Contentious cases

A look at the legal landmarks that have affected the profession recently and how they'll affect insolvency in 2016.

Bilta (UK) Ltd **v.** ***Nazir*** **(No 2) [2016] 1 AC 1**

Bilta is the most significant recent case on attribution of knowledge/acts of individuals to a company and the illegality defence in an insolvency context and the territorial scope of the fraudulent trading section (s213) of the Insolvency Act 1986.

Bilta and its liquidators sued various defendants after Bilta's directors (one of whom was the sole shareholder) caused it to enter into transactions generating a VAT liability of over £38m, which it could never satisfy.

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Two non-director defendants (to dishonest assistance and conspiracy claims) applied to strike out the proceedings, arguing that the illegality defence defeated Bilta's claim because Bilta could not found a claim on the illegal scheme run by the directors.

The Supreme Court held that where the company is the victim of wrongdoing by its directors, then that wrongdoing cannot be attributed to the company as a defence to a claim brought by the company's liquidator (on behalf of its creditors) against the directors, even where the directors were the only directors and shareholders of the company.

Attribution was the key issue discussed, but the Supreme Court indicated that the illegality defence needed consideration by a seven- or nine-panel court '*as soon as appropriately possible*'. Accordingly, practitioners should be aware that the proper scope of the illegality defence is a complicated and uncertain area. One can readily imagine insolvency situations where the defence might be raised (especially when liquidators are appointed over companies with a sole director/shareholder who commits fraud through the company). It may well be that the future case to which the court alluded will be an insolvency one.

Re Hampton Capital Ltd **[2015] EWHC 1905 (Ch)**

The administrators of Hampton Capital claimed to recover gratuitous dispositions from the company under the TUV provisions of the IA 1986 (s238) and restitution on the ground of unjust enrichment.

The dispositions had been ordered by an apparently plausible con-man. He did not have authority to act on behalf of the company but had instructed a director of the company to make the payments.

The judge held that the restitution claim succeeded. However, he found the application under s238 'difficult' because of questions as to the proper meaning of the term 'transaction' (defined in s436 IA 1986 as including a '*gift, agreement or arrangement*').

On the evidence, the director had never intended to make a gift when he authorised the gratuitous transfer (on instructions from the con-man). The judge said that the mere transmission of money without (i) any form of dealing or arrangement between the company and the recipient and (ii) any intention to make a gift could not constitute a 'transaction' within the section.

This is a surprising decision, given the broad terms of s238 and 436 and the range of circumstances in the Act in which the term 'transaction' is used. However, as the only recent decision on the meaning of 'transaction', it is important. Practitioners should be aware of it because it may make s238 applications less attractive in certain factual circumstances: restitution may be the preferred route to recovery.

Section 236 is an important tool for office-holders. It allows them to ask the court to order those with information about a company's affairs to appear before the court and be examined.

Oraki **v.** ***Bramston*** **[2015] EWHC 2046**

This was an unusual claim where bankruptcy orders against a husband and wife had been annulled subject to conditions on the ground that they should not have been made. The Orakis claimed that the erstwhile trustee in bankruptcy had mismanaged their estates; they said he owed them a common law duty of care that extended beyond the statutory duty to the estates (s304 IA 1986), in a situation where it was obvious that there was going to be a surplus and readily available cash. The court concluded that the trustee did not owe them a duty of care and that, even if he

did, any claim in negligence would have expired when the trustee got his release under s299 IA 1986.

The case is a rare example of the court scrutinising the duties owed by trustees to bankrupts; it is now under appeal and so is one to watch for in the coming year.

Vizcaya Partners Limited v. *Picard* [2016] UKPC 5

In this Gibraltarian appeal the Privy Council considered the rule that a foreign default judgment is enforceable against a judgment debtor who has made a prior submission to the foreign court's jurisdiction, and particularly whether that submission had to be express or implied. The relevant foreign court was the New York Bankruptcy Court: a jurisdiction not amenable to the Brussels or Hague Convention regimes. The board decided that the question of whether there has been a submission to the jurisdiction of the foreign court for the purpose of enforcement of foreign judgments depends on English law. That required an agreement to submit that could arise by implication. There was no evidence that the law of the contract, namely New York law, could lead the Gibraltar court to the conclusion that the term of the customer agreement relied upon by Mr Picard, the Madoff trustee, could apply to insolvency proceedings.

