Insolvency Commentary: Remuneration tips from the top

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Top tips for IP claims for remuneration

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Introduction

Those who have had experience with making office-holder remuneration applications to court will know how tedious and difficult they can be, particularly when faced with opposition from aggressive creditors who may be withholding approval of fees to suit their own agendas. The burden is always on the insolvency practitioner ("IP") to justify their fees, and so it can be a relatively easy task for stubborn creditors to, if so minded, cause IPs a headache by launching general and sweeping criticisms that cast doubt on the level of fees claimed. Once an IP is placed on the back foot, time-consuming and costly litigation is a likely inevitability.

The aim of this breakfast briefing is to look at how a robust remuneration application may be put together – as well as highlight what IPs can do from day one of their appointment, so as to make the task of putting together the application easier in the event that the need to do so arises. Forward planning is key: many of the pitfalls encountered by IPs can be avoided by increasing awareness of the way in which an application needs to be presented, and implementing robust policies and practices.

Key information and evidence for a remuneration application

Part 6 of the Practice Direction – Insolvency Proceedings ("the Practice Direction") sets out, in rather extensive detail, a list of information and evidence to be provided on any remuneration application. It would be neither useful nor interesting to repeat the content of that Practice Direction here, and for those of you who have not had the pleasure of reading through it, it is an essential resource to be

aware of and consider in the event the need to make a remuneration application arises – this paper is not intended to be a substitute for the guidance which is set out there. Additionally, reference should also be made to the Statement of Insolvency Practice (SIP) 9: Remuneration of insolvency office holders.

However, what is helpful to consider in this session, is how to actually go about providing the information which the Practice Direction requires. In particular, when making an application for remuneration in a complex and lengthy administration, considerable detail will be necessary in order to justify the amount of remuneration claimed. Presenting this material so as to comply with the Practice Direction, and ensuring the application includes all necessary evidence in a digestible and logical manner, is not always straightforward. Accordingly, here are some suggestions as to how it may be done.

Effective use of witness evidence

The Practice Direction requires, amongst other things, various detailed narratives pertaining to work done, time spent on different workstreams, explanations of which fee earners have been working on different tasks, and justifications having regard to why work was reasonable, necessary, and/or beneficial (see in particular paragraph 21.4.1). Paragraph 21.7(d) provides that the application may include *"any other schedules or such other documents providing the information referred to in paragraph 21.4 above, where these are likely to be of assistance to the court in determining the application."*

In a lengthy administration, where significant time costs have been incurred and work has been done over many months (or indeed years), providing narratives as required by paragraph 21.4 in a single witness statement is likely to at best cause a headache, at worst be simply impossible to follow in any meaningful way. Presentational clarity is important not only to ensure that all the information required by the Practice Direction is indeed provided in the first place, but also to make a robust case that justifies the level of remuneration claimed in a clear and logical manner. As the Practice Direction makes clear, in its "guiding principles" for remuneration claims, it will be the *IP* who is required to justify their remuneration, any doubt will be resolved *against* the IP, and there is a heavy emphasis on the work done and in respect of which remuneration is claimed, actually having provided *value*. An application which is evidentially messy bears with it the higher risk that a court will not be able to easily assess the justifications for work done, reasonableness of the amount of time spent on such work, and see how value has been provided by the IP. Furthermore, an application which is difficult to follow is likely to be criticised by any opposing creditors, with the resultant risk of the parties being

unable to agree on or narrow issues, and any litigation becoming even more time consuming and costly.

Some suggestions are:

- Use a witness statement, not to narrate every single item of work done, but rather to provide an overarching framework for more detailed evidence to follow (in schedules annexed to the statement). The witness statement should be used, in particular, to:
    - Emphasise headline successes and outcomes achieved. As mentioned, the level of remuneration claimed will be considered having close regard to the value of the service actually rendered, and so this ought to be an essential feature of the evidence in support of the application.
    - Provide a timeline of the administration, dividing it into periods (either temporally, or by reference to key activity periods such as trading and non-trading). The preferable approach is likely to differ depending on the nature of the administration and the issues in the particular case. A narrative of the different workstreams required throughout each period, and why these were necessary in order to achieve the objectives, is also helpful; along with an explanation of how staff have been allocated to different workstreams, where (and why) third parties/consultants have been utilised, and how efforts have been made to avoid duplication of work.
    - Highlight key issues and complexities faced during the administration, placing particular emphasis on any peculiar features which will have increased work involved and therefore time and cost. For example, did unforeseen issues arise? Have international elements increased work required? Were there any particular issues realising certain assets?
    - If there have been any particular issues raised by creditors (for example in pre-action correspondence) pertaining to the remuneration claimed, it will often be good to address these in an upfront manner.
    - Set out correspondence with creditors, attempts that have been made to obtain approval, and (if relevant) any matters which might demonstrate unreasonable conduct on the part of the creditors.

