Fiduciaries and the Financing of Insolvency Litigation: Some Legal and Practical Considerations

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Abstract

The costs of civil litigation have been in crisis for some time, and in a post-pandemic world expenditure on enforcing legal rights could see an unprecedented increase. The costs involved in insolvency work are no exception to this crisis. This article considers some of the legal and practical matters which an insolvency office-holder should take into account when contemplating embarking on litigation and how to finance it. Whilst it necessarily focuses primarily on contentious work, some of the matters addressed are relevant to instructing solicitors and others in relation to non-contentious work as well.

Keywords

Insolvency litigation, insolvency practitioners, fiduciary duties, litigation funding

I. INTRODUCTION

This article sits uneasily in a special edition on Law and Criminal Justice in times of Crisis. It has nothing to do with the criminal law. It does, however, have a place in a discussion of crisis, the crisis over costs that has dominated civil litigation since Lord Woolf's civil procedure reforms of the late 1990s and has continued in legal reforms that have seen the legalisation of conditional fees and a range of other funding options designed to compensate for the well documented decline of legal aid and counterbalance burgeoning litigation costs and fees. While Lord Justice Jackson was reviewing civil litigation costs, insolvency costs have also been the subject of scrutiny: Mr Justice Ferris's *Working Party Report on the Remuneration of Office-Holders and Certain Related Matters* was produced as long ago as 1998. Professor Elaine Kempson weighed in in 2013 with her *Review of Insolvency Practitioner Fees*, looking at the issue from a foreign as well as a domestic perspective. A more developed cross-border approach has been taken yet more recently by Wolverhampton University senior lecturer Dr

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Lézelle Jacobs, whose 2020 INSOL International Special Report, *Corporate insolvency practitioners, ethics and remuneration: Not a case of moral bankruptcy?* examines the subject matter of its title in an international context. The recent research work of Professor Peter Walton of Wolverhampton on the funding of insolvency litigation and related matters (on which this article draws) provides another connection.[1]

This article considers some of the legal and practical matters which an office-holder should take into account when contemplating embarking on litigation and how to finance it. Whilst it necessarily focuses primarily on contentious work, some of the matters addressed are relevant to instructing solicitors and others in relation to non-contentious work as well.

In *Excalibur Ventures LLC v Texas Keystone Inc*[2] Tomlinson LJ noted that "Third party funding is a feature of modern litigation." In doing so he differentiated between two forms of funding: so-called "pure funding", of which *Hamilton v Al Fayed (No.2)*[3] was an example and where the funders would not ordinarily be made the subject of an order to pay the costs of the successful unfunded party,[4] the court having held that pure funding was in the public interest provided that its essential motivation was to enable the funded party to litigate what the funders perceived to be a genuine case; and "commercial funding" where "[t]he commercial funder is an investor who hopes to make a return on his investment" and different costs consequences arise. Importantly for present purposes, he noted that now, "Litigation funding is an accepted and judicially sanctioned activity perceived to be in the public interest". He rejected any notion of its now being champertous, since "champerty involves behaviour likely to interfere with the due administration of justice."

It is, of course, the second form of funding (or litigation finance) with which the insolvency practitioner will usually be concerned. Whilst the majority of litigants using litigation finance will be troubled only by commercial considerations, there are additional considerations which apply to insolvency cases brought by office-holders because an insolvency office-holder is a fiduciary, a person who has undertaken to act for, or in the interests of, others and whose activities can be supervised in equity so as to prevent their being used for personal advantage.[5]

The nature of the fiduciary and the fiduciary relationship has been the subject matter of a certain amount of theoretical debate. A former Australian Lord Chief Justice has gone so far as to describe the latter as "a concept without a principle."[6] Be that as it may, it is firmly established on the practical level in the insolvency context. It was the starting point of, and was examined in detail in, the well-known judgment of Ferris J in *Mirror Group Newspapers plc v. Maxwell (No 2)*.[7] Although that case was decided in 1998 and dealt primarily with office-holders' remuneration, it remains an important and detailed statement of the principles governing not

[1] See in particular his *The Likely Effects of the Jackson Reforms on Insolvency Litigation* commissioned by R3 (2014) and his 2020 work on insolvency litigation cited below. His most recent contribution on the subject, *Insolvency Litigation Funding – What Should an Insolvency Practitioner Do?* (2020) 4 WLJ 1 asks (and answers) some of the points which this article seeks to develop from a different perspective.
[2] [2016] EWCA Civ 1144.
[3] [2003] QB 1175.
[4] Under section 51(3) Senior Courts Act 1981.
[5] For further discussion see, for example, Paul Finn, *Fiduciary Obligations: 40th Anniversary Republication* (Annandale, 2016) p 8 and Hamish Anderson, *The Framework of Corporate Insolvency Law* (Oxford, 2017) paras 11.08-11.12. For a brief but thorough examination of the nature of an insolvency practitioner's fiduciary obligations see also Peter Walton, *Insolvency Litigation – in the best interests of creditors?* (March 2020), the product of a research project conducted in 2019/2020 "to assess the current state of play in the insolvency litigation funding market."
[6] Sir Anthony Mason, "Themes and Prospects" in P D Finn (ed), *Essays in Equity* (Sydney, 1985) p 246 cited in Ewan McKendrick (ed), *Commercial Aspects of Trusts and Fiduciary Obligations* (Oxford, 1992) p 8. For a more conventional approach to the topic see generally Evan J Criddle, Paul B Miller and Robert H. Sitkoff (Eds), *The Oxford Handbook of Fiduciary Law* (Oxford, 2019), in particular chapter 11 on fiduciary duties in bankruptcy and insolvency (although the chapter focusses largely on US law).
[7] [1998] 1 BCLC 638.

only remuneration but the nature of an office-holder's fiduciary duties when incurring costs, and nothing in more recent legislative or regulatory change or the case law has altered the principles enunciated in it by Ferris J.[8] Furthermore, although remuneration cases of the kind with which the court was concerned in *Mirror v Maxwell* were and still are usually decided on the basis of evidence and submissions made only on behalf of the officer-holder (except where the remuneration application is disputed), in *Mirror v Maxwell* the court was assisted by an *amicus curiae* instructed by the Treasury Solicitor; so the case was properly and fully argued, which lends the judgment considerable weight.

