OFFICE-HOLDER CLAIMS AGAINST DIRECTORS AND THIRD PARTIES

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Introduction

1. This paper supports the talks on 31 January 2013 and 28 February 2013 which the authors will give at the DoubleTree by Hilton Hotel in Leeds and Hotel de la Tour in Birmingham.

2. The talks will focus on office-holder claims against, firstly directors for breach of trust and / or breach of fiduciary duty and, secondly, claims against third parties for accessory liability (dishonest assistance in breach of trust) and knowing receipt as well as for unjust enrichment. In addition, each section of the two sections will, to the extent relevant, review the usual defences which the proposed respondents might be expected to deploy in answer to the claims.

Breach of duty / fiduciary duty claims

3. Section 212 IA provides a summary remedy for challenging the conduct of directors who have (a) misapplied or retained corporate property or (b) committed misfeasance or breach of fiduciary or other duty. This section is procedural only; it does not confer any cause of action on the liquidators (*Phillips v McGregor-Paterson* [2009] EWHC 2385).

4. The section clearly applies to both de jure and de facto directors of the company (s 251 IA). It is less clear that the section applies to shadow directors.

5. Proceedings under s 212 IA do not require the sanction of creditors or the permission of the court (para 3A, Sch 4 IA).

6. In deciding whether or not a breach of s 212 IA has occurred, it is not necessary to demonstrate that the company was insolvent.

7. The general duties owed by a director to the company are set out in s 171-177 of the Companies Act 2006.

8. While the interests of a company are normally identified with those of its members, the interests of creditors can become relevant if a company has financial difficulties (*GHLM Trading Ltd v Maroo* [2012] 2 BCLC 369). In *West Mercia Safetywear Ltd v Dodd* [1988] BCLC 250 at 252–253 Dillon LJ (with whom Croom-Johnson LJ and Caulfield J agreed) approved the following statement of Street CJ in *Kinsela v Russell Kinsela Pty Ltd* (1986) 4 NSWLR 722 at 730:

> "In a solvent company the proprietary interests of the shareholders entitle them as a general body to be regarded as the company when questions of the duty of directors arise. If, as a general body, they authorise or ratify a particular action of the directors, there can be no challenge to the validity of what the directors have done. But where a company is insolvent the interests of the creditors intrude. They become prospectively entitled, through the mechanism of liquidation, to displace the power of the shareholders and directors to deal with the company's assets. It is in a practical sense their assets and not the shareholders' assets that, through the medium of the company, are under the management of the directors pending either liquidation, return to solvency, or the imposition of some alternative administration."

9. In this paper, we will consider three of the most common situations in which a liquidator may seek to allege that the director of an insolvent company has misapplied corporate property or has acted in breach of his fiduciary duties, namely:

(1) Where the director has caused or permitted the company to declare an unlawful dividend;

(2) Where the director has caused or permitted the company to give a preference;

(3) Where the director has operated a director's loan account with the company

Unlawful Dividends: The Issues

10. In the case of small companies, it is not uncommon for the director(s) to receive a nominal or sporadic salary but to supplement their income through the payment of dividends. This is generally more tax efficient for both the director and the company as it reduces the amount of PAYE payable.

11. In the classic scenario, the director will draw monies from the company throughout the year as and when there are sufficient funds without giving consideration to the nature of the payments (e.g. dividend, loan). At the year end, the accountant will then record the payment in the most tax efficient manner.

12. Following liquidation, it will generally be necessary for the liquidator to consider the company's accounts and seek to reconcile the payments made to the directors. In doing so, it may appear that the payments amount to unlawful dividends.

Unlawful Dividends: Relevant Law

13. A member of a company who knows or has reasonable grounds for believing that a distribution made to him, or part of one, is unlawful is liable to repay it (s 847(2) CA).

14. Similarly, the directors of the company will be prima facie liable to compensate the company if they know or ought to have known that a distribution is illegal.

