IP LIABILITY – AN OVERVIEW

INTRODUCTION

1. The framework within which an insolvency practitioner operates is statutory by nature. The Insolvency Practitioner requires a detailed knowledge of Insolvency Act 1986, its various schedules, the Insolvency Rules 1986 and Statements of Insolvency Practice. The applicable statutory provisions are substantial in amount and specific in nature setting the Insolvency Practitioner apart from most other professionals. Nevertheless in common with other professionals common law negligence has its part to play. Common law negligence will overlap the statutory framework so that the Insolvency Practitioner will, when transacting with another, in accordance with his statutory obligations, owe a duty of care to certain categories or classes of people. In addition the Insolvency Practitioner may at times, form obligations that will be cast in contractual terms.

2. It is apparent from the above that the danger of professional negligence for Insolvency Practitioners may lurk in every corner of his practice and will arise within very broad contexts: from personal insolvency issues to large corporate administrations and re-structuring. Whether the Insolvency Practitioner calls a meeting of creditors, steps into the shoes of a company's management to run a business or seeks to sell off assets his judgment will always be tested. A leading text on professional negligence puts the matter this way:

> "Traditionally, the professions operate in spheres where success cannot be achieved in every case. Very often success or failure depends upon factors beyond the professional person's control….Even where the critical factors are within the professional person's control, he still cannot guarantee success. In matters of fine judgment or great complexity no human being can be right every time[1]."

3. It may be a matter of perception, but the increase in news reports predicting a downturn for major world economies seems to have been accompanied by an increase in the uptake of litigation. One commonly held view is that clients start to turn upon their advisers more when economic growth takes a downward turn. Rather than exploiting an existing market or seeking new markets, the prospect of recovery from a professional advisor becomes increasingly appealing. It may be that recovery from a professional is nothing more than a last resort. Whatever the reason the insurance-backed professional becomes an attractive target. This paper and talk will look at some of the circumstances where an Insolvency Practitioner is exposed to risk by virtue of the statutory and common law duties to which he may be subject.

[1] Jackson & Powell para 2-001

THE STATUTORY FRAMEWORK

4. The Insolvency Act 1986 ("the Act") and the Insolvency Rules 1986 ("the Rules") forms the four corners of the frame within which the Insolvency Practitioner operates. As an office-holder the Insolvency Practitioner will occupy the following positions:

4.1. Provisional Liquidator

4.2. Liquidator

4.3. Trustee-in-Bankruptcy

4.4. Administrator

4.5. Administrative Receiver

4.6. Nominee

4.7. Supervisor

5. The duties of an office-holder will in most cases, but not all, be referable to the Act and the Rules. In the same way his powers will in most cases derive from the Act and Rules. The statutory duties can be divided between those which impose a positive obligations and those that impose a negative obligation.

6. All duties have to be considered in the context of the appointment taken:

6.1. Provisional Liquidators are in an unusual position in that the primary reason for such an appointment is to ensure the preservation of a company's assets pending the hearing of a winding up petition. Accordingly the position is very temporary (or should be very temporary). The functions and powers of a Provisional Liquidator will be provided by the court, will include a power to preserve and may include the power to sell assets: see *Ashborder BV v Green Gas Power Limited* [2005] 1 BCLC 623

6.2. On the other hand a Liquidator is appointed for the purpose of winding up the company's affairs and distributing its assets (s 91(1) of the Act (members voluntary liquidation) and s 100(1) of the Act (CVL)), which involves getting in the company's assets and then distributing them to the company's creditors and members (ss107, 143 of the Act 1986 (CL) and s165(5) of the Act (CVL))

6.3. Similarly a Trustee-in-Bankruptcy is appointed to 'get in, realise and distribute the bankrupt's estate' in accordance with the provisions of Chapter IV of the Act (ss305, 322-332 of the Act)

6.4. Administrators are appointed to manage the affairs, business and property of the debtor company in accordance with the directions of the court or the creditors' proposals, in order to achieve one of the purposes set out in paragraph 3 of schedule B12 to the Act: rescuing the company or, where it is not reasonably practicable to rescue the company, with the objective of achieving a better result for the company's creditors as a whole than would be likely if the company were wound up (without first being in administration) or, where it is not reasonably practicable to rescue the company or achieve a better result for the company's creditors as a whole than would be likely if the company were wound up (without first being in administration), with the objective of realising property in order to make a distribution to one or more secured or preferential creditors.

