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ARTICLE

Administrators: Conflicts of Interest and Removal

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Synopsis

There has been a flurry of decisions in 2018 in which allegations have been made of unacceptable conflicts of interest on the part of administrators. The key issue for practitioners is to distinguish between those actual or potential conflicts that will attract censure and those that can adequately be managed. Controversy surrounds, in particular, 'pre-pack' administrations, which are fertile ground for conflicts but are authorised by the legislature and the regulators. For the first time since the extensive reforms of the administration regime fifteen years ago, the courts have addressed these issues head-on in a series of important decisions. This article analyses the cases in turn to see what lessons can be learned by administrators and those who advise them.

Introduction

Some 15 years on, it is fair to say that the introduction (via the Enterprise Act 2002 amendments to the Insolvency Act 1986, 'IA') of the 'out-of-court' regime for the appointment of administrators by directors or qualifying floating charge holders has brought with it a degree of controversy, in particular with regard to pre-pack sales – a procedure which is commonplace yet perpetually controversial. The absence of any judicial scrutiny at the crucial point of entry, that is to say the administrator's out-of-court appointment, and the fact that interested stakeholders seemingly have no right to intervene at that stage, are all obvious contributing factors.

Yet, even 'in-court' appointments have also on occasion proved to be controversial for similar reasons, with the spotlight zooming in on what is often perceived as being, at its most innocent, an overly cosy relationship between the applicant for the administration order and the office-holder, especially in circumstances where the office-holder's firm has at the pre-appointment stage been heavily involved in advising the company or its directors.

The first seven months of 2018 alone has seen several important decisions in the Business and Property Court of England and Wales which address, either head on or tangentially the issue of administrators' conflicts of interest. These cases are (chronologically) *VE Vegas IV Investors LLC v Shinners and others* [2018] EWHC 186 (Ch), *Memon v Cork* [2018] EWHC 594, *Tailby and Courtman v Hutchinson Telecom FZCO* [2018] EWHC 360 (Ch), *Davey v Money* [2018] EWHC 766 and *Re Zinc Hotels (Investment) Ltd* [2018] EWHC 1936 (Ch). This article will explore the impact of those decisions and their implications for future insolvency practice.

The elephant in the room

Those of us who practise in insolvency, whether we are lawyers or insolvency practitioners are fully aware that the UK regime is replete with potential, if not actual, conflicts; these have either become so commonplace as to be ignored, or have been legitimised through a combination of custom and practice, as well as regulatory rules. This is the elephant in the room: obvious and recognised conflicts which exist in all but name which attract no censure.

Hence, as an obvious example, a bank panel insolvency practitioner will routinely be appointed as administrator by a floating-charge holding panel bank (as often as not having first acted as a reporting accountant). This is despite the prior existing relationship and despite the fact that by paragraph 3(3) of Schedule B1, the objective of 'realising property to make a distribution to one or more secured or preferential creditors' under paragraph 3(1)(c), is subordinated to the administrator's paramount duties under paragraph 3(1)(a), to pursue the objective of rescuing the company as a going concern and (if this is not possible, under paragraph 3(1)(b)), to achieve a better result for creditors 'as a whole' than would be likely were the company to be wound up.

The inherent potential conflict in these instances is an obvious one. Yet eyebrows are rarely raised. Quite the opposite, in fact; in *Zinc* (at [74-79] and [86-91], per Henry Carr J) and in Davey (per Snowden J at [339-340[1]]) the respective judges confirmed that the

Notes

1 Citing *Commonwealth Bank of Australia v Fernandez* [2010] 81 ACSR 262.

practices were not objectionable and were, in some instances, perfectly sensible ones.

Likewise (but more controversially), in the context of pre-packs, it is a given that the proposed administrator will, prior to his or her appointment, have been advising the directors/the company on insolvency options, albeit on behalf of his firm and will have been closely involved in negotiating the deal. Whilst such relationships often generated a degree of disgruntlement, it was a universally acknowledged truth that there was nothing inherently objectionable about the very same insolvency practitioner then taking the appointment.

