INSOL INTERNATIONAL
FOUNDATION CERTIFICATE
IN INTERNATIONAL INSOLVENCY LAW

SUMMATIVE (FORMAL) ASSESSMENT: MODULE 3B

THE INSOLVENCY SYSTEM OF THE UNITED KINGDOM (ENGLAND AND WALES)

This is the**summative (formal) assessment**for**Module 3B**of this course and is compulsory for all candidateswho **selected this module as one of their compulsory modules from Module 3**. Please read instruction 6.1 on the next page very carefully.

If you selected this module as **one of your elective modules**, please read instruction 6.2 on the next page very carefully.

The mark awarded for this assessment will determine your final mark for Module 3B. 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 MS Word format, using a standard A4 size page and a 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: **[studentID.assessment3B]**. An example would be something along the following lines: 20222-514.assessment3B. **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 "studentID" 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**.

6.1 If you selected Module 3B as one of your **compulsory modules** (see the e-mail that was sent to you when your place on the course was confirmed), the final time and date for the submission of this assessment is**23:00 (11 pm) GMT on 1March 2022**. The assessment submission portal will close at 23:00 (11 pm) GMT on 1 March 2022. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.

6.2 If you selected Module 3B as one of your **elective modules** (see the e-mail that was sent to you when your place on the course was confirmed), you have a **choice** as to when you may submit this assessment. You may either submit the assessment by **23:00 (11 pm) GMT on 1March 2022** or by **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. If you elect to submit by 1 March 2022, you **may not** submit the assessment again by 31 July 2022 (for example, in order to achieve a higher mark).

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 [WPA1]: 45/50 = 90% a very good piece of work indeed. It is only one misidentification of issue at the end which mars an otherwise near perfect paper.

Commented [WPA2]: 10/10

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

Please select the **most correct ending** to the following statement:

The Administration (Restrictions on Disposal etc to Connected Persons) Regulations 2021 restrict pre-pack sales which constitute a substantial disposal of the company's property to connected parties where the disposal occurs:

(a) within 10 weeks of the commencement of the administration.

(b) within 8 weeks of the commencement of the administration.

(c) within 4 weeks of the commencement of the administration.

(d) on the day the company enters administration.

Question 1.2

What is the **maximum length** of a Moratorium under Part 1A of the Insolvency Act 1986 to which creditors can consent without any application to the court?

(a) 40 business days.

(b) One year and 20 business days.

(c) One year and 40 business days.

(d) One year.

Question 1.3

Which of the following **is not** a requirement for a company that wishes to enter into a Restructuring Plan under Part 26A of the Companies Act 2006?

(a) The company has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, its ability to carry on business as a going concern.

(b) A compromise or arrangement is proposed between the company and its creditors, or any class of them, or its members, or any class of them.

(c) The purpose of the compromise or arrangement is to eliminate, reduce or prevent, or mitigate the effect of, any of the said financial difficulties.

(d) The company is, or is likely to become, unable to pay their debts, as defined under section 123 of the Insolvency Act 1986.

Question 1.4

In cases where the Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021 apply and an independent report from an Evaluator is obtained, the independent report must be obtained by whom?

(a) The administrator.

(b) Any secured creditor with the benefit of a qualifying floating charge.

(c) The purchaser.

(d) The company's auditor.

Question 1.5

Which one of the following **is not** a debtor-in-possession procedure?

(a) Administration.

(b) Restructuring Plan.

(c) Scheme of Arrangement.

(d) Company Voluntary Arrangement.

Question 1.6

A liquidator may pay dividends to small value creditors based upon the information contained within the company's statement of affairs or accounting records. In such circumstances, a creditor is deemed to have proved for the purposes of determination and payment of a dividend where the debt is **no greater than how much**?

(a) £500

(b) £750

(c) £1,000

(d) £2,000

Question 1.7

Which one of the following **is not**, in itself, a separate ground for disqualification of a director under the Company Directors Disqualification Act 1986?

(a) Wrongful trading.

(b) Breach of fiduciary duty.[1]
(c) Being found guilty of an indictable offence in Great Britain.

(d) Being found guilty of an indictable offence overseas.

Question 1.8

The administrator is under a general duty to provide a statement for creditors' consideration setting out proposals for achieving the purpose of administration.He or she must obtain a creditors' decision on whether or not to approve the proposals **within how many weeks** of the date the company entered administration?

