



Welcome

Hill Dickinson's specialist corporate restructuring and insolvency team advises on all aspects of corporate reorganisation and rescue. Led by Geraldine Ryan, the dedicated team of lawyers has wide-ranging expertise in all corporate business and financial areas.

We are committed to helping businesses of all sizes, including companies and partnerships, to avoid insolvency and enjoy a return to profitability. We advise on buy-outs, refinancing and asset protection schemes as well as personal insolvency and debt restructuring.

Where formal insolvency, including administration, receivership or liquidation, cannot be avoided, the team will handle the process from start to finish.

The team receives instructions from leading insolvency practitioners, corporates and their boards, stakeholders and creditors, banks and factoring companies. We also advise directors and other officers who are facing disqualification and are being pursued as guarantors.

We would welcome any feedback on the newsletter and invite you to call us if you have any queries or would like to discuss any of the contents further (see back for details).



CALLING ALL INSOLVENCY PRACTITIONERS – do you want to be on the Antiques Roadshow?

...Unfortunately we can't help you to get on television to show off your favourite objet d'art to the experts with the hope that your prized possession is worth more than the £2.50 paid for it when you bought it at the local car boot sale in 1981 BUT Hill Dickinson can assist you in discovering the possibly valuable treasures in an insolvent company.

We understand the importance of obtaining as much value as possible from a company in difficulty and the many factors which influence the decision in considering whether all or part of the business and assets of an insolvent company should be sold as a going concern. We also understand that unless the company is a large organisation with a well-known brand or product that it is sometimes difficult to establish what intellectual property is available to sell and even how to value such assets. Intellectual property such as trademarks, copyrights, patents, business methodologies, goodwill and brand recognition do not have the physical value of say, a factory and its plant and machinery, but they can prove valuable so they should not be simply over-looked.



Hill Dickinson has an "IP Capture Service" as we recognise that the assessment and valuation of registered intellectual property (patents, trade marks and designs) is essential in maximising financial recovery. Moreover, beyond registered intellectual property, the value of intangible assets such as brand, know-how, software, drawings, manufacturing processes and customer lists are fundamental to the assessment and valuation process. Our IP Capture Service looks beyond the balance sheet to determine the real value of the intellectual property of a business. Early instruction to our service can ensure that maximum profitability is attained since, just as the real financial value of such intellectual property can be over-looked, failure to identify such assets at the earliest stage can result in its value being eroded.

Samantha Lansbury
samantha.lansbury@hilldickinson.com

Alexandra Jackson
alexandra.jackson@hilldickinson.com

IF IT AIN'T FIXED DON'T BROKER IT – How secure is a floating charge?

In this article we investigate the impact of the Enterprise Act 2002 and recent case law on the legal position of floating charge holders in relation to insolvent companies.

Legislation and background

Section 176A of the Insolvency Act 1986 (as added by the Enterprise Act 2002) provides that where there is a floating charge over the assets of a company that has entered into liquidation, administration or administrative receivership, if the charge was created after September 2003, then the office holder must set aside a "Prescribed Part" of the company's realisable assets to pay unsecured creditors. The Prescribed Part is not permitted to be distributed to the proprietor of a floating charge without first satisfying all unsecured debts. The amount of the Prescribed Part is calculated with reference to a percentage of the company's net realisable assets and cannot exceed £600,000.

The impact of this change to the legislation is that in recent years, it has not been uncommon for a floating charge holder to find themselves in a position whereby their security is of insufficient value to discharge the debt. This has resulted in the practice of floating charge holders lodging proofs of debt in relation to the unsecured element of the debt. Until recently, the law has been unclear as to whether a floating charge holder can apply to join the ranks of unsecured creditors in this way.

Putting the legislation to the test

In the case of *Thorniley -v- HMRC & Another* [2008] All ER (D) 47 the administrators of two connected companies made an application to the Court to determine whether or not a floating charge holder was entitled to rank *pari passu* alongside other unsecured creditors in respect of any shortfall in the value of their security. Essentially, the charge holder advanced the case that not only were they entitled to benefit from the realised value of any secured assets, but also to the extent that this fell short of the overall debt, they were entitled to a share of the Prescribed Part along with the other unsecured creditors.