On the management side, directors of the insolvent company who wish to buy the assets via a pre-pack via a newco are inevitably in a position of conflict, as they are inevitably wearing two conflicting hats: as buyer, they wish to buy for the lowest price they can; as seller (i.e. as a director of the selling company), they owe a fiduciary and statutory duty to achieve the best price for the company.

Plainly, however, there can be no one-size fits all approach. It cannot sensibly be said that all panel appointments are objectionable. Equally, it cannot be said that no insolvency practitioner who has been involved in pre-pack negotiations should ever go on to take the actual appointment. Nor can it be said that there can never be a pre-pack sale to existing management.

Or can it?

The question, surely, is (or should be) what is in the best interests of the administration?

Interests of the administration vs conflict

There is plainly a tension between what are, in fact, the real, substantial and honest interests of the administration and the perception of conflict or potential conflict, or other impropriety – irrespective of whether that conflict actually exists.

For example, in cases where the removal of an administrator is sought on the grounds of 'unfair harm' under paragraph 74 of Schedule B1, or on the grounds of 'improper motive' on the part of the appointor under paragraph 81, the acid test is whether the objects of the administration remain likely to be achieved. If this is the case, the likely end result is that the administrators will be permitted to remain in office: see (with regard to paragraph 74) Blackburne J in *Re Lehman Brothers International Europe* (in Administration) [2008] EWHC 2869 (Ch) at paragraphs 38-39 and (with regard to paragraph 81) Philip Marshall QC (sitting as a Deputy Judge of the Chancery Division) in *Re FREP (Knowle) Ltd (in administration)* [2017] EWHC 25 (Ch) at paragraph 48.

Yet perhaps perversely in conflict cases where removal is sought under paragraph 88, the question of whether the objects of the administration are in fact likely to be achieved (notwithstanding any conflict, objectively viewed) seems to be of relatively little significance. Likewise, whereas the unfair harm cases under paragraph 74 require a demonstrable tangible detriment to the applicant and actual unfairness (see for example *Re Nortel Gmbh* [2013] UKSC 52 at 121-122 *and Holgate v Reid* [2013] EWHC 4630 (Ch)), the removal cases under paragraph 88 do not require proof of *actual* unfair or otherwise *actual* inappropriate conduct.

Moreover, the wishes of creditors (or other stakeholders with a tangible interest) are a significant consideration:

> '[The Court will] have regard to (but will certainly not be bound by) the wishes of the majority of those interested in deciding whether to remove an office-holder. It should not lightly remove its own *officer and must pay due regard to the impact of any removal on his professional standing and reputation*' (emphasis supplied)

per Warren J in *Sisu Capital Fund Ltd v Tucker* [2005] EWHC 2170 (Ch) at 86, citing *Re Edennote Ltd [1996]* 2 BCLC 389 per Nourse LJ at 398F. See also *re Zegna III Holdings Inc* [2010] BPIR 277 per Norris J at [10].

But there are powerful countervailing factors. In most cases a change of office-holder, or the appointment of an additional so-called conflicts administrator, will inevitably significantly add to the administration costs, and may well also lead to a duplication of work. Likewise, the removal of an administrator who has been in office for some time will usually mean that the new incumbent will simply have to start again. These are all highly relevant factors.[2]

The authors suggest that – at least – in those cases where (i) the administrator has been in office for some time, (ii) the quality and value of the work undertaken by him/her is not capable of serious attack and (iii) the objects of the administration remain reasonably likely to be achieved, even if he/she remains in office, the court should be slow to remove him/her from office on the grounds of conflict.

Regulatory framework

The Insolvency Service's 'Insolvency Code of Ethics' has been adopted by all the authorising bodies. It provides a framework that underpins the 'Fundamental Principles' set out in Part 1 paragraph 4. Fundamental principal 4(b) is 'Objectivity'.