(a) 6

(b) 8

(c) 10

(d) 12

Question 1.9

Which of the following statements is **incorrect**?

(a) An insolvency officeholder from an EU Member State will be automatically recognised by the courts in the UK whether the officeholder was appointed before or after Brexit.

(b) An insolvency officeholder from an EU Member State is automatically recognised by the courts in the UK if appointed before Brexit.

(c) An insolvency officeholder from an EU Member State appointed after Brexit may apply to a UK court for recognition under the Cross Border Insolvency Regulations.

(d) An insolvency officeholder from an EU Member State cannot apply to a UK court for recognition under section 426 of the Insolvency Act 1986.

Question 1.10

Under section 216 of the Insolvency Act 1986, a director of a company which has been wound up insolvent may not, unless an exception applies, be a director of a company that is known by a prohibited name **for what period of time**?

(a) 6 months.

(b) 12 months.

(c) 2 years.

(d) 5 years.

[1] Company Directors Disqualification Act 1986, Schedule 1

QUESTION 2 (direct questions) [10 marks]

Commented [WPA3]: 9/10

Question 2.1 [maximum 5 marks]

Commented [WPA4]: 4/5 – s 16(2) CDDA does not apply to s 6 applications

Who may bring an action under: (i) section 423 of the Insolvency Act 1986; (ii) section 6 of the Company Directors Disqualification Act 1986; and (iii) section 246ZB of the Insolvency Act 1986?

Those who may bring an action under the three sections mentioned include the following:-

(i) Under s. 423 of the Insolvency Act 1986 (the "Act") relating to defrauding creditors the following may bring an action:

- Where the company is being wound-up, the official receiver, the liquidator and the administrator as well as the any victim e.g. a creditor (with leave of the Court).
- If the supervisor of a CVA where the creditor victim is a party to a CVA or any victim whether or not they are a party to a CVA.
- Any other victim of the transaction in question.

(ii) Under s. 6 of the Company Directors Disqualification Act 1986 (the "CDDA") which is the most commonly used - deals with unfitness of Directors of insolvent companies. The criteria which requires satisfying includes that the person is or was the Director which has become insolvent and that his conduct makes him unfit to management the company[2]. The following may bring an action via Court or via the Secretary of State by accepting a disqualification undertaking:

- Liquidators, Administrators. Administrative Receiver
- Assignees (for example a third party funder)
- Secretary of State or Official Receiver[3]
- any past or present member or creditor of any company[4]

(iii) Under s.246ZB[5] of the Act where there has been alleged wrongful trading[6] by Directors, the following may bring an action:

- Administrators[7]

It was the Small Business, Enterprise and Employment Act 2015 that introduced the ability for administrators to bring an action, inserting the new s.246ZB into the Act[8]

Although not specifically asked in this part of the question, liquidators also have the ability to bring actions under s.214. Creditors and contributories are not permitted.

Question 2.2 [maximum 5 marks]

Commented [WPA5]: 5/5

List the **five(5)**qualifying decision procedures by which creditors may make decisions in the context of an insolvent company.

[2] Company Directors Disqualification Act 1986, s6(1)(a) and (b)
[3] Company Directors Disqualification Act 1986, s.7
[4] Ibid, s16(2)
[5] Insolvency Act 1986, s.246ZB
[6] Insolvency Act 1986, s.246ZB and s.214
[7] Insolvency Act 1986, s.246ZB(1)
[8] Ibid

The Act sets out that any decision to be made by creditors can be made by using one of the 5 qualifying decision procedures[9] that are deemed appropriate by the office-holder[10]. Under Part 15, "*Chapters 2 to 11 apply where the Act or these Rules require a decision to be made by a qualifying decision procedure, or by a creditors' decisions procedure, or permit a decision to be made by the deemed consent procedure…*"[11].

A 'decision procedure' means a qualifying decision procedure or a creditors' decision procedure as detailed in Rule 15.3[12]. It is deemed that a physical meeting will not be convened unless 10% in value of creditors, 10% in number or 10 creditors[13]. As listed in the Insolvency Rules the following are the 5 qualifying decision procedures[14] by which a decision may be sought from creditors:

1] Correspondence
A notice must be sent to the creditors providing a timeframe within which a decision is required.

2] Electronic-voting[15]
Any notice should give the creditor information about when and how to vote, if not taking place via a meeting, including providing the ability to vote e.g. providing the password for any platform to be used following delivery of the notice and up to when a decision is required to be made. Information must not be disclosed in relation to the voting cast by creditors.

