



Cases to Remember – Insolvency Seminar 2018

Ahmed and others v Ingram and another (Joint trustees in bankruptcy of the estate of Ahmed the above-named Debtor) [2018] EWCA Civ 519; [2016] All ER (D) 11 (Jul)

Introduction

This was a case which considered the proper approach to valuation of a non-cash asset (shareholdings) for the purposes of s. 284 of the Insolvency Act 1986 (“**IA 1986**”) following a void disposition of that asset in circumstances where (a) there was a considerable gap between the date of disposition and the appointment of a trustee in bankruptcy and (b) that asset had diminished in value.

The Application

The Joint Trustees in Bankruptcy of Eaitisham Ahmed (“**the Bankrupt**”) applied to the High Court for an order pursuant to s. 284 of the Insolvency Act 1986 (“**IA 1986**”) by which they sought a declaration that share transfers were void and an order restoring the bankruptcy estate with the fair value of the shares as at the transfer date.

At first instance, Proudman J (“**the Judge**”) found in favour of the Applicants (“**the Trustees**”) and held that the appropriate basis of valuation was fair value (as opposed to a market value) and declared that the fair value of the shares as at the transfer date was £2,216,000. However, she also gave the Respondents permission to appeal.

Factual background

The initial application was made in respect of transfers by the Bankrupt to the First Appellant (“**the Brother**”) of shares in three companies, with some of those shares subsequently being transferred to the remaining respondents (“**the Sisters**”). The companies were family companies and the shareholdings were minority holdings.

The first of those transfers took place on 6 June 2007 which was six months after the presentation of a bankruptcy petition. A bankruptcy order was subsequently made on 21 April 2009 (just under two years later) following revocation of an IVA on the basis that family members had inflated debts which had been used to approve the IVA in circumstances which were described by Deputy Judge Andrew Simmonds QC as tantamount to ‘vote rigging’.

Initially, the Respondents to the original application had sought to argue that the share transfers were not invalidated by s. 284. However, by the time that the matter came before the Judge, that had been



conceded and executed share transfer forms were delivered up on 27 February 2015 (i.e. over seven and a half years after the initial transfer).

The Court of Appeal

The Court of Appeal (with Lady Justice Gloster giving the judgment of the court) identified seven issues:

1. Effect of s. 284 IA 1986.
2. The approach to determination of liability
3. Pleading and evidence.
4. Date of calculation of loss.
5. Method of valuation
6. Liability of sisters

These were dealt with sequentially as follows.

Issue 1 - The effect of s. 282 IA 1986

The first question that the court had to deal with was whether s. 284 IA 1986 provided for a freestanding remedy (as claimed by the Trustees) with that right requiring the restoration of the bankruptcy estate as at the date of the impugned disposition. Alternatively (as the Appellants said) was it right that the court had to look to the general law for a remedy.

The court dealt with the issue comparatively quickly and first observed that s. 284 IA 1986 is silent as to the remedy with its effect being confined to avoiding relevant dispositions. In those circumstances the appropriate remedy was governed by the general law with the point already having been determined in *Hollicourt (Contracts) Ltd v Bank of Ireland* [2000] EWCA Civ 263 where Mummery LJ had held:

“As Oliver J pointed out in Re J Leslie Engineers Co Ltd [1976] 1 WLR 292 at 298 the invalidating provisions (then to be found in section 227 of the Companies Act 1948) do not spell out the appropriate remedy of the company when the disposition is avoided. The right of recovery of the company's property which has been disposed of is determined by the general law. It is common ground in these proceedings that the right of recovery, whether invoked against the payees or against the Bank, is restitutionary.”

Issue 2 – What was the correct approach to the determination of liability?



The Appellants' position was that (contrary to what the Judge had held) the Trustees were only entitled to be compensated for any diminution in the value of the shares which they could prove that the estate had actually suffered as a result of a breach of trust on the part of the Appellants.