6.5. Nominees submit reports to the court about voluntary arrangement proposals and if they think appropriate summon meetings to consider them (ss 2 and 3 of the Act for company insolvency and ss 256 and 257 of the Act for personal insolvency)

6.6. Supervisors are charged with supervising the implementation of the terms agreed between the debtor and his creditors in of a voluntary arrangement (ss 1(2) and 7(2) Act for company insolvency and ss 253(2) and 263(2) of the Act for personal insolvency)

6.7. Administrative receivers are in a class of their own in that their functions are not so specifically set out in the Act but are instead referable to the appointment document and the common law. As regards his powers, section 42 of the Act provides that the powers conferred on the administrative receiver of a company by the debentures by virtue of which he was appointed are deemed to include the powers specified in schedule 1 to the Act. His statutory duties are generally limited to reporting: section 48 of the Act: *Re Atlantic Computers* [1992] Ch 505, 525-526

Positive duties

7. As a professional man the insolvency practitioner is under a positive duty to exercise reasonable skill and care in the discharge of his duties. The standard of that duty is not always easy to mark but he will not be expected to use the highest possible degree of skill. Lord Denning remarked[2]:

> "Apply this to the employment of a professional man. The law does not usually imply a warranty that he will achieve the desired result, but only a term that he will use reasonable care and skill. The surgeon does not warrant that he will cure the patient. Nor does the solicitor warrant that he will win the case."

8. The duty to exercise skill and care arises not only in contractual terms and in the the tort of negligence but also as a statutory duty. In the case of a statutory duty a stricter duty may be prescribed so that there could be fault without a want of skill and care.

9. When holding the office the particular post provides specific positive duties and each duty is overlaid with an implied common law duty to exercise skill and care. Below we set out some examples taken from the office of Liquidator, Trustee-in-Bankruptcy and Administrator.

10. As regards a Liquidator the duties arise in the following different ways (this is not an exhaustive list, but intended to provide examples):

10.1. a Liquidator has a duty to investigate the affairs of the company, including its promotion and formation and the conduct of its business in the past, including the conduct of its officers. The duty is positive and he has to undertake the investigation exercising reasonable skill and care;

10.2. By sections 93 and 105 of the Act a Liquidator is under a positive duty to convene a general meeting of the company and in a CVL a meeting of creditors at the end of the first year from the commencement of the winding up and every succeeding year. Interim accounts have to be produced before the meeting;

10.3. The Liquidator is under a positive duty to settle a list of contributories for the purpose of ascertaining who may be liable to contribute to the assets of the company on a winding up: section 79 of the Act. This duty is consistent with his duty to get in the assets of the company. The duty to settle lists is placed on the court in compulsory liquidations, but this duty is delegated to the liquidator: see Rule 4.195 (in Australia the duty is given directly to the Liquidator). The Act also provides that if all shares are paid up or it is not necessary to adjust the lists of contributories, then the court may dispense with the need to draw up a list of contributories: s148(2) of the Act. The Rules allow the Liquidator to dispense with the list but court approval is required to rectify the register of members.

[2] Greaves & Co (Contractors) Limited v Baynham Meikle & Partners [1975] 1 WLR 1095

10.4. A Liquidator is under a positive duty to apply the debtor company's property in satisfaction of its debts and liabilities before making a distribution to shareholders: section 107 of the Act

10.5. The Liquidator has the power to realise assets of the debtor company by virtue of schedule 4 paragraph 6, and his or her duty is to realise the assets in the most efficient way in order to obtain the highest possible value for creditors.

10.6. "It is the duty of a Liquidator to inquire into all claims, to see whether they are well founded or not, to pay the good claims, to reject the bad, to settle the doubtful, or if need be, to contest them. It is only in this way that a Liquidator can fulfill his duty […] of seeing that the property of the company is applied in satisfaction of its liabilities pari passu": *Austin Securities Ltd v Northgate & English Stores Ltd* [1969] 1 WLR 529

11. A Liquidator has a discretion as to how the duties are to be performed.

12. When holding the office of Trustee-in-Bankruptcy a positive duty to exercise skill and care arises in accordance with his functions (again this is not an exhaustive list, but intended to provide examples):

12.1. A Trustee-in-Bankruptcy (in broad terms) is under a positive duty to realise the bankrupt's property for the benefit of creditors but in so doing his duties will include an investigation into the bankrupt's available assets (such investigation includes carrying out an inquiry as to what assets may have been dissipated in the proceeding 5 years)

12.2. To secure the creditors' interest in the bankrupt's assets (e.g. by obtaining a charging order pursuant to section 313 of the Act. After the charging order has been obtained a Trustee-in-Bankruptcy is under a positive obligation to apply to register under the Land Charges Act 1972 or the Land Registration Act 2002 "as soon as reasonably practicable": Rule 6.237D (8) of the Rules)

12.3. To realise the bankrupt's home before it ceases to form part of his estate by reason of the statutory provisions: section 283A of the Act

12.4. When occupying the office of Trustee an Insolvency Practitioner will be under a positive obligation to investigate the prospects of securing an income payments order or agreement pursuant to section 310 or 310A of the Act

12.5. If a bankrupt seeks to annul the bankruptcy order the Trustee-in-Bankruptcy is under a positive duty to file a detailed report on the application: Rule 6.207