3] Virtual Meeting[16]
The notice provided prior to these types of meetings must ensure it provides the creditor with the ability to access the meeting together with a statement that the meeting could be suspended or adjourned by the chair.

4] Physical Meeting[17]
Within 5 business days of a Notice being delivered to a creditor a request may be made for a physical meeting (unless the rules provide to the contrary). The convener must check any requests and check if they meet the requisite requirements[18]. If the requirements are met then Notice must be given to all creditors that the meeting will be physical in accordance with Rule 15.8 and the Notice must contain, a statement that the meeting could be suspended or adjourned by the chair, that the previous decision procedure or deemed consent has been superseded. This Notice must be sent within 3 business days after the requisite threshold requirement has been met requesting a physical meeting. Remote attendance can still be requested before the meeting and the Notice should include the convener's ability to be able to agree to a creditor attending a physical meeting remotely.

5] Any other procedure for decision making which allows all creditors to participate equally.

For a decision to be passed, on the whole, a majority in value is sufficient[19].

[9] Insolvency Act 1986, s. 246ZE and paragraph 8A of Schedule 8
[10] Insolvency Act 1986, s. 230 (must be a qualified insolvency practitioner)
[11] The Insolvency (England and Wales) Rules 2016, Part 15, Chapter 1, rule 15.1
[12] Ibid, Part 15, Chapter 2, rule 15.2
[13] Insolvency Act, s. 246ZE(7)
[14] The Insolvency (England and Wales) Rules 2016, Part 15, Chapter 2, rules 15.3 to 15.7
[15] Ibid, rules 15.4
[16] Ibid, rule 15.5
[17] Ibid, rule 15.6
[18] Insolvency Act 1986, s. 246ZE(7) (10% in value, 10% in number or 10 creditors)
[19] The Insolvency (England and Wales) Rules 2016, Part 15, Chapter 8, rule 15.34(1) and 15.31(5)

The Deemed Consent Procedure[20] is also used as an alternative to the above. Notice is given to creditors and if there is no objection to the decision, it will be deemed effective. Deemed consent can be used widely for most decisions but it cannot be used for deciding office-holders remuneration.

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

Commented [WPA6]: 15/15

Question 3.1[maximum 6 marks]

Commented [WPA7]: 6/6

Can an administrator who wishes to continue to operate the business of the company in administration require suppliers of goods and services to continue to supply those goods and services during the administration?

Whether an Administrator can require the suppliers to continue with service to the company while it is in administration depends upon whether what is being supplied is an essential service or not.

An Administrator who wishes to continue to operate the business which is in administration can continue using contracts which are already in place at the time the company goes into administration[21]. Contracts do not automatically terminate upon a company entering into administration. Executory contracts for the supply of goods and services are provided for under the Act[22]. It is with the backdrop of the purpose of the implementation of the Insolvency Act 1986 in mind, being to rescue a company where possible, that some of the protections to achieve this end were born.

Where a company goes into administration, after the effective date[23], the Administrator can request the supplier of the goods or services to continue. The supplier cannot withhold the supply on condition that unpaid debts accrued, prior to the effective date, are cleared first before the supply continues[24] - this is not permitted pursuant to the Act in relation to some deemed essential services [25] , such as gas, electric, water and communications. Communications includes, point of sale, computer hardware/software, advice/technical assistance, data storing/processing and web hosting[26]. Automatic terminations would likely be deemed void.

There are further protections and restrictions in this regard within the Act[27] for essential services. Even where the contract itself states that any insolvency related action would terminate the supply contract, a supplier of an essential service is not permitted to terminate under the Act[28] unless, the administrator consents, the Court grants permission or when any payments due within 28 days to the supplier, post the effective date, have not been paid by the Administrator[29]. A further protection outlined in the Act is that a supplier could write to the Administrator giving notice of termination unless a personal guarantee is given by the

[20] Insolvency Act 1986,s. 246ZF and The Insolvency (England and Wales) Rules 2016, Part 15, Chapter 2, rule 15.7
[21] Insolvency Act 1986
[22] Insolvency Act 1986, s. 233
[23] Insolvency Act 1986, s. 233(4)(a)
[24] Ibid, s. 233(2)
[25] Ibid, s. 233(3)
[26] Insolvency Act 1986, s 233(3A)
[27] Ibid, s.233A
[28] Insolvency Act 1986, s. 233A(3)
[29] Insolvency Act 1986, s.233A(4)

Administrator for payments in relation to the continuation of supply after the company went into administration. If the Administrator fails to respond within 14 days the supplier is permitted to terminate supply.

