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Funding liquidation: a functional view

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*L.Q.R. 295 I. INTRODUCTION

ENGLISH law provides a range of corporate insolvency procedures.[1] These serve a variety of functions, including collective execution by unsecured creditors, the facilitation of corporate rescue and the enforcement of security, as well as certain public goals including the enforcement of commercial morality.[2] Going to the heart of each procedure are fundamental questions about which *parties* are involved, which *assets* are included and how proceedings are to be *funded.* It is simple enough to suppose that the answers to these questions should differ according to the function of the particular procedure. Yet insolvency law has developed in the haphazard manner of a medieval building, with new parts being added to existing ones without much concern for the coherence of the resulting edifice or whether the foundations will take the weight. This process has resulted in confusion, sometimes even of fundamental matters, among judges, legislators and commentators.

One of the greatest sources of confusion has been the question of funding.Without funds to pay costs, insolvency practitioners are powerless to help creditors. It is therefore understandable that, at times, judges have been tempted to strain statutory construction so as to enhance the funds available to the office-holder. Thus, in *Re Barleycorn Enterprises Ltd,* [3] the Court of Appeal held that a liquidator's expenses were payable out of floating charge assets. Unfortunately, *Barleycorn* seemed to imply that a liquidator might recoup the costs of unsuccessful litigation out of floating charge assets, even where the action was a challenge to the validity of the debenture itself. This lead to further strained constructions as the judiciary sought to prevent the “loser pays” principle of civil litigation from being undermined.

Against this background, this article argues that the House of Lords' recent decision in *Buchler v Talbot,* [4] finding that liquidation expenses are not payable out of floating charge assets, is a welcome return to clarity. ***L.Q.R. 296*** The decision reasserts the importance of answering fundamental questions about the scope and funding of insolvency procedures by reference to their *function.* More importantly still, by overruling *Barleycorn* --the decision at the root of many of the difficulties relating to the funding of insolvency litigation--*Buchler* offers a means of rationalising the existing precedents in a way that may increase the chances that statutory rights of action vested in liquidators for the benefit of unsecured creditors will actually be used.

The rest of the article is structured as follows. Section II gives an overview of the decision in *Buchler.* Their Lordships' conclusion flows from two premises, which are considered in more detail in Sections III and IV respectively. These premises are first, that the *assets* available for distribution in liquidation form a fund distinct from those assets subject to security; and secondly, that the *function* of liquidation is a collective execution in favour of unsecured creditors. From these starting points, it follows logically that the general expenses of liquidation should not be payable out of assets “belonging” to a secured creditor who does not benefit from the liquidation, without very clear statutory words to the contrary. Rather, the assets available for the debenture-holder should only have to bear the costs associated with the administration, realisation and distribution of those assets. In Section V, the article turns to the positive consequences of *Buchler* for the funding of insolvency litigation, arguing that it has opened the way for the development of a market for the external financing of office-holder actions in insolvency. Section VI briefly concludes.

II. *BUCHLER V TALBOT* AND ITS ANTECEDENTS

The statutory framework

Section 115 of the Insolvency Act 1986 provides that the expenses of liquidation shall have priority over the claims of creditors in liquidation:

“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.”

This is a consolidation of a provision originally introduced as s.144 of the Companies Act 1862. Before the Court of Appeal's decision in *Barleycorn,* it was understood to elevate liquidation expenses ahead of other unsecured claims, but not floating charges.[5] It had been established early in the history of corporate insolvency law that assets subject to a charge--floating or otherwise--did not form part of the “assets of ***L.Q.R. 297** the company” available for the unsecured creditors in liquidation,[6] and hence that the 1862 Act did not affect the position of a debenture-holder.[7] The “assets of the company” were therefore the so-called “free assets”, meaning the company's unencumbered assets.

In *Barleycorn,* the Court of Appeal held that this position had been modified by the enactment of the provisions now consolidated as s.175 of the Insolvency Act 1986, which provides as follows:

“(1) In a winding up the company's preferential debts … shall be paid in priority to all other debts.

(2) Preferential debts--

(a) rank equally among themselves after the expenses of the winding up and shall be paid in full, unless the assets are insufficient to meet them, in which case they abate in equal proportions, and

(b) so far as the assets of the company available for payment of general creditors are insufficient to meet them, have priority over the holders of debentures secured by, or holders of, any floating charge created by the company, and shall be paid accordingly out of any property comprised in or subject to that charge.”

Subsections 175(1) and (2)(a) derive from s.4 of the Companies Act 1883, which elevated preferential debts (subject to liquidation expenses) ahead of other unsecured creditors. Subsection 175(2)(b) derives from the Preferential Payments in Bankruptcy Act 1897, which entitled preferential creditors to be paid from floating charge assets where there were insufficient free assets.

Re Barleycorn Enterprises Ltd

Barleycorn concerned a claim for unpaid fees by a firm of accountants who had been commissioned to produce a statement of affairs in respect of a company in liquidation. The statement of affairs contained useful information that would have assisted the liquidator in performing his functions, and the official receiver in any investigation into the company's demise. However, it transpired that the company had no free assets. Unless recourse could be had to charged assets, the accountants would receive no payment. Were this to happen, it would be difficult for liquidators to obtain statements of affairs--and hence to perform their functions--in ***L.Q.R. 298** subsequent similar cases.[8] The Court of Appeal, obviously influenced by a desire to do justice on the facts, allowed the accountants' appeal.

Lord Denning M.R., who gave the leading judgment, focused on the reference in what is now s.175(2)(b) to the “assets of the company available for payment of the general creditors” in contradistinction to the property comprised in or subject to a floating charge. The phrase was narrower than “assets of the company”. Accordingly, he concluded that whilst before 1897, the term “assets of the company” in what is now s.115 had referred to assets *other than* charged assets, the effect of the 1897 Act was to expand it to include assets subject to a floating charge.[9] Section 115 should therefore be interpreted as including assets subject to a floating charge, and hence liquidation expenses took priority over the claims of the debenture-holder.

Lord Denning's textual analysis was buttressed by Phillimore L.J.,[10] who envisaged absurd consequences if the section were not interpreted in this way. If the meaning of “assets of the company” had not changed, then the priority of liquidation expenses vis-à-vis preferential creditors would depend upon the extent (if any) of the floating charge. He explained[11] :

"[The liquidator's] submission at the conclusion of his argument was that if there were free assets, that is to say, assets not covered by some floating charge or debenture, then the proper order for payment would be: first, the costs of the winding-up; secondly, the preferential debts; and, thirdly, the floating charge. On the other hand if there were no free assets and everything was covered by the floating charge, then the order would be: first, the preferential debts; secondly, the floating charge; and, thirdly, the costs of the winding-up--which in practice would mean that whoever did the winding-up would not get anything unless he had made some prior bargain. I find it very difficult to defend the logic which would make the order of priority as between costs and preferential debts dependent upon whether or not there was a floating charge."

Buchler v Talbot

The decision in *Barleycorn* was overruled by the House of Lords in *Buchler v Talbot.* The issue was whether liquidation expenses were payable out of funds in the hands of an administrative receiver, where receivership ***L.Q.R. 299** had preceded the liquidation but had not yet been completed.[12] The lower courts applied *Barleycorn* to answer the question in the affirmative.[13] Their Lordships disagreed.

The first premise of their Lordships' analysis was the same as Lord Denning's, namely that prior to the 1897 Act, holders of floating charges had stood entirely outside the liquidation, because the assets subject to their security did not form part of the "assets of the company".[14] The second premise was that liquidation is conducted for the benefit of unsecured creditors--as Lord Hoffmann put it, the procedure is a "collective execution" for general creditors.[15] From these starting points, the House of Lords reasoned that the 1897 Act did simply what it said: it entitled preferential creditors to look for payment to floating charge assets where there were insufficient free assets to meet their claims. The Act made no mention of liquidation expenses. Thus it had no effect on the priority of liquidation expenses vis-à-vis the floating charge, and their Lordships could see no reason why it had *impliedly* changed the law as to the meaning of the "assets of the company" so as to make the debenture-holder bear the expenses of a procedure from which he did not benefit.[16]

In Lord Millett's view, Lord Denning had wrongly contrasted the term "assets of the company available for the payment of general creditors" with "assets of the company", when the proper counterpart was, in fact, "any property comprised in [a floating] charge".[17] Indeed, if Lord Denning were right, and "assets" were to be contrasted with "assets available for the general creditors" then, as Lord Millett observed, there was no logical reason to restrict its expanded meaning simply to assets comprised in a floating charge--fixed charge assets would be "assets" in this expanded sense too.[18]

The resulting position

After *Buchler,* the order of priority of payment from the "assets of the company" in liquidation is therefore: (i) liquidation expenses; (ii) preferential creditors[19] ; and (iii) unsecured creditors. Where the assets are insufficient to pay the preferential creditors, then recourse may be had ***L.Q.R. 300** to floating charge assets. It is legitimate to use free assets first to pay liquidation expenses, and then to throw the liability for the preferential debts onto the debenture-holder,[20] but it is impermissible, where the free assets do not even cover liquidation expenses, to recoup these expenses from floating charge assets. When the debenture-holder enforces his security against a company in liquidation by appointing a receiver, the order of payment from the realised assets will be (i) the expenses of the receivership; (ii) preferential creditors (insofar as the liquidator cannot pay them out of free assets); (iii) the debt secured; and (iv) the company.[21]

Their Lordships nevertheless conceded that in some situations, expenses incurred by the liquidator should be payable from floating charge assets. First, where a liquidator incurs costs in preserving and realising assets subject to a charge--perhaps because no receiver has been appointed--then the chargee takes the benefit of the realisation, and so it is appropriate for him to bear the costs.[22] Secondly, Lord Nicholls of Birkenhead suggested that the liquidator's costs in discharging his statutory obligation to pay preferential creditors might also be payable out of charged assets.[23]

Ironically, it is arguable that were the facts of *Barleycorn* to be litigated again today, these exceptions would apply in the accountants' favour. The statement of affairs that they had prepared enabled the subsequently appointed liquidator to ascertain the extent of the assets and liabilities, including the preferential debts, and to determine that there were no free assets. No receiver having been appointed, all that the liquidator was administering were assets subject to the debenture. It is at least arguable that the accountants' costs were incurred in the ascertainment of the debenture-holder's

assets, or alternatively in the performance of the liquidator's statutory duty to pay the preferential creditors.[24] It appears that *Barleycorn* not only made bad law, but did so unnecessarily.