13. In a similar way an Administrator is under a positive duty to exercise skill and care when carrying out his statutory functions and duties:

13.1. to give public notice of his appointment by post or by advertisement

13.2. cause the company to issue all business documents with his name upon them and state that the affairs, business and property of the company are being managed by him

13.3. to take custody or control of all the property which he thinks the company is entitled to

13.4. to ensure that any winding-up petition in respect of the company is dismissed or suspended if he is appointed by a floating charge holder

13.5. to require the relevant persons to make or to concur in the making of a statement of affairs

13.6. prepare and issue a set of proposals for achieving the purpose of the administration

13.7. convene and hold a meeting of creditors and subsequent meetings of creditors and act as chairman of the meeting or nominate another suitably qualified person to act as chairman

13.8. to get in the company's property, if necessary by litigation or by mediation or compromise

13.9. he is obliged to calculate the amount to which unsecured creditors are entitled under the prescribed part

13.10. to report to the court and creditors on occasions and to file copies of reports and other documents at Companies House

14. There is also a positive duty on Liquidators, Administrators and Administrative Receivers to report on the conduct of directors under s7(3) of the Company Directors Disqualification Act 1986

Negative duties

15. The term 'negative' in this context is not descriptive but intended to convey the idea that office-holders are sometimes under a statutory duty not to act in certain ways. An example arises in the context of a section 98 meeting. The meeting gives notice to creditors to attend at a certain place at a certain time for the purpose of voting for the appointment of a Liquidator. A Liquidator is expressly forbidden from improperly soliciting proxies in order to secure his appointment: Rule 4.150 of the Rules. Likewise section 164 of the Act makes it an offence for an Insolvency Practitioner to give or agree or offer to give a creditor any valuable consideration with a view to securing his own appointment, or securing or preventing the appointment of someone else.

Remedies provided by the Act

16. As an appointed Administrator, Administrative Receiver, Liquidator or Provisional Liquidator the office-holder may be liable for trespass and conversion of another's property. If the office holder can show that at the time of seizure or disposal he had reasonable grounds for believing that he was entitled to the property then section 234 of the Act affords some protection in respect of any loss or damage resulting from the seizure or disposal of the property.

17. The Act does not protect in two important respects. First where the loss is caused by the office-holder's negligence. Second where the interference with goods and property relates to property that is intangible, such as book debts: *Welsh Development Agency v Export Finance Co Ltd* [1992] BCC 270. In *SCI Games Limited v Argonaut Plc* [2005] All ER (D) Administrators were sued for unlawfully interfering in the performance of the debtor company's contractual obligations which it owed to the Claimant.

18. Liquidators and Administrative Receivers may be exposed to an action, that could be taken by a subsequent Liquidator, creditor, contributory or the official receiver, if there are grounds for showing he has "misapplied or retained or become accountable for any money or other property of the company or been guilty of any misfeasance or breach of fiduciary duty or other duty in relation to the company": section 212 of the Act. The provision is broad and provides a "summary remedy" to repay, restore or account for money or property and a path to bring a claim for breach of duty or misfeasance. However no new cause of action is created by the statute: *Re Eurocruit Europe Limited - Goldfarb v Poppleton* [2007] 2 BCLC 594

19. Similarly (and modeled on section 212 of the Act) paragraph 75 of schedule B1 to the Act allows the same category of persons (including Administrators) to bring an action in respect of the same matters against and an Administrator.

20. As regards Trustees-in-Bankruptcy section 304 of the Act provides a remedy against the office-holder where he has misapplied, retained or become accountable for money or property and permits an action in negligence or breach of fiduciary or other duty to be brought by the Secretary of State, the Official Receiver, a creditor of the bankrupt and (whether or not there is or is likely to be, a surplus for the purposes of a final distribution) the bankrupt himself. A court will have to be

satisfied that any loss to the bankrupt's estate arose as consequence of the breach of duty or misfeasance claimed in relation to the office-holder's functions. To protect an office-holder from harassment from a debtor, permission from the court is required before an action under this section can be launched.

SPECIFIC INSTANCES

21. A Liquidator is given power to carry on the business by schedule 4, paragraph 5 to the Act, but he must have reasonable grounds for believing that carrying on the business is beneficial. In *Re Wreck Recovery & Salvage Co* (1880) 15 Ch.D. 353 at 362 the Court of Appeal held (in the context of a compulsory winding up) that it must be both necessary and beneficial:

> "Now the word 'necessary' means that it must not be merely beneficial, but something more, though the necessity must be determined by the court having regard to all the circumstances of the case. It does not, of course mean that no other course would be possible. Then it must [also] be for the 'beneficial winding up' of the business of the company, not with a view to its continuance"

22. A claim was made by a creditor against a Liquidator pursuant to section 212 of the Act in *Re Centralcrest Engineering Ltd* [2000] B.C.C 727. The claim alleged misfeasance in allowing the company in liquidation to trade without the sanction of the court or the liquidation committee (as required by section 167 of the Act- a positive duty) and misfeasance for the way the Liquidator conducted the liquidation in allowing the company to trade when she should have realised its assets very quickly after her appointment. The Liquidator had allowed the company to trade from October 1992 to January 1995 and during the period of trade had caused the company to make losses of £120,826.

