



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: 202223-336.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 2023. The assessment submission portal will close at 23:00 (11 pm) GMT on 1 March 2023. 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 2023 or by 23:00 (11 pm) BST (GMT +1) on 31 July 2023. If you elect to submit by 1 March 2023, you may not**

submit the assessment again by 31 July 2023 (for example, in order to achieve a higher mark).

7. Prior to being populated with your answers, this assessment consists of 8 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.

Commented [WPA1]: 42/50 = 84% a generally very strong performance

Commented [WPA2]: 7/10

Commented [WPA3]: D is correct

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) GBP 500**

**(b) GBP 750**

**(c) GBP 1,000**

**(d) GBP 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**

Commented [WPA4]: B is correct

(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.

Commented [WPA5]: D is correct

QUESTION 2 (direct questions) [10 marks]

Commented [WPA6]: 8/10

Question 2.1 [maximum 5 marks]

Commented [WPA7]: 3/5 - only the Sec of State or the OR may bring an action under s 6 and only an administrator may bring an action under s 246ZB.

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?

*Under section 423 of the Insolvency Act 1986, the following parties have the right to attack transactions which are designed to defraud creditors:*

- (a) where the company is being wound up or is in administration, the official receiver, the liquidator, the administrator (and with the leave of the court) any victim of the transaction such as a creditor;*
- (b) where the victim is bound by a company voluntary arrangement (CVA), the supervisor of the CVA or any victim of the transaction (whether bound by the CVA or not); or*
- (c) in any other case, by a victim of the transaction.*

*Applications to disqualify a director under section 6 of the Company Directors Disqualification Act 1986 may be brought by the Secretary of State, or the Official Receiver or any liquidator, or a member or creditor of the company in relation to which the person against whom the disqualification order is sought is alleged to have committed the offence.*

*An application to court for wrongful trading under section 246ZB of the Insolvency Act 1986 can only be made by the liquidator, and not a creditor or contributory.*

Question 2.2 [maximum 5 marks]

Commented [WPA8]: 5/5

**List any five (5) of the debts which do not form part of the payment holiday under Part A1 of the Insolvency Act 1986 when a company is subject to a Moratorium.**

*Debts which do not form part of the payment holiday when a company is subject to a Moratorium include:*

- (a) the monitor's remuneration or expenses;*
- (b) goods or services supplied during the Moratorium;*
- (c) rent in respect of a period during the Moratorium;*
- (d) wages of salary arising under a contract of employment; and*
- (e) redundancy payments.*

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

Commented [WPA9]: 13/15

Question 3.1 [maximum 6 marks]

Commented [WPA10]: 4/6 quite good on s 233B but there is a lack of detail on s 233 (and its relation with s 233A).

**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?**

*Yes, the administrator can still require suppliers of goods and services to continue to supply those goods and services during the administration.*

*While terms in contracts of supply which provide for automatic termination upon the appointment of an administrator have historically been effective, they have increasingly become subject to statutory exceptions that render them void. Under section 233A of the Insolvency Act 1986 ("the Act"), a supplier of goods and services is generally unable to rely upon an "insolvency-related term" in a contract of supply which would otherwise entitle the supplier to terminate the supply, alter the terms of the supply or compel higher payments for continued supply. Moreover, section 233B of the Act prohibits clauses which allow the supplier of goods or services to terminate or "do any other thing" in relation to that contract if the company enters a formal insolvency procedure. In this way, not only does section 233B prevent suppliers from terminating a supply upon the company's insolvency; it also prevents suppliers from requiring payment of pre-insolvency arrears as a condition for continued supply, and from making other changes to the contract such as increasing prices. Under section 233B, a supplier also cannot insist on a personal guarantee from the administrator.*

*The contract between the company and the suppliers can only be terminated under section 233B where the company or the administrator consents, or if the suppliers apply to the court and the court is satisfied that the continuation of the contract would cause the supplier hardship.*

Question 3.2 [maximum 9 marks]

Commented [WPA11]: 9/9 a good answer

**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. How would this priority change if the company had been subject to a Moratorium under Part A1 of the Insolvency Act 1986 during the 12 week period prior to the commencement of the liquidation?**

#### Liquidation expenses

*Under section 115 of the Insolvency Act 1986, read with rules 6.42 and 7.108 of the Rules, a number of expenses are given priority over all other claims. These expenses which are payable in priority to those creditors are (in order of priority):*