**L.Q.R. 301* III. ASSETS OF THE COMPANY: TWO FUNDS OR ONE?

The first premise in Buchler

The two premises of their Lordships' reasoning in *Buchler* are worthy of more detailed consideration. The first--accepted also in *Barleycorn* --was that, save for any changes effected by the 1897 Act, property subject to a floating charge did not constitute "assets of the company" available for unsecured creditors in liquidation. This led Lord Hoffmann to dismiss Phillimore L.J.'s reasoning in *Barleycorn* as "a complete muddle".[25] Since the "assets of the company" did not include floating charge assets, it was incorrect to assert that claims for liquidation expenses, preferential debts and secured debts were all against the same "fund". Rather, the "assets of the company" and "assets subject to security" should be thought of as two distinct "funds", each of which bore its own expenses.

This analysis seems entirely orthodox.[26] It is consistent with the position that the enforcement of a charge does not constitute a disposition of the company's property under s.127 of the Insolvency Act 1986.[27] Moreover, other provisions in the insolvency legislation that refer to the "assets of the company" or the "property of the company" appear to relate solely to the free assets.[28]

Mortgages v charges

Nevertheless, it has been claimed by Rizwaan Mokal that the "two funds" theory is inconsistent with basic property law principles.[29] Mokal's argument is, in the first instance, based on the distinction between charges and mortgages. It is axiomatic that the grant of a mere charge does not involve any transfer of ownership,[30] but creates a security interest "without any transfer of title or possession".[31] How, it is asked, can a charge be said to give rise to a second fund "belonging" to the chargee? Surely, given that no title--legal or equitable--is transferred by the creation of a charge, the charged assets remain part of the chargor's estate?

**L.Q.R. 302* This objection assumes that the use of the term "charge" necessarily connotes the distinguishing characteristic of a *mere* charge, namely the specific appropriation of the charged assets to the payment of the underlying debt, without the transfer of any sort of "ownership".[32] This is not the case. In fact, the term "charge" is frequently used in a different sense--referring to an equitable mortgage--as was explained by Buckley L.J. in *Swiss Bank Corp v Lloyds Bank Ltd*[33] :

"An equitable charge may, it is said, take the form either of an equitable mortgage or of an equitable charge not by way of mortgage. An equitable mortgage is created when the legal owner of the property constituting the security enters into some instrument or does some act which, though insufficient to confer a legal estate or title in the subject matter on the mortgagee, nevertheless demonstrates a binding intention to create a security in favour of the mortgagee, or in other words evidences a contract to do so.… An equitable charge which is not an equitable mortgage is said to be created when property is expressly or constructively made liable, or specially appropriated, to the discharge of a debt or some other obligation, and confers on the chargee a right of realisation by judicial process, that is to say, by the appointment of a receiver or an order for sale."

This confluence of terminology probably originated in the sense in which the term "charge" was historically used in the Court of Chancery. It literally meant a "direction" enforceable in Equity against persons thereby bound.[34] Such directions could take more than one form, including a "mere" charge, being a direction to pay a debt from the proceeds of sale of a particular asset, and an "equitable mortgage by way of charge", being a direction to create a mortgage.

In contrast to the distinction between fixed and floating security, there has been no statutory imperative to distinguish between charges *stricto sensu* and mortgages of personal property. Rather, the relevant legislation has tended to bundle them together.[35] As a result, both those drafting debentures, and judges interpreting them, have often used the terms interchangeably.[36]

**L.Q.R. 303* If it were ever felt necessary to characterise a charge granted under a standard form debenture, whereby the "chargee" is routinely granted all the remedies available to a mortgagee,[37] the result would surely be that in substance it creates an equitable mortgage rather than a mere charge.[38] Indeed, it is common to find judicial reference to a "floating mortgage".[39] Of course, a floating security differs from a fixed charge by way of equitable mortgage in that until crystallisation, the chargee only

obtains an inchoate proprietary interest in the charged assets.[40]

Thus, in the vast majority of cases, the answer to Mokal's objection is simply that most debentures are drafted so as to create charges by way of equitable mortgage, both fixed and floating. For floating charges drafted in this fashion, it is the moment of crystallisation--rather than grant--at which the assignment becomes effective, as indeed was noted by Lord Hoffmann in *Buchler.* [41]

Ownership v property

It is nevertheless the case that a debenture may be drafted so as to create a floating security that is a *mere* charge.[42] The House of Lords gave no indication that their reasoning was not intended to extend to such cases. In relation to such cases, Mokal asserts that their Lordships have confused beneficial ownership of an asset with a proprietary right to payment from that asset.[43] During the lifetime of a mere charge, all the chargee has is the latter.[44] Hence, if the chargee is not the beneficial owner, then how can he be entitled to a "separate fund", rather than simply having a right to prior payment from a *single* fund to which the beneficial owner is also entitled?

***L.Q.R. 304** To answer this objection, it is necessary first to be clear that the word "fund" is not a term of legal art carrying with it certain necessary or innate attributes, but simply a description of a particular state of affairs. As Richard Nolan has carefully explained, to speak of "property in a fund" is no more than an ellipsis,[45] referring to a situation where the bundle of entitlements that together comprise "ownership" of a particular underlying asset are partitioned between more than one party.[46] Such a partition implies that one party--let us call him A--has proprietary rights in relation to certain assets,[47] which are not in his possession. The underlying assets are in the possession of another party--let us call her B--who also enjoys proprietary rights in relation to them. Both A and B's rights are limited by reference to each other's, and the sum of the entitlements they enjoy, between them, in relation to the asset would (if united in a single person) comprise the incidents of "ownership".[48]

The term "fund" is not, however, an appropriate term to describe every partition of proprietary rights in relation to an asset. The ordinary meaning of the word is "a stock or sum of money, *esp.* one set apart for a particular purpose".[49] It follows that it is ordinarily used as an ellipsis in relation to partitions that are understood in terms of a sum of money--typically, the sum A expects to receive on sale of the underlying assets--as opposed to the enjoyment to be had from the assets' use.[50] A corollary of A's lack of interest in the assets for their own sake is that B will typically be permitted, to a greater or lesser degree, to substitute the underlying assets.[51] Thus the term could encompass partitions where the value of A's entitlements are measured either by reference to a fixed sum (as with a security interest) or by reference to the residual value of the underlying assets (as with a beneficial interest).[52]

To say that a person is "entitled" to a fund is merely to say that he is entitled to the bundle of entitlements he enjoys in relation to the underlying assets. There is no inconsistency in saying that a fund to which an asset is subject "belongs" to A, even if A is not the beneficial owner of the underlying asset, or indeed even if the same underlying asset is subject to ***L.Q.R. 305** more than one fund. Seen in this light, it is apparent that the term "fund" in the speeches in *Buchler* is merely a way of summarising the parties' entitlements and obligations. The real question, therefore, concerns the *scope* or *terms* of the liquidator's fund. Why is it that charged assets fall outside it? The liquidator's fund being a creature of insolvency law, the answer to this question is not to be found in the general law of property, but in insolvency law.

Insolvency law and the "assets of the company"

Mokal's objection based on property law is misconceived because it starts from the wrong point in time. It asks how, when a (mere) charge is *granted,* a separate fund comes into existence which "belongs" to the chargee. This, however, was not at issue in *Buchler.* Rather, the starting point of the analysis in *Buchler* (and incidentally, in *Barleycorn*) was that *in liquidation,* assets subject to a charge are not part of the "assets of the company", at least as regards the amount of the secured obligation, and therefore not part of the "fund" available for distribution by the liquidator.

Mokal insists that assets subject to a charge remain subject to the company's beneficial ownership until the security has been enforced, and therefore do not cease to be "assets of the company" in liquidation.[53] Yet, if the company's "assets" include assets subject to (mere) charges, then, to echo Lord Millett,[54] how is it that liquidators are not bound to distribute property subject to fixed charges to the company's unsecured creditors?[55] It appears that the objection proves too much.[56]

Whilst it is true that their Lordships did not explain this point--presumably because they considered it to be so fundamental as not to require elaboration--it follows inexorably from their (orthodox) account of the function of liquidation. Like all statutory language, the meaning of the "assets of the company" in liquidation must be understood in the context in which it is used. As the House of Lords recognised, [57] liquidation is a collective enforcement mechanism for the benefit of unsecured creditors. ***L.Q.R. 306*** Once a compulsory liquidation has commenced, unsecured creditors can no longer execute individually and instead may only do so by participating in the collective proceedings.[58] Secured creditors stand "outside" this process,[59] not being entitled to participate in the collective proceedings,[60] but instead being permitted to enforce their security.[61] It follows from the foregoing that if a winding-up petition is disputed, it is the interests of the unsecured creditors that are paramount, it being understood that secured creditors retain their rights of individual recourse.[62] Moreover, the liquidator is selected by a vote of the unsecured creditors,[63] and his fiduciary duties to act in the "interests of the liquidation" promote the maximisation of realisations for that group.[64]

Liquidation is also the occasion for the termination of the company's affairs. So as to ensure that, consistently with the *pari passu* principle, creditors' claims are treated alike, it is necessary to identify a single point in time at which assets and liabilities can be quantified for the purposes of the final account.[65] For liabilities, the relevant date is when the company goes into liquidation.[66] Whilst the account will actually be drawn up at some later point in time, the entire process is deemed to take place instantaneously.[67] This raises questions about how events occurring after the accounting date, which are relevant to the status or quantification of creditors' claims, should be treated in the accounting process. The answer lies in what Lord Hoffmann has felicitously termed the "hindsight principle"[68] : namely, that subsequent events relevant to the quantification of liabilities or status of claims must be reflected in the accounts,[69] and the liability or claim in question should be valued as if the subsequent event had already occurred by the accounting date.[70]

L.Q.R. 307 The treatment of assets mirrors that of liabilities. When a company goes into liquidation, it is stripped of the beneficial ownership of its assets, which from that moment forward are subject to the "statutory trust".[71] Any purported alienation of the company's assets after the commencement of liquidation is void,[72] as is any prior contract purporting to grant an interest in the company's assets after the company has gone into liquidation.[73] The "assets" of the company falling into the statutory trust comprise all legally protected entitlements which the liquidator is capable of alienating for value for the benefit of the unsecured creditors.[74] Yet, where an asset to which the company is entitled in some way is subject to a proprietary claim that binds the liquidator and which is subsequently enforced, then by symmetry with the treatment of contingent liabilities, the hindsight principle implies that the "asset of the company" is treated as never having been more than the company's *net* entitlement, after the proprietary claimant has taken that to which he is entitled.[75]

This principle is well illustrated in the case of *Re Carl Hirth,* [76] which concerned a claim by a fraudster's trustee in bankruptcy against the liquidator of a shell company to which the fraudster had transferred his assets so as to defeat his creditors. The transfer was held to amount to an act of bankruptcy, and the trustee's title under the relevant Bankruptcy Act related back to that point. The trustee's prior claim meant that, although the assets appeared to belong to the company, they did not do so in fact and were therefore incapable of falling within the statutory trust. As Rigby L.J. explained [77] :

"What is meant by 'the property of the company'? The property which apparently is vested in the company at the time of the commencement of the winding-up, or the property which ultimately turns out to be the property of the company? I venture to think that the latter must be the proper construction. When the time for division has arrived you must find out if you can, and in the best way you can, what is the property of the company, and divide that, and that only."