- Use schedules to provide the substantive detail on time spent and costs incurred, which is required by the Practice Direction. This information will essentially be drawn from IP time records. An idea for the presentation of this material is to have:
    - An overview/executive summary of time/costs incurred per category of fee earner for the entire period of the administration, to provide a general snapshot of the work done.

- A spreadsheet overview per month (or other designated period of the administration), showing time/costs incurred per category of fee earner, for each of the five general SIP9 activity categories. These are (1) Administration and Planning; (2) Investigations; (3) Realisation of Assets; (4) Trading; (5) Creditors.
- A spreadsheet per month (or other designated time period), showing a more detailed numerical breakdown of time/costs incurred, per individual, per sub-category of activity within those five general categories.
- A table per month (or other designated time period) which provides a narrative for the work done by each individual in each of the sub-categories of activity.

The last two bullet points referred to above are the most important. As to this, the Practice Direction makes clear that work done must be described by reference to specific activity categories – the general SIP9 categories are insufficiently detailed for the purposes of a remuneration application.

Needless to say, there is no single correct formula as to how the evidence ought to be presented, and in every case it will be important to consider any particular features of the administration and how the evidence in support is best presented, in light of those features.

What to do from Day One?

Compiling the information required by the Practice Direction is a task that can be made significantly easier by IPs having good practices in place, particularly regarding the way in which their time is recorded, so that in the event an application becomes necessary, the information is already collated and simply needs transferring into a format presentable to the Court. Accordingly, here are some suggestions of what to do throughout the administration.

Good time recording practices

When recording time, an obvious (but key) principle which should be borne in mind is that the *more* time that is spent on a particular task, the longer the explanation and the justifying narrative for undertaking that particular task, ought to be. It will be easier to do this contemporaneously when the work is actually being done, than to try and do it at a later date, reconstructing from incomplete records. This principle is worth emphasising, given the number of times that time is not recorded with sufficient detail – a criticism often made in the reported cases on IP remuneration.

Helpful guidance on the level of detail was provided by Registrar Jones in *Re Brilliant Independent Media Specialists Ltd [2015] BCC 113 at paragraphs [47]–[48]: "… some activities will be standard, the length of time spent apparently reasonable and little need be narrated. In contrast tasks taking many hours or requiring high cost need to be explained, for example by briefly describing what was involved, why it was necessary and why it took the time it did… A succinct narrative analogous to the narrative within a solicitor's bill should not be expensive or require a disproportionate amount of work…"*

All individuals who are involved with work on the administration should be briefed on good time-recording practices. This includes not only on the level of narrative detail that should be provided, but also how to go about recording time against different activity codes. For example, an individual might perform multiple tasks during a working day. Ideally, different types of task should be recorded separately, under separate time entries (as opposed to bulk recording under one activity code).

Record keeping – workstreams and staff allocation

In addition to generally keeping a good narrative of work done, records should be kept of key decisions made at various stages throughout the administration, including staff allocation to workstreams, strategic plans, and reasons for the appointment of consultants or third parties.

It often becomes necessary, when making an application, to justify why individuals of a particular seniority were used, and why a certain level of staffing was required. Again, it is easier to make a record as the work is being done, as opposed to trying to remember, reconstruct and justify, at a later date.

It is also important to be mindful of who is allocated to perform particular tasks because of the general rule *against* recovering costs normally regarded as overheads. In particular, the Practice Direction, paragraph 21.4.7(b) states that *"where, exceptionally, the office-holder seeks remuneration in respect of time spent by secretaries, cashiers or other administrative staff whose work would otherwise be regarded as an overhead cost forming a component part of the rates charged by the office-holder and members of their staff, a detailed explanation as to why such costs should be allowed or should be provided."*

As to disbursements, in *Jacob v UIC Insurance Co Ltd* [2007] BCC 167, the court confirmed that it retains a power to examine all aspects of the expenses claimed (including disbursements in respect of third parties). Therefore, it is important to have justifications for engaging third party consultants, and the work done by them.

Keeping creditors updated on costs

An effective way to try and pre-emptively prevent creditors making complaints about fee levels, is to clearly communicate with creditors throughout the administration by estimating likely fees and providing regular updates as to fees actually incurred. Of course, fee proposals in initial estimates may be exceeded if unforeseen and unexpected issues arise during the administration. However, having an ongoing dialogue with creditors, and making creditors aware of any incremental changes to the fees incurred, removes the risk of surprising (and thereby antagonising) creditors with a larger-than-expected bill. It may also be possible to obtain incremental approval from creditors at least in respect of *some* remuneration, which may reduce the risk of having to litigate over the entirety of an IP's fees.

Further, under Rule 18.34(3) of the Insolvency (England and Wales) Rules 2016 ("the Rules"), creditors have a time limit eight weeks after receipt of a progress report to challenge the charging of remuneration or incurring of expenses in question. Whilst this rule does not obviate the need for an application to court for remuneration to be fixed, if there has been clear disclosure of costs and fees incurred throughout the administration, then a creditors' failure to raise objections might still be relied on – for example to demonstrate that a creditor is acting unreasonably.

