).

existing members are unable to make the payments due from them, nor is he liable in respect of any debt or liability of the company contracted after he ceased to be a member.[53] In *Barbor v Middleton*,[54] it was confirmed that the court may order retrospective rectification of the register of members if satisfied that a person alleged to be a member was in fact never a member.

6.19 The liability of a contributory in England and Wales creates an ordinary contract debt accruing from him at the time when his liability commences.[55] The limitation period is therefore 6 years.[56]

6.20 By s 74(1)(f) any sum due to a member in his character as a member by way of dividends, profits or otherwise is not deemed to be a debt of the company, payable to that member in a case of competition between himself and any other creditor who is not a member of the company. Such sum may be taken into account for the purpose of the final adjustment of the rights of the contributories among themselves. In *Soden v British and Commonwealth Holdings plc*[57] it was held that this provision required a distinction to be drawn between sums due to a member by way of dividends, profits or otherwise and sums due to him otherwise than in his character as a member. In this case sums due to a member as a result of misrepresentations having been made to him when he acquired his shares in the company were held by the House of Lords not to be due to him in his character as a member. Lord Browne-Wilkinson said:[58]

> 'in the absence of any other indication to the contrary, sums due in the character of a member must be sums falling due under and by virtue of the statutory contract between the members and the company and the members inter se constituted by s 14(1) of the Companies Act 1985.'

6.21 There used to be an exception to this limited liability principle. Where a public company has carried on business for more than 6 months with fewer than two members, any member during that excess period, who knows the situation, is jointly and severally liable with the company for all the debts of the company contracted during that period.[59] This provision has now, however, been repealed. Both public and private companies can exist with a single member.

6.22 In a voluntary winding up the liquidator himself has power to settle a list of contributories and to make calls.[60] In a compulsory winding up the court

53 IA 1986, s 74(2)(c).
54 (1988) 4 BCC 681.
55 IA 1986, s 80.
56 Prior to 1 October 2009 it was a specialty debt with a limitation period of 12 years but this was changed by the Companies Act 2006 (Consequential Amendments, Transitional Provisions and Savings) Order 2009, SI 2009/1941, Art 2 and Sch, para 75(9).
57 [1997] BCC 952, [1998] AC 298.
58 As from 1 October 2009 the corresponding provision is CA 2006, s 33.
59 CA 1985, s 24.
60 IA 1986, s 165(4).

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must settle a list of contributories as soon as possible after the making of the winding-up order unless the court is of the opinion that it will not be necessary to make calls or adjust the rights of contributories and so dispenses with the need for a list.[61] Although the Act states that it is for the court to settle the list of contributories, this duty is delegated to the liquidator.[62] In settling the list of contributories, the court has an express power to rectify the register of members should this be necessary.[63] However, once again the Rules delegate this power to the liquidator.[64] The liquidator in this regard acts as an officer of the court.[65]

In practice, calls are very rarely necessary since unpaid and partly paid shares are seldom encountered.

6.23 If a list of contributories does have to be drawn up, the voluntary liquidator can adopt his own procedure. However, he should have regard to the procedure which has to be followed by the compulsory liquidator. The list falls into two parts. First, there is the 'A' list which comprises of members who are liable to contribute because of their membership of the company as at the commencement of the winding up. Secondly, there is the 'B' list consisting of persons such as former members who are liable for the debts of others.[66] The terms 'A' and 'B' list are not to be found in either the Act or the Rules, but they are used as a matter of practice.

The lists must identify the name and address of each contributory, the number and class of shares held and the extent of his liability.[67]

6.24 Having settled the list, the compulsory liquidator must give notice to every person named on it. Such person may then object to the liquidator within 21 days from the date of the notice. Within 14 days of receiving such objection, the liquidator should notify the objector as to whether he is going to amend the list of contributories or whether he regards the objection as ill-founded.[68] An objector still aggrieved at a compulsory liquidator's refusal to amend the list, may apply to the court within 21 days of the liquidator's notice that he regards the objection as ill-founded.[69] The liquidator, however, may not without the special leave of the court, rectify the register of members, and must not make any call without either that special leave or the sanction of the liquidation committee.[70]

61 IA 1986, s 148.
62 IR 1986, r 4.195.
63 IA 1986, s 148(1).
64 IR 1986, r 4.196(1).
65 IR 1986, r 4.196(2).
66 IR 1986, r 4.197.
67 IR 1986, r 4.197(2).
68 IR 1986, r 4.198.
69 IR 1986, r 4.199.
70 IA 1986, s 160(2).

6.25 There is no specific procedure contained in the Rules whereby an alleged contributory can object to his inclusion in the list by a voluntary liquidator. It is thought that his remedy would be to apply to the court under s 168(5):

> 'If any person is aggrieved by an act or decision of the liquidator, that person may apply to the court; and the court may confirm, reverse or modify the act or decision complained of, and make such order in the case as it thinks just.'

6.26 Where there is a surplus for members in the liquidation, the voluntary liquidator will need to verify the register of members and on making a distribution, according to the rights of the members under s 107, to take back the share certificates as appropriate. Unless the company's articles otherwise provide, the distribution to the members must be pari passu.

A similar obligation falls on the compulsory liquidator under s 148.

6.27 In the event of a contributory's dying, his liability falls on his personal representatives and become payable from his estate.[71] However, the personal representatives incur no personal liability unless they agree to be registered as members.[72] If a contributory becomes bankrupt, his liability becomes a provable debt in the bankruptcy.[73] The trustee represents the bankrupt for all purposes of the winding up.

