Neutral Citation Number: [2020] EWHC 2928 (Ch)

BR-2018-001648

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
INSOLVENCY AND COMPANIES LIST (ChD)
IN THE MATTER OF ERIC ANDREW ROBINSON (IN BANKRUPTCY)
AND IN THE MATTER OF THE INSOLVENCY ACT 1986

Royal Courts of Justice
7 The Rolls Building
Fetter Lane
London
EC4A 1NL

Date: 04/11/2020

Before :

ICC JUDGE BARBER

- -

Between :

ADRIAN JOHN LEOPARD
(As Trustee in Bankruptcy of Eric Andrew Robinson)

Applicant

- and –

ERIC ANDREW ROBINSON

Respondent

- -

Kate Rogers (instructed by HCB Solicitors Limited) for the **Applicant**
Steven Fennell (instructed by Knox Insolvency Solicitors) for the **Respondent**

Hearing dates: 28, 29, 30 and 31 July 2020

- -

Approved Judgment

This judgment was handed down remotely by circulation to the parties' representatives by email. It will also be released for publication on BAILII and other websites. The date and time for hand-down is deemed to be 9 a.m. on 4 November 2020

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ICC Judge Barber

1. This is an application brought by the Trustee pursuant to ss.303 and 363 of the Insolvency Act 1986 (IA 1986) against the Respondent for declarations that:

   (1) The business operated by the Respondent at the date of bankruptcy, known as Anglesey Contract Cleaning ('the business'), formed part of the bankruptcy estate within the meaning of Section 283(1) IA 1986 including, without limitation, its goodwill, book debts, customer contracts, customer lists, stock, plant and machinery, cleaning equipment and any other assets ('the assets');

   (2) The business became vested in the Applicant as Trustee in Bankruptcy immediately upon his appointment taking effect on 20 October 2014;

   (3) The Applicant caused the business to continue to trade following the grant by the Secretary of State of sanction for that purpose, applied for on 22 October 2014 and granted on 24 October 2014;

   (4) From the date of bankruptcy the Respondent has carried on the business pursuant to Section 314(2)(b) IA 1986, or alternatively pursuant to a contract with the Applicant, but the Respondent has no beneficial entitlement to, or interest in, the business or the assets.

2. Further heads of relief were originally sought by the application notice but have been overtaken by events and are no longer required.

Overview

3. On 10 October 2014, the Respondent was made bankrupt on the petition of HMRC, following a failed attempt at an IVA, which was rejected by HMRC due to the Respondent's poor compliance history.

4. At the time of the bankruptcy order, the Respondent ran a cleaning business in Anglesey called Anglesey Contract Cleaning, employing approximately 10 staff. The Respondent had run the business for over twenty years and told the Official Receiver ('OR') that he was keen for it to continue.

5. The OR responded by arranging the urgent appointment of the Trustee on 20 October 2014. On 22 October 2014, the Trustee applied to the Secretary of State for urgent sanction to continue to trade and to use a local bank account. Sanction was granted on 24 October 2014.

6. Thereafter, the Respondent continued to operate the business on a day to day basis under the Trustee's supervision, accounting to the Trustee for all trading income. With the assistance of Robert Freestone, a tax consultant, the Trustee regularised the tax affairs of the Respondent, a process which involved re-opening many past accounting years running up to the date of bankruptcy. The Trustee paid the wages and other bills of the business, including ongoing tax, from the trading income. The Respondent and the Trustee agreed a monthly allowance for the Respondent, set at a figure which the Respondent himself proposed, and adjusted from time to time by agreement. This monthly allowance, together with incidental personal expenditure (to cover wedding trips and holidays etc) from time to time requested by the Respondent and authorised by the Trustee, was paid out of trading income.

7. This arrangement continued amicably for a number of years beyond the Respondent's automatic discharge on 10 October 2015. As confirmed by the Respondent in oral testimony, 'up to 2017, it was an amicable relationship'.

8. By 2017, the Trustee had no option but to issue an application for possession and sale of the Respondent's family home; section 283A(2) IA 1986 lays down a three year time limit for such applications. In June of the same year, the Trustee also urged the Respondent to purchase the business, with a view to ending the Trustee's involvement in the same and progressing administration of the bankruptcy estate. The Trustee, the Respondent and the Respondent's wife met to discuss these matters on 29 August 2017. Shortly thereafter, the Respondent and his wife took legal advice from Knox Insolvency and the current dispute ensued.