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2 See for example, HHJ Stephen Davies in *Tailby and Courtman* at [97].

This provides that:

> 'An Insolvency Practitioner should not allow bias, conflict of interest or undue influence of others to override professional or business judgments'.

Conflicts of interest are addressed at Part 2 (paragraphs 25, 31-32) and Section A (paragraphs 40-48). Paragraph 31 provides:

> 'An *Insolvency Practitioner* should take reasonable steps to identify circumstances that could pose a conflict of interest. Such circumstances may give rise to threats to compliance with the fundamental principles. Examples of where a conflict of interest may arise are where:
>
> a) An *Insolvency Practitioner* has to deal with claims between the separate and conflicting interests of entities over whom he is appointed.
>
> b) There are a succession of or sequential *insolvency appointments* ...
>
> c) A significant relationship has existed with the *entity* or someone connected with the *entity* (see also section A)'

Separately, paragraph 25 lists a number of safeguards 'to be considered'. These include obtaining legal advice (unsurprisingly), changing the members of the team, involving another insolvency practitioner to perform part of the work and/or taking a joint appointment where the conflict arises in the course of the insolvency appointment and the use of separate insolvency practitioners and/or staff.

Section A provides guidance for the identification of prior professional and personal relationships which can lead to 'threats to the fundamental principle of objectivity'. Examples of such relationships are listed at paragraph 42. They include relationships with creditors/debenture holders and the directors or shareholders of the insolvent company. However, the mere existence of such relationships will not per se give rise to an actual or potential conflict. This is wholly consistent with the case-law.

Once such a relationship has been identified, it is then incumbent upon the insolvency practitioner to evaluate the impact of that relationship in the context of the appointment being sought (see paragraph 44) and the extent of the threat to the principle of objectivity. This will involve considering the non-exhaustive list of factors prescribed in paragraph 44(a) to (i). These include: the extent of the familiarity with the entity, the nature of the previous duties undertaken, whether fees previously received were substantial, how recently the other work was carried out, whether the appointment being sought involves consideration of any work previously undertaken by the practice.

If a threat has been identified, it is then for the practitioner to consider whether it can be mitigated or eliminated by putting in place any particular safeguards, including those listed in paragraph 25. Additional safeguards (under paragraph 46) may include withdrawing from the team altogether. If, however, no or no reasonable safeguards can be put in place, then (by paragraph 47) the relationship in question will constitute 'a *significant* personal relationship' and 'Where this is the case, the Insolvency Practitioner should conclude that it is not appropriate to take the insolvency appointment'.

Finally – and importantly – paragraph 48 concludes as follows:

> 'Consideration should always be given to the perception of others when deciding whether to accept an *insolvency appointment*. Whilst an *Insolvency Practitioner* may regard a relationship as not being significant to the *insolvency appointment*, the perception of others may differ and this may in some circumstances be sufficient to make the relationship significant.'

Conflict of interest: a judgment call for the Insolvency Practitioner?

Plainly, the exercise of deciding whether an actual or potential conflict of interest exists is a matter for the subjective assessment of the insolvency practitioner immediately prior to the appointment, in the exercise of his/her professional judgment, having regard to the Code. Hence the prescribed form of proposed administrator's consent to act[3] requires the following statement:

> '3. I [have]/[have not] had any prior professional relationship with the company.
>
> [The following is a short summary of my prior professional relationship(s) with the company:]'

That subjectivity is also reflected in paragraph 103(6) of Schedule B1 which provides that an additional administrator may not be appointed without the consent of the administrator already in office. This reflects the deference with which the views of the incumbent office holder is to be treated. The incumbent has a de facto right of veto.

Notes

3 Insolvency (England and Wales) Rules 2016, rule 3.2.

Administrators' conflicts in the case law: conflicting authority?