DUTY TO EXAMINE CONDUCT OF OFFICERS

6.28 The liquidator has a general duty[74] (within the limits of the resources reasonably available to him for the purpose) to investigate the conduct of the company's past and present officers and to consider whether they have been guilty of any wrongful conduct towards the company or any criminal offence, and subsequent sections of this chapter discuss the courses of action which may then be open to him. Schedule 10 to the Act sets out a list of criminal offences which may be committed by company officers,[75] and Sch 24 to the Companies Act 1985 contained a further list.[76] This is in addition to the specific duty of the Official Receiver in a compulsory winding up to investigate the affairs of the company generally.[77]

6.29 The role of the Official Receiver was described by Lord Millett in *Re Pantmaenog Timber Ltd, Official Receiver v Wadge Rapps and Hunt*:[78]

71 IA 1986, s 81.
72 *Re City of Glasgow Bank; Buchan's Case* (1879) 4 App Cas 583; *Re Cheshire Banking Co; Duff's Executors Case* (1885) 32 ChD 301.
73 IA 1986, s 82.
74 See 6.29.
75 This is very similar in its form to Sch 24 to CA 1985, which schedule has not been repeated in CA 2006.
76 There is no such corresponding useful list in the Companies Act 2006.
77 IA 1986, s 132.
78 [2003] UKHL 49.

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- The landlords challenged this on the basis of unfair prejudice.

8.256 Etherton J held that because a company voluntary arrangement is an arrangement of a company's affairs, it could only operate between the company and its creditors. It could not affect third party obligations.[373]

8.257 It was held that the company voluntary arrangement was unfairly prejudicial and should therefore be set aside. The guarantees had real value. They would otherwise have been enforceable. Anything resulting in the creditors receiving less than their complete entitlement must of its nature be unfairly prejudicial in these circumstances.

OTHER COMPROMISES AND ARRANGEMENTS

8.258 Under company legislation, a company can enter into a binding compromise or arrangement with its creditors or members or any class of either under *a scheme of arrangement approved by the court* and by a majority in number representing three-fourths in value of those affected.[374]

8.259 Under insolvency legislation a voluntary liquidator may make compromises or arrangements with the sanction of an extraordinary resolution of the company in a member's winding up or consent of the court, or the liquidation committee (or, if none, the creditors) in a creditors' winding up.[375] The same power is enjoyed by a compulsory liquidator but under a different statutory provision.[376]

[373] A similar decision was reached in *Morant & Co Trustees Ltd, Mourant Property Trustees Ltd v Sixty UK Ltd* [2010] EWHC 1890 (Ch), a case concerning a proposed voluntary arrangement following the administration of the insolvent company.
[374] CA 2006, s 895, formerly CA 1985, s 425.
[375] IA 1986, s 165.
[376] IA 1986, s 167.

CHAPTER 9

THE LIQUIDATION COMMITTEE AND MEETINGS

MEMBERS' WINDING UP

9.1 In a members' winding up, control remains in the hands of the members; there are no meetings of creditors except under s 95 where the members' voluntary liquidator forms the opinion that the company will be unable to pay its debts within the period stated in the directors' declaration of solvency (see Chapter 2) since the directors state that all creditors will be paid in full and no liquidation committee is appointed.

9.2 The wishes of the members are ascertained in general meetings summoned in the manner required by the company's articles of association or CA 2006, s 308.

9.3 The liquidator can call such meetings at any time (s 165(4)(c)) and must call one for the following purposes:

(1) To fix the remuneration of the liquidator (ordinary resolution). Section 91 of the Act, unlike its predecessor, CA 1985, s 580, does not refer to the fixing of remuneration by the general meeting but r 4.148A now gives authority to the general meeting to fix the basis of the remuneration on the same lines as in a creditors' winding up, namely:
   (a) as a percentage of realisations and/or distributions; or
   (b) by reference to time properly expended by the insolvency practitioner and his staff; or
   (c) as a set amount.

   Different bases may be fixed for different things done by the liquidator.[1] If not fixed as above, the basis of the liquidator's remuneration shall be fixed by the court following an application by the liquidator. However, such an application cannot be made unless the liquidator has first sought to have the remuneration fixed by the members, and in any event cannot be made more than 18 months after the liquidator's appointment.[2] Further, if the liquidator regards the basis of the remuneration fixed by the company in general meeting to be insufficient or inappropriate, he may apply to the court for an order changing it or increasing its amount or

[1] IR 1986, r 4.148A(2A).
[2] IR 1986, r 4.148A(4).

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rate.[3] Members of the company with at least 10% of the total voting rights of all the members having a right to vote at general meetings, or any member with the permission of the court, may apply to the court for one or more of the following orders:

- a reduction of the amount of remuneration the liquidator is entitled to charge;
- the fixing of the basis of remuneration at a reduced rate or amount;
- a change in the basis of remuneration;
- that some or all of the remuneration or expenses be not treated as expenses of the liquidation;
- that the liquidator or his personal representative should repay to the company any excess of remuneration or expenses as the court might specify.[4]

Such an application can be made where if the applicant(s) is/are of opinion that the remuneration charged by the liquidator, or his expenses, or the basis of his remuneration is in all the circumstances excessive.[5] Such an application must generally be made no later than 8 weeks after the applicant has received notification of the liquidator's remuneration; this reduces to 4 weeks where the liquidator has resigned in accordance with r 4.142.[6] Unless otherwise ordered by the court, the costs of such application should be paid by the applicant and not be payable as an expense of the liquidation.[7]

Where a new liquidator is appointed in place of another, any determination or court order regarding the remuneration of the previous liquidator continues to apply in respect of the remuneration of the new liquidator until some further determination or court order is made.[8]

(2) To fill a vacancy in the office of liquidator.[9] The section provides that for the purpose of filling the vacancy a general meeting should be convened and held 'in manner provided by this Act'. The draftsman obviously bungled on this point since there is no provision in the Insolvency Act as to the holding of a meeting in a members' voluntary winding up. The reference should plainly have been to the Companies Act. Now see Part 13 of the Companies Act 2006.

