



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 5D

GUERNSEY

This is the **summative (formal) assessment** for **Module 5D** of this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

The mark awarded for this assessment will determine your final mark for Module 5D. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT

Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.
2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way. DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.
3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).
4. You must save this document using the following format: **[studentnumber.assessment5D]**. An example would be something along the following lines: 202021IFU-314.assessment5D. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentnumber” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked.**
5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words.**
6. The final submission date for this assessment is **31 July 2021**. The assessment submission portal will close at **23:00 (11 pm) GMT on 31 July 2021**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.
7. Prior to being populated with your answers, this assessment consists of **7 pages**.

ANSWER ALL THE QUESTIONS

QUESTION 1 (multiple-choice questions) [10 marks in total]

Commented [DJ1]: Total 9/10

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and **mark your selection on the answer sheet by highlighting the relevant paragraph in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

Question 1.1

Which one of the following statements **correctly describes** the sources of Guernsey law?

- (a) Guernsey's laws mirror that of England and Wales.
- (b) Guernsey's law is all set out in statute adopted from England.
- (c) Guernsey's law is based on Norman customary law.
- (d) Guernsey substantive law is set out in statutes and the historic customary law and complimented by case law from persuasive jurisdictions.**

Commented [DJ2]: Correct

Question 1.2

Which of the following types of security can be effectively taken over Guernsey **immovable property**?

- (a) A fixed charge / mortgage.
- (b) A lien.
- (c) A hypothèque by way of bond.**
- (d) A security interest agreement.
- (e) A floating charge

Commented [DJ3]: Correct

Question 1.3

Which **two** of the following are **essential requirements** for a valid security agreement pursuant to the Security Interests Law?

- (a) Registration with the Guernsey registry.
- (b) Executed as a deed.
- (c) Identify the secured party.**
- (d) Executed before the Court.
- (e) Be in writing.**

Commented [DJ4]: Correct

Question 1.4

Which of the following parties **rank first in priority** in a Guernsey compulsory winding up:

- (a) Trade creditors.
- (b) Local tax creditors.
- (c) Money lent by a sole trader to the company.
- (d) Fees and expenses of the liquidator.
- (e) Fully paid up shareholders.

Commented [DJ5]: The correct answer is d alone.

Question 1.5

Which one of the following procedures can be used to enforce against real property in Guernsey?

- (a) Saisie.
- (b) Arret de Gages.
- (c) Arret de Personnes.
- (d) Désastre.

Commented [DJ6]: Correct

Question 1.6

Which one of the following **is not** a standalone ground for the making of a compulsory winding up order as set out in the Companies Law?

- (a) Passing of a special resolution to wind up.
- (b) Deadlock on board of directors.
- (c) Suspension of business for a year.
- (d) Company is unable to pay its debts as they fall due.
- (e) Failure to hold a general meeting of members under specified provisions of the Companies Law.

Commented [DJ7]: Correct

Question 1.7

Which of the following **may not** be appointed as voluntary liquidator of a Guernsey company?

- (a) A director or former director.
- (b) A corporate entity.
- (c) A foreign resident individual.
- (d) A shareholder.

(e) None of the above.

Commented [DJ8]: Correct

Question 1.8

Which one of the following parties **does not** have automatic statutory standing to make an application for an administration order in respect of a Guernsey company?

(a) A shareholder.

(b) The Registrar of companies.

Commented [DJ9]: Correct

(c) A director.

(d) A creditor.

(e) None of the above.

Question 1.9

Which one of the following **is not** a ground for setting aside a judgment registered under the Reciprocal Enforcement Law?

(a) The courts of the originating country did not have jurisdiction.

(b) The enforcement of the Judgment would be contrary to public policy in Guernsey.

(c) The enforcement of the Judgment would be contrary to public policy in the home jurisdiction.

Commented [DJ10]: Correct

(d) The Judgment was obtained by fraud.

(e) The rights under the Judgment are not vested in the person by whom the application for registration was made.

Question 1.10

It is advisable for a creditor to take **which one** of the following steps before commencing a *saisie* action?

(a) Obtain a prohibitory injunction to prevent the debtor from disposing of the realty.

(b) Register an interest in the realty at the *Greffe*.

(c) Advertise in the local Gazette an intention to commence *saisie* proceedings against the debtor.

(d) Exhaust the debtor's personalty (personal property) and register a claim in *Livre des Hypotheques* in the interim.

Commented [DJ11]: Correct

(e) Enter into a security interest agreement with the debtor to ensure that the creditor's interest in the realty is protected.