Key pitfalls and matters to be aware of

Many of the key pitfalls for IPs align with the suggestions given above, for what ought to be done from day one.

Inadequate records

If time-keeping records are inadequate, IPs are likely to have insufficient narrative to support their remuneration application, with it being impossible to work out what was done at a later date when it comes to compiling the evidence. Indeed, individuals responsible for particular tasks may have left the firm, or simply not be able to remember what was done.

An example of a case where inadequate records led to a severe reduction in remuneration claimed is *Re Brilliant Independent Media Specialists Ltd* [2015] BCC 113. In that case, the claim remuneration at £389,340.50 was reduced by Registrar Jones down to £233,147.25: i.e. only 65% of the total fees claimed being finally awarded. The primary reason for the sharp reduction was that there was simply no narrative of specific work done in the spreadsheets of time/cost attached to the application.

Likewise, in *Jacob v UIC Insurance Co Ltd* [2007] 2 BCLC 46, there were serious gaps in the records with various "null" narrative entries. A significant deduction was made by the judge, going over and above the deduction which was recommended by the assessor.

Inappropriate staff allocation and delegation of work

Another common issue which arises is work duplication, or work carried out by senior members of staff where it should have been delegated. In some cases, there may be justifications for having more senior individuals carry out tasks, due to their complexity and in circumstances where major strategic decisions are required. It may also be more cost-effective for individuals of a certain seniority to carry out tasks, because this may result in the work being done more efficiently.

However, as the Practice Direction requires a breakdown of work done per category of fee earner, what may have been considered justified at the time can present badly if, upon collation of the data, there is a significant distortion in favour of more senior individuals carrying out work. Such distortions will often face criticism from creditors, and in the absence of robust justification for why individuals were allocated to certain workstreams, there is a risk of deductions to fees claimed (for example, with reductions being made, in line with the rates of lower-grade fee earners).

Don't forget future work

Often, it may become necessary to make a remuneration application in circumstances where the administration is still ongoing, such that IPs will still have work to do in future. Estimates for this should be included in the application.

Keep an eye out on the deadline

Under Rule 18.23(3) of the Rules, an application to court to fix the basis of remuneration must be made not more than 18 months after the date of the administrator's or liquidator's appointment. It is important to think ahead and be mindful of this deadline, because compiling the evidence for a remuneration application will often be very time-consuming and therefore needs to be prepared well in advance.

Tips for dealing with a contested remuneration application

Pre-Action Stage

The Practice Direction, at paragraph 21.4.11(b), requires the IP to provide details of *"what (if any) consultation has taken place between the office-holder and those persons [with an interest in the assets] and if no such consultation has taken place, an explanation as to the reason why."*

Thus, it is generally important (and good practice) to communicate and consult with creditors, prior to making an application for remuneration. In general, an approach to pre-action as would ordinarily be taken in other types of proceedings is desirable.

When communicating with creditors at the pre-action stage, it is important that adequate information is provided (in line with the Practice Direction) in order for creditors to make a meaningful assessment of the fees claimed. If inadequate information is provided, then creditors are likely to complain that the remuneration application was premature and that they did not have sufficient detail to approve fees.

Consider which costs to write off

It may be that, as a result of pre-action correspondence with creditors, and when going about compiling evidence for an application, it becomes apparent that there are issues with the fees claimed. For example, when reviewing time records, one might come across inadequate narratives, or various errors (such as time being recorded against incorrect activity codes, or bulk recordings which make it impossible to divide up the time against specific activities). Other errors might be in recording time, in circumstances where those time costs simply should not be claimed: such as where this is properly considered a firm overhead, with no exceptional justification for charging to the case.

Where errors are discovered, IPs may seek guidance on writing off costs. There are various reasons why one might wish to do so, including avoiding reputational damage: an IP may be concerned that (if the case proceeds to trial and judgment) a judge will publicly criticise their policies and practices, with this damaging future business. Another reason for considering writing off costs is to narrow the issues and to reduce the likelihood of creditor criticism, in an effort to avoid proceeding with a contested trial.

However, in the event an IP does have concerns, very careful consideration ought to be given to proposals for writing-off time. As a general guide, where there are time entries which obviously should not be claimed (such as overheads, in the absence of exceptional circumstances), there is little harm in writing these off (since it is highly unlikely such time costs will be awarded by a judge in any event). On the other hand, much more thought needs to be given ahead of a decision to write off time associated with other types of errors (such as insufficient narrative). Bearing in mind that the burden is on the IP to justify the level of fees claimed, there is a real risk that in *any* application, reductions to the level of fees claimed, will be made. It is therefore risky to pre-emptively reduce figures claimed, because an IP may still be faced with a contested application and difficult creditors, and deductions being made by the court in any event.

Payment on account

A potential weapon which should not be forgotten is the ability for an IP to apply for an interim payment. Under paragraph 21.8 of the Practice Direction, on any remuneration application the Court has power to *"make an order allowing payments of remuneration to be made on account subject to final approval whether by the Court or otherwise"*. This is a very important jurisdiction, and one which should be taken advantage of – particularly given that an IP, whose remuneration has not been approved by creditors, may have carried out significant amounts of work in an administration and not received any payment for their services.

