[2020] EWHC 2370 (Ch) **CR-2019-004456**

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
INSOLVENCY AND COMPANIES LIST (ChD)

Rolls Building, Fetter Lane,
London EC4A 1NL
Thursday, 3 September 2020

Before

HIS HONOUR JUDGE SIMON BARKER QC

IN THE MATTER OF RHINO ENTERPRISES PROPERTIES LIMITED

IN THE MATTER OF ASKWITH INVESTMENTS LIMITED

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

Between

(1) ROBERT NICHOLAS JASON SCHOFIELD
(2) RHINO ENTERPRISES HOLDINGS LIMITED

Applicants

-and-

(1) MATTHEW DAVID SMITH
(2) CLARE BOARDMAN

Respondents

Representation

Stephen Davies QC and **Neil Levy** (instructed by **Knights plc**) for the Applicants

Tom Smith QC and **Hannah Thornley** (instructed by **Stephenson Harwood LLP**) for the Respondents

Hearing date : 5 March 2020

JUDGMENT

Covid-19 protocol : This judgment was handed down remotely by circulation to the parties' representatives by email, release to BAILII and publication on the Courts and Tribunals website. The deemed time and date for hand down are 3.15pm on 3 September 2020

I direct that pursuant to CPR 39APD6 paragraph 6.1 no tape recording shall be made of this judgment and that copies of this version shall stand as authentic and be treated as the official transcript

HHJ Simon Barker QC :

Introduction

1 By this application the Applicants ('the AAs') seek an order that they be given permission under paragraph 75 of Schedule B1 to the Insolvency Act 1986 (respectively 'paragraph 75', 'Sch.B1' and 'IA 1986') to pursue an application against the Respondents as former joint administrators ('the JAs'). The application has already been issued, accordingly permission is sought - as it may be - retrospectively. The application is based on allegations that the JAs breached their fiduciary and other duties as administrators and/or have been guilty of misfeasance. The JAs have obtained their discharge under paragraph 98 of Sch.B1 to the IA 1986. Consequently, paragraph 75(6) of Sch.B1 is engaged, or potentially engaged, in that such an application may only be made with the permission of the court. It is common ground that the AAs are contributories and, in principle, have standing under paragraph 75(2)(e) of Sch.B1 to make such an application; however, the JAs contend that on the facts the AAs are bound, first, by their contrary conduct as members and, secondly, by an express undertaking not to bring any such claim.

2 A central issue or question in this application ('the CRTPA issue') is whether a company voluntary arrangement ('CVA') is a contract for the purposes of the Contract (Rights of Third Parties) Act 1999 ('the 1999 Act'). So far as relevant, s.1 of the1999 Act provides :

> "1(1) Subject to the provisions of this Act, a person who is not a party to a contract (a "third party") may in his own right enforce a term of the contract if-
>
> (a) the contract expressly provides that he may, or
>
> (b) subject to subsection (2), the term purports to confer a benefit on him.
>
> (2) Subsection 1(b) does not apply if on a proper construction of the contract it appears that the parties did not intend the term to be enforceable by the third party.
>
> (3) The third party must be expressly identified in the contract by name, as a member of a class or as answering a particular description …".

There is no definition of "contract" in the 1999 Act. The JAs contend that, on the

authorities, CVAs are contracts and, therefore, that the 1999 Act applies to CVAs. The AAs accept that for some purposes CVAs are treated as if they are contracts, and it is common ground that the principles of construction applicable to contracts apply to the interpretation of the terms of CVAs, but the AAs maintain that CVAs derive their legal force from statute, not the law of contract. That said, the AAs accept that if a CVA is a contract and the 1999 Act applies the JAs satisfy the qualification criteria at s.1(1)(a) and (b) in that they are expressly identified in the relevant CVAs ('the CVA') and that a particular clause ('cl.24.1') purports to confer a benefit on the JAs. However, and by reference to s.1(2) of the 1999 Act, the AAs do not accept that on its proper construction the terms of cl.24.1 of the CVA are enforceable; further, the AAs do not accept that they are parties to the CVA.

3 The benefit purportedly conferred by cl.24.1 in the CVA, which is a release clause in favour of the JAs, is in the following terms :

> "Each Creditor and the Companies[1] will release and undertakes not to bring a claim against the Administrators, their firms, fellow members, partners and employees, the legal and other professional advisors to the Administrators, and their fellow members, partners and employees from any Liability (whether present, future, prospective or contingent) arising in connection with :
>
> (a) their acts, omissions or defaults as administrators or advisors since the Administration Date; and/or
>
> (b) the preparation, negotiation and implementation of the Arrangement or any matter ancillary to the Arrangement".

4 For present purposes the application is not challenged on the basis that it is unmeritorious. Mr Smith QC, who appeared with Ms Thornley for the JAs, made clear that that is not a concession on the JAs' part other than for the purposes of this permission application. Mr Davies QC, who appeared with Mr Levy for the AAs, acknowledged that if permission is given it will still be open to the JAs to seek summary judgment under CPR 24 on the basis, which is the JAs' position, that the application is totally without merit.

Background

5 As to the relevant factual background, the First Applicant, Mr Jason Schofield ('JS'), is the controlling shareholder of the Second Applicant, Rhino Enterprises

[1] Rhino Enterprises Limited, Rhino Enterprises Properties Limited and Askwith Investments Limited.

Holdings Limited ('REHL'). REHL's group structure comprises or includes two subsidiary companies, Rhino Enterprises Limited ('REL') and Rhino Enterprises Properties Limited ('REPL'); the former is an operating company and the latter a property holding or property investment company. JS is also the controlling shareholder of Askwith Investments Limited ('AIL'). These companies carried on a document storage, self-storage, and related activities business. From about 2007 JS financed the purchase of properties with loans from Barclays Bank plc ('Barclays'). Barclays required JS to hedge against the risk of adverse interest rate changes through its interest 'swap' products ('the Swaps'). Barclays' security for the property loans and Swaps included floating charges over the undertakings of REL, REPL and AIL (collectively 'the Companies').

6 In 2013, and based on advice from leading counsel with expertise in interest swaps, JS was advised that there was a 60% chance of succeeding in a claim against Barclays based on LIBOR manipulation and mis-selling of the Swaps. On 29.5.13 the Companies, by their then solicitors, sent letters of claim to Barclays ('the Swaps Claims') asserting a right to rescind the Swaps. By letter dated 4.7.13 the Swaps were rescinded. Between 13.7.13 and 13.8.13 Barclays rejected the Swaps Claims, served a default notice on REPL and AIL, and, on 13.8.13, demanded repayment of property loans and sums claimed under the Swaps totalling £20.9m. On 14.8.13, the next day, Barclays, as holder of a floating charge, appointed the JAs as administrators of the Companies.

7 The JAs, Mr Matthew Smith ('MS') and Ms Clare Boardman ('CB'), are partners in and members of Deloitte LLP. On the facts alleged in the Draft Particulars of Claim ('the Draft P/C'), the JAs were provided with the advice obtained from specialist leading counsel as to the prospects of succeeding in the Swaps Claims but obtained their own advice from solicitors which put the chances of success of the Swaps Claims at just less than 50%, an important difference in the context of litigation funding and insurance. In consequence, the JAs accepted Barclays' claim to be owed £20.9m.

8 On 4.10.13 the JAs issued their statement of proposals pursuant to paragraph 49 of Sch.B1. By letters dated 10.12.13 and 11.12.13, which followed a meeting on 4.12.13, the AAs' then solicitors wrote to solicitors for the JAs setting out the AAs' complaints against the JAs for breach of duties and attempting to persuade the

JAs not to exchange contracts for the sale of REPL's and AIL's properties representing almost 90% in value of their pre-administration property portfolios. These letters expressly referred to claims under paragraph 74 and paragraph 75 of Sch.B1. The JAs' then solicitors rejected the complaints on the basis that the JAs considered that it was in the interests of the Companies' creditors as a whole to achieve the certain and expedited sale of the properties at the currently offered market value. The JAs proceeded to sell the properties from REPL's and AIL's portfolios.

9 In 2014 JS persuaded Barclays to agree that the Companies could exit their respective administrations through CVAs, the terms of which were to include that Barclays' indebtedness would be reduced by £663k, which was the balance claimed by Barclays as owing, and JS could proceed with the Swaps Claims.

10 The JAs, or their solicitors on their instructions, prepared a combined CVA proposal for the Companies which they circulated on 9.6.14. The JAs draw attention to an email from JS on 9.6.14 stating that he had "no objection to the CVA proposal being issued in tonight's post". The proposal recites that JS, with the support of Barclays, had approached the JAs with proposals to allow the companies to exit administration through the CVA. From the first draft, the CVA contained a release clause in the terms of cl.24.1. CB's evidence is that she is not aware of any objection being taken at the time to cl.24.1. On 23-24.6.14, following several intermediate drafts and a final draft prepared and circulated by the JAs, JS signed proxy consents as the shareholder in AIL and indirect controlling shareholder in REPL and REL and also on behalf of himself and connected companies as creditors of the Companies. At meetings chaired by CB on 25.6.14, and after a modification proposed by HMRC to increase the dividend for unsecured creditors from 25p/£1 to 33p/£1, the CVA was approved unanimously by the Companies' creditors and by their members. JS voted in favour of the CVA in respect of each company as a creditor and, in respect of AIL, as its sole shareholder. REHL voted in favour of the CVA as REL's and REPL's sole shareholder.

11 The 28 day period for challenging the CVA on the grounds of unfair prejudice and/or material irregularity passed without any application being made under s.6 IA 1986. The Companies were returned to the control of their directors on 1.8.14. The administrations came to an end on 13.2.15 and, after payment of the 33p/£1

to unsecured creditors, the CVA came to an end on 22.6.15.

12 During 2015 the Companies issued proceedings against Barclays for the Swaps Claims; these proceedings were settled on confidential terms on 1.12.15.

13 In separate proceedings the solicitors who advised the JAs about the prospects of succeeding on the Swaps Claims are being sued for professional negligence. Those proceedings are stayed pending the outcome of this application.

