



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 2024**. The assessment submission portal will close at 23:00 (11 pm) GMT on 1 March 2024. 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 2024** or by **23:00 (11 pm) BST (GMT +1) on 31 July 2024**. If you elect to submit by 1 March 2024, you **may not** submit the assessment again by 31 July 2024 (for example, in order to achieve a higher mark).
7. Prior to being populated with your answers, this assessment consists of **9 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 eight weeks of the commencement of the administration.**
- (c) within four 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

Section 426 of the Insolvency Act 1986 contains provisions for UK courts to provide assistance to overseas courts from certain listed jurisdictions. Which of the following is not a listed jurisdiction under section 426?

- (a) Malaysia.
- (b) Australia.
- (c) India.
- (d) Hong Kong.

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 filing by a company's directors of a Notice of Intention to Appoint an administrator produces a short-term moratorium on actions against the company which lasts for how long?

- (a) Five business days.
- (b) Twenty business days.
- (c) Ten days.**
- (d) Three months.

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 if the director has been a director of the company during which period prior to the insolvent liquidation?

- (a) Six months.
- (b) Five years.
- (c) Two years.
- (d) Twelve months.**

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 5 marks]

Who may bring an action under: (i) section 245 of the Insolvency Act 1986, (ii) section 6 of the Company Directors Disqualification Act 1986, (iii) section 246ZB of the Insolvency Act 1986, and (iv) section 127 of the Insolvency Act 1986?

- (i) Section 245 of the Insolvency Act 1986 covers Avoidance of a Floating Charge. It states that "a floating charge on the company's undertaking or property created at a relevant time is invalid"¹. This is a type of transaction that can be set aside should a company go into liquidation or administration, commonly referred to as reviewable or antecedent transactions. It is designed to prevent a company from giving any benefit to a creditor for existing liabilities, with no new consideration being provided. If the criteria set out in section 245 is met, the floating charge is automatically invalid, and no application should be required to be made by the office holder. The office holder should merely write to the floating charge holder stating that they believe the charge is invalid. The office holder may have to begin proceedings to prevent the charge holder enforcing the charge, therefore determination of whether a floating charge is valid or not under section 245 could trigger litigation, however in theory it should be an automatic invalidation.
- (ii) Under section 6 of the Company Directors Disqualification Act 1986 (CDDA), a director can be disqualified from holding the post of director, acting as a receiver or in any way managing a company, or acting as an insolvency practitioner if they are considered to be unfit to hold the role. This will be for a certain amount of time as deemed appropriate for the severity of the actions that led to the disqualification. These proceedings can only be brought by the Secretary of State, however the Directors Disqualification Unit considers reports made by liquidators regarding the conduct of directors. Under section 6 of the CDDA, the court shall make a disqualification where it is satisfied that the person is or has been a director of a company which has at any time become insolvent, and that their "conduct as a director of that company... makes the person unfit to be concerned in the management of a company"².
- (iii) Section 246ZB of the Insolvency Act 1986 covers wrongful trading in administration. This is where, after the company has gone into administration the court decides that a director or shadow director has failed to comply with their duty to take every step reasonably expected to minimise potential loss to the company's estate and therefore its creditors. If the court is satisfied this is the case, they can, "on the application of the administrator, may declare that that person is to be liable to make such contribution (if any) to the company's assets as the court thinks proper"³. From this, we can see that this type of action would be brought by administrator making an application to the court.
- (iv) Section 127 of the Insolvency Act 1986 covers avoidance of property dispositions. Section 127(1) states that "[i]n a winding up by the court, any disposition of the company's property, and any transfer of shares, or alteration in the status of the company's members, made after the commencement of the winding up is, unless the court otherwise orders, void"⁴. This can include payments made to third parties (including suppliers) after a winding up petition has been issued. If the court considers there to be transaction under section 127, they are deemed "void", and the property or funds must be returned to the liquidators as part of the insolvent's

¹ The Insolvency Act 1986, section 245 <<<https://www.legislation.gov.uk/ukpga/1986/45/section/245>>> accessed 18 February 2024

² The Company Directors Disqualification Act 1986, s.6(1) <<<https://www.legislation.gov.uk/ukpga/1986/46/section/6>>> accessed 17 February 2024

³ The Insolvency Act 1986, section 246ZB <<<https://www.legislation.gov.uk/ukpga/1986/45/section/246ZB>>> accessed 18 February 2024

⁴ The Insolvency Act 1986, section 127 <<<https://www.legislation.gov.uk/ukpga/1986/45/part/IV>>> accessed 18 February 2024

company's estate "unless the court otherwise orders". Claims under section 127 are brought by the liquidators of the insolvent company.

