



**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 candidates who **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 1 March 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 1 March 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]**

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.

**Commented [WPA1]:** 43/50 = 86% - an excellent effort. Apart from misidentifying the issue in the final question, there is very little wrong with the whole paper.

**Commented [WPA2]:** 8/10

(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.

Commented [WPA3]: C is correct

#### 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.

- (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

Commented [WPA4]: C is correct

**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.

**QUESTION 2 (direct questions) [10 marks]**

Commented [WPA5]: 10/10

**Question 2.1 [maximum 5 marks]**

Commented [WPA6]: 5/5

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?

- (i) Persons who may bring an action under section 423 of the Insolvency Act 1986 are mentioned in section 424 of the Insolvency Act. A distinction is made where the debtor is bankrupt, in liquidation or administration and where the victim of the transaction is bound by a voluntary arrangement.
  - (a) in a case where the debtor has been bankrupt or is a body corporate which is being wound up or [is in administration], by the official receiver, by the trustee of the bankrupt's estate or the liquidator or administrator of the body corporate or (with the leave of the court) by a victim of the transaction (section 424(1)(a));
  - (b) in a case where a victim of the transaction is bound by a voluntary arrangement approved under Part I or Part VIII of this Act, by the supervisor of the voluntary arrangement or by any person who (whether or not so bound) is such a victim section 424(1)(b); or
  - (c) in any other case, by a victim of the transaction (section 424(1)(c)).
- (ii) Persons who may bring an action under section 6 of the Company Directors Disqualification Act 1986 (CDDA) is contained in section 7(1) of the CDDA, which states that where
  - (a) If it appears to the Secretary of State that it is expedient in the public interest that a disqualification order under section 6 should be made against any person, an application for the making of such an order against that person may be made—
    - i. by the Secretary of State, or
    - ii. by the official receiver, if the Secretary of State so directs in the case of a person who is or has been a director of a company which is being [or has been] wound up by the court in England and Wales
- (iii) section 246ZB of the Insolvency Act 1986
  - (a) if while a company is in administration it appears that section 246ZB(2) applies in relation to a person who is or has been a director of the company, the **administrator** may apply to the court to declare that that person is to be liable to make a contribution (if any) to the company's assets as the court thinks proper.
  - (b) The conditions that need to be satisfied are that:
    - i. the company has entered insolvent administration,
    - ii. at some time before the company entered administration, that person knew or ought to have concluded that there was no reasonable prospect that the company would avoid entering insolvent administration or going into insolvent liquidation, and
    - iii. the person was a director of the company at that time.

**Question 2.2 [maximum 5 marks]**

Commented [WPA7]: 5/5

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

“Decision procedures” are the “process by which an insolvency office-holder asks creditors to make decisions in an insolvency proceeding.”<sup>1</sup>

The law that deals with decision procedures for corporate insolvency is contained in the following statutes and regulations:

- (a) sections 246ZE of the Insolvency Act 1986
- (b) rule 1.2 and Part 15 of the Insolvency (England and Wales) Rules 2016

Rule 1.2 of the 2016 Rules defines “decision procedure” as a decision procedure prescribed by rule 15.3.

Rule 15.3 prescribes the following decision procedures:

- (a) correspondence;
- (b) electronic voting;
- (c) virtual meeting;
- (d) physical meeting; or
- (e) any other decision making procedure which enables all creditors who are entitled to participate in the making of the decision to participate equally.

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

Commented [WPA8]: 14/15

**Question 3.1 [maximum 6 marks]**

Commented [WPA9]: 6/6 an excellent answer

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?

Law that deals with the supply of goods and services to a company under administration

Sections 233 and 233A refer to the supply of essential goods and services, which include water, gas, electricity and communication services. Section 233B is not restricted to the supply of essential goods and services. All three sections 233, 233A, and 233B apply to a situation where a company enters a process of administration.