23. In *AMF International Limited* [1995] 1 W.L.R. 77 a Liquidator was appointed to conduct a members' voluntary liquidation. In a declaration of solvency made prior to the winding up the surplus assets of AMF available to contributories were said to amount to £5.9m. However the declaration failed to take account of a lease either as an asset or a liability. A sum of £4.5m out of a total of £5.9m said to be owed to 'trade creditors' was in fact due from the parent company. After the commencement of winding up the Liquidator paid in full most of the creditors but made no payment to the landlords under the lease. He did pay the accruing rent and sought to sublet the unoccupied parts of the premises, but the receipts from the subletting were not enough to cover the passing rent.

24. The Liquidator paid a sum of £920,000 to the parent company as contributory and filed a notice of disclaimer on the landlord making the landlord a creditor to the extent of any loss or damage suffered. The loss and damage suffered was put at about £800,000 and the Liquidator admitted it as a proof for about £600,000. Only £200,000 was paid in respect of the debt and a section 95 meeting was called. A new Liquidator was appointed. Registrar Buckley made an order that the first Liquidator was guilty of breach of duty by failing to deal with the proof of the landlord in a diligent manner and breached his duty by paying the contributory ahead of creditors. The first Liquidator was bound to pay for the loss and damage suffered by the landlord and was not entitled to challenge the original proof submitted of £759,511. In addition the Liquidator was liable to pay interest, costs and the second Liquidator's remuneration.

25. The question of whether a creditor has a direct right to make a claim against an office-holder was considered in *A&J Fabrications Limited v Grant Thornton* [1998] 2 B.C.L.C. 227. The court declined to strike out a claim in negligence against a Liquidator (employed in the defendant firm of Grant Thornton) for failing to prosecute a cause of action with the result that it became limitation barred. On the facts of the case Jacob J. left open the issue of whether a creditor had a direct remedy not only against the defendant firm of accountants but also its chosen Liquidator.

26. The Court of Appeal considered the issue again in *Oldham v Kyriss* [2004] BPIR 165. In that case the appellants were creditors of an insolvent partnership and claimed that they had the benefit of

equitable charges over the partnership assets and in the alternative that they were unsecured creditors of the partnership and had suffered losses as a result of an alleged breach of duty of care which was owed to them by the Administrators. On the equitable charge issue the trial Judge refused to strike out the claims of the respondents as the evidence showed that there was an argument. As regards the claim in negligence the trial judge gave summary judgment for the appellants on the grounds that at common law no enforceable duty of care existed between the Administrators and the unsecured creditors.

27. The Court of Appeal upheld the trial Judge's finding. There is high authority for the proposition that there have to be special circumstances to raise a duty of care where the claimant is once removed: *Henderson v Merrett* [1995] 2 AC 145. The raising of special circumstances in order to bring a direct claim was evident in *Peskin v Anderson* [2001] BCLC 372 where the issue was whether directors of a company owed fiduciary duties to the shareholders.

28. Fiduciary duties owed by directors to the company and fiduciary duties owed to shareholders were a distinguishing feature of the case. The raising of the latter duties was held to be dependent upon establishing a special factual relationship between directors and shareholders. Likewise a special relationship is required for a claim to be made against the office-holder. In reaching this conclusion the Court of Appeal considered that *Caparo Industries plc* dictum was not appropriate to the circumstances (proximity of relationship, foreseeability of damage and reasonableness of imposing a duty). However it is interesting to note the speech of Lord Mance in *White –v- Jones* [1995] 2 AC 207 (para 92)

> "Lord Browne-Wilkinson, at pp 273G-274G addressed the doubts expressed by Lord Griffiths in *Smith v. Eric S Bush* and Lord Roskill in *Caparo Industries Plc v. Dickman* by explaining assumption of responsibility as 'assumption of responsibility for the task not the assumption of legal responsibility.' He said
>
> 'If the responsibility for the task is assumed by the defendant he thereby creates a special relationship between himself and the plaintiff in relation to which the law (not the defendant) attaches a duty to carry out carefully the tasks so assumed.'"
>
> "But if all that is meant by voluntary assumption of responsibility is the voluntary responsibility for a task, rather than of liability towards the defendant, then questions of foreseeability, proximity and fairness, reasonableness and justice may become very relevant…. Incrementalism operates as an important cross-check on any other approach."

29. Accordingly there may be life left in the approach of *Caparo Industries plc* when considering liability of an office-holder as it may be relevant to consider the proximity of relationship, foreseeability of damage and reasonableness of imposing a duty when determining whether or not a 'special relationship' exists.