(3) To pay any class of creditors in full or to make compromises with creditors or persons claiming to be creditors.[10]

(4) To sell the whole or part of the company's business in exchange for shares in the acquiring company for distribution among the members of the company (special resolution required).[11]

3 IR 1986, r 4.148A(6).
4 IR 1986, r 4.148C(6).
5 IR 1986, r 4.148C(1).
6 IR 1986, r 4.148C(2).
7 IR 1986, r 4.148C(7).
8 IR 1986, r 4.148D.
9 IA 1986, s 92.
10 IA 1986, s 165(2), Sch 4, Part 1.
11 IA 1986, s 110.

(5) In the event of the winding up continuing for more than 1 year, within two months of the end of the year and of each succeeding year to send to the members and such other persons as might be prescribed[12] a progress report.[13] Failure to comply with this provision renders the liquidator liable to a fine on summary conviction. The previous requirement to summon annual meetings has now been removed for England and Wales though it remains for Scottish liquidations.[14]

(6) As soon as the company's affairs are fully wound up, to lay before the general meeting an account of the winding up showing how it has been conducted and the company's property has been disposed of.[15] Again, failure to comply with this provision can result in a fine on summary conviction.

9.4 Where there has been an arrangement under s 110 and a distribution to members has taken place pursuant to s 110(2) or (4) (distribution of shares, policies or other like interests) the liquidator must in any account or report set out details of any property transferred during the period to which the account or report relates and provide details of the basis of the valuation.[16]

CREDITORS' WINDING UP AND COMPULSORY WINDING UP

Appointment of liquidation committee

9.5 In a creditors' winding up, control passes to the creditors and their nominees.

The creditors at their first meeting, which must be called within 14 days of the general meeting for the purpose of putting the company into liquidation, or at any subsequent meeting have power to appoint a liquidation committee of up to five persons. The members at their winding-up meeting or any subsequent general meeting may nominate up to a further five persons to the committee. The creditors may, however, exclude all or any of the company's nominees unless the court otherwise directs.[17] On an application by a rejected nominee, the court may select a substitute as an alternative to the applicant.

9.6 In a compulsory liquidation the Official Receiver must decide whether to call separate meetings of creditors and contributories to appoint a liquidator and to determine whether a liquidation committee should be established. If the

12 These other prescribed persons are the creditors and the Registrar of Companies: IR 1986, r 4.49C(6). It might, incidentally, be noticed that the creditors are not actually prescribed in the legislation but r 4.49C(6) works on the assumption that they have been prescribed!
13 IA 1986, s 92A.
14 IA 1986, s 93.
15 IA 1986, s 94.
16 I(A)R 2010, Sch 1, para 174.
17 IA 1986, s 101.

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winding-up order is on the ground of the company's inability to pay its debts, the committee will consist of three, four or five members appointed by the creditors' meeting.[18] The constitution of the committee is laid down in r 4.152 and it is interesting to note that in this case there is no right for a member of the company to be a member of the committee. If the winding-up order is made on grounds other than the insolvency of the company the committee will consist of three, four or five creditors appointed by the creditors and not more than three contributories appointed at the meeting of the contributories. By s 167(1), the functions of the committee are to supervise the conduct of the winding up by the liquidator and to consent to the exercise of certain of the liquidator's powers. While the committee may obviously express its wishes in regard to matters arising in the course of the liquidation, there is no obligation on the liquidator to do as the committee requires.

9.7 In practice, the liquidator will usually want to see a liquidation committee appointed as otherwise he will have to convene general meetings of the creditors to exercise powers which the committee could have exercised.[19] The object of appointing a liquidation committee is to provide a representative body to assist and supervise the liquidator, to receive periodic and other reports from him and to give or withhold its consent to the exercise of certain of his powers. It is thought that with the abolition of Crown preference, the tax authorities may in future show a greater presence on liquidation committees.

9.8 The liquidation committee must have at least three members before it can be established. The maximum number of creditor members is five. Creditors who have not lodged a proof of debt, or whose proof has been wholly disallowed for voting purposes or wholly rejected for distribution purposes or whose debts are fully secured are not eligible for membership. No person can be a member both as a creditor and a contributory. A body corporate may be a member but must act through a representative.[20]

9.9 The committee does not come into being and cannot act until the liquidator issues a certificate of its due constitution (if the chairman of the creditors' meeting is not the liquidator, he must give notice of the resolution to the liquidator and inform him of the names and addresses of the elected persons).[21] In practice, the appointment of any members' representatives will take place at the general meeting to put the company into liquidation in anticipation that the creditors at their first meeting will resolve on a liquidation committee.

9.10 No person may act as a member of the committee unless he has agreed to do so.[22] Usually, the liquidator issues a single certificate after both the creditors' and any members' representatives have been appointed, but he may not do so

[18] IA 1986, ss 136 and 141.
[19] IA 1986, ss 165(2) and 167.
[20] IR 1986, r 4.152.
[21] IR 1986, r 4.153.
[22] IR 1986, r 4.153(3).

until three (eligible) persons have agreed to act and been duly appointed. An amended certificate must be issued as and when there is any change in the constitution of the committee (for form of certificate,[23] see Form 4.47 in Appendix 2).