The Administrators in relation to the Thorniley case had set aside a Prescribed Part of £265,000 leaving net realisable assets for the floating charge holder in the value of just over £1,000,000. The amount owed to the floating charge holder was over six times this sum resulting in an unsecured shortfall of over £5,000,000. The other unsecured debts of the companies totalled over £1,000,000. Therefore, in the event that the charge holder was permitted to have a stake in the Prescribed Part, he would have been entitled to just under £200,000 of the £265,000 "in the pot". In simple terms, once the taxman had been paid, this resulted in a dividend of just 4 pence in the £1 to the majority of unsecured creditors. Conversely, if the Court were to find that the charge holder was not entitled to a share of the Prescribed Part, a much higher rate of recovery of 16 pence in the £1 could be realised for the same creditors.

HMRC submitted that given that the purpose of the introduction of section 176A was to ensure that floating charge holders would be prevented from receiving payments out of the Prescribed Part, if the Court found that the same charge holders could turn to the Prescribed Part for the unsecured element of the debt, then the entire purpose of the new legislation would be defeated. The result would be that on the one hand, the Prescribed Part would be taken away from the assets caught by the floating charge but then on the other hand given back when the balance of the secured assets proved insufficient to discharge the debt.

Conclusion

As section 176A is silent as to whether the unsecured shortfall due to a floating charge holder fits within the definition of unsecured debts for the purpose of that section, this question fell to the Judge in *Thorniley* to decide. The importance of the outcome was not lost on the Judge who made various references in his judgment to the 2001 White Paper which preceded the 2002 Act. In particular, the Judge focused on the introduction of schedule B1 which granted wide powers to Administrators to distribute to a company's creditors without Court permission. The Judge also placed emphasis on the significant reduction to the categories of preferential creditors, and in particular the Crown, and stressed that these changes to the legislation were of significant benefit to the position of preferential creditors.

In light of the 2001 White Paper and the submissions made on behalf of HMRC, the Judge found in favour of the unsecured creditors. Although the charge holder had submitted that such a finding would be contrary to the *pari passu* rule due to the unsecured nature of the shortfall, the judge found that a distinction must be drawn between creditors with some security and those with none at all. Nevertheless the decision is a far reaching one to say the least and one that has left the corporate lending industry reeling.

Doubtless to say, careful consideration will be given by lenders in future as to whether a floating charge is a safe form of lending.

Christine Newton
christine.newton@hilldickinson.com



USE IT OR

Retention of Title clauses allow the seller to retain title in goods supplied until the sale price has been paid in full. This means that the seller will have a right to the return of those goods in the event that the buyer becomes insolvent. In this way the seller avoids many of the pitfalls of becoming an unsecured creditor of an insolvent company. Retention of Title clauses vary greatly in enforceability and enforcement is often prevented by, inter alia, an inability to identify the goods concerned or the fact that goods have been absorbed into other products. These difficulties have now been supplemented however by the decision in [Fashoff \(UK\) Limited t/a Moschino, Forall Confezioni SPA -v- Martin Henry Linton, Baron Jon Menswear Ltd \[2008\] EWHC 537 \(Ch\)](#), in which the Court refused to enforce the applicants' Retention of Title clauses because their delay in making their application had impeded the Administrator's ability to carry out his duties.

Facts of the case

Fashoff and Forall traded with Baron Jon, a men's fashion company under their respective standard terms and conditions which incorporated Retention of Title clauses. Baron Jon entered administration on 28 February 2006. It soon became

apparent that the goods supplied by both Fashoff and Forall had been sold on to Premium Retail Limited ("PRL"). However the sale did include the provision that PRL would honour any valid Retention of Title claims for a reasonable period of time after the sale.

Fashoff

On 14 March 2006 Fashoff wrote to PRL alerting them to the existence of the Retention of Title clause and stating that they would begin negotiations with Foulds Ingham Associates, who had been appointed to deal with Baron Jon's stock. Unfortunately, after taking this first proactive step, Fashoff became increasingly unresponsive and uncooperative. For example a questionnaire for further information sent to Fashoff in March was not returned until May and points raised in a letter in June were not substantially answered until December. Further repeated requests for information as to the terms of sale went unanswered to the point that Foulds Ingham stated more than once that they would close their file on this matter. One of the key issues of disagreement between the parties was whether English law was in fact applicable as the terms of sale made reference to Italian law and the Court of Como, although this point was never resolved.