THE TRANSACTING OFFICE-HOLDER

30. When disposing of assets an office-holder will have to achieve the best price obtainable. The duty is consistent with the duty owed by a mortgagee to the mortgagor to obtain the best price reasonably obtainable on a sale of the mortgaged property : Cuckmere Brick Co. Ltd. and Another v Mutual Finance Ltd [1971] 2 W.L.R. 1207.

31. In the context of administrative receivers, the duty is owed primarily to the appointor. As an administrative receiver the duty is to realise assets in order to repay the money owed by the debtor company to the appointor: Silven Properties Ltd and another v Royal Bank of Scotland and others [2003] EWCA Civ 1409,[2004] 1 BCLC 359 at para 27.

32. There are circumstances when third parties may seek to make a claim against a receiver. The circumstances arise where it can shown that a receiver has caused loss and damage to their interests. This was the position in Medforth v Blake [1999] 3 WLR 922 where a claim was made by a company (against the appointed receivers) for failure to run its pig farming business efficiently so as to maximise returns.

33. When a mortgagee or his agent (a receiver) does exercise the power to sell the equitable duty to obtain a reasonable and fair price is triggered. A thorough exposition of the duty is provided by Lightman J sitting in the Court of Appeal in Silven Properties Ltd and another v Royal Bank of Scotland and others [2003] EWCA Civ 1409,[2004] 1 BCLC 359, 368:

> "When and if the mortgagee does exercise the power of sale, he comes under a duty in equity (and not tort) to the mortgagor (and all others interested in the equity of redemption) to take reasonable precautions to obtain 'the fair' or 'the true market' value of or the 'proper price' for the mortgaged property at the date of the sale, and not (as the claimants submitted) the date of the decision to sell. If the period of time between the dates of the decision to sell and of the sale is short, there may be no difference in value between the two dates and indeed in many (if not most cases) this may be readily assumed. But where there is a period of delay, the difference in date could prove significant. The mortgagee is not entitled to act in a way which unfairly prejudices the mortgagor by selling hastily at a knock-down price sufficient to pay off his debt: see *Palk* [1993] Ch 330 at 337–338 per Sir Donald Nicholls V-C. He must take proper care whether by fairly and properly exposing the property to the market or otherwise to obtain the best price reasonably obtainable at the date of sale. The remedy for breach of this equitable duty is not common law damages, but an order that the mortgagee account to the mortgagor and all others interested in the equity of redemption, not just for what he actually received, but for what he should have received: see *Standard Chartered Bank Ltd v Walker* [1982] 1 WLR 1410 at 1416."

34. It is in practice not always easy to ensure that the duty has been discharged. The assets in question may be of uncertain or diminishing value. An administrator or administrative receiver may not have the time or resources to continue to trade the business or to engage in any extended period of marketing. The Court has repeatedly recognised that office holders have to make commercial judgments and that it should not interfere with these or be called upon to make such decisions itself: T & D Industries Plc [2000] 1 WLR 646; Transbus International Limited [2004] 2 BCLC 550; DKLL Solicitors v HMRC [2008] 1 BCLC 112

35. Whenever possible effort should be made to expose the assets to the market and/or to create an environment in which competitive bidding occurs. It is acknowledged that this will not always be possible and that is particularly so in the case of pre-packaged sales. It is instructive that (despite all the controversy about pre packs) there are still no reported cases of office holders being successfully challenged for disposing of assets on this basis.

36. It is nevertheless essential in every case that the office holder takes steps to satisfy himself that the best price reasonably obtainable has been achieved. These steps must include at the very minimum the following:-

- The full extent and nature of the assets to be sold must be investigated and any obvious additional value identified; in Cuckmere Brick the complaint made (and upheld) was that no account was taken of the fact that the property had planning permission for development

- Independent expert advice must be taken to help safeguard the transacting Insolvency Practitioner from risk: valuations are usually easily obtained in respect of real property and plant and machinery values, but presents more difficulties in respect of intellectual property

- Consideration must be given to assets that can realistically be realised such as debtors and work in progress. The rights to the debtors can be sold to debt collection enterprises, but before selling the office-holder should consider exposing such an asset to the market.

37. Particular difficulties arise in relation to intangible items such as goodwill and intellectual property rights. Whilst these assets may not be immediately apparent or may not feature on the balance sheet, they are nevertheless assets and the office- holder will have a duty to obtain the best price he can: see the dicta of Jacob J in *Western Intelligence Ltd v KDO Label Printing Machines Ltd [1998] BCC 472*.

38. If an office-holder sells assets on the basis that there will be a deferred consideration he should as a matter of practice ensure that the deferred consideration is secured in case of default. If the purchaser is a newco or is otherwise unable to give adequate security personal or parent company guarantees should be sought.