QUESTION 2 (direct questions) [10 marks]

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Question 2.1 [maximum 5 marks]

What are the most common forms of security granted over immovable and movable property in Guernsey? Explain the formalities (if any) that the security documents, the secured creditor or the debtor must comply with.

Immovable Property: Other than *rentes foncieres*, security over immovable property (including real estate) is taken as a *hypothèque* – that is a legal right over the debtor's property in favour of the creditors – by either: (a) *rente hypothèque*, securing a fixed annual sum; or (b) *hypothèque conventionnel* (or bond). In practice, *rente hypothèque* is relatively infrequently used / unknown, and the bond has become the dominant form of security over real estate.

The bond is a personal obligation to create a charge over the corpus of the debtor's assets by acknowledging the debt to the creditor and (if appropriate) including a covenant to repay the sum, with interest. The bond can either be: (a) a general charge, which confers priority to the creditor over all other claimants to the immovable property belonging to the debtor at the time the bond is registered; or (b) a specific charge, which confers priority to the creditor only over the immovable property specified in the bond.

A bond does not confer legal title to the subject property owned by the debtor to the creditor.

It must be in writing and consented to by the debtor before the Royal Court of Guernsey sitting as a contract court; before being registered at the registry of the Royal Court (*Greffe*). Other than a testamentary disposition, other documents consented to before the Contract Court do not need to be signed by the parties. However, this is frequently required by the creditor.

Following ratification by the Contract Court: (a) the bond is assessed for document duty of 0.50% of the secured amount, the fees of the Contract Court and registration fees; (b) the document duty and fees are paid; and (c) the bond is registered in the *Greffe*, and available for public inspection to anyone wishing to conduct a search against the debtor.

A bond which is not ratified by the Contract Court is invalid and non-registration of the bond at the *Greffe* will render the security ineffective.

Immovable Property: The most common forms of security over tangible immovable property are: (a) lien – being the right to retain another's property if an obligation is not discharged; (b) pledge – being a bailment or deposit of personal property with a creditor to secure repayment for a debt or engagement; (c) *tacite hypothèque* – being a landlord's right to priority for unpaid rent which is secured by movable property on the demised premises; (d) reservation of title clauses; and (e) mortgage (e.g. over a ship or aircraft).

There are two common forms of security over intangible immovable property, as follows: (a) a security interest under the Security Interests (Guernsey) Law, 1993 (the "**Security Interests Law**"); and (b) a security under the Law of Property (Miscellaneous Provisions) (Guernsey) Law, 1979 (the "**Property Law**").

A security interest under the Security Interests Law may be created by a security agreement over any intangible immovable property (other than a lease) and can be created by the secured party being in possession of, under a security agreement: (a) certificates of title (such as securities); or (b) policy documents (such as a life insurance policy).

To be valid, a security agreement must: be in writing; be dated; identify and be signed by the debtor; identify the secured party; contain provisions regarding the collateral sufficient to enable its precise identification at any time; specify the events which constitute a default; and contain provisions regarding the obligation, payment or performance to be secured, sufficient to enable it to be identified. To the extent any requirement is not complied with, the security agreement will not necessarily be void, however, it will take the security agreement outside the scope of the Security Interests Law.

If title to collateral is to be assigned, then express notice in writing of the assignment must be given to assignees.

A security under the Property Law is a set-off agreement and an assignment with a proviso for reassignment and relates to agreements under which, in respect of mutual dealing between them, any debt from one party is to be set off against any debt from the other. Unless the parties have expressly or by implication agreed otherwise, the only action which can be taken in relation to what otherwise would be those mutual debts, is in respect of the balance after the set-off.

The legal right to a debt or other chose in action can be assigned to a third party. To be effective, an assignment must be: (a) executed in writing by the assignor; and (b) express notice in writing of the assignment must be served on the debtor, trustee or other person from whom the assignor would be able to claim the debt / chose in action.

Failure to comply with any of these requirements will not necessarily render the assignment void.

As noted above, all bonds in respect of real property must be registered in the *Greffe*, and available for public inspection. There is no register of charges in respect of Guernsey companies and accordingly, save for bonds, there are no Guernsey-law requirements in respect of perfecting security by registration.

Question 2.2 [maximum 5 marks]

Michael was recently appointed liquidator of Dodge Co Limited, a Guernsey incorporated company. There are two directors of the company, Roger and Novak. The books and records of the company show that Novak paid £5,000 to purchase a car from the company two months prior to the company entering into liquidation. However, the fixed asset register had listed the car as having a value of £20,000.