Yet on the case-law it seems that where, ex post facto, removal of an administrator is sought under paragraph 88 of Schedule B1, there may be little or no place for the engagement of subjective criteria and little or no scope for the evaluation of what the administrator actually thought or did at the point of his appointment by reference to the circumstances pertaining at the time.

Hindsight, it seems, is wonderful thing…

Likewise, the cases universally demonstrate that the question of whether what the administrator actually did in fact achieved a better outcome for creditors than might otherwise have been the case, or whether the objects of the administration had nonetheless been achieved or remained achievable is largely irrelevant, as is the question of whether there is, prima facie, a claim in misfeasance.[4]

Thus, in the well-known case of *Clydesdale Financial Services Ltd v Smailes* [2009] EWHC 1745, the joint administrators were removed by David Richards J under paragraph 88 without any criticisms having been made by the Court of their conduct. They were removed because they were 'too closely involved'[5] in the pre-pack sale and therefore could not be expected to conduct an independent review of it in circumstances where the terms and circumstances of the sale were a legitimate matter for consideration.

Conversely, the existence of an actual conflict will not inevitably lead to the administrator having to give up his appointment. See HHJ Stephen Davies in *Tailby and Courtman as joint administrators of TPS Investments (UK) Ltd Hutchinson Telecom FZCO.* It must all depend on the particular circumstances including:

> '37 … (a) the nature and extent of the conflict (clearly different considerations will apply where the investigation is still at an early stage to those where litigation is already in prospect); (b) the point at which the question is being considered (clearly different considerations will apply when the officeholder has not been appointed to those where he has been in position for some time); (c) whether and if so how the conflict can properly be managed at that time and – insofar as can be known – at a future stage; (d) the consequences for and against removal both in terms of time and cost and more generally'

> '94 I have already referred to the relevant legal principles. It is plain in my judgment that Hutchinson's primary submission, which is that the existence of an actual conflict by itself means that the administrators must apply to the court for permission to cease acting as administrators for one, if not more, of the relevant companies, is wrong as a matter of law. It is also plain in my judgment that what the court needs to consider, and what the parties ought to have addressed in their evidence, but did not in any of or any sufficient detail, is the question as to how, if at all, such conflicts can properly be managed without the need for the administrators having to cease acting…'

> '98 Moreover I am also satisfied that this is not a case where the conflict has become so acute that steps to manage it must be taken immediately…'

Management of conflicts: has anything changed?

As to the management of actual or potential conflicts, guidance is to be found in *Sisu Capital Fund Ltd v Tucker* at paras 91 to 120, *Parmelat Capital Finance Ltd v Food Holdings Ltd* [2008] BCC 371 and *Re York Gas Ltd* [2010] EWHC 2275 (Ch). The following principles can be distilled:

- Licensed insolvency practitioners are professional men who are well accustomed to dealing with conflicts
- In general, it is in the interests of creditors, at least in the first instance, to appoint a single officeholder and any conflicts are usually best left to be managed if and when that becomes necessary
- If and when it becomes clear that any conflict is sufficiently material to require to be managed, one of a variety of different approaches may be appropriate depending on all the circumstances
- Such different approaches may include, for example, obtaining legal advice, the appointment of an additional partner from the same firm or the appointment of an independent partner from a different firm and/or applying to Court for directions.
- If the conflict cannot be managed, then the office holder must give up his conflicting appointment.

This is all still good law, notwithstanding the alarm generated by the decision in *VE Vegas*.

Notes

4 See also *Shepheard v Lamey [2001] BPIR 939* (on removal of liquidators); if there is a possibility of misfeasance proceedings against a liquidator, he should, ordinarily, be removed. Per Jacob J: 'The fact is that these documents alone indicate a case for removal. After all, all that one has to find is some good cause why a person should not continue as liquidator. You do not have to prove everything in sight; you do not have to prove, for example, misfeasance as such; you do not have to show more than there may well be a case for misfeasance or, indeed, incompetence.'

