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From Dust to Dissolution:

Fraudulent Trading, Restoration and Carbon Credits in *Tradition Financial Services Ltd v Bilta (UK) Ltd* [2023] EWCA Civ 112

Zachary Kell

26th September 2023

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INTRODUCTION: A BRIEF HISTORY

- Fraudulent Conveyances Act 1571 (Statute of 13 Elizabeth)
- *Twyne's Case* (1601) 3 Coke 80
- Section 75 of the Companies Act 1928
- Companies Acts 1929, 1947, 1948, 1981, 1985
- Insolvency Act 1985, Sch. 6
- Section 213 of the Insolvency Act 1986

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INTRODUCTION: TODAY'S TALK

- A refresher on section 213 of the Insolvency Act 1986
- The judgment at first instance (Marcus Smith J.): [2022] EWHC 723 (Ch), [2022] B.C.C. 833
- The Court of Appeal's judgment (Lewison L.J.): [2023] EWCA Civ 112, [2023] 2 W.L.R. 1160

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SECTION 213, INSOLVENCY ACT 1986

213.— Fraudulent trading.

(1) If in the course of the winding up of a company it appears that any business of the company has been carried on with intent to defraud creditors of the company or creditors of any other person, or for any fraudulent purpose, the following has effect.

(2) The court, on the application of the liquidator may declare that any persons who were knowingly parties to the carrying on of the business in the manner above-mentioned are to be liable to make such contributions (if any) to the company's assets as the court thinks proper.

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SECTION 213, INSOLVENCY ACT 1986

"Section 213 may well be the ultimate statutory encapsulation of the legal maxim that "fraud unravels all". In the litigation that has followed the financial crisis of 2008, it has become an increasingly popular weapon in the armoury of corporate liquidators. A third party can be liable for being "knowingly part[y] to carrying on of the business" even though it played no managerial role in the business in question. The requirement that "any business of the company has been carried on with intent to defraud" can be satisfied by a single transaction (and the third party can be "party to [that] carrying on" by being the counterparty to that single transaction.) […]"

Foxton Q.C.
"Accessory Liability and Section 213 Insolvency Act 1986"
[2018] J.B.L. 324

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SECTION 213, INSOLVENCY ACT 1986

- Report of the Review Committee on Insolvency Law and Practice (1982) Cmnd 8558 ("the **Cork Report**")
- Issues of pleading and proving "fraud": *Re Patrick and Lyon Ltd* [1933] Ch. 786 (Maugham J.)
- Sections 213 vs. 214 ("Wrongful Trading")

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[2022] EWHC 723 (Ch) (Marcus Smith J.)

- Missing trader intra-community fraud (or "**MTIC Fraud**")
- EU Emissions Trading Scheme ("**EUA's**")
- *Re Gerald Cooper Chemicals Ltd* [1978] Ch 262 (Templeman J.)
- *Bilta (UK) Ltd (In Liquidation) v Natwest Markets Plc* [2020] EWHC 546 (Ch) (Snowden J.)
- *Banque Arab Internationale d'Investissement v. Morris* [2002] B.C.C. 407 (Neuberger J.)
- *Morris v Bank of India* [2005] EWCA Civ 693

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[2023] EWCA Civ 112 (Lewison L.J.)

"[…] Although it might be anomalous for criminal liability to be wider than civil liability, it is not necessarily anomalous for civil liability to be wider than criminal liability, particularly where the statutory provisions are now contained in different sections and different Acts of Parliament. Moreover, as noted, the criminal offence may be committed even if the company is not in the course of winding up. Quite apart from that, a person with no managerial controlling role within a company can be convicted of aiding and abetting fraudulent trading. […]"

Lewison L.J at [108]

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[2023] EWCA Civ 112 (Lewison L.J.)

"A person cannot be made amenable under the section unless he has actively participated in the management of the company. To impose liability on a shareholder it must be shown that he took part in making management decisions which were intended to defraud creditors. A third party who knowingly participates in an act of fraudulent trading committed by a company's directors (for example, a creditor of the company who accepts payment of his debt out of money which he knows its directors have obtained by fraud) may be compelled personally to restore the money so applied by means of an order under the section: In re Cooper Chemicals Ltd [1978] Ch 262."

