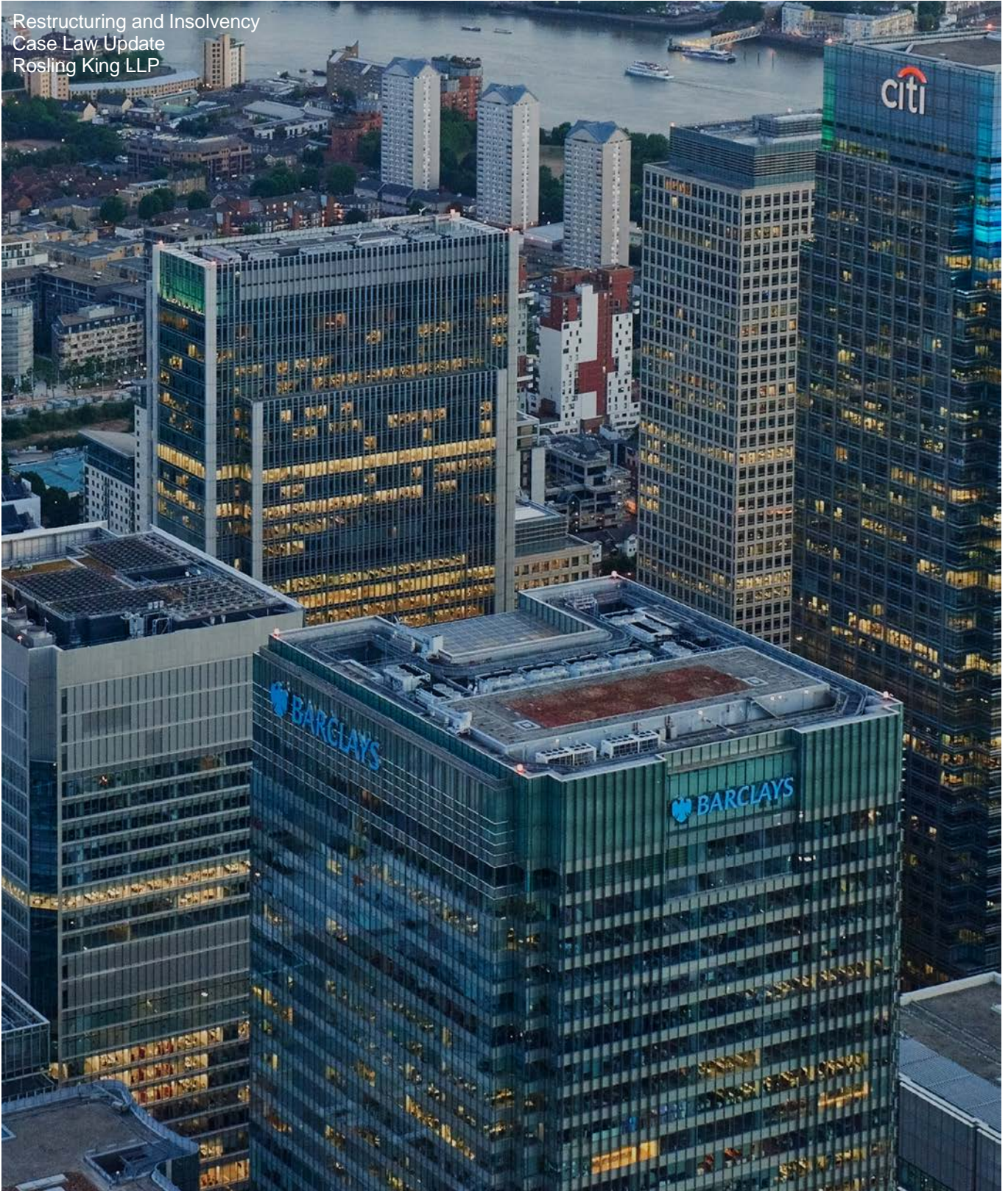


Restructuring and Insolvency
Case Law Update
Rosling King LLP



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Page 2

The High Court has considered whether a former liquidator should be held liable under section 212 of the Insolvency Act 1986 (the “Act”) for misapplying company monies in excess of half a million pounds.

The Facts

By an application issued on 28 October 2014 pursuant to section 212 of the Act, Top Brands Limited and Lemione Services Limited (together the “Creditors”), sought an order that Mrs Gagen Sharma (“Mrs Sharma”) repay, restore, account or pay compensation to Mama Milla Limited (in liquidation) (“MML”) for the sum of £548,074.56 (the “Sum”).