5 At paragraph 30.

VE Vegas Investors IV LLC and *Ors v Shinners and Ors*

VE Interactive Ltd ('VE') was a provider of software and related services to online retailers. It was traded from 2009 but made losses throughout its life. These losses totalled £25 million by 2015. The company had persuaded many wealthy individuals to invest and buy shares, but by the end of 2016 it was balance sheet insolvent with a deficit of least £9 million. As of April 2017, VE was late in paying its staff, and its essential suppliers (in particular Microsoft) were threatening to cut off supplies in the absence of a substantial payment. A new board of directors had been appointed in March 2017; their view was that VE needed to raise £20 million urgently. This funding was not secured.

On around 10 April, S & W Ltd (the IP practice in which the Respondents were all directors) was retained to advise VE on insolvency options. The Respondents then worked with VE's management and staff over a period of around six business days to achieve a pre-packaged sale of the business before a threatened collapse. During that period, they experienced some delays in the provision of information by the company's management staff, which heightened the difficulty of securing a competitive sale.

Over this period, VE had been intending to make an in-court administration application. However, VE was trumped by a group of creditors, who made their own application, seeking the appointment of IPs at Deloitte. That application was heard on notice to VE at the Leeds District Registry on 25 April 2015. It was common ground that VE should go into administration. The issue for the Court at the hearing was whether the Deloitte team should be appointed as administrators, or whether the Respondents should be. In the event, the Respondents were appointed based on creditor support (the independence of those creditors was later challenged).

The following day, they entered into a pre-pack sale of greater part of VE's business and assets. The purchasing entity was Rowchester Ltd, which was connected to the company's management. Rowchester had submitted the highest of two bids (the pool of potential bidders whom the respondents were able to attract at short notice).

Certain aggrieved creditors alleged that VE's management had won the pre-pack by acting in breach of their duties and by prejudicing other bidders, who were deprived of information. Hence they claimed that there were grounds on which both the management and S & W should be investigated, which necessitated the removal of the Respondents as administrators. Hence the application under paragraph 88. Whilst it was suggested by the applicants that the business may have been sold at an undervalue, there was no evidence to this effect.

The application was contested, but before it had concluded, the administrators offered their resignation and asked the court to abridge time for those resignations to take effect immediately. If the court did not abridge time, then the administrators would remain in office for a further 5 days before their resignations could take effect. Registrar Jones did not abridge time but nonetheless held that administrators should be removed immediately rather than remaining in office for another 5 days.

Registrar Jones did not abridge time; he held that administrators should be removed immediately rather than remaining in office for another 5 days. This was because 'The Respondents' failure to approach this matter correctly' persuaded him that he should not wait for their resignations to take effect (paragraph 31)

Plainly, he wished to deliver a full, reasoned judgment, but was unable to do so because of the resignations.

Based on the facts as outlined by him at paragraph 19 of the judgment, Registrar Jones found, at paragraph 20, that there were 'two possible scenarios at either end of the spectrum of possibilities referred to'. These were that:

> 'i) Those facts occurred within a significantly short time-scale because of the Company's dire financial position, deficient books and records and issues of dispute (in particular with Ve Interactive LLC) which meant that the directors/management and/or S&W did the best they could in the circumstances and/or in any event achieved the only realistic sale, for good value at the best possible price.
>
> ii) Those behind Rowchester Limited took advantage of their position as directors of the Company and used that position and resulting knowledge to achieve an advantage for themselves and intentionally or unintentionally in practice effectively exclude others from a realistically competitive pre-pack process. This enabled Rowchester Limited to agree a pre-pack purchase on terms at an undervalue.'

Whilst recognizing (at paragraph 21) that 'there is potential for many other scenarios' and stressing that he was not seeking to give a decision on the merits, the Registrar found (at paragraph 22) that 'the second possible scenario' made it 'clear there is serious issue for investigation' and that it should have been apparent to the Respondents from the date of their appointment that there were 'at least' two issues to investigate: first, whether the pre-pack was entered into in circumstances where the directors were in breach of duty (putting their own interests first), at the expense of other outcomes (including a better market price) and second, whether S & W whilst acting (pre-administration) in accordance with their contractual retainer, breached their duties of reasonable care and skill with the result that loss was caused to VE as a result of or upon the sale of the business.