Question 2.2 [maximum 5 marks]

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.

The Corporate Insolvency and Governance Act 2020 introduced, by way of a new Part A1 to the Insolvency Act 1986 Act (the Act), a standalone procedure of a Moratorium. Directors can apply for a Moratorium if the company is, or is likely to become, unable to pay its debts as fined in section 123 of the Act⁵, and this may not require a court hearing unless there is an outstanding winding up petition or the company is an overseas company. A Moratorium is subject to the supervision of a monitor, who must monitor the company's affairs so as to form a view as to whether the Moratorium will result in the rescue of the company as a going concern.

A Moratorium only provides a stay on actions in relation to debts which were incurred prior to the Moratorium, therefore the company must pay any debts as they fall due during the Moratorium. This stay of creditor actions in relation to pre-moratorium debts is known as a 'payment holiday', however there some exceptions to this payment holiday, which include the following:

1. Any expenses or remuneration of the monitor;
2. Any goods or services which are supplied during the Moratorium;
3. Any rent in respect of a period during the Moratorium;
4. Any wages or salaries that arise under a contract of employment; and
5. Any redundancy payments.

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

Question 3.1 [maximum 6 marks]

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?

A debtor company may have entered into contracts prior to the commencement of administration, which place obligations on both sides, and where both parties still have obligations to perform. These are known as executory contracts, and a key example of this type of contract is a contract for the sale and supply of goods and services. Prior to the Corporate Insolvency and Governance Act 2020 (CIGA), a common problem for a company entering into administration or insolvency procedures would be the existence of insolvency-related termination clauses (*ipso facto* clauses) in these executory contracts. This could lead to problems, especially if an administrator or liquidator wishes to continue to operate the business of the company, in the hopes of increasing the opportunities to rescue the business, but also the opportunity for sale of the business as a going concern.

For some time, section 233 and 233A of the Insolvency Act 1986 Act (the Act) has covered essential supplies required to continue operating the business of the company, such as

⁵ *idem* section 123

supplies of gas, water, electricity, etc.⁶. The services that this section covers are listed in section 233(B) of the Act. Section 233(2)(a) makes it a condition that, if any of these supplies are given after the effective date (in this instance the date on which the company entered administration.⁷) the administrator must personally guarantee the payment of any charges in respect of the new supply. They cannot, however, make it a condition that, if further supplies are given, that any outstanding charges owed prior to the effective date will be paid.⁸ This is to prevent suppliers from compelling the payment of any debt that existed prior to the effective date by threatening to cut off the supplies. As there may be no choice but to pay to continue operating the business, this creditor would be paid ahead of other creditors regardless of priority, and it would also take essential money away from the business.

Section 233A prevents a supplier from enforcing insolvency-related clauses in a contract which allow them to terminate the contract. It prevents a supplier of these essential services from relying on any insolvency-related term which would allow them to terminate the supply, change the terms of the supply or require higher payments to continue the supply.

The CIGA went further than protecting the supply of essential services. Section 14 of the CIGA introduced section 233B into the Act, making it so if a company has entered into an insolvency process (including administration.⁹) a supplier cannot rely upon an insolvency related clause in a contract in terminating the supply of goods and services. Although it does not list what supplies and goods this section would include, it is assumed it would include most services subject to some exclusions as detailed in Schedule 4ZZA which includes financial services. Under section 233B(3) this includes any clauses that allow the following:

- "(a) the contract or the supply would terminate, or any other thing would take place, because the company becomes subject to the relevant insolvency procedure, or
- (b) the supplier would be entitled to terminate the contract or the supply, or to do any other thing, because the company becomes subject to the relevant insolvency procedure."¹⁰

Therefore any clause in a contract that would allow for the automatic termination of the contract or 'any other thing' to take place, or that provides discretion to the supplier to terminate the contract or do 'any other thing' cannot be relied upon. Section 233(4) prevents a supplier from terminating a contract or supply of goods in relation to an event that occurred prior to the company entering into insolvency procedures if that entitlement was not exercised at that time. The use of the term 'any other thing' in section 233(3) is not defined within the Act, but the explanatory notes to the CIGA states this would include 'changing payment terms'.¹¹, so this could include demanding cash on delivery or acceleration clauses.