Lewison L.J at [112]

Quoting O'Flaherty J. in *O'Keeffe v Ferris* [1997] 3 IR 463

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[2023] EWCA Civ 112 (Lewison L.J.)

"I should make it clear, however, that nothing I say must be taken as setting the outer limits of the scope of section 213 . All that we are asked to decide is whether a person cannot fall within the scope of section 213 unless he has a controlling or managerial function within the company. Whether an "outsider" can be said to be party to the carrying on by a company of a fraudulent business may well be a question of fact and degree which requires careful analysis. That question does not arise in this case, because of the settlement agreement."

Lewison L.J at [118]

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CONCLUSIONS

- Section 213 requires pleading and proving fraud. Litigators must consider their ethical obligations in this case (clear instructions and reasonably credible material to justify the allegation).
- Section 213 has as wide a scope as possible for the fraudulent acts capable of being caught.
- The Court of Appeal judgment confirms the potential defendants under s.213 is open to any third parties who have participated in the fraud. The question of their participation will be one of fact and degree.
- In order to craft a strong s.213 case, liquidators should use all of the tools available to obtain information and evidence, such as s.236 of the Insolvency Act 1986.

Thank you!

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Annulling a bankruptcy order

Lauren Kreamer

26 September 2023

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The process

Common pitfalls and how to avoid them

Costs and *Re Kooter*

The process

Section 282(1), Insolvency Act 1986

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A bankruptcy order may be annulled if it appears to the court that:

s.282(1)(a) – it ought not to have been made (on any grounds existing at the time); or

s.282(1)(b) – the debts and expenses of the bankruptcy have all been paid or secured for to the extent required by the rules since the making of the order.

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Rule 10.132-10.141, The Insolvency (England and Wales) Rules 2016

- An application under s.282(1) must specify whether it is made under subsection (1)(a) or (1)(b)
- It must be supported by a witness statement stating the grounds on which it is made
- Slightly different notice requirements – under (a), notice to the OR, the trustee, and the petitioner; under (b), notice to the OR and trustee
- Where the applicant is not the bankrupt, you must deliver all notices and documents to the bankrupt

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- Rule 10.138 contains matters to be proved in a subsection (1)(b) application
  - Some 'musts' and some 'mays'
- All bankruptcy debts which have been proved must have been paid in full or secured in full
- If a debt is disputed, the bankrupt must have given security (money paid into court or a bond) as the court considers adequate to satisfy any sum that may subsequently be proved to be due to the creditor concerned
- The court may direct advertisement of an alleged debt in the case of an untraced creditor, plus security (which will be released twelve months later by order of the court on application)
- The court may take into account whether sums have been paid/secured in respect of post-commencement interest on the debts which have been proved

- In a subsection (1)(b) application, not less than 21 days before the hearing (per r.10.133(2)), the trustee must file with the court a report relating to various matters (circumstances of the bankruptcy, a summary of the bankrupt's assets and liabilities, details of creditors who are known but haven't proved and any other matters the court needs to know about)
- Plus, where the trustee is not the OR, a statement of the trustee's remuneration, the basis for it under r.18.16 and the trustee's expenses
- The report must also include particulars of the extent to which the debts and expenses of the bankruptcy have been paid or secured
- Together with whether the trustee considers the security given to be satisfactory
- The OR may file its own report if it is not the trustee

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- The bankrupt can apply for an order in relation to the trustee's remuneration at the same time as the annulment where they say that the remuneration charged, or expenses incurred, are excessive (r.10.134(1))

- Subsection (4):

> *"If the court annuls the bankruptcy order under section 282(1)(b) and considers the application to be well-founded, it must also make one or more of the following orders –*
>
> *(a) an order reducing the amount of remuneration…;*
> *(b) an order that some or all of the remuneration or expenses in question be treated as not being bankruptcy expenses;*
> *(c) an order that the trustee…pay to the applicant the amount of the excess of remuneration or expenses or such part of the excess as the court may specify; and*
> *(d) any other order that the court thinks just."*

- The trustee must attend the hearing unless the court directs otherwise (r.10.137(1))
- The OR may attend, but does not have to do so unless they have filed a report under r.10.133
- No rules about the applicant's attendance, but it is their application!