15. A company may only make a distribution out of profits available for the purpose (s 830(1) CA).

16. 'Distribution' includes every transfer of a company's assets to its members except those falling within certain excluded categories in s 829(2) CA (s 829(1) CA). Accordingly, s 830 CA applies to payments by way of dividend.

17. A company's 'profits available for distribution' are its accumulated, realised profits, so far as not previously utilised by distribution or capitalisation, less its accumulated, realised losses, so far as not previously written off in a reduction or reorganisation of capital duly made (s 830(2) CA).

18. The ability to make a distribution is not dependent only on the current year's financial position: if reserves created from previous year's profits are sufficiently large, a company may be able to sustain dividend payments despite recording trading losses.

19. Whether or not a dividend is unlawful is determined by reference to the 'relevant accounts'. It is not possible to look behind those accounts to determine if distributable profits exist (*Bairstow v Queens Moat Houses plc* [2001] 2 BCLC 531, CA).

20. The 'relevant accounts' are the company's last annual accounts except where:

(a) the company wishes to declare an interim dividend which would contravene the statute if reference were made solely to the last annual accounts, where reference may be made to 'interim accounts' (s 836(2)(a) CA); or

(b) the company proposes to make a distribution during its first accounting reference period or before any accounts have been circulated in respect of that period, where reference may be made to 'initial accounts' (s 836(2)(b) CA).

21. In either case, the initial or interim accounts must enable a reasonable judgment to be made as to the amounts of the Company's profits, losses, assets, liabilities, provisions, share capital and reserves (s 838(1), 839(1) CA). If this requirement is not complied with, the accounts may not be relied upon and the distribution is treated as unlawful (s 836(4) CA).

22. Where a distribution or distributions have already been made by reference to particular accounts, and a further distribution is proposed by reference to the same accounts, the amount of the distribution(s) already made must be taken into account in determining the validity of the further distribution (s 840(1) CA).

23. Where the company's capital has been depleted following the preparation of the last annual accounts, it may still be possible to attack a distribution on the basis that it infringes the common law prohibition on the payment of dividends out of capital (cf *Re Exchange Banking Co, Flitcroft's Case* (1882) 21 ChD 519).

24. If the director of a corporate director of a company deliberately procures the payment of unlawful dividends by the company and has the de facto power to do so, he may be held liable pursuant to s 212 IA as a de facto director of the company (*Holland v Revenue and Customs Commissioners* [2010] UKSC 51).

<u>Preference: the issues</u>

25. Whilst s 239 IA provides protection for creditors where the company has given a preference at a relevant time, it is of limited practical utility where the preference was made outside the statutory time period or where the recipient of the preference is himself impecunious. In such circumstances, the only possible redress may be to challenge the directors of the company pursuant to s 212 IA.

<u>Preferences: Relevant Law</u>

26. In *GHLM Trading Ltd v Maroo* [2012] 2 BCLC 369, Newey J considered that the relevant principles which apply where it is alleged that the director of a company which has given a preference is guilty of misfeasance are as follows:

(a) It is necessary to distinguish the questions of breach and remedy.

(b) Since a director has a statutory duty to promote the success of the company for the benefit of its members as a whole (s 172 Companies Act 2006), where creditors interests are relevant, it will be a breach of that duty to advance the interests of a particular creditor without believing the action to be in the interests of the creditors as a class. Whether or not s 239 IA is in point cannot be determinative since a director responsible for a fraudulent preference will not necessarily commit a breach of duty (cf *Re Brian D Pierson (Contractors) Ltd* [2001] BCLC 275) and the fact that the conditions laid down by s 239 IA are not all met should not, of itself, preclude a finding of breach of duty.

(c) The applicability of s 239 IA may have a bearing on what, if any, remedy is available in respect of the breach of duty. Where a factual preference is not caught by s 239 IA, it will be necessary to demonstrate that:

(1) the company has suffered loss;
(2) the director has profited (so that the "no profit" rule operates);
(3) the transaction in question is not binding on the company.