L.Q.R. 308 Similar reasoning applies to the case of property subject to a security interest. Whilst secured creditors are formally stayed from enforcing their claims in liquidation by s.130(2) of the Insolvency Act 1986, they are given leave to proceed as of right.[78] This is because the liquidator, who stands in no better position than the company, has no right to resist a secured creditor's action where the company itself does not.[79] When a chargee enforces, the proceeds of sale of the charged assets become their property, up to the value of the assets or the debt secured, whichever is the smaller. By a symmetric application of the hindsight principle, these assets are treated *pro tanto* as never having fallen into the statutory trust. This point is made clear in a passage from Cotton L.J.'s judgment in *Re Pyle Works Ltd* [80] :

"But then the question arises, what are to be considered 'assets' or 'property' of the company? … [I]f

the legal estate, so to speak, is outstanding in a mortgagee, then the only portion of that property which the liquidator can look upon as a fund in the winding-up for payment of the debts of the creditors will be the equity of redemption, or, in other words, *that portion of the property remaining after the satisfaction of all the obligations which the directors have properly thrown upon this part of the property of the company.* Therefore, in my opinion, although the assets of the company must … be applied by the liquidator in payment *pari passu* of all the creditors then unpaid, yet property which is in mortgage is not, in my opinion, 'assets' of the company in the sense in which that is to be done, namely, free assets, *assets which can be dealt with by the company in payment of their debts without regard to those who have a mortgage on this portion of the property of the company* " (emphasis added).

This is a particularly helpful illustration, for the italicised portion of his Lordship's reasoning makes clear that the starting point for the analysis is not that the secured creditor is, at any point prior to enforcement, the "owner" of the property, but rather that because he enforces, its *value* is deemed *pro tanto* to be outwith the "assets of the company". Although Cotton L.J. refers to "mortgages", the conceptual machinery he employs is equally applicable to assets subject to a charge, or more generally to any contract specifically enforceable against the liquidator. The reasoning illuminates why the enforcement of such contracts does not amount to ***L.Q.R. 309** a "disposition of the company's property" under s.127 of the Insolvency Act 1986.[81]

Indeed, the statutory scheme goes further than merely waiting for enforcement to take place before deeming assets subject to security to be *pro tanto* outside the liquidator's fund. The treatment of proof by secured creditors shows that they are presumed to enforce their security unless they indicate otherwise. A secured creditor may not prove in liquidation unless he elects to surrender his security for the benefit of the creditors.[82] This demonstrates that the legislation proceeds on the common-sense assumption that any creditor with valid security will, on the liquidation of his debtor, proceed to enforce it.[83]

To recapitulate: insofar as they are subject to valid security, assets simply do not form part of the liquidator's fund. Of course, legal title to the entirety of the charged assets will remain with the company until the moment they are sold or foreclosed upon. Yet it follows from the foregoing analysis that, insofar as they are subject to the secured creditor's rights, they form a separate fund from that which the liquidator is required to administer.

Returning briefly to *Buchler,* we can see that the "liquidator's fund" is merely shorthand for the ultimate pecuniary value of the "company assets" falling into the statutory trust, which as we have seen, does not include charged assets. The "debenture-holder's fund", on the other hand, comprises only the proprietary entitlement to the *value* of the security as regards the assets secured.[84] To object that the debenture-holder is not "owner" of the underlying assets, absent foreclosure, is simply beside the point that his entitlements lie outside the reach of the statutory trust. It follows that in the numerous instances in which members of the judiciary have referred to assets subject to security as the "property" of the debenture-holder,[85] the term is used in the sense of holding *proprietary rights,* as opposed to ownership.

*L.Q.R. 310 Re M.C. Bacon Ltd

Before leaving this section, it is necessary to consider a related objection based upon certain other principles of insolvency law. This is that *Buchler* appears to be inconsistent with views expressed by Millett J. (as he then was) concerning the grant of a charge in *Re M.C. Bacon Ltd.* [86] In that case, the liquidator challenged a standard debenture package (including fixed and floating charges) on the basis that its grant had constituted a transaction at undervalue.[87] For s.238 of the Insolvency Act to apply, a company must have entered into a transaction gratuitously, or in return for a consideration significantly less than that which it gave. Millett J. held that the grant of a security over the company's property did not amount to the company giving any "consideration" at all. His Lordship explained[88] :

"The mere creation of a security over a company's assets does not deplete them and does not come within [s.238]. By charging its assets the company appropriates them to meet the liabilities due to the second creditor and adversely affects the rights of other creditors in the event of insolvency. But it does not deplete its assets or diminish their value."

Mokal asserts an inconsistency between this statement and the reasoning in *Buchler* : how can *M.C. Bacon* be right and yet a charge create a separate fund?[89] Again, however, this confuses different questions. First, s.238 is by definition concerned with transactions that take place *before* the company

goes into liquidation.[90] Hence Millett J. speaks of the *creation* of a charge, not of its treatment in liquidation. Secondly, the section makes no reference to the "assets of the company", but simply to the value of consideration. Thus when Millett J. speaks of "assets", he uses the phrase in a different sense to that employed in the provisions of the Act dealing with the mechanics of liquidation. He refers to the company's net assets in a going-concern accounting sense, not the assets available for the unsecured creditors in liquidation as defined by statute. A transaction for which the company receives significantly less consideration than it gives will necessarily deplete the net assets. However, the grant of a charge does not, because it simply gives the chargee an alternative right of recourse.[91] The chargee may not pursue the company for any greater sum than he was otherwise entitled, and so the net assets are unaffected.[92]

**L.Q.R. 311* IV. THE FUNCTION OF LIQUIDATION

The second premise in Buchler

The second premise of the reasoning in *Buchler* is that liquidation is "a form of collective execution by all its creditors against all its available assets." [93] As liquidation is run purely for the benefit of unsecured creditors (and possibly, contributories) and a debenture-holder has no interest in the proceeding,[94] it follows that it is unfair to subject the debenture-holder's fund to the expenses of liquidation.

Whilst this is a good account of liquidation's basic function, does it fail to give sufficient weight to the public aspects of insolvency law? In particular, a subsidiary function of liquidation is to act as a vehicle for the *ex post* enforcement of "commercial morality".[95] It may be objected that floating charge-holders derive benefits from the proper performance of these public functions, and it is therefore justifiable to require them to pay for this through the funding of liquidations.[96] However this objection, like that from property law, is also misconceived.[97] In order to see why, it is necessary to consider--in general terms--the relationship between the public and private elements of insolvency law.

Historically, insolvency proceedings have been concerned with the enforcement of morality through the retrospective investigation of the debtor's affairs and the visitation of appropriate sanctions. In relation to corporate debtors, this pattern has complemented English law's rather more diffident approach to the enforcement of directors' duties whilst companies are still trading. There are sound commercial reasons why litigation against delinquent directors of trading companies may be undesirable--cost, loss of management time and negative publicity, to name but a few.[98] These concerns are reflected in the restrictive standing requirements for derivative actions,[99] and the still-evolving requirement that to be remediable under s.459 of the Companies Act 1985, a breach of directors' duties harming the petitioner's interests must be **L.Q.R. 312* sufficiently serious as to constitute "unfair" prejudice.[100] For participants in solvent companies, there are, of course, a number of other practical ways of dealing with directors that are cheaper and more effective than litigation. The law's "hands off" approach to the working boardroom developed in the shadow of its traditionally "hands on" approach to the *ex post* investigation and sanctioning of directorial conduct in the context of corporate failure. The public elements of insolvency law are the major planks of this *ex post* approach. In liquidation, there are three such elements[101] : prosecution, disqualification and civil remedies against directors and others.[102] In the rest of this section, we consider prosecution and disqualification in turn, paying particular attention respectively to how the processes are funded and which parties may be expected to benefit from their effects. The funding of civil remedies raises rather more complex issues that we postpone until the next section.

Prosecution

The Insolvency Act, subs.218(3) and (4) require a liquidator, to whom it appears that any officer of the company may have been guilty of an offence in relation to the company,[103] to report the matter to the official receiver or Secretary of State, who will then consider whether prosecution is warranted. Moreover, in compulsory liquidation, the official receiver is, in all cases, obliged to investigate the company's affairs and, in particular, the reasons for the company's failure.[104] Thus, the liquidator's functions involve a certain amount of investigative work. The costs of any actual prosecution will, of course, be at public expense,[105] but the costs of preparing any liquidator's or official receiver's report, and of precursory public or private examinations of the company's officers,[106] are chargeable to the liquidation expenses.[107] Increasing the likelihood of prosecution in **L.Q.R. 313* this fashion may be

expected to have a deterrent effect on the proscribed conduct. Thus the benefit of the office-holder's investigations might be expected to be reaped by all those dealing with companies.

Disqualification

Investigation and reporting by the office-holder of directors' conduct is also the mechanism by which liquidation facilitates the disqualification of delinquent directors. Under s.7(3) of the Company Directors Disqualification Act 1986 ("CDDA"), every office-holder to whom it appears that there may be grounds for concluding that a director or former director is "unfit to be concerned in the management of a company" must submit a report to the Secretary of State.[108] If the Secretary of State decides to proceed, then the court is obliged under CDDA, s.6 to disqualify the director in question where it is satisfied as to his "unfitness".[109] Thus office-holders' reports provide the foundation upon which disqualification cases are built.

Whilst the costs of the disqualification process are largely borne by the Secretary of State, the office-holder's costs in investigating and preparing the report are expenses of the relevant insolvency proceeding.[110] As with prosecution, disqualification is said to benefit the public at large by keeping unfit directors "off the road" and by encouraging other directors, through general deterrence, to maintain standards in their conduct of the company's affairs.[111]

Funding the public functions of liquidation: a provisional assessment

The picture so far is that the initial investigations leading to prosecution or disqualification are carried out by liquidators at the expense of the company's creditors, even though the benefits of these processes ultimately go to the general public. Yet the existence of such public functions, which must be funded from liquidation expenses, does not undermine the second premise of *Buchler* --that liquidation is essentially a procedure for the benefit of unsecured creditors.