There are some safeguards to suppliers where termination of a contract will be allowed. This includes where the office-holder consents to the termination, where the company consents to the termination, or where, on application to the court, the court is satisfied

⁶ The Insolvency Act 1986, section 233 <<https://www.legislation.gov.uk/ukpga/1986/45/section/233>> accessed 11 February 2024

⁷ *idem* section 233(4)

⁸ *idem* section 233(2)(b)

⁹ *idem* section 233B(2)(b)

¹⁰ *idem* section 233B(3)

¹¹ Explanatory Notes - Corporate Insolvency and Governance Act 2020 <<https://www.legislation.gov.uk/ukpga/2020/12/pdfs/ukpgaen_20200012_en.pdf>> accessed 17 February 2024

that continuation of the contract would cause the supplier hardship and therefore grants permission for the contract to be terminated.

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. 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?

As part of the liquidation process, the role of the liquidator is to take over control of the company, and get in any assets of the company, which they will then ultimately distribute according to the statutory order. It should be noted that prior to entering into formal insolvency proceedings, any creditors with a fixed charge will normally be paid first from the proceeds of sale of any of the assets subject to the fixed charges.

Subject to section 115 of the Act and Rule 6.42.¹² and 7.108.¹³ of the Insolvency Rules 2016 (the 'Rules'), there are a number of expenses which take priority over the company's preferential creditors, holders of floating charges and any unsecured creditors. Section 115 states that "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".¹⁴ Under Rule 6.42 and 7.108 expenses include all "fees, costs, charges and other expenses incurred in the course of the winding up". These are listed in order of priority within the Rules, and include, but are not limited to, the following:

- (a) Expenses properly incurred by the liquidator in preserving, realising or getting in the assets of the company, including any conduct of legal proceedings;
- (b) Amounts payable to any person who has assisted in the preparation of a statement of affairs;
- (c) Any necessary disbursements incurred by the liquidator in the course of the liquidation;
- (d) The remuneration of the liquidator; and
- (e) Any other expenses properly chargeable by the liquidator during the course of the liquidation.

Once any expenses of the liquidation have been paid, the assets are then used to pay any preferential creditors. These are set out in Schedule 6 of the Act and are split between 'ordinary preferential debts' and 'secondary preferential debts'. Ordinary preferential debts are paid ahead of secondary preferential debts, but otherwise they rank equally amongst themselves. Ordinary preferential debts include, but are not limited to:

- (a) Any contributions owed to occupational pension schemes;
- (b) Any amount owed by the debtor to a person who is or has been an employee of the company and is payable by way of salary or wages in respect of the whole, or any part of the period of four months prior to proceedings (capped at £800, any amount above this is considered an unsecured debt);

¹² Part 6, Rule 6.42 is in relation to Creditors Voluntary Winding Up procedures <<The Insolvency (England and Wales) Rules 2016>> accessed 17 February 2024

¹³ Part 7, Rule 1.108 is in relation to compulsory liquidation by the Court <<<https://www.legislation.gov.uk/ukSI/2016/1024/rule/7.108/made>>> access 17 February 2024

¹⁴ Subject to section 174A, Insolvency Act 1986 section 115 <<<https://www.legislation.gov.uk/ukpga/1986/45/section/115>>> access 17 February 2024

- (c) Any accrued holiday pay due to employees of the company in respect of the period before liquidation proceedings; and
- (d) Any amount due to EU levies for coal and steel production.

Secondary preferential debts include any debts due to the Financial Services Compensation Scheme, and also any HMRC debts in respect of VAT and relevant reductions such as PAYE tax deductions, National Insurance deductions VAT payments and student loan deductions, amongst other things.