Forall

Forall claimed that at the time of entering administration Baron Jon was indebted to them in the amount of £34,034.00. This amount was later disputed. On 30 May 2006 Forall was informed by the Administrator that if their Retention of Title claim was accepted this would be paid by PRL. However, on 3 July 2006 Foulds Ingham notified Forall that they would be recommending that the Administrator reject the claim. This was partly because of questions over the incorporation of the Retention of Title clause into the sale agreement and partly because of a perceived inability to differentiate between the paid and unpaid goods held by PRL. A further complication was that Forall had apparently assigned the debt and rights under the Retention of Title clause to Barclays Bank plc. While there was some evidence that the debt was re-assigned to Forall it was not clear if the same could be said of the rights under the Retention of Title clause.

It was not until 7 November that Forall asked Foulds Ingham to re-consider. A full response to the rejection did not occur

viable to ensure the most advantageous realisation of the company's assets as possible.

In this case the Administrator had twice applied for an extension of time to submit a statement of proposals to the Registrar of Companies due to the ongoing issue of the Retention of Title clauses. Further, the length of time it took Forall and Fashoff to make their application to the Court after the Administrator's initial rejection had led to doubt over whether the goods in dispute could be said to be in the possession of Baron Jon, a fundamental consideration derived from the Court of Appeal case of Atlantic Computer Systems [1992] Ch 505 at 542. While it was arguable that PRL's agreement to honour any valid Retention of Title clause made within a certain time led Baron Jon to have constructive possession of the goods during that period, that time had long since elapsed.

It was therefore held that due to their inefficient and inexcusable delay Fashoff and Forall had missed their opportunity to enforce against PRL. The result was that what should have been a relatively straightforward matter had instead entangled the

R LOSE IT

until 27 February 2007 when Fashoff's representatives notified Foulds Ingham's solicitors that the companies would be jointly applying to the Court for the enforcement of their Retention of Title clauses.

Ruling

After some initial confusion Forall and Fashoff confirmed that they were making their application under paragraph 43(3), schedule B1 of the Insolvency Act 1986, which allows for the repossession of goods held under a Hire Purchase Agreement, including those subject to Retention of Title clauses. Such repossession requires the consent of the Administrator, which in this case had been refused, or the permission of the Court, which was now being sought.

In considering whether to grant such permission the Court considered paragraph 72(1) which provides that the Court can approve such an application if they think "that disposal of the goods would be likely to promote the purpose of administration in respect of the company." Under schedule B1 of the Insolvency Act 1986 the purpose of an Administrator is to rescue the company as a going concern or, if this is not

Administrator in lengthy proceedings to the detriment of the overall administration and the other creditors. Permission to enforce the Retention of Title clauses was refused as in Judge Toulmin's words "it is impossible on the evidence before me to begin to justify the lengthy delay in this case".

Conclusion

The decision reached in this case will have consequences, both positive and negative, for all those affected by a company's administration. For Administrators the case provides helpful guidance as to when their rejection of claims under a Retention of Title clause will be upheld by the Court. For holders of Retention of Title clauses this provides a stark warning as to the consequences of delaying enforcement and failing to cooperate with the Administrator. Finally for unsecured creditors in general this case confirms that they will not be made to suffer because of the delay and inefficiency of those who have the benefit of a Retention of Title clause.

Christopher Tyrrell
christopher.tyrrell@hilldickinson.com



The Great Pre-Pack Debate with Reference to DKLL Solicitors -v- HMRC

Pre-pack administrations involve arranging the sale of a debtor's insolvent business prior to appointing an Administrator. The sale will be concluded immediately on the appointment of the Administrator so that completion and appointment are virtually simultaneous with the result that the insolvent business is sold as a going concern, which is beneficial to the debtor as there is no public marketing of the administration and prior approval of the unsecured creditors is not required. Another important feature is that the goodwill of the business remains as the deal is arranged before administration commences. Secured creditors are notified of the impending administration and are therefore in a stronger position to protect their interests by ensuring that the business is sold for sufficient consideration to cover what is owed. It has been suggested that pre-packs could be criticised as being more favourable to secured creditors.

