CHALLENGING OFFICE-HOLDER DECISIONS AFTER BAGLAN OPERATIONS LIMITED [2022] EWHC 647 (CH)

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Introduction

1 The purpose of this article is to consider two key issues that arise in connection with applications brought to challenge the decisions of office-holders in the course of their conduct of an insolvency. There have been recent decisions on this topic under s.168(5) of the Insolvency Act 1986 ("IA 86"), but the issues go wider than just liquidation and apply to administrators, trustees in bankruptcy and others. I propose to deal with them as follows:

- First, identifying which applicants a court will accept as having standing to challenge an office-holder's decision;
- Second, considering how the Court approaches such a challenge. What test does it apply to decide whether to modify the decision in question?

s.168(5)

2 Section 168(5) of IA 86 provides as follows:

"If any person is aggrieved by an act or decision of the liquidator, that person may apply to the court; and the court may confirm, reverse or modify the act or decision complained of, and make such order in the case as it thinks just".

Standing

3 In Mahomed v Morris [2001] BCC 233 Peter Gibson LJ noted at [24] that while the words "person aggrieved" in s.168(5) "are very wide at first sight and are not on their face limited to creditors and contributories", there was (at that time) only one reported decision in which a person not being a creditor or contributory had been allowed to apply under the section. Further, in Re Edennote Ltd [1996] BCC 718 at 721 Nourse LJ suggested that "an outsider" to the liquidation would not normally have standing to apply.

4 The one reported decision he referred to was Re Hans Place Ltd [1992] BCC 737 in which a landlord was permitted to challenge a decision by a liquidator to disclaim a lease despite not being a creditor.

5 In Brakes v Lowes [2020] EWCA Civ 1491; [2021] Bus LR 577 Asplin LJ explained the reasoning in Hans Place and Mahomed at [82] on the basis that:

"The ability to disclaim onerous property under section 178 of the Insolvency Act 1986 is specific to a liquidator and arises in the liquidation. It is not surprising, therefore, that the decision to disclaim should be challenged in the liquidation itself. As Peter Gibson LJ put it in the Mahomed case [2000] 2 BCLC 536, the landlord was directly affected by the exercise of a power granted to the liquidator which he would not have been able to challenge otherwise.".

6 Even creditors will not constitute 'persons aggrieved' if their challenge is not in the interests of the class of creditors as a whole:

a. In Walker Morris v Khalastchi [2001] 1 BCLC, a law firm which was a creditor of the insolvent company in the sum of £237 was seeking to prevent the liquidator from handing over documents relating to the company's tax affairs to the Inland Revenue so as to protect its other clients from possible proceedings by the company. The firm was held not to have standing because it was seeking to advance the interests of possible debtors rather than creditors.

b. In Re Edengate Homes (Butley Hall) Ltd [2022] EWCA Civ 626 the Court of Appeal held that a creditor who sought to challenge the assignment to a litigation funder of possible claims which the insolvent company had against her and her family was seeking to advance her personal interests rather than that of the creditors generally, and accordingly did not have standing.

7 It thus appears that there are three elements to the question of whether an applicant has standing:

a. First, they must be directly affected by the proposed exercise of the power. This is a necessary, but not sufficient, ingredient; the courts are astute to protect liquidators from collateral attacks from an infinite array of third parties. The impact on the applicant does not have to be purely financial (Brake at [84]).

b. Secondly, the power that the applicant challenges must be a power given to the liquidator as part of the liquidation.

c. Finally, the challenge must be consistent with furthering the interests of the liquidation as a whole.

8 In the recent case of Baglan Operations Limited [2022] EWHC 647 (Ch) customers of an insolvent power company who were not creditors challenged the decision of the Official Receiver (as liquidator) not to continue supplying power due to the extent of his vires under IA 86. In his judgment at [40] Norris J recognised that the applicants came "within the narrow class of persons directly affected by the exercise of a power given to the Official Receiver who would not otherwise have the right to challenge their exercise".

The Correct Test

9 It is easy to find commentators that describe the test for a challenge under s.168(5) IA86 as akin to perversity. That is usually based on a statement in In Re Edennote Ltd [1996] BCC 718 at 722, as follows:

> "[…] (fraud and bad faith apart) the court would only interfere with the act of a liquidator if he has done something so utterly unreasonable and absurd that no reasonable man would have done it."

10 However that test applies to what may be called "commercial" decisions by office-holders, but it is not a complete statement of the position. Indeed the wording of s.168(5) allows the court a wide discretion to modify a decision of an officeholder and "make such order in the case as it thinks just".

11 It is thus not surprising that issues of fairness between affected persons can also prompt the court to modify a decision. In Hellard v Michael [2010] BPIR 418 at [8]-[9] Sales J noted (in a case dealing with the near equivalent power in s.303(1) IA 86 in relation to bankruptcy proceedings):[1]

> "In my view, however, the test in In re Edennote Ltd does not exhaustively state the grounds for intervention by the court. As is clear from the provisions of the Insolvency Act 1986, the court retains a general supervisory jurisdiction in respect of trustees in bankruptcy to ensure they behave properly and fairly as between persons affected by their decisions"

12 The touchstone for identifying when a court should apply the test in In re Edennote Ltd and when it should apply a different test is the nature of the decision under challenge. As noted above, a "commercial" decision will attract a high threshold for challenge. But where a decision is not simply a commercial one, different considerations will apply.

13 Thus in Re Buckingham International plc [1998] BCC 943 the Court of Appeal considered a challenge under s.168(5) IA86 to a liquidator's decision to apply to a US court under the US Bankruptcy Code to restrain steps by certain creditors of the company in liquidation that sought to gain precedence over other creditors in the liquidation by using "garnishment" proceedings in the USA.

14 At first instance Harman J had accepted the liquidators' submission that they were seeking to give effect to an overriding principle of pari passu distribution of assets among creditors of the same class. He rejected the challenge to the liquidators' decision, relying on Re Edennote Ltd [1996] BCC 718 at 722 in describing his jurisdiction under s.168(5) IA86.[2]

15 The Court of Appeal considered this reliance to be misplaced, as the nature of the decision complained of was not a "commercial one". Instead it concerned whether competing creditors could jump the queue in priority to general unsecured creditors. That was "eminently a matter for the Companies Court" and not one for the liquidator's discretion in the way realising assets requires the liquidator's discretion. In essence, it concerned how properly to enforce the statutory scheme for insolvencies under IA86.

16 In Baglan, the decision complained of was a decision by the liquidator that he had no vires under IA 86 to continue trading the business of the company in liquidation. The Court agreed this was a matter of law, under Schedule 4 to IA86, and not one for the Edennote test.

17 The question then becomes where to draw the line between (i) a decision that is one for liquidators in their discretion, applying commercial judgment, and (ii) a decision where the underlying dispute is one of law or where the liquidator may be said to be (wrongly) implementing the statutory scheme? If the latter, the applicant should get away from the high bar of a perversity test. Those acting for and against office-holders will need to think carefully about the nature of the decision that may be challenged.

1 Which provides that the court may give directions or make such other order as it thinks "fit", rather than "just" as in s.168(5).

2 At 953.

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