Any secured creditors with a floating charge would be dealt with next. If there is more than one floating charge holder, priority is usually given based on which floating charge was created first. However, payment to floating charge holders is subject to section 176A which applies to any company in liquidation which has a floating charge created on or after 15 September 2003. Pursuant to this section, the liquidator must make a 'prescribed part' of the company's assets available for satisfaction of unsecured debts. They cannot distribute any of this 'prescribed part' to a floating charge holder unless it is in excess of the amount that would be required to satisfy all unsecured debts. This is calculated after the liquidation expenses and preferential creditors have been paid.

Unsecured creditors, who have no security, are usually paid last in the statutory order, and they rank equally among themselves. Unsecured creditors include suppliers, customers, contractors, and clients. The risk for unsecured creditors is that, once all other expenses and debts have been paid, there will be little or nothing left from the proceeds of the liquidation to pay them.

Finally, if there any funds remaining once all the above have been paid, any surplus funds will be distributed amongst the shareholders according to the company's constitution. This is normally according to each shareholder's respective shareholding rights.

Each class of creditor or expense can enjoy the right of *pari passu* distribution. This is the principle that creditors of the same class will be dealt with equally, and proportionately to their claim out of the assets available for distribution. This distribution of any assets is also in order of priority of creditors, so secured creditors will have a stronger claim than unsecured creditors.

The Corporate Insolvency and Governance Act 2020 (CIGA) introduced Part A1 to the Act, which is a new procedure of a Moratorium. This is a debtor-in-possession procedure whereby the directors stay in day-to-day control of the company and lead any discussions on rescue and restructuring, but under the supervision of monitor who may also provide expert advice on the restructuring. Directors can apply for a Moratorium, the intention being to try and rescue the company as a going concern, and this allows them some 'breathing space'. It provides a stay on actions in relation to any pre-Moratorium debts only, therefore the company is expected to pay their debts as they fall due during the Moratorium. A Moratorium comes to an end either if the company enters into a restructuring plan or scheme, or if it enters into insolvency proceedings. It can also be brought to an end by the monitor, if they do not think that the rescue of the company is likely or if the company is unable to pay its Moratorium debts.

If, within 12 weeks of the end of the Moratorium, the company enters into administration or liquidation, this changes the priority of debts in the subsequent liquidation. Section 174A of the Act states that "the following are payable out of the company's assets (in the order of priority shown) in preference to all other claims—

- (a) any prescribed fees or expenses of the official receiver acting in any capacity in relation to the company;

(b) moratorium debts and priority pre-moratorium debts."¹⁵

This therefore affords certain pre-Moratorium or Moratorium debts that were unsecured (such as debts owed to employees or financial services debts) a form of 'super priority' in the subsequent liquidation, in that they will be paid even prior to the liquidator's fees and expenses.

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

Prior to going into compulsory liquidation on 28 February 2024, under pressure from its bank, Ambitus Bank plc, and in order to prevent it from demanding repayment of the company's loans, Blazer Laser Limited (the Company), granted a debenture in favour of Ambitus Bank plc in June 2023. 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 13 January 2024.

Sometime in January 2023, as the Company continued to suffer cash flow problems, the directors approved the sale of two laser cutting machines to Angela Bannister (a director) for GBP 40,000 in cash. The machines had been bought for GBP 100,000 a year before.

A month before the winding up order was made, Angela Bannister received an email from Aluminium Alumini 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 metal was seen as essential by the Company, the board authorised a payment of GBP 20,000 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 8,000 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 Ambitus 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 Ambitus Bank plc;

We know that the Company had loans with Ambitus Bank plc (the "Bank"). Following pressure from the Bank in demanding repayment of these loans, the Company granted a debenture in favour of the Bank in June 2023 to prevent the Bank from demanding repayment of the loans, which contained a floating charge over the whole Company's undertaking. We are also aware that the Company has been suffering cash flow problems since at least January 2023, and went into compulsory liquidation in February 2024.

Floating Charge Avoidance

¹⁵ Insolvency Act 1986 section 174A(2) <<<https://www.legislation.gov.uk/ukpga/1986/45/part/IV>>> accessed 17 February 2024

Section 245 states that "a floating charge on the company's undertaking or property created at a relevant time is invalid"¹⁶. This means a court could find that the floating charge contained in the debenture granted in favour of the Bank is invalid, therefore retrospectively invalidating it.