Further protections were more recently introduced by the Corporate Insolvency and Governance Act 2020[30] in relation to the supply of goods and services generally. This Act inserted a new section into the Act[31], section 233B, which applies to most insolvency related procedures, including administration. The supplier is unable to terminate or do any other thing that would allow the supplier to terminate, save for some limited exceptions - similar in part to those mentioned above. There are also exclusions in the application of this new section which are detailed in Schedule 4ZZA to the Act.

Question 3.2[maximum 9 marks]

Commented [WPA8]: 9/9

Explain the order of priority of payments in a liquidation and explain the nature of the rights enjoyed by each class of creditor or expense.

Section 115 of the Act and the Insolvency Rules[32], detail that priority is given to expenses of the liquidation[33] before all other classes[34] -

1. Liquidators fees and expenses
   - Expenses incurred properly by the liquidator in the process of bringing in or realising company assets, including legal expenses
   - Any security costs provided by the liquidator
   - Costs involved in preparing the statement of affairs
   - Necessary dibs in the winding-up
   - Those employed by the liquidator to carry out work for the company
   - Remuneration of the liquidator
   - Corporation tax on realised assets in the course of the liquidation
   - Any other expenses properly incurred in the course of the winding-up

   The rights enjoyed by the Liquidator are a long standing and necessary part of the order of priority of payments. If there was no ability for a Liquidator to recover the necessary costs and expense of the liquidation then it would be unlikely that any professional would have the financial ability to deal with the complex process of winding-up a company.

2. Preferential Creditors are defined in the Act. This preferential debts regime[35] applies to not only companies in liquidation but to all insolvency procedures and is considered once the expenses noted above have been paid out and before floating charge holders or unsecure creditors. There are two classes of preferential debts, ordinary[36] and secondary[37]. The ordinary are paid before the secondary and both respective classes are paid on an equal footing within the two classes[38]. They include the following:

[30] Corporate Insolvency and Governance Act 2020
[31] Insolvency Act 1986, s. 233B
[32] The Insolvency (England & Wales) Rules 2016, rules 6.42 and 7.108
[33] Insolvency Act 1986, s. 115
[34] Save for any 'Moratorium debt' which may require payment pursuant to s. 174A of the Act (introduced by the Corporate Insolvency Governance Act 2020)
[35] Insolvency Act 1986, ss. 386, 387 and Schedule 6 and general provisions in a winding-up under s. 175
[36] Ibid, s. 175(1A) and Schedule 6 paragraphs 8 – 15B
[37] Ibid, s. 175(1B) and Schedule 6 paragraphs 15BA, 15BB or 15D
[38] Ibid

- Employment claims:
    - Contribution by the employee to a pension in the 4 month period prior to commencement of winding-up
    - Contribution by the company to the employee pension for the 12 month period before the relevant date
    - Monies owed by the company to someone who is/has been an employee over the 4 month period before commencement (max total £800)
    - Monies owed to any employee in relation to holiday entitlement, a authorised absence from work or sickness (deemed wages)
    - Monies advanced to pay wages or holiday pay – which is designed to protect lenders where money has been used for that purpose
- Levies on the production of coal and steel (rarely required to be used)
- Claims ordered to be owed by the company under the Reserve Forces (Safeguard of Employment) Act 1985 (rarely required to be used)
- Other recently added that are classed as ordinary preferential in this specific context, where payments have been made to those with deposits but the financial institution has itself become insolvent and compensation has been sought under the Financial Services Compensation Scheme [39] (that do not exceed the compensation payable to a person under the Scheme)
- Other deposits are treated as secondary preferential and include[40],
    - Deposits where the sums exceed the compensation payable to a person(s) under the Scheme
    - Deposit made via a non-UK branch and would be eligible if made via a UK branch
- Another secondary preferential debts includes, PAYE, VAT, National Insurance, Construction Industry Scheme and student loan contributions[41]. Taxation liability claims, where the company has effectively acted as a tax collector for the Government then these may fall into the 'Preferential' debts bracket[42]. However, where tax liabilities are not preferential, for example where corporation tax on chargeable gains accruing when assets are obtained, will rank down with the unsecured creditors.