9.11 The certificate and any amended certificate must be forwarded by the liquidator as soon as reasonably practicable to the Registrar of Companies, as must notification of any change in the committee's membership[24] (Forms 4.48, 4.49 in Appendix 2).[25]

9.12 In the case of a compulsory winding up, a liquidation committee has no function so long as the Official Receiver is the liquidator. For this reason the establishment of such a committee does not have to be considered unless and until the Official Receiver decides, within the 12-week period allowed by s 136, to summon meetings of creditors and contributories to consider whether to appoint some other liquidator. If the creditors' meeting called under s 141 does not decide that a liquidation committee should be established then it is still possible that the meeting of the contributories may appoint one of their number to apply to the court for an order that the liquidator should summon a further creditors' meeting for the purpose of establishing a liquidation committee.[26] The court may make such an order if it thinks that there are special circumstances to justify it.[27] If the creditors' meeting so summoned does not establish a liquidation committee then a meeting of contributories may do so, in which case the committee will consist of three, four or five contributories elected at that meeting.[28]

9.13 The liquidator must report to the committee on all matters which he or the committee consider to be of concern in the winding up. However, he need not comply with any request where he considers it frivolous or unreasonable or where the cost of complying would be excessive, or when the company's resources are insufficient to enable him to comply.[29]

9.14 Where the committee has come into being more than 28 days after the appointment of the liquidator he must report in summary form on the actions he has taken since appointment and must answer their questions regarding the conduct of the winding up.[30]

9.15 As and when directed by the liquidation committee and otherwise once every 6 months, the liquidator must also send a written report to the committee

[23] IR 1986, r 4.153(4).
[24] IR 1986, r 4.153(6).
[25] IR 1986, r 4.153.
[26] IR 1986, r 4.154(2).
[27] IR 1986, r 4.154(2)(a).
[28] IR 1986, r 4.154(4).
[29] IR 1986, r 4.155.
[30] IR 1986, r 4.155.

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members as to the progress of the winding up and any matters arising. Such a request for a report may not be made by the committee more than once in any 2-month period.[31]

9.16 Proceedings of the liquidation committee are governed by rr 4.156 to 4.169:

(1) It meets as and when determined by the liquidator who must call a first meeting within 6 weeks of his appointment or of the committee's establishment (whichever is the later). Thereafter, the liquidator must call a meeting within 21 days of request by a creditor member or his representative and also for any specific date if the committee have so resolved.[32]

(2) The liquidator must be given 5 business days' written notice of the venue of the meeting to each committee member unless that member waives this request.[33] Waiver may be signified either at or before the meeting.

(3) The liquidator or an experienced employee or an insolvency practitioner appointed by the liquidator in writing must chair the meetings of the committee.[34] In the case of the appointment of an insolvency practitioner, he must be qualified to act in relation to the company.[35]

(4) A meeting is properly constituted if due notice of it has been given to all its members and at least two creditor members are present or represented.[36] However, in the case of a members' voluntary winding up, the requirement is simply for two members.

(5) At a meeting of the committee each member of the committee present or his representative has one vote. A majority of those present or represented must vote in favour of a resolution if it is to be passed.[37] The chairman has no vote. Members of the committee who are either themselves contributories or represent contributories may vote and their votes should be recorded. However, their votes do not count in determining whether a resolution has been passed unless either the creditors have not appointed any members of the committee to represent them or, alternatively, the liquidator has certified that the company has paid all its debts and liabilities in full whereupon the creditors' representatives cease to be members of the committee.[38] In either of these situations a resolution is passed if it has the support of the majority of the members of the liquidation committee representing contributories.

31 IR 1986, r 4.168.
32 IR 1986, r 4.156.
33 IR 1986, r 4.156.
34 IR 1986, r 4.157.
35 IR 1986, r 4.157(2)(a).
36 IR 1986, r 4.158(2).
37 IR 1986, r 4.166.
38 IR 1986, rr 4.165 and 4.171(8).

(6) It is possible to avoid meetings if written resolutions are signed by a majority of committee members. The liquidator must send to every member or his designated representative a copy of the proposed resolution.[39]
If there is more than one proposed resolution, they must be set out in such a way that agreement or dissent can be indicated separately on each one. Unless any member of the committee, within 7 business days of the sending out of the resolution, requires the liquidator to summon a committee meeting, the resolution is deemed passed if and when the liquidator is so notified in writing by a majority of the members of the committee.[40]

(7) Every resolution passed must be recorded in writing either separately or as part of the minutes, signed by the chairman and kept with the liquidator's records.[41] In the case of resolutions otherwise than at a meeting, there must be a note attached to the record that the committee's concurrence was obtained.[42]

(8) A member of the committee may be represented by another person. No member may be represented by:
- another member of the committee;
- a person who is at the same time representing another member;
- a body corporate;
- an undischarged bankrupt or a person in relation to whom a moratorium period under a debt relief order applies;
- a disqualified director; or
- a person subject to a bankruptcy restrictions order or undertaking, or a debt relief restrictions order or undertaking.[43]

A person acting as a representative must hold a letter of authority, signed by or on behalf of the committee member which may be either general or specific. The chairman of a meeting may request production of the letter of authority and may exclude the holder if the authority is deficient. Where any document is signed on a member's behalf by his representative, he must state this *below* his signature.[44]

(9) A member vacates office if he resigns by notice in writing delivered to the liquidator if he becomes bankrupt or compounds or arranges with his creditors, if he or his representatives is absent from three consecutive meetings unless otherwise resolved by the committee or if a creditor member ceases to be a creditor or is found never to have been a creditor. On a member's bankruptcy his trustee in bankruptcy replaces him as a member.[45]

39 IR 1986, r 4.167.
40 IR 1986, r 4.167.
41 IR 1986, r 4.165(4).
42 IR 1986, r 4.167.
43 IR 1986, r 4.159(4).
44 IR 1986, r 4.159.
45 IR 1986, rr 4.160 and 4.161.