First, they would need to consider if the if the floating charge was created at a 'relevant time'. As the charge was not created in favour of a connected person¹⁷, we would look to section 245(3)(b) which states that "a floating charge is created by a company is a relevant time for the purposes of this section if the charge is created... at a time in the period of 12 months ending with the onset of insolvency"¹⁸. This is qualified by section 245(4), which states that "that time is not a relevant time for the purposes of this section unless the company... is at that time unable to pay its debts within the meaning of section 123". We know the debenture was granted in June 2023, which was less than 12 months prior to the onset of insolvency¹⁹, so this requirement would be satisfied. We also know the debenture was granted to prevent the Bank from demanding payment of loans, so it is safe to say they would be considered unable to pay their debts under section 123.

There are two possible exceptions to this within the legislation. Under section 245(2) a floating charge will not be considered invalid if:

- (a) "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,
- (b) 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"²⁰.

This means that the floating charge will not be considered invalid if it has increased the company's assets in any way or if it has provided new consideration. In this case there is no new consideration for the charge that we are aware of, we are only told it was granted to prevent the Bank demanding payment of the current consideration.

As the requirements of the legislation have been met, it is likely that the floating charge granted in favour of the Bank would be rendered invalid. It should be noted that the underlying debt will remain valid.

Wrongful Trading

It is worth considering whether an action for wrongful trading could be brought against the company's directors. Wrongful trading is covered in section 214 of the Act, can occur when a company's directors have continued to trade even though they knew, or should have concluded, that there was a prospect the company would enter liquidation.

From what we can see here, they were under pressure from their bank, and granted in order to prevent the Bank from demanding payment. This shows a clear suggestion that the company that the company in financial distress and the directors should have been aware

¹⁶ The Insolvency Act 1986, section 245 << <https://www.legislation.gov.uk/ukpga/1986/45/part/VI>>> accessed 18 February 2024

¹⁷ The Insolvency Act 1986, section 249 << <https://www.legislation.gov.uk/ukpga/1986/45/section/249>>>, accessed 17 February 2024

¹⁸ The Insolvency Act 1986, section 245(3)(b) << <https://www.legislation.gov.uk/ukpga/1986/45/part/VI>>> accessed 18 February 2024

¹⁹ *idem* section 245(5)(d)

²⁰ *idem* section 245(2)

that there was a prospect of liquidation. If this was the case, they potentially should not have continued trading beyond this point.

If the directors are found liable of wrongful trading under section 214 of the Act, they will be liable to "make such contribution (if any) to the company's assets as the court thinks proper".²¹

Question 4.2 [maximum 6 marks]

The sale of the laser cutting machines; and

We are aware that, in January 2023 when the Company was suffering from cash flow problems (which suggests they were unable to pay their debts as they fell due), the directors approved the sale of two laser cutting machines to Angela Bannister, also a director. Although they had been purchased for GBP 100,000 a year earlier, they sold these machines for GBP 40,000 in cash.

Transaction at an Undervalue

One of the first actions the liquidator could consider is whether this transaction could be attacked as a transaction at an undervalue under section 238 of the Act. If so, the liquidator could apply to the court for an order under this section and, upon such an application the court shall "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".²² In this situation, it is for the applicant (the liquidator) to satisfy the court as to the value of the consideration provided to the Company when entering into the transaction, and whether there was a deficiency.

Under section 238(4), it states that a company enters into a transaction at an undervalue if "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".²³

For this to be an actionable offence, the transaction must have taken place "at a time in the period of 2 years ending with the onset of insolvency"²⁴, which would be the date of the commencement of the winding up.²⁵, which we know was 13 January 2024. It also must be shown that at the time of the transaction the Company was unable to pay its debts or, as a result of the transaction, became unable to pay its debts. As the transaction was entered into in January 2023, this is within the relevant time period to be considered a transaction at an undervalue. We have not been given enough information to know if the Company was unable to pay its debts within the meaning as defined in section 123 of the Act, however we do know they were continuing to suffer cash flow problems, suggesting this is not a new situation and could have been ongoing for some time. There is however a presumption under section 240(2) that if the transaction at an undervalue is entered into by the company with a person who is connected to the company, which would include a director.²⁶ there is a presumption that the company is insolvent.