Of the two mechanisms considered so far, disqualification is by far the most significant in practice. In 2002, nearly 2,000 directors were ****L.Q.R. 314*** disqualified,[112] about ten times the number of convictions secured following winding-up.[113] Moreover, the contribution of insolvency proceedings to disqualification is not unique to liquidation. All office-holders must make reports under CDDA, s.7(3). The investigatory and preparatory costs of such reports must be borne as "expenses" of the relevant procedure in administrative receivership, administration and liquidation alike. Of course, only liquidation is a vehicle for investigations leading to prosecution. However, conduct which would render a director liable to prosecution would also render him liable to disqualification, so the same investigatory work may be expected to suffice for both. Thus, there will be minimal *extra* cost which must be borne by the estate in liquidation.[114] The emergent picture is that *all* corporate insolvency proceedings--not just liquidation--involve public aspects which must be paid for in part from the expenses of the proceeding.[115] In light of this, it is perfectly apt to describe liquidation as "essentially" a process of collective execution. It undeniably involves some public aspects, but these are subsidiary, and more importantly for present purposes, are not what distinguishes it from other insolvency proceedings.

Distinguishing other insolvency procedures

Other insolvency procedures may, however, be distinguished from liquidation by reference to the parties for whose benefit they operate. After *Buchler,* the burden of the expenses of each procedure is now allocated consistently with this distinction. In liquidation, expenses are borne by the unsecured creditors, for whose benefit the procedure is run, whereas in administrative receivership, which functions for the exclusive benefit of the debenture-holder, the expenses are borne solely out of the debentureholder's fund.[116] Administrative receivership has of course been prospectively abolished by the insolvency provisions of the Enterprise Act 2002, ****L.Q.R. 315*** and in its place chargees are now encouraged to use a streamlined administration regime.[117] The new procedure is run for the benefit of all creditors, and it is therefore appropriate that the costs should be shared between secured and unsecured creditors--an approximation to which is achieved by making the expenses of administration payable ahead of the floating charge.[118]

V. FUNDING INSOLVENCY LITIGATION

The context

The civil actions potentially available to a liquidator are, in outline:

(i) A summary procedure for *misfeasance* by officers of the company, intended to provide an expedited mechanism whereby wrongdoing by the company's directors may be remedied in liquidation.[119]

(ii) Actions for *fraudulent* or *wrongful trading,* intended to encourage directors not to take actions during the "twilight" period that will harm creditors' interests.[120]

(iii) Actions for *transaction avoidance,* intended to discourage misbehaviour during the transition from factual to formal insolvency.[121]

It is well known that these actions, which form the third "public aspect" of liquidation, have been rendered ineffective by difficulties with the funding of litigation.[122] What has been less well understood, however, is the extent to which these difficulties in funding are in large part "ripple effects" traceable to the Court of Appeal's decision in *Barleycorn.* This means that the House of Lords' excision of *Barleycorn* from the jurisprudence has potentially significant implications for the funding of insolvency litigation. It paves the way to the amelioration of the existing difficulties, increasing the likelihood of privately-financed enforcement in the future, with consequent public benefits by way of deterrence.

**L.Q.R. 316 A framework for analysis*

Three particular questions have taxed courts and commentators in relation to the funding of these actions. The way in which these questions are answered affects the likelihood that an office-holder will be able to enforce any relevant claims. The questions, and their implications, are as follows:

(i) *Destination:* Do recoveries from successful actions fall within the scope of a floating charge? No liquidator would wish to bring an action simply to see the proceeds go to a debentureholder. Yet if the proceeds do fall within the scope of the charge, then the debenture-holder may be willing to fund the litigation themselves.

(ii) *Expenses:* Even where recoveries go to the unsecured creditors, can a liquidator recoup the costs of an action as "expenses of the liquidation"? Clearly, if he cannot, he has no incentive to bring proceedings.

(iii) *Assignability:* Can liquidators assign rights in such actions to third parties, on terms that the assignee funds the action in return for a share of any recoveries, without contravening the law's general prohibition on champerty?[123] If such assignment is possible, then it may be possible for actions to be financed *externally* even if the liquidator is unable to charge the costs as "expenses of the liquidation".

We now chart, chronologically, how the answers to these questions had evolved prior to the decision in *Buchler,* and in particular, how they were influenced by the decision in *Barleycorn.*

Before Buchler v Talbot

Destination: *Re Yagerphone Ltd*

The destination question was first considered in relation to misfeasance recoveries. In *Re Anglo-Austrian Printing and Publishing Union,* [124] Vaughan Williams J. held that they fell into the floating charge, being the fruits of a right that had come into existence when the relevant wrongs had been done to the company prior to liquidation.

A distinction was subsequently drawn between actions for misfeasance, which may be brought in the company's name to enforce pre-existing causes of action, and what may be termed "office-holder actions", namely those causes of action that are not created until the commencement of ***L.Q.R. 317*** insolvency proceedings, and must be brought in the office-holder's name (such as actions for transaction avoidance, and now for wrongful trading). In *Re Yagerphone Ltd,* [125] Bennett J. held that a liquidator's recoveries from a successful preference action could not be claimed by a debenture-holder, because the right to recover the money from the preferred creditor vested in the liquidator exclusively for the benefit of unsecured creditors. Thus the recoveries were[126] :

"[A] sum of money received by the liquidators impressed in their hands with a trust for those creditors

amongst whom they had to distribute the assets of the company."

This ground was approved in subsequent cases as being the *ratio* of the decision.[127]

Expenses: *Re M.C. Bacon Ltd (No.2)*

One such case was *Re M.C. Bacon Ltd (No.2),* [128] a decision at the heart of the problems in this area. A liquidator had unsuccessfully challenged the validity of a bank's debenture under ss.238 and 239 of the Insolvency Act.[129] The liquidator was ordered to pay the bank's costs. He applied for an order permitting him to recoup the bank's and his own costs from assets subject to the bank's now vindicated floating charge. His argument, which seemed "unassailable" in light of *Barleycorn,* [130] was that the costs were liquidation expenses and therefore payable out of floating charge assets in priority to the preferential debts and the bank's claim under s.175.

The outcome for which the liquidator contended was patently unjust. It required the vindicated charge to be subordinated to the costs of the failed challenge, thereby violating the "loser pays" principle of civil litigation.[131] The just result was equally obvious: ss.238 and 239 being office-holder actions, any recoveries would have benefited the unsecured creditors alone, and hence the costs should only ever have been chargeable to the free assets.[132] However, Millett J.'s ability to reach this result was constrained by the decision in *Barleycorn.* His precarious route ***L.Q.R. 318** of escape was to hold that the costs fell outside the "expenses of the liquidation"--that is, that they were not "expenses properly chargeable or incurred…by the liquidator in preserving, realising or getting in any of the assets of the company" within r.4.218(1)(a) of the Insolvency Rules, as then worded. His reasoning was as follows. First, he applied *Yagerphone* to hold that recoveries following a liquidator's application under s.239 enured for the benefit of the "general body of creditors", and as such never became part of the company's assets, but were simply held by the liquidator subject to the statutory trust for the unsecured creditors.[133] Secondly, in a step dictated by expediency rather than rigour, he concluded that, because the recoveries fell directly into the statutory trust, the costs had not been incurred in "preserving, realising or getting in any of the *assets of the company* ".[134] Thus the liquidator's costs were not payable as liquidation expenses, and Millett J. avoided the unjust result that would otherwise have followed as an unintended consequence of *Barleycorn.* Unfortunately, *M.C. Bacon* itself had an unintended consequence: by denying a liquidator recoupment of his costs from liquidation expenses, it negated his incentive to bring office-holder actions. The ripples from *Barleycorn* continued to spread.

Assignability: *Re Oasis Merchandising Ltd*

Worse still, the distinction drawn in *M.C. Bacon* between "assets of the company" and "office-holder recoveries" was applied mechanically in a subsequent line of authorities to reach the conclusion that the liquidator had no power to assign any interest in the proceeds of these causes of action. This further exacerbated the funding difficulties. The high watermark was *Re Oasis Merchandising Services Ltd,* [135] a case in which the liquidator, who had commenced wrongful trading proceedings, entered into an agreement with an external funder on terms that the funder would meet the liquidator's costs in return for a share of any recoveries. The agreement was prima facie champertous,[136] but the liquidator argued that it was validated by his statutory power "to sell any of the company's property".[137] The Court of Appeal held that recoveries from a successful wrongful trading action were not "company property" falling within the liquidator's power of sale and stayed the action on the ground that it was tainted by the illegal funding agreement. Drawing on both *Yagerphone* and *M.C. Bacon (No.2),* Peter Gibson L.J. distinguished between assets which ***L.Q.R. 319** are the "property of the company" at the time of the commencement of liquidation--including any rights of action that might have been pursued by the company prior to liquidation--and those assets which only arise after the liquidation of the company, including recoveries obtained by the liquidator pursuant to statutory powers conferred on him.[138] In his view, only the former constituted "property of the company" which an office-holder was entitled to sell.

Expenses again: the "Floor Fourteen amendment"

Although dicta of the Court of Appeal in *Katz v McNally* [139] appeared to cast doubt on the reasoning in *M.C. Bacon (No.2),* a differently-constituted court took the opportunity to reinforce the *M.C. Bacon/Oasis* orthodoxy in *Re Floor Fourteen Ltd.* [140] In response to disquiet over the outcome in the latter case, Parliament amended r.4.218(1)(a), to provide that the expenses of liquidation should include[141] :

"Expenses or costs … relating to the conduct of any legal proceedings which he has power to bring or defend whether in his own name or the name of the company."

Unfortunately, the amended rule went much further than was necessary as it seemed to require a court faced with the facts of *M.C. Bacon (No.2)* to reach the very outcome that Millett J. had struggled so hard to avoid.[142] Whereas *M.C. Bacon (No.2)* and *Oasis* stifled office-holder litigation, the amendment appeared to have disinterred the original problem caused by the *Barleycorn* decision.

Implications of the pre-*Buchler* position

As this brief review has demonstrated, the ripples from the Court of Appeal's decision in *Barleycorn* gave rise to a sequence of troublesome cases that impacted upon the funding of insolvency litigation. To summarise the position prior to *Buchler,* the three basic questions in this area were answered as follows:

(i) *Destination:* It was a hard and fast rule that the future recoveries of office-holder actions were neither "assets" nor "property" of the company for the purposes of the various ***L.Q.R. 320** statutory provisions concerned with the expenses of winding up and the office-holder's power of sale.[143]

(ii) *Expenses:* The law had oscillated between absurdities: first (under *M.C. Bacon*) the costs of office-holder actions were not recoverable as liquidation expenses at all; later (following the amendment to the Insolvency Rules), they could be recouped as of right as an expense of the winding up, out of floating charge assets, seemingly even in respect of an unsuccessful challenge to the validity of the debenture.