Those who fall into the preferential classes have been permitted to enjoy these rights for various reasons. Employment related priority has been enjoyed for a long period of time under various statutory protections for what are usually fairly modest claims, including when a company goes into liquidation.

The reasoning behind the reintroduction of certain tax related liabilities being given preferential treatment recently was outlined in the Explanatory Notes to the Finance Bill[43]. It stated that "*the government would change the rules so that when a business enters insolvency, more of the taxes paid in good faith by its employees and customers and temporarily held by the business go to fund public services rather than being distributed to other creditors*"[44].

3. After preferential creditors have been paid then floating charge[45] holders are next in line (charges that are not fixed or secured on a particular asset). Should there be multiple floating charge holders then usually the charge which was created first takes

[39] Insolvency Act 1986, Schedule 6 paragraphs 15AA and 15B
[40] Insolvency Act 1986, Schedule 6, paragraphs 15BA, 15BB, 15D
[41] Insolvency Act 1986, Schedule 6, paragraph 15D
[42] Finance Act 2020, Section 95
[43] Explanatory Notes to the Finance Bill 2020
[44] Ibid, Clause 95, Background Notes, paragraph 13
[45] Insolvency Act 1986, s. 176A(9)

priority, following the maxim '*qui prior est tempore potior est jure'* meaning the first in time prevails. Any Liquidator should initially look to section 176A of the Act[46] that applies to all floating charges after 15 September 2003[47], where the company has gone into liquidation (and other insolvency procedures). The section was added to the Act during the myriad of changes implements by the Enterprise Act 2002. The Liquidator essentially must carve out a 'prescribed part'[48] of 'net property'[49] of the company, after liquidator expenses and preferential creditors have been paid, and save it for unsecured creditors - it cannot be used to pay floating charge holders.

The minimum value of the company's net property is £10,000[50] the prescribed part will be 50% if the assets do not exceed £10,000. If the assets do exceed then the prescribed part is calculated at 50% up to £10,000 and then 20% over up to a limit of £800,000 for floating charges after 6 April 2020[51]. Floating charges prior to this date or "*Grandfather floating charges"* will still have the limit of £600,000[52].

The main reason, as outlined in the Explanatory Note for the 2020 Order[53] why the lowest ranking creditors enjoy some protection in effect as a result of there being a 'prescribed part' is to ensure that the higher ranking floating charge holder does not absolutely prevent the lowest ranking from recovering a proportion of realised assets (if indeed there are any assets left)[54].

4. Unsecured Creditors often end up with nothing after all other creditor have been paid out. The prescribed part above goes some way at least to ensure those unsecured creditors enjoy and possibly recover something.

5. Shareholders are paid last.

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

Commented [WPA9]: 11/15

Prior to going into compulsory liquidationon 23rdDecember 2021, under pressure from its bank, Stercus Bank plc, and in order to prevent it from demanding repayment of the company's loans, Corfee Zero Limited ("the Company"),granted a debenture in favour of Stercus Bank plc in February 2021. The debenture contained a floating charge over the whole of the Company's undertaking.

The winding up order followed a creditor's winding up petition issued on 14th October 2021.

[46] Insolvency Act 1986, s. 176A
[47] The Insolvency Act 1986 (Prescribed Part) Order 2003, paragraph 1
[48] Insolvency Act 1986, s. 176A (2)
[49] Ibid, s. 176A(6)
[50] The Insolvency Act 1986 (Prescribed Part) Order 2003, paragraph 2
[51] Insolvency Act 1986 (Prescribed Part) (Amendment) Order 2020 (this amends the limit from £600 to £800k)
[52] https://www.engage.hoganlovells.com/knowledgeservices/news/prescribed-part-to-increase-from-600000-to-800000-from-6-april-2020 and the [52] Insolvency Act 1986 (Prescribed Part) (Amendment) Order 2020 , Explanatory Note, paragraph 7.5
[53] Insolvency Act 1986 (Prescribed Part) (Amendment) Order 2020
[54] Insolvency Act 1986 (Prescribed Part) (Amendment) Order 2020 , Explanatory Note, paragraph 7.2: https://www.legislation.gov.uk/uksi/2020/211/pdfs/uksiem_20200211_en.pdf

In July 2021, as the Company continued to suffer cash flow problems, the directors approved the sale of 5coffee roasting machines to Ann Young (a director) for £10,000 in cash. The machines had been bought for £25,000 a year before.