9. Since instructing Knox Insolvency in 2017, the Respondent has maintained (among other things) that at all material times from the date of the bankruptcy order onwards, he has been carrying on the business in his own right and not on behalf of the estate. As a corollary of this, his position has been that, save for a sum representing the value of book debts at the date of the bankruptcy order, all trading income from the business since that date belongs to him personally, rather than to the estate.

10. The adoption of this position by the Respondent in 2017 created an impasse. The Trustee had wanted to sell the business to the Respondent at this stage, but the Respondent maintained that the business was his.

11. In 2018 a further dispute, leading to an application for injunctive relief, arose when the Respondent set up a company (ACC North Wales Limited) and appeared to the Trustee to be intent on moving customers of the business over to his new company. The Respondent maintains that the new company was only ever intended to be used as a 'last resort' and that it never traded as he was unable to obtain a business bank account for it (Robinson (1) paras 121,122).

12. In the event, the dispute regarding the new company was ultimately resolved by undertakings given to the Caernarfon County Court on 6 June 2018. In summary, the undertakings given were (1) that the Respondent would not operate in competition with the business pending the determination of a s.303 application to be issued by the Trustee; (2) that the Trustee would issue the s.303 application within 14 days; (3) that the Respondent would cooperate with the Trustee in preserving the business in the meantime, and (4) that the Trustee would (from trading income) pay any costs (excluding legal costs) incurred by the Respondent in preserving the business and in paying its trade creditors, employees and other outgoings within 7 days of the Respondent providing evidence of any such payments.

13. Pursuant to the agreed undertakings, on 19 June 2018, the Trustee issued the current application in the Llangefni County Court, seeking (inter alia) declarations as to entitlement to the business and trading income, together with attendant relief. By consent order dated 31 July 2018, the application was transferred to this court.

14. The consent order of 31 July 2018 also contained a provision permitting the Respondent to 'file and serve a Witness Statement by way of Defence and Counterclaim…... to include all issues relating to the business dispute and any other

matters in this bankruptcy that he considers relevant.' The Respondent then filed a 58-page witness statement dated 14 September 2018. The witness statement contained a number of criticisms of the Trustee, which are strenuously disputed by him. In the event, the parties have very sensibly agreed to confine the issues which I am to decide to an agreed list.

15. Before addressing that list, I should mention the heads of relief sought by the Respondent at paragraph 154 of his witness statement of 14 September 2018. In summary these were as follows:

(1) a declaration that at all material times since the date of the bankruptcy order, the business has been owned and traded by the Respondent;

(2) orders that an account be taken of the value of the business at the date of the bankruptcy order and for payment of this amount by the Respondent to the Trustee;

(3) an order that the Trustee do account to the Respondent for the entire business income since the date of the bankruptcy order, less payments made to trade creditors of the business;

(4) orders that an account be taken of the losses caused to the business by the Trustee's act in writing to customers and for payment by the Trustee to the Respondent of a sum representing such losses;

(5) an order that all payments of trading income into the Insolvency Services Account be refunded;

(6) indemnity costs; and

(7) further or other relief.

16. By 2019, the business had suffered a significant loss of turnover and was no longer profitable. The Trustee became increasingly concerned to extricate himself from a loss-making business. In July 2019 his solicitors wrote to the Respondent's solicitors confirming that the Trustee would 'withdraw' from the business with effect from 31 July 2019. From the correspondence in evidence, it appears that the Respondent's solicitors were initially resistant to this proposal. Over time, however, it proved possible for the parties to agree certain transitional arrangements, which have served to reduce the Trustee's ongoing involvement in the business. As the parties have been unable to resolve the other points of dispute between them without the assistance of this court, however, the Trustee has not yet been able to extricate himself completely.

The Issues

17. For the purpose of the hearing before me, the parties have helpfully agreed a list of issues for me to determine. The issues are as follows:

(1) Which assets vested in the Trustee on his appointment and which assets are outside the estate as tools of the trade, or for any other reason?

(2) It is common ground that goodwill vests in a trustee, but on the facts of this case, did the business have any goodwill capable of being realised?

(3) Who, in fact, traded the business from the date of the Trustee's appointment to the handover date on 31 July 2019?

(4) Following the finding on issue 3, do the monies held in the Insolvency Service Account belong to the bankruptcy estate or to the Respondent personally?