(d) In a typical case, it may be impossible to establish that the company has suffered any loss as a result of a preferential payment since the company's balance sheet position is likely to be unaffected.

(e) It may be problematic to establish breach of the no profit rule where the company has not entered an insolvency regime. If the preference involved the discharge of a debt owed to a director, it could be hard to say whether or to what extent the director was better off than he would have been if he had still been owed the money by the company.

(f) Where a director has caused a company to enter into a contract in pursuit of his own interests, and not in the interests of the company, its members or (where appropriate) its creditors as a class, and the other contracting party had notice of that fact, the better view was that that contract was void (and not merely voidable). In consequence, the requirements of s 239 are irrelevant.

<u>Director's Loan Account</u>

27. In *Maroo*, the substantive claim against the former directors concerned their use of the directors' loan account which, it was alleged, contained considerably more transactions than would typically be expected to be accounted for through that account for a business of that size and nature.

28. In the relevant period, debit entries totalling approximately £1.3m were made to the DLA, representing in particular cash withdrawn and the directors' receipt of sums owing to the company. At the same time, credit entries in the sum of approximately £1.29m were made to the account. The company challenged many of the credit entries.

29. Considering the relevant burden of proof, having regard to the recent decisions in Burke (*Liquidator of Idessa (UK) Ltd) v Morrison* [2011] BPIR 957 and *Re Mumtaz Properties Ltd, Wetton v Ahmed* [2011] EWCA Civ 610 (both decisions concerning applications by liquidators), Newey J noted that, whilst the burden is on the liquidator to prove that a company director has received company money, it was for the director to show that the payment was proper.

30. Accordingly, where debit entries have correctly been made to a directors' loan account, the burden is on the director to justify credit entries on the account.

<u>Defences: Discretionary Relief</u>

31. Section 212 IA is subject to s 1157 CA, which empowers the court, in any proceedings against an officer of a company for negligence or breach of duty to relieve the defendant either wholly or partly from liability if he has acted honestly and reasonably and ought, in the circumstances, fairly to be excused.

32. To fall within s 1157 CA, the director must establish three distinct things: (1) that he acted honestly; (2) that he acted reasonably; (3) that, having regard to all the circumstances, he "ought fairly to be excused".

33. It is possible for a director to succeed on the first two points, yet fail on the third, which is a matter for the court's discretion in each case (cf *Green v Walking* [2008] 2 BCLC 332).

34. A director may have acted reasonably for the purposes of s 1157 CA if they acted in good faith and their breach of duty was technical or minor in character, and not "pervasive and compelling" (*Barings plc (in liq) v Coopers & Lybrand (a firm), Barings Futures (Singapore) Pte Ltd (in liq) v Mattar* [2003] EWHC 1319 (Ch)).

35. In *Re D'Jan of London Ltd* [1994] 1 BCLC 561, a director negligently signed an insurance proposal completed by an insurance broker without reading it. The insurers repudiated liability under the policy on the basis that the proposal contained inaccurate information. Hoffman LJ accepted that the director had acted honestly and reasonably and ought fairly to be excused liability as the negligence was not gross and at the time the proposal was completed the only persons whose interests were foreseeably being put at risk were those of the director and his wife (the sole shareholders).

36. In *Re Loquitur Ltd* [2003] 2 BCLC 442, Etherton J considered that he had no jurisdiction to grant relief from liability for the wrongful payment of a dividend under s 727 of the Companies Act 1985 (the equivalent of s 1157 CA) if the consequence was to leave the company insolvent. However, he noted that the court's discretion under s 212(3) IA was additional to that under s 727 and not subject to a similar limitation.

<u>Defences: Ratification</u>

37. By s 239 CA, a company may by ordinary resolution resolve to ratify conduct by a director amounting to negligence, default, breach of duty or breach of trust in relation to the company. However, neither the misfeasant director nor any member connected with him is eligible to vote in respect of the resolution. Moreover, any rule of law that provides that a particular kind of breach is not able to be ratified still applies (s 239(7) CA).