(iii) *Assignability:* Neither office-holder actions nor their fruits could be assigned under the power of sale to external funders on sensible commercial terms.[144]

The impact of Buchler v Talbot

In a telling passage in his speech in *Buchler,* Lord Millett made the following observations[145] :

"In *Re M.C. Bacon Ltd* [*(No.2)*] a liquidator claimed that the costs of an unsuccessful attempt to set a floating charge aside should be paid out of the assets subject to the charge in priority to the claims of the charge-holder. But for the decision in *Barleycorn* the claim could not have got off the ground. A more absurd and unjust outcome could hardly be imagined. The court was able to avoid it only by finding a way to disallow the costs of the action as recoverable expenses of the liquidation."

By overruling *Barleycorn,* the House of Lords cured the malady for which the reasoning in *Bacon* was prescribed. There is no longer any need to continue to endure the side effects of the prescription. *Buchler* therefore opens the way to a rationalisation of these authorities in a way that could facilitate the development of a market for the funding of insolvency litigation. Let us now consider the impact of the decision on each of these questions in turn.

***L.Q.R. 321** Destination

This question goes to the heart of the relationship between property law and insolvency law, and in particular the function of liquidation. These are issues to which, as we have seen, *Buchler* speaks clearly. The decision reaffirms (i) that insolvency proceedings should not, absent clear statutory language to the contrary, be the occasion for the alteration of pre-existing proprietary rights[146] ; and (ii) that winding-up proceedings are for the benefit of unsecured creditors alone.[147] These propositions serve to reinforce the pre-existing position in relation to destinations: that the recoveries falling into the debenture-holder's fund should be, and should *only* be, those recoveries which the debenture-holder would be capable of realising by an action brought outside liquidation.

Considering first recoveries from misfeasance actions, the two propositions square exactly with the reasoning of Vaughan Williams J. in *Anglo-Austrian Printing and Publishing Union.* [148] Such recoveries are the fruits of causes of action that came into being during the company's life. These causes of action could have been enforced on the debenture-holder's behalf by a receiver. The fact that the company has gone into liquidation is not an occasion for the expropriation of the debenture-holder, and so the recoveries are for his benefit, minus an allowance for the liquidator's particular costs in obtaining them.

Turning to office-holder actions, the propositions also tend to support the conclusion of Bennett J. in

Yagerphone. Office-holder actions vest in the liquidator and form part of the means at his disposal for carrying out his functions in the interests of unsecured creditors. They represent assets which come into existence on liquidation, and so cannot be recovered by the company when solvent. It follows that neither a debenture-holder nor his receiver has standing to pursue an office-holder action, and so the fruits of such actions cannot be reached by a debenture-holder enforcing his security outside liquidation.[149] Just as the advent of liquidation does not deplete a chargee's pre-liquidation proprietary rights, it surely cannot be the occasion for their enhancement.[150] It follows that a debentureholder should not be allowed to claim office-holder recoveries arising from the exercise of the liquidator's statutory powers.[151] This analysis rests solely on *Yagerphone* and does not depend on the distinction drawn in *Bacon* and *Oasis* between "company property" at the commencement of ***L.Q.R. 322** liquidation and subsequently accruing office-holder recoveries.[152] Rather, the point is that as office-holder actions vest in the liquidator in his capacity as manager of the fund of free assets (which enures to the benefit of unsecured creditors), the structure of the insolvency legislation necessarily implies that such recoveries are not so chargeable.[153]

All this is not to say that an office-holder action can *never* bring benefits to a debenture-holder. There may be circumstances where a debentureholder has continuing rights in property that has been alienated by the company through a transaction subsequently vulnerable to challenge by an office-holder action.[154] In such cases, the "two funds" theory implies that a portion of the "recoveries" of any such action, commensurate to the value of the chargee's rights, would be directed to the debenture-holder's fund.[155] This respects the chargee's pre-insolvency entitlements. As a corollary, the debenture-holder should not benefit from the liquidator's "recovery" if its former proprietary rights have been extinguished--for example, if the alienation of the assets occurred in the ordinary course of business at a time when the charge was uncrystallised.[156] To allow the debenture-holder to benefit in such circumstances would make him better off in liquidation than under the general law.[157]

Expenses

If *Buchler* merely clarified and reinforced the pre-existing position in relation to the destination of recoveries, it clearly changed matters in relation to the "expenses question". Although, by virtue of the 2002 amendment to the Insolvency Rules, it is beyond doubt that the costs of office-holder actions count as liquidation expenses, *Buchler* means that these expenses can now only be recouped from the free assets. This has the welcome effect of ensuring that the debenture-holder can never be forced to pay for the costs of an unsuccessful challenge to the debenture. At the ***L.Q.R. 323** same time, by reducing the likely size of the asset pool available to pay liquidation expenses, it appears to undermine the liquidator's incentives to pursue office-holder actions.[158] But as we shall see, to focus on this is to lose sight of the bigger picture.

Assignability

It appears that *Buchler* may have had a positive impact on the assignability of office-holder recoveries. In short, it is arguable that the House of Lords have impliedly overruled the Court of Appeal's decision in *Oasis.*

The starting point for the argument is the conceptual problems of the analysis in *Oasis.* Recall that in *Barleycorn,* the "assets of the company" had been viewed as a *single* fund, comprising a blend of free assets and those subject to a floating charge. Against this background, the courts in *M.C. Bacon (No.2)* and *Oasis* were driven to hold that the fruits of officeholder actions fell *outside* this single fund.[159] To sidestep *Barleycorn* in this way, the office-holder recoveries had to exist in the ether, being neither charged assets available to the debenture-holder, nor "company property" to be administered by the liquidator. This, however, was conceptually flawed, for if office-holder recoveries were not "assets of the company" in liquidation, then how were they to be administered, given that the statute directs the liquidator to distribute only "assets of the company"?[160] If there ever was a "separate funds fallacy", this was surely it.[161]

The decision in *Buchler* resolves this confusion. It clarifies that the debenture-holder's and unsecured creditors' assets form *two* separate funds. In this milieu, office-holder recoveries either form a third fund (in the ether),[162] or are properly understood as falling within the liquidator's fund--in which case the House of Lords has impliedly overruled *Oasis.* The latter is the better view, for three reasons. First, as we have seen, the *Oasis* analysis is conceptually flawed. Secondly, the benefit of officeholder recoveries will ordinarily go to the unsecured creditors. *Buchler* makes clear that costs are borne by the fund available to the party who benefits from the relevant expenditure. It would be a curious result if, because they were not classed as part of the "assets of the company", office-holder

recoveries were not available to pay the general expenses of the liquidation--incurred for the exclusive benefit of the unsecured creditors--notwithstanding that such recoveries are a fund available for the unsecured creditors. Thirdly, and most importantly, by excising ***L.Q.R. 324*** *Barleycorn* from insolvency jurisprudence, *Buchler* removes the need for conceptual contortions. In light of *Buchler,* the better view is that office-holder recoveries fall into the "assets of the company".[163] In turn, this implies that office-holder recoveries are "property of the company" within the power of sale.

If, as we contend, the interpretation of "company property" in *Oasis* cannot stand with *Buchler,* it would be open to a judge at first instance to disregard *Oasis* were an appropriate test case to be brought.[164] A market for external financing of office-holder actions, stopped in its tracks by the *Oasis* decision, could be allowed to develop.[165] This would provide access to a much wider range of funding for office-holder actions than would be available even if the office-holder's costs could be recouped from floating charge assets. At the same time, the possibility that a debenture-holder might have to fund a challenge to his own security is eliminated. Thus, if the impact on assignability is fully appreciated, the position after *Buchler* may represent a considerable liberalisation of the possibilities for funding insolvency litigation. In turn, this could--counter-intuitively--allow the public functions of liquidation to be performed much more effectively.

Summary

The effects of the decision in *Buchler* on the three "funding questions" may be summarised as follows:

(i) *Destinations* : By emphasising the function of liquidation as primarily benefiting unsecured creditors, *Buchler* supports the conclusion in *Yagerphone* that recoveries from office-holder actions that would benefit unsecured creditors, in contrast to actions brought under the misfeasance procedure, are not chargeable by the company.[166]

(ii) *Expenses* : The costs of office-holder recoveries remain recoverable as "expenses of the liquidation." However, because floating charge assets are no longer available to pay these ***L.Q.R. 325*** expenses, the funds available to the liquidator from this source have been curtailed.

(iii) *Assignability* : By overruling *Barleycorn, Buchler* has removed the need for the illogical distinction drawn between "company property" and office-holder recoveries in *Bacon* and *Oasis.* Insofar as they rest upon this reasoning, these decisions can no longer be supported. The better view is that officeholder recoveries are "property of the company" capable of assignment by the liquidator.

VI. CONCLUSION

This article has explored the reasoning and implications of the House of Lords' decision in *Buchler* with two goals in mind. First, it has sought to demonstrate that the decision is consistent both with general property law concepts and with the structure of insolvency law. The decision has not disturbed settled jural relations in relation to security interests. Rather, it concerns the unravelling of such relations and their value in the insolvency context. Whether a charge-holder is an "owner" at point of grant is not the issue. Moreover, the House of Lords' characterisation of liquidation as a mechanism for collective execution by unsecured creditors is apt. Whilst there are some public aspects to liquidation proceedings, these are in large part common to all insolvency proceedings, and so do not distinguish liquidation from other insolvency procedures.

Secondly, the analysis suggests that the decision could form the basis for a beneficial approach to the resolution of the difficulties that have plagued the funding of litigation by office-holders. Whilst liquidators may bemoan the fact that the costs will not be recoverable from floating charge assets, this will avoid any transgression of the "loser pays" principle where a debenture is unsuccessfully challenged. Moreover, with the Court of Appeal's decision in *Barleycorn* consigned to history, the difficulties in the case law concerning assignment of office-holder actions may be ironed out. Indeed, the way may now be open for a market in these claims to be developed, enhancing the likelihood of enforcement and the consequent public benefits that this will entail.

The government has recently made clear that it intends, through a clause included in the Company Law Reform Bill, to reverse the decision in *Buchler.* [167] Such a move, which would weaken the function-based demarcation between insolvency procedures and open the door once more to the use of floating charge assets to challenge a debenture-holder's security, is not supported by this article's analysis. Nevertheless, even ***L.Q.R. 326*** if the specific result of the decision is reversed by statute,

this should not detract from the broader principles it enunciates regarding the function of liquidation, and the implications of these for the funding of insolvency litigation.

