

3/4 DIGEST



a monthly review of relevant news, cases and articles Vol 9 No 5 May 2003

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The Cayman Islands' Court of Appeal has set aside a ruling which had laid down scales of fees for liquidators (at a level below their normal rates) and which it appeared required all fees to be approved by the Court even if they had been approved by the creditors' committee or the creditors. The Court affirmed the applicability of the procedure set out in the UK Insolvency Rules 1986.

Gabriel Moss QC appeared on behalf of the liquidators.

The Digest is delighted to be able to congratulate Dr Fidelis Oditah, called to the Bar in 1992, on his appointment as Queen's Counsel in this year's list. All at 3/4 South Square wish him every success for the future.

This edition of the Digest was compiled by Stephen Robins.

Richard Fisher

GENERAL NEWS

The Department of Trade and Industry has published the latest statistics showing insolvencies in the first quarter of 2003. There were 3,684 company insolvencies in England and Wales in the first quarter of 2003 on a seasonally adjusted basis. This was a decrease of 13.9 per cent on the previous quarter and a decrease of 8.2 per cent on the same period a year ago. Just over one per cent of active companies became insolvent in the twelve months ended Q1 2003, the same as the previous quarter and the corresponding quarter in 2002. There were 8,103 individual insolvencies in England and Wales in the first quarter of 2003 on a seasonally adjusted basis. This was an increase of 1.7 per cent on the previous quarter and an increase of 11.9 per cent on the same period a year ago.

BANKING

**Sirius International Insurance Co v
FAI General Insurance Ltd
CA (May LJ, Carnwath LJ, Wall J).
[2003] EWCA Civ 470. New Law
Online, 4 April 2003.**

D gave C a letter of credit which C agreed not to draw down unless (1) D had agreed that C should pay a claim but had not put C in funds to do so notwithstanding the simultaneous settlements provisions in the retrocession agreement between them or (2) the syndicate obtained a judgment or arbitration award against C which C was obliged to pay. C having commenced arbitration proceedings against D, D entered provisional liquidation. The arbitration was therefore stayed. An application by C to remove the stay was compromised by a Tomlin order in which D acknowledged that it was indebted to C in the sum of

US\$22.5m and that C was entitled to prove in the liquidation for that amount. C contended that the terms of the Tomlin order in substance fulfilled the first condition entitling it to draw on the letter of credit or alternatively autonomous agreement not affected by the conditions.

The Court of Appeal held as a matter of construction that the acknowledgement in the Tomlin order that D was indebted to C in the sum of \$22.5m was not also an agreement by D that C should pay the syndicate's claim as the condition required. D was entitled to withhold its agreement to C paying the syndicate. Although letters of credit were autonomous in the sense that the court would not restrain payment where there was a dispute under the underlying sale contract, in this case the terms agreed between the parties included express contractual restrictions on the circumstances in which C would be entitled to draw on the letter of credit. Although these restrictions were not terms of the letter of credit itself, as between C and D the underlying agreement was binding. To that extent the letter of credit was less than the equivalent of cash and C's security was correspondingly restricted.

"Are financial services over-regulated?" The Company Lawyer, May 2003.

COMMERCIAL LITIGATION

Silvera v Urquhart

Ch D (Ferris J). [2003] EWHC 809. Unreported, 16 April 2003.

A claimant brought an action in respect of the alleged misappropriation of a 50% share in a golf club near London. The Court held that the action failed for a number of reasons including that there was no basis for finding that the parcels of land comprising the club were held on trust for the individual investors by the company which was the registered proprietor and in which the investors claimed to hold shareholdings through nominees. In addition, the appropriate forum for adjudicating on steps taken in relation to the shareholdings in that company (which was a Hong Kong company) was the companies court in Hong Kong and not the High Court in England. The Court also ruled on the use of documentary evidence obtained pursuant to letters rogatory under the Criminal Justice (International Co-operation) Act 1990.

[Tom Smith]

COMPANY

MT Realisations Ltd v Digital Equipment Co Ltd CA (Dame Elizabeth Butler-Sloss P, Mummery LJ, May LJ). [2003] EWCA Civ 494. Lawtel, 10 April 2003.

C had been a loss-making subsidiary of D, dependent

on loans from D which were secured by debentures. In 1994 a sale of C to a new holding company ("MTI") was achieved by a sale of the shares in C to MTI for £1 and a separate assignment to MTI, at a discounted price payable by instalments, of C's obligations to repay the loans due to D and of the security under the debentures.