II. GENERAL PRINCIPLES: THE OFFICE-HOLDER AS FIDUCIARY

A number of general principles enunciated in *Mirror v Maxwell* have implications for decisions about instructing lawyers and financing litigation.[9]

The starting point of the judgment in *Mirror v Maxwell* is that an insolvency practitioner is a fiduciary in relation to the office he or she holds – the assets under his/her control and for which he/she is responsible are beneficially owned by others:

> "The essential point which requires constantly to be borne in mind is that office-holders are fiduciaries charged with the duty of protecting, getting in, realising and ultimately passing on to others assets and property which belong not to themselves but to creditors or beneficiaries of one kind or another. They are appointed because of their professional skills and experience and they are expected to exercise proper commercial judgment in the carrying out of their duties. The fundamental obligation is, however, a duty to account, both for the way in which they exercise their powers and for the property which they deal with."

Ferris J acknowledged, however:

> "Office-holders are nowadays not normally expected to act gratuitously. It is salutary to remember, however, that the rule that a trustee must not profit from his trust is a rule that applies to all kinds of person who are in a fiduciary position (see *Snell's Equity* (28th edn, 1982) pp 249-252). The allowance of remuneration in particular cases represents an exception to this rule, but it inevitably involves a conflict between the interest of the fiduciary who is to receive such remuneration and the interests of those to whom the fiduciary duties are owed, who will bear whatever remuneration is allowed[10]. A consequence of this is that it must be for the office-holder who seeks to be remunerated at a particular level to justify his claim. As I see it this is simply one aspect of the obligation to account. What he retains for himself out of the property which comes into his hands as office-holder is not available for those towards whom he is a fiduciary. He cannot therefore account for it by paying it over. The only other way in which he can

[8] For a useful, if now dated, treatment of this topic see Susie Meikle, "Fiduciary duties and office holder remuneration," (2007) 23 IL and P 32.
[9] What follows does not pretend to be an exhaustive examination of all the implications of the authority, the whole of which repays close reading; instead I concentrate here on the matters raised which appear to be most relevant to the topic under discussion.
[10] For discussion of the remuneration exception in the context of insolvency and trusts see Hamish Anderson, "Trusts Assets in English Insolvency Law" in Ewan McKendrick (ed), *Commercial Aspects of Trusts and Fiduciary Obligations* (Oxford, 1992).

account for it is by showing that he ought to be allowed to retain it for himself. But this is necessarily a matter for him to establish."

Ferris J went on to say:

"Certain more particular consequences follow from what I have said so far. First, office-holders must expect to give full particulars in order to justify the amount of any claim for remuneration. If they seek to be remunerated upon, or partly upon, the basis of time spent in the performance of their duties they must do significantly more than list the total number of hours spent by them or other fee-earning members of their staff and multiply this total by a sum claimed to be the charging rate of the individual whose time was spent. They must explain the nature of each main task undertaken, the considerations which led them to embark upon that task and, if the task proved more difficult or expensive to perform than at first expected, to persevere in it. The time spent needs to be linked to this explanation, so that it can be seen what time was devoted to each task. The amount of detail which needs to be provided will, however, be proportionate to the case.

The charging rate claimed must also be proved by evidence; and what is relevant is not the charging rate of the particular individual, but the broad average or general rate charged by persons of the relevant status and qualifications who carry out this kind of work […].

Second, office-holders must keep proper records of what they have done and why they have done it.

Third, the test of whether office-holders have acted properly in undertaking particular tasks at a particular cost in expenses or time spent must be whether a reasonably prudent man, faced with the same circumstances in relation to his own affairs, would lay out or hazard his own money in doing what the office-holders have done. It is not sufficient, in my view, for office-holders to say that what they have done is within the scope of the duties or powers conferred upon them. They are expected to deploy commercial judgment, not to act regardless of expense. This is not to say that a transaction carried out at a high cost in relation to the benefit received, or even an expensive failure, will automatically result in the disallowance of expenses or remuneration. But it is to be expected that transactions having these characteristics will be subject to close scrutiny."

And later:

"It is important not to place too great an emphasis on time spent […] In my judgment it is vital to recognise three things in this field. First, time spent represents a measure not of the value of the service rendered but of the cost of rendering it. Remuneration should be fixed so as to reward value, not so as to indemnify against cost. Second, time spent is only one of a number of relevant factors, the others being, as I have said, those which find expression in r 2.47 and similar rules. The giving of proper weight to these factors is an essential part of the process of assessing the value, as distinct from the cost, of what has been done. Third, it follows from the first two points that, as the task is to

> assess value rather than cost, the tribunal which fixes remuneration needs to be supplied with full information on all the factors which I have mentioned."

It is worth bearing in mind that *Mirror v Maxwell* also touched on legal costs and the office-holder's obligation to scrutinise them properly before agreeing to them. Ferris J bemoaned the restricted jurisdiction of the court to look at these, but, as we know, that has now changed.[11]

(a) Sub-contracting

The decision to instruct solicitors and counsel is in essence a decision to sub-contract work which the office-holder is entitled and (at least in theory) able to do him/herself.