JOHN ARMOUR.[168]

ADRIAN WALTERS.[169 170]

L.Q.R. 2006, 122(Apr), 295-326

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1. At the last count, there were seven general procedures (compulsory and voluntary winding-up, administration, administrative receivership, schemes of arrangement, CVAs and CVAs with a moratorium of claims). In addition, there are numerous special insolvency regimes open only to companies conducting particular types of business (e.g. infrastructure companies).

2. See generally, *Insolvency Law and Practice: Report of the Review Committee* (Chairman: Sir Kenneth Cork), Cmnd.8558 (1982), Ch.3; Goode, *Principles of Corporate Insolvency Law* (3rd edn, 2005), at pp.18-29; Insolvency Service, *Review of Company Rescue and Business Reconstruction Mechanisms* (1999), Sect.6; Finch, *Corporate Insolvency Law: Perspectives and Principles* (2002), Ch.2.

3. [1970] Ch. 465.

4. [2004] UKHL 9; [2004] 2 A.C. 298.

5. See, e.g. Stiebel, *Stiebel's Company Law and Precedents* (3rd edn, 1929), Vol.II at pp.1062-1063; Wright and Buchanan-Dunlop (eds), *Palmer's Company Precedents* (17th edn, 1960), Vol.2 at p.549.

6. See, e.g. *Re David Lloyd & Co* (1877) 6 Ch.D. 339 at 344; *Re Wanzer Ltd* [1891] 1 Ch. 305 at 314; *Strong v Carlyle Press* [1893] 1 Ch. 268 at 276.

7. *Re Regent's Canal Ironworks Co, ex p. Grissell* (1875) 3 Ch.D. 411 at 426-428.

8. Sachs L.J. noted that such a result would “enure to the detriment of the public interest when there is a winding-up order of the court” [1970] Ch. 465 at 475.

9. [1970] Ch. 465 at 474.

10. Sachs L.J. also delivered a short judgment concurring with Lord Denning.

11. [1970] Ch. 465 at 476.

12. Had the receivership been completed, then there would no longer have been any “assets subject to a floating charge”, and hence the Insolvency Act 1986 (“IA 1986”) s.175 could not in any event have applied: see *Re G.L. Saunders Ltd* [1986] 1 W.L.R. 215 at 220.

13. [2001] 1 B.C.L.C. 419 (Rimer J.); [2002] EWCA Civ 228; [2002] 1 B.C.L.C. 571, CA.

14. [2004] UKHL 9; [2004] 2 A.C. 298 at [10], [28], [52].

15. At [28]. See also at [51].

16. At [16], [35], [58], [77].

17. At [72]-[79].

18. At [73].

19. Where, as in *Buchler,* there has been a prior receivership, and the receiver has made payments to preferential creditors under IA 1986 s.40, then the debenture-holder will be entitled to recoupment out of the free assets *after* the liquidation preferential creditors are paid: s.40(3), *Buchler* at [88]. The freedom of a debenture-holder to appoint an administrative receiver is now constrained by IA 1986, s.72A (inserted by the Enterprise Act 2002).

20. *Westminster Corp and United Travellers Club Co Ltd v Chapman* [1916] 1 Ch. 161 at 168.

21. Where the receivership occurs without the company being in liquidation at the time, then the order of priorities is (i) the expenses of the receivership; (ii) the creditors preferential in the receivership; (iii) the debt secured; and (iv) the company.

22. *Re Regent's Canal* (1875) 3 Ch.D. 411 at 427; *Re Berkeley Applegate (Investment Consultants) Ltd* [1989] Ch. 32 at 50-53; *Buchler* at [19], [31], [63]. Moreover, IA 1986, s.144 envisages that the liquidator will take custody of charged assets in such circumstances and the Insolvency Rules 1986 (SI 1986/1925) ("IR 1986"), r.4.127B makes provision for him to be remunerated from those assets for that work.

23. *Buchler* at [18]-[19].

24. Had a receiver been appointed in *Barleycorn,* the debenture-holder would necessarily have had to bear these costs in order to make distributions to the preferential creditors under IA 1986, s.40 outside winding up.

25. *Buchler* at [37]. Phillimore, L.J.'s. reasoning is explained above, text to fn.11.

26. Cf. Mokal, "Liquidation Expenses and Floating Charges--the Separate Funds Fallacy" [2004] L.M.C.L.Q. 387.

27. *Re Margart Pty Ltd* [1985] B.C.L.C. 314.

28. See, e.g. IR 1986, r.4.181 (referring to payment of unsecured creditors' claims "from the assets of the company").

29. Mokal, fn.26 above.

30. See, e.g. *National Provincial and Union Bank of England v Charnley* [1924] 1 K.B. 431 at 449-450; Goode, *Legal Problems of Credit and Security* (3rd edn, 2003), at pp.35-37.

31. *Re B.C.C.I. International SA (No.8)* [1998] A.C. 214 at 226, *per* Lord Hoffmann. In addition to their substantive differences, a mere charge also differs from a mortgage in terms of remedies. The holder of a mere charge is not entitled to any remedies other than the right to apply to the court for an order for sale or to appoint a receiver. Unlike a mortgagee, such a chargee has no right to take possession of the property, and no right to foreclose upon it: *Carreras Rothman Ltd v Freeman Mathews Treasure* [1985] Ch. 207 at 227.

32. See fnn.30-31, above.

33. [1982] A.C. 584 at 594-595 (aff'd HL *ibid.* , at p.615). See also the careful discussions by Scrutton L.J. in *London County and Westminster Bank v Tompkins* [1918] 1 K.B. 515 at 528-530; Ferris J. in *Re ELS Ltd* [1995] Ch. 11 at 20-26 and Goode, fn.30 above, at 36-37.

34. See, e.g. *Rodick v Gandell* (1852) 1 De G.M. & G. 763 at 777; 42 E.R. 749 at 754.

35. See, e.g. Companies Act 1985, s.396(4) ("'charge' includes mortgage."); Law of Property Act 1925, s.205(1)(xvi) ("'mortgage' includes any charge").

36. One of the few contexts in which the distinction really matters for personal property is where security consists of a "charge back" of a debt owed by the chargor to the chargee as security for a countervailing indebtedness. As an assignment of a debt to the debtor will discharge the indebtedness, such a "charge back" can only take effect by way of *mere* charge, as opposed to an equitable mortgage by way of charge: *Re B.C.C.I. (No.8)* [1998] A.C. 214 at 226-227; cf. *Re Charge Card Services* [1987] Ch. 150 at 175-177.

37. See, e.g. Lingard, *Bank Security Documents* (3rd edn, 1993), at p.355 (specimen debenture, clause 6.01); Gough, *Company Charges* (2nd edn, 1996), at pp.18-20.

38. See *London County and Westminster Bank v Tompkins* [1918] 1 K.B. 515 at 525, 528-530. See also Gough, fn.37 above, at pp.100-101; Oditah, *Legal Aspects of Receivables Financing* (1991), at pp.94-96.

39. See, e.g. *Re Colonial Trusts Co* (1879) 15 Ch.D. 465 at 472; *Evans v Rival Granite Quarries Ltd* [1910] 2 K.B. 979 at 999.

40. See, e.g. *Biggerstaff v Rowatt's Wharf Ltd* [1896] 2 Ch. 93 at 101, 104, 105; *N.W. Robbie & Co Ltd v Witney Warehouse* [1963] 1 W.L.R. 1234 at 1337, 1339; *Re ELS Ltd* [1995] Ch. 11 at 25-26. See Oditah, fn.38 above at p.113. The way in which the floating charge holder's rights are analysed prior to crystallisation does not affect the current discussion.

41. [2004] UKHL 9; [2004] 2 A.C. 298 at [30].

42. See, e.g. *Re Marriage, Neave & Co* [1896] 2 Ch. 663 at 673, 675, 677-678; *Re ELS Ltd* [1995] Ch. 11 at 20-26.

43. Mokal, fn.26 above, at 393-396.

44. Mokal makes a bold attempt to expand the impact of his objection by asserting that even a mortgage is better characterised as conferring upon the mortgagee only a "proprietary right to priority" as opposed to "ownership" (*ibid.*). That is, he asserts that the beneficial ownership taken by a mortgagee is, when viewed alongside the entitlements reserved to the mortgagor by virtue of his equity of redemption, not truly "ownership" at all. As Mokal's objection from property law is demonstrably ungrounded (Sections 0 and 0, below) in even its strongest possible case--namely, in relation to a mere charge--we need not detain ourselves further with this subsidiary claim.

45. Nolan, "Property in a Fund" (2004) 110 L.Q.R. 108 at 108-110.

46. The entitlements that together comprise "ownership" were classically described by Honoré, "Ownership" in Guest (ed.), *Oxford Essays in Jurisprudence* (1961), p.107.

47. To say that A's rights are "proprietary" means simply that they are capable of binding third parties, notwithstanding that certain parties particularly endeared to Equity may not be so bound.

48. See Honoré, fn.46 above.

49. *Oxford English Dictionary* (2nd edn, 1989), *www.oed.com.*

50. On the distinction between "use-value" and "wealth-value", see generally Rudden, "Things as Thing and Things as Wealth" (1994) 14 O.J.L.S. 81.

51. See Goode, fn.30 above at pp.114-115.

52. However, the word "fund" is not apt to describe every situation where ownership entitlements are partitioned between more than one party. An easement, for example, is not usually taken for the wealthvalue it represents in relation to the underlying asset, as opposed to the enjoyment of the use-value it permits.

53. Mokal, fn.26 above, at 394-395.

54. Text to fnn.17-18 above.

55. See IR 1986, r.4.181 and IA 1986, s.107 (directing liquidator to pay unsecured creditors from "assets" and "property" of the company respectively).

56. An attempt is made to deflect the force of this point by distinguishing fixed and floating charges on policy grounds (Mokal, fn.26 above, at 397-400). Fixed charges, it is said, are "true" priority devices, whereas floating charges are taken by bankers simply to secure control. The implication, it seems, is that bankers will suffer no real loss if floating charges are subordinated to liquidation expenses. Even assuming that as an empirical matter this is true, the response is a *petitio principii* : one of the very reasons that bankers have tended to obtain few recoveries from floating charge assets is that since *Barleycorn* this type of security has been subordinated to liquidation expenses. The mere fact that they have been treated as subordinated *because* of the Court of Appeal's decision cannot tell us anything about whether that decision was correct.