(5) What did the Trustee have the power to do in accordance with IA 1986 Sch 5 para 1 and IA 1986 s.314(2) and/or the express sanction dated 24 October 2014?

(6) Has the Trustee acted outside his powers and, if so, what are the consequences?

(7) What, if anything, was agreed between the Trustee and the Respondent as to the conduct of the business, when was it agreed and how?

(8) Did such agreement give rise to a binding contract?

(9) If so, did the Trustee act within his powers in entering into such a contract?

(10) Is the Respondent, by virtue of his acquiescence/waiver in carrying on the business, estopped from now contending that the Trustee acted outside his powers and/or from denying the existence of a contract?

(11) Has the Trustee acted in breach of the rule in ex parte James?

(12) What relief is the Trustee/Respondent entitled to on the matters on which the court finds in his favour?

(13) If the Trustee is not entitled to his fees and expenses, is he entitled to be remunerated on a quantum meruit basis?

The Evidence

18. For the purposes of this hearing, I have read and considered the following witness statements and their attendant exhibits:

(1) the third, fourth, fifth and sixth witness statements of Adrian John Leopard dated 19 June 2018, 28 May 2019, 19 March 2020, and 25 March 2020 respectively;

(2) the first and second witness statements of Eric Andrew Robinson dated 14 September 2018 and 24 March 2020 respectively.

I have also considered further documents contained in bundles agreed for use at the hearing, to which reference will be made where appropriate.

19. I heard oral evidence from the Trustee and the Respondent.

The Trustee

20. The Trustee qualified as a Chartered Accountant in 1973. He is a Fellow of the Institute, a member of the Chartered Institute of Arbitrators and a CMC registered mediator.

21. The Trustee took his last new insolvency appointment in July 2015 and planned to retire once he had completed his outstanding insolvency cases, which he had anticipated to be by the end of 2019. The Respondent's bankruptcy was one of the last few cases that he took on ahead of retirement. At the date of trial, he was 69 years old.

22. In cross examination, the Trustee was clear and direct in his responses. He engaged openly with questions put to him. I have every confidence in the veracity of his testimony.

The Respondent

23. The Respondent is a hard-working man in his mid-fifties. By the time of his bankruptcy, he had carried on business as a self-employed cleaner for over 20 years. He has been married to his wife Amanda for 30 years and they have three adult children. In 2010, their son Oliver was severely injured in a hit and run accident in Germany whilst serving in the armed forces and suffered life changing injuries. The Respondent and his wife are still involved in his 24 hour care needs to this day. Their home has been specially adapted for him.

24. With the benefit of hindsight, the Respondent believes that Oliver's accident was a contributing factor to his bankruptcy in 2014. For some time, the Respondent was distracted from the business. His absences from work were also a drain on the business.

25. Prior to becoming bankrupt, the Respondent had handled his own tax affairs. For many years he had been preparing his tax returns incorrectly, including VAT in his gross income without showing VAT payments as expenses. This meant that his profits were markedly overstated, which in turn triggered a heavy tax burden. By the time of the bankruptcy order, he had also fallen behind with VAT returns, having failed to file returns for four consecutive quarters. At the date of the bankruptcy, he had no real grasp on the overall level of his indebtedness. He believed it to be in the region of £75,000 (Robinson (1), para 23), whereas in reality it was £180,000-£200,000. His underestimate of creditors coupled with his overstatement of profits led to early hopes in the bankruptcy of a s.282(1)(b) annulment, when on the true figures, this was not attainable.

26. On the Respondent's own admission, paperwork was not his strong point. This may serve in part to explain, although not entirely to excuse, a marked 'disconnect' between the Respondent's written evidence and his oral testimony. A significant proportion of the Respondent's witness statement dated 14 September 2018 consisted of assertions and legal submissions which he could not begin to defend (or sensibly explain) in cross examination. He could not explain or justify paragraphs 26, 32-44, 58 or 103 of his first witness statement, for example. On behalf of the Trustee, Ms

Rogers invited me to treat the Respondent's written evidence with caution. As she put it: 'it is not just the submissions in law; even the factual evidence is not his'. A comparison of the Respondent's written and oral testimony on the matters addressed at paragraphs 26 and 58 of his witness statement of 14 September 2018 lent considerable support to this submission.