In *Jacob v UIC Insurance Co Ltd*.[12] Peter Smith J, hearing an appeal from Mr Registrar Nichols in a remuneration case, dealt with the question whether the registrar was correct in disallowing as remuneration sums that represented a mark-up to the office-holder's firm's rates on the costs of an independent contractor who had been engaged to undertake certain specialist work. In that context he identified and elaborated on a conflict alluded to by Ferris J in *Mirror v Maxwell* clarifying it in stark terms:

> "57… [The joint provisional liquidators] cannot negotiate with themselves over their remuneration. If one analyses the position in the terms of legal responsibilities it appears to me to be as follows. The JPLs as office holders owe fiduciary duties to maximise the return for the benefit of the estate. They are of course allowed remuneration but that remuneration must be subject to the principle that it can only be reasonable remuneration. As a matter of legal analysis when the JPLs are partners in a firm of accountants they technically retain the firm to act on their behalf. However in practice the JPLs' remuneration rates as partners in a firm of accountants are used as the yardstick for the basis for their remuneration. Technically I do not think that is correct because it is the remuneration of the JPLs *qua* office holders that is being assessed and not their remuneration qua partners in a firm of accountants. There may be a large difference between what might be justified in those two differing capacities. A firm of accountants may be very large and have large overheads which require each partner to charge out his time at a certain hourly rate to cover the overheads and make a profit. It does not follow that all the overheads burden for example can be reflected in an hourly rate for which an Office Holder would charge..."

He noted:

> "69. […] The JPLs decided to retain their firm. As such they ought as Office Holder to negotiate the best rate possible (i.e. the cheapest[13]) for the utilisation of their firm. It is not sufficient in my view simply to expect that the partner's hourly rate would necessarily be appropriate."

[11] In fact, in *Mirror v Maxwell* the legal costs and the office-holders' remuneration were overwhelmingly approved on assessment.
[12] [2006] EWHC 2717.
[13] I would respectfully disagree: price may be a significant factor, but it cannot be the only one in every case. An office-holder will almost always have to take other matters into consideration such as reputation, expertise, available resourced and so on (see para 54 of the *Ethics Code* of the Insolvency Practitioners Association.

So, the consequences of properly identifying the conflict between the office-holder's fiduciary duty to the estate and that to, say, his or her partners[14] may be that he or she must cut his or her firm's rates or – arguably – subcontract certain work, even perhaps to another firm, to get "the best rate possible for the job (i.e. the cheapest)."

Unsurprisingly, Peter Smith J disallowed the mark up (as had the registrar below) and held the office-holder in the case to the true sub-contract rates agreed.

If what Peter Smith J says is correct as it applies to specialist work undertaken in the administration of an insolvency in relation to which the office-holder has been appointed, as was the case in *Jacob v UIC*, it must apply similarly to more routine work that is sub-contracted (e.g. to solicitors and counsel or to valuers).

Another way of looking at the proper approach to sub-contracting is by reference to the office-holder's obligation when incurring disbursements.

> "The office-holder must act responsibly in incurring disbursements, and in particular legal fees. Most disbursements will however be a matter for the office-holder's discretion and the court will not interfere unless it appears that the office-holder has acted outside [the] generous ambit of allowable discretion (see, e.g. *Freeburn v Hunt* [2010] BPIR 494). In [*Jacob v UIC*] the court held that…the success of the provisional liquidation could be taken into account when fixing remuneration, but that should not involve a success fee beyond reasonable remuneration."[15]

That statement of the law, which it is submitted must be correct, necessarily applies to legal costs, which again has implications for the process an office-holder ought to go through in considering how any litigation on which he or she intends to embark is to be conducted, i.e. by whom, at what cost and even how it will be funded.

(b) Testing the market

A modern office-holder faces a bewildering array of choice when deciding how to finance litigation. Where he controls funds or assets that enable him to litigate in the same way as any other party he may legitimately do so provided that he exercises proper commercial judgment, considers whether he would hazard his own money as he plans to use that which he holds for the creditors (and possibly the members) and keeps the costs under review to ensure that they are justified. Lack of funds or assets coupled with the need to be indemnified if things go wrong may, and often do, militate against a decision to fund litigation in this way. Broadly, that leaves the office-holder with the following funding options: a conditional fee agreement, a damages based agreement, funding or assignment of the proposed cause of action. He must decide which broad funding model (or combination thereof) to adopt as well as negotiate appropriate terms (especially where there is to be a success fee, and even within litigation funding models which vary widely as between the different providers). He must now test the market and be able to support with reasons the decision he makes if it is later questioned. He must make his decision with his fiduciary obligations firmly in mind. The astute office-holder will, then, be

[14] The conflict does not apply only in insolvency; indeed it is present in many fiduciary relationships: see, for example, *Fripp v Chard Railway Co* (1853) 11 Hare 241 where the court identified it in the appointment as manager of a canal of one of that canal's most important customers: "There must…be, so long as he occupies his double position, a considerable conflict between his interest and his duty…" (*per* Page-Wood VC).

[15] Bailey and Groves, *Corporate Insolvency: Law and Practice* (5th edition) para 6.51.

concerned to litigate in the most efficient way possible, i.e. so as to concentrate on getting his or her claim disposed of (whether at trial or by settlement) as cheaply, quickly and efficiently as possible.

