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Legal Q&A

Rebecca Walker answers your insolvency queries.

Q The administrators of a company have received an offer for the company's business and assets of £1, plus the assumption of certain liabilities. Are there any issues with this?

A The administrators need to remember that they have a duty to act in the interests of creditors as a whole (which includes unsecured creditors). In discharging their duties, they should consider whether the prescribed part applies in order to ensure that the interests of unsecured creditors are not prejudiced by a no-cash deal.

What is the prescribed part?

The prescribed part is a fund set aside for unsecured creditors out of floating charge realisations. Broadly, it applies where a company created a floating charge over its assets on or after 15 September 2003.

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The prescribed part is calculated on a sliding scale, depending on the value of floating charge realisations, and is capped at £600,000. As it is not necessary to carve out a prescribed part from fixed charge realisations, it is important to establish whether each of the company's assets are subject to fixed or floating charges.

Fixed or floating charge?

There is a two-step process in analysing this question:

1. *What are the terms of the debenture?* Debentures typically purport to create a fixed charge over a list of assets; include a 'catch all' provision, such that, if any of the listed assets are not caught by the fixed charge, they will instead be caught by a floating charge; and allow disposals of some or all charged assets in the ordinary course of business (known as a 'permitted disposals' clause).
2. *What does the law say?* Case law has developed the following list of characteristics of a floating charge:
   - the charge is over a class of assets, present and future;
   - the charged assets change from time to time; and
   - the company is free to deal with the charged assets in the ordinary course of its business (ie they are not under the charge holder's control) (see *National Westminster Bank PLC* v. *Spectrum Plus Ltd* [2005] UKHL 41). In this regard, an unprecedented or exceptional transaction can be regarded as being in the ordinary course of business even if it is not part of the company's day-to-day operations, but a transaction that is intended to bring an end to the company's business cannot (see *Ashborder BV* v. *Green Gas Power Ltd* [2004] EWHC 1517 (Ch)).

So where a debenture purports to create a fixed charge over an asset that has the characteristics of a floating charge, the charge will instead take effect as a floating charge (under the 'catch all' provision in the debenture). And the 'permitted disposals' clause is key to determining whether an asset is secured by a fixed or floating charge: while the debenture might state that the asset is subject to a fixed charge, if the debenture permits the company to dispose of it without the charge holder's consent, it must be a floating charge asset.

Conclusion

A review of the debenture and applicable case law will be required in every case. In the event that the prescribed part would apply to a cash offer, unsecured creditors may be prejudiced by a no-cash deal unless the purchaser increases the cash element of its offer to cover the prescribed part liability.

Q My client is looking to acquire a (solvent) business. The parties have agreed that a proportion of completion monies will be paid into escrow to collateralise certain warranties in the sale agreement provided by the seller. Are there any risks if either the seller or the buyer goes insolvent while the monies are still held in escrow?

A Naturally, the answer will depend on how the escrow arrangement has been set up and the escrow agreement has been drafted.

Typically, the buyer will hold back a proportion of the completion monies and place these into escrow. Whether or not the escrow arrangement expressly deals with this, it is usually the case that the monies remain the property of the depositor (buyer) until the end of the warranty period, at which point any balance will be paid to the seller. The result of this is that the seller (or an insolvency practitioner appointed in respect of the seller) has no title in, or claim to, the monies until the end of the warranty period.

The escrow monies are, however, not safe in the event of the depositor's insolvency. In *Re A/Wear UK Ltd (In Administration)* [2013] EWCA Civ 1626 it was noted that, as title in the escrow monies remained with the depositor until the trigger condition occurred requiring the monies to be paid out to the other party,

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any insolvency practitioner appointed to the depositor would normally have the right to claim the escrow monies as forming part of the depositor's insolvent estate. In *Re A/Wear*, it was only because the trigger condition had occurred prior to the date of administration that the administrators failed in their attempts to claim the monies for the benefit of creditors. □

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