Who can apply?

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- The bankrupt, usually!
- But also anyone affected by a bankruptcy order who can satisfy the court that they have a legitimate interest in applying for the annulment of another person's bankruptcy order (*F v F* [1994] 1 FLR 359)
  - Like a divorcing spouse
  - Creditors (either where they think the bankrupt has sufficient assets to pay their debts or, more commonly, where there are COMI issues)
- Burden is on the applicant
- Unless the bankruptcy order was made on the debtor's application, and they have assets in excess of their liabilities and have been dishonest in obtaining the order

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When to apply?

- No time limit
- But applications must be made promptly (*Taylor v The Macdonald Partnership* [2015] EWCA Civ 921
- Can be made after discharge from bankruptcy (per s.282(3), IA 1986)

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Process

- Typically, the first hearing is fifteen minutes
- Directions are given for the filing of evidence, unless the application is undisputed and uncontroversial
- Orders may be made for service of documents if they have not already been served (or only short notice has been given - must typically be 28 days)

When will the court annul?

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- Where the debt could have been disputed by the bankrupt
- Where set-off was available
- Where the court did not have jurisdiction (often for COMI reasons)
- Where there was procedural irregularity

- The jurisdiction is discretionary and wide
- It can include a review of the validity of the debt on which the creditor founded the bankruptcy petition (*Khan v Singh-Sall* [2022] EWHC 1913 (Ch))
- Even where one of the grounds exists, the court can still decline to annul the bankruptcy order

Section 282(1)(a) – the test

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- *JSC Bank of Moscow v Kekhman* [2015] EWHC 396 (Ch)
- Three-stage test:
  - What grounds existed at the time the bankruptcy order was made;
  - Whether, on those grounds, the bankruptcy order ought not to have been made; and
  - Whether the court should exercise its discretion to annul if the bankruptcy order ought not to have been made

Disputed debt

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- Where the debt is disputed, the bankrupt must show substantial grounds for disputing the debt – the test is the same as for setting aside a statutory demand
- You do not have to prove that the debt is not owed at all (*Woolsey v Payne* [2015] EWHC 968 (Ch))
- The test is whether there was a genuine triable issue over the existence of the debt and not showing that, on a balance of probabilities, the debt was not due at all (*Dusortuth v Orca Finance UK Ltd* [2022] EWHC 2346 (Ch))

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Where an IVA has been agreed

- Section 261(2)
- No discretion to refuse
- Annulment cannot be ordered while there is any possibility of the IVA being challenged
- Procedure contained in rule 8.32-8.37, IR 2016

- Look at r.10.137(4) and (5) for the contents of the order
  - Identification details for the proceedings
  - Name and address of the applicant
  - Date of the bankruptcy order
  - Date of the petition or making of the bankruptcy application
  - Date and reference number of registration as a pending action with the Chief Land Registrar
  - Date and reference number on register of writs and orders affecting land with the Chief Land Registrar
  - A statement that it appears to the court that the bankruptcy order ought not to have been made, or the bankruptcy debts and expenses have been paid or secured to the satisfaction of the court, and that the bankruptcy order ought to be annulled under s.282(2)
  - An order annulled the order, dismissing the petition, vacating the Chief Land Registrar registrations
  - The date of the order
  - Plus, a notice to the bankrupt that they must deliver notice of a requirement for the annulment order to be gazetted to the OR and that it is their responsibility to deal with the cancellation of the registration of the petition and bankruptcy order with the Chief Land Registrar

- Notice must be given to creditors where an annulment is ordered (r.10.139(1))
- Expenses incurred by the OR in delivering such notice are a charge in the OR's favour on the property of the former bankrupt
  - Usually these will be agreed and paid in advance
- And the trustee must deliver a final report to the SoS *"as soon as practicable"* after the annulment order (r.10.141(2)) and file it with the court
- The trustee will be released from such time as the court may determine, having regard to whether final accounts have been delivered and any security given has been or will be released