(c) Satellite litigation

That means avoiding, if possible, unnecessary interlocutory applications and satellite litigation. The law reports are replete with statements deploring satellite litigation, especially when it comes to questions of costs, whether they arise before or after trial. In recent times it was arguments about CFAs that started the ball rolling in the form of a range of technical arguments about the Conditional Fee Agreements Regulations 2000. The Court of Appeal commented on the phenomenon in *Jones v Wrexham Borough Council*,[16] Waller LJ noting:

> "The unsatisfactory way in which satellite litigation has mushroomed with challenges to the enforceability of CFAs, by reference to those regulations, was spelt out in the judgment of the court…in a decision dealing with a number of cases including *Hollins v Russell*…The court in the above decision sought to discourage the taking of technical points by Defendants on the 2000 regulations."

Even before then in *Hamilton v Al Fayed (No 2)*,[17] a case about third party funding costs orders, the Court of Appeal had commented on satellite litigation on costs; and it has done so more recently again in ***R (on the application of Buglife) v Thurrock Thames Gateway Development Corporation***[18] on costs budgets and protective costs orders in which the Master of the Rolls said,

> "In our opinion the courts should do their utmost to dissuade parties from engaging in expensive satellite litigation on the question of whether [protective costs orders], and thus cost capping orders, should be made. […] The expenditure of such costs cannot be in the public interest."

Funded cases have made their contribution too, in the third-party costs realm but also in relation to applications for security for costs which have seen arguments over the terms of ATE insurance backed funding. (For examples of cases in which the courts have looked closely at the policy see *Michael Philips Architects Ltd v Riklin*[19] and more recently *Hotel Portfolio II UK Limited (in liquidation) and Anor v Ruhan and Anor.*[20]) Happily the position has been simplified and clarified as a result the decision of Stuart-Smith J, as he then was, in *Geophysical Service Centre Co v Dowell Schlumberger (ME) Corp*[21] in which he said,

> "In the absence of evidence to the contrary, the court's starting point should be that a properly drafted ATE policy provided by a substantial and reputable insurer is a reliable source of litigation funding;"

[16] [2007] EWCA Civ 1356.
[17] [2002] EWCA Civ 665.
[18] [2008] EWCA Civ 1209.
[19] [2010] BLR 569.
[20] [2020] EWHC 233 (Comm).
[21] [2013] EWHC 147 (TCC).

but the court's qualifications ("properly drafted" and "substantial and reputable") should be noted.

The "Arkin cap", so called after the decision of the Court of Appeal in *Arkin v Borchard Lines Ltd*,[22] in which the court capped the costs liability of a litigation funder which had funded part of the unsuccessful claim but not the whole, has given rise to its fair share of satellite litigation; but in reality it was always fact-specific. To the extent that anyone thought otherwise it is now clear they were wrong: the Arkin cap has recently been firmly put in its place by Snowden J. In a case called *Davey v Money*[23] he rejected the idea of its being a legal principle. In his view the Court of Appeal was "simply setting out an approach that it envisaged might commend itself to other judges exercising their discretion in similar cases in the future;" it was not, he said, "a rule to be applied automatically in all cases involving commercial funders, whatever the facts…" He went on, having regard to the facts of the case before him, to award full costs against the funder in favour of the successful party. Snowden J's decision should come as no surprise, given the wide ambit of the court's discretion when it comes to questions of costs. Similarly, it is unsurprising that Snowden J's judgment was upheld on appeal (see *Chapelgate Credit Opportunity Master Fund Ltd v Money).*[24]

(d) Proper purpose

Before bringing legal proceedings, an office-holder might also wish to consider that he or she is bringing them for a proper purpose, i.e. for a purpose that accords with the purpose of appointment.

The proper purposes principle generally applies to directors, but it has been suggested that it can apply to any person exercising a fiduciary duty. Thus,

> "The proper purposes doctrine, also known as fraud on a power, is a cornerstone of the law of legal powers. The donee of a fiduciary power must exercise it only for the purposes for which it was conferred by the donor. For company directors, this rule is codified in s 171(b) of Companies Act 2006, which states that directors must 'only exercise powers for the purposes for which they are conferred'."[25]

Its application to holders of an insolvency related fiduciary office was recently considered by Chief ICC Judge Briggs in *Brewer and another (as joint liquidators of ARY Digital UK Ltd) v Iqbal*:[26]

> "[43]The authors of Lightman and Moss *The Law of Administrators and Receivers* state, in short, that the obligation to act for a proper purpose is a duty imposed on directors who have trust-like duties. At para 12–037 the authors say that there are controls 'on the exercise of powers vested in fiduciaries' and —

[22] [2005] EWCA Civ 655.
[23] [2018] EWHC 766 (Ch).
[24] [2020] EWCA Civ 246, although Newey LJ also said that the court's judgment did not mean that *Arkin* had become redundant: "There will, I am sure, continue to be cases in which judges decide that it is right to follow the course espoused in *Arkin*, as Zacaroli J did in *Burnden Holdings (UK) Ltd v Fielding*."
[25] Remus Valsan, "The exercise of fiduciary powers for mixed purposes: A comment on Eclairs Group Ltd v JKX Oil and Gas plc," *Edinburgh Centre for Commercial Law blog*, 8 April 2016 (http://www.ecclblog.law.ed.ac.uk/2016/04/08/the-exercise-of-fiduciary-powers-for-mixed-purposes-a-comment-on-eclairs-group-ltd-v-jkx-oil-and-gas).
[26] [2019] EWHC 182 (Ch) [2019] 1 BCLC 487.

