There's a time and a place for expert evidence...

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The High Court recently granted permission for an examination into the prior conduct of two partners of insolvency practice BDO, who had been appointed as the former administrators of One Blackfriars Limited, owner of the site on which the tower, also known as the "Vase", is currently nearing completion on the South Bank.

Humphries Kerstetter acted for the applicants, the liquidators of One Blackfriars Limited. Mayer Brown represented the respondents, the former joint administrators of One Blackfriars Limited. The claim is being funded by Therium Capital Management Limited.

The case promises to be high-profile in view of its subject matter and the parties involved. It has already clarified the law on the bar a statutory officeholder needs to reach to bring insolvency proceedings of this nature. It also banishes what might have been a chilling effect on the ability of liquidators to commence proceedings without a significant front-loading of costs and the disclosure of pre-action expert evidence.

Overview and background

The recent High Court decision in *Re One Blackfriars Limited [2018] EWHC 901 (Ch)* examines both the merits threshold and the evidential burden required to be met by officeholders pursuing applications under Paragraph 75(6) of Sch B1 to the Insolvency Act 1986 (the "IA 1986") for permission to examine the conduct of former administrators of a company[1] .

The property was sold in October 2011at what the liquidators allege, was a significant undervalue (particularly taking into account the 3rd party valuations prepared at the time), leaving millions owing to the lower ranking secured, unsecured and equity investors.

The joint administrators were subsequently discharged and the Company dissolved. In early 2016, upon the application of one of its creditors, the Company was restored and placed into liquidation. The liquidators carried out a thorough investigation of the prior conduct of the joint administrators and concluded that there was a case to answer. They sought permission from the court to commence proceedings.

Against this background, the joint administrators fiercely opposed the liquidators' application for permission. In so doing the joint administrators argued:

(i) Despite the contemporaneous valuations in this case, no proceedings could be commenced in the absence of pre-action expert evidence as to undervalue;

(ii) Notwithstanding its privileged and confidential nature, such expert evidence needed to be disclosed and relied upon for the purposes of seeking the court's permission;

(iii) The relevant time for assessing the quality of that expert evidence was the point at which the application for permission was issued, as opposed to what was put in evidence for the hearing of the application; and

(iv) Without advanced expert evidence at the time of issue, the proceedings amounted to an abuse of process.

[1] Section 98 only permits such claims to be made "with the permission of the court".

Executive summary

Whilst making clear that every application of this nature will turn on its facts, the Judge despatched each of the joint administrators' grounds of opposition. In so doing, he clarified that there is a distinction to be drawn between cases brought by bankrupts against their trustees in bankruptcy, which tend to be vexatious or misplaced, and claims of this nature brought by professional persons. The Judge also clarified that the test for permission was whether the applicant could show a reasonably meritorious cause of action which was reasonably likely to result in a benefit to the estate. The threshold may be similar to what would be needed to survive a strike-out application, but the Judge made no finding in this regard and specifically emphasised that the applicants were not required to undertake a reverse burden of proof.

The Judge held there was no absolute requirement for expert evidence relating to valuation prior to issuing proceedings of this nature. In this case a valid claim could be advanced on the basis of contemporaneous valuation evidence. He further held that in proceedings brought by insolvency professionals against former statutory officeholders, 3rd party expert evidence showing a breach of duty falling within the expertise of the claimants, would not be required.

Procedural background

The liquidators of the Company served draft particulars of claim in support of their application for permission that there should be an examination of the conduct of the Company's former joint administrators pursuant to Paragraph 75(6) of Sch B1 to the IA 1986. The particulars of claim alleged that breaches of duty by the joint administrators, principally comprising negligence and a lack of independence, resulted in the Company's sole asset, a prime development site on the South Bank of the Thames at Blackfriars, being sold for a price which was substantially less than the best price reasonably obtainable and some £47m below an independent valuation provided to the Company the previous year.

The liquidators sought and obtained early draft expert evidence in relation to liability and quantum at a pre-action stage and prepared the draft particulars of claim with the benefit of that evidence. The draft particulars of claim were exhibited to a supporting witness statement by one of the liquidators who affirmed his belief in their veracity. On the basis of the draft valuation evidence available to the liquidators, it was pleaded that the site had a value of at least £115m at the time of sale. The liquidators confirmed to the joint administrators that that figure was based on preliminary expert analysis.