Section 375, IA 1986

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- Section 375 contains a power to review, rescind or vary orders made in bankruptcy matters
- You can apply under both sections 282 and 375
- The principles are similar, the only significant difference being that in a s.375 application, the court can take into account things that have happened since the bankruptcy order was made, whereas under s.282, it can only consider the circumstances that existed at the time of the making of the order (see, e.g., *Haworth v Cartmel* [2011] EWHC 36 (Ch))

Common pitfalls for applicants and how to avoid them

- Applying too early (i.e., before the position with the debts and expenses is known in full or the time to challenge an IVA has expired)
  - Ensure the evidence is full and detailed in this regard, and that you have checked the rules in relation to s.282(1)(b) applications and payment/security for debts
  - Make sure the IVA is beyond the point of challenge

- Trying to rehash arguments already made at earlier hearings
  - Manage clients' expectations about their ability to have an order annulled

- Not having sorted out the costs position prior to the hearing
  - Make sure that the OR's and the trustee's fees are ascertained and paid in advance (in a subsection (1)(b) application)
  - In a subsection (1)(a) application, similarly, have some idea of costs in advance and know that they will be provided for in the order

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- Making a second application where the first was dismissed
  - *Lambert v Forest of Dean* [2019] EWHC 1763 (Ch)
  - First annulment application had been struck out due to a failure to comply with a costs order
  - Second application was made, with the court stating that the proper way of seeking to reinstate an application that had been struck out was by applying for relief from sanction (or, presumably, appealing)
  - The second application was an abuse of process
  - Particularly where the costs order still hadn't been complied with
  - Plus the application was dismissed on its merits

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And not reading the rules!

Costs and *Re Kooter*

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- Four categories of costs:
  - The petitioning creditor’s costs
  - The OR’s costs
  - The trustee’s costs
  - The costs of the annulment application itself

Trustee's costs

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- *Oraki v Dean* [2013] EWCA Civ 1629 – the innocence of the bankrupt does not preclude liability for the trustee's costs
- The court has an unfettered discretion in relation to the trustee's costs
- The court must examine the matter not only from the perspective of the bankrupt but also that of the trustee
- A trustee who has acted properly can ordinarily expect to have their reasonable remuneration provided for
- Ordinarily this will be dealt with by way of payment out of the estate, if necessary, or by some other mechanism of payment proposed by the bankrupt

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Kooter v OR & Radeva (Re Radeva) **[2023] EWHC 594 (Ch)**

- A bankruptcy order was made on the application of the bankrupt, Ms Radeva
- That order was annulled on the basis of COMI following an application by the majority creditor (99.5%), Mr Kooter
- Ms Radeva had forged documents and lied about her habitual residence being in England and Wales
- The question was who should pay the trustees' costs following that annulment, in circumstances of a jurisdictional challenge and where the bankrupt was unlikely to be able to meet any costs order made against her

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Kooter v OR & Radeva (Re Radeva) **[2023] EWHC 594 (Ch)**

- There was no difficulty in the judge's mind in making an indemnity costs order against Ms Radeva, including liability to pay the trustees' costs, remuneration and expenses
- There was no authority directly on point, but she reviewed *Butterworth v Soutter* [2000] BPIR 582 and *Oraki v Dean*
- There was *"no really just result bearing in mind that the real culprit is not before the Court"*
- The judge was influenced by the trustees having been served with the annulment application, such that they were aware that a successful jurisdictional challenge meant that the bankruptcy order would be annulled as of right and, also, that this was an application with obviously strong merits

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Kooter v OR & Radeva (Re Radeva) **[2023] EWHC 594 (Ch)**

- The judge felt that the trustees should have been less involved in the litigation than they were – they should have put in only a simple witness statement setting out the fees incurred to date, given their neutral role
- There had been a number of adjournments in this case which had caused costs to escalate
- The trustees could have obtained a direction at an early stage that they need not participate further
- Not a happy outcome for anyone – Mr Kooter was ordered to pay £7,500 plus VAT towards the trustees' legal costs of £32,500

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