²¹ The Insolvency Act 1986, section 214 <<<https://www.legislation.gov.uk/ukpga/1986/45/part/IV>>> accessed 17 February 2024

²² The Insolvency Act 1986, section 238 <<<https://www.legislation.gov.uk/ukpga/1986/45/part/VI>>> accessed 17 February 2024

²³ *idem* section 238(4)(b)

²⁴ *idem* section 240(1)(a)

²⁵ *idem* section 240(3)(e)

²⁶ The Insolvency Act 1986, section 249(a) <<<https://www.legislation.gov.uk/ukpga/1986/45/section/249>>>, accessed 17 February 2024

Should the court decide that the conditions of the legislation have been fulfilled and the transaction was at an undervalue, they can make an order under section 241.²⁷, in an attempt to restore the position to what it would have been had the transaction not been entered in to. In this situation, this could be an order requiring that any property transferred as part of the transaction be vested back in the Company if it is still in Ms Bannister's possession, or they could order that the proceeds from the sale of the property be vested in that Company. If an order is made, whatever proceeds are made would go to the insolvent estate to be distributed amongst the creditors by order of priority.

Section 238(5) does state that a court shall not make an order under this section in respect of a transaction if it is satisfied that either the company entered into the transaction in good faith and for the purpose of carrying on business, or if at the time it did so there were reasonable grounds for believing that the transaction would benefit the company.²⁸.

Misfeasance

Under section 212 of the Act, if in considering the conduct of certain persons the court finds a wrongdoer "has misapplied or retained, or become accountable for, any money or other property of the company, or been guilty of any misfeasance or breach of any fiduciary or other duty in relation to the company" it may make an order for repayment or restoration of the money or property to the company. A section 212 claim can only be brought by a liquidator during a company's liquidation.

In bringing this claim, the liquidator must be able to demonstrate that the respondent to the claim owed relevant duties to the company, and that they breached these duties which cause a loss to the company. If successful and repayment or restoration is made to the Company, this will form part of the assets available for distribution to the creditors.

There is a defence to this under section 1157 of the Companies Act 2006 (the 'Companies Act'). Here it states that if it appears to the court that "the officer or person is or may be liable but that he acted honestly and reasonably, and that having regard to all the circumstances of the case (including those connected with his appointment) he ought fairly to be excused, the court may relieve him, either wholly or in part, from his liability on such terms as it thinks fit." Therefore the court may relieve them from any liability if they believe the director acted honestly and reasonably.

Director disqualification

A further consideration is disqualification of the directors under the Company Directors Disqualification Act 1986 (CDDA). This can disqualify a person from holding the post of director, acting as a receiver or in any way managing a company, or acting as an insolvency practitioner if they have are considered to be unfit to hold the role. These proceedings can only be brought by the Secretary of State, however the Directors Disqualification Unit considers reports made by liquidators regarding the conduct of directors.

Under section 6 of the CDDA, the court shall make a disqualification where it is satisfied that the person is or has been a director of a company which has at anytime become

²⁷ The Insolvency Act 1986, section 241 <<<https://www.legislation.gov.uk/ukpga/1986/45/part/VI>>> accessed 1 March 2024

²⁸ *idem* section 238(5)

insolvent, and that their "conduct as a director of that company... makes the person unfit to be concerned in the management of a company".²⁹.

Examples of conduct that can lead to a director being disqualified are not keeping proper company accounting records, using company money or assets for their own personal benefit, failing to submit tax returns, allowing the company to continue to do business when it is unable to pay its debts.

Question 4.3 [maximum 4 marks]

The payments to Aluminium Alumini Ltd.

We know that, a month before the winding up order was made, Aluminium Alumini Ltd (AAL), a creditor of the company, contacted a director of the company demanding immediate payment of all sums owing to it, and informing the company that further supplies would only be made on a cash on delivery basis. The company considered the continued supply of the metal to be essential for the continuation of the business, and therefore authorised a payment of GBP 20,000 to cover the existing sums owed and agreed further payments of GBP 8,000 for further supplies on a cash on delivery basis. These transactions took place up to the date of the winding up order being made.

Preferential transactions

We know the company was suffering from cash flow problems in January 2023, and therefore must have been aware a year on that it would be going into voluntary liquidation proceedings. In these circumstances, the company should not have taken any action which would place one of its creditors in a better position than the others. The liquidator should therefore consider whether these transactions with AAL can be attacked under section 239 of the Act. Section 239 has a range of terms in common with section 238, which has been discussed in detail above.

