INSOLVENCY PRACTITIONERS AND LITIGATION

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Minimising litigation risks

1. There are alternatives to litigation or ways of minimising exposure to costs (eg ADR, Assignment/Financing, Conditional Fee Agreement ("CFA") , choice of legal advisers) and it is obvious that an office holder will wish to limit exposure to costs liability.

Assignments

2. In general, in the insolvency context, assignments should be limited to "company claims" and cannot extend to pure "office-holder" claims. Accordingly, the purported assignment of a claim for wrongful trading under ***s.214 IA 1986*** will be invalid.

   Re Oasis Merchandising Ltd [1997] 1 All ER 1009

3. Extremely important to draft the terms of the assignment precisely and clearly – " *In consideration of the Assignee's covenants .. the Liquidator so far as he is able to do so transfers, conveys and assigns to the Assignee absolutely all those rights of the Liquidator to prosecute and carry on the Action against such defendant or defendants … as the assignee considers proper and all rights to recover and receive from the Defendants in the Action all such sums of money, property and benefits as shall be awarded and adjudged to the Claimant in the Action or in any appeal .."* ; this language was not sufficient to enable the Assignee to commence proceedings in its own name. The Court held that the proper claimant was the company (in liquidation) itself. The only right that was assigned (on the terms of this clause) was the right of the Liquidator to commence proceedings in the name of the company in liquidation:

   Ruttle Plant Hire v Secretary of State for the Environment and Rural Affairs [2007] EWHC 2870 (TCC)

4. It may also be necessary to consider the "public interest" in agreeing an assignment of a director's breach of duty claim.

   Whitehouse v Wilson [2007] BCC 595

5. A CFA backed with an adverse costs insurance policy ought to "see off" a security for costs application . But clearly each CFA has to be scrutinised and considered carefully otherwise it may be open to debate; eg professionals may differ in their approach to the payment of fees.

   Wright Hassall LLP v Morris [2012] EWCA Civ 1471

6. Further if the legal costs incurred by the office holder come under attack it may be that they will not be payable as an expense of the liquidation/administration. In one case Administrators were not allowed to charge the costs of briefing Leading Counsel as an expense of the Administration

Re Wedgwood Museum Trust [2012] EWHC 1974 (Ch)

Personal liability for legal costs

7. The main focus of costs in post insolvency litigation is clearly on legal costs and the costs of litigation . The “normal” CPR provisions regarding costs generally apply (***IR 1986 r.7.33, CPR Part 44.3****)* and therefore: (i) loser pays the winner;(ii) regard to the conduct of the parties ;(iii) issue by issue approach (iv) payment into court; (v) partial costs can be awarded. However there are no “immutable” rules and the Court has an overriding discretion.

8. One area that has not been the subject of much analysis is the position of claiming some part of the time costs of the office holder's investigation/litigation as part of the litigation costs . Costs of wasted management time may be recoverable in tortious/contractual context (***Aerospace Publishing Ltd v Thames Water Utilities, 11th January 2007, Earp v Kurd [2013] BPIR 965*** *)* , or eg where a solicitor conducts his own claim/defence or "in house" experts are used (***London Scottish Benefits Society v Chorley (1884) 12 QBD 452, Re Nossen's Letter Patent [1969] 1 WLR* 638**) but this reasoning has yet to be extended to an insolvency practitioner context.

Office holder as Respondent

9. ***IR 1986 r.7.39*** - where an office holder is made party to proceedings by another party then he/she shall not be personally liable unless the Court otherwise directs *(****Re Mordant [1995] 2 BCLC 647****)* . It would require an unusual case for the Court to make a personal costs order against an office holder who is usually brought into proceedings without any choice and/or he/she is in a position of defending funds in the insolvency procedure in question.

Office holder as Applicant

10. ***Re Wilson Lovatt & Sons Ltd [1977] 1 All ER 274*** . The office holder is not in a special position when he/she initiates litigation in his/her own name. The office holder is personally liable but he/she may claim the costs as an expense of the liquidation/administration provided of course that there are sufficient assets. To the extent that there are not sufficient assets he/she must make sure that adverse costs are covered by insurance or some third party funding.