The Registrar concluded that the Respondents as members of S & W were conflicted and could not carry out those investigations: 'This is not technical legal analysis. It is obvious' (paragraph 25). The Respondents were inextricably bound up in the process and therefore could not carry out those investigations. He noted that that did not necessarily mean they should therefore vacate office. Alternative solutions might have included the appointment of 'conflict administrators', although because of the Respondents' resignations, this was not an option (paragraph 34).

Having heard them give their oral evidence under cross-examination, Registrar Jones considered that the Respondents had become primarily concerned with the defence of potential claims against S &W, which led them to lose perspective on the claims that might be brought in connection with the sale and on the conflict arising.

Therefore, he concluded that their removal would be appropriate on the facts of the case, but with the proviso that 'this is not a case where removal will or should encourage unjustified applications' (paragraph 36). That aspiration, and whether or not it is a realistic one, is returned to below.

Zinc Hotels (Investment) Limited v Beveridge and others

It was not long before a High Court judge was asked to apply the decision of Registrar Jones in *VE Vegas*. *Zinc v Beveridge* concerned a group of 25 companies comprising the Zinc Group, which had been placed into administration by the security agent for a syndicate of secured creditors in its capacity as qualifying floating chargeholder. Administrators from Alix Partners, who had advised the secured creditors on pre-appointment contingency planning, had been appointed. Some of the shareholders made an application seeking the removal and replacement of the administrators under paragraph 88 of Schedule B1, as well as other relief under paragraphs 74 and 75 arising from (it was said) unfair harm caused to the shareholders by the secured creditors, along with misfeasnce. It was alleged that the administrators (and their solicitors) lacked independence and were conflicted as a consequence of their relationship with the secured creditors.

Following a first directions hearing, the shareholders then made a further application seeking interim relief on an urgent basis in the form of (among other things) the appointment of 'additional concurrent joint administrators', whose function (it was said) would be 'to represent the interests of contributories/shareholders for the purpose of achieving the statutory purpose of the administrations.'

The incumbent administrators resisted that proposal, on the principal ground that it would lead to a deadlock situation that would inhibit the realisation of the companies' assets. It was suspected by the secured creditors (who were separately represented at the hearing) that the shareholders were using the proceedings to try to exert pressure and encourage the secured creditors to take a 'haircut' on the debt.

The interim application came on before Henry Carr J for a three day hearing. Front-and-centre of the shareholders' submissions was the decision of Registrar Jones in *VE Vegas*. It was said by the shareholders that the existence of conflicts of interest, giving rise to a 'serious issue for investigation', justified the relief they sought. There were two aspects to the shareholders' allegation of conflict.

Firstly, the shareholders contended that the administrators were conflicted because of their engagement with the secured creditors pre-appointment. Henry Carr J disagreed that there was a conflict on that basis. The judge drew attention to several authorities that spelt out that such a prior relationship was no bar to an appointment, including the very recent judgment of Snowden J in *Davey v Money* [2018] EWHC 766 (Ch), which dealt in considerable detail with various aspects of an administrator's duty. Having referred to Australian authorities, Snowden J considered in *Davey v Money* that the relevant question was not whether or not there had been a prior relationship, but:

> 'whether the insolvency practitioners could be relied upon to act impartially and in accordance with their duties required an assessment of all the circumstances.'

Henry Carr J accepted the submissions of the respondents that it would be unusual in an insolvency of any complexity for there *not* to have been pre-appointment engagement. The judge also drew attention to the specific provisions in rr.3.35(10)(a), 3.36 and 3.52 of the Insolvency Rules 2016 requiring disclosure in an administrator's statement of proposals of any pre-appointment costs incurred by them. It was obvious from the very existence of such provisions that pre-appointment involvement did not preclude a subsequent appointment as administrator.