57. *Buchler v Talbot* [2004] UKHL 9; [2004] 2 A.C. 298 at [28]. See also *Re Lines Bros Ltd* [1983] Ch. 1 at 20.

58. IA 1986 ss.126, 130(2), 130(4); *Wight v Eckhardt Marine GmbH* [2003] UKPC 37; [2004] 1 A.C. 147 at [27].

59. *Food Controller v Cork* [1923] A.C. 647 at 670-671, *per* Lord Wrenbury.

60. IR 1986 rr.4.88, 12.3. A secured creditor may of course prove for the balance of his debt if there is a deficiency in his security, or may elect to surrender his security and prove as an unsecured creditor.

61. *Re David Lloyd & Co* (1877) 6 Ch.D. 339.

62. *Re Crigglestone Coal Co* [1906] 2 Ch. 327; *Re Demaglass Holdings Ltd* [2001] 2 B.C.L.C. 633 at 638.

63. IA 1986, ss.100, 139.

64. See *Re Adam Eyton Ltd* (1887) 36 Ch.D. 299 at 306; *Quickson (South & West) Ltd v Katz* [2004] EWHC 2443 (Ch) at [168].

65. See *Re Humber Ironworks and Shipbuilding Co* (1869) L.R. 4 Ch. App. 643 at 646; *Re Dynamics Corporation of America* [1976] 1 W.L.R. 757 at 761.

66. IR 1986, r.4.75(1)(b). That is, the date at which a winding-up order is made or at which the resolution was passed: IA 1986, s.247(2).

67. *Re Dynamics Corp* [1976] 1 W.L.R. 757 at 764.

68. *M.S. Fashions Ltd v B.C.C.I.* [1993] Ch. 425 at 434-435; *Stein v Blake* [1996] A.C. 243 at 256; *Wight v Eckhardt* [2003] UKPC 37; [2004] 1 A.C. 147 at [32].

69. See, e.g. *Re Northern Counties of England Fire Insurance Co, Macfarlane's Claim* (1880) 17 Ch.D. 337; *Re Dodds* (1890) 25 Q.B.D. 529; *Sovereign Life Assurance Co v Dodd* [1892] 2 Q.B. 573; *Stein v Blake,* fn.68 above; *B.C.C.I. (Overseas) Ltd v Habib Bank Ltd* [1998] 2 B.C.L.C. 459; *Wight v Eckhardt,* fn.68 above.

70. IR 1986, r.4.86(1).

71. *Re General Rolling Stock Co* (1872) L.R. 7 Ch. App. 644 at 648, 649, fn.68 above 650; *Ayerst v C. & K. Construction Ltd* [1976] 167 at 176-180; *Re Cases of Taffs Well Ltd* [1992] Ch. 179 at 191-192; *Wight v Eckhardt,* fn.68 above, at [22]. The ultimate beneficiaries will not be determined until the assets have been sold and all proofs of claim have been submitted. As a consequence of this uncertainty, an unsecured creditor is in a position akin to that of a residuary legatee prior to execution of a will: *Ayerst,* at 177-178.

72. IA 1986, s.127.

73. *British Eagle International Airlines Ltd v Cie Nationale Air France* [1975] 1 W.L.R. 758; *Money Markets International Stockbrokers Ltd v London Stock Exchange Ltd* [2002] 1 W.L.R. 1150.

74. *Re Celtic Extraction Ltd* [2001] Ch. 475 at 486-489.

75. See Goode, fn.2 above at pp.140-153.

76. [1899] 1 Q.B. 612.

77. *Re Carl Hirth* [1899] 1 Q.B. 612 at 624.

78. *Re David Lloyd & Co* (1877) 6 Ch.D. 339; *Re Henry Pound, Son & Hutchins* (1889) 42 Ch.D. 402; *Re Wanzer Ltd* [1891] 1 Ch. 305 at 314.

79. *Re David Lloyd* (1877) 6 Ch.D. 339 at 344, 345, 346; *Re Henry Pound* (1889) 42 Ch.D. 402 at 421, 422; *Strong v Carlyle Press* [1893] 1 Ch. 268 at 274, 275, 276.

80. (1890) 44 Ch.D. 534 at 577-578.

81. *Re Margart Pty Ltd* [1985] B.C.L.C. 314; *Re French's (Wine Bar) Ltd* [1987] B.C.L.C. 499.

82. IR 1986, r.4.88(2). He is, of course, entitled to prove insofar as his claim exceeds the estimated value of his security (r.4.88(1)). The hindsight principle also applies to this valuation: once he has enforced his security, he must revise his estimate of the its value according to the actual sum realised from sale, which is then used to calculated the deemed value of the unsecured portion of his claim as at the date of the winding-up (r.4.99).

83. Moreover, the commencement of liquidation does not stop the running of the limitation period for secured debts, as it does automatically for unsecured claims: *Financial Services Compensation Scheme Ltd v Larnell (Insurances) Ltd* [2005] EWCA Civ 1408 at [23]-[24]; *cf. Re General Rolling Stock Co Ltd* (1872) L.R. 7 Ch. App. 646.

84. What “belongs” to the debenture-holder is not, of course, the underlying assets, but rather the entitlement to have them realised and the proceeds appropriated for his benefit: see *Baker v Archer-Shee* [1927] A.C. 844.

85. See, e.g. *Re David Lloyd* (1877) 6 Ch.D. 339 at 344; *Strong v Carlyle Press* [1893] 1 Ch. 268 at 276; *Re Aro Co Ltd* [1980] Ch. 196 at 204; *Re Atlantic Computers Plc* [1992] Ch. 505 at 520.

86. [1990] B.C.C. 78.

87. IA 1986, s.238(4).

88. [1990] B.C.C. 78 at 90.

89. Mokal, fn.26 above, at 394, 403.

90. IA 1986, s.240.

91. Goode, fn.2 above, at pp.436-438.

92. To be sure, if liquidation were to supervene, the grant of a charge for past value will have depleted the assets available to the unsecured creditors. Yet this is not the mischief to which s.238 is directed. Such transactions are the domain of ss.239 and 245, which are limited respectively to transactions effected under the influence of a desire to prefer the counterparty, and grants of floating charges. In contrast, s.238 is concerned with the overall size of the pie, rather than the way in which it is sliced up amongst the creditors: see Armour, “Transactions at an Undervalue” in Armour and Bennett, *Vulnerable Transactions in Corporate Insolvency* (2003), at pp.37, 71.

93. [2004] UKHL 9; [2004] 2 A.C. 298 at [28], *per* Lord Hoffmann. See also at [51], *per* Lord Millett.

94. *Ibid.* at [31].

95. *Re Pantmaenog Timber Co Ltd* [2003] UKHL 49; [2004] 1 A.C. 158.

96. Mokal, fn.26 above, at 401-403.

97. This second objection also proves too much. If floating charge-holders obtain a “free ride” on the liquidator's pursuit of the public interest, so too do many other parties, including fixed charge-holders, retention of title claimants, leasing financiers and the like. Yet no one argues that they should be required to contribute to the expenses of liquidation.

98. See, e.g. *Regentcrest Ltd v Cohen* [2001] 2 B.C.L.C. 80 at 111.

99. *Foss v Harbottle* (1843) 2 Hare 641; *Prudential Assurance v Newman Industries (No.2)* [1982] Ch. 204 at 210-225.

100. *Re Saul D. Harrison & Sons Plc* [1995] 1 B.C.L.C. 14 at 18; *O'Neill v Phillips* [1999] 1 W.L.R. 1092; *Clark v Cutland* [2003] EWCA Civ 810; [2004] 1 W.L.R. 783.

101. *Re Pantmaenog Timber Co Ltd* at [83], *per* Lord Walker of Gestingthorpe.

102. That is, for misfeasance, wrongful and fraudulent trading, and transactions tending to undermine the interests of creditors.

103. This includes not only the “winding-up offences” of fraud in anticipation of and during winding-up (IA 1986, ss.206-211) and re-use of a prohibited corporate name (s.216) but any offence relating to the conduct of the company's affairs--including offences under the companies legislation such as failure to keep accounting records (CA 1985, ss.221-222), fraudulent trading (s.458) or being concerned in the management of a company whilst disqualified, bankrupt or subject to bankruptcy restrictions (CDDA 1986, ss.11, 13) and general offences such as theft, obtaining a pecuniary advantage by deception and false accounting.

104. IA 1986, s.132. He must in the first instance report to the court, although where it appears criminal offences may have been committed, the court may direct the matter to be referred to the Secretary of State for prosecution (IA 1986, s.218(1)).

105. Prior to 1929, prosecutions in liquidation were initiated at the discretion of the liquidator and funded from liquidation expenses. It is unsurprising that few such prosecutions were launched. See Keay, *McPherson's Law of Company Liquidation* (2001), at p.853.

106. IA 1986, ss.133, 236.

107. IR 1986, r.4.218(a)(i),(b),(c),(d)(i).

108. See also Insolvent Companies (Reports on Conduct of Directors) Rules 1996 (SI 1996/1909).

109. On what types of conduct may render a director "unfit", see CDDA, s.9 and Sch.1. In addition, ss.2-5 and 8 provide for discretionary disqualification on a variety of grounds, e.g. following conviction of certain criminal offences. See generally Walters and Davis-White, *Directors' Disqualification and Bankruptcy Restrictions* (2nd edn, 2004).

110. See fn.107 above. Moreover, office-holders may be permitted to use the private examination procedure in IA 1986, s.236 to obtain information or documents from relevant parties with a view to discharging their reporting obligation: *Re Pantmaenog Timber Co Ltd* [2003] UKHL 49; [2004] 1 A.C. 158.

111. *Re Grayan Building Services Ltd* [1995] Ch. 241; *Re Westmid Packing Services Ltd* [1998] 2 All E.R. 124.

112. DTI, *Companies in 2003-2004* (2004), at p.44 (Table D1). The majority of these disqualifications were procured through the offer and acceptance of undertakings, a procedure introduced by the Insolvency Act 2000 which makes it possible for directors to be disqualified without the need for court proceedings: see CDDA, s.7(2A); Walters and Davis-White, fn.109 above, Ch.9.

113. In 2002 there were approximately 200 convictions, following about 500 reports submitted pursuant to IA 1986, s.218: Insolvency Service, *General Annual Report for the Year 2002* (2003), at pp.10-11 (Table 4).

114. Moreover, where there are insufficient assets to cover the official receiver's expenses, the shortfall will be borne by the state.