11. An office holder will only lose the right of recoupment/indemnity from the company's assets where he/she has acted unreasonably, negligently or otherwise acted improperly eg ***Smurthwaite v Simpson-Smith [2006] BPIR 1504***

Name of the company

12. Where proceedings are run in the name of the company an office holder (as a non-party) will not have personal liability for costs save in exceptional circumstances eg where there has been impropriety or other inappropriate conduct in the course of the litigation: ***Metalloy Supplies Ltd (In Liquidation) v MA (UK) Ltd [1997] 1 All ER 418.*** The Court can make an order for costs against a non party. ***s.51 Senior Courts Act 1981***and the procedure is set out in ***CPR 48.2*** and the discretion stated in ***CPR 44.3***.

13. In such circumstances, the receiving part can recover his costs directly from the company's free assets in priority to the liquidator's own costs and expenses**:** ***Re Pacific Coast Syndicate [1913] 2 Ch 26***

14. An exception to the above applies in relation to the costs of getting in, maintaining and realising assets which in general ought to take priority to an adverse costs order: ***Re Movitex Ltd [1990] BCC 491.***

Discontinuance issues

15. The general rule in civil litigation that on the discontinuance of a claim the discontinuing party should pay the other party's costs (unless the Court otherwise orders ***CPR Part 38.6, 44.12(1)(d)***), applies equally to insolvency proceedings.

16. Where a liquidator applied to discontinue misfeasance proceedings on terms that there should be no order as to costs, the court held that there was no reason to depart from the general rule and ordered that he pay the respondents' costs: ***Walker v Walker [2005] BPIR 454***.

17. A liquidator should therefore think very carefully before bringing or continuing proceedings when it may not have the funds to pursue the matter to trial: ***RBG Resources plc v Rastogi [2005] 2 BCLC 592***. In this case, however, the costs payable by the liquidator were discounted because of the other party's unreasonable refusal to negotiate.

Adverse costs and super priority

18. A successful litigant in proceedings is prima facie entitled to be paid immediately the costs ordered to be paid to him in full. The court has jurisdiction to order that the costs of litigation which has been continued by the liquidator be paid as an expense of the liquidation in priority to the general costs of the winding up.

Re Movitex Ltd [1990] BCLC 785

19. If costs are ordered they have to be met prior to any of the costs and expenses of the liquidation and therefore any previous payment of remuneration to the liquidator may have to be repaid.

Re Pacific Coast Syndicate Ltd [1913] 2 Ch 26

Security for costs

20. Where an ordinary claim is brought in the name of an insolvent company, the defendant may apply for security for costs against the company in the usual way pursuant to ***CPR 25.12***. Where, however, a claim is made in the name of the office-holder, no order can generally be made: ***Re Strand Wood Co [1904] 2 Ch 1.***

21. For office-holders resisting an application, there will often be the possibility of running the *Aquila Design* "stifling" defence to an application for security.

Aquila Design (GRB) Products v Cornhill Insurance [1988] BCLC 134

22. Properly drawn arrangements involving a CFA and an adverse costs policy ought to "see off" a security for costs Application and the mere existence of such arrangements does

not militate in favour of the grant of security based on the alleged impecuniousity of the liquidator.

Wu v Hellard 25th November 2013 (Lawtel AC9401440)

How to make recoveries

23. Important to have a "team approach" with the professionals involved and a clear strategy particularly concerning the amount of resources to devote to the progress of the claim.

24. Use of **s.235** (*invitation for a "chat" - bring along legal advisers?)* - **s.236** (*private examination - pros and cons - attendance of creditors?)*

25. Tactical considerations and knowing your target!

Undertaking in damages on a Freezing Injunction

26. Ordinarily the office holder should explain in the supporting Affidavit any request to limit the undertaking to the assets of the Company. This would differ from the normal undertaking referred to in the model form of Freezing Injunction Order and it must be pointed out to the Judge. An undertaking limited to the assets of the estate has commonly been used in cases of this kind

RBG (Resources) PLC v Rastogi [2002] BPIR 1028

Re DPR Futures Ltd [1989] 1 WLR 778

Michael v Assemakis 4th April 2012, page 11 -13, per Mr Livesey QC

27. Frequently there are no assets of substance in the liquidation of the Company but it is just and convenient to make the Freezing Injunction Order nevertheless. In any event though the absence of assets is an important factor in the exercise of the Court's discretion it is not necessarily a determinative one .