Where a company is in administration, Suppliers of all goods and services are not permitted to:

- (a) require payment of outstanding debts in order to secure a new or continued supply to the company in administration. (ss. 233(2) and 233B(7))
- (b) terminate the contract, where there is an insolvency-related term of a contract which terminates the contract or allows the supplier to terminate because the company goes into administration (ss. 233A(1) read with (8) and 233B(3))
- (c) terminate where the contract allows him to terminate for an event occurring before the start of the administration (ss. 233A and 233B(4))

However, a supplier may, upon a request made by the administrator or with the permission of the administrator, make it a condition that the administrator personally guarantees the

<sup>1</sup> Practical Law, Glossary: Decision procedure < [https://uk.practicallaw.thomsonreuters.com/w-005-1130?transitionType=Default&contextData=\(sc.Default\)&firstPage=true](https://uk.practicallaw.thomsonreuters.com/w-005-1130?transitionType=Default&contextData=(sc.Default)&firstPage=true) > accessed on 26 February 2022

payment of any charges in respect of the supply of essential goods and services. (section 233(2)).

Where the supplier gives written notice to the administrator that the supply will be terminated unless the administrator personally guarantees the payment of any charges in respect of the continuation of the supply after the company entered administration and he fails to do so within 14 days of the notice, the supplier may terminate the contract of supply. (233A(5)) however, this too applies only to the supply of essential goods and services.

Can an administrator require suppliers of goods and services to continue to supply those goods and services during the administration?

Whilst the question does not specify the nature of the goods and services that are to be supplied, whether the goods and services are deemed 'essential' or not (under the Insolvency Act) the administrator can require the supplier to continue supplying goods, unless:

- (a) the administrator consents to the termination of the contract to supply goods (s. 233B(5))
- (b) the contract is terminated pursuant to the court granting permission for such termination, on the basis that the court is satisfied that the continuation of the contract would cause the supplier hardship (s. 233B(5))

Where the goods and services in question are essential in nature, the supplier may terminate the contract to supply (in which case the administrator cannot require the supplier to continue supplying the said goods and services) where:

- (a) there is an insolvency related term of a contract (which terminates the contract upon the company entering into administration or allows the supplier to terminate), the term is effective to the extent that:
  - the supplier can terminate a contract to supply or do any other thing, if company enters anything procedure other than administration, the supplier the supplier can terminate a contract to supply because of an event that occurs after the company enters into administration
- (s. 233A(2))
- (b) any charges after the administration are not paid within 28 days from which the payment is due (233A(4))
- (c) if the supplier gives written notice to the administrator that the supply will be terminated unless the administrator personally guarantees the payment of any charges in respect of the continuation of the supply after the company entered administration and he fails to do so within 14 days of the notice (233A(5))

Therefore, whilst an administrator may generally require that the supplier should continue to supply goods and services. There are limited grounds under which the supplier can seek to terminate such a contract, although it would not be easy to qualify for such termination under ss 233, 233A, or 233B of the Insolvency Act.

**Question 3.2 [maximum 9 marks]**

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.

Sections 386, 387 and Schedule 6 of the Insolvency Act set out the law in relation to preferential debts.

**Commented [WPA10]:** 8/9 generally very good but it is a little strange that repealed categories of preferential debts are listed without explanation



The priority of payments in liquidation are as follows:<sup>2</sup>

**1. Fixed charge holders.**

- (a) Fixed charge holders are paid the amount that is realised from the sale of the asset over which they have a charge.
- (b) If the debt owed to such creditors is more than the said sale, then the creditors may claim the balance as unsecured debtors.

**2. Liquidators' fees and expenses**

- (a) Under section 115 of the Insolvency Act, subject to any claims under section 174A, all expenses properly incurred in the winding up, including the remuneration of the liquidator, are payable out of the company's assets in priority to all other claims.
- (b) Chapter 6 in Part 6 of the Insolvency Rules 2016 sets out the Priority of payment of costs and expenses in Creditors' Voluntary Winding Up (specifically Rule 6.42). Chapter 14 in Part 7 sets out the Priority of payment of costs and expenses in Winding Up by the Court (specifically rule 7.108).
- (c) Whilst most of the expenses and costs referred to under Rules 6.42 and 7.108 are the same, Rule 7.108 provides for the expenses/costs/fees of the provisional liquidator and the official receiver.
- (d) The most common expenses are:
  - (i) expenses that are properly chargeable or incurred by the official receiver or the liquidator in preserving, realising or getting in any of the assets of the company or otherwise in the preparation, conduct or assignment of any legal proceedings, arbitration or other dispute resolution procedures
  - (ii) the cost of any security provided by the provisional liquidator, liquidator or special manager under in accordance with the Act or these Rules
  - (iii) remuneration of the provisional liquidator and/or special manager
  - (iv) any amount payable to a person employed or authorised, under Chapter 26 of this Part, to assist in the preparation of a statement of affairs or of accounts
  - (v) any necessary disbursements by the liquidator in the course of the administration of the winding up
  - (vi) the remuneration or emoluments of any person who has been employed by the liquidator to perform any services for the company, as required or authorised by or under the Act or these Rules;
  - (vii) the remuneration of the liquidator, up to an amount not exceeding that which is payable under Schedule 11 (determination of insolvency office-holder's remuneration);
  - (viii) the amount of any corporation tax on chargeable gains accruing on the realisation of any asset of the company (irrespective of the person by whom the realisation is effected);
  - (ix) the balance, after payment of any sums due under paragraph 2(d)(vii) above, of any remuneration due to the liquidator; and
  - (x) any other expenses properly chargeable by the liquidator in carrying out the liquidator's functions in the winding up