Influence of the Enterprise Act 2002

There has been a significant increase in the use of pre-packs since the Enterprise Act 2002 which came into force in September 2003. The ethos behind the Enterprise Act 2002 was to help businesses survive by promoting collective insolvency procedures, in particular through streamlined administration procedures and the removal of the Crown's preferential rights such as priority payment of debts to HMRC and social security contributions. This includes debts such as unpaid taxes, VAT and arrears of PAYE. The Crown has previously enjoyed preferential treatment to other secured creditors but now, pursuant to the Insolvency Act 1986, as revised by the Enterprise Act 2002 under section 251, such preferential rights have been removed. The result of this is that HMRC (amongst others) is now an unsecured creditor along with the others.

DKLL Solicitors -v- HMRC 2007 EWHC 2067

This is relevant in particular to the ruling in the case of DKLL Solicitors -v- HMRC (2007) EWHC 2067 whereby pre-packs gained Court approval. HMRC objected to the sale of the business of DKLL Solicitors (an insolvent limited liability partnership) when they made an application to the Court to be placed into administration. The reason for this was to allow the transfer of the business to a new firm, Drummonds Kirkwood LLP (a newly incorporated LLP). HMRC petitioned for the winding up of the firm and appeared at the hearing to object to DKLL's application. HMRC was the majority creditor and was owed a sum in the region of £1.7 million. They argued that they had the absolute right to vote against the Administrator's proposals and subsequently had the right to veto the choice of Administrator. HMRC also felt that the value of the business was significantly higher than the figure incorporated into the sale agreement.

The Judge was minded to reject HMRC's claim, one of the principal reasons being that the proposed sale appeared to be the only way to save approximately 50 of DKLL's employees. Consideration was also given to minimising the disruption to existing clients.

Conclusion

In the case of DKLL -v- HMRC it was therefore left to the Judge's discretion as to whether he made the administration order in favour of the applicants. The Judge also noted that the Court placed great reliance upon the experience and expertise of insolvency practitioners. It therefore would have required clear evidence from HMRC to support its contentions that the pre-pack strategy could not be achieved and therefore to overturn the insolvency practitioner's view.

It should be noted that the Judge did not state in particular that the strategy of the pre-pack was in fact unlawful and in doing so did not state that there was anything inherently objectionable to the pre-pack strategy. This, in effect, validates the pre-pack as a legal rescue technique which provides assistance to insolvency practitioners when applying for administration appointments.

Carole Hopkinson
carole.hopkinson@hilldickinson.com

CASE LAW UPDATE

[Peter Mills -v- \(1\) Robert William Birchall and \(2\) Barry Gordon Gilbertson \[2008\] EWCA Civ 385](#)

The Court of Appeal has held that where receivers appointed under a Bank Charge caused an insolvent company to sue for breach of contract and the action was unsuccessful, the Judge had properly exercised his discretion in declining to make a Costs Order against the receivers under section 5 of the Supreme Court Act 1981. It was considered that the Judge at first instance had properly applied the “exceptional circumstance” test and that this was an entirely normal case of receivers seeking to enforce a contractual right forming part of a security. Furthermore, there was no element of impropriety or unreasonableness to make the claim exceptional. In the circumstances, the Court of Appeal considered there was no justification for making the receivers personally responsible for the costs of the unsuccessful party.

[McGrath and Others -v- Riddell and Another \(HOL\) 09/04/08](#)

This Appeal to the House of Lords concerned the question of whether English assets (under the control of a provisional liquidator) of a number of insurance companies in compulsory liquidation in Australia should be remitted to the Australian liquidators for distribution under the Australian Statutory Scheme for Insolvent Insurance Companies or be retained in England for distribution here. It was held that the assets should be remitted to Australia and the fact that in the country of principal winding up there would be a class of preferential creditors who would not have priority under English insolvency laws was insufficient reason for an English Court to refuse a request made pursuant to section 426 of the 1986 Act.