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(10) A creditor member of the committee may be removed by resolution at a meeting of creditors (and a contributory member may be removed by a resolution at a meeting of contributories). Fourteen days' notice of the intention to move the resolution must be given.[46]

(11) If a vacancy occurs among the creditor members and there are at least three remaining creditor members, the liquidator and a majority of creditor members may agree not to fill the vacancy. The liquidator may appoint any qualified creditor to fill the vacancy if that person consents and a majority of creditor members agree. Alternatively, a meeting of creditors (to whom 14 days' notice of the meeting stating the intention to make an appointment has been given) may appoint, provided again that the person concerned consents.[47] If there is a vacancy among the contributory members, broadly similar provisions apply. However, the creditor members may object to the appointment and (unless the court otherwise directs) that person may not be appointed a member of the committee.[48]

9.17 Rule 4.170 restricts the ability of a member of the committee or his representative, any associate of either of them (for associates, see 5.86), or any person who has within the previous 12 months been a committee member from:

(a) receiving out of the company's assets any payment for services given or goods supplied in connection with the administration (of the winding up);
(b) obtaining any profit from the administration; and
(c) acquiring any of the estate's (ie the company's) assets.

9.18 This is because the object of the liquidation committee is to protect the interests of the creditors and contributories of the company which is in liquidation. These restrictions, however, do not apply if the prior sanction of the court is obtained or the liquidation committee permits so long as it is satisfied, after full disclosure, that the member concerned will be giving full value in the transaction.[49] It is suggested that any liquidation committee which is faced with an offer from one of its members should consider very carefully the possibility of looking elsewhere. No member or representative who is interested may vote on the resolution to sanction such a transaction. The leave of the court may subsequently be obtained if a member has entered into a transaction as a matter of urgency or by way of a pre-liquidation contract provided he has applied for the court's leave without delay. The cost of an application for leave is not payable out of the company's assets unless the court so orders.[50] The court may set aside a prohibited transaction or make any other order it thinks fit including ordering the person to account for any profits he has made from the transaction. If the court is satisfied that a member's associate

[46] IR 1986, r 4.162.
[47] IR 1986, r 4.163.
[48] IR 1986, r 4.164.
[49] IR 1986, r 4.170(3).
[50] IR 1986, r 4.170(7).

or representative entered into a transaction without having any reason to suppose that he was breaching r 4.170, it should not make an order against him.[51]

9.19 The liquidator may defray the reasonable travelling expenses of members and representatives in respect of their attendance at the committee's meetings or otherwise on the committee's business.[52]

9.20 Since a creditor's membership of the liquidation committee automatically ceases on his ceasing to be a creditor, his membership terminates when the liquidator pays what is due to him.[53]

9.21 Where the creditors have been paid in full with interest in accordance with s 189, the liquidator must issue a certificate to that effect and send notification of this together with a copy of the certificate to the Registrar of Companies.[54] On such a certificate being issued, the creditor members of the committee cease to be members, though the committee continues in existence unless the contributories decide to abolish it or membership falls below three.[55]

9.22 The powers of the liquidation committee in a creditors' winding up are as follows:

(1) to have access to the liquidator's records;[56]
(2) to fix the basis of the liquidator's remuneration;[57]
(3) to sanction the continuance of the directors' powers;[58]
(4) to sanction the payment of any class of creditors in full or to compromise with creditors, members or other debtors;[59]
(5) to sanction the acceptance of shares, policies or other like interests in the transferee company as consideration for the sale of the company's property;[60] and
(6) to sanction the entering into of a transaction with a connected person (see 5.86).[61]

9.23 Where there is no liquidation committee on a voluntary winding up, the above powers are generally exercisable by the creditors as a body, except that in the case of (4) the creditors or the court can act. In the case of (5) and (6) also, the court may sanction such a transaction.

[51] IR 1986, r 4.170(6).
[52] IR 1986, r 4.169.
[53] IR 1986, r 4.161.
[54] IR 1986, r 4.171A(1).
[55] IR 1986, r 4.171(A)(3).
[56] IR 1986, r 4 4.155(5).
[57] IR 1986, r 4.127(3).
[58] IA 1986, s 103.
[59] IA 1986, s 165(2) and Sch 4, Part I.
[60] IA 1986, s 110.
[61] IR 1986, r 4.170.

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CHAPTER 14

THE ADMINISTRATION PROCEDURE

INTRODUCTION

14.1 Administration was introduced as a regime in corporate insolvency by Part II of the Insolvency Act 1986. The theory was that the assets of an insolvent company should be ring-fenced while an administrator sought a resolution of the company's problems without its having actually to slide into an insolvent liquidation. However, it is probably true to say that the regime never really became widely accepted because of a number of deficiencies. First, the directors of a company seeking an administration had to give notice of this to any person entitled to appoint an administrative receiver of the company, in other words the company's bank.[1] This person then had 5 days to appoint an administrative receiver,[2] and such an appointment would effectively trump the application for an administration order, because if an administration application was heard at a time when there was already an administrative receiver in post, the administration application would automatically fail unless the administrative receiver vacated office.[3] And why should the bank do this? Why should it allow in an administrator appointed by the court when it could appoint its own administrative receiver? Secondly, the administration tended to be expensive and accordingly not available in practical terms for smaller companies. Thirdly, it was a cumbersome procedure. The result was that for many companies their only option was either to move directly into liquidation or else consider a CVA which until the implementation of the Insolvency Act 2000 did not carry with it a ring-fencing moratorium enjoyed in administrations.

14.2 At the same time, the administrative receiver has to be seen for what he was. His appointment was essentially contractual. The contract was contained in the debenture and the facility agreement. These documents would state how the loan had to be serviced, when interest had to be paid and when capital had to be repaid. They would also state the lender's rights in the event of default by the company – the appointment of a receiver, or where he took control of the whole or substantially the whole of the undertaking of the company, an administrative receiver.[4] The problem with the contractually appointed receiver is that having paid back the secured creditor, he has to vacate office because

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1 IA 1986, s 9(2).
2 IA 1986, s 10(2) (now repealed).
3 IA 1986, s 10(3) (now repealed).
4 IA 1986, s 29(2).