Identify the issue with this transaction and explain the possible causes of action against the company or directors, as well as the possible remedies for recovery of the difference in value between the value and sale price of the asset.

The issue is that it appears that Dodge Co Limited ("**Dodge Co**") sold one of its assets – a car – for less than its market and/or book value to a related or connected party – one of its directors – in the period leading up to its liquidation (i.e. at a time when it was or may have been insolvent), and as a result of which there are now fewer assets available to satisfy claims against Dodge Co and/or for distribution to shareholders (in the event of a surplus).

It appears that such transaction may constitute a 'transaction at an undervalue'. There is no such codified law relating to transactions at an undervalue under Guernsey law. However Michael may consider the following actions under Guernsey's customary law:

Commented [DJ13]: One mark – Whilst the answer correctly identifies the issues, the narrative is largely a lightly edited copy of the guidance text .

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(a) First, a claim that Novak committed an equitable wrong – Novak in his capacity as recipient of the car from Dodge Co for a price below market / book value has knowledge that he and Roger, in their capacities as directors of Dodge Co, were acting in breach of their fiduciary duties by selling Dodge Co's assets at an undervalue, and as a result of which Novak's conscience is affected such that it is impermissible to allow Novak to retain the misappropriated car (i.e. that Novak holds the car by way of constructive trust for Dodge Co); **or**

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(b) Second, a customary law Pauline action. Two critical elements must be proved in respect of any such claim: (i) Dodge Co must have been insolvent on a balance sheet basis at the time of the sale of the car to Novak; and (ii) Dodge Co must have carried out the sale with the intention to defraud creditors. It is not clear from the fact pattern above whether such elements **exist**

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Additionally, Michael may consider bring claims against each of Roger and Novak (in their capacities as directors of Dodge Co) for misfeasance and/or breach of fiduciary duty in connection with the sale of the car to Novak below market / book value. The test for breach of fiduciary duty is subjective (see *Carlyle Capital Corporation Limited (in liquidation) and others v Conway and Others*, in which HH Marshall LB held that: "There is no fiduciary duty to make an objectively 'right' **decision**").

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If Michael is successful in proving misfeasance or breach of duty on the part of either (or both) Novak and Roger, Novak may be ordered to: transfer the car back to Dodge Co and/or each of Novak and/or Roger may be required to pay cash equal to the balance of the value of the car (i.e. £15,000) to Dodge Co and to pay interest **thereon**

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QUESTION 3 (essay-type questions) [15 marks in **total**]

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Question 3.1 [maximum 7 marks]

Guernsey has not adopted the UNCITRAL Model Law on Cross-Border Insolvency. Explain what methods are available to foreign insolvency officeholders seeking recognition in Guernsey and the limitations of those options.

Notwithstanding that Guernsey has not adopted the UNCITRAL Model Law on Cross-Border Insolvency, it is relatively easy for a foreign insolvency officeholder to seek recognition in Guernsey. There are two possible mechanisms by which a foreign insolvency officeholder may seek recognition in Guernsey: pursuant to Section 426 of the UK Insolvency Act 1986 (the "**UK Insolvency Act**"), having been extended to Guernsey by the Insolvency Act 1986 (Guernsey) Order, 1989; and pursuant to Guernsey common **law**

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Pursuant to the Insolvency Act 1986 (Guernsey) Order, the Royal Court is able to provide judicial assistance to the courts of England and Wales, Scotland, Northern Ireland, the Isle of Man or Jersey in insolvency matters. Accordingly, this relief is limited as it is not available to *all* foreign insolvency officeholders.

For these purposes, assuming that the foreign insolvency officeholder was appointed in one of the designated countries and territories, pursuant to section 426 of the UK Insolvency Act, the procedure for obtaining recognition in Guernsey to be followed by an eligible foreign insolvency officeholder is as follows: the foreign insolvency officeholder will apply to the court with jurisdiction for insolvency matters in his home jurisdiction, in order that the home court will send a letter of request for assistance to the Royal **Court**

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Pursuant to section 426(5) of the UK Insolvency Act, the Royal Court "shall assist" the requesting court. However, it is not mandatory and the Royal Court will consider whether assistance may be properly granted in accordance with: (i) its own general jurisdiction and powers; (ii) its own insolvency law; or (iii) the insolvency law applicable by the requesting court to comparable matters in its jurisdiction. In practice, the Royal Court will generally not have any discretion to accede to the request unless by doing so it offends public policy (in Guernsey) or the outcome is **oppressive**.