- (a) expenses that are properly incurred by the liquidator in preserving, realizing or getting in any of the assets of the company (including the conduct of any legal proceedings);*
- (b) the cost of any security provided by the liquidator;*
- (c) any amount payable to a person to assist in the preparation of a statement of affairs or accounts;*
- (d) any necessary disbursements by the liquidator in the course of the winding up (including, for example, any expenses incurred by members of the liquidation committee);*
- (e) the remuneration of any person who has been employed by the liquidator to perform any services for the company;*
- (f) the remuneration of the liquidator (which is subject to effectively the same rules as those which apply to administrator, specifically including the fees estimate regime where a time cost basis for the liquidator's fees is adopted);*



- (g) the amount of any corporation tax on chargeable gains accruing on the realization of any asset of the company; and*
- (h) any other expenses properly chargeable by the liquidator in carrying out the liquidator's functions in the winding up.*

#### Preferential creditors

*Once the expenses of the liquidation have been paid in full, the assets of the company are then used to pay preferential creditors before any payment may be made to holders of floating charges or unsecured creditors. Ordinary preferential debts are paid before secondary preferential debts. This preferential debts regime applies to all insolvency procedures, and the terms of company voluntary arrangements cannot alter the priority of preferential creditors. Preferential creditors are mainly limited claims of employees and some taxation liabilities to the Crown. The latter was abolished by the Enterprise Act 2002 but has largely been reintroduced by section 95 of the Finance Act 2020. While it has always been a characteristic of the statutory preferential debts regime that employees' remuneration be given some priority, there are significant limits on such claims. In most insolvencies, the statutory protection afforded to employees under the Employment Rights Act 1996 provides considerably more extensive protection for employees, and it has been questioned why the Act retains its historic employee protection provisions. Schedule 6 of the Insolvency Act 1986 lists the categories of preferential debts.*

#### Floating charge holders

*After preferential creditors have been paid, floating charge holders will be paid. If there is more than one floating charge holder, priority between the floating charge holders generally turns upon which floating charge was first created. However, before paying the floating charge holder, the liquidator must first consider whether section 176A of the Insolvency Act 1986 applies. Section 176A applies to a company with a floating charge created on or after 15 September 2003 and the company has gone into liquidation or administration.*

*Under s 176A, the liquidator or administrator is under a duty to make a "prescribed part" of the company's net property available for the satisfaction of unsecured debts, and must not distribute that part to a floating charge holder except insofar as it exceeds the amount required for the satisfaction of unsecured debts. "Net property" is the amount of the company's property which otherwise would be available for the satisfaction of debts of floating charge holders, and is calculated after the liquidation expenses and preferential debts have been paid.*

*Where the company's net property does not exceed GBP 10,000, the prescribed part is 50% of that property. However, in such circumstances, if the liquidator thinks that making a distribution to unsecured creditors would be disproportionate to the benefits, then the duty to make the distribution of the prescribed part does not apply.*

*Where the company's net property exceeds GBP 10,000, the prescribed part is the sum of 50% of the first GBP 10,000 in value, plus 20% of the excess in value above the GBP 10,000, subject to a maximum amount of the prescribed part of GBP 800,000.*

*A floating charge holder or any secured creditor who may have an outstanding unsecured balance owing to it is not permitted to participate in the distribution of the prescribed part.*

#### Unsecured creditors

*Unsecured creditors, who are ordinary trade creditors, are paid out last in the statutory order. At this point, there is frequently little or nothing left to pay the unsecured creditors.*

#### Shareholders

*If there are sufficient funds to pay all the creditors with interest, any surplus is distributed among the shareholders according to the company's constitution, which normally permit a distribution *pro rata* the shareholders' respective shareholdings.*

*It should also be noted that a subordination agreement is an agreement between two creditors whereby they agree between themselves to vary their priority. Since a subordination agreement is a contractual agreement between two or more creditors, it is valid as they do not affect the priority of other creditors.*

#### Effect of a Moratorium

*If the company had been subject to a Moratorium under Part A1 of the Insolvency Act 1986 during the 12-week period prior to the commencement of the liquidation, the priority of debts in the liquidation may change to the priority of debts which existed prior to the Moratorium. Section 174A of the Insolvency Act 1986 affords certain unsecured debts a form of "super priority" in the subsequent liquidation. Section 174A provides that certain unpaid pre-Moratorium or Moratorium debts (debts which are not part of the payment holiday), e.g. debts owed to employees or "financial services debts"), are paid in the subsequent liquidation, in priority to even the liquidator's fees and expenses. Unsecured (or secured) pre-Moratorium bank debt falling within the definition of "financial services" will acquire such "super priority", unless such debt is accelerated debt, *ie*, any pre-moratorium financial services debt which fell due by reason of the operation of, or exercise of rights under, an acceleration or early termination provision in the financial services contract.*

