Neutral Citation Number: [2021] EWHC 800 (Ch)

Claim No: CR-2020-002382

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
INSOLVENCY AND COMPANIES LIST (ChD)

IN THE MATTER OF ZOOM UK DISTRIBUTION LIMITED (in administration)
AND IN THE MATTER OF THE INSOLVENCY ACT 1986

Royal Courts of Justice, Rolls Building
Fetter Lane, London, EC4A 1NL
Date: 31 March 2021

Before:

STUART ISAACS QC (sitting as a Deputy Judge of the High Court)

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Between:

Francis Wessely and Joann Louise Leach (in their capacity as joint administrators of Zoom UK Distribution Ltd (in administration))

Applicants

- and –

(1) Stephen Rubra
(2) Anthony Bekesi
(3) Zoom UK Distribution Ltd (in administration)

Respondents

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Ms Rachael Earle (instructed by Kingsley Napley LLP) appeared on behalf of the Applicants.

Mr Philip Currie (instructed on a direct access basis) appeared on behalf of the 1st and 2nd Respondents.

Hearing date: 31 March 2021

Approved Judgment

Covid-19 Protocol: This judgment was handed down by the judge remotely by circulation to the parties' representatives by email and release to Bailii. The date and time for hand-down is deemed to be 2pm on 31 March 2021.

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

Stuart Isaacs QC:

Introduction

1. There are two applications before the court. The first is an application pursuant to paragraph 63 of Schedule B1 to the Insolvency Act 1986 (the "IA"), made by a notice dated 25 February 2021 issued by the joint administrators (the "Administrators") of Zoom UK Distribution Ltd ("Zoom"), for (i) a declaration that their appointment on 5 May 2020 was valid despite a defect in procedure relating to their appointment and (ii) relief that any of their acts since that date are valid (the "Directions Application"); and, in the alternative to the Directions Application, to the extent that the Administrators' appointment is invalid, an order that the directors of the company, the 1st and 2nd respondents (the "Directors"), indemnify them against any liability which arises solely by reason of the invalidity of the appointment (the "Indemnity Application").

2. By the second application, made by a notice dated 16 March 2021 issued by the Directors, the court is asked, in the event that the Directions Application is refused, to make a retrospective administration order to take effect from 5 May 2020 and to appoint the proposed persons to be administrators with effect from that date (the "Retrospective Administration Order Application").

3. Before dealing with the substantive issues which arise, I should record that, in advance of the hearing, I drew the parties' attention to the fact that Ms Earle, who appears on the Administrators' behalf, and I are members of the same chambers and asked whether that would be an obstacle to my hearing this case. Both parties, through their counsel, confirmed that there was no objection to my hearing it.

Factual background

4. On 3 March 2009, Zoom executed a debenture in favour of Lloyds TSB Bank plc ("Lloyds") as security for a loan (the "Lloyds Debenture"). In consequence, Lloyds became a qualifying floating charge holder within the meaning of the IA. Under paragraph 14(1) of Schedule B1, the holder of a qualifying floating charge in respect of a company's property may appoint an administrator of the company. On 3 January 2010, Zoom executed another debenture in favour of Lloyds TSB Commercial Finance Limited as security for a loan (the "TSB Debenture"). In 2017, Zoom refinanced its borrowings, involving the provision of alternative invoice financing by Aldermore Bank plc ("Aldermore"), secured by way of another debenture (the "Aldermore Debenture") and designed to satisfy and replace the TSB Debenture. As a result, the TSB Debenture was marked at Companies House as satisfied on 22 November 2017. Due to an error in the Aldermore documentation, the Lloyds Debenture was also marked at Companies House as satisfied. Zoom subsequently repaid its indebtedness to Aldermore and the Aldermore Debenture too was marked as satisfied.

5. The Administrators were appointed out of court by the Directors on 5 May 2020 pursuant to the Directors' power to do so under paragraph 22(2) of Schedule B1. Under paragraph 26(1)(b) of Schedule B1, the Directors were required to give at least five business days' written notice to Lloyds of their proposal to appoint an administrator. By paragraph 28(1) of Schedule B1, an appointment under paragraph 22 may not be made unless inter alia the notice period has expired or each person to whom the notice has been given has consented in writing to the making of the appointment. Unbeknown at the time to the Administrators, the Directors inadvertently failed to give the requisite written notice to Lloyds. The Administrators only became aware of the situation after having been informed by Lloyds on 25 August 2020 that the Lloyds Debenture remained outstanding. Zoom repaid the outstanding loan to Lloyds in about December 2020.