<sup>2</sup> Practical Law, Restructuring and insolvency in the UK (England & Wales): overview, [https://uk.practicallaw.thomsonreuters.com/9-501-6812?originationContext=document&transitionType=DocumentItem&contextData=\(sc.Default\)&ppcid=6e2cf03ab0c3440ab961c54cd0d1eddd&comp=pluk&firstPage=true#co\\_tempAnchor](https://uk.practicallaw.thomsonreuters.com/9-501-6812?originationContext=document&transitionType=DocumentItem&contextData=(sc.Default)&ppcid=6e2cf03ab0c3440ab961c54cd0d1eddd&comp=pluk&firstPage=true#co_tempAnchor), accessed on 27 February 2022  
Practical Law, Order of creditor and contributory ranking on a debtor's insolvency, <[https://uk.practicallaw.thomsonreuters.com/9-518-5211?transitionType=Default&contextData=\(sc.Default\)&firstPage=true](https://uk.practicallaw.thomsonreuters.com/9-518-5211?transitionType=Default&contextData=(sc.Default)&firstPage=true)>, accessed on 27 February 2022

### 3. Preferred creditors

- (a) There are two classes of preferential debts, ordinary and secondary. Ordinary claims are paid before secondary claims.
- (b) Section 386 states that any reference to 'preferential debts' of a company or an individual in the Insolvency Act is to the debts listed in Schedule 6 of the Act. The Ordinary claims set out paragraphs 8 to 15B of Schedule 6 and the secondary claims are set out in paragraphs 15BA to 15D of Schedule 6 (Categories 8 and 9, in Schedule 6)
- (c) The categories of Preferential Debts, as set out in Schedule 6, are as follows:
  - (i) Category 1: Debts due to Inland Revenue
  - (ii) Category 2: Debts due to Customs and Excise
  - (iii) Category 3: Social security contributions
  - (iv) Category 4: Contributions to occupational pension schemes, etc.
  - (v) Category 5: Remuneration, etc., of employees
  - (vi) Category 6: Levies on coal and steel production
  - (vii) Category 6A: Debts owed to the Financial Services Compensation Scheme
  - (viii) Category 7: Deposits covered by Financial Services Compensation Scheme
  - (ix) Category 8: Other deposits
  - (x) Category 9: Certain HMRC debts
- (d) UK HM Revenue and Customs (HMRC) has been promoted to secondary preferential creditor status in insolvency procedures that commence on or after 1 December 2020

### 4. Floating charge holders.

- (a) Floating charge holders will be paid after the preferential creditors.
- (b) They will be paid up to the amount realised from the assets covered by the floating charge.
- (c) However, a distinction is made between the floating charges created before and after on or after 15 September 2003.
- (d) Where the floating charge was made on or after 15 September 2003, part of the proceeds of the assets that are realised should be set aside for the satisfaction of unsecured debt ("Prescribed Part"). No part of these proceeds can be used to satisfy the debt owed to floating charge holders, unless all the unsecured debt has been satisfied.
- (e) Where the net property of the company is less than £10,000, the liquidator need not create a prescribed part if the liquidator is of the opinion that the making a distribution to the unsecured creditors would be disproportionate to the benefits of such a distribution
- (f) Where the net property of the company is more than £10,000, the prescribed part is the aggregate of the following, capped at £800,000:
  - (i) 50% of the sum up to £10,000
  - (ii) 20% of the remaining sum

### 5. Unsecured creditors.

- (a) This is where the debt of the creditor is not secured against any of the assets of the company
- (b) The unsecured creditors will be paid from the remaining asset realisation and from the "prescribed part"
- (c) Generally however, there is little or nothing left to pay the unsecured creditors

### 6. Interest incurred on all unsecured debts post-liquidation

7. Shareholders.

- (a) Any surplus that is remaining after the distribution of the funds among the creditors is distributed to the shareholders pro rate based on their respective shareholding

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

Commented [WPA11]: 11/15

Prior to going into compulsory liquidation on 23<sup>rd</sup> December 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 14<sup>th</sup> October 2021.