28. When acting for an office holder it will be maintained that the undertaking limited to the assets in the liquidation should be accepted because in particular the reason why there are no assets or appear to be no assets in the liquidation of the Company is due to the actions of the Respondents;

29. The question of fortification of the cross undertaking was considered in ***Re Bloomsbury International Ltd [2010] EWHC 1150 (Ch)***. In that case the respondents applied for fortification on the basis that the applicant companies were in administration and clearly insolvent. The court considered that the applicants were in no position themselves to fortify the undertaking but it would not be unreasonable for the administrators to approach the main creditors who were banks to seek an indemnity; albeit for considerably less than the respondents requested. The court balanced the potential harm to the respondents if it transpired that the Freezing Injunction Order had been wrongly granted (which was assessed as significant), with the harm to the applicants if the fortification was ordered unnecessarily. The court concluded that fortification would not stifle the action nor put the administrators to unreasonable risk. The court placed particular emphasis on the identity of the creditors as banks and ***Re DPR Futures Ltd*** was distinguished as being a case involving a large number of small creditors who were not in a position to offer fortification.

30. In approaching the question of fortification the evidence of the applicant should deal with any attempts to approach creditors and/or legal insurance providers which have taken place. Though the absence of immediate assets is an important factor to be taken into consideration it is not necessarily a determinative one. Clearly an applicant must be careful to ensure that he complies with the duty of full and frank disclosure

Franses v Al Assad and others [2007] BPIR 1233.

31. The duty of disclosure would extend to the source of the information obtained for the purposes of making an application. The HMRC is potentially a good source of information about asset intelligence but the scope of its ability to provide information is not at all clear.

s.18(2) Commissioner of Revenue and Customs Act 2005

32. Registering the Freezing Order , *Form RX1, restriction in Form AA, Land Registration Act 2002)*

Litigation and sanction

33. ***Sch 4 para 3A*** - sanction for bringing legal proceedings - claims under **s.213, 214, 238, 239, 423** - not needed for misfeasance (**s.212**)

34. ***Sch 4 para 4*** - not needed to bring or defend action in the name of the company

35. ***Sch 4 para 6A*** - not needed to approve a compromise - but ordinarily better to get sanction

36. Retrospective sanction ***Gresham International v Moonie [2010] Ch 285, IR 1986 r.4.184(2)*** *(ratification in cases of urgency)*

Litigation expenses in a winding up and floating charge assets

37. The expenses of winding up take in priority to the claims to property comprised in a floating charge ***s.176ZA(1)*** but exceptions can be made (***s.176ZA(3)***).

38. An exception has been made involving litigation expenses of legal proceedings taken in a liquidation whether they are "company" claims or "office holder" claims ***IR 1986 r.4.218A-4.218E***.

39. "*Litigation expenses shall not have the priority ... over any claims to property comprised in or subject to a floating charge .... and shall not be paid out of any such property unless and until approved or authorised in accordance with Rules 4.218B to 4.218E"* ***IR 1986 r.4.218A(2)***

40. The provisions contemplate obtaining approval or authorisation from the floating chargeholder or the Court. In a case where the proceeds of a claim constitute property *"property comprised in or subject to a floating charge"* does this mean prior approval of the floating chargeholder must be obtained? Does "*property"* include a right of action against errant directors? What if approval is not sought until settlement?

Update on Clawback claims and Director claims

41. Test of insolvency - ***Re HLC Environmental Projects Ltd [2013] EWHC 2876 (****see also,* ***BNY Corporate Trustee Services Ltd v Eurosail-UK [2013] UKSC 28***

42. Shadow directors - do they owe directors' duties generally? Extension of possible liability to shadow directors ***Vivendi SA v Richards [2013] EWHC 3006 (Ch)***

43. Transactions at an undervalue ***Re Ovenden Colbert Printers Ltd [2013] BPIR 370, [2013] EWCA Civ 1408, Bibby ACF Ltd v Agate [2013] BPIR 685***

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