38. This provision is unlikely to arise very often in the context of applications pursuant to s 212 IA and, in any event, it is unlikely that s 239 CA can apply once the company is insolvent.

<u>Defences: Limitation</u>

39. As s 212 IA is purely procedural, it does not have a limitation period distinct from the Company's underlying claim (*re Eurocruit Ltd* [2007] BCLC 598).

40. A claim for breach of fiduciary duty is treated as equivalent or analogous to a breach of trust, to which a 6 year limitation period generally applies (s 21(3) LA).

41. However, by s 21(1)(b) LA, no period of limitation applies to an action by a beneficiary under a trust to recover trust property from the trustee such as a case where a director has obtained property from the company in breach of trust (cf *Snelling House Limited v Alford* [2012] EWHC 440 (Ch)).

42. Where the six year period does apply, limitation begins to run from the time when the breach occurred or was discovered by the company, and not on the appointment of the liquidator (*Brown v Button* [2011] 2 BCLC 597).

Office-holder claims against third parties

43. All office-holders and their advisers will be familiar with the frustrating factual scenario where it is comparatively straightforward to point to an act committed by a director of a company which amounts to a breach of that director's duties to the company, and to establish that the act has caused the company loss, but where there would nevertheless be little practical point in the office-holder pursuing a claim against the director, for example because the relevant company asset has passed to a third party and / or because the director is impecunious and therefore not worth pursuing.

44. This part of this papers focuses on the claims which office-holders can make against third parties as accessories to the breach of director's duties (dishonest assistance) or for "knowing receipt" where the respondent is the beneficial recipient of company property or separately on a restitutionary basis (interceptive subtraction).

<u>Accessory Liability</u>

45. There is little doubt that an outsider who participates in the misapplication by directors of company property can be made liable as an accessory: *Selangor v United Rubber Estates Ltd v Cradock* (No 3) [1968] 1 WLR 1555, *Belmont Finance Corp Ltd v Williams Furniture Ltd (No 2)* [1980] 1 All ER 393 and *Brown v Bennett* [1999] 1 BCLC 649.

46. A useful and recent summary of the ingredients of the cause of action known as accessory liability or dishonest assistance can be found in the judgment of Hamblen J in *Brown and others*

v InnovatorOne plc and others [2012] EWHC 1321 (Comm.)[1]. It is difficult to do better than cite the relevant passages from Hamblen J's judgment in full:

> [1039] The legal principles for a claim in dishonest assistance are well established and are summarised in Lewin on Trusts at para 40-09, namely:
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> "(1) there is a trust;
>
> (2) there is a breach of trust by the trustee of that trust;
>
> (3) the Defendant induces or assists that breach of trust;
>
> (4) the Defendant does so dishonestly."
>
> [1040] In relation to the first requirement it is established that "fiduciary obligations in relation to the property of another person come within the reference to a trust" – see Morgan J in *Aerostar Maintenance International Ltd v Christopher Wilson* [2010] EWHC 2032 (Ch) at 178.
>
> [1041] The Claimants contended that there is no requirement for there to be trust property and relied in particular upon the judgment of Peter Smith J in JD *Weatherspoon v Van de Berg* [2009] EWHC 639 (Ch) at 518, [2009] 16 EG 138 (CS). Lewin on Trusts describes this (at 40-16) as an "open question" and I shall assume (without deciding) in the Claimants' favour that there is no such requirement.
>
> [1042] In relation to the third requirement, the assistance "must be an act which is part of the fraudulent and dishonest design and must not be of minimal importance" – see *Baden v Société Générale Pour Favoriser le, Developpement du Commerce et de L'industrie en France SA* [1993] 1 WLR 509 at 246.
>
> Dishonesty
> [1043] In relation to the fourth requirement, the authorities support a combined test containing both a subjective and an objective element.
>
> [1044] The test for dishonesty was considered in detail by the House of Lords in the *Twinsectra* case. The majority (Lord Slynn agreeing with Lord Hutton and Lord Steyn agreeing with Lords Hutton and Hoffmann. Lord Millett dissenting) adopted what is generally known as the combined test.
>
> [1045] Lord Hutton rejected that dishonesty was purely subjective, ie was dishonest by the individual's own standards, even if the individual's own standard of honesty is contrary to that of reasonable and honest people. He also rejected the notion that dishonesty was purely objective, ie that an individual could be found to be dishonest by the standards of reasonable and honest people even if the individual did not himself realise that he was acting dishonestly. Lord Hutton stated at 27:
>
>> ". . . there is a standard which combines an objective test and a subjective test, and which requires that before there can be a finding of dishonesty it must be established that the Defendant's conduct was dishonest by the ordinary standard of reasonable and honest