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

Commented [WPA12]: 14/15

***Prior to going into compulsory liquidation on 23<sup>rd</sup> December 2022, under pressure from its bank, Fretus Bank plc, and in order to prevent it from demanding repayment of the company's loans, Marbley Q Limited ("the Company"), granted a debenture in favour of Fretus Bank plc in February 2022. 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 2022.**

**In July 2022, as the Company continued to suffer cash flow problems, the directors approved the sale of two (2) marble cutting machines to Rita Perkins (a director) for GBP 10,000 in cash. The machines had been bought for GBP 25,000 a year before.**

**A month before the winding up order was made, Rita Perkins received an email from Hard and Fast 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 marble was seen as essential by the Company, the board authorised a payment of GBP 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 GBP 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 Fretus 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]

**The floating charge in favour of Fretus Bank plc;**

*The liquidator may rely on section 245 of the Insolvency Act 1986 ("the Act") to render the floating charge in favour of Fretus Bank plc void. Section 245 renders floating charges given by a company at a relevant time invalid, except to the extent that "new" consideration is provided for the charge. Section 245 applies where a company is in administration or liquidation and the provision is aimed at preventing pre-existing unsecured creditors obtaining the security of a floating charge shortly before a company enters a formal insolvency procedure. Where the person in whose favour the floating charge is created is connected with the company, the relevant time is any time within the period of two years prior to the onset of insolvency. Where the person in whose favour the floating charge is created is not connected with the company, the relevant time is any time within the period of 12 months prior to the onset of insolvency, but only if at the time of the creation of the charge the company was either unable to pay its debts (within the meaning in section 123 of the Act) or became unable to do so in consequence of the transaction.*

*First, it is clear that the floating charge granted falls within the scope of s 245 of the Act. In the present case, assuming that the Company granted the floating charge in favour of Fretus Bank plc after the creditor's winding up petition on 14 October 2022 but just before going into compulsory liquidation on 23 December 2022, section 245*

**Commented [WPA13]:** 4/5 good on the law but its application to the facts is a little confused as the charge was executed in Feb 2022 not after the petition.

*will apply to render the floating charge in favour of Fretus Bank plc invalid. Under section 129 of the Act, where a winding-up order is made, the liquidation is deemed to have commenced at the date of the petition and not the date of the winding-up order. The issuance of the winding-up order shows that at the time of the winding up petition on 14 October 2022, the Company was unable to pay its debts within the meaning in section 123 of the Act. Therefore, the Company's granting of a debenture containing a floating charge in favour of Fretus Bank plc clearly runs afoul of section 245 of the Act and can be declared invalid.*

*Second, no new consideration was provided for the floating charge. Section 245 of the Act sets out two main categories of "new consideration" which, if satisfied, mean the floating charge will not be invalid:*

- 1. the value of so much of the consideration for the creation of the charge as consists of money paid, or goods or services supplied, to the company at the same time as, or after, the creation of the charge.*
- 2. the value of so much of that consideration as consists of the discharge or reduction, at the same time as, or after, the creation of the charge, of any debt of the company.*

*There is no evidence that Fretus Bank plc furnished the above "new" consideration for the floating charge. The floating charge was granted not in discharge or reduction of the Company's existing debt, but only to "prevent" Fretus Bank plc from demanding repayment of the Company's loans, ie, a delay in repayment of the debt. In these circumstances, it is unlikely that Fretus Bank plc would be found to have furnished "new" consideration for the floating charge. The floating charge will therefore be declared invalid.*

Question 4.2 [maximum 6 marks]

Commented [WPA14]: 6/6 good

**The sale of the marble cutting machines; and**

*The liquidator can apply to set aside the sale of the marble cutting machines to Rita Perkins on the basis that the sale was a transaction at an undervalue under s 238 of the Insolvency Act 1986 ("the Act"). In this case, under section 238, the liquidator must show that the Company's sale of the marble cutting machines to Rita Perkins was for a consideration which, in money or money's worth was, at the date of the transaction, significantly less than the value, in money or money's worth, of the consideration provided by the Company. The sale must also have taken place at a "relevant time", which is in the period of two years prior to the commencement of the liquidation or administration. Moreover, under section 238, it must be shown that at the time the transaction was entered into, the Company was either unable to pay its debts as they fell due within the meaning of section 123 or became unable to pay its debts within the meaning of section 123 as a consequence of the transaction. In the case of a transaction with a connected person, however, the company is presumed to have been insolvent, or to have become insolvent as a result of the transaction, unless the contrary is proven.*