THE ADVISING INSOLVENCY PRACTITIONER

39. An Insolvency Practitioner may find that a claim is made against him for negligent advice when not in office. A claim (such as that considered in Demarco) could equally be made in contract if there is shown to be consideration.

40. In *Prosser v Castle Sanderson and others* [2002] All ER 507 the first defendant was a firm of solicitors. The second defendant was a firm of insolvency practitioners. The claimant was a property developer, and a shareholder of a company. He was faced with a number of personal liabilities to creditors. He had sufficient assets to pay his creditors, but needed time in which to do so. He sought advice from the first and second defendants, and it was explained to him what would be involved in an Individual Voluntary Arrangement (IVA) under Pt VIII of the Act. The decision was taken to propose an IVA, and a creditors' meeting was held.

41. The meeting became heated, and in large measure hostile to the claimant. There was an adjournment during which the claimant and representatives of the defendants retired to discuss their position. The claimant was unwilling to agree to the immediate liquidation of the company, but was told by the defendants' representatives that there was no alternative.

42. Neither suggested that he might seek an adjournment of the meeting for up to 14 days. The meeting resumed, and the representative of the second defendant was appointed to act as chairman (as was envisaged by r 5.20 of the Insolvency Rules 1986).

43. The claimant accepted that the proposal be modified to include the liquidation of the company.

44. The claimant issued proceedings against the defendants claiming damages for negligence. The first defendant conceded that they owed the claimant a duty of care, but no such concession was made by the Insolvency Practitioner.

45. The court at first instance concluded that the Insolvency Practitioner had not owed a duty of care to the claimant as its representative had been acting as supervisor of the meeting, and accordingly could not owe individuals a duty of care as he was acting as an officer of the court.

46. The Judge found the first defendant in breach of its duty in that its representative ought to have advised the claimant of the possibility of an adjournment. However, he found that that breach had caused the claimant no damage as it had not been shown that it was more probable than not that he would have been able to have changed the creditors' minds within 14 days.

47. The claimant appealed on the grounds that, in the case of the Insolvency Practitioner, the court had been wrong to hold that it owed him no duty of care and, in the case of both defendants, it was more likely than not that a better outcome would have resulted had the meeting been adjourned.

48. It was common ground that when the Insolvency Practitioner initially gave advice to the claimant (before the meeting) he did so pursuant to a contract and that he owed him a duty of care in both contract and tort at that time.

49. Reliance was placed on *King v Anthony* [1998] 2 BCLC 517, where it was held that a person acting as a supervisor under section 263 of the 1986 Act did not owe individual creditors a duty of care because when so acting he was an officer of the court and Part VIII of the Act contained a self-contained statutory scheme which included express powers of the court to give appropriate directions if complaint was made to the court about a supervisor's conduct. It had been conceded in *King v Anthony* that a person owes no such duty as nominee or chairman of the meeting, by reason of section 262 of the 1986 Act.

50. The Court of Appeal accepted that it should be careful not to impose duties upon nominees or chairmen of creditors' meetings when they were acting in that capacity. It was to be emphasised that it was important for a nominee or chairman of a creditors' meeting to make clear to a debtor in what capacity they were acting at any time.

51. Appearing to use the taxonomy of tort of negligence the Court of Appeal said that:

> "In the absence of a clear indication to the appellant that he was no longer acting in that capacity but as nominee or chairman it would be fair just and reasonable to impose a duty upon him. Indeed, to my mind he was then acting pursuant to the contract just as he had been before."

52. Although it was fair just and reasonable to impose a duty there was no causal loss on the facts. However the case is a useful illustration of how an Insolvency Practitioner may incur a liability when advising a client.

53. Recently Insolvency Practitioners were joined in relation to proceedings issued against director for wrongful trading and misfeasance under sections 212, 214, 238 and 239 of the Act on the ground that the Insolvency Practitioners had be in breach of their duty to exercise skill and care when giving pre-insolvency advice. It was argued that the claims for contribution were misconceived because the statutory requirements for claiming contribution under the Civil Liability (Contribution) Act 1978 were not satisfied.

54. In order to succeed in a claim for contribution under the 1978 Act there has to be a common liability of one or more persons to another person who has suffered damage for which the claimant can claim compensation from those persons: *Royal Brompton NHS Trust v Hammond* [2002] 1 WLR 1397. The claims brought by the Liquidator under ss 214, 238 and 239 of the Act could not be treated as claims brought by the companies who had been advised. They were claims brought by the Liquidator which had been conferred on him by statute. It followed that the Insolvency Practitioner could not be under a common liability to the Liquidator; as there was no common liability and thus the claim against the Insolvency Practitioner was struck out: *In the Matter of International Championship Management Limited* [2007] 2 BCLC 274

LIMITING DAMAGES
(an application of common sense?)