In July 2021, as the Company continued to suffer cash flow problems, the directors approved the sale of 5 coffee 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:**

1. The role of a liquidator mainly involves taking over a company and gaining control of its assets. To do so, the liquidator has power to, inter alia, investigate the affairs of a company.
2. In the process, certain transactions can be set aside, if upon such investigation the liquidator uncovers any activity that might require further action. The liquidator may attack such transactions and call for their reversal. The liquidator can bring an action on behalf of a company against the directors, directly or the liquidator may assign such causes of action to a 'third-party' funder who may then sue the director themselves.

3. It will be considered below whether the floating charge in favour of Stercus Bank plc, sale of the coffee roasting machines, and the payments to Beans and Leaves Ltd fall within the purview of such transactions that may be set aside.

#### Question 4.1 [maximum 5 marks]

##### The floating charge in favour of Stercus Bank plc;

4. A floating charge is a charge that floats/hovers over assets or a group of assets until the said charge becomes crystallised. A floating charge crystallises into a fixed charge if the grantor ceases its business, the secured party takes enforcement action (such as the appointment of a receiver or a liquidator) or a trigger event defined in the security instrument occurs.<sup>3</sup>

##### *Grounds on which the transaction should be investigated/set aside*

5. In relation to the floating charge in favour of Stercus Bank plc (the "Bank"), it is relevant that the
- The Company granted a debenture in favour of Stercus Bank plc in February 2021
  - The creditor's winding up petition was issued on 14th October 2021
  - The company went into compulsory liquidation on 23rd December 2021
  - The debenture contained a floating charge over the whole of the Company's undertaking
  - Factors that appear to have influenced the company granting the debenture:
    - the Company was under pressure from its bank, Stercus Bank plc to grant the debenture
    - to prevent the Bank from demanding repayment of the company's loans
  - even in July 2021 the Company continued to suffer cash flow problems
6. The liquidator may wish to investigate whether there are circumstances to take action against the directors for Preferences (dealt with s. 239 of the Insolvency Act 1986 ("Act") and/or Floating charge avoidance (dealt with s. 245 of the Act). They will be dealt with in turn below.
- ##### *Preferences*
7. This is designed to prevent a director or a company from placing a creditor in a better position, shortly before the company enters liquidation, than what it would have been if not for the transaction.
8. S. 239 contains the conditions which need to be fulfilled in making an application under s. 239. Another relevant section is s. 238 The conditions that must be satisfied are as follows:
- The company has to be in liquidation or administration (s. 238)
  - The applicant, who may be the liquidator or the administrator, must show that:
    - A preference was given to a person, in that the company does anything or suffers anything to be done which (in either case) has the effect of putting that person into a position which, in the event of the company going into

**Commented [WPA12]:** 5/5 a good answer – the s 245 is very convincing. The discussion of s 239 is reasonable but clearly of no application to the facts.

<sup>3</sup> Practical Law, Lending and Taking Security in the UK (England and Wales): Overview, Practical Law Country Q&A, < [https://uk.practicallaw.thomsonreuters.com/4-501-3222?transitionType=Default&contextData=%28sc.Default%29#co\\_anchor\\_a602023](https://uk.practicallaw.thomsonreuters.com/4-501-3222?transitionType=Default&contextData=%28sc.Default%29#co_anchor_a602023)> accessed on 27 February 2022

insolvent liquidation, will be better than the position he would have been in if that thing had not been done (s. 239(4)(b))

- (ii) That such a person to whom the preference was given was one of the company's creditors or a surety or guarantor for any of the company's debts or other liabilities (s. 239(2) and (4))
- (iii) The preference was given at the relevant time (s. 239(2))
- (iv) The company, in giving the preference should have been influenced in deciding to give it by a desire to produce in relation to that person the effect mentioned in paragraph 8(b)(i) above.