> 'While these controls have been developed primarily in cases concerning the powers of express trustees and company directors, they apply mutatis mutandis to insolvency office-holders. Accordingly, an administrator must: (i) act within his powers; (ii) exercise his powers in good faith; and (ii) exercise his powers for a proper purpose. The "proper purpose" control on the exercise of office-holder powers derives from the "fraud on a power" doctrine in trusts law and its variant in corporate law, the duty of a company director to exercise powers for the purpose for which they are conferred, now codified in the Companies Act 2006 s. 171(b). Its effect is to prohibit the administrator from exercising his powers for a purpose, or with an intention, beyond their scope. It follows that the administrator must not act perversely or irrationally or for irrelevant or extraneous reasons as, properly understood, in doing so he would be abusing his powers by acting beyond their scope'.
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> [44]In my judgment this is an accurate statement of the law. Even though the proper purpose doctrine is not itself a fiduciary duty, because it is not special to fiduciaries, that does not mean that the doctrine of proper purpose has no role to play for those who exercise fiduciary powers […]"

Whilst cases in which an office-holder would seek to bring insolvency proceedings for an improper purpose will be rare, the reason for bringing such proceedings will necessarily be a matter to which any funder will wish to apply its mind before funding or taking an assignment of such proceedings.

III. ASSIGNMENT OF CLAIMS

The assignment of claims by an office-holder does not necessarily involve consideration of all the fiduciary duties considered above, although plainly some will still apply (notably the need to exercise commercial judgment).[27]

An office-holder has always been able to assign certain claims. In fact the ability of an office-holder to assign a cause of action is older than one might think. In 1880, the Court of Appeal approved the practice of what was a form of litigation funding in an insolvency context in a case called *Seear v Lawson*.[28] The case report records:

> "The trustee in bankruptcy of a man who had conveyed away some real property absolutely, commenced an action against the grantee to have it declared that the conveyance was a mortgage, and that the deed ought to stand as a security only for the money advanced. The action had proceeded no further than the issue of the writ, when the trustee sold and assigned the subject-matter of the action to a purchaser for value."

The Court of Appeal held that the assignee was entitled to continue the action. So, once you were bankrupt it was possible for your trustee simply to sell your cause of action, but if you were merely poor, it was wrong, indeed (at least until 1967) a criminal offence, for you to get a third party even to fund your litigating the action, whether or not in return for a share of the proceeds.

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[27] For a good, if now dated, treatment of the topic of assignment and insolvency see Rick Munro, "Assignment of causes of action – by insolvency office holders", (1998) Vol 14, No 2 IL & P 148; and more recently, Robert Hantusch, "Powers and responsibilities: assignments of causes of action by Office Holders", (2012) 4 CRI 118.

[28] (1880) 15 Ch D 426.

In addition to acting *bona fide* and within his or powers, an office-holder who decides to sell an asset owes a duty of care. He or she will be judged according to the standard of the reasonable person acting in his or her own affairs. He or she will be expected to exercise reasonable commercial judgement[29] and to act with reasonable care and skill. In this regard the standard by which he is judged is the standard of a reasonably skilled and careful practitioner.[30] If an office-holder decides to sell a company's business or a particular asset, including a cause of action, the duty of care will extend to decisions as to the time to sell and to valuation and marketing, all of which should be done with a view to obtaining the best price for the asset.[31] A decision to sell or assign is also likely in many cases to give rise to regulatory matters to which an office-holder will have to pay regard.[32]

The decision to assign could involve personal risk to the office-holder in the form of a claim for costs.[33] A liquidator may be held to have been unable to assign certain rights that he enjoyed by reason of the exercise of his office. Thus, in *Re Ayala Holdings Ltd (No 2)*[34] the court held that although the assets of a company were assignable by sale under para 6 of Sch 4 Insolvency Act 1986, the rights conferred upon a liquidator in relation to the conduct of litigation were not because they were an incident of his office, for which reason a deed of assignment he entered into in that case did not operate to vest in another litigant any rights which he might have under s. 127 Insolvency Act 1986[35] or s. 395 Companies Act 1985 to recover payments made by the bank after the commencement of the winding up of the company.[36] That position has changed (although not in relation to s. 127 relief or the procedural route available to an office-holder under s. 212) as a result of the insertion into the Insolvency Act 1986 of s. 246ZD:[37]

> (1) This section applies in the case of a company where—
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> (a) the company enters administration, or
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> (b) the company goes into liquidation;
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> and "the office-holder" means the administrator or the liquidator, as the case may be.
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> (2) The office-holder may assign a right of action (including the proceeds of an action) arising under any of the following—
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> (a) section 213 or 246ZA (fraudulent trading);
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> (b) section 214 or 246ZB (wrongful trading);
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> (c) section 238 (transactions at an undervalue (England and Wales));

[29] *Re T & D Industries plc* [2000] 1 WLR 646.
[30] *Re Charnley Davies Ltd (No.2)* [1990] BCC 605.
[31] See e.g. *Davey v Money* [2018] EWHC 766 (Ch); [2018] Bus. LR 1903; *Silven Properties Ltd v Royal Bank of Scotland Plc* [2000] BCC 727.
[32] For example, those set out in *Statement of Insolvency Practice 13* where the assignment is to a connected third party.
[33] For a comprehensive review of the law as it stood in 2012 see Stephen Davies QC and Paul French, *Assignment of Claims*, Guildhall Chambers, May 2012. (https://www.guildhallchambers.co.uk/files/Assignments_of_Claims_StephenDaviesQC_&_PaulFrench_May2012.pdf).
[34] [1996] 1 BCLC 467.
[35] Whether in fact the right to litigate to recover void dispositions is that of the liquidator or the company is, however, open to question: see McPherson & Keay in their *Law of Company Liquidation* (4th edn para 7-038) and the judgment of HHJ Kolbert in *Mond v Hammond and Suddards* [1996] 2 BCLC 470.
[36] See also *In re Oasis Merchandising Services Ltd* [1998] Ch. 170.
[37] Section and cross-heading inserted (1 October.2015) by Small Business Enterprise and Employment Act 2015. For a recent authority disposing of an ingenious but unsuccessful attack on the ability to assign an office-holder's cause of action see *Cage Consultants Ltd v Iqbal & Anor (Re Totalbrand Ltd and the Insolvency Act 1986)* [2020] EWHC 2917 (Ch).