115. To be sure, all civil litigation gives rise to a public good--in the form of precedents (see Landes and Posner, "Legal Precedent: a Theoretical and Empirical Analysis" (1976) 19 J.L. & Econ. 249; Brunet, "Measuring the Costs of Civil Justice" (1985) 83 Mich. L.Rev. 916 at 933-934). This aspect of insolvency proceedings may therefore amount only to a difference of degree, rather than in kind, from ordinary civil litigation.

116. IA 1986, s.45(2).

117. See generally, Finch, "Re-Invigorating Corporate Rescue" [2003] J.B.L. 527; Frisby, "In Search of a Rescue Culture--the Enterprise Act 2002" (2004) 67 M.L.R. 247; Armour and Mokal, "Reforming the Governance of Corporate Rescue: the Enterprise Act 2002" [2005] L.M.C.L.Q. 32.

118. IA 1986, Sch.B1, para.99.

119. IA 1986, s.212. See generally, Oditah, "Misfeasance Proceedings against Company Directors" [1992] L.M.C.L.Q. 207.

120. IA 1986, ss.213, 214, respectively. See generally, Prentice, "Creditors' Interests and Directors' Duties" (1990) 10 O.J.L.S. 265; Oditah, "Wrongful Trading" [1990] L.M.C.L.Q. 205; Mokal, "An Agency Cost Analysis of the Wrongful Trading Provisions" (2000) 59 C.L.J. 335; Milman, "Strategies for Regulating Managerial Performance in the 'Twilight Zone'" [2004] J.B.L. 493.

121. E.g. IA 1986, ss.127, 238, 239, 245. See generally, Parry, *Transaction Avoidance in Insolvencies* (2001); Armour and Bennett (eds), *Vulnerable Transactions in Corporate Insolvency* (2003).

122. See, e.g. Oditah, fn.120 above at 215-220; Walters, "Foreshortening the Shadow: Maintenance, Champerty and the Funding of Litigation in Corporate Insolvency" (1996) 17 Co. Law. 165; Parry, "The Destination of Proceeds of Insolvency Litigation" (2002) 23 Co. Law. 49; Tolmie, "Funding Litigation by Liquidators" [2003] Ins. Law. 153; Gregorian and Butler, "Liquidators' Litigation Expenses, Funding Arrangements and the Amendment to Rule 4.218" (2004) 20 Ins. L. & P. 151.

123. Champerty is a doctrine that seeks to prevent non-parties from acquiring a stake in other people's litigation because of a fear that such arrangements could compromise the administration of justice: see *R. (on the application of Factortame Ltd) v Secretary of State for the Environment (No.8)* [2002] EWCA Civ 932; [2003] Q.B. 381 at [31]-[44]; Walters, *ibid.*

124. [1895] 2 Ch. 891.

125. [1935] 1 Ch. 395.

126. [1935] 1 Ch. 395 at 396.

127. The judge's other ground, namely that the charge had crystallised before the preference recoveries were got in, seems dubious, for property acquired by a chargor after crystallisation is still caught by an after-acquired property clause: *Holroyd v Marshall* (1862) 10 H.L. Cas. 191; *N.W. Robbie & Co Ltd v Witney Warehouse Co Ltd* [1963] 1 W.L.R. 1324. See Oditah, fn.120 above at 220.

128. [1991] Ch. 127. See also *Re Oasis Merchandising Services Ltd* [1998] Ch. 170; *Re R.S. & M. Engineering Co Ltd (No.2)* [2000] Ch. 40; *Re Floor Fourteen Ltd* [2001] 3 All E.R. 499; *Re Demaglass Ltd* [2002] EWHC 3138 (Ch); [2003] 1 B.C.L.C. 412.

129. On the s.238 aspect of the case see above, text to fnn.86-92.

130. [1991] Ch. 127 at 134.

131. CPR, r.44.3(2). The importance of the principle lies in its deterrence of spurious claims, and the protection it thereby guarantees from such litigation: Andrews, *English Civil Procedure* (2003), at pp.116-117.

132. See also *Re R.S. & M. Engineering Co Ltd (No.2)* [2000] Ch. 40.

133. [1991] Ch. 127 at 137.

134. IR 1986, r.4.218(1)(a) (emphasis added).

135. [1998] Ch. 170.

136. Although the liquidator remained the nominal claimant, the agreement conferred significant rights on the funder concerning the control and conduct of the proceedings.

137. IA 1986, Sch.4, para.6; *Seear v Lawson* (1880) 15 Ch.D. 426; *Re Park Gate Waggon Works Co* (1881) 17 Ch.D. 234; *Ramsey v Hartley* [1977] 1 W.L.R. 686; *Re Oasis Merchandising Services Ltd* [1998] Ch. 170; *Elfic Ltd v Macks* (2001) 162 F.L.R. 41; Walters, fn.122 above.

138. [1998] Ch. 170 at 181.

139. [1997] 2 B.C.L.C. 579 at 586-588, 595-596.

140. [2001] 3 All E.R. 499.

141. Insolvency (Amendment) (No.2) Rules 2002 (SI 2002/2712) (emphasis added). As a quid pro quo, designed to limit the scope for speculative or hopeless claims, the liquidator must obtain court or creditors' committee sanction before bringing proceedings under ss.213, 214, 238, 239, 242, 243 or 423: IA 1986, ss.165(2), 167(1); Sch.4, para.3A (inserted by Enterprise Act 2002, s.253); IR 1986, r.4.184.

142. The court would be forced to reason that the costs were not “properly chargeable or incurred”: Tolmie, fn.122 above.

143. Actions for misfeasance were of course treated as property of the company: see text to fn.124, above.

144. In *Oasis,* it was suggested obiter that a liquidator should be allowed to “sell the fruits of an action” but only if the funder were to have no rights “to influence the course of, or to interfere with the liquidator's conduct of, the proceedings” ([1998] Ch. 170 at 186). In the context, it appears that the Court was referring to *corporate* rights of action rather than office-holder actions (see *Elfic Ltd v Macks* (2001) 162 F.L.R. 41 at 78). It is difficult to see how the court could have had office-holder actions in mind given the holding that the liquidator has no statutory power to sell the fruits of office-holder actions. Either way, it is doubtful that commercial funders would be prepared to support actions without control rights that allow them to manage their exposure.

145. [2004] UKHL 9; [2004] 2 A.C. 298 at [86].

146. See text to fnn.15-16, above. See also Prentice, “The Effect of Insolvency on Pre-Insolvency Transactions” in Pettet (ed.), *Company Law in Change: Current Legal Problems* (1987).

147. Text to fnn.93-94, above.

148. [1895] 2 Ch. 891 at 893-894.

149. *Ibid.*

150. The secured creditor should fare no better under insolvency law than under the general law: Jackson, *The Logic and Limits of Bankruptcy Law* (1986), at pp.21-27.

151.

See Oditah, fn.120 above, at 218-219.

152.
A point developed below, Section 0.

153.
See *Re Pyle Works* (1889) 44 Ch.D. 534, esp. Lindley L.J. at 584 (concluding that a company was able to charge its uncalled capital precisely because the making of calls was a matter ordinarily within the control of the directors, as opposed to a claim which by virtue of the statutory scheme was payable only on a winding-up). See also Russell L.J.'s analysis of *Yagerphone* in *Robbie v Witney Warehouse* [1963] 1 W.L.R. 1324 at p.1338: "a statutory right in and only in the liquidator to make such a claim could never have been property of the company *subject to the charge.* " (emphasis added).

154.
See Armour, fn.92 above, at pp.90-92.

155.
This would be subject to pro rata deduction of the liquidator's costs: see *Re Anglo-Austrian Printing and Publishing Union* [1895] 2 Ch. 891.

156.
Similar consequences should follow where the debenture-holder takes no steps to enforce, effectively waiving any surviving proprietary rights: see *G. & M. Aldridge Pty Ltd v Walsh* (2001) 203 CLR 662, noted (2003) 119 L.Q.R. 34.

157.
See *N.A. Kratzmann Pty Ltd v Tucker (No.2)* (1968) 123 C.L.R. 295 at 300-301. This may in turn explain why in *Yagerphone,* Bennett J. was at pains to emphasise that the charge had not crystallised at the time the money used to make the preferential payment: [1935] 1 Ch. 395 at 396. Presumably he regarded the payment as having been made in "the ordinary course of business" with the consequence that the money had left the charge and the chargee had no remaining rights in relation to it. See also *Ashborder BV v Green Gas Power Ltd* [2004] EWHC 1517 at [227].

158.
See Mokal, fn.26 above, at 402.

159.
See text to fnn.128-138, above.

160.
There is every reason to suppose that the phrase "assets of the company" in IA 1986, ss.115, 175 bears the same meaning as the "company's property" in relation to the liquidator's statutory power of sale in Sch.4, para.6. After all, it would be odd if the power of sale did not encompass selling the "assets of the company" for the benefit of unsecured creditors.

161.
Cf. Mokal, fn.26 above.

162.
See Gregorian and Butler, fn.122 above.

163.
By virtue of IA 1986, s.436, "company property", meaning the free assets, extends to "… every description of interest, whether present or future or vested or contingent …"

164.
Young v Bristol Aeroplane Co Ltd [1944] K.B. 718; *Midland Bank Trust Co Ltd v Hett, Stubbs & Kemp* [1979] Ch. 384.

165.
The claim in the text is that *Buchler* impliedly overrules *Oasis* on the question of the liquidator's *vires.* The propriety of the exercise of the liquidator's powers is a separate matter: see *Elfic v Macks Ltd* (2001) 162 F.L.R. 41 at 59-60, 78; *Anc Ltd v Clark Goldring & Page Ltd* [2001] B.C.C. 479 at 485. There is scope for argument as regards the terms of any assignment, especially over the extent to which control of the litigation could legitimately be ceded to the funder. On the question of propriety, the court would need to strike a balance between two legitimate policy concerns: the liquidator's need for access to justice and the court's need to protect the integrity of its own process. See *Abraham v Thompson* [1997] 4 All E.R. 362; *Stocznia Gdanska SA v Latreefers Inc* [2001] 2 B.C.L.C. 116 and *Elfic v Macks,* fn.144 above, where, *post-Oasis,* the courts have tended to give greater weight to access to justice.

166.
It is a separate point that sometimes restoration of the *status quo ante* may involve restoring to secured creditors assets that comprise part of their security: see Armour, fn.92 above, at pp.90-92.

167.
Company Law Reform Bill 2005 (HL Bill 34), cl.868. The Explanatory Notes simply recite that the clause is intended to reverse *Buchler* (HL Bill 34-EN, para.1679).

168.
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169.
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170.
Corporate insolvency; Creditors; Expenses; Floating charges; Liquidation; Priorities

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