[1] The claimant is understood to be appealing the decision of Hamblen J.

people and that he himself realised that by those standards his conduct was dishonest. I will term this the 'combined test'."

Lord Hoffmann put the test as follows:

> "For the reasons given by my noble and learned friend, Lord Hutton, I consider that those principles require more than knowledge of the facts which make the conduct wrongful. They require a dishonest state of mind, that is to say, consciousness that one is transgressing ordinary standards of honest behaviour."

[1046] The test of dishonesty was reviewed again by the Privy Council in *Barlow Clowes International v Eurotrust International* [2005] UKPC 37, [2006] 1 All ER 333, [2006] 1 WLR 1476. Lord Hoffmann stated at 10 that:

> "The judge stated the law in terms largely derived from the advice of the Board given by Lord Nicholls in *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378. In summary, she said that liability for dishonest assistance requires a dishonest state of mind on the part of the person who assists in the breach of trust. Such a state of mind may consist in knowledge that the transaction is one in which he cannot honestly participate (for example, misappropriation of other people's money), or it may consist in suspicion combined with a conscious decision not to make inquiries which might result in knowledge: see *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd* [2003] 1 AC 469. Although a dishonest state of mind is a subjective mental state, the standard by which the law determines whether it is dishonest is objective. If by ordinary standards a Defendant's mental state would be characterised as dishonest, it is irrelevant that the Defendant judges by different standards. The Court of Appeal held this to be a correct state [sic] of the law and their Lordships agree." (Emphasis added)

[1047] Lord Hoffmann went on to state that this was consistent with the test of dishonesty set out in *Twinsectra*. As he stated at 15:

> "Their Lordships accept that there is an element of ambiguity in these remarks which may have encouraged a belief, expressed in some academic writing, that the Twinsectra case had departed from the law as previously understood and invited inquiry not merely into the Defendant's mental state about the nature of the transaction in which he was participating but also into his views about generally acceptable standards of honesty. But they do not consider that this is what Lord Hutton meant. The reference to 'what he knows would offend normally accepted standards of honest conduct' meant only that his knowledge of the transaction had to be such as to render his participation contrary to normally acceptable standards of honest conduct. It did not require that he should have had reflections about what those normally acceptable standards were."

[1048] There are a number of recent decisions that have considered the test to be applied in the light of the leading authorities. In *Aerostar Maintenance International Ltd v Wilson* [2010] EWHC 2032. Morgan J stated at 183 and 184:

> "The legal test for dishonesty in this context has been much discussed. The principal authorities are the decisions of the Privy Council in *Royal Brunei Airlines v Tan* [1995] 2 AC 378, of the House of Lords in *Twinsectra Ltd v Yardley* [2002] 2 AC 164 and of the Privy Council in *Barlow Clowes International Ltd v Eurotrust International Ltd* [2006] 1 WLR 1476. The two decisions of the Privy Council represent the law to be applied in this jurisdiction: see *Abou-Rahmah v Abacha* [2007] 1 All ER (Comm) 827, at 66 – 70.
>
> The test as to dishonesty, distilled from the above authorities, is as follows. Dishonesty is synonymous with a lack of probity. It means not acting as an honest person would in the circumstances. The standard is an objective one. The application of the standard requires one to put oneself in the shoes of the Defendant to the extent that his conduct is to be assessed in the light of what he knew at the relevant time, as distinct from what a reasonable person would have known or appreciated. For the most part dishonesty is to be equated with conscious impropriety. But a person is not free to set his own standard of honesty. This is what is meant by saying that the standard is objective. If by ordinary objective standards, the Defendant's mental state would be judged to be dishonest, it is irrelevant that the Defendant has adopted a different standard or can see nothing wrong in his behaviour."

[1049] In *The Secretary of State for Justice v Topland Group plc* [2011] EWHC 983 (QB), King J stated:

> "First, on any current understanding of the law on accessory liability (see the analysis of recent authority by the Chancellor in *Starglade Properties Ltd v Nash* [2010] EWCA Civ 1314), although the test of dishonesty or put another way the standard of honesty, is an objective one, there being a single standard of honesty objectively determined by the court and the views of the Defendant on what is dishonest are irrelevant, (see *Barlow Clowes Ltd v Eurocrest Ltd* [2006]1 WLR 1476 where the Privy Council explained and interpreted the decision of the House of Lords in *Twinsectra v Ltd v Yardley* [2002] 2 AC 164)), the subjective state of mind of the Defendant, and what he knew or did not know about the circumstances of the impugned transaction, is still highly relevant since it is to the conduct of the Defendant in the light of that subjective state of mind that the court has to apply the objective test."

[1050] The test for dishonesty that the court needs to apply in the light of these authorities was not in dispute. As explained by Lord Hoffmann in *Barlow Clowes*, the combined test of dishonesty has two elements:

> "(1) The subjective element – The court must consider the Defendant's subjective state of mind and what the Defendant actually knew and understood; and
>
> (2) The objective element – The court must consider whether or not, with that state of mind, knowledge and understanding, the relevant conduct is dishonest, applying an objective standard of dishonesty."

[1051] It is not necessary for the court to establish whether or not the individual considered that he was acting dishonestly. This is not an element of the test of dishonesty as set out in *Twinsectra* and explained by *Barlow Clowes*.

Knowing receipt

47. The cause of action in "knowing receipt" involves the office-holder alleging that a third party has received company property

48. In *Arthur v Attorney General of the Turks & Caicos Islands* [2012] UKPC 30, a recent decision of the Privy council on an appeal from the Court of Appeal of the Turks and Caicos Islands, Sir Terence Etherton, summarised the ingredients of the cause of action as follows:

[31] A Defendant incurs an equitable liability for knowing receipt when he or she acts unconscionably by receiving and retaining trust property with the knowledge that it was transferred in breach of trust. Liability for knowing receipt can also be incurred when property is transferred in breach of a fiduciary duty other than a breach of trust. An obvious example would be the transfer of a company's property in breach of the directors' fiduciary duties, a director not being a trustee of the company's assets. That is also the basis of the claim in the present case since it is not alleged that the Property was held by or for the Crown on trust, but rather that the Minister acted in breach of fiduciary duty to the Crown in authorising the transfer to the Appellant.

[32] The essential requirements of knowing receipt were stated by Hoffmann LJ in *El Ajou v Dollar Land Holdings plc* [1994] 2 All ER 685, 700, [1994] 1 BCLC 464, [1994] BCC 143, as follows:

> "For this purpose the Plaintiff must show, first, a disposal of his assets in breach of fiduciary duty; secondly, the beneficial receipt by the Defendant of assets which are traceable as representing the assets of the Plaintiff; and thirdly, knowledge on the part of the Defendant that the assets he received are traceable to a breach of fiduciary duty."