MTI failed to meet its obligations to D under the assignment agreement and the instalments were rescheduled. As part of the rescheduling agreement, it was agreed that any sums due from D or any member of D's group to C would be used by or paid to D in reduction of the outstanding instalments of the purchase price under the loan assignment. The loan assignment indebtedness of MTI to D was subsequently paid off in this way.

C entered liquidation and the liquidator claimed that the setting-off of debts due to C against what was due from MTI to D under the rescheduling agreement was contrary to section 151 Companies Act 1985 so that the rescheduling agreement was liable to be set aside with the result that the debts due to C from the remainder of the D group would revive.

Laddie J held that there was no breach of section 151 and struck out C's particulars of claim. On appeal, the Court of Appeal confirmed the approach in Charterhouse Investment Trust Ltd v Tempest Diesels Ltd (1986)

BCLC 1 and *Chaston v SWP Group plc* (2003) BCC 140 and considered the “commercial realities of the transaction”. On this basis, the appeal was dismissed. It was held that the legal position at the date of the rescheduling agreement was that MTI was entitled as assignee of the debentures to enforce its rights as a secured creditor against C in respect of sums due to C from D and its associated companies. By enforcing its security rights as chargee it would recover its legal entitlement rather than be the recipient of financial assistance from C. Both as a matter of commercial reality and of legal principle such an arrangement did not involve C giving financial assistance to MTI within the meaning of section 151(2). Apart from the point that the transaction did not have any negative impact on M's overall net balance sheet position, the relevance of which was disputed, there was no “gift” by C to MTI.

Re In-A-Flap Envelope Company Ltd; Willmont v Jenkins

Ch D (Companies Court) (Mr Crow, sitting as a deputy judge of the Chancery Division). Lawtel, 14 April 2003. Where a director fails to make any inquiries into the financial state of a company prior to signing a statement pursuant to section 156(2), it could not be said that the statement was made honestly. In order

for there to be a valid statutory declaration, all directors (including de facto directors) had to sign the declaration. No proper statutory declaration was given in this case and, as such, financial assistance would not be given in accordance with the white-wash procedure in sections 155-158 of the Companies Act 1985 and monies received by any party were received pursuant to an illegal contract and recoverable. In causing or permitting a company to make an illegal payment of this sort, the director had acted in breach of his fiduciary duties and, in the circumstances of this case, ought not to be excused for breach pursuant to section 727 of the Companies Act 1985.

Rock Nominees Ltd v RCO (Holdings) plc

Ch Div (Peter Smith J). Unreported, 29 April 2003. The second respondent (“ISS”) made a takeover bid for the first respondent (“RCO”), in which the petitioner (“Rock”) was a minority shareholder. It failed to acquire sufficient shares as a result of its bid to enable it compulsorily to acquire Rock's holding under the “squeeze-out” provisions of section 429 of the Companies Act 1985. ISS subsequently appointed its nominees to RCO's board. The directors sold RCO's assets to ISS at a price broadly reflecting the final offer price, and RCO was put into members'

voluntary liquidation. Rock petitioned under section 459 of the Companies Act 1985, contending that the sale was in breach of the directors' fiduciary duties to RCO, and that the transaction was a device to frustrate Rock's ability to command a premium on any sale of its shares to ISS. It was held (1) the sale was in breach of the directors' fiduciary duties to RCO; but (2) there was no prejudice to Rock since the sale was, on the facts, for full value. The price did not have to take into account the alleged value of synergies realised by ISS by excluding minority shareholdings; and (3) Rock's conduct in relation to the takeover had been unmeritorious. There was no “unfairness” in any event.

[Andreas Gledhill]

Tesco Stores Ltd v Pook
Ch D (Peter Smith J). [2003] EWHC 823 (Ch). Lawtel, 30 April 2003.

Tesco brought an action to recover the sum of £323,750 allegedly paid as a bribe to the third defendant (UP) by a company (Delta) who supplied services to Tesco. The first defendant (P) counterclaimed in respect of his right to exercise share options granted to him under an executive share option scheme for Tesco's employees. UP was a company owned and controlled by P.

Tesco contended that P, who was in a position to decide whether or not Tesco would

continue its relationship with Delta, blackmailed Delta into paying the bribe to him by threatening to withdraw Tesco's custom from Delta. Upon discovery of the alleged bribe, Tesco dismissed P. P maintained that the money in question had been loaned to him by Delta.