(d) section 239 (preferences (England and Wales));

(e) section 242 (gratuitous alienations (Scotland));

(f) section 243 (unfair preferences (Scotland));

(g) section 244 (extortionate credit transactions).[38]

The assignment of the causes of action covered by s. 246ZD has become increasingly attractive to office-holders, in particular in cases where it is undesirable to keep an administration or liquidation open for a long period to deal with potential litigation and/or because of the prospect of a more certain and immediate realisation of an asset. Whilst, as noted above, assignment may still engage fiduciary duties, in common with any other asset sale it is more likely to engage the obligation to sell for the best price obtainable.[39] This does not, however, mean that such assignments can always be made without regard to potential consequences other than a failure to get the best prices, as is amply demonstrated by the recent decision of David Halpern QC, sitting as a deputy judge of the High Court, in *Re Meem SL Ltd Goel v Grant*.[40]

Valuable guidance as to the proper approach to the assignment of causes of action has now been given by Morgan J in *LF2 Ltd v Supperstone and Shiners*.[41] It is worth setting out fully:

> "65. A viable claim by the company against a third party is an asset of the company. A claim which is arguably viable, is a potential asset of the company. In principle, an administrator ought to be ready to investigate whether such an asset should be preserved and pursued. Of course, there may be obstacles in the way of doing so. The administrator may have no funds with which to take legal advice. In such a case, it may be open to the body of creditors to provide the necessary funds.
>
> 66. If the administrator has no funds to investigate a possible claim against a third party and he receives an offer from a potential assignee of the claim to pay for an assignment, that offer will potentially constitute an asset of the company. The administrator should normally wish to preserve and pursue that asset. If it is clear to the administrator that the claim would be hopeless and that the potential assignee is bent on pursuing a hopeless claim in order to harass the third party, then the administrator should normally decline to assign the hopeless claim. The administrator is an officer of the court and the court expects him to behave honestly and fairly. In the same way as the court would not direct an assignment of a hopeless claim where the court was of the view that the assignee's intention was to use the hopeless claim to harass a third party, then the administrator might well take the same view as to his own participation without finding it necessary to seek a direction from the court.
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> 67. But there will be other cases. One such case is where the administrator does not have a clear view that the proposed claim would be vexatious and he is offered a sum

[38] For an ingenious but unsuccessful attack on the principle of an office-holders ability to assign under s. 246ZD see *Cage Consultants Ltd v Iqbal* [2020] EWHC 2917 (Ch) and Snowden J's discussion of the policy informing the provision.
[39] Cf the duty of a mortgagee to the mortgagor to obtain the best price reasonably obtainable on a sale of the mortgaged property: *Cuckmere Brick Co. Ltd v Mutual Finance Ltd* [1971] 2 WLR 1207. See also *Standard Chartered Bank Ltd v Walker* [1982] 1 WLR 1410 and *Silven Properties Ltd v Royal Bank of Scotland* [2003] EWCA Civ 1409; [2004] 1 BCLC 359. For a recent example of judicial criticism of an office-holder for failure to do this see *Brewer v Iqbal* [2019] EWHC 182 (Ch); [2019] BCC 746.
[40] [2017] EWHC 2688 (Ch), [2018] Bus LR 393, [2018] BPIR 878.
[41] [2018] EWHC 1756 (Ch).

> of money for the assignment of the claim. In such a case, the administrator should be prepared to obtain a proper payment for the assignment. If it is not clear that the offer reflects the true value of the cause of action, then the administrator may well be advised to conduct some process of inviting rival bids or to hold an auction of the cause of action. The receipt of a sum of money for the claim would be likely to benefit someone, whether it is the administrator (as a contribution to his expenses) or the creditors.
>
> 68. There may also be practical considerations and time pressures which the administrator has to take into account. If the administrator is considering whether the company has a potential claim and there is a high risk that the limitation period for the claim may be about to expire, the administrator may have to take immediate action to protect a potential asset of the company. The administrator may have to cause the company to issue a protective claim form or even to conduct some rapid negotiations to obtain the best available offer for an assignment of the cause of action."

(a) Challenges to office-holder decisions

The question arises, to what extent can an office-holder's decision about funding be challenged by a creditor or other party with an interest in the insolvency?

Para 74 Sch B1 Insolvency Act 1986 allows a creditor or member to apply to the court if an administrator is acting "unfairly [so as] to harm the interests of the applicant;" para 75 allows the court to examine the conduct of an administrator (albeit in restricted circumstances); and para 88 allows the court to remove an administrator from office. Section 167(3) puts every winding up by the court under the control of the court. Section 168(5) permits a person "aggrieved by any decision of the liquidator…to apply to the court" such that "the court may confirm, reverse or modify the act or decision complained of, and make such order…as it thinks fit." Section 108 gives the court jurisdiction to remove a liquidator. Section 363 provides for the general control of a bankruptcy by the court, while s. 303(1) enables any person "dissatisfied by any act, omission or decision of a trustee in bankruptcy" to "apply to the court" such that "the court may confirm, reverse or modify any act or decision of the trustee" or give directions.