The joint administrators opposed the application, which was issued following a substantial pre-action protocol period, with an 11th hour argument that the claim was not supported by expert evidence. This was on the basis that no such evidence had been placed in evidence before the court for the purposes of the application. The joint administrators also advanced the argument that, absent such expert evidence, it was an abuse of process for the liquidators to have issued the claim at all, especially in circumstances where issue was designed to prevent a limitation defence arising.

The liquidators argued that the authorities relied upon by the joint administrators for these propositions were distinguishable in that they related to vexatious or unmeritorious claims by non-professional persons, typically claims by bankrupts against their former trustees in bankruptcy. The liquidators argued further that in so far as the authorities suggested expert evidence was

appropriate, the present case was distinguishable on the basis that a claimant who is also a statutory officeholder is capable of determining for themselves whether there has been a breach of statutory duty, in cases concerning the duties imposed by insolvency legislation. While expert evidence may in due course lend weight to that determination, it was not essential for the officeholder to reach such a conclusion.

In relation to the alleged need for expert valuation evidence, the liquidators relied on the contemporaneous valuations which demonstrate there was a case to answer. Additionally, the liquidators argued that expert evidence had in any event been obtained in this case, which was a different matter from whether it should be disclosed at the permission stage, and had signed a statement of truth in support of draft particulars of claim, verifying they had been prepared with the benefit of expert input.

A two-hour hearing took place on Friday 13 April 2018 before Mr William Trower QC sitting as a Deputy Judge of the High Court. Mr Simon Davenport QC and Mr Tom Poole (3 Hare Court) instructed by Humphries Kerstetter, appeared for the liquidators, and Mr David Turner QC and Mr Ben Smiley (4 New Square) instructed by Mayer Brown International, appeared for the joint administrators.

The Law

The Judge acknowledged that Sch B1 contains no express guidance on the factors to be taken into account when determining an application for permission under Paragraph 75(6) of Sch B1, nor is there very much case law on the correct approach. However, as the paragraph tracks similar provisions to where the court's leave is required under section 212(4) of the IA 1986 (for post-release misfeasance applications against liquidators), the Judge held that some guidance could be gained from the authorities concerned with that section.[2]

While a similar provision under which the court's leave is required for seeking post-release relief against a trustee in bankruptcy exists under section 304(2) of the IA 1986, the Judge cautioned the relevance of jurisprudence in relation to applications brought by the bankrupt himself.[3] The Judge concurred with Hart J's views in *Brown v Beat [2002] BPIR 421, 424D* that applications by bankrupts against the trustee "*have a tendency to be vexatious and therefore it is appropriate for there to be a filter for that reason.*"[4] He found that such considerations do not apply where proceedings are brought by a subsequently appointed officeholder under section 212 of the IA 1986 or Paragraph 75 of Sch B1:

> *…In such cases, it is apparent from the wording of each provision that the filter is introduced for a different reason. It is required because the former officeholder has received a discharge or release and no longer has the assets of the estate in his possession. He is therefore no longer able to indemnify himself in respect of unmeritorious claims, a point made by Sales J in Re Hellas Telecommunications (Luxembourg) II SCA [2011] EWHC 3176 (Ch) (at [96]).*[5]

The Judge then examined the different bases on which the threshold for applications in previous cases had been characterised. He concurred with Rose J in *Re Angel Group Ltd [2015] EWHC 3624 (Ch)* (at [46]) who said that test was whether or not the claims sought to be brought had "*a proper foundation*". The Judge found that approach to the merits was further considered in the Court of Appeal in *Parkinson Engineering Services plc v. Swan [2010] Bus LR 857* per Lloyd LJ in paragraph 34

[2] Paragraph 21.
[3] Paragraph 22.
[4] Paragraph 22.
[5] Paragraph 23.

which introduced the concept of potential benefit to the estate:-[6]

> *"The judge started by considering whether it would be appropriate to allow proceedings under section 212. It seems to me that this was the correct starting point. He had seen (as we did) the decision of Hart J in Brown v. Beat [2002] BPIR 421 where the judge, considering the corresponding provision as regards bankruptcy, identified two criteria: whether or not a reasonably meritorious cause of action has been shown, and whether giving permission for its prosecution is reasonably likely to result in a benefit to the estate. Those are not exhaustive, but they are certainly relevant and likely to be among the most important factors."*

This second requirement will depend not only on the merits of any particular claim, but also the level of any potential recovery having regard to the costs of the litigation such that a distribution to unsecured creditors could reasonably be expected in the event of success.