The court held that P's case was not credible and found that P had extorted the money in question from Delta as the price of keeping Tesco's business. The secret payment had therefore been a bribe that had put P in a position of conflict of interest and constituted a secret commission. P was held liable to account for the payment and held it on trust for Tesco (see *Attorney General for Hong Kong v Reid* (1994) 1 AC 324). It was an implied term of Tesco's share option scheme that P should not be entitled to take advantage of his wrongdoing and therefore P should not be entitled to exercise his share options for so long as he was in such breach of contract as would have entitled Tesco to terminate his contract of employment. If necessary, the court would have held that Tesco was entitled to succeed on P's counterclaim on the basis that P was in breach of a positive duty on his part to disclose that he had received the bribe.

Stephen Griffin, "Evidence justifying a person's capacity as either a de facto or shadow

director: *Secretary of State for Trade and Industry v Becker*," [2003] 3 *Insolvency Lawyer* (May 2003).

"Litigation costs and indemnities under articles of association," *The Company Lawyer*, May 2003.

"In what circumstances should breaches of directors' duties give rise to a remedy under sections 459-461 of the Companies Act 1985?" *The Company Lawyer*, April 2003

"Directors and Employee Status: An examination of relevant Company Law and Employment Law Principles," *The Company Lawyer*, May 2003.

GUARANTEES

Actionstrength Ltd v International Glass Engineering IN.GL.EN SpA HL (Lords Bingham of Cornhill, Woolf, Hoffmann, Clyde and Walker of Gestingthorpe). [2003] UKHL 17.

C agreed to provide labour to D1, who had contracted to build a factory for D2. C and D2 made an oral agreement that, in consideration of C not withdrawing its labour from the site, D2 would attempt to persuade the D1 to meet its obligation to C under the supply contract and failing that would withhold moneys due from D2 to D1 and pay C itself.

D1 failed to meet its liability under the supply

contract. C withdrew its labour and sued D1 for the money due under the supply contract and the D2 for the money due under the agreement.

D2 claimed that the agreement amounted to a guarantee which was unenforceable by reason of section 4 of the Statute of Frauds 1677 for want of a written note or memorandum. C averred that D2 was estopped from relying on the Statute of Frauds because D2 had encouraged C to remain on the site to its detriment.

The House of Lords held that the extending of credit on the faith of a promise made by a guarantor in the knowledge that the creditor would suffer loss if the agreement was not honoured was a normal feature of a contract of guarantee. Section 4 of the Statute of Frauds would be rendered nugatory if the courts were to admit an estoppel solely on the ground that a creditor had acted to its detriment on the faith of a guarantor's oral promise. In the absence of an explicit assurance by D2 not to plead the Statute, there was no ground for holding that the D2 was estopped from disputing the affect of the guarantee.

Singer & Friedlander Commercial Finance Ltd v Thomas QBD (HHJ Thompson QC). *New Law Online*, 11 April 2003.

C brought a claim on a personal guarantee which had been given subject to a

chattel mortgage being “put in place”. Although the parties had signed the mortgage and it had been registered at Companies House, certain deeds of release and/or priority were required in respect of pre-existing charges over the chattels before the mortgage could be properly effected. C submitted that the personal guarantee remained in place because the intended mortgage had not technically been “put in place”, the deeds of release never having been obtained from the relevant parties.

The Court held that where a personal guarantee for asset finance had been given pending the “putting in place” of a chattel mortgage, the guarantee lapsed when the chattel mortgage was registered even though the necessary deeds of release and/or priority had not been obtained. In choosing to register the chattel mortgage, the claimant had obtained the benefit of priority over unregistered debts and later charges. The claimant could not have both the benefit of registering chattel mortgage and the benefit of the defendant’s personal guarantee.

INJUNCTIONS

Bates v Microstar Ltd

**Ch D (Bernard Livesey QC).
The Times, 15 April 2003.**

The purpose of a cross-undertaking imposed on an applicant for a freezing order was to prevent the order from causing injustice or being used

as a weapon of oppression against the defendant. Where an applicant undertook not to bring proceedings in another jurisdiction without the permission of the court, “oppression” included the institution of multiple proceedings in different jurisdictions as well as the institution of proceedings based on the improper use of information obtained by compulsion under the very order obtained.

INSOLVENCY – CORPORATE

London Flight Centre (Stansted) Ltd v Osprey Aviation Ltd

Ch D (Hart J).

[2002] BPIR 1115.