9. In the present case, the Company is in liquidation and the Bank is a creditor. By granting the Bank the debenture over the whole of the Company's undertaking, it appears as though the Bank is now in a position which, now that the Company has gone into insolvent liquidation, is in a better position than the position that the Bank would have been in if the debenture had not been granted, as the Bank is now a preferential creditor and will receive more priority as opposed to the unsecured creditor that it was prior to the debenture.
10. However, the liquidator will also need to establish, as required by section 239(5) of the Act, that the Company was influenced in deciding to give the preference by a desire to prefer the Bank. This is a subjective test.
11. Pressure by the creditor could be an indication of a desire to give a preference but is not in itself evidence that the transaction amounts to a preference. Pressure for payment by the creditor may afford a defence.<sup>4</sup>
12. Where a Company is under substantial pressure to pay its creditors, the said company may grant a debenture to its bank to secure past indebtedness. If the said company was influenced by a wish to avoid the bank calling in the company's overdraft (as opposed to a desire to prefer the bank), this may be sufficient to avoid a preference. This was the case in the case of *Re MC Bacon Ltd*,<sup>5</sup> where the company merely wished to continue trading as opposed to placing the creditor in a more beneficial position.
13. Similarly, in this case, although there was pressure from the Bank to grant the debenture, it is more likely that the Company merely wanted to continue trading as it did not want the Bank to call upon the loans it had granted the Company.
14. Further, the requirement of the relevant time (s. 239(2) read with s. 240(1)) is not satisfied here as:
  - (a) The Bank is not a connected Party under s. 249, read with s. 435 of the Act
  - (b) Therefore, the relevant time is **six months** ending with the onset of insolvency (s. 240(1)), which is the date on which the winding-up petition was presented to the court, in a compulsory liquidation (s. 129 of the Act)
  - (c) The Company granted a debenture in favour of Stercus Bank plc in February 2021 and the creditor's winding up petition was issued on 14th October 2021, there appears to be a gap of more than 6 months
15. Therefore, the liquidator is unlikely to succeed on setting aside the transaction on the grounds of Preferences.

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<sup>4</sup> Practical Law, [Preferences in corporate insolvency, Practical Law UK Practice Note](#), accessed on 28 February 2022

<sup>5</sup> [1990] BCC 78

*Floating charge avoidance*

16. Section 245 of the Act is designed to prevent a company benefiting a creditor by giving a floating charge for existing liabilities for no new consideration<sup>6</sup>
17. To set aside the floating charge, the liquidator needs to establish that: S. 245 states that,
- (a) The company was insolvent at the time of granting the floating charge or became insolvent as a result of the transaction in which the floating charge is granted<sup>7</sup> (s. 245(1))
  - (b) Where the floating charge was not created in favour of a connected person, that the said floating charge was created in the 12 months before the onset of insolvency (filing of the winding up petition) (s.245(3)(b))
  - (c) The floating charge was given in exchange only for prior consideration, for example, to secure loans previously made
18. However, the floating charge would be valid if it were provided for consideration provided to the company at the same time or after the creation of the charge, which may be:<sup>8</sup>
- (a) Money paid, or goods or services supplied, to the company at the same time as, or after, the creation of the charge.
  - (b) Discharge or reduction of any debt of the company at the same time or after the creation of the charge.
  - (c) Interest on such consideration.
19. In the present case,
- (a) No new consideration has been provided by the Bank for the floating charge
  - (b) The floating charge has been provided, on the onset of the insolvency (which in the case of a compulsory winding up is within a year from the date on which the winding-up petition was presented to the court, as per s. 245(5)), as
    - (i) The Company granted a debenture in favour of Stercus Bank plc in February 2021; and
    - (ii) The creditor's winding up petition was issued on 14th October 2021 (approximately 6 months from the date the denture was granted in favour of the Bank)
  - (c) As for whether the floating charge was created at the relevant time as per 245(4), the fact that the Company continued to suffer cash flow problems even in July 2021 may be an indication that the Company was unable to pay its debts at the time the charge was created. In any event the Company went into liquidation shortly thereafter in December 2021.
20. Therefore, the liquidator is likely to be able to set aside the transaction based on the avoidance of certain floating charges provided for under s. 245 of the Act.
21. Once the requirements under section 245 are satisfied, in theory, the floating charge in question is automatically invalid. No application needs to be made by the office holder, at least in theory. The office holder will usually simply write to the floating

<sup>6</sup> Practical Law, [Avoidance of floating charges in corporate insolvency, Practical Law UK Practice Note](#), accessed on 28 February 2022