The shareholders also relied on the provisions of the Code of Ethics in support of their argument. But Henry Carr J regarded this as being of limited interest to the court. The judge held that there was a distinction between professional guidance given to practitioners and the interests of the relevant insolvency proceedings; it was the latter with which the court was primarily concerned – the Code of Ethics was a matter for the regulators. This distinction was not a new one: it had been drawn by Millet J (as he then was) in *Re Polly Peck International plc* [1991] BCC 503 and applied to the post-Enterprise Act 2002 landscape by Warren J in *Sisu Capital Fund Limited v Tucker* [2006] BCC 463. The implications of this apparent tension between the scope and content of the duties that an administrator owes in his or her capacity as an officer of the court and in his or her capacity as a regulated professional are still to be worked out, but for the purposes of *Zinc v Beveridge* they relegated the Ethics Code to a side-issue.

Secondly, the shareholders contended that the administrators' decision to continue to use the same solicitors as the secured creditors gave rise to a conflict, in that the solicitors partiality towards the secured creditors infected the independence of the administrators' proposals. Once again, Henry Carr J pointed to previous authority that made clear that not only was there no bar on officeholders using the same solicitors as a creditor, in some circumstances it may be a good thing. In the most recent example, Arnold J had stated in *Avonwick v Shlosberg* [2017] Ch 210 that it 'may well be convenient because of the creditor's familiarity with the debtor's affairs and because of the absence of any real likelihood of a conflict of interest'.

Henry Carr J considered that it had been appropriate for the administrators to consider that the existing knowledge of the secured creditors' solicitors and the absence (at least at the outset) of any conflict justified retaining them to act in the administration. There had been no reasonable prospect of conflict on the part of the solicitors at the outset because it had been expected (based on a Red Book valuation) that the proceeds of sale of the secured assets would break within the value of the secured debt, which meant there would be no surplus and therefore no economic interest on the part of the shareholders. The administrators had, however, instructed fresh solicitors once it appeared that there was a real possibility of a surplus for shareholders. Henry Carr J concluded that there was nothing about the arrangements that was inappropriate and the decisions of administrators were not ones with which the court would interfere.

Perhaps the greatest long-term significance of the judgment in *Zinc v Beveridge* lies in the interpretation given by Henry Carr J to the decision of Registrar Jones in *VE Vegas* and *Clydesdale v Smailes*. The judge pointed out (at [66] to [68]) that both those cases had concerned pre-pack administrations and allegations that the administrators had effected sales at an undervalue.

This was a clear point of distinction from the situation in *Zinc v Beveridge*. Henry Carr J considered that the conflict in the earlier cases arose because the administrators (as the party arranging the pre-pack sale) were said to be involved in the wrongdoing and could not investigate their own conduct. That analysis would seem to limit the ambit of *VE Vegas* to cases of pre-pack, rather than administrations more widely.

Memon v Cork

Some support for that interpretation may be found in the decision of ICC Judge Barber in *Memon v Cork* [2018] EWHC 593, which was argued on the same day that judgment was handed down in *VE Vegas*. *Memon v Cork* has attracted far less notice in the insolvency industry than *VE Vegas*, but it is submitted that it is likely to reflect an approach to removal applications that will more usually be encountered in non-pre-pack situations.

This was an application for the removal of liquidators under s.108(2) (i.e. the equivalent in a liquidation of paragraph 88 of Schedule B1) and/or s.171(2) of the IA. The liquidators had previously been the company's administrators, having been appointed in-court on the application of a 50% shareholder in his capacity as a creditor. The applicant was the other 50% shareholder.

Very serious allegations were made against the liquidators, including that they had been negligent, acted in breach of trust, and had fabricated documents. One of the key steps taken by the liquidators (while they still administrators) had been to sell the company's principal asset.