55. The wording of sections 212, 304 and paragraph 75 of Schedule B1 implicitly accept that where the office-holder carries out his functions he will be susceptible to a claim in negligence if he fails to exercise reasonable skill and care. Such was accepted by Hoffmann L. J. in *Re D'Jan of London Limited* [1993] B.C.C 646 where he concluded that section 212(2) of the Act covered breached of

duty including a 'duty of care' and applied the section in a negligence case brought against a director.

56. When considering a claim in negligence against an office-holder, issues concerning relief and inevitably damages will arise. The question posed will nearly always be whether or not the negligent act caused loss or whether the loss claimed is too remote or not reasonable. The following is intended to provide a summary of the principles only.

Limiting loss

57. If the claim is made in contract the object of the remedy is to put (as far as possible) the parties in the same position that they would have been had the breach not occurred. If the claim is made in the tort of negligence the object is to place the party against whom the tort has been committed into the same position he would have been had the wrong not been committed. It has been said that the basic object of an award of damages is to put the innocent claimant "in the same position as he would have been in if he had not sustained the wrong for which he is now getting compensation or reparation": see *Livingstone v Rawyards Coal Company* (1880) 5 App.Cas 25, 39 ; *Henderson v Merrett Syndicates Ltd* [1995] 2 AC 145

58. In respect of a claim for damages for breach of contract the court recognises that only genuine loss should be compensated, *Radford v De Froberville* [1977] 1 WLR 1262, 1270:

> "subject to the proviso, of course, that he is *seeking compensation* for a *genuine loss* and not merely using a technical breach to secure an *uncovenanted profit*" (emphasis supplied)

59. There can be said to be five principles that limit compensatory damages for both torts and breach of contract:

59.1. a claimant can not succeed if the loss is too remote from the breach of duty. The tests for remoteness centre on reasonable foreseeability or contemplation of loss

59.2. an intervening cause will bar a claimant from successfully claiming compensation. This may arise where an intervening cause is more responsible for the loss than the defendant's breach of duty

59.3. a claimant will have to show that the loss was within the scope of duty of the defendant: *South Australia Asset Management v York Montague Limited* [1995] QB 375

59.4. a claimant will be barred from succeeding if subsequent to the tort of breach of contract he could have reasonably avoided the loss

59.5. the amount of damages may be reduced where the defendant's negligence has contributed to by the claimant

60. Since all these legal principles enshrined in case law are aimed at reducing or limiting compensation it may not be a total surprise that the same result may often be reached by applying more than one: see *Demarco v Perkins and another* [2006] BPIR 645; [2006] All ER 650 CA (discussed below) which provides an example of this:

> "The loss which Mr Demarco has suffered was *not* the loss of the chance of obtaining an annulment of his bankruptcy under s 282(1)(b) – there never was such a chance….. An alternative way of making much the same point would be to say that, given that the Defendants were engaged to attempt to achieve an annulment *via the IVA route* as being the only available route, the special damage claimed is not in any sense "attributable to" the Defendants' breach of contract (see *SAAMCO* at p 213C per Lord Hoffman)."

61. The distinction between remoteness and intervening causes are often not drawn in the cases. One explanation for this is that both principles concern the dame policy of limiting compensation. Accordingly it may matter in substance not that a defendant uses the term 'remoteness' or 'causation' or 'proximate cause'. Lord Wright provided a useful explanation in *Liesbosch* [1933] AC 449, 460:

> "…the law cannot take account of everything that follows a wrongful act: it regards some subsequent matters as outside the scope of selection…In the varied web of affairs, the law must abstract some consequences as relevant not perhaps on the grounds of pure logic, but simply for practical reasons"

62. As regards remoteness of damages in contract, the general principle is that damages for breach of contract "should be such as may fairly and reasonably be considered either (1) arising naturally, i.e. according to the usual course of things from such breach of contract itself, or (2) such as may reasonably be supposed to have been in the contemplation of both parties at the time they made the contract, as the probable result of a breach of it": *Hadley v Baxendale* (1854) 9 Ex 341, 354.

63. In the tort of negligence the test formulated for deciding whether or not the loss recoverable is whether or not the loss was reasonably foreseeable: *The Wagon Mound (No 2)* [1967] 1 AC 617. In policy terms the remoteness test is formulated to avoid an unfair burden on those responsible for losses they could not have reasonably foreseen.