14 By proceedings issued on 9.8.19, for which retrospective permission is now sought, the AAs seek to challenge the JAs' bona fides and conduct.

15 The essence of the AAs' complaint and claim is that (1) the JAs (a) should not have accepted the administration appointment because of a close relationship through which Barclays enjoyed the upper hand or "informal control"[2] and/or (b) having accepted the appointment, acted in breach of duty because their close relationship with Barclays disabled them from exercising sufficient independence to properly investigate, pursue, and litigate the Swaps Claims against Barclays; and, (2) had the Swaps Claims been properly pursued, the Companies' liabilities would have been extinguished or reduced to a level which could have been refinanced. Thus, the claim concerns allegations of breaches of fiduciary, common law, and statutory duties owed to and misfeasance against the Companies giving rise to an obligation to provide compensation under paragraph 75(4) to the assets of REPL and AIL. The AAs seek compensation of £18.668 million. Alternatively, the AAs claim a contribution of around £212k reflecting the cost of the JAs' solicitors' advice against the likelihood of success on the Swaps Claims.

16 In evidence in response to the application CB says that the JAs relied on the inclusion of cl.24.1. The JAs had been the subject of allegations in correspondence, which they regarded, and regard, as unfounded and were concerned that once out of office they would be without access to funds. CB observes that they now face similar allegations to those made before the CVA and intended to be covered by cl.24.1.

The Issues

[2] Defined at [19] of the Draft P/C

17 The following issues emerged from the skeleton arguments and submissions during the hearing :

(1) Should the CRTPA issue be determined or is it sufficient to dispose of the application by deciding whether the AAs have a real prospect of persuading the court at a trial that cl.24.1 does not provide a defence to a misfeasance application under paragraph 75 of Sch.B1?
(2) The CRTPA issue. Is a CVA a contract for the purposes of the 1999 Act? Is cl.24.1 of the CVA directly enforceable by the JAs? Can non-parties enforce the terms of the CVA?
(3) Can the AAs apply as a contributory given that they voted in favour of the CVA as members and creditors?
(4) If otherwise potentially capable of applying to an application under paragraph 75, is cl.24.1 of the CVA ineffective in equity as a provision intended by the JAs to secure a personal benefit outside the scope and purpose of the CVA?
(5) Are the AAs estopped from denying the binding effect of cl.24.1 for the purpose of paragraph 75 of Sch.B1?

The IA 1986 framework for CVAs

18 CVAs were introduced by the IA 1986 to provide a more economical and less complex method of restructuring the debts of a company than provided for under the companies' legislation, then the Companies Act 1948 and now the Companies Act 2006 at Pt 26 ('CA 2006'), by compromises or arrangements.

19 A CVA is a composition or a scheme of arrangement based on a proposal put forward by directors, an administrator or a liquidator depending on whether or not the company is or is not in administration or in the course of being wound up (s.1 IA 1986). If, as in this case, the company is in administration it is for the administrator(s) to put forward a proposal for a CVA. The proposal is put to a meeting of the company and to the company's creditors for consideration and approval (s.3 IA 1986). The company and its creditors consider and decide whether or not to approve the proposed arrangement with or without modifications. What may be proposed and the scope for modifications is almost open ended. Requirements as to general principles and format and content are set out in insolvency rules, then the Insolvency Rules 1986 at Pt 1, now the Insolvency (England and Wales) Rules 2016 at Pt 2. Beyond that, statutory

constraints are imposed by s.4(3) and (4) IA 1986. By s.4(3) the rights of a secured creditor to enforce the security may not be affected without the secured creditor's concurrence. By s.4(4) the priority and/or ranking of preferential debts may not be affected without that preferential creditor's concurrence. Those matters apart, the essential feature is some degree of give and take between the company and its creditors. In addition, there is an expectation that the proposal will be considered by the proposer acting properly to be fair to all creditors and to the company. A CVA may be challenged on the grounds that it unfairly prejudices the interests of a creditor, member or contributory and/or that there has been some material irregularity at or in relation to the meeting or the relevant qualifying decision procedure (s.6 IA 1986).

20 The requisite majority for creditors' approval of a CVA is 75% or more in value of those present or represented at the meeting voting in favour. For members, subject to the provisions of a company's articles, a proposal is approved once a simple majority in voting rights of those voting have voted in favour. Provided it is approved by the requisite majority, a CVA takes effect under s.5(2) IA 1986 as follows :

"The voluntary arrangement-

(a) takes effect as if made by the company at the creditors' meeting, and

(b) binds every person who in accordance with the rules-

(i) was entitled to vote at that meeting (whether or not he was present or represented at it), or

(ii) would have been so entitled if he had had notice of it,

as if he were a party to the voluntary arrangement".

The effect of s.5(2) is that, once formally approved, the company and all creditors are bound to its terms.

Issue 1 : Should the CRTPA issue be determined or is it sufficient to dispose of the application by deciding whether the AAs have a real prospect of persuading the court at a trial that cl.24.1 does not provide a defence to a misfeasance application under paragraph 75 of Sch.B1?

21 This issue raises for consideration together the nature of an application under paragraph 75(6) and the proper approach to summary determination of an issue.

22 As to paragraph 75(6), both Mr Davies QC and Mr Smith QC referred to Katz v Oldham [2016] BPIR 83 at [4]-[12] and Mr Davies QC further referred to Hyde v Bannon [2018] EWHC 901 (Ch). Mr Smith QC also referred to Brown v Beat [2002] BPIR 421 and the Court of Appeal decision in Parkinson Engineering Services plc v Swan [2010] BCLC 163 approving and applying the decision in Brown v Beat.

23 It is common ground that the authorities identify two principal criteria : (1) the need to show a reasonably meritorious cause of action and (2) whether giving permission is reasonably likely to result in a benefit to the estate. As stated by Lloyd LJ in Parkinson at [34], those are not exhaustive criteria but they are certainly relevant and likely to be among the most important factors.

24 As noted in Katz at [10], the policy reason for requiring permission is to provide a level of protection from unmeritorious claims to former officeholders because they no longer enjoy access to the company's assets for indemnification. Thus, the test is similar to, but not the same as, that for summary judgment and it is not necessary for a court to be satisfied, before granting permission, that no summary judgment application by a respondent could succeed. In Hyde Mr Trower QC, sitting as a Deputy High Court Judge, reviewed the authorities and observed, at [30], that in most cases the test equates to asking whether a reasonable litigant would commence and pursue the claim. As with summary judgment applications, it is also not appropriate for the court to embark on a mini trial, Hyde at [42].

25 On the point of whether it is sufficient to dispose of the application by limiting consideration of the CRTPA issue rather than deciding it, Mr Davies QC drew attention to the judgment of Lewison J in Easyair Ltd v Opal Telecom Ltd [2009] EWHC 339 (Ch) at [15] and the observation thereon by Floyd LJ in TFL Management Services Ltd v Lloyds Bank TSB plc [2014] 1 WLR 2006 at [27]. In Easyair Lewison J made the point that if a short point of law arises and all the evidence necessary for proper determination is available to the court and the parties have had an adequate opportunity to address it in argument the court should "grasp the nettle and decide it". The reason is that it is in the interests of justice to decide unanswerable and, conversely, hopeless points sooner rather than later and cases should not be allowed to go to trial on the basis of

Micawberism. The caution added by Floyd LJ is that difficult points of law, particularly those in developing areas, are better suited to decision in the context of actual, rather than assumed, facts; but, Floyd LJ also observed that it might be different where "the trajectory of the law will never on any view afford a remedy".

26 Both Mr Davies QC and Mr Smith QC argued the CRTPA issue fully and on the basis that each was unquestionably correct in their respective opposing views and submissions. If the claim is reasonably meritorious and, if permitted to continue, reasonably likely to result in a benefit to the estates of REPL and/or AIL, that suffices for a reasonable litigant to cross the threshold and commence and pursue the claim.

27 Mr Davies QC observed that this is the first case concerning the jurisdictional scope of CVAs including a release clause and commented that these are deep waters. I understand this to be a reference to the likely level of interest on the part of insolvency practitioners; and, also, that Mr Davies QC was placing a marker that this area of the law is still developing. Mr Davies QC submitted that there should be no final finding on the point for reasons including that the AAs contend that the release in cl.24.1 is a fraud on a power which renders it unsuitable for summary determination because the AAs require to cross-examine the JAs about their alleged breach of fiduciary duty at a trial. Mr Davies QC submitted that there is no need to grasp any nettle and whether the claim is susceptible to summary judgment on a respondent's application is for another day.

28 Mr Smith QC did not contend that the evidence was incomplete or that there had not been an adequate opportunity to address it in argument; nor did he submit that the issue should, or would, be better left to decision at the trial. Mr Smith QC's position was that the issue was fully prepared for and argued out, and it could and should be decided. Indeed, Mr Smith QC's submission was that there can be no doubt as to the legal validity of a release clause in an arrangement whether under CA 2006 or IA 1986, as to which there is no relevant difference, or to the meaning and effect, i.e. the applicability, of the cl.24.1 release to the CVA.

29 Given the conviction with which the opposing submissions were made, I consider that the most sensible approach is to consider the arguments and decide the point if I come to the conclusion that one or other of Mr Davies QC and Mr Smith QC is

unquestionably correct. However, if I (1) harbour doubts or, more accurately, if I consider that a reasonable litigant would commence and pursue the claim but am not able to decide the issue on the available material, and/or (2) consider this to be a developing area of the law, and/or (3) am not in a position to conclude that the trajectory of the law will inevitably lead to only one conclusion, I should leave the issue over to trial if, after considering all the issues raised on this application, I decide that permission should be given. If I decide against giving permission then the AAs' application against the JAs will be dismissed. In this context it is relevant to keep in mind that a conclusion based on the clear outcome of incomplete material should not give rise to a conclusive decision although it may found a provisional view.

Issue 2 : The CRTPA issue : Is a CVA a contract for the purposes of the 1999 Act? Is cl.24.1 of the CVA directly enforceable by the JAs? Can non-parties enforce the terms of the CVA?