<sup>7</sup> Practical Law, [Reviewable transactions in insolvency: a quick guide, Practical Law UK Practice Note](#), accessed on 28 February 2022

<sup>8</sup> Practical Law, [Avoidance of floating charges in corporate insolvency, Practical Law UK Practice Note](#), accessed on 28 February 2022

charge holder, stating that the office holder believes the floating charge is invalid.<sup>9</sup>

22. Where such statutory action is being brought against an officer of the company, it is also common to see the liquidator also include a more general "misfeasance" claim as part of the action being brought. This is referred to in s. 212 of the Act. However, s. 212 is a procedural section and does not create any new causes of action.

#### Question 4.2 [maximum 6 marks]

Commented [WPA13]: 6/6 another very clear and well applied answer

#### The sale of the coffee roasting machines; and

1. Since the coffee machines were sold at undervalue, the liquidator can investigate whether the said sale can be set aside on the basis that it was a transaction at undervalue, under s. 238 of the Act.
2. In relation to the floating charge in favour of Stercus Bank plc (the "Bank"), it is relevant that the
  - a. The coffee machines had been bought for £25,000 a year before (that is in 2020)
  - b. In July 2021 the Company continued to suffer cash flow problems
  - c. the directors approved the sale of 5 coffee roasting machines, apparently due to the Company's cash flow problems
    - i. to Ann Young (a director) for £10,000 in cash,
    - ii. in July 2021
  - d. The creditor's winding up petition was issued on 14th October 2021
  - e. The company went into compulsory liquidation on 23rd December 2021
3. For the transaction to be set aside on this basis, the liquidator must establish that the
  - a. The company is in liquidation
  - b. The transaction in question has been entered into at the relevant time (s. 245(2)), which is, in the case of a compulsory liquidation, two years before the winding-up petition was presented to the court (s. 240(3)(e))
  - c. At the time the transaction was entered into the company was unable to pay its debts at the time of the transaction or became unable to pay its debts as a result (the insolvency requirement) (s. 240(2))
  - d. The transaction was at an undervalue, which is when,
    - i. the company makes a gift to that person or otherwise enters into a transaction with that person on terms that provide for the company to receive no consideration, (s. 238(4)(a)) or
    - ii. the company enters into a transaction with that person for a consideration the value of which, in money or money's worth, is significantly less than the value, in money or money's worth, of the consideration provided by the company. (s. 238(4)(b))

<sup>9</sup> Practical Law, [Avoidance of floating charges in corporate insolvency, Practical Law UK Practice Note](#), accessed on 28 February 2022

4. It is for the applicant to satisfy the court as to the value (and deficiency) of the consideration provided to the insolvent company<sup>10</sup>
5. If the liquidator succeeds in his application, the court may make such order as it thinks fit for restoring the position to what it would have been if the company had not entered into that transaction (s. 238(3))
6. However, a defence to this action can be raised where it can be satisfied
  - a. that the company which entered into the transaction did so in good faith and for the purpose of carrying on its business (s. 238(5)(a)), and
  - b. that at the time it did so there were reasonable grounds for believing that the transaction would benefit the company (s. 238(5)(b)).
7. An application to court must comply with the requirements of rule 1.35 of the Insolvency Rules 2016.
8. In this case, the liquidator is likely to be able to apply for the transaction to be set aside for being one of undervalue under s. 238 of the Act as:
  - a. The Company is now in liquidation
  - b. The transaction in question, which is the sale of the coffee machines, was made at the relevant time, as
    - i. The transaction was conducted in July 2021,
    - ii. which is less than two years before the winding up petition was presented to court in October 2021
  - c. was at an undervalue, in that
    - i. the coffee machines were sold for less than half the price at which they were bought, which could be said to be 'significantly less than the value, in money or money's worth, of the consideration provided by the company'
  - d. At the time the transaction was entered into, it is likely that
    - i. the Company was unable to pay its debts as the Company is reported to have had cash flow problems, for which reason the sale was deemed necessary
    - ii. In any case, since this transaction was with a connected person, that is a director of the Company (as per s. 249 of the Act) the company is presumed to have been insolvent, or to have become insolvent as a result of the transaction, unless the contrary is proved (s. 240(2))
9. However, on the other hand, the Company is likely to be able to come under the 'good faith' defence, in that the transaction was carried out for the purpose of carrying on the business or there were reasonable grounds for believing that the transaction would benefit the Company since the Company was facing cash flow problems immediately before the transaction.