*In the present case, the Company's sale of the marble cutting machines to Rita Perkins was indeed for a consideration significantly less than the value of the consideration provided by the Company. The Company sold both marble cutting machines to Rita Perkins at GBP 5,000 each (GBP 10,000 in total). This is a steep discount from the price the Company had acquired the marble cutting machines, at GBP 25,000 just the year before. Under section 129 of the Act, where a winding-up order is made, the liquidation is deemed to have commenced at the date of the petition on 14 October 2022. The sale of the marble cutting machines in July 2022 falls within the "relevant time" of two years prior to the commencement of the liquidation. Moreover, as Rita Perkins was a director of the Company at the time of the sale, she is a "connected person". The Company is therefore presumed to have been insolvent or to have become insolvent as a result of the transaction. There is no evidence to suggest that Rita Perkins will be able to prove the contrary.*

*In resisting the application, Rita Perkins is likely to argue that the sale was done in good faith and for the purpose of carrying on its business, and that at the time the Company did so there were reasonable grounds for believing that the transaction would benefit the Company. If she is able to satisfy the court on these points, then the court will not make an order under section 238.*

*On the facts, it is unlikely that Rita Perkins will be able to discharge this burden. As mentioned above, the machines were bought at a steep discount of GBP 15,000. Given that the Company bought the marble cutting machines at GBP 25,000 just the year before, Rita Perkins will not be able to argue that the marble cutting machines had suffered such wear and tear or depreciation in value as to justify a price of merely GBP 5,000 each. In these circumstances, a reasonable person in Rita Perkins' position is unlikely to believe that the transaction would benefit the Company.*

*Therefore, the liquidator will likely be able to persuade the court that the sale of the marble cutting machines was a transaction at an undervalue. The court will then make an order restoring the position to what it would have been if the transaction had not been entered.*

Question 4.3 [maximum 4 marks]

**The payments to Hard and Fast Ltd.**

Void disposition

*The liquidator can seek to render the payments to Hard and Fast Ltd void under section 127 of the Insolvency Act 1986 on the basis that the payments were made after the commencement of liquidation. In a compulsory winding up, section 127 avoids any disposition of the property of the company made after the commencement of winding up, unless the court orders otherwise. Under section 129 of the Act, the commencement date is the date of the presentation of the petition to wind up. The*

**Commented [WPA15]:** 4/4 the grade is based upon the s 127 part of the answer. Section 239 cannot apply as the payments were made after not before the commencement of the liquidation.

avoidance provision in section 127 therefore acts in a backdated manner to avoid any dispositions of company property which has happened in the interim period between the winding up petition and the winding up order. The words “disposition of property” in section 127 of the Act are given a wide meaning and affect any payment of money as well as assets being sold or transferred.

In the present case, the payments clearly fall within the definition of “disposition of property” in section 127. The liquidation is deemed to have commenced at the date of the creditor’s petition for winding-up issued on 14 October 2022. The payments were done one month before the winding up order was made on 23 December 2022, and were therefore done after the commencement of liquidation. The payments can hence be voided by the court under section 127 of the Act.

The impact of section 127 is, however, not absolute. The court has a discretionary power to declare that dispositions shall not be void under a validation order. To that end, it is likely that Hard and Fast Ltd would apply for a validation order, and would bear the burden of proving that the order should be made. The court has a wide discretion whether or not to make a validation order, with the underlying rationale for such an order being that, where a company is trading, if transactions in the ordinary course of business which are entered into *bona fide* are not permitted, the parties interested in the assets of the company could be prejudiced. A validation order will only be made in relation to an insolvent company where the circumstances indicate that the disposition has been made *for the benefit of the general body of unsecured creditors*. The court will consider the following general guidelines:

1. Save in exceptional circumstances, the court will be reluctant to depart from the basic principle of *pari passu* distribution among creditors in order to validate payments made in relation to pre-liquidation transactions where the effect is to give a preference to a pre-liquidation creditor over other creditors (*Re Changtel Solutions UK Ltd*[2022] EWHC 694 (Ch)).
2. Payments are likely to be sanctioned where they are necessary to ensure continued supplies enabling the company to continue trading in cases where the court considers that the continuance of trading was in the best interests of creditors.
3. Transactions which do not diminish the company’s net assets and which increase the value of the company’s assets will normally be validated.
4. In cases where the parties are unaware that a petition has been presented and so the disposition is in good faith and in the ordinary course of business, the transaction is likely to be sanctioned as long as it was likely to be for the benefit of creditors generally.
5. Where goods have been paid for on terms of cash on delivery the court will consider the benefit to the company, including whether the payment will enable further supplies to be received and so enable the business to continue.
6. Although the court can authorize or validate a particular disposition it may also authorize a general continuance of trading.