27. At paragraph 58 of his witness statement, for example, he asserted that insurance policies for assets of the business should have been in the Trustee's name if it was really the Trustee's business. In cross examination, however, he accepted that the Trustee had told him by email of 29 October 2014 that it was 'essential' that the Trustee's interest was noted on all such policies, and explained that he (the Respondent) had not done this because he thought that the Trustee's assistant at the time, Anthony Davis, would be arranging it. This begged the question of why he had included paragraph 58 in his witness statement.

28. The overall thrust of the Respondent's written testimony was that at all material times he had been carrying on business in his own right and not on behalf of the bankruptcy estate; as put at paragraph 104 of his first witness statement, for example, 'What I believe is that I have continued as self-employed but utilised assets that fell within the Bankruptcy estate and should account to the Applicant for any benefit that I receive from this.' And at paragraph 105, 'Conversely, the post-bankruptcy income is all mine as a sole trader and the Applicant needs to account to me for all of this.'

29. This was in marked contrast to matters accepted by the Respondent in oral testimony. In cross examination, he accepted that on being made bankrupt, the OR had told him that he would have to cease trading. He also accepted that, if the Trustee had not agreed to continued trading, there would be no business. As he put it: 'If the Trustee had said the business is going to close, then that would be it.'

30. The Respondent further accepted that, on receipt of the Trustee's email of 29 October 2014 confirming that he was happy for the Respondent to 'recommence trading under the aegis of the bankruptcy', he had not thought he was setting up a new sole trader business. He also made clear that following the bankruptcy order, he had actively wanted ongoing trading income from the business to go to his creditors. This was in contrast to his written evidence, the thrust of which was that he had been trading in his own right after the bankruptcy order and the Trustee had been 'inter-meddling' with his business, taking trading income to which the estate was not entitled. In cross-examination the Respondent accepted that he had not made any such allegation prior to instructing solicitors in 2017.

31. When it was put to him that it was only since instructing solicitors in 2017 that he had 'chosen to adopt a position', he responded (with emphasis added): 'now I've been made aware of how the bankruptcy should have been run, I am in possession of more knowledge. I didn't know any different at the time. It *should* have been organised in a different way.'

32. The Respondent's belief of how the bankruptcy should have been run coloured his oral testimony to an extent. There were times in his oral testimony when it was clear that he was trying to persuade himself of matters consistent with the 'party line' set out in his written evidence and to frame his answers accordingly. This led to a degree

of inconsistency in his responses and also to some responses which were flatly contradicted by contemporaneous correspondence put to him. Overall, however, although there were undoubtedly mis-recollections and inconsistencies from time to time, I am satisfied that the Respondent did his best in oral testimony to assist the court to the best of his ability and recollection. I have also concluded that, where his written testimony is inconsistent with his oral testimony, in the absence of substantiating documentary evidence, his oral testimony is to be preferred.

33. I turn now to consider the issues which the parties have invited the court to determine.

Issue 1: the assets

34. A sole trader business does not have separate legal personality. All property belonging to, or vested in, the bankrupt at the commencement of the bankruptcy (as defined at s.278(a) of the Insolvency Act 1986) ('IA 1986') forms part of the bankruptcy estate: s.283 IA 1986. In the present context, the only assets which would not vest in the trustee are those that fall within the definition of 'exempt property' within the meaning of s.283(2)(a) IA 1986.

35. By Section 283(2)(a) IA 1986, 'exempt property' includes:

'such tools, books, vehicles and other items of equipment as are necessary to the bankrupt for use personally by him in his employment, business or vocation' ('tools of the trade').

36. It will be seen that, to qualify as exempt, tools of the trade must be both 'necessary' and 'personal'. Items to be used not only by the bankrupt but also by anyone employed in his business are not personal to the bankrupt and not within the definition: Official Receiver v Lloyd [2015] BPIR 374.

37. The tools of the trade must be physical property; they cannot be choses in action: Mikki v Duncan [2017] BPIR 490.

38. In Birdi v Price [2019] Bus LR 489, HHJ Eyre QC sitting as a judge of the High Court analysed the caselaw on tools of the trade and at [58] set out a helpful summary of guiding principles. In the interests of brevity, I do not propose to repeat them all in this judgment; suffice it to state that I have considered and gratefully accept such guidance.