The applicant shareholder contended the fresh liquidators were necessary in order to investigate and decide whether proceedings should be brought against the incumbent liquidators. In dismissing the application, ICC Judge Barber held in a detailed reserved judgment that:

> 'It takes more than a mere hope that new office holders might spot something that the current office holders may have missed to warrant their replacement…'

Applying the same test ('serious issue for investigation') as had Registrar Jones in *VE Vegas*, ICC Judge Barber held that:

> 'Even applying this lowest bar in the range indicated in the authorities to which I was referred, on the evidence before me I am not persuaded that any cause is shown for the Respondents' removal.'

The reason for the stark difference in outcome between *VE Vegas* and *Memon v Cork* appears to have been that the company's assets in the latter case were realised following what ICC Judge Barber described as a 'bidding war' between one of the former directors and an arm's length purchaser. Accordingly, the concerns that tend to arise in pre-pack situations did not arise.

Where are we now?

It is clear from the decisions in *Zinc*, *Memon v Cork* and *Tailby and Courtman* that in non-pre-pack cases, it will be very difficult for an aggrieved applicant to secure the removal of an administrator on the ground of conflict alone. Moreover, the clarification that has been provided with regard to the propriety of pre-existing relationships between secured creditors, IPs and lawyers is to be welcomed.

However, where pre-packs are concerned, the picture is a different one. It is fair to say that the decision in *VE Vegas* has caused a degree of disquiet in the insolvency industry, especially given the stridently critical tone of some of Registrar Jones' observations about the administrators' initial decision to resist the application. But it is probably the case that its implications are not as far-reaching as some have feared. It appears from the decision of Henry Carr J in *Zinc v Beveridge* that *VE Vegas* is likely to be limited to pre-pack situations, rather than administrations more widely. The approach of Henry Carr J in that case, and of ICC Judge Barber in *Memon v Cork*, will probably be the more conventional one in non-pre-pack administrations.

But where does this leave pre-packs? Despite Registrar Jones' clear indication, as noted above, that 'this is not a case where removal will or should encourage unjustified applications', it is not clear from the reasoning in VE Vegas whether such an application in a pre-pack context will ever be 'unjustified'. This is because the judgment in *VE Vegas* clearly spells out that a conflict of interest will *always* arise in a pre-pack situation (paragraph 19(vi)) and that it is 'obvious' (paragraph 25) that the administrators were implicated in that conflict to a degree that meant they could not investigate the sale by reason of their contractual retainer to arrange the pre-pack. Those facts, in the judgment of Registrar Jones, well justified the removal application in *VE Vegas*. Yet those features will, it is submitted, be present in every pre-pack. It is not easy, therefore, to see how any application to appoint conflict administrators and/or remove existing administrators will be 'unjustified' in any pre-pack.

That may well be the right outcome; as noted at the beginning of this article pre-packs have long been a source of disquiet for these reasons. But the need for an independent officeholder in every case where a dissentient creditor or contributory raises a grievance had not, until the advent of *VE Vegas*, been regarded as an automatic requirement. Hitherto, it had been understood by those operating in this environment that the legislature and the regulators had decided (a) to permit pre-packs; and (b) that the way to manage the conflict and achieve the best value for the creditors was the interpolation between buyer and seller of a licensed insolvency practitioner to supervise the sale, subject to compliance with SIP16.

If *VE Vegas* means that (at least) an additional 'conflicts administrator' is required whenever dissent is expressed, it is perhaps surprising that the legislature and/or the regulators did not spell this out when putting in place a regime that permits pre-packs to take place. It is possible that practitioners may now approach potential pre-pack appointments on the assumption that they will fall within the logic of VE Vegas and that they will not be in a position to resist the appointment of (at least) a 'conflict administrator' if a disgruntled creditor or contributory makes an allegation of undervalue.

If that is right, then it will inevitably alter the risk and costs profile of pre-packs as a tool in the restructuring armoury. It remains to be seen how these issues will be approached by the industry in practice and by the courts in due course.

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