The creditors of LFC, a company in administration, approved proposals for a CVA on terms which included the recommencement of business using an aircraft. This aircraft was to be released to LFC by a secured creditor whose interests had been expressly reserved by the administration order. The aircraft was, however, in the possession of O. O claimed a contractual lien over the aircraft in respect of services provided pre-administration. O did not, however, come into possession of the aircraft until after the date on which the administration order was made. Although it was clear that O intended to assert the lien against the administrators, their consent was not sought to do so pursuant to section 11(3) of the Insolvency Act

1986 and no application was made for leave to take steps to enforce the lien.

On the administrators application for a declaration that O had no rights to detain the aircraft in respect of any debt due from LFC to O, the court granted the declaration sought by the administrators and held (1) It was neither against principle nor contrary to any provisions of the Insolvency Act 1986 for a creditor to acquire substantive rights of a secured creditor after the commencement of an administration. (2) Procedurally, steps to enforce such a lien could only be taken with the consent of the administrators or the leave of the court granted pursuant to section 11(3). (3) Although the administrators had not formally requested delivery up of the aircraft by O, on the facts there was every reason why the court should insist that O should apply promptly for leave before taking steps to enforce its security in respect of the pre-administration debt. (4) As a matter of principle, O ought not to be entitled to enforce a lien which it had acquired post-administration and thereby to gain priority over unsecured creditors and undermine the purposes for which the administration order was made.

[Gabriel Moss QC]

Rolph v AY Bank Ltd**Ch D (Pumfrey J).****[2002] BPIR 1231.**

The Administrators of AY Bank ("AY") entered into an agreement with the Macedonian National Bank ("NB") whereby NB would use its reasonable endeavours to procure repayment of debts owed to AY by Macedonian borrowers and, following such payment, the linked deposits would be repaid to NB but only on the basis that, in the event of liquidation, NB would repay any excess it received beyond its dividend entitlement and that a bank guarantee was provided in respect of such obligation on the part of NB. The court approved the agreement and held (1) the proposed payment would have the effect of enabling the administrators to achieve the purposes of the administration in the manner set out in their proposals and (2) NB would not be treated any differently from the other creditors in the event of liquidation of AY.

[Mark Phillips QC and Tom Smith]

Re Waterford Insurance Ltd and Others**Cayman Islands Court of Appeal. Unreported, 29 April 2003.**

The Court of Appeal set aside in its entirety an en banc ruling by the Grand Court of the Cayman Islands which had laid down scales of fees for liquidators (at a level below

their normal rates) and which it appeared required all fees to be approved by the Court even if they had been approved by the creditors' committee or the creditors. In a brief summary judgment (to be followed by detailed reasons later) they held that the UK Insolvency Rules 1986 applied to the Cayman Islands in relation to remuneration of liquidators and that resort should be had to the procedure laid down in those rules.

[Gabriel Moss QC]

Richard Fisher, "Liquidators' fighting funds: a question of priority", (2003) 16 Insolvency Intelligence 29

[Richard Fisher]

Professor Ian Fletcher, "Rateable Occupation and Administrative Receivership", (2003) 16 Insolvency Intelligence 25

[Ian Fletcher]

David Marks and Tom Smith, "The Enterprise Act 2002 and the EU Regulation on Insolvency Proceedings 2000", Eurofenix, May 2003.

[David Marks, Tom Smith]

David Marks, "The EC Regulation on Insolvency Proceedings", Legal Week, Issue 8 May 2003.

[David Marks]

Gerard McCormack, "Security over shares – reform is in the air," [2003] 3 Insolvency Lawyer (May 2003).

David Milman, "New Insolvency Procedures in Force," [2003] 3 Insolvency Lawyer (May 2003).

Michael Mulligan and John Tribe, "The Remuneration of Office Holders in Corporate Insolvency – Liquidators, Administrators and Administrative Receivers: Part 1," [2003] 3 Insolvency Lawyer (May 2003).

"The European Insolvency Regulation and the Global Rescue Culture," The Company Lawyer, April 2003.

"Should debenture holders be required to meet the costs of winding up the company?" The Company Lawyer, April 2003.

INSOLVENCY – PERSONAL**Yee Fun Chu v Alan Price****Ch D (John McDonnell QC). Lawtel, 7 May 2003.**

Mr Yee Fun Chu ("Y") appealed against the order of a district judge whereby he amended a bankruptcy order to make it clear that Y was the person adjudged bankrupt. The bankruptcy order was headed "Michael Yee Cam Chu" ("M"). Y contended that he was not M, but he admitted that he had adopted the name Michael when he came to England. He said that he had guaranteed a loan to M, the source of the original debt, who had since defaulted on it and returned to China.