39. I should however mention specifically three principles highlighted in Birdi v Price (loc cit, at [58]). The first is that the burden of proof lies on the bankrupt to establish that a particular chattel falls within the exception. The second is that the test is one of necessity and not of convenience or desirability. The third is that to qualify, the tools in question must be used personally 'by' the bankrupt; which in context requires physical use of the chattel in question by the bankrupt.

40. The parties have achieved some common ground on the issue whether given assets in existence at the date of the bankruptcy order vested in the Trustee or were exempt, but have not agreed values. The issue of value is not a matter I am invited to determine in the context of this application.

41. I set out below my conclusions on the issue whether given assets in existence at the date of the bankruptcy order vested in the trustee or were exempt under s.283(2)(a). In the interests of brevity, I shall use the descriptions employed at paragraph 8 of the Trustee's skeleton argument when considering this issue and shall indicate where the parties have agreed a given item.

(1) Cash at bank in business account: it is agreed that this forms part of the bankruptcy estate;

(2) Book debts and WIP: it is agreed that these form part of the bankruptcy estate;

(3) Customer contracts: on the evidence before me, these form part of the bankruptcy estate, regardless of whether they were written or oral. Insofar as any of the contracts were 'spot' contracts, I accept the Trustee's submission that they form part of 'goodwill';

(4) Contracts with staff and contracts with suppliers: on the evidence before me, I conclude that these are an element of goodwill and form part of the bankruptcy estate;

(5) Customer lists/database: on the evidence before me, I conclude that these are an element of goodwill and form part of the bankruptcy estate;

(6) Cleaning equipment of note: it is common ground that these items of equipment all qualify as tools of the trade save for 1 buffer machine and 10 Henry vacuum cleaners, which form part of the bankruptcy estate;

(7) Two vehicles: on the evidence before me, I conclude that the Ford Transit van registration DA53 VTV is exempt property as a tool of the trade. In closing submissions it was rightly conceded that the Vauxhall Corsa van registration KX03 ZGV vests in the bankruptcy estate. The Respondent had not adduced evidence establishing on a balance of probabilities that two vehicles were 'necessary' for his 'personal' use;

(8) Stock: This is of minimal value (less than £100). The Respondent has not adduced evidence establishing on a balance of probabilities that these were tools of the trade. On the evidence before me I conclude that the stock formed part of the bankruptcy estate;

(9) Goodwill: It is common ground that this vests in the bankruptcy estate, but the parties are in dispute as to whether it had any value.

Issue 2: Goodwill

42. The next issue I am asked to address is whether the business had any value capable of being realised.

43. In IRC v Muller & Co Margarine Ltd (1901) AC 217 at pp 223-224, The House of Lords addressed the matter thus:

'What is goodwill? It is a thing very easy to describe very difficult to define. It is the benefits and disadvantage of the good name, reputation and connection of a business.

It is the attractive force which brings in custom. It is the one good thing which distinguishes an old-fashioned business from a new business at its first start. '

44. The goodwill in a business will vest in a trustee in bankruptcy. The bankrupt can be required by his trustee to join in the assignment of the goodwill and can be restrained from using the former trade name and from representing that he is carrying on the same business as previously. The bankrupt cannot be restrained from carrying on in his own name a similar business, from soliciting customers of the old business, or from competing with it: Muir Hunter at 3-169; Walker v Mottram (1881) 19 Ch D 355.

45. The Respondent accepts that the Trustee had the right at the outset of the bankruptcy to try to realise the value of a cleaning business called 'Anglesey Contract Cleaning'. He claims however that the goodwill was entirely dependent upon him, had no independent value and was barely profitable.

46. On the evidence before me, the goodwill of the business plainly had realisable value. I so find. The business had been established for over 20 years, had numerous customers (including local authorities) and, importantly, repeat business. Its reach extended beyond Anglesey itself. Whilst its profits may have been overstated in the run-up to the bankruptcy order as a result of the Respondent's unconventional accounting methods, it was nonetheless a profitable business as at the date of bankruptcy, as was conceded in submissions. The Respondent himself clearly considered the reputation of the business to be of some value, having (on his own admission) set up a company, ACC North Wales Ltd, using a name which reflected that of the business; 'ACC' being a trading style of 'Anglesey Contract Cleaning'. He also told at least one customer that he was setting up a limited company but that the business was one and the same; again, there would be little point in seeking to reassure customers in this way unless the Respondent considered the reputation of the business to be of value. Whilst there may have been a relatively limited market for the business, I am satisfied that there was one. If anything, the goodwill value of the business was higher in bankruptcy, as the business would be sold free of prior liabilities. A sale back to the bankrupt was perfectly permissible (pursuant to Schedule 5, Part 2, Paragraph 9 IA 1986) and would have been the obvious choice.