The Directions Application

6. The Directions Application is supported by the Directors. Lloyds does not oppose the continued appointment of the Administrators and it too consents to the relief sought by the Directions Application. I have therefore not had the benefit argument in opposition to the Directions Application, although the arguments against the position contended for by the Administrators appears from the earlier cases to which detailed consideration was given in the subsequent case-law.

7. Schedule B1 does not specify the consequences of a failure to comply with paragraph 26(1)(b). The issue before the court is whether the Directors' failure to give notice to Lloyds of their proposal to appoint the Administrators renders their appointment void or else only defective and capable of cure. The commentary to paragraph 26 in Sealy & Milman Annotated Guide to the Insolvency Legislation (23rd edition, 2020) states that "[t]*he question whether the failure to comply with the notice requirements of para. 26 inevitably invalidates the appointment of the administrator has been much debated in recent cases at first instance, and remains the subject of controversy. Only a ruling of a higher court can resolve the current impasse*."

8. The Administrators submitted that although there are conflicting first instance decisions, none is binding on the court on the Directions Application and that the more recent High Court and Insolvency and Companies Court ("ICC") decisions show a consistent approach, which should be followed in the present case, in favour of the Administrators' appointment being only defective and not void. The conflicting authorities on the consequences of a failure to comply with the requirements of Schedule B1 generally were reviewed at length in *Re A.R,G. (Mansfield) Limited* [202] BCC 641 by His Honour Judge David-White QC sitting as a judge of the High Court and considered by Arnold J in *Re Ceart Risk Services Ltd* [2013] Bus LR 116.

9. The only decision which is directly in point is that of ICC Judge Jones in *Re Tokenhouse VB Ltd (formerly VAT Bridge 7 Ltd)* [2021] BCC 107 ("*Tokenhouse*"), which is not binding on this court. In that case, it was submitted on behalf of the applicant, a qualifying floating charge holder who had not been given the requisite notice under paragraph 26(1)(b), that the clear wording of the relevant provisions of Schedule B1 meant that the appointment of administrators could not have been made and cannot have had effect. The applicant submitted that the court was bound by higher authority to reach that conclusion, first because case-law, including *Re Euromaster Ltd*

[2012] EWHC 2356 (Ch) establishes that the purpose of the notice of intention is to give a charge holder the opportunity to appoint its own administrator or administrative receiver, which a breach of paragraph 26(1(b) would prevent; and, second, because cases such as *Re Skeggs Beef Ltd* [2019] EWHC 2607 (Ch) establish that an appointment is a nullity if there is a fundamental defect which, applying the approach in cases such as *Adjei v Law for All* [2011] EWHC 2672 (Ch), a breach of paragraph 26(1)(b) would be. On the other hand, the respondents, the appointed administrators, submitted that the starting point was to take the approach to statutory construction laid down by the House of Lords in *Soneji (Kamlesh Kumar)* [2005] UKHL 49, and to answer the question whether Parliament intended the outcome to be total invalidity by focusing on the consequences of non-compliance. That being so, they submitted that Norris J's approach in *Re Euromaster Ltd* should be applied and a distinction drawn between those provisions which define the circumstances in which the power to appoint arises and those which prescribe procedural requirements that must be fulfilled for the appointment to be made. If there is no power to appoint, then the appointment will be a nullity but if there is a breach of a procedural requirement the appointment will more naturally be treated as irregular. Norris J's statement that paragraphs 22 to 25 of Schedule B1 relate to the power to appoint and paragraphs 26 to 32 of Schedule B1 relate to the procedural requirements for the exercise of the power mean that the answer to the issue is that the appointment is valid but with procedural irregularity.

10. In *Tokenhouse*, Judge Jones conducted a thorough review of the applicable statutory background concerning the out of court appointment of administrators and identified the underlying problem as:

> *"31. … the tension between: (i) the normal meaning of the words used within those provisions strongly suggesting that non-compliance with their out-of-court procedural requirements should prevent an appointment being effective; and (ii) the fact that this may have a disproportionate result when compared with the prejudice caused by breach and, even more importantly, may adversely affect a company's ability to achieve the purposes it would have been likely to achieve had the appointment been valid.*
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> *32. This tension exists because provisions which are framed in mandatory terms exist within the context of scenarios which will require the company to be quickly placed into administration, whilst it is or is likely to be (at least) cash flow insolvent, if it is to be rescued through the aims and purposes of an administration. Assuming, which it is right to do for these purposes, that aim is reasonably likely to succeed, it is not difficult to appreciate that it may be considered counter-intuitive for an appointment to be invalid if it is subsequently discovered that a notice of intention was not given when it should have been. The consequence of invalidity potentially does not appear to fit the breach and the purpose of the requirement for notice.*
>
> *33. These potentially straightforward provisions have been considered in a variety of circumstances ranging from minor defects when complying with the form of notice or the requirements for filing documents to more serious breaches concerning the failure to give notices. In some of the cases the breach was not appreciated for a considerable time and significant steps had been taken to implement the purposes of an administration. Indeed, there has been a case*