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This case, although of general application, decides an important question for multi-jurisdictional insolvencies; it is relevant not just to Gibraltar but also to many other offshore jurisdictions.

Gabriel v. *BPE Solicitors* [2015] AC 1663

When a bankrupt has been in litigation, the trustee in bankruptcy may wish to appeal the decision that has gone against the debtor and, indeed, the bankrupt may urge him to continue the fight that he has lost. Until now, there has been a powerful incentive against doing so.

When a trustee is appointed, the bankrupt's estate vests in the trustee, including the right to conduct or appeal litigation. Where a trustee conducts litigation, he does so in his own name, even though it is for the benefit of the bankrupt's estate; he is therefore personally liable to pay any costs order made against him. Ordinarily he can recoup that liability from the estate but only if there are assets.

Until this decision, if he adopted litigation that was already afoot, he became potentially liable for all of the opponent's costs, *even those incurred before the bankruptcy order was made*.

This rule feels unfair because the trustee is at risk of paying costs that he had no part in incurring. But it came about before the court could make third-party costs orders and when costs orders were not provable unless made before the bankruptcy.

The Supreme Court decided that this rule no longer stands now that costs liabilities are provable. But it stressed that there was still a discretion to order the trustee to pay the pre-bankruptcy costs. No guidance was given on this discretion but common sense suggests there would need to be circumstances that would ordinarily justify a third-party costs order. With this change in the law, it may be more viable for trustees to appeal judgments against bankrupts.

The extraterritorial effect of s236, Insolvency Act 1986

Section 236 is an important tool for office-holders. It allows them to ask the court to order those with information about a company's affairs to appear before the court and be examined. It also allows the court to order them to submit an account of their dealings with the company, together with supporting documents.

Last year there were two decisions on whether this power can be exercised against respondents resident abroad. In *Re MF Global UK Ltd* [2015] BCC 891, special administrators sought information from a French company. The respondent contested the court's jurisdiction. David Richards J sympathised with the view that s236 had extraterritorial effect but ultimately decided he was bound by a decision made under the old Bankruptcy Act 1914: he concluded that it does not.

Shortly afterwards, HHJ Hodge QC had to decide the same issue in *Re Omni Trustees Ltd* (No.2) [2015] BCC 906. Here the official receiver, as liquidator, sought an account of dealings and supporting documents from an entity resident in Hong Kong. He argued that *MF Global* failed to take account of the differences between s236 and the Bankruptcy Act, and also a decision on a related issue by the Court of Appeal. Judge Hodge was persuaded to depart from the earlier decision. He concluded that, while there might be no power to order someone from outside the jurisdiction to attend for examination, he could order such a person to produce an account of their dealings with the company.

> "The trustee did not owe them a duty of care and, even if he did, any claim in negligence would have expired when the trustee got his release under s299 IA 1986."

Office-holders will prefer the wider decision in *Omni Trustees* but only time will tell which of the two will become established.

End of the LASPO insolvency exemption

In December, the Ministry of Justice announced that the insolvency exemption would not be renewed. From April 2016 CFA uplifts and ATE insurance premiums cannot be recovered from defendants in insolvency litigation.

The consequences are significant. While CFAs and ATE insurance will remain available in appropriate cases, if the uplift and premium cannot be recovered from defendants, they must be paid from sums recovered. CFA funding will probably cease to be viable for all but high-value cases. Ultimately creditors will lose out.

In some cases it may be possible to persuade creditors to fund and indemnify claims. In others litigation funders may fill the gap. But it seems likely that many claims otherwise available to 'insolvent insolvencies' will simply not be pursued. Perversely, this may provide an incentive to directors who are only moderately misfeasant to empty their companies of assets before the start of an insolvency process in order to stifle claims against them. ◻

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