47. For all these reasons, whilst I am not asked to determine the value of the goodwill as at the date of the bankruptcy, I am satisfied that the business had a goodwill value at that date which was capable of being realised. I so find.

Issues 3-6: Trading and Vires

48. I shall deal with issues (3) to (6) together.

49. The powers of a trustee in bankruptcy to trade a business are governed by section 314 IA 1986, which in turn cross refers to Schedule 5. Section 314 was amended with effect from 25 May 2015.

50. Prior to 25 May 2015, s.314(2) provided as follows:

'With the permission of the creditors committee or the court, the trustee may appoint the bankrupt –

(a) To superintend the management of his estate or any part of it,

(b) To carry on his business (if any) for the benefit of his creditors, or

c) In any other respect to assist in administering the estate in such manner and on such terms as the trustee may direct.'

51. Section 302 gives the Secretary of State the power to exercise the function of the creditors committee when no committee is established, as was the case here.

52. Since 25 May 2015, there has been no requirement in s.314(2) for a trustee to obtain permission from the creditors committee or the court to appoint the bankrupt.

53. The editors of Muir Hunter comment on s.314(2) as follows:

> 'The carrying on of the bankrupt's business falls within para 1 of Sch 5. This subsection enables the trustee (with permission) to employ the bankrupt to assist therein. This was a power conferred by s57 of the Act of 1914 which similarly provided that the trustee's power to appoint the bankrupt was to be 'on such terms as the trustee may direct' thereby enabling remuneration or an allowance to be made to the bankrupt. In s.58 of the Act of 1914 the trustee also had the power to make an allowance to the bankrupt out of his property for the support of the bankrupt and his family. This power has not been reproduced in the IA 1986, presumably because general social welfare is now readily available for those in need.'

54. Before 25 May 2015, s.314(1) provided that the trustee could exercise any of the powers specified in Parts 1 and 2 of Schedule 5, with the powers in Part 1 requiring the permission of the creditors' committee or the court.

55. Paragraph 1 of Schedule 5 conferred the following power:

'Power to carry on any business of the bankrupt so far as may be necessary for winding it up beneficially and so far as the trustee is able to do so without contravening any requirement imposed by or under any enactment'

56. Since 25 May 2015, all the powers in Parts 1 and 2 of Schedule 5 have been exercisable without the need to obtain sanction.

57. An issue raised in submissions before me is whether s.314(2)(b) is a subset of Paragraph 1 of Schedule 5 or a free-standing power. In my judgment, s.314(2)(b) must be read subject to Part 1 of Schedule 5. The trustee has the power to run the bankrupt's business in order to wind it up beneficially and by virtue of s.314(2)(b) he has the ability to appoint the bankrupt to assist in doing so. In this regard, I concur with the views expressed by the editors of Sealy & Milman at p 437 and Muir Hunter at para 13-1051.

58. There is little authority on what is meant by the phrase 'winding it up beneficially', as employed in Schedule 5 para 1. I accept that the term 'beneficially' in context must include 'for the benefit of the creditors as a whole'. Benefit for the creditors as a whole, however, is not of itself a sufficient condition: see for example Re Batey (1881) 17 Ch D 35, addressed below.

59. I am told that there is no post-1986 Act authority on the scope of these provisions. That said, as noted by Lord Neuberger in In re Lehman Bros International (Europe) (No 4) [2017] UKSC 38 at [11] – [12], whilst it cannot be assumed that judicial decisions, even at the highest level, relating to previous insolvency legislation necessarily hold good, where the wording of a provision in the 1986 legislation has not changed from that of a provision in previous legislation, then, at least prima facie, it may normally be assumed that the effect of the provision was intended to be unaltered.

60. I turn then to consider caselaw under predecessors to Schedule 5; s.25(2) of the Bankruptcy Act 1869 and s.56(1) of the Bankruptcy Act 1914.

61. Section 25 of the Bankruptcy Act 1869 provided:

'Subject to the provisions of this Act the trustee shall have power…

(2) to carry on the business of the bankrupt so far as may be necessary for the beneficial winding-up of the same…

(6) to sell all the property of the bankrupt (including the goodwill of the business, if any, and the book debts due or growing due to the bankrupt)….'.