Y relied on a witness ("W") who stated that she had known both Y and M and had taken over M's business when he returned to China. The district judge rejected Y's case and accepted the submission on behalf of the trustee in bankruptcy ("T") that the evidence showed that Y and M were the same person.

On appeal, the Court held that there was no proper basis for the district judge's conclusion. Y and W were not cross-examined, and the evidence relied on by T consisted merely of witness statements by solicitors putting forward submissions on the documents but offering no counter-evidence even in the form of hearsay. The case of *Re Myles* (1891) 8 Mor 255 could be distinguished as Y did not admit that he had entered into the credit agreement under the name of Yee Cam Chu nor that it was himself whom the petitioning creditor had intended to sue or to serve with the statutory demand and the petitioning creditor did not apply to amend the title of the bankruptcy by introducing Y's name until five years after obtaining judgment against M and 11 months after leaving a statutory demand in that name at the restaurant where Y worked. It had not been shown that Y had used M's name or allowed it be used in such a way as to induce or even permit the petitioning creditor to believe

that it was Y who was the borrower. Further, the district judge went fundamentally astray in his approach to the evidence. The appeal was allowed and the district judge's order was set aside.

PROCEDURE

Coppard v Commissioners of Customs and Excise Court of Appeal (Thorpe, Sedley and Mance LJ). *The Times*, 11 April 2003.

A judge who was believed and believed himself to have had the necessary judicial authority would be regarded in law as possessing such authority, even if he had not been validly appointed. He was a tribunal established by law for the purpose of Article 6 of the European Convention on Human Rights.

E D & F Man Liquid

Products Ltd v Patel CA (Peter Gibson and Potter LJ). [2003] EWCA Civ 472. *New Law Online*, 4 April 2003.

The Court of Appeal considered the issue of whether the tests set out under CPR 24 (summary judgment) and CPR 13.3 (application to set aside default judgment) were different and held that, in the CPR, the phrase "real prospect of successfully defending the claim" in both CPR 13.3(1) and CPR 24.2 could be taken to have contemplated a similar test under each rule, subject to the question of burden of proof. Both provisions required

the defendant to have a case that was better than merely arguable, as had formerly been the case under RSC Ord 14. The only significant difference between the provisions of CPR 24.2 and 13.3(1) was that under the former the overall burden of proof rested upon the claimant to establish that there were grounds for his belief that the respondent had no real prospect of success whereas, under the latter, the burden rested upon the defendant to satisfy the court that there was no good reason why a judgment regularly obtained ought to be set aside. A defendant applying under CPR 13.3(1) could encounter a court less receptive to applying the test in his favour than if he were a defendant advancing a timely ground of resistance to summary judgement under CPR 24.2.

PROFESSIONAL NEGLIGENCE

Equitable Life Assurance Society v Ernst & Young QBD (Commercial Court) (Langley J). [2003] EWHC 804 (Comm). *New Law Online*, 15 April 2003.

Granting permission to amend the Particulars of Claim to allege that, if the defendants had made provision in the accounts, the directors would not have declared or announced the bonuses they did but would have acted differently, the Court held that the fact that a dividend was overpaid by a company in one year and that they then decided that

less should be paid out in the next had not been determined to be preclusive of a claim for loss and the contrary was arguable. If the scope of the defendant's duty arguably extended to the consequences of sums being paid away on the basis of the accuracy of the accounts which would not otherwise have been paid, there was no reason in principle why the resulting loss ought not to be the excess paid. It was possible that the directors faced with the defendant flagging the possibility of a defeat in the Hyman litigation, together with a provision, might have been moved to seek perhaps a larger cut in bonuses than if the provision had stood alone.

RESTITUTION

R. B. Grantham and C. E. F. Rickett, "Disgorgement for Unjust Enrichment?" (2003) 62 Cambridge Law Journal (March 2003)

The digest is a collation of references to reported and unreported cases and other items of relevance to the professional practices of the Barristers at 3/4 South Square, Gray's Inn, London WC1R 5HP. It is not intended to constitute legal advice, and the contents should not be relied upon without checking the original text of any authority or periodical cited. No duty of care is hereby assumed to any person, and no liability is accepted for the content.
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