30 Mr Davies QC began by distinguishing between what a CVA is and what it is not. Its subject matter is claims against a company, that is a company's liabilities to its creditors. It is not concerned with the position of a company vis a vis its debtors, that is compromising or making arrangements concerning its claims against its debtors. The JAs are not creditors of the Companies, rather they are outsiders in the position of debtors (or, more accurately in my view, contingent debtors) because the Companies, or REPL and AIL, have, and have notified, claims against them. The JAs had no right to participate in the CVA. Crucially, they had no right to - and did not - vote, rather they were officeholders charged with the duty to propose an arrangement which would be regarded as objectively fair to the creditors and the Companies. The JAs, not being parties to the CVA, are outsiders and the CVA's terms are not enforceable by non-parties.

31 Mr Davies QC submitted that the focus of any release proposed by the JAs should only have been by the creditors of the Companies' liabilities for the benefit of the Companies, not by the Companies of their debtors to the detriment of both the Companies and the creditors. In Mourant & Co Trustees Ltd v Sixty UK Ltd (in administration) [2010] EWHC 1890 (Ch) Henderson J, after observing that the CVA in that case should never have seen the light of day, continued, at [88], by emphasising the duty of administrators to maintain an independent stance, to act

in good faith, and to confine their proposals to such as will not unfairly prejudice the interests of any creditor, member or contributory of the company. The point was forcefully made by Warren J in Sisu Capital Fund Ltd v Tucker [2005] EWHC 2170 and 2321 (Ch) at [116]-[120] which included the observations that :

" … officeholders, in putting forward proposals for a CVA, are not negotiating or agreeing anything. It is not for the officeholders to advocate the interests of one group of creditors as against another group, nor to engage in brinkmanship, or attempt to extract ransom payments, on their behalf by refusing to put forward what he, the officeholder, regards as a fair proposal in order to extract a better proposal for the first group".

32 Mr Davies QC submitted that the JAs were fiduciaries. Their proposal of their own release, as in cl.24.1, was in flagrant disregard by them of their position and duties as officeholders. As with directors, see Howard Smith Ltd v Ampol Petroleum Ltd [1974] AC 821 and the speech of Lord Wilberforce at p.834, a fiduciary's powers must be exercised for the purpose for which it is granted, i.e. a proper purpose. An intention or purpose to secure a personal benefit or a benefit for someone not an object of the power is not a proper purpose, see Vatcher v Paull [1915] AC 372, Lord Parker at p.378. Mr Davies QC submitted that in this case, as with any CVA, the proper purpose is defined by s.1 IA 1986 and is to make a proposal for a composition in satisfaction of a company's debts or a scheme of arrangement of its affairs. That was the JAs' duty; however, the JAs, knowing of the claims against them, did not disclose or include the claims as assets - or contingent assets - but did the opposite and, out of self-interest, sought to provide for their release through cl.24.1. The release was formulated by fiduciaries for their own benefit. On this basis the release, being a flagrant breach of the proper purpose rule and the JAs' fiduciary obligation when exercising their power, is, and must be, ineffective and unenforceable by the JAs.

33 As to the proposition that a CVA is a contract, there is no doubt that as between those intended to be the subject of a CVA, the company and creditors entitled to vote, once passed by the requisite majorities, they are bound as if parties. That is the purpose and effect of s.5 IA 1986.

34 In Heis & Ors v Financial Services Compensation Scheme Ltd & Anor [2018] EWCA Civ 1327 the Court of Appeal, Sir Colin Rimer at [22] with whom McFarlane

and Asplin LJJ agreed at [70]-[71], adopted a short passage from the judgment of Hildyard J at first instance that, by statute, a CVA has contractual effect and is subject to the ordinary principles of interpretation applying to contracts. This was common ground in that case and is common ground in this case. The issue raised in this case is whether or not a CVA is a contract, at least for the purposes of the 1999 Act, not how it takes effect or is to be construed.

35 Mr Davies QC referred to the other authorities addressing the effect of a CVA and submitted that there is not a single authority where a CVA has been held to be, or described without some qualification as, a contract. The authorities refer to CVAs as analogous to and as having equivalent effect and as "hypothetical" contracts, but not as being actual contracts.

36 Mr Davies QC submitted that having contractual effect does not render a CVA a contract as such. Mr Davies QC referred to Johnson v Davies [1999] Ch 117, in which Chadwick LJ gave the judgment of the Court of Appeal, which concerned an individual voluntary arrangement ('IVA'). IVAs are subject to equivalent provisions under the IA 1986, with s.260(2) matching for individuals s.5(2) for companies. Addressing the effect of the "as if" provisions, Chadwick LJ described the provisions, at p.129H and p.138B-D, as a "statutory hypothesis" which

> ".. does not purport, directly, to impose the arrangement on a dissenting creditor whether or not he has agreed to its terms; rather, he is bound by the arrangement as the result of a statutory hypothesis. The statutory hypothesis requires him to be treated as if he had consented to the arrangement".

Addressing the effect on an individual's co-debtors and sureties, Chadwick LJ continued :

> "The consequence, as it seems to me, is that the legislature must be taken to have intended that both the question whether the debtor is discharged by the arrangement and the question whether co-debtors and sureties are discharged by the arrangement were to be answered by treating the arrangement as consensual; that is to say, by construing its terms as if they were the terms of a consensual agreement between the debtor and all those creditors who, under the statutory hypothesis, must be treated as being consenting parties".

37 The same analogy was drawn by Etherton J in Prudential Assurance Company

Ltd v PRG Powerhouse Ltd [2008], which concerned a CVA, who said, at [46] – [47] :

"The hypothetical agreement is a bilateral agreement between each creditor and the company. Section 1(1) of the IA refers to the intention to make a proposal to the company and *its* creditors for a composition in satisfaction of *its* debts or a scheme of arrangement of *its* affairs.

In short, each creditor is a party to the arrangement by virtue of being, and in the capacity of, a creditor of the company. It is the company and not any third party which has the benefit of and can enforce the rights and obligations conferred by the CVA. This interpretation of the statutory provisions is supported by the case law".

38 Mr Davies QC emphasised the characterisation of an IVA and a CVA as being based on a statutory hypothesis or as being a hypothetical contract.

39 Mr Davies QC also referred to the analysis of Jacob J in R A Securities Ltd v Mercantile Credit Co Ltd [1994] 2 BCLC 721, which concerned the liability of an original tenant to a landlord after the lease had been assigned and the assignee had entered into a CVA, and which Etherton J referred to at [56] in Powerhouse. The hypothetical agreement was a bilateral agreement between the landlord as creditor and the assignee tenant as the company, i.e. those entitled to vote; the original tenant, having no entitlement to vote, was not treated as if bound but was an outsider. That said, events might happen on which the original tenant would be able to rely, such as surrender of the lease, but the entitlement of reliance arose from some other act or event not through a CVA.

40 Applying that to the CVA, Mr Davies QC submitted that the Companies' members and the Companies' creditors were entitled to vote and the Companies and their creditors, being the persons exclusively identified by the legislation as being bound by the voluntary arrangement once approved, were taken to be the parties to the hypothetical bilateral agreement. The JAs had no entitlement to vote, and were not and could not be hypothetical parties; rather, they were debtors and, as such, they were outsiders to the arrangement and, like the original tenant in R A Securities, could get no assistance from it. This was clear from the CVA itself. The summary of key commercial terms referred only to the proposal representing the best outcome for creditors; further, other arrangements under the CVA, set out at part H thereof, made no reference to the JAs. Claims against the JAs were not

expressly referred to in the schedule of unissued/potential claims listed among other matters potentially affecting outcome, but the Companies' rights in relation to other (i.e. unlisted) unissued/potential claims were expressly reserved.

41 The question of whether a CVA is a contract was directly in point and carefully considered by Mr Christopher Pymont QC, sitting as a Deputy High Court Judge, in Re SHB Realisations Ltd (formerly BHS Ltd) (in liquidation) [2018] EWHC 402. Mr Pymont QC distinguished between classification and effect. After referring at [20] to Johnson v Davies and ss. 5(2) and 260(2) IA 1986, Mr Pymont QC continued :

"Thus the arrangement has contractual effect (see further LloydsBank PLC v Elliott [2003] BPIR 632 at para 51 per Chadwick LJ). In *Tanner v Everitt [2004] EWHC 1130* , Mann J summarised the position thus:
"The arrangement is therefore contractually based, with the statute providing the consent or deemed consent of the otherwise dissenting parties" (para 71)".

42 Analysing the question of whether the CVA in that case was a contract Mr Pymont QC said at [28] – [29] :

" … the fact that the CVA has contractual effect does not mean that it has every attribute of a contract or that every principle of the law of contract applies to it. The Insolvency Act creates a "*statutory hypothesis* " (as Chadwick LJ described it in *Johnson v Davies* above) or deeming provision (as Mann J characterised it in *Tanner v Everitt*, above) which enables, and compels, the court to apply a contractual analysis to issues such as the true construction of the CVA (as in, for example, *Re Brelec Installations Ltd [2001] BCC 421* at p 423E to F per Blackburne J and *Sea Voyager Maritime Inc v Bielecki [1999] BCC 924* at p 939B per Richard McCombe QC, then sitting as a deputy judge of the High Court) or the effect on co-debtors and sureties (as decided in *Johnson v Davies* itself). In so providing, however, the Act makes it unnecessary and inappropriate to consider any of the usual principles of contract formation (offer, acceptance, consideration, intention to create legal relations), all of which are irrelevant. Instead, the CVA takes effect " *as if made by the company at the time the creditors decided to approve the voluntary arrangement* " (section 5(2)(a) of the Act) and binds every person entitled to vote (or who would have been entitled had the relevant notice been given) " *as if he were a party to the voluntary arrangement* " (section 5(2)(b)). The statutory hypothesis thus works to bind all those affected by the arrangement, including the company itself.