[33] There has been debate in England and Wales and elsewhere about the nature of the recipient's state of knowledge necessary to give rise to equitable liability for knowing receipt of trust property transferred in breach of trust. In the present case both parties accept that the correct test is that stated by Nourse LJ in *Bank of Credit and Commerce International (Overseas) Ltd v Akindele* [2001] Ch 437 at 455, [2000] 4 All ER 221, [2000] 3 WLR 1423, namely that the Defendant's state of knowledge must be such as to make it unconscionable for the Defendant to retain the benefit of the receipt. Mr Misick accepted that such unconscionable conduct can properly be described as equitable fraud.

[34] When considering relief for the consequences of knowing receipt it is necessary to distinguish between proprietary and personal remedies. The beneficiaries or innocent trustees will pursue a proprietary claim by following the trust property wrongly transferred or tracing its inherent value into something substituted for it: *Foskett v McKeown* [2001] 1 AC 102, 127 – 129, [2000] 3 All ER 97, [2000] 2 WLR 1299 (Lord Millett). The claim for personal liability is for the recipient to account as a constructive trustee and will usually only be necessary where following or tracing is not possible because, for example, the property has been acquired by a bona fide purchaser for value without notice or has been dissipated and is otherwise no longer identifiable. As Sir Robert Megarry V-C said in *Re Montagu's Settlement Trusts* [1987] Ch 264, 285, [1992] 4 All ER 308, [1987] 2 WLR 1192:

> "The equitable doctrine of tracing and the imposition of a constructive trust by reason of the knowing receipt of trust property are governed by different rules and must be kept distinct. Tracing is primarily a means of determining the rights of property, whereas the imposition of a constructive trust creates personal obligations that go beyond mere property rights."

49. Recent examples of case involving allegations of knowing receipt against a defendant are *Odyssey Entertainment Ltd (in liquidation) v Kamp and others* [2012] EWHC 2316 (Ch) and *Bilta (UK) Ltd (In Liquidation) v Nazir* [2012] EWHC 2163 (Ch) which is digested in the notes prepared by our colleagues Holly Doyle and Christopher Brockman. A further case where a claim in "knowing receipt" succeeded was in *Relfo Ltd (in liquidation) v Varsani* [2012] EWHC 2168 (Ch) (Sales J).

<u>Interceptive subtraction (restitution)</u>

50. This cause of action is based on the decision of Nourse J in *Official Custodian for Charities and Others Mackey and Others (No 2)* [1985] 2 All ER 1016. In that case, Nourse J described the principle thus:

> "In Goff and Jones The Law of Restitution (2nd edn, 1978) p 447 the case of a person who wrongly collects another's rents is treated as an example of a wider class of case where the defendant, intervening without right between the plaintiff and a third party, renders himself accountable to the plaintiff for the sum which he receives from the third party. It seems to me that it is of the essence of all those cases both that there is a contract or some other current obligation between the third party and the plaintiff on which the defendant intervenes and that the third party is indebted to the plaintiff in the precise amount of the sum which he pays to the defendant, so that he cannot claim repayment from the defendant in the face of a claim made against the defendant by the plaintiff. It is that which enables the plaintiff to sue the defendant without joining the third party, who no longer has any interest in the subject matter of the suit. It would be a waste of time and money if the plaintiff had to sue the third party and the latter had to sue the defendant. The suit for money had and received avoids circuity of action."

51. An obvious example when this cause of action would be engaged is where a trade debtor of a company in liquidation (A), rather than paying the said company, pays a third party (company B). Plainly, such a payment may have been procured by a misfeasant director in breach of their duties to the company in liquidation (A). This cause of action is an additional string to the liquidator's bow in the sense of being able to proceed directly against company B as well as against the director. This would, of course, be a cause of action vested in the company and not

the liquidator, so that the liquidator may require sanction to bring it (see Part II of Schedule 4 to IA 1986).

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