> *before me when the breach was first identified by liquidators after the conclusion of the administration. In one of the many reported cases the outcome would determine whether the company was in administration or whether a creditors' voluntary liquidation had commenced by a resolution passed shortly after the purported appointment.*
>
> *34. It is not difficult to see that potentially an automatic conclusion based upon the plain meaning rule that an appointment has no effect may cause significant damage to the company and its creditors. Automatic invalidity would do so even though the chargeholder and/or the Prescribed Person concerned does not object to the appointment or "only" wants the appointee replaced by their own nominee. Nevertheless, if that is the wording of the statute and the intention of Parliament, that must be followed subject in exceptional circumstances to the court's extraordinary inherent jurisdiction which confers "scope for the court to direct that things be done (or not done) in apparent conflict with express provisions of the legislation" (see the judgment of Lloyd LJ in Donaldson v O'Sullivan [2008] EWCA Civ 879; [2009] 1 W.L.R. 924; [2009] B.C.C. 99 at [38]–[41]). That has not been suggested within case law to date.*
>
> *35. The tension has resulted in the above-mentioned "conflict of judicial opinion" in cases which have considered (in the context of the application of principles of statutory interpretation) whether there was power to make an appointment or if an appointment was made and, to the extent that there was an appointment: (i) whether the provisions requiring notice provide for the consequences of breach; or. if not, (ii) the plain meaning overrides any contrary purpose arguments; or (iii) insofar as purpose is relevant, whether non-compliance with the notification requirement(s) must be a fundamental breach because the absence of notice cannot be cured and, certainly in the case of a chargeholder, the rights lost cannot be revived; or (iv) whether the breach is not fundamental taking into consideration it is procedural and/or the overriding purpose of achieving the aims of an administration.*"

11. Judge Jones accepted the administrators' submissions and concluded, after an extensive review of the authorities, that the breach of paragraph 26(1)(b) did not mean that their appointment by the directors was void: see paragraphs [42] to [54] of the judgment.

12. *Tokenhouse* was followed by Deputy ICC Judge Frith in *Re NMUL Realisations Limited* [2021] EWHC 94 (Ch), a case in which it was held that the failure of a debenture holder to serve notice of intention to appoint administrators on the holder of a prior security under paragraph 15 of Schedule B1 was an irregularity which could be remedied by an order under Rule 12.64 of the Insolvency (England and Wales) Rules 2016 (the "Insolvency Rules") and which did not render the administrators' appointment void.

13. Rule 12.64 only applies to "*insolvency proceedings*". It is common ground between the parties that the out of court appointment of administrators pursuant to paragraph 22 of Schedule B1 constitutes "*insolvency proceedings*" for the purpose of Rule 12.64.

14. Ms Earle submitted that in the present case the court should adopt the reasoning in *Tokenhouse* and conclude that the breach of paragraph 26(1)(b) of Schedule B1 did not render the Administrators' appointment void. She submitted that (1) such a conclusion would be consistent with Norris J's decision in *Euromaster Ltd* as well as the recent approach taken in *Re NMUL Realisations Limited* and that consistency is desirable until the issue has been resolved by the Court of Appeal; (2) the consequences of the breach would then be proportionate: a qualifying floating charge holder who was not given the requisite notice would still be able to apply to the court for the defect to be cured and have an administrator of its choice put in place but the key consideration is for there to be an administration in the first place; and (3) such a conclusion would remove the need for the parties to resort to unattractive applications for retrospective appointments in the event that the purported original appointment was held to be invalid, see *Tokenhouse* at [39], citing *Re Elgin Legal Data Ltd* [2016] EWHC 2523 (Ch) and *Pettit v Bradford Bulls (Northern) Ltd (in administration)* [2016] EWHC 3557 (Ch).

15. I accept Ms Earle's submissions. It is, in my judgment, right that the *Soneji* approach should be followed. There is now a consensus, from which I should not depart, that the answer to the question whether non-compliance results in invalidity depends on whether Parliament intended that outcome – a question to be answered by first identifying the purpose of the requirement breached and then by identifying the consequences of non-compliance, see *Re Ceart Risk Services Ltd* per Arnold J.