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In addition, Section 426(5) of the UK Insolvency Act provides the Royal Court with the means to apply the insolvency law of either Guernsey or the relevant foreign jurisdiction in relation to matters failing within its jurisdiction.

There is very little case law in Guernsey, but given the commonality of legislation in this area with England and Wales, guidance can be taken as to the application of the section and its limited from English **jurisprudence**. The leading case within Guernsey is *The Liquidator of Seagull Manufacturing Company Limited v Colin and Susan Slinn* (Guernsey Court of Appeal, August 1991), where an English liquidator sought a private examination of the directors of an English registered company who were resident in Guernsey (under section 236 of the UK Insolvency Act).

Commented [DJ23]: Beware of not copying Guidance Text.

Section 426 of the UK Insolvency Act only applies to designated jurisdictions and officeholders from those jurisdictions have to make an application to their home court for the letter of request to be sent to the Royal Court – this can be time-consuming and **expensive**.

Commented [DJ24]: One mark – agreed but often the use of this procedure is better approach as it provides much broader scope for use of powers than might be available under the common law.

Alternatively, the foreign insolvency officeholder may seek recognition under Guernsey common law – this is through the 'sufficient connection' test, which was first applied in the English case of *Schemmer and others v Property Resources Limited* [1975] Ch 273). The Guernsey case of *Roy Terry Junior and Durette Bradshaw plc v Bank of Butterfield (Guernsey) Limited (2006)*, applied the "sufficient connection" test in Guernsey, and in which the Royal Court held that there is a "sufficient connection" where: (i) the foreign insolvency officeholder is appointed in the jurisdiction where the company is incorporated or individual domiciled and (ii) if the defendant submits to the jurisdiction by whose order the appointment was made. It also held that there might be a sufficient connection where: (iii) the order of the foreign court is recognised by the law of the place where the company is incorporated, or (iv) the office holder is appointed in a jurisdiction where the management and control of the company is exercised or where it carries on **business**.

Commented [DJ25]: One mark

The recent decision in *Singularis Holdings Limited v PriceWaterhouseCoopers (2014)* [2014] UKPC 36 provides that "there is a principle of the common law that the court has the power to recognise and grant assistance to foreign insolvency proceedings" and sets out the scope of the extent and nature of the jurisdiction for recognition under common law, as follows: (a) common law power does not enable the foreign insolvency officeholder to do something which they could not do under the law pursuant to which they were appointed. The Royal Court may make an order against persons within its own jurisdiction in favour of the foreign insolvency officeholder, provided that such right exists under the local law of the court which appointed them – although the availability of 'as if' relief is limited to circumstances where the Royal Court has the common law power to order such relief; and (b) the order sought is consistent with the substantive law and public policy of the assisting state (i.e. **Guernsey**).

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In summary, as a matter of common law, the Royal Court / Guernsey will co-operate in foreign insolvency proceedings, particularly where there is a sufficient connection between an officeholder appointed in the jurisdiction where the company is incorporated (or individual domiciled) and the company (or individual) has submitted to the jurisdiction of the court by which the appointment was made. The Royal Court retains residual discretion to refuse to recognise and/or assist the foreign insolvency officeholder.

The Royal Court has exercised its discretion in favour of recognition of US appointed receivers, UK appointed liquidators, UK appointed trustees in bankruptcy in Guernsey, South African trustees of an insolvent estate, and a Norwegian trustee in bankruptcy.

Question 3.2 [maximum 8 marks]

Write a short essay on the method of enforcing creditor's rights against real estate owned by individuals in Guernsey.

Saisie is the customary procedure used in Guernsey whereby a creditor can enforce against the real property of their debtor and ultimately have the realty vested in them in order to satisfy the applicable debt.

The *Saisie* process has recently been revised by the *Saisie* Procedure (Simplification) (Bailiwick) Order 1952 (the "**Saisie Order**"), however, the substantive law remains rooted in customary law (see *Selwood v Madely* [2001] RC).

Commented [DJ27]: Again – beware of copying Guidance Text

The procedure is split into the following stages:

(a) Stage 1: Preliminary Vesting Order

As an initial matter, the creditor (the "**principal creditor**") must first consider whether the debtor has any significant assets (being personalty) against which it may seek enforcement first – this is because as a matter of Guernsey law, the creditor may not seek payment from the debtor for any shortfall following the sale of the charged property and once a nomination for proceeding against realty is made (i.e. once a personal vesting order is sought, pursuant to *saisie* proceedings) against the debtor's personal property. Enforcement should therefore be sought first against the debtor's personal assets (if any) and enforcement against charged property by *saisie* proceedings may then be used to recover the balance of the debt. If judgment has been granted in favour of the creditor leave is automatically granted to execute against the debtor's **personalty**.