*While transactions allowing the company to continue trading are generally validated, the court has also refused to grant validation orders where the disposition was going to benefit only one creditor to the detriment of other unsecured creditors of the company.*

*In the present case, it is likely that Hard and Fast Ltd would seek a validation order on the basis that the payments were necessary to ensure a continued supply of marble for the Company to continue trading. However, the liquidator can argue against the validation order on the grounds that there are no exceptional circumstances present which would justify the court's departure from the *pari passu* principle. While the payments were necessary to ensure the continued supply of marble to the Company, the payments were done and will be done to benefit only one creditor, Hard and Fast Ltd, to the detriment of other unsecured creditors of the company. Moreover, it can be argued that the payments were not done in good faith - both Hard and Fast Ltd and the Company were well aware of the creditor's winding up petition given that the terms of the cash on delivery arrangement was for further payments of GBP 3,000 up to the date of the winding up order. In these circumstances, it is likely that the liquidator would be able to argue that the payments to Hard and Fast Ltd should be voided under section 127 and that there should be no validation order.*

Preference?

*The liquidator may also have considered setting aside the payments to Hard and Fast Ltd on the ground that the payments were preferences under section 239 of the Insolvency Act 1986. The underlying purpose of section 239 is to prevent a company, shortly before entering a formal insolvency procedure, from placing one of its creditors in a better position than others. Section 239 prevents preferences like a payment in full where the creditor could have expected only a dividend as an unsecured creditor. It will also open up to attack a security given to a creditor, or other property of the company made available to the creditor, who previously only had priority as an unsecured creditor.*

*However, it is unlikely for an application under section 239 to succeed.*

*To successfully bring an application under section 239, the liquidator must show that:*

- (a) Hard and Fast Ltd was, at the time of the payments, a creditor of the Company;*
- (b) The payments had the effect of putting Hard and Fast Ltd in a better position than the position Hard and Fast Ltd would have been in if the payments had not been made (i.e. Hard and Fast Ltd has been preferred);*
- (c) The Company was, in giving the preference, influenced by a desire to prefer Hard and Fast Ltd; and*
- (d) The preference was given at a relevant time.*

*The first, second and fourth requirements will be satisfied in the present case. First, it is clear that Hard and Fast Ltd was at the time of the payments a creditor of the Company as the Company owed Hard and Fast Ltd sums for Hard and Fast Ltd's supply*

*of marble. Second, the payments were a preference as they had the effect of placing Hard and Fast Ltd in a better position than the position Hard and Fast Ltd would have been in if the payments had not been made. Had the payments not been made, Hard and Fast Ltd may not have been able to recover the full GBP 8,000 the Company owed it. Hard and Fast Ltd, being an unsecured creditor, would only have been paid out after the liquidation expenses, preferential creditors and floating charge holders have been paid in full. Third, the payments were given at the relevant time, having occurred within the six months prior to the onset of insolvency.*

*The difficulty is with the third requirement. The liquidator is unlikely to be able to show that the Company was, in making payment to Hard and Fast Ltd, influenced by a desire to prefer Hard and Fast Ltd. In *Re MC Bacon Ltd* [1990] BCC 78, Millett J drew a distinction between intention, which is objective, and desire which is subjective: "A man is taken to intend the necessary consequences of his actions [but a] man can choose the lesser of two evils without desiring either." In other words, one can intend to do something yet not desire it. It has been held that where the company was influenced solely by commercial considerations, specifically attempts to ensure that the company continued trading, there could be no desire to prefer. This is likely the case here. While Hard and Fast Ltd did apply pressure on the Company by demanding payment, the facts show that the Company was only driven to prefer Hard and Fast Ltd on the basis that Hard and Fast Ltd was a key supplier and the continued supply of marble was seen as essential by the Company. In these circumstances, the Company may have *intended* to prefer Hard and Fast Ltd, but cannot be said to have been influenced by the *desire* to prefer Hard and Fast Ltd.*

*Therefore, the liquidator is advised that voiding the payments under section 127 of the Insolvency Act 1986 remains the best option.*

**\* End of Assessment \***