A month before the winding up order was made, Ann Young received an email from Beans and Leaves Ltd, one of the Company's key suppliers. The supplier demanded immediate payment of all sums owing to it and informed the Company that further supplies would only be made on a cash on delivery basis. As the continued supply of coffee beans was seen as essential by the Company, the board authorised a payment of £8,000 to cover existing liabilities and agreed to further payments, on a cash on delivery basis, for further supplies which amounted to further payment of £3,000 up to the date of the winding up order.

The liquidator has asked for advice whether any action may be taken in respect of the floating charge in favour of Stercus Bank plc and the two subsequent transactions.

Using the facts above, answer the questions that follow.

Identify the relevant issues and statutory provisions and consider whether the liquidator may take any action in relation to:

Question 4.1 [maximum 5 marks]

Commented [WPA10]: 5/5

The floating charge in favour of Stercus Bank plc;

A Debenture containing a floating charge was taken out over the whole Company's undertakings in February 2021 and 8 months later a Winding-up Petition was issued by creditors of the Company. In this context section 245 of the Act appears to apply as it applies to floating charges when a company is in liquidation. However, consideration would need to be given to whether the Debenture also contained any fixed charge (secured), noting that lenders may agree both fixed and floating charges within a Debenture. The security document would likely include acknowledgement of the debt in this scenario, the loan having already been previously advanced.

On the facts provided, and on the assumption that there is only a floating charge over the whole of the Company's undertaking, the date of the Petition is deemed to be the onset of the insolvency, in compulsory liquidations. Therefore, the onset or commencement[55] of insolvency in this case is the when the Petition was issued, on 14 October 2021.

Insolvency triggers the floating charge to crystallise and become a fixed charge[56]. However, the categorisation of the charge does not change for insolvency purposes. The floating charge would still be classed as such. Notwithstanding the commencement converting the floating charge to a fixed charge (secured), section 245 of the Act is designed to prevent previously unsecure creditors gaining an advantage over other creditors by obtaining a floating charge. The section would mean that the floating charge is invalid.

In this scenario the creditor is also a lender, Stercus Bank Plc (the 'Bank') and there can be exceptions in such cases where, for example, there has been fresh funding provided and the

[55] Insolvency Act 1986, s. 245(5)(d)
[56] https://uk.practicallaw.thomsonreuters.com/3-542-5285?transitionType=Default&contextData=(sc.Default) (Glossary: Crystallization)

floating charge is over such new funding, or there has been some discharge or reduction of the existing debt, there having been new consideration for the floating charge[57]. In this scenario there has been no such consideration or indeed any new funding, therefore the two main categories of section 245 regarding new consideration would not apply as there has been none. Even if there had been, the company's undertaking was that the floating charge would cover the whole of the company's undertakings, therefore, section 245 would render the floating charge created within the 12 months[58] of the commencement of the liquidation invalid.

The Bank is not a connected party (unless there was some connection currently unknown)[59] so as long as the company was either unable to pay its debts within the meaning of section 123[60] or became unable to pay its debts within the meaning of that section as a result of the transaction under which the charge was created[61] then in relation to the latter, the creation of the floating charge does not, on the current facts, appear to have created the situation where the company could not pay its debts and in relation to the former it is unknown and would therefore require further consideration.

Section 123 of the Act defines the inability to pay debts. A company is deemed unable to pay its debts when:

a. A creditor who is owed more than £750 has served a formal demand for payment upon the company and the company has failed to pay or secure or compound it within 3 weeks of the demand to the satisfaction of the creditor; or
b. A creditor has an unsatisfied judgment or similar process (England & Wales), or and unsatisfied charge or expired bond/protest (Scotland),or an unenforceability certificate was granted (N. Ireland)[62]; or
c. It has been proven to the Court that the company is unable to pay its debts as and when they fall due[63]; or
d. *"A company is also deemed unable to pay its debts if it is proved to the satisfaction of the court that the value of the company's assets is less than the amount of its liabilities, taking into account its contingent and prospective liabilities"*[64]

In relation to 'a' above it is unclear whether the pressure that the Bank were imposing upon the company prior to the execution of the floating charge was in fact a written demand. It would appear that possibly a written demand was not formally sent because the floating charge appears to have been a mechanism the company used in order to avoid the Bank 'demanding repayment of the company's loan'. If this was the case and no demand was sent in accordance with section 123(1)(a) then the company would not be deemed unable to pay its debts in accordance with this subsection and, save for subsections b-e applying, section 245 would still apply and the floating charge would be deemed invalid.