**Question 4.3 [maximum 4 marks]**

The payments to Beans and Leaves Ltd.

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<sup>10</sup> Practical Law, [Transactions at an undervalue in corporate insolvency, Practical Law UK Practice Note](#), accessed on 28 February 2022

**Commented [WPA14]:** 0/4 – an inventive answer but unfortunately it misses the point which is that the payment would be prima facie void under s 127.



1. The relevant facts here are that

- a. A month before the winding up order was made (that is in November 2021), the supplier:
  - i. demanded immediate payment of all sums owing to it
  - ii. made further delivery conditional on a cash on delivery basis
- b. the board
  - i. authorised a payment of £8,000 to cover existing liabilities and
  - ii. 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.
- c. The creditor's winding up petition was issued on 14th October 2021
- d. The company went into compulsory liquidation on 23rd December 2021

*Demanding immediate payment of sums owing to it*

1. As far as a company registered in England and Wales is concerned, any attachment, sequestration, distress or execution put in force against the estate or effects of the said company after the commencement of the winding up is void (s. 128(a))
2. The liquidation is deemed to have commenced with the presentation of the winding-up petition. Therefore, in this case the liquidation is deemed to have commenced on 14th October 2021.
3. The supplier, as a creditor of the Company, cannot demand payment once the liquidation process has commenced.
4. Therefore, this payment need not be made.

*Making further delivery conditional on a cash on delivery basis*

1. Sections 233 and 233A refer to the supply of essential goods and services, which include water, gas, electricity and communication services. Section 233B is not restricted to the supply of essential goods and services. Only sections 233 and 233B apply to a situation where a company enters a process of liquidation.
2. Suppliers of all goods and services are not permitted to:
  - a. terminate the contract or do any other thing, where there is an insolvency-related term of a contract which terminates the contract or allows the supplier to terminate or do any other thing because the company goes into liquidation (s 233B(3))
  - b. terminate where the contract allows him to terminate for an event occurring before the start of the liquidation (s. 233B(4))
3. Any other thing' referred to in s. 233B(3) could also include a variation in the payment terms or an increase in pricing.<sup>11</sup>

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<sup>11</sup> [Restrictions on terminating supply contracts in insolvency proceedings, Practical Law UK Practice Note, 1 March 2022](#)

4. Since the supplier has changed the terms to cash on delivery, the court may view this as being prohibited under s. 233B(3) of the Act.
5. The liquidator can require the supplier to continue supplying goods, unless:
  - a. the liquidator consents to the termination of the contract to supply goods (s. 233B(5))
  - b. the contract is terminated pursuant to the court granting permission for such termination, on the basis that the court is satisfied that the continuation of the contract would cause the supplier hardship (s. 233B(5))

Where payments are not made to a supplier for supplies provided after the commencement of insolvency proceedings, it will be treated as an expense of the insolvency proceedings. This will give the supplier higher payment priority for his/her goods, although the payment may not be immediate.<sup>12</sup> However, where it is found that the liquidator has breached his fiduciary duty in continuing to obtain supplies and thereby accruing costs, he could be personally liable.

Therefore, the supplier in this case cannot threaten to terminate.

However, a supplier may attempt to exercise his common law rights to terminate for repudiatory breach.<sup>13</sup> Further, if the supplier's right to terminate the contract, that is stop supplying goods, arises after the insolvency procedure begins then this right is not prohibited under s. 233B.<sup>14</sup> Therefore, the supplier may refuse to provide goods if payment is not made for goods supplied after the commencement of insolvency proceedings. Although the liquidator may still be able to argue that the payment terms should not be changed.

**\* End of Assessment \***

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<sup>12</sup> [Restrictions on terminating supply contracts in insolvency proceedings, Practical Law UK Practice Note](#), 1 March 2022

<sup>13</sup> [Restrictions on terminating supply contracts in insolvency proceedings, Practical Law UK Practice Note](#), accessed on 1 March 2022

<sup>14</sup> Paragraph 229, Explanatory Notes to the CIGA 2020, [https://www.legislation.gov.uk/ukpga/2020/12/pdfs/ukpgaen\\_20200012\\_en.pdf](https://www.legislation.gov.uk/ukpga/2020/12/pdfs/ukpgaen_20200012_en.pdf)