Commented [DJ28]: One mark

The *saisie* process begins with the principal creditor making an application to seek a preliminary vesting order (or "**PVO**") from the Royal Court – this is essentially an application to seek leave to pursue the debtor's realty. The PVO may be sought upon granting of the judgment in favour of the principal creditor (which occurs without notice) or subsequently by summoning the debtor. A creditor may also apply for registration in the *Livre des Hypotheques*, either in addition to or instead of the **PVO**.

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A PVO will usually be granted by the Royal Court unless there is a compelling reason to the contract – e.g. if the debtor can prove there is a realistic prospect of payment or has a valid appeal.

The effect of the PVO is that the debtor retains ownership of the realty, but loses the right to use, let, possess and receive payment of rent in respect of the realty – such rights are assigned to the principal creditor. The principal creditor may (if it chooses) evict the debtor and/or their family. During the *saisie* process, the debtor may sell the realty, but the consent of the PVO holder (i.e. principal creditor) and other secured creditors is **required**.

Commented [DJ30]: One mark but again beware of repeating the Guidance Text

(b) Stage 2: Interim Vesting Order

At this stage, the principal creditor will apply, by way of summons, for the debtor to appear before the Jurat Commissioner to determine whether there is any dispute over the amount claimed. The principal creditor will provide a statement of account of the debt, including all costs and expenses, less any sums received (e.g. rent). The debtor has an opportunity to examine and make representations in respect of such account. The Jurat Commissioner will make a finding and certify an amount due to the principal creditor in their report, which the Commissioner will sign.

Commented [DJ31]: One mark

Following this, the debtor will be summonsed before the Royal Court, known as *Plaids d'Heritage* - the PVO holder (i.e. principal creditor) will request that the debtor either repay the debt owed to them or renounce their ownership of and vacate the realty. If the debtor does not pay the debt (as certified by the Commissioner), then an IVO will be granted.

An IVO extinguishes the debtor's right and title in the realty and the realty is vested in the principal creditor as trustee for all claimants against the realty. The principal creditor then has to insure, let or maintain the realty for the benefit of other creditors.

After the IVO is granted, the principal creditor must then request that the *Greffe* opens the Register in order that the debtor's creditors may come forward to register their claim(s). The principal creditor must publish a notice to other creditors on two occasions in the *Gazette Officielle* that the Register is open. The Register remains open for 28 working days from the date of the second notice. Every creditor who registers a claim loses the right to enforce their claim against the debtor's personality.

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When the Register closes, the principal creditor must summons all creditors who have registered claims to appear before the Jurat Commissioner in order to marshal all received claims (i.e. verified and placed in order of priority) – claims are ordered in date of registration and then by date entered on the Register of Claims. The principal creditor must also present the costs and expenses incurred by it since the IVO was granted. The outcome of the marshalling of claims and priority is certified by the Jurat Commissioner in a further report. The Jurat Commissioner will also set a date for the Final Vesting Order ("FVO").

The principal creditor who opened the Register can elect to pay all of the registered creditors' claims – if so, such registered creditor may apply for a FVO, but may not then challenge the amount of a registered claim (see *Moulin Huet Holdings v Moulin Huet Hotels [1995] RC*).

Commented [DJ33]: One mark

(c) Stage 3: Final Vesting Order

The principal creditor may summons each registered creditor to appear before the *Plaids d'Heritage* and the principal creditor will then appear with each registered creditor, starting with the lowest priority. Each registered creditor is asked to elect if they wish for the realty to be vested in them, on the condition that they pay all higher ranking creditors, or if they wish to renounce their claim to the realty. There will be a certain point at which the 'value breaks' – i.e. where the value of the realty will be sufficient to pay a creditor's debts and those higher ranking creditors above him.

If the registered creditor renounces his claim, he loses the right to pursue the claim in any form against the debtor (or any other party).

If a creditor elects to accept the realty, he will be granted the FVO. The creditor must pay all higher ranking creditors within 15 days (or such other time limited as ordered).

If the creditor defaults on this obligation, higher ranking creditors can make claims against the creditor or seek rescission of the FVO in favour of the next ranking creditor who will accept the realty.