29. This, in my judgment, renders it impossible to apply the law as to penalties, which is not designed to apply to hypothetical contracts of this kind. The foundation of the law of penalties was described by Dickson J in the Supreme Court of Canada in *Elsey v JG Collins Insurance Agencies Ltd (1978) 83 DLR* (3rd) 1 as follows:

"It is now evident that the power to strike down a penalty clause is a blatant interference with freedom of contract and is designed for the sole purpose of providing relief against oppression for the party having to pay the stipulated sum. It has no place where there is no oppression."

This passage was cited by the Privy Council with apparent approval in *Phillips Hong Kong Ltd v AG of Hong Kong (1993) 61 BLR 41* (itself cited with apparent approval in *Cavendish Square*[3], above). Whether there is oppression is " *judged by reference to the circumstances at the time of contracting* " (para 243 of *Cavendish Square* per Lord Hodge) and is likely to involve considerations such as the respective bargaining power of the parties in their negotiations (ibid, para 35 per Lord Neuberger and Lord Sumption and para 152 per Lord Mance) and the legitimate commercial interests of the innocent party at the time of contracting (ibid, para 32 per Lord Neuberger and Lord Sumption, para 152 per Lord Mance, para 255 per Lord Hodge). It is impossible to see how such principles can be applied to a situation where there has been no negotiation and where there has been no actual contract between the parties but rather where the arrangement has been brought about by a statutory procedure and is binding on the company itself and its members and creditors (consenting or dissenting) by reason of a statutory hypothesis. It is equally impossible to see how a proposal put forward by or on behalf of the company in the interests of itself, its members and creditors, approved by a statutory procedure and having effect by the statutory hypothesis, can somehow be said subsequently to have oppressed the company in some respect".

Mr Davies QC submitted that the clear conclusion reached by Mr Pymont QC was that a CVA is not a contract.

43 Mr Davies QC submitted that the JAs' proposition that the 1999 Act applies to CVAs because a CVA is a contract is, "on any view of life" a novel proposition, without support in any authority or textbook.

44 Turning to schemes of arrangement under Companies Act legislation, Mr Davies QC submitted that they are different and more flexible. Under s.895 CA 2006 a compromise or arrangement may be proposed between a company and its creditors or any class of them or between a company and its members or any class of them, and an arrangement may involve the reorganisation of a company's

[3] Cavendish Square Holdings BV v Makdessi [2016} AC 1172

share capital. The import of the difference was noted by Etherton J in Powerhouse at [95]–[96] and by reference to the judgment of Warren J in Sisu Capital Fund Ltd. Under a Companies Act scheme a separate class may block a scheme; but, under the IA 1986, a group of creditors able to carry a class vote may well not have sufficient voting power to block a CVA.

45 Mr Davies QC referred to Re Lehman Brothers International (Europe) [2009] EWCA 1161 ('LBIE as the entity, 'LBIE' as the case) which concerned a scheme proposed by administrators under s.895 CA 2006. LBIE provided services to institutional clients, mainly hedge funds, under contracts a key feature of which was that the clients obtained or retained proprietary interests in the assets the subject of the contracts. The proposals of the scheme included an envisaged release of the proprietary claims in exchange for a right to share in a pool of securities and other assets with any shortfall ranking as an unsecured creditor. The issue was whether LBIE's clients with proprietary claims were to be treated as creditors in respect of their rights in rem over the property held by LBIE as trustee. The Court of Appeal upheld the first instance decision that the court had no jurisdiction to sanction the scheme so as to bind dissentients because the scheme was concerned with property held on trust. The scope of an arrangement was circumscribed by the parties to it ~ a company and its creditors. A creditor was a person owed money and a person having a purely proprietary claim was not a creditor. An arrangement was concerned with the rights inter se of a company as debtor and its creditors. A scheme which had as its purpose something else, in LBIE the distribution of property held by a company on trust, fell outside the scope of a scheme of arrangement. In LBIE the Court of Appeal recognised that a scheme of arrangement might come within the Companies Acts statutory scheme notwithstanding that it altered the rights of creditors against a third party, but, as Lord Neuberger MR put it succinctly at [80], :

" … there is no getting away from the fact that, in order to be within s.895, an arrangement must be made with the 'creditors' (or members) of the company concerned".

At [77]-[78] Lord Neuberger also rejected, as unsupported by any clear authority, the argument that a scheme affecting a beneficiary who was also a creditor, albeit unaffected as creditor, would come within the scope of a scheme of arrangement under CA 2006.

46 Mr Davies QC acknowledged that a scheme might include an ancillary provision in order to make the scheme work. Examples included (1) the references in LBIE at [45]-[55], [63], [65] and [68] to approval of a scheme which varies or releases creditors' claims against a company on terms which require the bringing into account of rights of action against third parties to recover the same loss because the release of the third party claims was merely ancillary to the arrangement between the company and its own creditors or gave rise to a ricochet claim back against the company. Mr Davies QC also noted that at first instance in In re Lehman Brothers International (Europe) [2018] EWHC 1980 (Ch) Hildyard J referred to a release of officeholders but only to the extent that they would have an indemnity or similar claim against the company, i.e. a ricochet claim, which excluded a misfeasance claim; (2) Re Far East Capital SA [2017] EWHC 2878 (Ch) in which Snowden J acknowledged that a scheme might provide for the company to execute, on behalf of the creditors, a deed of waiver and release to third parties involved in the formulation and promotion of the scheme where the scheme would provide for the creditors not to bring claims against those parties. This was another example of protection of the company from a ricochet claim which had the effect of curtailing the risk of the scheme being undermined by a collateral attack; (3) Re Noble Group Limited and another [2018] EWHC 3092 (Ch) in which Snowden J, at [24]-[25], again emphasised that officeholder releases by creditors, usually through the mechanism of a deed of release executed by an attorney appointed under the scheme, would not prevent the sanctioning of a scheme if justified by the need not to allow scheme creditors to undermine the scheme; and, (4) Re Instant Cash Loans Limited [2019] EWHC 2795 (Ch), in which Zacaroli J had raised the question whether a scheme which imposed a surrender of leases came within the jurisdiction of a CA 2006 scheme of arrangement because the surrender appeared to be unrelated to the debtor/creditor relationship between the company and the landlords. Zacaroli J analysed the proposed scheme as a deal by which, in return for the tenant (company) agreeing to pay disclaimer damages, the landlord (creditor) would agree (a) to forego its debt claim for rent and (b) to the tenant going out of possession with the consequence that the lease would be terminated. The giving up of possession was not part of the quid pro quo but was an "additional something" to be imposed on the landlord by the scheme. Zacaroli J held that the "additional something" fell outside the permissible scope of a scheme.

47 Referring to Re Far East Capital SA and Re Noble Group Limited, Mr Davies QC observed that while the releases there mirrored the release of the JAs at cl.24.1(b) in relation to the "preparation, negotiation and implementation" of the CVA, there was no equivalent to the release at cl.24.1(a) in respect of the JAs "acts, omissions or defaults as administrators or advisors since the Administration Date". The JAs attempt to circumvent a statutory right preserved by paragraph 75 of Sch.B1 to sue administrators even after their statutory discharge is without precedent after more than three decades since the introduction of CVAs, and could lead to far reaching consequences in denial of a remedy for misfeasance.

48 Commenting on the above, and Re Instant Cash Loans Limited in particular, Mr Davies QC submitted that the present case is far stronger because the JAs are not creditors but are outsiders or strangers to the hypothetical bilateral contract and there is no prospect of cl.24.1 giving rise to a ricochet claim or otherwise preventing the CVA from being undermined.

49 Commenting further, Mr Davies QC referred to the LBIE 2018 scheme. Under that scheme LBIE's administrators were to be parties together with LBIE and scheme creditors. Certain claims, including by LBIE against its administrators, were retained or preserved, and the scheme creditors released and waived ricochet claims against the administrators and other claims. Mr Davies QC submitted that that is simply impossible under a CVA because s.5(2) IA 1986 limits the scope of a CVA to a company and its creditors.

50 Mr Davies QC acknowledged that in the sanctioned LBIE 2018 scheme, under Miscellaneous Provisions at cl.35, third party rights under the 1999 Act were expressly excluded save as permitted under the proposed scheme. As to that, the LBIE scheme was under the CA 2006 and under those schemes a third party may be a party to the scheme and, in fact, LBIE's administrators were parties. Further, the provision at cl.35 was unnecessary and merely belt and braces. Moreover, the LBIE scheme was quite different from a CVA under the IA 1986, constrained as it is by provisions including s.5(2) IA 1986.

51 Mr Davies QC drew the threads of his argument on this issue together by submitting (1) the IA 1986 does not refer to a contract but to an arrangement and the words "as if", which have generated consistent judicial references to a

hypothetical contract and statutory hypothesis, also serve to distinguish a CVA from a contract; (2) the consistent approach of first instance and appellate courts has been to distinguish a CVA from a contract; (3) hypothetical is not a meaningless word and it is consistently used in the authorities to avoid describing or referring to a CVA as a contract; (4) CVAs are creatures of statute, variously referred to as arising on a statutory hypothesis or as a form of statutory contract, under the IA 1986 and having a specific purpose (s.1(1) IA 1986) and clearly defined effect (s.5(2) IA 1986); (5) a provision in a CVA for release by the company of a debtor with no entitlement to vote is outside the scope of a CVA (see s. 5(2)(b) IA 1986) and is of no effect; (6) acceptance of the JAs proposal for their own release and Mr Smith QC's submissions would have the effect of expanding the effect of CVAs beyond that defined and confined by statute (s.5(2) IA 1986) and recognised by and explained and applied in all the authorities (e.g. Johnson v Davies, Powerhouse, SHB Realisations Ltd and LBIE); (7) a release is only permitted to the extent that it is ancillary to the compromise between a company (debtor) and the creditors and necessary to ensure the effectiveness of the CVA, i.e. that it is not undermined; (8) accordingly, there is no possibility of the release under cl.24.1 being ancillary and it is not necessary to prevent the scheme being undermined; and, (9) cl.24.1 of the CVA is, therefore, unquestionably unenforceable by the JAs against the Companies and the AAs. Further, in almost 25 years there has been no authority and nothing in any textbook to support the proposition that the 1999 Act is applicable to CVAs, i.e. that a CVA is a contract. The effect of finding that a CVA is a contract and, therefore, that rights created by the 1999 Act are applicable to CVAs would be seismic. As to give and take or quid pro quo, there is nothing given by the JAs; theirs is a one way street by which they intend to arrive at complete personal exoneration and evade the statutory provisions and consequences under paragraph 75 of Sch.B1 which expressly permit a challenge to a release under paragraph 98 of Sch.B1 and provide for remedies at paragraph 75(4). The JAs have given nothing for that claimed benefit and the inclusion of cl.24.1 is a serious negation and transgression of, and flies in the face of, their duties as officeholders.