An application for a payment on account should be made when bringing the remuneration application, and IPs should not be shy asking for a substantial proportion of the final fees they are claiming. Even in cases where there have been serious issues with the justifying evidence, it is highly unlikely for the Court to make deductions reducing the fees claimed to below 60 per cent. It is therefore worthwhile asking for a payment of at least this proportion of fees, especially where robust evidence has been presented in support of the application.

The secrets of a successful challenge

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The burden is on an officeholder to justify his entitlement to remuneration. Given this requirement it might be thought that there would be far more successful challenges to an officeholder's remuneration than is, in fact, the case. It is generally easier to attack, than justify. However, my advice to creditors and others thinking about challenging remuneration is: "be careful what you wish for" because a challenge is usually (a) very time-consuming; (b) expensive; (c) and unsatisfying because it is rare that a court disallows a sufficiently large amount that the applicant feels vindicated in having brought the challenge.

Further, as the years have passed, legislation and guidance applicable to the claiming of remuneration has become more and more detailed so that, provided that the officeholder follows the guidelines, there should be little scope for a challenge of any significance. And, if the challenge is not significant it is unlikely that the officeholder will be heavily (or at all) penalised in costs in connection with a challenge and an appreciable prospect that a court will order the costs to be paid out of the estate resulting in a wholly pyrrhic victory for the applicant even if he has demonstrated a number of instances of overcharging.

The rules on claiming remuneration are all now contained in the same place, the Insolvency Rules 2016 (IR 2016), Chapter 4 r.18.15 and following. In addition, there is the Practice Direction: Insolvency Proceedings [2018] BCC 421 Part 6 which provides additional guidance on the principles that will be applied by the court if the remuneration of an officeholder is challenged. One of the most important provisions introduced by the 2016 Rules is r.18.16(4) which provides that where an office-holder proposes to be remunerated by reference to time properly given (which is the usual basis adopted) the officeholder is required prior to the determination of which of the bases are to be fixed provide a fee estimate and details of the expenses likely to be incurred. The fee estimate must contain details of the work that the officeholder proposes to undertake. This is a substantial improvement on the situation that prevailed before the change because inevitably officeholders must now give close attention at the outset of the assignment as to what the job is going to entail and to provide an idea of what it is going to cost.

The Routes of Challenge

Under the IR 2016

In terms of challenges, the first port of call is the creditors' committee or in default a meeting of creditors. It is the creditors' committee that determines the basis of remuneration under r.18.18(2). The determination of a basis is not technically the place where an officeholder's fees are challenged. However, it can provide a forum for discussing the basis and requesting the officeholder to explain why he/she considers that one basis is better/more appropriate than another. My advice to any creditor who is not particularly happy with the choice of officeholder and has concerns (perhaps based on previous experience or reputation) as to whether the particular officeholder will provide value for money, is to get onto the creditors' committee or if that is not possible funnel questions to the officeholder through one or more members of the creditors' committee about remuneration at the earliest possible stage.

If that does not work then r.18.34(2) provides that a secured creditor, or an unsecured creditor with either the concurrence of 10% in value of the unsecured creditors (including that creditor) or the permission of the court may challenge the remuneration charged by the officeholder on the basis that it is in all the circumstances excessive or the basis fixed is inappropriate or the expenses incurred are in all the circumstances excessive.

Under r.18.34(3) the application to challenge must be made no later than eight weeks after receipt by the applicant of the progress report or final account which first reports the charging of remuneration or expenses. This rule is somewhat of a ticking time bomb for the unwary challenger. Also, it is a little unfair. It can often be the case that a progress report contains details of fees that look rather high but rather than make a fuss about it at that stage the creditor will grin and bear them in the hope that fees in the future will be more modest. The next progress report comes along and the fees are even higher, bordering on the grotesque. Strict application of the rules precludes re-opening of the earlier fees charged. This approach goes back to a 2004 case, *Re UIC Insurance Co Ltd (in provisional liquidation)* [2006] EWHC 2717 (Ch), where at first instance Registrar Nichols acceded to the application of the creditor to re-open the previous six years of remuneration claims. On appeal, without opposition, for reasons that will be explained in more detail below, the order to re-open earlier years was overturned on the basis that it would be unjust to do so when the provisional liquidators in that case had provided details of their remuneration to the informal creditors' committee and the challenging creditor, Equitas, without any real objection, for years.