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there is no reason for his existence. Therefore the level of duty owed to the unsecured creditors and even more so to the members was minimal. It was not completely non-existent but it was certainly not substantial.[5]

14.3 It was therefore extremely welcome that in general terms the enforcement of floating charges created on or after 15 September 2003 should be by the appointment of an administrator rather than the appointment of an administrative receiver. The administrator is essentially a statutory appointment rather than a contractual one, and the administrator now has duties which he owes expressly to the company.

PRE-PACKAGED ADMINISTRATIONS

14.4 However, the changes which will now be examined in detail have not been without some controversy. In particular, and as will be seen, there have been five changes to insolvency and corporate law over recent years, each of which viewed separately is quite innocuous, but which looked at cumulatively have resulted in pre-packaged administrations which do sometimes allow the directors of a failing company to leave the company's creditors carrying its debts while the directors are able to walk away from the company taking its business with it. These will be considered over the following pages.

14.5 The five changes to look out for are:

(1) the purpose of the administration;
(2) the manner of appointment;
(3) the dispensing with the creditors' meeting in certain situations;
(4) substantial property transactions; and
(5) exceptions from the phoenix syndrome prohibitions.

These will be identified during the process of considering administrations generally.

WHAT IS ADMINISTRATION?

14.6 Administration is a collective insolvency procedure with one, albeit hierarchical, purpose, namely:

- the rescue of the company as a going concern;
  if that is not reasonably practicable, the administrator may pursue the secondary objective of
- achieving a better result for creditors than would be achieved on a formal winding up;

[5] See eg *Medforth v Blake* [1999] 3 All ER 97.

  and, failing that, the third objective of
- realising assets to make a distribution to secured or preferential creditors.[6]

14.7 There is here a significant change from the previous regime as envisaged in the Insolvency Act 1986 as enacted where the court for one or more purposes. The original choice of purposes is now replaced by what the head-note describes as the 'purpose'. The use of the word in the singular is, however, unhelpful. It would probably be better to call it a 'hierarchy of purposes'. Under the new regime there is, at least in theory, a seemingly greater emphasis on company rescue. Ideally the administration should achieve the survival of the company in whole or in part; failing this there should be a better realisation than would be achieved on a formal winding up; and if this is not possible, then at least there should be an attempt to make a distribution to the secured and/or the preferential creditors.

14.8 The preferential creditors now include arrears of salary for employees of up to £800, accrued holiday pay and payments to occupational pension schemes.[7] Crown debts are no longer preferential.

THE PURPOSE IN MORE DETAIL

14.9 The use of the expression 'rescuing the company as a going concern' is in marked contrast to the words previously used: 'the survival of the company in whole or in part, and the whole or any part of its undertaking, as a going concern'.[8] In *Re Rowbotham Baxter Ltd*,[9] Harman J explained that this required the survival of the company together with all or part of its undertaking as a going concern. Accordingly the learned judge found that this could not be achieved through a hiving down of part of the business into a new company. It is suggested that the wording of the first of the hierarchy of purposes should be read in the same way as the former s 8(3)(a) and that the approach adopted in *Re Rowbotham Baxter Ltd* is equally applicable to the current terminology. This is confirmed in the DBIS's Explanatory Notes which accompany the Enterprise Act which refer rescuing 'the company and as much of its business as possible'.[10] However, there seems little doubt hiving down would fall within the former fourth alternative ground for an administration order, namely 'a more advantageous of the company's assets than would be effected on a winding up'.[11] It could therefore be argued that this interpretation makes it easier for the administrator to form the view that he cannot achieve the rescue of the company as a going concern and so move on to the second of the hierarchy of purposes, 'achieving a better result for the company's creditors as a whole than

[6] IA 1986, Sch B1, para 3.
[7] IA 1986, Sch 6.
[8] IA 1986, s 8(3)(a) (now repealed).
[9] [1990] BCC 113.
[10] Explanatory Notes, para 647.
[11] IA 1986, s 8(3)(d) (now repealed).

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would be likely if the company were wound up'. This argument, if correct, makes pre-packaged administrations justifiable under the new administration regime.

14.10 The DBIS gives an example of the better realisation purpose in its Explanatory Notes.[12] A company has both good products and a sound customer base. However, its machinery is out of date and its debts and overheads have been rising for some time. An administrator has been appointed and the administrator feels that: (a) there are insufficient funds to either continue the business or to purchase the necessary replacement machinery; and (b) a break-up sale of its assets would realise less than would the sale of the business as a going concern. He markets the business and with the best offer received could pay off the secured creditors completely and still have sufficient left to pay a dividend of 40p in the £ to the unsecured creditors.

14.11 An example of the third of the hierarchical purposes is again to be found in the Explanatory Notes.[13] A company running a service industry has previously enjoyed a good reputation as a result of the standard and quality of its customer service. However, recently a number of key staff have left the company with the result that its customer service has seriously deteriorated. So far has its reputation suffered that it can no longer able either to attract or even to retain business. After some months of heavy loss-making, the company is now unable to pay its debts. The company is placed in administration. The administrator takes the view that the business is not viable and that a sale of the business cannot be achieved. Accordingly he markets the assets with the result that sufficient funds are available to make a part payment to the secured creditors but nothing for the unsecured creditors other than what will go to them as a result of the ring-fencing under s 176A.[14]

14.12 The hierarchical purpose of the administration was considered recently in *Bank of Scotland v Targetfollow Properties Holdings Ltd*.[15] Targetfollow was a company in a group involved in property investment and development. Together with a some subsidiaries it owned properties worth over £250m. It owed the bank £233m made up of a 3-year loan of £190m and £43m under a guarantee of the liabilities of an associated company. The loan facility, which was secured by a floating charge over Targetfollow's undertaking and assets, terminated in 2010 when a payment of £89m became due. Targetfollow did not make this payment thus defaulting under the loan agreement and entitling the bank to appoint an administrator. The bank could have made an out-of-court appointment, but because another secured creditor was threatening to challenge such an appointment on the ground of its alleged failure to follow a prescribed consultation procedure set out in an inter-creditor deed, it elected to apply to the court for the appointment.

