TRAVERS SMITH

Finance Monthly

April 2015

Welcome to the monthly finance bulletin from our finance and restructuring group. This issue contains our usual overview of some recent market developments and trends in the finance sector, including a spotlight on the distinction between remedies exercised under a mortgage and simple contractual remedies. Please get in touch if it raises any issues that you would like to discuss.

Matthew Ayre, Head of Finance

In the event of inconsistency?

A recent case highlights the potential fallibilities of an "in the event of inconsistencies" clause where a contractual relationship is founded on multiple documents. The Court may be less inclined than expected to discover contradictions and clear and irreconcilable discrepancies which qualify as "inconsistencies".

A mortgage offer ("**Offer**") was expressed to be subject to Mortgage Conditions ("the **Conditions**") and the Conditions contained a clause which stated that if there were inconsistencies between the Conditions and the Offer, the terms of the Offer would prevail.

The Offer provided for (i) a fixed interest rate for an initial two-year period, at the expiry of which a variable rate would apply comprising the BoE Base Rate plus 1.99%; and (ii) a twenty-five year repayment term with the possibility of early termination.

The Conditions specified (i) that the variable rate could be changed, including inter alia to ensure that West Bromwich's business was carried out efficiently and competitively and to reflect market conditions; and (ii) that the mortgage was repayable in a number of circumstances, varying from one month's notice to fairly normal insolvency provisions.

Mark Alexander, as representative of several hundred West Bromwich tracker mortgagors, argued that the above Offer terms and the Conditions were clearly inconsistent and the terms of the Offer should prevail. In *Mark Robert Alexander (as representative of the "Property 118 Action Group") v West Bromwich Mortgage Company Ltd [2015] EWHC 135*, the Court explained that where a contractual relationship between parties (where neither was a consumer) was founded on a number of different documents, the Court's task was to read the provisions together and, if possible, give effect to them. "Clear and irreconcilable discrepancies" would be necessary before the Courts could conclude that inconsistencies were such as to invoke any kind of "trumping" clause which prioritised the terms of one document over another. In this case, the Offer terms imposing a variable rate after the two year term did not specifically state that the variable rate could not be changed, whereas the Mortgage Conditions permitted change and an increase in the margin from 1.99% to 3.99% was therefore permissible. The interest provisions in the Conditions qualified the Offer terms, they did not contradict them. Clearly the same principle applied in relation to the term of the mortgage.

Discharging a public duty can be expensive

Section 236(3) of the Insolvency Act 1986 permits an insolvency officeholder (which includes a liquidator, administrator or administrative receiver) to require anyone who has information about the business and affairs of an insolvent company to produce relevant documents. An officeholder can also require attendance at an examination in Court and in these circumstances, an examinee's reasonable travel expenses must be refunded and the Court has a discretion to require the insolvent company to meet "other costs". Previous Court cases have been inconsistent with respect to the Court's power to order an insolvent company to meet "other costs" under Rule 9.6(4) of the Insolvency Rules 1986. In a recently published case *Harvest Finance Ltd (in liquidation) v Cannons Law Practice LLP and another [2014] EWHC 4327 (Ch)*, the Court accepted that it had the jurisdiction to make an order for costs in connection with the provision of documents requested under s.236, but declined to do so in this case, notwithstanding that the relevant law firm had encountered difficulty in tracing and delivering all the documents and had assessed the costs of complying with the order to be in excess of £40,000. The Court concluded that the law firm's difficulties were largely a result of its inadequate IT systems and that as a matter of public policy (particularly in a case where the enquiry was as to fraudulent conduct) a party should not, in fulfilling its public duty, ordinarily expect to receive its costs. The law firm was, however, entitled to recover its legal representation costs in connection with the Court case.

Spotlight on… the distinction between remedies exercised under a mortgage and simple contractual remedies

Unlike most civil code systems (many of which impose a court-supervised public auction sale process) mortgagees and chargees exercising a power of sale are not, as a matter of English law, subjected to very much judicial control or constraint. Most practitioners are familiar with the long-established common law principle that an enforcing mortgagee must act in good faith and take reasonable care to obtain, in relation to mortgaged property, "the market value at the date of sale", or a "proper price", or "the best price reasonably obtainable". Save for a brief, adventurous frolic by Lord Denning, who attempted in the early '80s to impose a duty on enforcing mortgagees to take reasonable care as to the timing of enforcement, the Courts have set their face against this principle and reaffirmed on many occasions that a mortgagee is under no duty of care to the mortgagor in respect of the timing of the sale and can act in its own interests in deciding whether and when it should exercise the power of sale. Of course, any decision as to timing may be constrained by the duty to act in good faith – particularly where the relevant asset is a wasting asset such as perishable goods, but the basic principle is that an enforcing mortgagee or chargee may sell when it likes, but that when it does so, it must obtain the best price reasonably obtainable.