52 So, although it would suffice to hold that there is a real prospect that at a trial the Court will find that a CVA is not a contract and that cl.24.1 is unenforceable and that non-parties cannot enforce the terms of a CVA on jurisdictional grounds, the JAs have taken a point which is unquestionably misconceived.

53 Mr Smith QC began his submissions by emphasising certain features of the background. The AAs had raised complaints about their essential claim, that the JAs should have pursued valuable claims against Barclays, in correspondence in 2013. The AAs' complaints were misconceived because the JAs did not have funding. Thus, the AAs' claims were known and understood on both sides before the proposal. There can be no doubt about the terms of the release; cl.24.1 is in clear and unambiguous terms, and the clear intention of the clause was to release any and all claims relating to the administrators of the Companies. Mr Davies QC did not suggest otherwise, and the AAs were advised throughout. The concern at the time was about the CVA releasing claims against Barclays, a creditor, which was addressed by a carve out. The release at cl.24.1 was in the proposal for the CVA from the outset. At no point was any concern expressed or issue taken with the release of the JAs under cl.24.1. Further, in the event in this case, the proposal received unanimous approval and the AAs both voted in favour of the CVA.

54 There has been no unfair prejudice or material irregularity challenge. There is no dispute that the claims which the AAs seek to pursue are caught by cl.24.1. The JAs could have applied to the court during their term of office, instead cl.24.1 was introduced to bring finality. Everyone consented to the CVA with their eyes open. What the AAs now seek to do is take a course of action in breach of that contract, i.e. a volte face.

55 In Discovery (Northampton) Ltd v Debenhams Retail Ltd [2019] EWHC 2441(Ch), a retail CVA aimed at managing what were said to be over-rented and unsustainable property costs, certain landlords challenged the CVA on grounds including that (1) in respect of future rent they were not creditors, there being no present debt, and, therefore, they fell outside the scope of a CVA under s.1 IA 1986; (2) they were unfairly prejudiced by certain terms; (3) there was a material irregularity through non-disclosure; and, (4) removing the right of forfeiture abrogated proprietary rights which also fell outside the jurisdiction conferred by s.1 IA 1986. Norris J agreed with the last challenge and modified the CVA accordingly, but otherwise dismissed the challenge. At [8] Norris J cited Neuberger LJ's description of the CVA regime in IRC v Wimbledon Football Club Ltd [2004] EWCA Civ 655 as intended to be an additional and particularly flexible option to the corporate insolvency alternatives. Norris J continued at [9] :

"CVAs provide a contractual mechanism through which a company can restructure its debts and liabilities, allowing it to continue trading for the benefit of the creditors as a whole. They facilitate compromises or variations of contractual rights or other obligations whereas other insolvency regimes (in a broad sense) suspend enforcement of existing rights and obligations and substitute for them rights to participate in the collective insolvency process".

At [100] Norris J addressed the argument that the words of s.895 CA 2006 are different from the words of s.1(1) IA 1986 :

"In my judgment, not in any material respect. In each case the "arrangement" has to be addressed to "creditors"".

56 For further authority on there being no material difference between a CVA and a scheme of arrangement under CA 2006 Mr Smith QC relied, first, on the judgment of Zacaroli J in Re Instant Cash Loans Limited as support for the proposition that conceptually there is no difference between a CVA and a scheme under the CA 2006. The relevant passage is at [9] where Zacaroli J addressed a submission of Mr Smith QC, in that case appearing for the applicant seeking the sanction of a scheme under the CA 2006. At [9] Zacaroli J summarised Norris J's decision in Discovery (Northampton) Ltd as holdings that forfeiture, being a proprietary right, fell outside the jurisdiction of a CVA, and where a pecuniary obligation is modified forfeiture can only be exercised in relation to the modified pecuniary obligation; and, noted that Mr Smith QC accepted that there is no material distinction between schemes and CVAs so far as this question is concerned. Pausing here, neither of these authorities seems to me to constitute an unqualified ruling that there is no material difference between a CVA and an arrangement under CA 2006.

57 Mr Smith QC also relied on the judgment of the Court of Appeal in LBIE. At [28] Patten LJ noted that Part 26 of the CA 2006 confers on the court a jurisdiction to sanction compromises or arrangements between a company and its creditors which have been approved by the requisite majority of creditors and continued :

"Although the discretion to approve the scheme is a general one to be exercised judicially

having regard to the objects of the scheme and its general fairness in relation to creditors, the jurisdiction is not an unlimited one. The arrangement must have the necessary features of give and take described by Brightman J in Re NFU Development Trust Ltd [1972] 1 WLR 1548 and it has to be an arrangement between a company and its creditors or members".

At [29] Patten LJ noted that there is no statutory definition of 'creditor' or 'arrangement' and, in relation to 'arrangement', the courts have been careful not to attempt to provide one beyond the limited criteria in Re NFU Development Trust Ltd. Mr Smith QC also relied on a passage in the judgment of Lord Neuberger MR at [74] referring to authorities which endorse giving a wide meaning to the terms 'creditors' and 'arrangement' in the context of CA 2006 schemes of arrangement.

58 For further support in the authorities Mr Smith QC referred to two decisions of Blackburne J. First, in Davis v Martin-Sklan [1995] BCC 1122 a bankruptcy order was made on the petition of a supervisor of an IVA. The issue was as to entitlement to £20,000 in the supervisor's hands. Blackburne J noted that the effect of an IVA, once approved, is to prevent a creditor bound by the IVA from pursuing the debtors personally except in accordance with the terms of the arrangement. After citing the terms of s.260(2) IA 1986, Blackburne J described the effect of approval of an IVA as :

"In other words approval of the arrangement gives rise to a species of statutory contract binding on the debtor and the creditors referred to in [s.260(2)]".

59 Secondly, in Re Brelec Installations Ltd [2001] BCC 421 at p.423E Blackburne J said :

"For the effect of the creditors' approval of the debtor's proposal is, as is well-established, to give rise to a species of statutory contract between the creditors bound by the arrangement on the one hand and the debtor on the other. The court's task is to construe in that contract".

60 Mr Smith QC referred also to the judgment of the Court of Appeal in In re N T Gallagher & Sons Ltd [2002] EWCA Civ 404, a case concerning and giving guidance on the effect of a liquidation on funds collected and held by the

supervisor of a failed CVA. Giving the judgment of the Court of Appeal, Peter Gibson LJ said at [4] :

"By section 5(2) the approved CVA binds every person who, in accordance with the Insolvency Rules 1986, had notice of and was entitled to vote at the meeting, whether or not he was present or represented at the meeting, as if he were a party to the CVA. Thus, the CVA, if approved, operates as a form of statutory contract to which even dissentients and non-voters receiving notice of and entitled to vote at the meeting are treated as parties";

and at [48] :

"The real difficulty … is in showing why a fully constituted trust created by a CVA should terminate on the CVA failing or terminating in the absence of any provisions requiring the trust to terminate and specifying what is to happen to the trust assets. It is not suggested that any moneys paid to creditors pursuant to the trust can or should be recovered. The fact that Gallagher was in breach of its obligations under the statutory contract constituted by the CVA and went into liquidation, thereby rendering it impossible to fulfil any further the statutory purpose of the CVA, does not entail the consequence that the trust also failed when plainly it can still be carried into effect".

61 Turning to the position of the JAs as third parties and their right to rely on a release, Mr Smith QC submitted that the contention that the JAs cannot rely on cl.24.1 because they are not parties is a bad point. Mr Smith QC submitted that third party releases are commonplace. They arise in either of two ways : (a) as where a scheme compels creditors to give up claims against third parties, such as third party guarantees, and/or (b) where a company voluntarily gives up its claims against a third party. The reason why a third party can rely on the release is straightforward, a CVA takes effect as a statutory contract.

62 Mr Smith QC also referred to Re Noble Group Limited. In this case the scheme was part of a broad restructuring of a global commodities trader which had recently reported a net deficiency of US$1.1billion. The purpose of the scheme was to provide the restructured group with substantial new hedging and trade finance. Mr Smith QC drew attention to the judgment of Snowden J at [22] where the terms of the particular release, which was by Scheme Creditors, (a) was expressed to be irrevocable, unconditional, full and absolute in respect of Scheme Claims and (b) included past, present and future claims against Released Parties

in respect of the preparation, negotiation, sanction or implementation of the Schemes and the execution of documents and the carrying out of the steps and transactions contemplated therein. Snowden J continued at [24]-[25] :

"24 It is well established that the Court has jurisdiction under Part 26 CA 2006 to sanction a scheme which includes a mechanism (usually the execution of a deed of release by an attorney appointed under the scheme) under which scheme creditors are required to release claims against third parties where such a release is necessary in order to give effect to the arrangement between the company and the scheme creditors. That test is most clearly satisfied where the scheme compromises debts which are guaranteed and where, absent such release, pursuit of the guarantor by a scheme creditor would undermine the compromise between the creditor and the company : see Re Lehman Brothers International (Europe) (No 2) [2010] Bus LR 489 at [65] (Patten LJ). On the facts of the instant case, it seems to me that the releases of any claims "arising out of, relating to or in respect of Scheme Claims and any of the facts and matters giving rise to the Scheme claims" must fall into the same category.