At the time of the judgment in *re UIC* there was no rule which prohibited a challenge unless it was made within a set period of time. By the time of *Re Calibre Solicitors Ltd* [2014] BPIR 435 there was. In that case the applicant sought to challenge the remuneration and expenses detailed in the first administrators' report. During the progress of this application, a second progress report was issued and the applicant sought to challenge those fees and expenses in the same original application. Registrar Jones held that that could not be done, there had to be a separate application for each progress report and that the applicant was out of time for launching a challenge in relation to the fees and expenses contained in the second progress report. Fortunately, Registrar Jones went on to hold that the court had jurisdiction to extend time and did so in the circumstances of that case. Nevertheless, having to fall back on the exercise of judicial discretion is never an enviable place to be, particularly if you are the hapless solicitor or counsel who has misunderstood or miscalculated the time for challenge.

Interestingly, outside a solvent members' voluntary winding up where it is for the company in general meeting to determine the basis of remuneration, shareholders have no statutory say under IR 2016 r.18 on the determination of remuneration. This is surprising and can lead to problems where during an administration a company is rescued, all creditors are paid and the company is returned to shareholders. In such circumstances, creditors may not be terribly interested in how, or the manner in which, the officeholders are paid for the work. Alternatively, they may feel, perhaps with justification, that the officeholder deserves every penny claimed because they have been paid in full. On the other hand, as the creditors have been paid in full, it is not they who will suffer if, on an objective basis, the officeholders have been overpaid. It is the shareholders who will be prejudiced. Yet there is no obvious route of challenge under the IR 2016.

This is to be contrasted with the position of a bankrupt under r.18.35 who can challenge the remuneration and expenses of the trustee in bankruptcy with the court's permission. The court is not permitted to give permission unless the bankrupt can show that there is, or it is likely that there will be a surplus of assets to which the bankrupt would be entitled (or would be but for the remuneration and expenses in question). In addition to this outright prohibition on giving permission unless there is or is likely to be a surplus the court has a discretion under r.18.35(4) not to grant permission even if there is or is likely to be a surplus. In *re Singh (in Bankruptcy)* [2018] EWHC 3277 (Ch) Nugee J held that the discretion in r.18.35(4) was a broad one and that it was not appropriate to lay down any prescriptive test as to how the discretion should be exercised. Essentially, permission could be granted if it was appropriate to do so having regard to all the relevant circumstances which could include a consideration of whether once the fees and expenses are assessed there would be a surplus for the bankrupt. So, for example, if the surplus assets excluding fees and expenses are £100,000 and the fees and expenses being claimed are £200,000, the court would be entitled to

consider on a rough and ready basis the prospect of the fees and expenses being reduced to below £100,000 in determining whether to give permission for the assessment to proceed.

It may be seen, then, that a bankrupt will not easily obtain permission to challenge remuneration and expenses of a trustee in bankruptcy. Nevertheless, a bankrupt is in a better position under IR 2016 than shareholders who have no statutory means of challenge under r.18.

Other Routes of Challenge

Creditors

Where a creditor is either too late for a challenge to a particular period of remuneration or where excessive remuneration is merely one of a number of complaints, one possibility is for a creditor to seek the removal of an officeholder. There are different provisions of the IA 86 and IR 2016 that apply depending upon the type of officeholder. The provisions that apply to a trustee in bankruptcy are s.298 and rr.10.78-10.80; to a liquidator in a compulsory liquidation, s.172 and rr.7.63-7.65; to a liquidator in a creditors' voluntary liquidation, s.171 and rr.6.26 and 6.27 and to an administrator, paragraph 88, Sched B1 and r.3.65. Excessive remuneration alone would not be a ground for removal. It would be necessary to combine this complaint with others. In recent times we are all aware of the courts being sympathetic to removal applications where it perceives there is a conflict of interest. Excessive remuneration, perhaps approved by a secured creditor who will be paid in full, may constitute a ground for removal and replacement with an officeholder with modest ambitions for his/her remuneration.

Another avenue in an administration but one which has not to date been properly tested and one which does not appeal much to me is to apply for an order under paragraph 74, Sched B1 to the effect that the creditor has been unfairly harmed by the acts of the administrator. It will be recalled that the paradigm paragraph 74 case is where the administrator has treated the applicant less favourably than creditors as a whole in circumstances where the unfair treatment cannot be justified by reference to the interests of creditors as a whole or the interests of the administration. In my view, the charging by the administrator of excessive remuneration does not readily fit within paragraph 74. That has not, however, prevented attempts to do so.

In *Re BW Estates Ltd* [2015] EWHC 517 (Ch), the applicants were in dispute with the majority shareholder of a property company and had obtained a £2 million judgment against him and obtained a charging order over the shares in the company which were vested in the name of the