In relation to 'b', 'c' and 'd' above we do not know if the company is based in England & Wales, Scotland or N. Ireland or whether any such proceedings are in play. In order to provide advice in this regard, further information would be required.

[57] https://www.quadrantchambers.com/news/valuation-services-purposes-section-245-insolvency-act-1986-robert-jan-temmink-qc-and-victoria
[58] Insolvency Act 1986, s. 245(3)(b)
[59] Insolvency Act 1986, s. 249
[60] Ibid, s. 245(4)(a)
[61] Ibid, s.245(4)(b)
[62] Insolvency Act 1986, s. 123(1)(b)-(d)
[63] Insolvency Act 1986, s. 123(1)(e)
[64] Insolvency Act 1986, s. 123(2)

The Advice to the liquidator client would be as described and the Bank would need to be informed with reasons why section 245 is applicable, subject to any further information being provide which may change the advice, and the Bank would revert back to an unsecured creditor, the floating charge essentially being deemed invalid. Notwithstanding this the underlying debt would remain.

Finally, section 239 of the Act was considered but given the case of Re MC Bacon Ltd.[65] and the comments made in that case by Millet J., specifically in relation as to whether lenders if granted a debenture in the above scenario, the company at the time would have been motivated not by a desire to prefer the Bank but a desire to avoid their company being driven to cease trading or into liquidation.

Question 4.2 [maximum 6 marks]

Commented [WPA11]: 6/6 although some of these arguments are barely tenable the s 238 explanation and application are very clear.

The sale of the coffee roasting machines; and

In July 2021 the company was in cash flow trouble and the Directors of the Company approved the sale of 5 coffee roasting machines to Ann Young, who was a Director, for £10,000 when the company only bought the machines the year prior for £25,000.

This sale of some of the company's assets took place prior to the commencement of the insolvency proceedings, approximately 4 months prior. The Director is clearly a connected party pursuant to the Act[66]. The liquidator under section 238 of the Act, which applies to liquidations[67], is permitted to attack any transaction for consideration by making an application to Court [68] which was entered into within the 'relevant time' [69] (2 year) before the commencement of the insolvency proceedings, if they consider any such transaction to have been carried out at an undervalue[70].

Generally it is a prerequisite of liability under section 238 that the company was unable to pay its debts when due in accordance with section 123 of the Act or it became unable to pay its debt as a result of the transaction entered into. However, in this case and as a result of the transaction having taken place with a connected person[71], Ms Young, there is a presumption already that the company was insolvent or became insolvent as a result of the transaction. The burden therefore would be upon Ms Young to rebut that presumption. Further, the Court shall not make such an order if Ms Young tried and successfully argued that the transaction was carried out in good faith and to assist the company is carrying on its business and that, at that time, there were reasonable grounds to think that it would benefit the company[72].

If the Court decides to make an order under section 238, finding that the sale of the coffee machines were at an undervalue or a preference it will order that the parties be put back into the position they were in had the transaction not have happened. The coffee machine may

[65] [1990] BCC 78
[66] Insolvency Act 1986, s. 249
[67] Insolvency Act 1986, s. 238(1)(b)
[68] Ibid, s. 238(2)
[69] Ibid, s. 240
[70] Ibid, s. 238(4)(b)
[71] Insolvency Act 1986, s. 249
[72] Ibid, s 238(5)(a) and (b)

have to be returned[73] or Ms Young may be ordered to pay an amount deemed appropriate by the Court to the liquidator[74].

Another possible line of attack could be under s.423 of the Act. The two requirement would have to be met 1] that the transaction was entered into at an undervalue[75] (similar to s. 238) and 2] that the transaction was entered into with the purpose of putting assets beyond the reach of an actual or potential claimant or otherwise prejudicing the interest of other actual or potential claimants[76]. There is no time limit with these types of claims in terms of when the transaction occurred. The liquidator or any other victim can bring such a claim. Gifts are often attacked using this measure.