25 The jurisdiction is not, however, limited to guarantees and claims closely connected to scheme claims. In Far East Capital SA [2017] EWHC 2878 (Ch) at [14], I expressed the view that a release of claims against persons involved in the preparation, negotiation or implementation of such a scheme and their legal advisers would also be within the scope of Part 26. Such clauses can be justified by a need not to allow scheme creditors to undermine the terms of the scheme itself, and have become a regular feature of schemes. I see no difficulty arising from the inclusion of such a clause in the terms of Clause 2.1(b)(ii) and (iii) in the instant case".

Then at [26]-[28] after considering a hypothetical situation in which a negligence claim by one or more scheme creditors against a financial adviser might give rise to a ricochet claim, the release of which might ordinarily be within the jurisdiction of Part 26, but which on the facts might also raise issues of class composition, Snowden J expressed his view that the releases in the scheme before him did not give rise to any class issue. After working through the four stages for approval of a CA 2006 scheme (compliance with statute, whether the majority was fairly representative of the class and acting properly, fairness, and defects in or blots on the scheme), Snowden J concluded that the Part 26 statutory requirements had all been satisfied and it was appropriate to sanction the scheme.

63 Turning to Johnson v Davies on the question of release of co-debtors with the individual the subject of an IVA, Mr Smith QC drew attention to the judgment of

Chadwick LJ at p.128D :

"I am satisfied, therefore, that this is not a case in which the bargain evidenced by the voluntary arrangement between Mr Hopkins and his creditors has led to a release by accord and satisfaction of the joint debt owed by Mr Hopkins and the defendants to the plaintiffs, such that that debt can no longer be enforced against the defendants".

At p.129 B-H Chadwick LJ disagreed with a proposition stated by Jacob J in R A Securities Ltd that a term which would discharge a third party surety in a consensual document would not do so in an IVA or CVA, at least not unless the creditor had in fact consented to the IVA/CVA. As to the notion that actual consent was distinguishable from "statutory binding" under the IA 1986 in that proposals for a compromise between a debtor and his creditors imposed by an IVA are "in some way different from the effect which proposals in precisely the same terms would have if contained in a consensual document" Chadwick LJ expressed his view that :

"There is nothing in [s.260(2) IA 1986], or elsewhere, which saves a party who is bound "as if he were a party to the arrangement" from the consequences which would follow as a matter of law if he were indeed a party to the arrangement".

After reviewing the bankruptcy legislation over the preceding 100 years Chadwick LJ observed at p.131E-H :

"It seems clear, therefore, that when the Act of 1986 was enacted the legislature was well aware of the problem: that is to say, that one consequence of releasing the debtor from the debts owed to his creditors was that, under the general law, that release would or might have the effect of releasing co-debtors and sureties in respect of the same debts".

And, after noting that the IA 1986 did not expressly adopt the precedent offered by earlier bankruptcy legislation Chadwick LJ continued :

"There is to my mind a strong inference that that was the result of a deliberate decision that, in this respect, voluntary arrangements should be treated as - and have the same consequences as – consensual deeds of arrangement".

Mr Smith QC submitted that Chadwick LJ's judgment is that the effect of the statutory hypothesis is that there is a contract and that the general law of contract

applies.

64 Mr Smith QC then referred to a further Court of Appeal decision Lloyds Bank PLC v Ellicott [2002] EWCA Civ 1333 where at [51] and referring back to Johnson v Davies Chadwick LJ said :

> " … an IVA takes effect as a contract between the debtor, Mr Ellicott, and those of his creditors who are bound by its terms under statute".

65 As to SHB Realisations Ltd and Mr Davies QC's reliance on the judgment of Mr Pymont QC sitting as a Deputy High Court Judge, Mr Smith QC observed that at [20] Mr Pymont QC referred to the CVA as operating as a contract, having contractual effect, and – citing Mann J - being contractually based; at [28] reference was made to the court being enabled and compelled to apply contractual analysis to issues such as the true construction of the CVA and the position of co-debtors. The fact that, as noted at [28] the effect of the IA 1986 renders it unnecessary, inappropriate and irrelevant to consider the principles of contract formation (invitation to treat, offer, acceptance, consideration) because the statutory hypothesis binds all affected parties does not mean that a CVA is not a contract. Mr Smith QC submitted that the decision at [29] that it is impossible to apply the law as to penalties because the CVA is a "hypothetical contract" is wrong; a CVA is, as is clear from for example the judgments of Chadwick LJ and Peter Gibson LJ, and at first instance Norris J and Blackburne J, an actual contract.

66 Turning to the LBIE 2018 scheme, Mr Smith QC drew attention to cl.28.1.4-6 providing for the release of claims against administrators and cl.35 which provided, subject to express contrary provision in the scheme, for the exclusion of third party rights under the 1999 Act. The scheme was approved and then sanctioned by the Court. Hildyard J, at [44] – [46] in a section of the judgment summarising the terms of the approved scheme, referred to releases by Scheme Creditors against third parties. At [45] Hildyard J referred to give and take being a feature of the releases. Mr Smith QC acknowledged that there was no reference in terms to the applicability of the 1999 Act had it not been excluded, but he noted that the scheme was approved and sanctioned.

67 Mr Smith QC submitted that there is no doubt that the release of claims against third parties is legally effective when included as part of an arrangement under

Part 1 of the IA 1986, see Re Noble Group Limited and LBIE. Those cases concerned a scheme of arrangement under Part 26 CA 2006 but the concept of an arrangement for a CVA under the IA 1986 is the same, see Discovery (Northampton) Ltd, Norris J at [100], and so the reasoning therefore applies equally to CVAs. Mr Smith QC observed that the decision in Discovery (Northampton) Ltd goes to the question of whether the Court has jurisdiction to impose a release on third party creditors against their interest; thus, neither that case, nor any other, has any relevance to a release by the company. Mr Smith QC submitted that there is nothing that precludes a company from including within a scheme whatever it wants.

68 Mr Smith QC submitted that given that it is common ground that the terms of s.1 of the 1999 Act are met, the critical question is whether a CVA is a contract. This is a short point of law on which the court can and should come to a view. If the JAs are correct, the conclusion must be that the CVA is a contract and the action should be stopped as the JAs have a complete answer. The review of the authorities is consistent with the JAs' case. Finally, and irrespective of the 1999 Act, cl.24.1 is a clause in a CVA which is binding as between the Companies and all creditors. It would be sanctioning a breach of that contract to permit the AAs to pursue a claim against the JAs which they have expressly agreed to release and undertaken not to bring. On that basis the inevitable conclusion is that non-parties can enforce the terms of a CVA and, in this case, cl.24.1 of the CVA is directly enforceable by the JAs.

69 Mr Davies QC's submissions to the contrary are misconceived. The allegations of breach of fiduciary duties set out at paragraphs 59-66 of the Draft P/C are all within the scope of cl.24.1. This is nothing short of fatal to the AA's claims, and, thus, to both the application for permission under paragraph 75 and to the AA's application more broadly.

70 In summary (1) the CVA, in common with other voluntary arrangements, is a contract; (2) Cl.24.1 is enforceable by the JAs; and, (3) the JAs are entitled to rely on cl.24.1 pursuant to s.1 of the 1999 Act.

71 For the reasons which follow I do not accept as correct Mr Smith QC's submissions that a CVA is a contract, that the 1999 Act applies to CVAs so that

they are enforceable by third parties, or that cl.24.1 is directly enforceable by the JAs. In my view, Mr Davies QC's submissions that a CVA is something other than a contract and that there is no authority or jurisprudence to the effect contended for by Mr Smith QC is at least realistically arguable. It suffices for this permission application if I find that that it is realistically arguable, or a reasonably meritorious argument and if right likely to result in a benefit to the estate, that a CVA is not a contract; or, put another way, that a reasonable litigant would not be deterred from pursuing the claim in this case on the ground that a CVA is, or is likely to be found to be, a contract. I think Mr Davies QC's argument is compelling. However, I bear in mind (1) that neither side cited authorities or texts considering the definition or minimum essential elements for finding that a contract exists between two or more parties, (2) Mr Davies QC's reference to deep waters, and (3) Floyd LJ's cautionary guidance. For those reasons I do not grade my conclusion that a CVA is not a contract as more than a provisional holding. I do however make clear that Mr Davies QC's desire to cross-examine the JAs is irrelevant to this issue and has no bearing on this aspect of my decision.

72 I take as the starting point the 1999 Act and the IA 1986. The 1999 Act does not contain a definition of a contract. Neither Mr Davies QC nor Mr Smith QC ventured or took me to authority or texts containing a definition of a contract, rather they both addressed the issue by reference to the way in which voluntary arrangements or their effect have been described or characterised in the insolvency authorities. Mr Davies QC did submit, and Mr Smith QC did not demur, that there is no commentary in any textbook or legal journal which describes or characterises a voluntary arrangement under the IA 1986 as a contract. Of course, Mr Smith QC's position is that that is nothing to the point given the authorities he relies upon. Again, I do not find that a compelling argument; if it is clear that voluntary arrangements are a contract it is surprising that no text has picked up on that point.

73 The IA 1986 provisions relating to voluntary arrangements do not refer to CVAs or IVAs as contracts, agreements, enforceable promises, or bargains but to arrangements. The IA 1986 provides a mechanism by which, if the statutory procedure is followed, a debtor (a company in a CVA) may achieve a particular end or outcome in relation to liabilities to certain creditors even in the face of opposition from some of them. As Norris J noted in Discovery (Northampton) Ltd,

voluntary arrangements bring about compromises or variations of contracts; it does not follow that they are contracts. The validity of a CVA is founded not upon the agreement of or the consent of those bound (albeit that, as a procedural step, requisite majorities must vote in favour of the proposal for the voluntary arrangement to come into being) but upon compliance with the procedure prescribed by the statute. S.5(2) IA 1986 sets out the consequence of approving a CVA proposal; it does not refer to those affected, the company and its creditors, as or make them actual parties to the CVA; rather, it sets out how the CVA takes effect. That is twofold, by s.5(2)(a) it takes effect "as if" made by the company at the time it is approved by the creditors and by s.5(2)(b) it binds every person who, in accordance with the Insolvency Rules, was - or would have been if given notice - entitled to vote in the qualifying creditors' decision "as if" he was a party. In ordinary English "as if" is used conjunctively to liken something to something else which it is not, i.e. to something different.