Commented [DJ34]: This section is largely copied from the Guidance text

An FVO acts as a conveyance of realty and is automatically registered with the *Greffe* – the creditor that elected to take the realty is then sole legal owner and may dispose of it (or not) as they choose. The creditor is under no obligation to inform the debtor of any 'equity' (or windfall) realised (see *Pirito v Curth [2004] RC (on appeal from COAld)*). The debtor's rights are protected by virtue of the ability to postpone the IVO in order to sell the property and discharge the debt. In practice, banks will often pay back any surplus.

The *saisie* process is relatively long (approximately 6 months) and is designed to provide the debtor the maximum opportunity to pay off debts and keep their property.

Before commencing the *saisie* process, a creditor should consider the following: (a) whether the debtor has any personal assets which can be enforced against; (b) enforcement pursuant to any security; (c) the creditor's position amongst creditors of the debtor (e.g. priority and ranking), and the potential consequences of the *saisie* process.

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QUESTION 4 (fact-based application-type question) [15 marks in total]

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In July 2016, Andy and Bob incorporated a company (Athletico Ltd) that specialised in selling novelty football T-shirts. Andy and Bob were the company's only members and directors. For the past 18 months, the company has been experiencing financial difficulties. In September 2018, the company's overdraft with Beardsley Bank plc had reached its limit of £250,000. In return for increasing the overdraft limit to £300,000, Beardsley Bank plc demanded security for the additional borrowing and took a bond over the company's property (valued at £100,000). In December 2018, Athletico Ltd borrowed £100,000 from a friend, Barry Homeowner, who also took a bond over the same property.

The business continued to struggle and in February 2019 Andy and Bob were informed by the company's auditor that insolvent liquidation was inevitable, although Andy and Bob disagreed and held out hope that the company's financial prospects would improve. Andy and Bob decided to try and trade their way out of their financial difficulties by having a sale. Unfortunately, the sale failed to increase business and in May 2019 Athletico Ltd was wound up compulsorily. By this time, the company's overdraft with Beardsley Bank amounted to £290,000.

Debbie and Rahid have been appointed as joint liquidators and have discovered several facts:

- in March 2019, Andy and Bob caused the company to repay an unsecured loan of £5,000, which Bob had made to the company some months before;
- in addition to the money owed to Beardsley Bank and Barry Homeowner, the company owes £10,000 to the Guernsey Revenue Service for unpaid tax, £30,000 to employees in wages, and £100,000 to unsecured creditors.

Debbie and Rahid estimate that the total remaining assets of Athletico Limited amount to £440,000. Debbie and Rahid's expenses in acting as liquidators amount to £3,000. Advise Debbie and Rahid, addressing the following:

- (a) the role of the joint liquidators;
- (b) how to pool the assets;

(c) potential claims against the directors; and

(d) how to manage distributions to creditors.

Role of Joint Liquidators

In summary, the role of the joint liquidators is to collect and realise Athletico Ltd's ("**Athletico**") assets and to distribute dividends according to the statutory order of priority.

In particular, upon appointment as liquidators, Debbie and Rahid may: (i) bring or defend civil actions on behalf of Athletico; (ii) carry on the business of Athletico, to the extent beneficial for the winding up of Athletico; (iii) make capital calls; (iv) sign all receipts and other documents on behalf of Athletico; (v) do any other act relating to the winding up of Athletico; and (vi) do any Court-authorized act. To the extent they consider it necessary, Debbie and Rahid may approach the Court to seek the Court's directions in respect of any matter arising in connection with the winding up of Athletico.

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Importantly, following the appointment of Debbie and Rahid as liquidators, all the powers of Andy and Bob as directors of Athletico will cease, except to the extent otherwise ordered or agreed by the Court and Debbie and Rahid (in their capacities as liquidators), and Athletico must cease to carry on business, except so far as is necessary for the beneficial winding up of Athletico.

Immediately following their appointment, Debbie and Rahid (in their capacities as liquidators) must send a copy of the compulsory winding up order to the Registrar of Companies within 7 days of their appointment. It would also be good practice for Debbie and Rahid to contact all known creditors of Athletico to provide them notice of their appointment.

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How to pool Athletico's assets

As a matter of Guernsey law, subject to any preferential payments, all creditors participate in the common pool of Athletico's assets in proportion to the size of their admitted claims (i.e. on a *pari passu* basis).

This principle will only apply to provable debts payable to the general body of creditors; and within each separate class of preferential, ordinary and postponed creditors. It will not affect the rights of secured creditors, any suppliers of goods with retention of title rights; or creditors for whom Athletico hold assets on trust.