Where a lender enters into a contractual agreement with a debtor under which the lender may participate in sale proceeds of a particular asset owned by the debtor and, in certain circumstances, step in and force the sale of that asset, one might assume that in the conduct of the forced sale, the lender will be subject to the same constraints as an enforcing mortgagee. This was precisely the argument recently advanced in *(1) Rosserlane Consultants Ltd, (2) Swinbrook Developments Ltd v Credit Suisse International [2015] EWHC 384 (Ch)*. In that case, the Court declined to introduce any implied term imposing such constraints into the arrangements set out in a Participation Agreement concluded between the parties in the above terms. The Participation Agreement was freely negotiated by experienced commercial lawyers and drafted in terms that whilst the *debtors* had an obligation to both sell the relevant assets by a particular date and achieve the best price obtainable, Credit Suisse was under no such equivalent obligation when exercising its forced sale rights. The Court attributed special significance to the fact that the obligations were not reciprocal and that the Participation Agreement was silent as to Credit Suisse's duties. The essential issue was that the Participation Agreement was not a mortgage and the Court was prepared to imply a duty of good faith only.

Companies House Registration Delays

Practitioners are understandably concerned, given the potentially fatal consequences for their clients' security, to ensure that charges required to be registered at Companies House are submitted well within the twenty-one day period required under the Companies Act. Direct and anecdotal experience suggests that recent paper filings, even when promptly submitted, have not been processed until the end, or even beyond, the twenty-one day period. This means that errors in accompanying paperwork are simply incapable of being resolved following the expiry of the twenty-one day period, without client co-operation and resubmission, or recourse to the Courts. There are indications that recent delays were a temporary phenomenon, but a solution is in any event afforded by on-line electronic filing, which permits much quicker response times.

In the courts

Jetivia SA and another v Bilta (UK) Limited [2015] UK SC 23

Bilta's liquidators claimed against Bilta directors and third parties who had facilitated a VAT "carousel" fraud for (a) damages in tort, (b) compensation based on constructive trust, and (c) a contribution under s.213 of the Insolvency Act 1986 (*Fraudulent Trading*). The appellants sought to repeat the defences they originally advanced before the Court of Appeal. They argued that (i) as a matter of public policy (the *ex turpi causa* rule) the cause of action was founded on an illegal act by Bilta (the company used as a vehicle for the fraud) and (ii) s.213 did not have extra-territorial effect. The Supreme Court rejected the appeal, concluding that:

(i) whilst a company has separate legal personality, it acts through its directors and agents. Whilst in most cases, the acts and state of mind of a company's directors can be attributed to the company, much depends on the context. It was perfectly possible, as between the company and the defrauded third party, that the company should be treated as the perpetrator of the fraud. In the different context of a claim between the company and its directors, however, the defaulting directors should not be able to rely on their own breach of duty to defeat the operation of the provisions of the Companies Act in cases where those provisions were intended to protect the company; and

(ii) section 213 provides a remedy against any person who has knowingly become a party to the carrying on of that company's business with a fraudulent purpose. Whilst the context of s.213 may be the winding-up of a company registered in the UK, the effect of that winding-up is worldwide. The Supreme Court concluded that it would seriously handicap the efficient winding-up of an insolvent company in an increasingly globalised economy if the jurisdiction of the court responsible for the winding-up did not extend to people and corporate bodies resident overseas. In addition, section 238 of the IA 1986 (*Transactions at an Undervalue*), also preoccupied with reviewable transactions, had previously been held by the Court of Appeal to apply without territorial limitations.

Wilson v SMC Properties Ltd [2015] EWHC 870 (Ch)

A company contracted to sell a property in order to realise proceeds which were to be used to discharge a mortgage debt. Before completion of the purchase, a winding-up petition was presented against the company. Section 127(1) of the Insolvency Act 1986 states that once a winding-up petition has been presented, any disposition of the company's property is void unless the Court orders otherwise. The Court can validate any such disposition in circumstances where it is made in good faith in the ordinary course of business at a time when the parties were unaware that a winding-up petition had been presented. The purchaser applied for the sale to be validated arguing that the transaction had been made in good faith (not at an undervalue) at arm's length and without notice. The company's liquidator argued that the sale was at an undervalue and should be declared void.

The Court concluded that when assessing whether the purchaser had acted in good faith, the element of undervalue was relevant. The Court would be slow to validate a transaction if there was a significant reduction in the value of the company's assets available to the general body of creditors even where the purchaser was unaware of the presentation of a winding-up petition before the purchase. Here, however, the Court found that the transaction had been concluded in good faith, at arms' length and in circumstances where there was no loss to creditors and the Court was therefore prepared to validate the transaction.

Transaction News

We have advised Pinewood Group on a fund raise of £30m and new bank facilities of up to £135m with Lloyds Bank plc, The Royal Bank of Scotland plc, HSBC Bank plc and Barclays Bank plc, to be used by the group to part fund the first phase of development of the Pinewood Studios Development Framework, which aims to double the existing capacity of the studios.

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