74 As pointed out by Mr Pymont QC in Re SHB Realisations Ltd, the usual principles of formation of contracts are irrelevant and need not be met; indeed, and as noted above, a person who not only did not accept but positively rejected the terms proposed may nevertheless be bound. Further, a CVA is not required to contain every attribute of a contract or to conform to every principle. In Re SHB Realisations Ltd consideration of whether a CVA is a contract was directly on point and Mr Pymont QC gave a carefully reasoned judgment which led him to the conclusion that it is not.

75 The fact that the established principles of construction of an instrument apply to a CVA, as they do to a contract, does not lead to a conclusion that a CVA is a contract. All cats are animals, but all animals are not cats.

76 As the authorities have made clear the IA 1986 creates a statutory hypothesis (Johnson v Davies in the Court of Appeal) or hypothetical agreement (Powerhouse) or contractually based deeming (Tanner v Everitt). These authorities carry through the point that a voluntary arrangement is aligned with or treated as something which it is not.

77 Mr Smith QC submitted that Chadwick LJ's judgment in Johnson v Davies is to the effect that, by statutory hypothesis, a CVA is a contract. I disagree. The issue for

decision was whether co-sureties are released from their obligation if one co-obligee enters into a voluntary arrangement. The Court of Appeal, upholding the first instance decision, held that on its proper construction the terms of the particular IVA did not lead to an immediate or absolute release of the debts owed by the debtor and the coming into effect of the arrangement did not lead to the release of co-debtors. Per curiam rejecting Jacob J's observation in R A Securities Ltd that a distinction was to be drawn between actual consent in a consensual document discharging a surety and a term to the same effect in a voluntary arrangement, Chadwick LJ observed that whether the effect of a voluntary arrangement is to discharge a co-debtor or surety is to be determined by construing the arrangement as if it was a consensual agreement between the debtor and all creditors who are to be treated as if they had consented. Construing an arrangement on the same basis as a consensual agreement in order to ascertain its effect and consequences is not the same thing as declaring an arrangement to be a consensual agreement. Chadwick LJ's per curiam observations in Johnson v Davies cannot fairly be read as declaring or having the effect of declaring an IVA to be a contract. Further, Chadwick LJ's reference at p.128D to a "bargain" evidenced by the voluntary arrangement between a debtor and his creditors was, on a fair reading, a convenient shorthand description of the effect of the IVA not a binding finding as to the general status of IVAs as bargains and therefore, by inference, contracts.

78 In Davis v Martin-Sklan and Re Brelec Installations Ltd voluntary arrangements were referred to as a "species of statutory contract". This description was not essential to the decision and anyway it falls short of unqualified classification of voluntary arrangements as contracts. Moreover, although the former case preceded, the latter case followed the reporting of Johnson v Davies but it was not referred to in the judgment, rather Blackburne J referred to it being "well established" that the effect of the creditors' approval of a debtor's proposal is "to give rise to a species of statutory contract". What was being described was the effect of the statutory procedure; it was not to create a contract but something else, "a species of statutory contract".

79 In In re N T Gallagher & Sons Ltd, in which Johnson v Davies was also not referred to in the judgment or in argument, Peter Gibson LJ, giving the judgment of the Court of Appeal, referred to the CVA in that case as ".. operat[ing] as a form of

statutory contract to which even dissentients and non-voters receiving notice of and entitled to vote at the meeting are treated as parties" and later to the company being "in breach of its obligations under the statutory contract constituted by the CVA" and then going into liquidation which did not entail the consequence that the trust constituted by the company paying contributions provided for under the CVA to the supervisor of the arrangement failed. As to the first reference to "statutory contract", the Court of Appeal did not classify the voluntary arrangement as a contract but described its operative effect by drawing an analogy. As to the second reference to "statutory contract", it important to put the use of that phrase in its relevant context at [48] :

"The real difficulty … is in showing why a fully constituted trust created by a CVA should terminate on the CVA failing or terminating in the absence of any provisions requiring the trust to terminate and specifying what is to happen to trust assets. It is not suggested that any moneys paid to creditors pursuant to the trust can or should be recovered. The fact that Gallagher was in breach of its obligations under the statutory contract constituted by the CVA and went into liquidation, thereby rendering it impossible to fulfil any further the purpose of the CVA, does not entail the consequence that the trust also failed when plainly it can be carried into effect. … In the present case the supervisors can carry the CVA trust into effect".

I do not read that passage as a holding that a CVA is a contract, but as a metaphor or shorthand description, drawing on the same analogy as earlier in that judgment, when describing the consequence of the failure of the CVA in the context of a holding as to the rights to payments made by the debtor, Gallagher, to the supervisor for the benefit of the creditors bound "as if" parties. What the Court of Appeal held was that part performance by a company of the proposal approved by the procedure set by the IA 1986 created a complete trust which continued even if and when the debtor company failed to make all payments and went into liquidation. The Court of Appeal's decision was directed to a question concerning the law of trusts. The reference to "statutory contract" was not a finding that voluntary arrangements are in fact contracts.

80 I also do not think that likening CVAs to schemes under the CA 2006 takes this question any further. The reference in Discovery (Northampton) Ltd to CVAs providing a "contractual mechanism" falls short of a finding that CVAs are contracts. Norris J's reference to a "contractual mechanism" was not to classify CVAs as

contracts but to describe how they operate, namely to "facilitate compromises or variations of contractual rights". The contractual rights were pre-existing not created by the CVA.

81 Further, I do not read Norris J's observation at [100] in that case that CVAs and schemes under the CA 2006 were not different in "any material respect" as a general or unqualified finding, but as an observation on the case before him. CA 2006 schemes may concern only a company and its members and may be blocked by the exercise of class rights, see Lord Neuberger MR at [80] in LBIE and Warren J at [134] in Sisu Capital Fund Ltd v Tucker. These are important, not immaterial, differences.

82 The relevance of the similarity is that third party rights have been recognised in CA 2006 schemes including in particular releases. As to this I agree with and accept Mr Davies QC's submission that releases are only permitted in so far as they are ancillary to the purpose of the scheme and necessary to prevent the scheme from being undermined. Indeed, Mr Smith QC did not refer to any contrary authority. In the LBIE scheme the administrators were parties which is not possible in a CVA. In Re Noble Group Limited, relied on by Mr Smith QC, Snowden J made the point at [25] that release clauses relating to claims against those involved in the preparation etc. of a CA 2006 scheme are justified by the need not to allow scheme creditors to undermine the scheme, i.e. to avoid ricochet claims. Further, there is no CA 2006 authority – or at least none cited to me - in which the release has purported to protect officeholders from the provisions of paragraph 75 of Sch.B1 or generally from misfeasance claims.

83 Further, and as noted by Mr Pymont QC in Re SHB Realisations Ltd, a voluntary arrangement is not formed or analysed as a contract. Certain legal principles applicable to contracts, for example their interpretation, are applied to voluntary arrangements; that is no less true of other instruments which are not contracts. Other principles of contract law, for example those relating to penalties, are not applicable to voluntary arrangements. Mr Pymont QC concluded that a voluntary arrangement is not a contract. Characterising a CVA as a hypothetical agreement or by reference to a statutory hypothesis neatly and accurately makes clear that a CVA is different from, and is not in fact, a contract.

84 Strictly, it is enough to find that Mr Davies QC's argument is realistic and carries sufficient conviction that a reasonable litigant would pursue the point. I have no hesitation in making that finding. I add that I am left wholly unconvinced by Mr Smith QC's submissions and consider Mr Davies QC's submissions to be persuasive and sound. I fall short of making an outright finding because I am not satisfied that, in the absence of submissions as to and consideration of the interaction between the law of contract and statutes generally, full argument has been deployed, and, therefore, I cannot be satisfied as to the inevitable landing point of the trajectory of the law. I can form a provisional view and in my provisional view it is at least strongly arguable, and I think probably correct, that, at most, CVAs are a form of quasi-contract, for some purposes seemingly or apparently treated as if contracts, but in fact in all cases not actual contracts.

85 As to enforceability, it being at least realistically arguable that a CVA is not a contract, it is no less likely that the 1999 Act does not apply and that the CVA is not enforceable by third parties and further, that falling outside the categories of persons deemed bound by s.5 IA 1986, the JAs, as outsiders, cannot directly enforce the CVA. Mr Davies QC raised a separate point on enforceability, the JAs position as officeholders, and I shall return to that later in this judgment.

86 Thus, my conclusion on the CRTPA issue is that it is at least as likely as not (and, provisionally, I think in fact more likely than not) that (1) a CVA is not a contract, (2) the 1999 Act is of no application to the CVA, and (3) cl.24.1 is of no effect and not enforceable by the JAs.

Issue 3 : Can the AAs apply as a contributory given that they voted in favour of the CVA as members and creditors?

87 Both Mr Davies QC and Mr Smith QC referred to the provisions of paragraph 75(2) of Sch.B1 which provides an exclusive list of permitted applicants seeking an examination into the conduct of present or past actual or purported administrators of a company. They are :

"(a) the official receiver,
(b) the administrator of the company,
(c) the liquidator of the company,

(d) a creditor of the company, or
(e) a contributory of the company".

88 The Draft P/C states that the AAs bring the proceedings as contributories, respectively of AIL and REPL.

89 Contributories are defined at s.74 of the IA 1986. So far as relevant s.74(1) and (2) provide as follows :

"(1) When a company is wound up, every present and past member is liable to contribute to its assets to any amount sufficient for payment of its debts and liabilities, and the expenses of the winding up, and for the adjustment of the rights of the contributories among themselves.

(2) This is subject as follows—
… …
(d) in the case of a company limited by shares, no contribution is required from any member exceeding the amount (if any) unpaid on the shares in respect of which he is liable as a present or past member".