Commented [DJ39]: One mark

It is not clear from the fact pattern above, that Athletico forms part of a group of companies. Accordingly, it would not be necessary for Debbie and Rahid to consider issues relating to the pooling of assets and liabilities between companies forming a single group. However, to the extent this was the case, there is authority in Guernsey for such approach (see *In the matter of Huelin Renouf Shipping Limited in liquidation (2015) (Unreported, Royal Court, 4th September) (Guernsey Judgment No. 46/2015)*).

Commented [DJ40]: Excellent answer – one mark

Potential claims against the directors

There are a number of potential grounds upon which Debbie and Rahid may assert and/or pursue claims against Andy and Bob in their capacities as directors of Athletico:

(a) **Breach of Fiduciary Duty:**

It would appear from the fact pattern outlined above that from at least September 2018, Athletico has been struggling financially. It has been necessary for Athletico to seek further financial support in order to continue operating – including extending Athletico's overdraft with Beardsley Bank and borrowing further funds from Barry Homeowner.

It appears that notwithstanding advice obtained from Athletico's auditor that "insolvent liquidation was inevitable", Andy and Bob (in their capacities as directors) considered that they knew better and sought to attempt to trade-out of Athletico's financial difficulties. In such circumstances, it may not have been reasonable for Andy and Bob to adopt the view that it was appropriate to continue to trade.

Athletico was clearly in the "zone of insolvency" and Andy and Bob ought to have borne in mind the interests of creditors in making any determination to continuing to trade.

It is not clear from the fact pattern outlined above whether Andy and Bob (in their capacities as directors) initiated the compulsory liquidation proceedings in respect of Athletico. If Andy and Bob did not initiate the compulsory liquidation proceedings in such capacity, there may be grounds to bring a claim for breach of fiduciary duty for failing to do so, in circumstances where Athletico had no prospect of avoiding insolvent liquidation.

Moreover, Debbie and Rahid may consider whether to bring claims for breach of fiduciary duty against Andy and Bob on the basis that they incurred further financial liabilities at a point when they knew (or ought to have known) that there was no realistic prospect of Athletico avoiding insolvency – in that they extended their overdraft with Beardsley Bank and incurred a £100,000 liability to Barry Homeowner. This was not *bona fide* in the best interests of the company.

Additionally, Andy and Bob failed to act for proper purposes and/or to avoid conflicts of interest in determining that it was appropriate to repay the £5,000 loan to Bob immediately prior to Athletico's entry into liquidation and at a time when they knew (or ought to have known) that there was no realistic prospect of Athletico avoiding insolvency.

To the extent that Debbie and Rahid are able to prove to the satisfaction of the Court that Andy and Bob breached their fiduciary duties, the Court may order that they be required to contribute to the assets of Athletico (i.e. Bob may be required to repay the £5,000 funds received by him) or they both may be required further amounts (i.e. the amount lost (together with any interest thereon) between the period in which Athletico should have ceased trading, but did not).

The test of whether Andy or Bob acted in breach of fiduciary duty is subjective – and Andy and Bob may be able to show that they honestly believed the steps they were taking were in the best interests of Athletico, in which case they may not be found to be in breach of fiduciary duty.

(b) Preference:

Debbie and Rahid may consider whether to apply to the Court for an order to set aside the transaction whereby Athletico repaid the unsecured loan in the amount of £5,000 to Bob in March 2019 – it would appear that such payment may constitute a preference:

- (i) the loan repayment appears to have been made at a time when Athletico was insolvent. It is not clear from the fact pattern whether Athletico became insolvent as a result of such loan repayment;

Commented [DJ41]: One mark

Commented [DJ42]: One mark

Commented [DJ43]: One mark – this is a good summary of the directors' duties considerations.

- (ii) although it is not clear from the fact pattern than date of the compulsory liquidation application, it would appear that the loan repayment was made within 2 months preceding the order for compulsory winding up of Athletico. For these purposes, it is noted that Bob would be a 'connected party' to Athletico – being a director of Athletico – and therefore the subject payment would fall within the look back period of two years;
- (iii) moreover, the loan repayment was made to Bob – being one of Athletico's creditors - and resulted in him being paid in full, therefore improving his position in the liquidation of Athletico (see below for more information – however, it would not appear that Bob would have been repaid in full in the liquidation); and
- (iv) whilst it is not clear from the fact pattern that Andy and/or Bob (in their capacities as directors of Athletico) were motivated by the 'desire to prefer' Bob in paying him back in full. However, given Bob is a 'connected party' and the payment was made during the reference period, the loan repayment will be presumed to be outside the course of ordinary business of Athletico and therefore a **preference**.