The Trustees responded by arguing that the Judge had found that actual loss had been suffered and there could not have been any evidence of an actual sale as the Appellants deliberately and wrongly detained the shares.

The court held that *Hollicourt* showed that the right to recovery was "restitutionary" and that the word "restitutionary" as used in the authorities was used in the sense of restoring trust property actually lost as a result of a breach of trust. Such relief may be awarded in appropriate cases in addition to the restoration of property and was compensatory in nature. Gloster LJ then relied upon the decision of Lord Toulson in *Rose v AIB Group (UK) PLC* [2003] EWHC 1737 (Ch) where he had held:

"Placing the beneficiary in the same position as he would have been in but for the breach may involve restoring the value of something lost by the breach or making good financial damage caused by the breach. But a monetary award which reflected neither loss caused nor profit gained by the wrongdoer would be penal.

...

The purpose of a restitutionary order is to replace a loss to the trust fund which the trustee has brought about

....

As the beneficiary is entitled to have the trust properly administered, so he is entitled to have made good any loss suffered by reason of a breach of the duty. The purpose of a restitutionary order is to replace a loss to the trust fund which the trustee has brought about."

With the above in mind, Gloster LJ observed that liability in equity is fault based, and the relevant loss for which compensation is payable must be caused by the actions or omissions of the relevant trustee. In this regard, the decision of the House of Lords in *Target Holdings v Redferns* [1996] AC 421 represented the highest authority for the proposition that, in order to recover equitable compensation, the Trustees must show actual loss caused by the breach, thus equating the equitable principle for calculating compensation, with the common law principle of assessing loss.

The Court of Appeal held that the Judge had been wrong in her approach in imposing the diminution in value of the holdings from the date of transfer as a measure of liability on the Appellants, apparently as a consequence of her view as to the effect of s.284. Rather, what the court should have done was:



- Identify what constituted the breach of trust.
- When it occurred.
- What was the loss actually caused to the estate as a result of the breach of trust on the part of the Appellants.

Accordingly, the Trustees needed to prove that the bankruptcy estate had suffered actual loss as a result of the Appellants' breach of trust.

Issue 3 – The pleading point

Under the third issue, the Appellants submitted that as the Trustees had failed to prove or plead actual loss, their claim “necessarily failed”. Gloster LJ felt that in the circumstances, this missed the point. Rather the real point was that the Judge's conclusion that the Appellants were simply fixed with liability as of the date of transfer because of s.284, without requiring them to show actual loss, was wrong in law.

Issue 4 – Date of calculation of loss

The fourth issue was when the court should determine that loss should be calculated from. This raised three questions:

1. When did the First Appellant or the Sisters become trustees of the shares?
2. When did the First Appellant or the Sisters commit a breach of trust?
3. When did the loss occur?

Question 1 – when did the Appellants become Trustees?

Gloster LJ reviewed a number of authorities and accepted that in *In re Gray's Inn Construction* [1980] 1 WLR 711 Buckley LJ had held that:

“The section must, in my judgment, invalidate every transaction to which it applies at the instant at which that transaction purports to have taken place.”

However, Gloster LJ observed that Buckley LJ was looking at a case where a winding up order had already been made as at the date that the judge had to determine the application to validate, before concluding that the position was somewhat more nuanced in the interim period. Gloster LJ then concluded that:



45. *In my judgment, the effect of sections 278, 283, 284 and 306 of the Insolvency Act 1986 was that, in the present case, as from the transfer date, the first appellant held the legal title to the shares on the following trusts:*

- i) contingently for the bankrupt, in the event that a bankruptcy order was indeed made against him; and*
- ii) subject thereto (i.e. in the event that no such order was made), for himself as absolute owner of both the legal and beneficial title.*

As from the date when the bankruptcy order was made on 21 April 2009, the first appellant and/or the sisters (if they had had some of the shares transferred to them by this date, as to which see below) held the legal title on trust for the bankrupt and title to them was vested in Mr Hosking, on the latter's appointment as trustee in bankruptcy on 22 July 2009

Applying that reasoning, it was held that from the date of transfer on 6 June 2007, the Brother had held the shares on trust for the Bankrupt but on a contingent basis with the contingency being whether the bankruptcy order was made. Following the making of the bankruptcy order on 21 April 2009 the Brother had held the shares on a bare trust for the Bankrupt. Then, upon the appointment of a Trustee on 22 July 2009, title to the shares had vested in him.