90 It is common ground that JS voted in favour of AIL's CVA as a member and as a creditor, and that REHL voted in favour of REPL's CVA as a member. Mr Davies QC said that REHL did not vote as a creditor. Mr Davies QC also acknowledged that in respect of the Companies there is no actual difference between the members and the contributories.

91 Mr Davies QC submitted that neither JS nor REHL were parties to the CVA whether as members or contributories. They did vote in favour as members but not as contributories. Members and contributories are outsiders to the CVA, which is between the Companies and their creditors.

92 Further the terms of cl.24.1 do not mention members or contributories. Mr Davies QC submitted that this is important because the court will not readily conclude that rights have been given up without a clear expression to that effect. Indeed, clauses intended to limit liability which arises legally or by operation of law fall to be construed narrowly. In Impact Funding Solutions Ltd v Barrington Support Services Ltd [2016] UKSC 57 Lord Toulson stated that words of exception or

exemption had to be read in the context of the contract as a whole and that, as was well established, exclusion or limitation of liability requires clear words. Mr Davies QC also referred to the recent judgment of the Court of Appeal in First Tower Trustees Ltd v CDS (Superstores International) Ltd [2018] EWCA Civ 1396, Lewison LJ at [84] with whom Leggatt LJ and Sir Colin Rimer agreed, to the same effect in a case of trustees seeking to limit their liability to third parties, including for misrepresentation.

93 Mr Davies QC submitted that the release clause does not purport to bind contributories and is not expressed to limit the scope of paragraph 75. Set in context, which includes in the CVA (1) express reference to the JAs obtaining their discharge under paragraph 98 of Sch.B1, a provision which expressly preserves the powers provided for at paragraph 75 and (2) express reservation, without any waiver by the CVA, of the Companies' rights in relation to unissued/potential claims, a reasonable person, or notional creditor, having the requisite background knowledge would not consider that paragraph 75 of Sch.B1 was caught by cl.24.1.

94 Had the release under cl.24.1 been intended to release the JAs from claims by contributories, that could easily and should have been spelt out in the clause. That would not have overcome the fundamental problem that the JAs were not parties to the CVA. What the JAs could have done, but they did not, was to attempt to secure their release by a deed executed by all relevant persons in their relevant capacities.

95 The only situations where a third party may be released from liability under a scheme is where the third party's liability would give rise to a ricochet claim or where necessary to save the scheme from the risk of being undermined or imploding. Those situations are not this case.

96 The relief sought by the contributories is, as is stated in the application, permission under paragraph 75(6) to make the application against the JAs.

97 Mr Smith QC submitted that Mr Davies QC was missing the point. Paragraph 75 is a purely procedural provision, as is s.212 IA 9186. The claim is not personal to the contributory, rather the contributory pursues or seeks permission to pursue a cause of action belonging to a company. Thus, like s.212 IA 1986, paragraph

75(6) is simply a gateway provision enabling a claim which could otherwise have been brought by a company to be brought by another person, identified in the relevant statutory provision, for the benefit of the company or its estate. Mr Davies QC interrupted this submission by Mr Smith QC to say that he accepted the point that paragraph 75 is a procedural provision and the authorities to that effect cited by Mr Smith QC and Ms Thornley in their skeleton argument at [42]-[49], but that was not an answer to his submissions.

98 Mr Smith QC referred to Re Eurocruit Europe Ltd (in liquidation) [2007] EWHC 1433 (Ch). In that case a claim, which was time barred at the suit of the company, was commenced by a liquidator within 6 years of the commencement of the liquidation. Blackburne J, at [24], referred to the procedural nature of s.212 and to the facts that "the claimant is in substance the company" and that any relief would be granted to the company by way of compensation for the wrong in question. Applying that reasoning to the present case Mr Smith QC submitted that there is nothing for the contributories to litigate because, by cl.24.1, the Companies have released and undertaken not to bring any claim against the JAs. There is thus nothing to litigate as any possible claim no longer exists.

99 On my primary finding the CVA is, at least arguably, not a contract and third party rights under the 1999 Act are, at least arguably, of no application. Putting that conclusion to one side for the moment, and recognising and notwithstanding that paragraph 75 provides a procedure for identified parties to make a claim to benefit the company not themselves, it seems to me that Mr Smith QC's analysis breaks down because the contributories had no role in making the CVA and are not affected by the CVA or the release. They are entitled to take their own view of the CVA in their capacity as contributories and as outsiders, and they are entitled to exercise the rights conferred by statute. The fact that in other capacities they may have voted in favour of the CVA or that the Companies are the beneficiaries of any success in litigation does not remove or disqualify their distinct status as contributories or undermine the rights afforded to them in that capacity. Thus, and as Mr Davies QC submitted, Re Eurocruit Europe Ltd (in liquidation) is nothing to the point.

100 In principle the AAs are not precluded from applying under paragraph 75 with any resultant benefit being, of course, for the estates of the Companies not the AAs.

Issue 4 : If otherwise potentially capable of applying to an application under paragraph 75, is the CVA ineffective in equity as a provision intended by the JAs to secure a personal benefit outside the scope and purpose of the CVA?

101 As noted at [32] above, Mr Davies QC submitted that the JAs, as officeholders, were fiduciaries and that the proper purpose rule applied to them. The hallmark quality of a fiduciary is loyalty. Features of this quality include avoiding conflicts of interest and self-dealing or acting out of self-interest. The same principle underlies the proper purpose rule.

102 For a succinct exposition of the rule Mr Davies QC referred to the speech of Lord Sumption in Eclairs Group Ltd v JKX Oil and Gas plc [2015] UKSC 71 at [30], with which the other JJSC agreed :

> "The proper purpose rule is a principle by which equity controls the exercise of a fiduciary's powers in respects which are not, or not necessarily, determined by the instrument. Ascertaining the purpose of a power where the instrument is silent depends on an inference from the mischief of the provision conferring it, which is itself deduced from its express terms, from an analysis of their effect, and from the court's understanding of the business context".

103 The power under the IA 1986 is conferred for the purpose of making a proposal for a composition in satisfaction of a company's debts or a scheme of arrangement of its affairs. Mr Davies QC submitted, as noted above, that some forms of release may be included but the scope is confined to releases to avoid undermining or having a knock-on or ricochet effect on the arrangement. It would be inconsistent with the scheme of Sch.B1 to allow an office holder to exclude liability or the risk of liability expressly provided for and preserved after release by the statute itself.

104 Mr Davies QC submitted that statute (Sch.B1 to the IA 1986) expressly provides a procedure for taking misfeasance proceedings against administrators and expressly provides, paragraph 98(4)(b) of Sch.B1, that discharge of an administrator does not prevent the exercise of the power under paragraph 75. Mr Davies QC submitted that it is improper for an administrator to use the machinery of a CVA to exclude a liability after the event which could not be excluded before or during the event. The inclusion of cl.24.1 was for a purpose outwith Part 1 of

the IA 1986. It did not benefit or affect the Companies' creditors; its purpose was to benefit a debtor who was also a fiduciary.

105 Mr Davies QC further submitted that the consequences of permitting such personal exclusion from liability would be far reaching. In one example he postulated a carte blanche exclusion which protected an administrator from misuse of the company's money for personal benefit, such as gambling or a holiday, during the course of the administration.

106 Mr Smith QC submitted that Mr Davies QC had missed the point and his argument was misconceived. If a provision in a CVA was considered unfair or otherwise to be impugned the challenge should be under s.6 IA 1986 for unfair prejudice and should have been brought within a deadline, now long expired, of 28 days.

107 Further, and in the circumstances of this case, the AAs were closely involved in the development of the CVA and voted in favour of the CVA which had included, at all times from inception and first proposal in draft, cl.24.1.

108 Further still, the doctrine of fraud on a power or the proper purpose rule is not applicable because cl.24.1 takes effect as a matter of law, by ss.4 and 5 IA 1986, through the decisions of the creditors and the members to approve the arrangement. If anything is to be impugned it is what the members and creditors did by approving the CVA.

109 As I understand it, Mr Davies QC is not raising a point that cl.24.1 unfairly prejudices the interests of a creditor, member or contributory of a company, which is the express scope of s.6(1)(a) of the IA 1986. Rather he is raising an overarching point about the duty of the proposer of a CVA, in this case the JAs, to maintain an independent stance, to act in good faith, and to eschew self-interest or personal benefit. That is quite different. I agree with Mr Davies QC's submissions and regard those of Mr Smith QC as missing the point and misconceived.

Issue 5 : Are the AAs estopped from denying the binding effect of cl.24.1 for the purpose of paragraph 75 of Sch.B1?

110 Mr Smith QC stated that the JAs would not pursue the contention that the AAs are

estopped from denying the binding effect of cl.24.1 on this application.

Conclusion

111 By this application the AAs ask the court to grant permission under paragraph 75 of Sch.B1 to the IA 1986 to make an application against the JAs so that the court will examine the conduct of the JAs, as former administrators of the Companies, and order them to contribute a sum to the Companies' property by way of compensation for breach of duty or misfeasance. The court's power is conferred as a discretion under paragraph 75(1). The threshold test for granting permission under paragraph 75(6) is that the cause of action in the claim the AAs wish to advance is reasonably meritorious and that, if permission is given so that the claim may be pursued, there is a reasonable likelihood of benefit to the estates of the Companies.

112 The circumstances in which the JAs disregarded the advice of leading counsel and sought and relied on the advice of solicitors which resulted in the scope for litigation funding evaporating, is a suitable subject for examination. Mr Smith QC's submission that the AAs' complaints were misconceived because the JAs did not have funding is not an answer, rather it begs the question. The claim advanced in the Draft P/C is coherent and reasonably meritorious. The relief claimed is consistent with that reasonably meritorious claim and is reasonably likely to result in the Companies' estates benefitting.

113 The obstacle presented by cl.24.1 of the CVA is, in my provisional view, unlikely to provide a defence to the AAs' claim for the reasons given above.

114 In my judgment, the only proper way in which to exercise the discretion conferred by paragraph 75(6) of Sch.B1 is to grant permission as sought by the AAs on this application.