The transaction could potentially fall within the section 239 of the Act in relation to preferences within the relevant time, within 2 years of the commencement date, to a connected person, Ms Young in this case. As a connected person Ms Young would likely have been preferred putting her in a better position. There would be a presumption that she would have been preferred and the burden would be on her to rebut it. This provision is has many similarities to section 238 of the Act. As with section 238, it is a prerequisite that that the company must have been unable to pay its debts as they fell due within the meaning of section 123 of the Act, including as a result of that preferential transaction. Mr Young may struggle to rebut the presumption, moreso given the amounts involved in the transaction. If, per Re MC Bacon case, the desire was to save the company then why pay only £10,000 for the assets and not much more. It may appear more likely that the motivation or desire was to provide a preference.

Not only Ms Young but all of the Directors could potentially be attacked by the liquidators for breaching their duties as Directors via a misfeasance claim for making a preferential transaction. Directors' duties are found in statute, under the Companies Act 2006[77]. If one or all of the Directors do not fulfil their duties then they may find themselves liable to company for any losses. The liquidator could use the procedure under section 212 of the Insolvency Act and include misfeasance. Perhaps the most relevant in this context are that a Director has a duty to 'promote the success of the company' (also in certain circumstances to consider the interest of creditors)[78], they should exercise independent judgment[79] and avoid direct or indirect conflicts of interest with the company[80]. If the solvency of the company is in doubt then there is a shift to consider not only the company but what would be in the best interest of the creditors.

The anti-deprivation rule may also be briefly looked at. However, should Ms Young may be able to defend against this avoidance provision by arguing that the transaction was carried out in "*commercial good faith*" as set out by Lord Collins in the *Belmont Park Investments PTY Ltd v BNY Corporate Trustee Services Ltd.*[81].

Any court action commenced by the liquidator could include any or all of the above.

[73] Ibid, s. 241(1)(a)
[74] Ibid, s. 241(1)(d)
[75] Insolvency Act 1986, s. 423(1)
[76] Insolvency Act 1986, s. 423(3)
[77] Duties contained in Companies Act 2006, ss. 171 to 177
[78] Companies Act 2006, s. 172
[79] Companies Act 2006, s. 173(1)
[80] Companies Act 2006, s. 175(1)
[81] Belmont Park Investments PTY Ltd v BNY Corporate Trustee Services Ltd [2011] UKSC 38

Question 4.3 [maximum 4 marks]

Commented [WPA12]: 0/4 although some very intelligent points are made, they do not deal with the only realistic point on the facts and that is s 127.

The payments to Beans and Leaves Ltd.

Post commencement of the insolvency proceedings on 14 October 2021 but prior to the winding-up Order being made by the Court, the suppliers contacted the Director, Ms Young, requesting payment of debts owing and payment in cash for further deliveries. The Directors authorised the payment of an initial £8,000 towards debts and agreed to make cash payments resulting, a further £3,000 being paid to that supplier up to the date of the winding-up order.

Beans and Leaves Ltd would be an unsecured creditor. This supplier would not fall under the essential suppliers as detailed in Section 233[82] relating to gas, electricity, water and communications services. Section 233B applies to the suppliers of goods and services and effectively stops them from terminating or demanding payment or they will cease supply or "do any other thing"[83] when insolvency procedures have been started. Suppliers are therefore restricted from terminating under this section. It may be that this supplier could still terminate if with consent or by court order but they would be caught by this section as they do not fall within one of the exceptions. The onset or commencement[84] of insolvency in this case is the when the Petition was issued, on 14 October 2021.

Given that insolvency proceedings had already been commenced[85], upon the presentation of the Petition and the company has become subject to an insolvency procedure. It is not apparent whether a provisional liquidator was appointed following the petition, it would appear not. Upon commencement the focus shifts to acting in the best interest of all creditors. If the Directors are all still in place and no provisional liquidator has been appointed to oversee matters until the Petition is heard and any order is made then it is the duty of the Directors to ensure that assets are preserved for the benefit of all creditors as already outlined above in 4.2. The conduct of the Director is also a line of attack, reference being made again to the duties owed by this Director to all creditors, especially given the commencement of insolvency proceedings which at that time was already in motion. The Director was under a duty to act in the interests of all creditors not only one.

Section 239 may also come into play as well given the clear preference that was given to the coffee bean supplier, who in the normal priority would have likely been an unsecured creditor at the bottom of the list.

End of Assessment

[82] Insolvency Act, s. 233
[83] Ibid, Section 233B (3)(b)
[84] Insolvency Act 1986, s. 245(5)(d)
[85] Insolvency Act 1986, s. 129(2)