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12 Explanatory Notes, para 650.
13 Explanatory Notes, para 651.
14 IA 1986, s 176A.
15 [2010] EWHC 3606 (Ch).

14.13 Two requirements had to be satisfied for the court to be able to make an appointment. First, the company had to be unable to pay its debts. There was no dispute that this was the case. Secondly, the administration order had to be reasonably likely to ensure that the purpose of the administration would be achieved. The application for the order was opposed on the ground that the statutory purpose could not be achieved. This was because an administration would considerably reduce the value of Targetfollow's assets at a time when negotiations with the company's creditors might well allow the continuation of the company as a going concern, something which evidence showed could not be established by an administrator. Further, Targetfollow wanted to pursue certain claims against the bank which would be stifled by an administration order.

14.14 In spite of these objections the court was nevertheless prepared to make the administration order. There was no guarantee that the bank would continue to fund Targetfollow nor that it would agree to any restructuring. Indeed, the possibility of a restructuring outside an administration was almost non-existent. On the other hand, there was a real prospect that an administration would give a better result for the creditors than would be achieved on a winding up. Moreover, while it was impossible to reach a conclusion in regard to the alleged claims against the bank, any such claim that might exist would be insubstantial in comparison with what Targetfollow owed to the bank. Taking everything into account, there was no reason not to make the appointment of an administrator given that all parties involved had a common interest in achieving the best realisation of the assets. In this regard an administrator had a duty to act in the interests of the company's creditors as a whole as well as being subject to his own professional responsibilities. This affords an excellent example of the factors which the court will take into account in making an administration order.

14.15 In *Re Logitext UK Ltd*,[16] an insolvent and non-trading company had no assets other than some causes of action for matters such as undervalue transactions and breach of duty by directors. A substantial creditor was willing substantially to fund these actions so long as they were brought by an administrator so as to produce a better realisation of the assets than would be achieved on a formal winding up. He was not willing to fund a liquidator in this way. Lindsay J made an administration order.

ADMINISTRATIONS AND OTHER INSOLVENCY PROCEDURES

14.16 Administration should not be confused with:

- Liquidation

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16 [2004] EWHC 2899 (Ch).

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This is the winding up of a company, with its assets being got in by a liquidator, its debts being paid (so far as there are assets available to do so), and the company ultimately being dissolved.

- Administrative receivership
  This, as has been said, is a contractual appointment by the holder of a floating charge with the administrative receiver seeking to pay back his appointor and then vacating office.
- Law of Property Act 1925 (non-administrative) receivership
  This is an extra-judicial appointment made by a mortgagee in the event of default by a mortgagee.[17]
- Company voluntary arrangement (CVA)
  This is an arrangement which binds all the creditors of the company on a positive vote of three-quarters in value of those creditors who vote at the meeting to approve it and which is intended to achieve the survival of the company.

TERMINOLOGY USED

14.17 The word 'administrator' is used to describe a person appointed under Sch B1 to the Insolvency Act 1986 to manage the company's affairs, business and property.[18]

14.18 A company 'enters administration' when the appointment of an administrator takes effect.[19] So long as this appointment has effect, the company is said to be 'in administration'.[20] It ceases to be in administration when the appointment of an administrator ceases to have effect.[21] However, the company does not cease to be in administration merely because no administrator is in office whether because of resignation, death, removal from office or any other cause (such as, perhaps, debilitating illness).[22]

14.19 There appear to be seven instances where the appointment of an administrator 'ceases to have effect':

(1) at the end of one year beginning with the date on which the appointment takes effect (unless there has been a permitted extension);[23]
(2) by order of the court following an application by an administrator;[24]

17 LPA 1925, s 101 et seq.
18 IA 1986, Sch B1, para 1(1).
19 IA 1986, Sch B1, para 1(2)(b).
20 IA 1986, Sch B1, para 1(2)(a).
21 IA 1986, Sch B1, para 1(2)(c).
22 IA 1986, Sch B1, para 1(2)(d).
23 IA 1986, Sch B1, para 76(1).
24 IA 1986, Sch B1, para 79(1).

(3) when the administrator files a notice in the prescribed form with the court and with the Registrar of Companies that he believes that the purpose of the administration has been sufficiently achieved;[25]
(4) by order of the court following an application by a creditor of the company;[26]
(5) by order of the court following an application for the winding up in the public interest of a company which is in administration;[27]
(6) when the administrator files a notice with the court and with the Registrar of Companies, and sends a notice to the creditors, that the company should be wound up as if a resolution for voluntary winding up under s 84 were passed on the day on which the notice is registered;[28] and
(7) when the administrator files a notice with the court and with the Registrar of Companies, and sends a notice to the creditors, that the company should dissolved on the ground that that the company has no property which might permit a distribution to its creditors.[29]

