Briefing

BURGES SALMON

Corporate Turnaround and Insolvency

When will a court sanction the sale of fixed charge assets by an administrator?

Paragraph 71 of Schedule B1 to the Insolvency Act allows an administrator to apply to court to sell assets subject to a fixed charge as if they were not subject to the security. The case of *O'Connell v Rollings and others [2014] EWCA Civ 639* is a rare illustration of such an application and provides useful guidance on the factors the court will take into account.

The background

This case concerned the breakdown in relationship between the three company directors of Musion Systems Limited (Musion). Two of the directors (Mr O'Connell and Mr Rock) were creditors of Musion, whose debts were secured under a single debenture (i.e. one document securing the obligations to both directors).

The dispute arose, at least in part, from the termination of IP licences to Musion by the third director (Mr Maass) and companies associated with Mr Maass. That dispute was the subject of arbitration proceedings at the time Musion went into administration.

Intially Mr O'Connell filed for the compulsory winding up of Musion. Mr Rock intervened and appointed administrators out of court under the debenture. Once appointed, the administrators – who had originally intended to rescue the company – realised that cash flow limitations and the ongoing director dispute meant rescuing Musion was unlikely. Instead they set about selling its business and assets as a going concern.

In due course, and after protracted negotiations with multiple bidders, a buyer was identified. The administrators approached Mr O'Connell for a release of his security and, when he refused, applied to the court for an order for sale under Paragraph 71 of Schedule B1 IA 1986. Part of the reason for an application at short notice was that the contract for sale could be unwound if an order for sale was not obtained within 7 days of exchange. The High Court granted the order (Mr Rock having released his security), subject to the condition that the proceeds of sale attributable to the secured assets be applied against Musion's liabilities to the directors.

Mr O'Connell appealed the decision.

The issues

Mr O'Connell substantive objections were that: (i) the amounts owed to Mr O'Connell and Mr Rock were disputed and that the judge had not weighed the prejudice to Mr O'Connell; (ii) that the scope of Musion's IP rights was in dispute, some of them being the subject of the ongoing arbitration; (iii) that the uncertainty as to the IP rights prevented a proper price from being obtained; (iv) that the hearing should have been adjourned to allow Mr O'Connell time to prepare his response to the expedited application.

What did the court decide?

The Court of Appeal rejected all of Mr O'Connell's grounds of appeal. Dealing with the particular points:

(i) The court had duly weighed the prejudice to Mr O'Connell, and had assumed that Mr O'Connell was secured for the full amount he contended.

(ii) As to the scope of IP rights, the administrators had little other option than to sell the assets – the cash flow problems meant that they had to focus on a sale as a going concern rather than sale on a piecemeal basis.

(iii) A proper price had been obtained, and in fact that there had been a full bidding process with a wide public marketing campaign, resulting in multiple interested parties including one (ultimately unsuccessful) bidder who appeared to be completely independent of Musion's directors.

(iv) As to giving further time to Mr O'Connell, there were good reasons for the urgency of the application. Mr O'Connell had very likely anticipated such an application in advance and in any event had articulated his objections quite clearly at the hearing. Nor was there cause to wait until a creditors' meeting had occurred, as the pre-pack line of authority clearly demonstrated that the courts were to take a *"more pragmatic approach to the commercial pressures facing administrators".*

continued overleaf

What does this mean for practitioners?

This decision represents a rare and welcome example of the factors the courts will weigh when considering para 71 applications. Ultimately the courts are showing themselves to be commercially sensitive in weighing such applications, together with applications for directions by administrators in general, and will ultimately be prepared to make a decision where the benefit to creditors and stakeholders as a whole outweighs the prejudice to one or more objecting parties.

Practitioners need to be mindful, however, that where such applications are made at short notice, a trail of correspondence which demonstrates the need for urgency, and the fact that any potential opposing party should have contemplated an expedited hearing, will stand such applications in substantially better stead.

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