Drawing these threads together, the Judge held that an applicant under Paragraph 75 had to demonstrate a "reasonably meritorious" cause of action which was "reasonably likely" to result in a benefit to the estate. He found that in substance this amounted to the same question which was posed in *Mc Guire v Rose [2014] BPIR 650* (paragraphs 23 to 25) as to whether the case was one which a reasonable litigant would commence and pursue, and also that "reasonably meritorious" was synonymous with the requirement for the case to have a "proper foundation" per Rose J in *Angel Group*.

The Judge held that in the circumstances of this case, the requirements were clearly made out.

A supplementary argument was raised by the joint administrators whereby the claim was alleged to have been an abuse of process at the point of issue. The liquidators served their draft expert evidence on the joint administrators prior to the hearing of the application without prejudice to their primary arguments that it was not necessary for them to do so. The joint administrators alleged that given the date of the draft expert evidence disclosed by the liquidators post-dated the date of issue of the application, it could be inferred that there was no known basis for the claim nor did the liquidators hold an intention to prosecute it at the point the application was filed. This ambitious argument was robustly rejected by the Judge, who held it was of "no substance".

The Judge specifically held that it made no difference if the liquidators issued proceedings because of the imminent expiry of the limitation period or not. All this demonstrated, he held, *"is that the timing of the issue of process was dictated by limitation issues when, in the absence of such constraints, they may have done more preparatory work before issuing their application. This does not demonstrate that additional preparatory work was absolutely necessary in order to render it proper (in the sense of not being an abuse) to issue the application when they did"*[7]. He went on to find that the existence of near contemporaneous valuations by third parties around the date of the sale were capable of evidencing an arguable value which would be sufficient to justify the issue of proceedings – a point which had been made by the liquidators from the outset.

The acid test

What then does the threshold for permission amount to in practice?
The joint administrators submitted that it was a "high hurdle". This was rejected by the Judge, who

[6] Paragraph 25.
[7] Paragraph 45.

noted this point was not argued with any conviction at the hearing – indeed the joint administrators accepted in argument that the test was lower than that which would need to be established by a claimant to survive a summary judgment application – a point with which the Judge concurred, holding that a mini trial on the merits was not appropriate in an application of this nature.

Whilst not stating so expressly, it is submitted that it can be inferred from the judgement that the test is not dissimilar to the strike-out threshold under CPR 3.4 (that a claim should disclose reasonable grounds for its continued prosecution), albeit the judge noted that the burden in any such application would fall on the defendants and it was not for applicants in hearings of this nature to assume that burden:[8]

> *The reason for this is that the burden of establishing that a claim has no real prospect of success, or should be struck out as an abuse, rests with the respondents, while the burden of satisfying the court that proceedings under paragraph 75 of Schedule B1 can be pursued lies with the applicants. If the court can clearly see that summary judgment would be given against the applicants, then doubtless it will not give permission under paragraph 75(6), because it would be pointless to do so, but the authorities do not support a proposition that the applicant is required to demonstrate that no application by the respondents to strike out or obtain summary judgment would succeed.*

Conclusion

The joint administrators' opposition to the application was highly ambitious and it would appear that its primary purpose was not to halt proceedings, but to force early disclosure of the liquidators' expert evidence for tactical reasons in the face of a very clear costs risk. The point was one of principle in this case given that the liquidators had the benefit of written expert evidence on liability and quantum which they relied upon without prejudice to their primary case. Nevertheless, had the joint administrators' arguments held sway, it would have had a chilling effect on the ability of other claimants to commence proceedings against misfeasant former statutory officeholders without first front-loading the costs of obtaining expert assistance on each separate area of alleged breach.

A sensible and pragmatic judgment, the Judge also corrected any future attempts by defendants in insolvency proceedings of this nature to import jurisprudence from bankruptcy cases and seek to convene a mini trial on the basis of otherwise privileged expert evidence.

Re One Blackfriars Limited is the only reported decision on Paragraph 75(6) of Sch B1 to the IA 1986 and has helpfully clarified the law in this area.

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[8] Paragraph 28.