Accordingly, the Judge was wrong to determine that the Brother had become a bare trustee of the shares upon their being transferred to him.

Question 2 - When did the First Appellant or the Sisters commit a breach of trust?

In addressing the second question, the court held that in order to ascertain when the Brother and/or the Sisters committed a breach of trust, it was necessary to determine the scope of their duty as a trustee. As to the Brother, Gloster LJ held that once he had possession of all the relevant knowledge that made him a bare trustee (the final stage being knowledge of the appointment of a trustee) he was under a duty to tender the shares immediately. Given his dishonesty, if he had any doubts as to his legal position he had a duty to enquire:

“If the first appellant was unsure as to his legal position, the level of dishonesty in this case meant he had a duty to inquire.”



Whilst in other situations the duty may arise from the date on which demand was made by a trustee, the level of dishonesty in the instant case meant that this was not the case here.

Question 3 - When did the loss occur?

Gloster LJ then went on to look at the date on which the loss occurred. The fact that the breach of trust occurred on the making of the bankruptcy order did not mean that loss had been incurred on that date. She then held that the loss occurred, or flowed from, the date at which the trustee in bankruptcy would have actually sold the shares. On the evidence before her, she accepted that a date just over a year after the bankruptcy order had been made was the date on which such a sale was likely to have taken place.

Conclusion

On that basis the court held that the Judge had been wrong to hold that the Appellants' liability for loss flowed from the transfer date and allowed the appeal supplementing the date of likely sale as the appropriate date.

Issue 5 – method of valuation

The fifth issue was whether the shares should be valued on the market value or fair value basis in circumstances where the latter was likely to be higher given the closely held nature of the companies. On the facts, Gloster LJ held that the proper method of valuation was the fair value basis and concluded:

“I am also persuaded that, in the circumstances of this case, the reasons which would apply in a sale between family members similarly apply in the context of a sale from a trustee in bankruptcy to a family member: first that the family would not want a third party holding 24% of the shares in the companies; and second, that the first appellant, as the most likely buyer, would consider the trustee in bankruptcy's next best option of selling to somebody outside the family. I consider the second reason would likely lead to a higher valuation.”

Issue 6 – The liability of the sisters

The Sisters had not received the shares from the Bankrupt but from the Brother and had subsequently transferred the shares back to him. Gloster LJ applied the reasoning which she had set out under Issue 4 to the Sisters and concluded that their liability also arose upon the appointment of trustees and did not conclude upon their transferring the shares back to the Brother as their obligation was to transfer the shares to the trustees:

“[The Sisters'] liability for loss in the diminution in value did not cease on 30 June 2010 (when they re-transferred the shares to the first appellant) because, as I have said, their obligation was



to retransfer the shares to the trustees in bankruptcy – not to do the first appellant. Their failure to do so was also causative of the estate's loss.”

Conclusion

The decision makes clear that s. 284 does not provide a free-standing right to recover loss. Rather that the court will apply restitutionary principles when establishing the loss suffered by the bankruptcy estate. The key questions are (i) when the recipients of a disposition committed a breach of trust and (ii) when did the relevant loss occur.

This is of significance to a trustee in that if a trustee does not demand return of the relevant property and absent knowledge on the part of a beneficiary of the obligation to return the property, then it may be the case that no breach of trust has been committed until such a demand is made. Further, if a trustee cannot show that the property would have been realised in a timely manner, then it will be difficult to show that loss would have been suffered until such time as the property would have been realised.

In those circumstances, it is imperative that trustees faced with void dispositions of property which is falling in value take prompt steps to realise the same.