majority shareholder's son. The son was also a director of the company. The director put the company into administration notwithstanding the fact that a secured creditor had already appointed LPA receivers over all of the company's properties and that the company was balance sheet solvent. The company was temporarily cash flow insolvent because the bank had frozen the company's bank account after the applicants had obtained a freezing order against the beneficial owner of the majority of the shares in the company, which freezing order had also extended to the company's assets. The applicants acquired by assignment a small debt owed by the company to its former solicitors. In that capacity the applicants challenged the administrators' remuneration under the predecessor to r.18, r.2.109 Insolvency Rules 1986 (IR 86) and at the same time issued an application under paragraph 74 Sched B1. The nub of the argument was that that administrators should have bought the administration to an end immediately after their appointment because the business was a property company, it was already subject to an LPA receivership and they should have realised that the company did not need administration as well. However, the administrators remained in office to carry out an investigation into the validity of a debt purportedly owed to an off-shore company owned by the majority shareholder. The administration did eventually come to an end and the company was rescued by being placed under the control of the applicants who by then had enforced their charge over the shares. The argument of the applicants was that by the time they were able to take control the company was in exactly the same position that it had been in prior to the administration save that it was now saddled with the costs of the administration. It was contended that the remuneration of the administrators should be disallowed entirely or reduced significantly. HHJ David Cooke rejected the paragraph 74 application on the basis that the applicants could not demonstrate how they had been unfairly harmed. However, the judge did not in terms say there could never be a paragraph 74 application which had as its objective a challenge to an administrator's remuneration. The judge also held that an administrator's remuneration would not, necessarily, be disallowed even if, with hindsight the administration served no purpose. The question of whether the remuneration should be reduced at all was adjourned to another day, although the applicants having failed thus far were ordered to pay the administrators' costs to date.

A more fertile route of challenge is in a claim for misfeasance. The applicable provision to a trustee in bankruptcy is s.304 IA 86; liquidators, s.212 and administrators, paragraph 75 Sched B1. Officeholders are fiduciaries and therefore can be found liable for breaches of fiduciary duty and also for breach of their common law duty of care. Charging excessive remuneration could constitute a breach of fiduciary duty even if it has been approved by the majority particularly where the applicant can show that the officeholder has not been fully transparent in what is being charged for. Again, it would be prudent when launching a misfeasance claim complaining of excessive remuneration to combine it with other complaints. Not to do so is likely to attract the obvious response that the proper forum for a remuneration challenge is r.18.

Interestingly, misfeasance claims where charges of excessive remuneration have been made have not been made by individual creditors but more often by liquidators against former administrators. This makes sense because the proceeds of a misfeasance claim will be received for the benefit of all creditors and not the applicant alone. Another consideration is that even if a creditor is successful and costs awarded in his favour he will rarely receive a complete indemnity for his costs so that there will be an appreciable risk that a successful creditor applicant will find himself out of pocket. By contrast the successful officeholder can look to the assets of the company for both his own fees in dealing with the application and any shortfall in his costs.

Ian Richards, Kevin John Hellard (in their capacity as joint liquidators of FW Mason & Sons Limited) (in creditors' voluntary liquidation) v Christopher Michael White and Andrew Philip Wood [2017] EWHC 1512 (Ch) is a case where liquidators issued a misfeasance claim against former administrators and liquidators who, it was alleged, dishonestly took remuneration to which they were not properly entitled. The case settled before it came to trial. But it is an example, albeit an extreme one, of a challenge to an officeholders' remuneration by other officeholders under paragraph 75.

Re MK Airlines Ltd (in Liquidation) [2018] EWHC 540 (Ch) is another example of a misfeasance claim against a former administrator by a liquidator. There had, in this case, been 3 administrators and the administrator in question was the last man standing in that the other two had been made bankrupt. The firm to which the three administrators were attached had also folded and the former administrator was not even a member of the firm, he was a consultant. At first instance this former administrator was ordered to repay all the remuneration received by him and his co-administrators on the basis that the monies had been paid out to them in breach of the rules on priority of payments in an administration. On appeal the judgment was overturned. The Deputy Judge, Sarah Worthington QC, held that the source of the remuneration had not been company funds but in fact funds provided by an investor which were never at the company's free disposal but were to be used solely for the administrators' remuneration.

Shareholders

As explained above, r.18 contains no provisions entitling shareholders to challenge remuneration.

If a company goes into administration and there has been a rescue but shareholders have not been consulted at all about the level of remuneration, one possibility is that once the company has been returned to its directors either the company could bring a claim against the former joint administrators or, if the directors refuse to do so because they have worked closely with the joint

administrators to achieve the rescue, minority shareholders could do so, if the court grants permission, using the provisions for bringing a derivative action. What would be the cause of action in such circumstances? Drawing remuneration without authority is unlikely to bear fruit given the provisions of r.18 which provide for administrators' remuneration to be approved by creditors. If creditors approved the remuneration an argument that the administrators drew remuneration without authority will not succeed.

An alternative route might be to claim that the administrators breached their fiduciary duty to the company in drawing excessive remuneration. The argument would be based on the reverse side of the principle that when a company is insolvent or arguably insolvent fiduciaries (ordinarily the directors) must take into account the interests of creditors. Here it could be argued that where, notwithstanding an administration, the company turns out to be solvent, administrators owe a fiduciary duty to consider the interests of shareholders (as well as the interests of creditors) which would include a duty to consider whether the remuneration drawn is excessive in all the circumstances of the case.