GENERAL DUTIES OF THE ADMINISTRATOR

14.20 An administrator must perform his functions in the interests of the creditors as a whole, and where he seeks to recover something for the preferential and/or secured creditors he must not unnecessarily harm the interests of the creditors of the company as a whole.[30] This highlights the distinction between receivers and administrators noted above. While the receiver owes his duties primarily to the secured and preferential creditors and is under no general duty to carry on the business of the company, the administrator's role is far more collective. He must act so as to show regard to the interests of the company's creditors as a whole. Indeed in looking at the prioritised purpose of the administration[31] the interests of the secured and preferential creditors come last. As noted below, a creditor has locus standi to apply to the court on the ground that the administrator has acted in a manner such as unfairly to harm his (the creditor's) interests.[32] Moreover, it is to be observed that this duty is owed regardless of the manner of his appointment, even where he is appointed by the holder of a qualifying floating charge.[33]

14.21 He must also act as quickly and efficiently as is reasonably practicable.[34] It has to be said that this is rather vague and it might be questionable whether

25 IA 1986, Sch B1, para 80(3).
26 IA 1986, Sch B1, para 81(1).
27 IA 1986, Sch B1, para 82(3).
28 IA 1986, Sch B1, para 83(6).
29 IA 1986, Sch B1, para 83(4).
30 IA 1986, Sch B1, para 3(2) and (4).
31 IA 1986, Sch B1, para 3(1).
32 IA 1986, Sch B1, para 74.
33 IA 1986, Sch B1, para 14.
34 IA 1986, Sch B1, para 4.

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it adds anything to any duties previously owed by administrators at common law. It does, however, tie in with the time restrictions imposed on the administrator under the new regime.[35]

14.22 A reasonable prospect of selling the company's business and assets, whether or not the sale is effected under a 'pre-packaged administration' (see below), is frequently used as justification of administration to achieve the secondary objective of a better realisation for creditors than would be achieved in a winding up.

14.23 Even though a sale of business and assets may be achieved by putting the company into creditors' voluntary liquidation, it is sometimes considered to be quicker and easier to control such a sale by putting the company into administration.

14.24 The advantage of an administration over a winding up when seeking to achieve a better realisation of the assets than would be achieved on a formal winding up is well illustrated by the facts of *Re Consumer & Industrial Press Ltd*, one of the early cases on administrations under the regime envisaged by the Insolvency Act 1986 as originally enacted.

Re Consumer & Industrial Press Ltd[36]

14.25 The company was a small printing and publishing house. It was heavily insolvent. Its only asset of value was the magazine title 'Pins and Needles'. As will be seen an administrator has power, like an administrative receiver, to borrow so as to continue the business of the company. An administration order was granted so that the administrator could continue publishing the magazine so that he could sell the title as a going concern. In other words, he would achieve a more advantageous realisation of the company's assets than would be achieved on a formal winding up.

14.26 It is generally accepted in the insolvency world that administration to achieve the sale of a business is justified. However, it must always be borne in mind that there may be cases in which the advantage creditors may achieve from a sale out of administration over those which may be achieved from a sale out of creditors' voluntary liquidation are marginal.

THE ADMINISTRATOR

14.27 From the date of appointment, the affairs of the company are managed by an administrator, who must be a licensed insolvency practitioner.[37] The administrator is an officer of the court regardless of how he is appointed.

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35 IA 1986, Sch B1, paras 76–78.
36 [1988] 4 BCC 68.
37 IA 1986, Sch B1, para 6 and see also ss 388(1)(a) and 390.

14.28 Except in cases where there is some form of special relationship between a claimant and an administrator, there is no general common law duty of care owed to the unsecured creditors in the conduct of an administration. This point was considered by the court in *Charalambous v B & C Associates*.[38] Ms Connor was the administrator of Henry Charles Ltd and a partner in B & C Associates. A secured loan had been made to Henry Charles Ltd by Hickory Holdings Ltd. Mrs Charalambous' husband had been the managing director of Henry Charles Ltd. The children of Mr and Mrs Charalambous, Bradley and Tallyia-Marie were the beneficiaries of a trust fund which owned Hickory Holdings Ltd. After the administration of Henry Charles Ltd had commenced Mr Charalambous commenced divorce proceedings. Because he had no assets, Mrs Charalambous was unable to receive any financial provision in ancillary relief proceedings. However, it was anticipated that the children would benefit from the disposal of the assets of Henry Charles Ltd in consequence of the hoped for repayment of the secured loan to Hickory Holdings Ltd, thereby benefiting the trust of which the children were beneficiaries. However, the administration resulted in no payment for the creditors of Henry Charles Ltd.

14.29 Mrs Charalambous commenced proceedings on behalf of herself and the children against Ms Connor, claiming negligence and wrongful misappropriation in the administration. Ms Connor and the partnership sought a striking out on the ground that it disclosed no cause of action and that it had no reasonable prospect of success, the reason being that no duty of care was owed in tort by an administrator to the unsecured creditors. Moreover, the children were no more than the beneficiaries of a trust which happened to own a company which was itself in turn a creditor with the result that there was no special relationship between the parties.

14.30 HHJ Michael Furness held that there was indeed no evidence of a special relationship between the administrator and Mrs Charalambous or the children and for this reason no duty of care was owed. The mere knowledge of the administrator that Mrs Charalambous and the children need and relied on the receipt of the realisations was not of itself sufficient to create a special relationship.

14.31 This case is an extremely useful one for administrators because it clarifies what sort of duty might be owed to the unsecured creditors. Except where a special relationship exists, there is apparently no duty of care owed to unsecured creditors.

14.32 The court may remove an administrator under para 88 of Sch B1 to the Insolvency Act 1986. Interestingly the provision gives no ground on which the order for removal might be made. The removal of office-holders was considered in depth by Warren J in *Sisu Capital Fund Ltd v Tucker*:[39]

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38 [2009] EWHC 2601 (Ch).
39 [2006] BPIR 154.

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