16. Applying that approach, a conclusion that the breach of paragraph 26(1)(b) does not render the appointment of the Administrators a nullity is consistent with Norris J's decision in *Euromaster Ltd*, as explained in *Tokenhouse*. In *Re Skeggs Beef Ltd*, Marcus Smith J identified three categories of case to be applied when deciding the consequences of a breach of the requirements for an out of court appointment, namely where the breach is (i) fundamental, (ii) not fundamental but has caused no injustice and (iii) not fundamental but has caused substantial injustice. A conclusion that the breach of paragraph 26(1)(b) is a fundamental one such as to render the appointment a nullity would wrongly rank the importance of receiving a notice above the importance of there being an administration. For the reasons given by Judge Jones in *Tokenhouse*, which I gratefully adopt, a breach of paragraph 26(1)(b) falls into the second category of case. In the result, the Administrators' appointment was admitted defective but the defect is curable.

17. Paragraph 104 of Schedule B1 provides that an act of the administrator of a company is valid in spite of a defect in his appointment or qualification. In *Re Ceart Risk Services Ltd*, Arnold J determined that paragraph 104 was effective to validate the acts of an administrator whose appointment was defective but not those where the purported appointment was a nullity. Rule 12.64 of the Insolvency Rules provides that no insolvency proceedings will be invalidated by any formal defect or any irregularity unless the court before which objection is made considers that substantial injustice has been caused by the defect or irregularity and that the injustice cannot be remedied by any order of the court. As I have stated, the present case falls within the second and not the third category of case identified in *Re Skeggs Beef Ltd*. No substantial injustice has been caused by the defect.

18. In the result, the Directions Application is granted. The Administrators are entitled to a declarations that their appointment on 5 May 2020 was valid and that any of their acts since that date are valid.

19. In the circumstances, it is unnecessary to determine the Indemnity Application and, except on the question of costs, the Retrospective Administration Order Application.

Costs

20. The Administrators seek their costs of both the Directions Application and the Retrospective Administration Order Application. The Directors argue that the costs of both of those applications should be in the administration. It is unnecessary to deal separately with the costs of the Indemnity Application since it forms part of the relief sought by application notice dated 25 February 2021 and it was not suggested that it should be dealt with differently from the Directions Application.

21. Ms Earle submitted that the Administrators should be entitled to their costs on the basis that it was the Directors' inadvertent mistake in not giving Lloyds the requisite notice which led to the need for the present proceedings and that the Administrators were unaware of the Directors' failure to give notice until almost three months after their appointment. Mr Currie, who appears on the Directors' behalf, submitted that the costs should be in the administration because, while they accept that the failure in procedure in not notifying Lloyds was theirs, they were relying on the advice of others, including the Administrators, they as laymen were unaware of the need to notify Lloyds and, had they been asked whether Lloyds was still a secured creditor, would have responded in the affirmative.

22. I am unconvinced by Mr Currie's submissions. As I have stated, it is not in dispute that the defect in the Administrators' appointment resulted from the Directors' mistake, albeit that the mistake was inadvertent and originated in the Aldermore documentation. I am also doubtful about the Directors' evidence, in paragraph 36(d) of Mr Rubra's first witness statement, to the effect that they were aware that Lloyds was a secured creditor. That evidence appears inconsistent in particular with the contemporaneous documentation in which the Directors refer to Lloyds as an unsecured creditor.

23. In my judgment, none of the matters advanced by Mr Currie leads to a different conclusion to that expressed by Norris J in *Adjei* at [22] that the Directors "*purported to make the original appointment and made a mistake in doing so, so that the present application … was necessary in order to remedy their previous mistake. The return to the creditors should not be depleted and the directors should not receive the first fruits of the administration by way of reimbursement of the expenses of their corrective action*". The fact that the Directions Application was brought by the Administrators rather than there being an application by the Directors for the making of an administration order with retrospective effect as in *Adjei* is not a material point of distinction. In my judgment, the same position prevails in relation to the Retrospective Administration Order Application.

24. In those circumstances, the Directors apply for permission to appeal the costs orders against them, on the basis that the court exercised its discretion wrongly. For the reasons stated above, there is, in my judgment, no real prospect of an appeal on the question of costs succeeding. I have taken into account but have rejected the reasons put forward by the Directors for the costs to be in the administration. The Directors' application for permission to appeal the costs orders is accordingly refused.

25. I shall leave it to counsel to seek to agree the orders which follow from this judgment and to submit them to me for approval. To the extent that any consequential issues arise, I direct that there be brief written submissions exchanged on or before 7 April 2021 and reply submissions on or before 9 April 2021 at midday. Unless either side informs the listing office by 3pm on 9 April 2021 that a further oral hearing on the consequential issues is required, I shall proceed to determine those issues on paper.