Where a company is in administration members of a company could apply for an order under paragraph 74, Sched B1 of the IA 86 on the grounds that the administrator, when obtaining the approval of excessive remuneration or expenses, acted so as unfairly to harm the interests of the applicant shareholders. An example of such possible unfairness in the context of remuneration might be in a rescue situation where an administrator has obtained the approval of excessive remuneration or expenses from the majority of shareholders in the knowledge that it would be approved provided that the rescue of the company was conducted in the way that the majority of shareholders wanted rather than in the way being promoted by the applicant. Such a situation could arise if the effect of the rescue was to favour certain interests of the majority shareholders over those of the applicant.

The difficulty, though, with a paragraph 74 application by a shareholder is what will it achieve? Invariably such a paragraph 74 application in a rescue case will only be made shortly before the end of the administration because administrations in rescue cases never last very long. In *Coniston Hotel (Kent) LLP* [2015] BCC 1 Norris J did not see why a paragraph 74 application could not be issued after an administration had ceased (although in that case the order discharging the joint administrators contained an express reservation for a paragraph 74 application made during the usual 28 day period after which the discharge took effect). However, Norris J also pointed out in an obiter passage that if the unfair harm could not be undone by regulating the conduct of the administration differently because the administration had ceased, the only relief that could be given would be a compensating payment to the applicant alone and that such relief would be exceptional. If the applicant was a shareholder, in the unlikely event that the shareholder was able to make out

that it had suffered unfair harm by the administrators drawing excessive remuneration, any payment to the shareholder would be likely to be miniscule because, fairly, it would be nothing more than a sum representing that part of the excess referable to the shareholder's shareholding.

In *re Hotel Company 42 The Calls Ltd* [2014] BCC 136 a company went into administration but its debts were then discharged by third parties which resulted very quickly in a rescue of the company without the remuneration of the administrators being approved. The joint administrators applied for an order authorising them to grant themselves a charge over the company's assets to secure their remuneration. The company's director and a shareholder opposed the application contending that there had been unfair harm and misfeasance by, amongst other things, the charging of excessive remuneration and that the administrators should not be permitted any remuneration at all. HHJ Purle dismissed the administrators' application on the basis that they were fully secured by the charge under paragraph 99, Sched B1 which the court would enforce against the assets of the company irrespective of any attempts by the company/directors to avoid payment, It will be recalled that paragraph 99 creates a charge over the assets of the company to secure a former administrator's remuneration and expenses where he ceases to hold office. The judge went on to observe, obiter, that although there was no express power for the court to determine remuneration on the application of a shareholder there was an inherent power in the court, in an appropriate case to order the administrators' remuneration to be assessed on the application of a shareholder. If there were no power there would, he thought, be an unacceptable lacuna in the legislation. The shareholder had, in fact, issued an application challenging the administrators' remuneration and their conduct generally under paragraphs 74 and 75 but that application was not before the judge. However, it is clear from the judgment that HHJ Purle also assumed that, in principle, remuneration could be challenged under paragraph 74 or 75.

Successful Challenges – what to do and what not to do

Challenging remuneration is hard work. The information that is given by an officeholder in his reports in order to obtain approval of his remuneration is normally insufficient to mount any decent challenge. However, the report should be the first port of call to determine whether there is something to complain about. If the amount claimed looks unreasonably large for what has been done then the officeholder should be asked to produce his records which support the amount he is claiming. In any challenge to an officeholder's remuneration he will have to produce those records. It therefore makes sense to ask for the records prior to issuing any application and the officeholder should not refuse to provide them.

If those records reveal discrepancies in charging or gaps in narratives there is a prima facie case for a challenge. However, unless the discrepancies or gaps are substantial, serious consideration should be given to whether to mount a challenge because, as already stated, they are expensive and with officeholders of any standing rarely result in a reduction that is large enough to justify the expense, time and trouble of mounting a challenge. The types of things to look for are:

- Inadequate records
- Excessive time charged for a task that should have taken a much shorter time
- Excessive time charged for letters-out and letters-in where the records show that the letters were short and should have taken less time to deal with them
- Excessive time spent in meetings of fee earners to discuss issues that should have been discussed in less time and with fewer fee earners
- The use of high level fee earners for work that could have been done by a lower level fee earner
- Excessive time spent on reviewing the work of others
- Over-management of the appointment
- Failure to delegate
- Charge out rates being above the norm for the type of appointment, the experience of the fee earner and size of firm
- No narrative or documentary support for time charged
- Charging an uplift when using outside contractors.