[HM Commissioners for Revenue & Customs -v- Royal Bank of Scotland \[2008\] BCC 135](#)

This decision of the Court of Appeal dealt with the realisation of a floating charge security and the obligations to account to preferential creditors, clarifying the scope of section 196 Companies Act 1985.

HMRC was a preferential creditor and the Court of Appeal was asked to determine whether section 196 was relevant to the particular facts of the case. It noted that in determining whether section 196 has any application, it is necessary to distinguish acts which are in substance (whatever their form), acts by which the charge holder realises its security from acts which are no more than the ordinary discharge of the debtor’s liability.

In this case, the Court of Appeal considered that HMRC was likely to establish that section 196 would apply to the facts of the matter.

[\(1\) Dynamex Friction Limited \(2\) Ferotec Reality Limited -v- \(1\) Amicus \(2\) Barton, Jones Lamerick Love Roberts and Williams \(3\) Secretary of State for Trade and Industry \[2008\] EWCA Civ 381](#)

In this Appeal against a decision of the Employment Appeal Tribunal, the issue to be determined was whether the Administrator of an insolvent company who had dismissed the insolvent company’s staff had done so for economic reasons or whether the dismissal was within the scope of TUPE. The Appeal was allowed on the basis that at the time of the dismissals, the Administrator had been the directing mind and will of the insolvent company and it was his reasoning that had to be ascertained. It was considered impossible to attribute the knowledge of the Director’s strategy for the insolvent company to the Administrator and to replace the Administrator’s reasons for dismissal with the Director’s strategy.

Elizabeth Greaves
elizabeth.greaves@hilldickinson.com



About Hill Dickinson

Hill Dickinson offers a comprehensive range of legal services from offices in Liverpool, Manchester, London and Chester, and its associated firm Hill Dickinson International has offices in London and Greece. Collectively the firms have over 150 partners and a complement of more than 1000 staff.

Hill Dickinson is a major force in insurance and is well respected in the company and commercial arena. The firm's marine expertise is internationally renowned and it has one of the largest marine practices in the UK following a merger with Hill Taylor Dickinson on 1 November 2006. The firm has an award winning property practice and is widely regarded as a leader in the fields of commercial litigation, employment, intellectual property, NHS clinical/health related litigation and private client.

For further details please contact:

Geraldine Ryan

Partner

0161 817 7288

geraldine.ryan@hilldickinson.com

Hill Dickinson LLP:

Liverpool Office

No.1 St Paul's Square
Liverpool
L3 9SJ

T: +44 (0)151 600 8000
F: +44 (0)151 600 8001
DX 14129 Liverpool

Manchester Office

50 Fountain Street
Manchester
M2 2AS

T: +44 (0)161 817 7200
F: +44 (0)161 817 7201
DX 14487 Manchester 2

London Office

Irongate House
Duke's Place
London EC3A 7HX

T: +44 (0)20 7283 9033
F: +44 (0)20 7283 1144
DX 550 City of London

Chester Office

34 Cuppin Street
Chester
CH1 2BN

T: +44 (0)1244 896600
F: +44 (0)1244 896601
DX 19991 Chester

Hill Dickinson International:

Greek Office

2 Defteras Merarchias St.
Piraeus, 185 35
Greece

T: +30 210 428 4770
F: +30 210 428 4777

London Office

Irongate House
Duke's Place
London EC3A 7HX

T: +44 (0)20 7283 9033
F: +44 (0)20 7283 1144
DX 550 City of London

The information and any commentary contained in this newsletter are for general purposes only and do not constitute legal or any other type of professional advice. We do not accept and, to the extent permitted by law, exclude liability to any person for any loss which may arise from relying upon or otherwise using the information contained in this newsletter. Whilst every effort has been taken when producing this newsletter, no liability is accepted for any error or omission. If you have a particular query or issue, we would strongly advise you to contact a member of the corporate restructuring and insolvency team, who will be happy to provide specific advice, rather than relying on the information or comments in this newsletter.

www.hilldickinson.com