For this to be an actionable offence, the transaction must have taken place 'at a time in the period of 6 months ending with the onset of insolvency'.³⁰, which we know was the case. This time period is shorter than the time period for the 238 offence discussed above, as the creditor would not be considered a connected person under section 249 of the Act.³¹. It must also be shown that at the time of the transaction the company was unable to pay its debts or, as a result of the transaction, became unable to pay its debts, within the meaning as defined in section 123 of the Act. Section 123 (1)(e) states that a company is deemed to be unable to pay its debts '... if it is proved to the satisfaction of the court that the company is unable to pay its debts as they fall due'. Section 123 (2) says that '[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'. We do not know enough about the company and its liabilities, however we do know the transactions were entered into a month before the winding up order was made, and we also know the company has been suffering from cash flow problems since January 2023, so there is a chance the court would consider the company unable to pay its debts. Just because it managed to pay AAL, the mere fact they had a balance owing

²⁹ The Company Directors Disqualification Act 1986, s.6(1)

<<<https://www.legislation.gov.uk/ukpga/1986/46/section/6>>> accessed 17 February 2024

³⁰ The Insolvency Act 1986, section 240(1)(b) <<<https://www.legislation.gov.uk/ukpga/1986/45/part/VI>>> accessed 17 February 2024

³¹ The Insolvency Act 1986, section 249 <<<https://www.legislation.gov.uk/ukpga/1986/45/section/249>>>, accessed 17 February 2024

in sums of GBP 20,000 suggests they had not been paying the supplier as the debts fell due, and there is a likelihood this will be the same for other creditors.

Under section 239(4), 'a company gives a preference to a person if -

- (a) that person is one of the company's creditors or a surety or guarantor for any of the company's debts or other liabilities, and
- (b) 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 insolvent liquidation, will be better than the position he would have been in if that thing had not been done.³²'

We know AAL is one of the company's secured creditors, most likely an unsecured creditor as they are a supplier and we have no information to suggest they have any security over the company. We also know that the transactions had the effect of putting AAL into a better position than they would have been had the payments not been made once the company went into liquidation. AAL, assuming they were an unsecured creditor, would have been unlikely to receive payment once all other creditors with higher priority had been paid.

If the court was to decide that the requirements for a section 239 have been met, they may be minded to make an order under section 241 requiring AAL 'to pay, in respect of benefits received by him from the company, such sums to the office-holder as the court may direct'.³³

A possible defence for the company under section 239 is that '[t]he court shall not make an order under this section in respect of a preference given to any person unless the company which gave the preference was influenced in deciding to give it by a desire to produce in relation to that person the effect mentioned in subsection (4)(b)'.³⁴ As discussed above, the key word here is 'desire'. It must be shown that they had a desire to give them preference, not just an intention.³⁵ We have been told that the company saw the supply of the metal as essential, it is safe to assume they were attempting to continue operating the business. There is nothing to suggest they had a desire to give preference to the supplier as a creditor, merely that they were commercially motivated to make payments as needed to keep the business running.³⁶, therefore the court may not be minded to make a section 239 order in this situation.

Dispositions Void unless Validated

Section 127 of the Act is intended to avoid any distribution of property or assets of the company after the commencement of the winding up, which we know here was 13 January 2024 when the winding up petition for this was issued. Any actions taken after this date, unless the court orders otherwise, are void. The liquidator can take steps to enforce section 127 in order to recover and retrieve any company assets that have been disposed within during the period between the petition and the winding up order.

Given that we know the payment was made to AAL a month before the winding up order was made on 28 February 2024, this would have been around 28 January 2024. As the winding up petition was issued on 13 January 2024, the liquidator could take the necessary steps

³² The Insolvency Act 1986, section 239 <<<https://www.legislation.gov.uk/ukpga/1986/45/part/VI>>> accessed 18 February 2024

³³ *idem* section 241

³⁴ *idem* s.239

³⁵ *Re M C Bacon Ltd* [1990] B.C.C. 78

³⁶ *Re New Generation Engineers* [1993] BCLC 435

under section 127 to recover the funds, which will form part of the assets available for distribution to the creditors.

*** End of Assessment ***