An early case where a successful challenge was mounted was *re UIC Insurance* (supra). This insurance company had been in provisional liquidation since 1996 (at a time when the administration regime did not apply to insurance companies). Typically, the way in which an insurance company would exit provisional liquidation would be by a scheme of arrangement. Equitas (the Lloyd's re-insurer) became fed up with what they saw as the deliberate delay by the provisional liquidators in proposing a scheme because the company had significant assets and each year the provisional liquidators had been able to draw a substantial amount of remuneration which had been approved by the informal creditors committee. After 6 or 7 years of being in provisional liquidation Equitas challenged the remuneration. At a preliminary hearing the Registrar appointed an assessor. At trial, having received a critical report from the assessor, the Registrar reduced the remuneration claimed by £235,882, approximately 25%. The facts took place at a time when IPs were much less assiduous in keeping proper time records even though the recording systems existed. The Registrar made substantial reductions where there were no records at all and a 1% reduction for over-management. There were also reductions for using staff of too high a grade and the use of 15 minute segments for charging rather than 6 minute segments. The most scathing criticism was reserved for the practice that had been adopted by the provisional liquidators in respect of work done by an independent

contractor who was employed by the firm at one rate and then substantially marked up by the firm when the independent contractor's services were provided to the insurance company at an additional cost of £38,000. The Registrar ordered the provisional liquidators to pay the costs of the remuneration application themselves and directed that earlier years' remuneration claims should be re-opened. The provisional liquidators appealed. However, by the time of the appeal was heard a scheme had been promoted by the provisional liquidators whereby all creditors were to receive 145p in the £. Not surprisingly, Equitas was no longer interested and did not oppose the appeal. They had got what they wanted which was to be paid. On appeal, the Judge overturned the costs award in recognition of the success of the provisional liquidation and overturned the order re-opening the earlier years on the grounds of unfairness, but the reductions made to the remuneration that was challenged, remained.

A far more recent case is *re Nortel Networks France SAS* [2019] EWHC 2778 (Ch). In that case all creditors had been paid in full and the administrators/also supervisors of a CVA applied to court for the assessment of their remuneration. No creditor appeared to oppose but there was no fulsome support either because, as stated by the creditors' committee, they did not feel equipped to do so. Snowden J appointed an assessor. When the matter returned to court the assessor was generally supportive of the administrators' claim for remuneration but suggested that the charge out rates as supervisors of the CVA did not merit being charged 15% above those agreed in the administration. The assessor also criticised the administrators' failure to engage with creditors and the creditors' committee over the issue with remuneration at a much earlier stage in the proceedings and their failure to provide complete and accurate information. It was suggested that it was this failure to engage which resulted in creditors not having a view one way or another whether the remuneration was fair. The judge reduced the officeholders' remuneration by the amount recommended by the assessor (about £34,000) and, although there was no certainty that it would have made any difference if there had been more engagement with creditors, the court ordered the officeholders to pay just under 50% of the cost of the application to approve their remuneration.

In *re Brilliant Independent Media Specialists Ltd (in Liq)* [2015] BCC 113 is another interesting case. On the date the company entered administration the business was sold to a third-party purchaser by pre-pack. The creditors committee approved proposals that the company move from administration into liquidation within 6 months. The administrators decided to seek directions on the validity of a secured debt which took them beyond the 6 months. The administrators proposed revised proposals to extend the administration which were rejected and the company eventually went into liquidation over 2 months after the end of the six month period. The administrators applied to court for the approval of their remuneration at £389,340. The creditors' committee argued that the administrators should receive remuneration only for the work that they did in the first two months

in office and not for the entire period; alternatively it was argued that the administrators should not be entitled to remuneration for the period after the 6 month period had ended or for work which fell outside the proposals. It was also argued that the administrators should not receive remuneration for services provided to the liquidators, at their request. The court held that there was no bar on the administrators being paid for periods that they remained in office after the date provided in the proposals. However, the court had to take into account whether the work carried out in this period was for the purposes of the objective of the administration or otherwise formed part of the administrators' duties and responsibilities. The court also held that the administrators could be remunerated for services provided to the liquidators. Nevertheless, the judge reduced the remuneration to £233,147 and, also and perhaps most significantly, refused the administrators' costs of the application to fix the remuneration, which were £90,000, down to £7,500. On the face of it this looks like a stunning victory for the opposing creditors' committee. However, as far as can be seen from the judgment, the judge made no provision for the costs of those appearing to oppose the administrators' claim for remuneration.

Having considered the above cases what are the points to bear in mind when considering whether to challenge an officeholder's remuneration:

- Don't do nothing for months or years and then launch a complaint. Creditors (and shareholders) should engage from the outset. (In *UIC* I hazard a guess that remuneration would have been controlled much earlier and a scheme promoted much earlier if Equitas had taken action earlier).
- Don't challenge unless there are serious concerns. Small gripes will get you nowhere
- Don't expect to recover all the costs of a challenge.
- Don't take on the burden of a challenge oneself, if you can avoid it. Try to get the support of other creditors.
- Don't challenge unless success will make a significant difference to the outcome for creditors.
- Don't expect the challenge proceedings will be over quickly. They normally take months, if not years, to come to trial.
- Don't expect the ICC Judge to be on your side. Where unprofessional or slippery conduct is detected, ICC Judges tend to be hypercritical but in the absence of such conduct the officeholder is frequently given the benefit of the doubt.

This commentary was originally published in January for our Insolvency Breakfast Briefing held in chambers. If you would like to be added to our mailing list to receive invitations to future insolvency events, please email events@wilberforce.co.uk

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