Generally, however, the ability to challenge an office-holder's decision is limited to those with a proper interest in doing so, in the case of corporate insolvency usually only creditors and contributories.[42]

An office-holder enjoys what the courts have described as a generous ambit of discretion in his/her decision making. He is entitled to make decisions without having constantly to look over his shoulder.[43] His decisions are not immune from challenge, but unless he has gone badly off the rails, he can generally expect the court to support him in the proper exercise of his judgment.[44]

Directions may be sought by the office-holder too;[45] but it would seem unlikely that the courts will help when it comes to what they are likely to consider to be a commercial decision

[42] See, for example, *Re Stay in Style Ltd* [2020] EWHC 538 (Ch).
[43] Cf *Re A Debtor, (No 400 of 1940) ex parte Debtor v Dodwell (Trustee)* [1949] 1 Ch 236, [1949] 1 All ER 510; *Re Edennote Ltd* [1996] 2 BCLC 389; *Osborn v Cole* [1999] BPIR 251, followed in *Supperstone v Hurst (No 3)* [2006] BPIR 1263 and *Shepherd v Official Receiver*[2007] BPIR 101.
[44] For the reasons given in the authorities cited in the previous footnote.
[45] See, for example, ss. 168(3) & s. 303(2) Insolvency Act 1986.

for the office-holder. Practitioners will be all too aware of the well-known *dictum* of Neuberger J in *Re T & D Industries plc (in administration); Re T & D Automotive Ltd (in administration).*[46]

> "My decision tends to emphasise the fact that a person appointed to act as an administrator may be called upon to make important and urgent decisions. He has a responsible and potentially demanding role. Commercial and administrative decisions are for him, and the court is not there to act as a sort of bomb shelter for him."[47]

In *LF2 Ltd v Supperstone* Morgan J referred, albeit in passing, to the rule in *Ex parte James*[48] in a way that implied that it might provide a route by which an office-holder's decision of the kind under consideration might be scrutinised. He said:

> "55. This passage [he was citing from another authority] does not identify the legal principle which produces the result that the office holder should be circumspect before assigning a cause of action. As the office holder has a statutory power to assign the cause of action and has a duty to act in the interests of the creditors, it might be thought that if the assignment produced a benefit for the creditors then the office holder should be prepared to receive that benefit, unless the case came within the principle in *Ex parte James, In re Condon* (1874) LR 9 Ch App 602. That principle might mean that it would not be honest and fair for the office holder to assign an alleged cause of action where a claim by the assignee would be frivolous or vexatious."

The rule fared less well, however, before Hildyard J in *Lehman Brothers Australia Ltd (in liquidation) v Lomas*[49] who reiterated a fear he himself had already expressed that if used too liberally the rule could become an "unruly horse". It might, therefore, be safer to assume that the courts will be unlikely to favour reliance on it when it comes to challenging office-holders' commercial judgments.

IV. CONCLUSION

As Arden LJ noted in *In Re Stanford International Bank Ltd,*[50] "[L]ike a director, [a liquidator][51] is a distinct species of fiduciary whose office is an amalgam of statutory rules and agency and trust principles."[52] As regards the fiduciary aspect of the office-holder's duties, it would seem from the case law examined in the earlier part of this article that an officer-holder needs to have in mind the following fundamental propositions when he or she is contemplating engaging solicitors/counsel, or indeed any other sub-contractor:

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[46] [2000] 1 All ER 333, [2000] 1 BCLC 471.
[47] Cf *Re Stetzel Thomson & Co Ltd* (1988) 4 BCC 74 in which Harman J decided that it would not be appropriate for the court to give directions to a liquidator as to which of two courses he should take: "In my view, the only possible answer to this matter is to say that the liquidators must take their own view, administer the fund as they think fit, and if adverse claims are brought against them they will have to resist those adverse claims as best they can."
[48] *In re Condon, ex parte James* (1874) LR 9 Ch App 602. For a recent and thorough review of the authority see *Lomas and others (Joint Administrators of Lehman Brothers International (Europe) (In Administration) v Burlington Loan Management Limited* [2015] EWHC 2270 (Ch).
[49] [2018] EWHC 2783 (Ch).
[50] [2011] Ch 33.
[51] And, presumably, an administrator.
[52] To those duties one must now add the duties that arise from increasing regulation.

(a) The fiduciary nature of his/her duties. Whilst he/she is entitled to be paid out of the assets under his/her control, that represents an exception to the general obligation to account to the beneficiaries.
(b) For that reason, he/she must justify the work done and the remuneration sought for doing it. (That applies also to work done by others on the office-holder's behalf.)
(c) That means keeping proper records recording decision-making processes so as to be able to account for expenditure made.
(d) An office-holder needs to be alive to the conflict between his/her duties to partners (or their equivalent in non-partnerships) and to the estate under his/her control.
(e) An office-holder is expected to exercise proper commercial judgment.
(f) That means the office-holder must ask whether he/she would spend ("hazard") his/her own money in the way for which he/she seeks to claim.
(g) The value of the work done is more significant than time spent doing it. (But value does not necessarily equate to success.) If time cost is not the be all and end all as regards an office-holder's own remuneration, the same must apply to legal costs.
(h) Overall cost is more important than the time cost rate of any individual employed.
(i) Market rates may be taken into account.
(j) Best value should be sought when sub-contractors are being used.
(k) All costs and expenses should be the subject of critical scrutiny.
(l) Success may be rewarded (presumably by reference to the criterion implied by value).
(m) Satellite litigation should be avoided.
(n) The whole range of funding options must be considered when contemplating litigation.

He or she will also have to comply with or take into account a range of statutory, equitable, common law and regulatory obligations.