64. Often in cases against professionals an alternative claim is made in contract and tort. The question that arises (and it probably remains an open question) is what is the correct remoteness test in such circumstances? The test in contract is harsher to the claimant than the test in tort: an assimilation between the two where there is a contractual relationship is thought by some academics to be desirable as the contractual position test is based on there being an opportunity for a contracting party to inform the other party of unusual risks. Once informed of unusual risks that other party may then either exclude (contractually) or limit the liability or even negotiate a higher price. This is not an opportunity that a defendant to a claim in tort has as such a person is usually a stranger: Andrew Burrows "Remedies for torts and breach of contract" 3rd ed

Introducing reasonableness

65. The question of reasonableness of the loss or damage arises in a number of different ways. As confirmed in *Hadley v Baxendale* (in the words quoted above) it is necessary that the damages must "fairly and reasonably be considered" as arising from the breach. That reasonableness is itself an essential element in establishing damages: *Ruxley Electronics Ltd v Forsyth* [1996] 1 AC 344. The judgments of their Lordships contain many references to the importance of reasonableness in selecting the appropriate measure of damages and determining the extent and measure of damages. For instance Lord Lloyd of Berwick says at page 368A and 370A

> "Once again one finds the court emphasising the central importance of reasonableness in selecting the appropriate measure of damages … So I cannot accept that reasonableness is confined to the doctrine of mitigation. It has a wider impact …

A Claimant should avoid unnecessary loss

66. Reasonableness as a separate element is to be distinguished from the "duty" to mitigate. That is described in the well-known speech of Viscount Haldane LC in *British Westinghouse Co v Underground Railway* [1912] AC 673, 689:

> "The fundamental basis is thus compensation for pecuniary loss naturally claimed from the breach; but this first principle is qualified by a second, which imposes on a claimant the duty of taking all reasonable steps to mitigate the loss consequent on the breach, and debars him from claiming any part of the damage which is due to his neglect to take such steps.

67. The onus of establishing a failure to mitigate is upon the defendant. The duty to mitigate does not impose a heavy onus on a claimant.

68. The duty to mitigate is, generally, not a contractual or statutory duty. For instance Pearson L.J. in *Darbishire v Warran* [1963] 1 WLR 1067 properly said:

> "It is important to appreciate the true nature of the so-called 'duty to mitigate the loss' or 'duty to minimise the damage'. The claimant is not under any contractual obligation to adopt the cheaper method: if he wishes to adopt the more expensive method, he is at liberty to do so and by doing so he commits no wrong against the defendant or anyone else. The true meaning is that the claimant is not entitled to charge the defendant by way of damages with any greater sum than that which he reasonably needs to expend for the purpose of making good the loss. In short, he is fully entitled to be as extravagant as he pleases but not at the expense of the defendant."

Add some common sense

69. As has been noted above subject the limiting of damages principles of remoteness and reasonableness, a claimant must establish that any loss is not only proved as having occurred but also that it has effectively been caused by the breach or breaches of duty established against the defendant. In determining this issue the court may apply a common sense.

70. In *Galoo Ltd v Bright Grahame Murray* [1994] 1WLR 1360 at 1374G, the Court of Appeal stated that the breach must first be proved to have been an "effective" cause of the loss:

> "The test in *Quinn v Burch Bros. (Builders) Ltd* [1966] 2 QB 370 that it is necessary to distinguish between a breach of contract which causes a loss to the plaintiff and one which merely gives the opportunity for him to sustain the loss, is helpful but still leaves the question to be answered 'How does the court decide whether the breach of duty was the cause of the loss or merely the occasion of the loss?'"

71. The court answered its own question: "by the application of the court's common sense." (1375A).

72. Common sense prevailed in *Demarco v Perkins and another* [2006] BPIR 645; [2006] All ER 650 which concerned a bankrupt's claim against his Trustee. A bankruptcy order was made against the claimant in March 1997. Thereafter, the claimant retained the defendants to obtain an annulment of the bankruptcy order via the route of entering into individual voluntary agreements (IVAs) with his creditors, pursuant to s 261(1)(a) of the Act. As that route was only available to an undischarged bankrupt, any IVAs had to be established by March 2000, when the claimant's bankruptcy would be automatically discharged. That was not achieved and any opportunity for the claimant to obtain annulment of the order in that way was lost forever in March 2000. The claimant subsequently issued proceedings against the defendants seeking damages in respect of their negligence and/or breach of their implied contractual duty of care.

73. The defendants admitted that they had been retained to act in securing an annulment pursuant to s 261(1)(a) of the 1986 Act. The judge found that the defendants were liable to the claimant and went on to consider the measure of damages to be awarded. The claimant had sought special damages in respect of the cost of obtaining an annulment under the only remaining route open to him, that of paying off the bankruptcy debts, pursuant to s 282(1)(b) of the 1986 Act: a sum in excess of £300,000. He further sought general pecuniary and non-pecuniary damages in respect of the costs and stigma of bankruptcy which should have been annulled. The judge found that special

damages were not recoverable on the basis claimed, as that would put the claimant in a different position to the one he would have been in had the defendants performed their retainer correctly. He further rejected the claim for general damages in respect of pecuniary loss but made an award of £2,000 for non-pecuniary damages, to be discounted by 15% to reflect the chance that any IVA achieved would subsequently fail. The Court of Appeal upheld the Judge's conclusions but increased the award for stigma to £6,000 with a discount of 15%.

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