Commented [DJ44]: One mark

To the extent that Debbie and Rashid are able to prove to the satisfaction of the Court that the repayment of the loan to Bob is a preference it may make such order as it thinks fit to restore Athletico to restore it to the position it would have been in had the loan repayment not been made. In particular, the Court may make an order that Bob in his capacity as recipient of the £5,000 repay the sum to Athletico, and/or Bob and Andy (in their capacities as directors) be personally liable for such **amount**.

Commented [DJ45]: One mark – excellent answer again.

(c) Wrongful Trading / Fraudulent Trading:

Debbie and Rahid may consider whether to bring claims against Andy and Bob (in their capacities as directors) in respect of wrongful trading and apply for the Court to make a declaration that Andy and Bob be liable to contribute to the assets of Athletico.

It would appear that from at least February 2019 (if not before) that Andy and Bob were aware that there was no reasonable prospect of Athletico avoiding insolvent liquidation. There is no evidence in the fact pattern above that Andy and Bob have any available defences – namely that they took every reasonable step to avoid and minimise losses to creditors – in fact they diminished the assets of Athletico available for distribution to creditors by repaying a loan in the amount of £5,000 to Bob in March 2019. In such circumstances, if Debbie and Rahid are successful in this claim, Andy and Bob would be required to pay at least £5,000 to Athletico (plus applicable **interest**).

Commented [DJ46]: One mark

To the extent Debbie and Rahid are able to prove that Andy and Bob ought to have been aware of Athletico's insolvency before this date – which may be possible depending on the facts – then Andy and Bob may be required to contribute more towards Athletico – e.g. any amounts incurred and paid out from that **time**.

Commented [DJ47]: One mark

It is not clear from the fact pattern above that Andy and Bob carried out the business of Athletico with any intent to defraud creditors as a result of which Andy and Bob may be required to both contribute towards the assets of Athletico and may be criminally liable.

Distributions to creditors

Based on the fact pattern above, it is understood that each of Beardsley Bank and Barry Homeowner have a bond over a property which has been valued at £100,000. Their claims are in the amount of £290,000 and £100,000, respectively – being a total amount of £390,000. To the extent that they seek to enforce their security, and assuming that Beardsley Bank properly registered the bond at the time it was granted or immediately thereafter (i.e. before the bond granted to Barry Homeowner), it will rank in **priority**.

Commented [DJ48]: One mark

The proceeds of the sale of the property the subject of the collateral will be applied in the following order: (i) first, to pay the costs and expenses of the sale; (ii) second, to discharge any prior security interest – it does not appear from the fact pattern that any security ranks in priority to Beardsley Bank; (iii) third, to discharge all monies properly due in respect of the obligation secured by the security agreement – in this case, it does not appear that there will be sufficient proceeds realised by the sale to discharge the debt due and payable to Beardsley Bank. It is not necessary to consider the remaining waterfall of payments.

Each of Beardsley Bank and Barry Homeowner will then claim in the liquidation for the balance of their claims against Athletico, in the amount of £190,000 and £100,000 (i.e. in full), **respectively**.

Commented [DJ49]: One mark – very good analysis save that the facts suggest that only the bank's further borrowing may have been secured by its bond so that there may have been a balance available to repay some of Barry's secured debt.

I understand that Athletico's assets, less the value of the property (£100,000) amounts to £340,000. Following the realisation of these assets by Debbie and Rahid, this balance will be applied in the following order of priority:

- (a) Expenses of the winding up – in this case in the amount of £3,000 (leaving a balance of £310,000);
- (b) Preferential debts – in this case, in the total amount of £40,000 (of which £10,000 is payable to the Guernsey Revenue Service for unpaid tax, and £30,000 is payable to employees in wages) (leaving a balance of £270,000);
- (c) Ordinary debts – in this case, in the total amount of £390,000. There are insufficient assets realized from the proceeds of the sale of Athletico's assets to satisfy all unsecured claims (including the unsecured portion of Beardsley Bank and Barry Homeowner's claims) in full. These debts will be paid *pari passu* (i.e. pro **rata**).

Commented [DJ50]: One mark

Following realisation of Athletico's assets, Debbie and Rashid must apply for the appointment of a Court Commissioner to examine their accounts and distribute the funds derived from Athletico Ltd's assets. The Commissioner must: (a) arrange a creditors' meeting to examine and verify the financial statements and the creditors' claims and preferences; and (b) fix a date for distribution of Athletico's **assets**.

Commented [DJ51]: One mark – this final answer was overall very strong.

*** End of Assessment ***

Commented [DJ52]: Total mark of 43/50