The Complaint

The allegations against Mrs Sharma were that the Sum belonged to MML and, whilst acting as liquidator of MML, she negligently and/or in breach of her fiduciary duties misapplied the Sum when paying it out by making or authorising 18 transfers of money between 30 November 2011 and 30 April 2012.

The central issue was whether Mrs Sharma’s payment of the Sum was a breach of a statutory duty and/or negligent and/or in breach of fiduciary duty. Specifically, the misfeasance application against Mrs Sharma was that the Sum which should have been available for distribution to creditors was paid out by her to third parties in circumstances where:

1. inadequate steps were taken by Mrs Sharma to ascertain MML’s state of affairs at liquidation (in particular Mrs Sharma was not alive to any aspect of the fraudulent trading which MML had been undertaking prior to its liquidation and because she appeared to have been the victim of a separate fraud when deceived into paying out the Sum by way of the 18 transfers of money);
2. inadequate, if any, consideration was given by Mrs Sharma to the material available as to MML’s trading, assets and liabilities;
3. inadequate instructions were given by Mrs Sharma to an experienced insolvency lawyer who advised that payment could be made;
4. inadequate enquiries were made by Mrs Sharma as to the payees of the Sum before payment; and
5. Mrs Sharma failed to notice, before making payments out, that indemnities sought were not in the required form.

Counsel for the Creditors characterised Mrs Sharma’s fulfilment of her duties as “slipshod and slapdash” and her approach as “being geared towards bringing about a quick conclusion to the liquidation”.

The Decision

Mrs Sharma’s conduct throughout certain stages of the liquidation of MML was described by the Court as capable of being “characterised as a conscious disclaimer or disregard of responsibility for the assets in her charge on a material scale” and, on the evidence, the Court found that Mrs Sharma acted in breach of the duty implicit in section 107 of the Act

(Distribution of a company's property) and had acted negligently. But for the omissions and errors on the part of Mrs Sharma in the performance of her duties as liquidator, the true position as to MML's trading, assets and liabilities would have become apparent. Had Mrs Sharma acted with the care and diligence to be expected of an ordinary, skilled insolvency practitioner, the loss of the Sum would not have occurred. However, whilst the Court held the view that such conduct crossed the border into the territory of breach of fiduciary duty, Mrs Sharma was not found to have acted for an improper purpose in the sense of denial or betrayal of a duty owed as a fiduciary and the evidence did not support a finding that Mrs Sharma consciously acted for an improper purpose.

In reaching its decision, the Court agreed that Mrs Sharma, when acting as liquidator of MML, owed a duty of care, enforceable through the process provided by section 212 of the Act, in the performance of her duties and in the exercise of her powers. However, the Court accepted that there is no duty on a liquidator to investigate the affairs of a company before appointment. However, any insolvency practitioner taking on the role of liquidator should appreciate that reviewing the available information and obtaining further basic, objectively reliable information at a very early stage would be essential to the due performance of a liquidator's duties.

In any event, the Court held that the loss suffered by MML was caused by Mrs Sharma's failure to conduct the liquidation of MML with the care and diligence to be expected of an ordinary, skilled insolvency practitioner. As such, the Sum, which should have been available for distribution to creditors, was paid out to third parties. In the circumstances, and taking into account Mrs Sharma's conduct, the Court refused Mrs Sharma relief from liability under section 212 of the Insolvency Act 1987 and ordered her to make good the loss of the Sum to MML.

Conclusion

The facts of this case highlight the consequences an insolvency practitioner may face should they fail to act in good faith and exercise their powers with reasonable skill and care and for their proper purpose. Further, insolvency practitioners must remain aware that they will be unable to claim that they have taken proper advice where their instructions to their legal adviser were flawed by reason of a failure on the part of a liquidator to identify relevant considerations or a failure to use all proper care and diligence to obtain information relevant to the instructions given.

This case also serves as a useful reminder that when evaluating a liquidator's conduct, it is essential not to start with the current state of knowledge; the liquidator's conduct is not to be judged through the vision of hindsight. Instead, the Court in this case highlighted that it is essential to consider the allegations against a liquidator in context.

For further information, please contact [Jonathan Hyndman](#) or the Partner with whom you usually deal.