If the foregoing is a correct analysis of the law, then, when thinking about litigating, an office-holder needs to consider carefully the identity and expertise of the legal firm to which he intends to sub-contract (or pay by way of disbursement) as part of his/her obligation to exercise proper commercial judgment. He or she must, as part of that exercise, also consider how any litigation on which he or she intends to embark should be financed or whether assignment would be a better option. If there is to be a success fee (whether under a CFA or DBA or in less direct form by payment of an element out of the recovery to a funder) it should be reasonable in all the circumstances: it should reflect the value of the work done or to be done. If funding is to be used, again the office-holder must consider whether it represents good value. He must ask which of the funding possibilities available is the most reasonable, having regard to risk and all the other factors properly to be taken into account; and answer that question by reference to Ferris J's proposition that he/she must ask whether he would hazard his own money in the way he plans to hazard that of the estate under his control.

When it comes to assigning causes of action the office-bolder will now have to apply his or her mind to the matters set out by Morgan J in the *LF2 Ltd* case as well as the more familiar question, applicable to a cause of action as to any asset, whether any assignment envisaged will produce the best possible result in terms of value for the creditors. There may still, however, be scope for exposure to a third party costs order, so assignment to a funder with an appropriate indemnity may still be the preferred option for a prudent office-holder. At all times

he or she, whilst enjoying the ambit of the famously wide discretion discussed above, will also have a weather eye on the possibility of adverse costs awards, a challenge to his or her decision making and, in extreme cases, the possibility of being attacked on the basis of having brought an ill-judged or improper action that might be said to amount to misfeasance or negligence or (rarely, one would suppose) to have been brought for an improper purpose.

(a) Postscript: empirical research

In late 2019/early 2020 Prof Peter Walton undertook empirical research on the state of the funding market for insolvency cases.[53] He found that CFAs remained a popular method of funding insolvency cases, especially the smaller ones,[54] but that funding was rapidly gaining ground, with three in five insolvency practitioners confirming that they had begun to use funders or turn to them more often than in the past (although funding still had some way to go in gaining traction in the insolvency market[55]). He concluded that,

> "There are…some IPs whose practice is very litigious in nature and they appear to be using the full array of funding options available to them. Some IPs are beginning to use funders whilst others have yet to do so (or at least did not do so in the previous 12 months)."[56]

Loss of control was a perceived objection to funding, especially where the case is assigned (which suggests that many office-holders are astute to keep in mind the interests of creditors), but as against that many recognised "the use of funders as most likely to lead to a swift commercial resolution to an insolvency claim although over a third favours the use of CFAs and ATE."[57]

Significant in terms of recognition of an office-holder's fiduciary duties is this finding:[58]

> "Of the 80 respondents who answered [question 10[59]], nearly all said yes but a very small minority stated no. Some expanded upon their answer in the negative by explaining they did not consider funding options until they had initial advice or followed legal advice on funding. Overwhelmingly IPs said they did consider all possible funding options although one said his or her belief was that many IPs did not do so."

Equally encouraging is his finding that maximising returns to creditors was a factor that 87.06% of respondents took into account in deciding how to fund a legal action. Walton goes on, however, to note:[60]

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[53] Peter Walton, *Insolvency Litigation – in the best interests of creditors?* (Wolverhampton, 2020).
[54] "The answers to [question 6], when compared to the answers to Question 2 above, suggest that funders tend to be used in bigger value cases. Smaller cases are more likely to continue to use (often informal) CFAs with or without ATE cover" (p. 28) Cf later: "The answers to [question 12] show that, due to the Jackson Reforms, a significant number of IPs have started to use funders (28%) or increased their use of funders (29%) although over a third have continued as before using CFAs and ATE" (p. 35).
[55] "Only 43 of respondents had used a third party funder or assignee in the previous 12 months. This is almost half of the number of IPs who had used a CFA. Of the 43, 26 had also used CFAs (in significant numbers – in total 177 CFA-backed actions bringing in a net figure of £38,160,000). This suggests a reasonable number of IPs are considering their options and using either a CFA or funding depending upon the facts of each case" […] "Nearly half of the 43 (19) had used funding or assignment in only a single case" (p. 27).
[56] Page 27.
[57] Page 32.
[58] Page 33.
[59] Before starting a legal action do you consider all the ways in which it might be funded before instructing solicitors?
[60] Page 34.

> "The next two most popular answers were using trusted lawyers and securing an indemnity for adverse costs. It is perhaps reassuring that the most popular answer to this question was 'Maximising the return to creditors.' Adverse costs concern is certainly extremely understandable and again it is reassuring that legal advice from trusted lawyers is such a popular answer. It suggests that lawyers' advice is being sought and followed in such cases. This is consistent with the fiduciary duty of an IP discussed above in Part III. Speed of getting to trial or settlement was the next popular answer followed by an IP recognising the fiduciary duty to consider expending funds in the same manner as if they were the funds of the IP. Maximising fees was a minority answer but still relatively popular."

Also gratifying is Walton's finding that:[61]

> "A number of respondents emphasised the need to consider all funding options. There was a divergence of views in terms of which funding option provided better returns to creditors. Some suggested that litigation funding was more effective whilst others believed that using a CFA (with or without ATE insurance) generally led to better creditor returns."

This would appear to indicate that a significant number of office-holders have their fiduciary obligations well in mind when considering how to fund litigation they are contemplating. Other findings suggest that the funding market needs to develop and enhance its products to meet practitioners' needs and concerns.

Walton concludes his study with a number of recommendations, but helpfully includes an appendix entitled "Suggested Checklist When Using a Funder or Assignee". It is an admirable summary of the practical questions an insolvency practitioner should be asking when thinking about funding. It should be on every insolvency practitioner's desk.

[61] Page 37.