62. Section 26 of the Bankruptcy Act 1869 also provided:

'The trustee may appoint the bankrupt himself to … carry on the trade of the bankrupt … for the benefit of the creditors … in such manner and on such terms as the creditors direct.'

63. In Re Sneezum ex parte Davis (1876) 3 Ch D 463, James LJ (at p 473) concluded that s.25(2) of the 1869 Act

> '…does not give the trustee the power to carry on any contracts of the bankrupt, whatever be their nature, for any time, but only to carry on the business of the bankrupt so far as may be necessary for the beneficial winding-up of the same. That is only a temporary provision until the trustee can dispose of the good-will.'

64. As put by Mellish LJ in Re Sneezum at p475:

> 'They [the words in section 25] merely say that the trustee 'may' carry on the business as far as is necessary for the purpose of a beneficial winding up, and they do not, in my opinion, give the trustee any greater power than assignees in bankruptcy had previously to the passing of this Act. The

> words do not give the trustee power to enter into any new business, but only power to carry on the existing business so far as may be necessary for the beneficial winding up. If there is any beneficial contract existing he may carry it out, but, in my opinion, that is not sufficient so as to change the law as to make the trustee liable, either personally or out of the assets, to pay damages if the contract is subsequently broken.'

65. In Re Batey (1881) 17 Ch D 35, the court held that, in authorising the trustees to carry on the bankrupt's ginger beer manufacturing business indefinitely, the creditors had acted ultra vires the powers conferred upon them by the Bankruptcy Act 1869. In that case, the creditors had not contemplated a sale of the business at all; they were merely authorising its continuance to make a profit for themselves, as suppliers of the raw materials to the business in question.

66. As put by James LJ at p39:

> 'The Act evidently contemplates … a carrying on of the business only for the purpose of its beneficial winding-up, not because the creditors may think that the business will be a very profitable one, and that the longer it is carried on the better it will be, and that they will make a profit from it… They had not contemplated a sale of it, but they thought they could make more profit by carrying it on'.

67. James LJ went on to state (at pp39-40):

> 'So far as the resolution authorized the trustees to carry on the business for twelve months, it might very well be said that it was in spirit a compliance with the Act, as it might well have been understood as passed with a view to the beneficial winding-up of the business. Twelve months was a long time, but not necessarily an unreasonable time….'

68. At p.42, Cotton LJ was at pains to emphasize that:

> 'The power is given simply for the purpose of the beneficial winding-up of the business, not the estate. Then sub-sect. 6 empowers the trustee "to sell all the property of the bankrupt, including the goodwill of the business, if any, and the book debts due or growing due to the bankrupt", showing that the intention is that, subject to the qualification supplied by [s.25(2)], where the bankrupt is carrying on a business, his property shall at once be realised, and that as soon as possible there shall be a sale of the business and goodwill.'

69. On the facts, Cotton LJ concluded (at p.43):

> '[the creditors'] object, in my opinion, was to obtain a profit by carrying on the business during the thirsty season of the year. That, however, is not a purpose which is justified by the Act.'

70. It will be seen that the court stressed the temporary nature of the power to carry on trading. Two of the three lord justices considered that a period of 12 months trading of the business in question would not have been unreasonable for the purpose of winding it up beneficially.

71. Section 56 of the Bankruptcy Act 1914, so far as material, was in similar terms. Section 56 provided:

'The trustee may, with the permission of the committee of inspection…

(1) Carry on the business of the bankrupt, so far as may be necessary for the beneficial winding up of the same,,,'

72. Section 57 of the Bankruptcy Act 1914 provided:

'The trustee, with the permission of the committee of inspection, may appoint the bankrupt himself to … carry on the trade (if any) of the bankrupt for the benefit of his creditors…. in such manner and on such terms as the trustee may direct.'

73. In Clark v Smith [1940] 1 KB 126, the trustee, with the approval of the committee of inspection, had agreed with a third party that he would carry on the business of the bankrupt in consideration of a guarantee against loss provided by the third party. At first instance, it was found that one of the purposes of the contract was to carry on the business for the benefit of the bankrupt. As put by Charles J (quoted at p132-3), the trustee was 'influenced and biased in the action which he took in carrying on this business by, as he has sworn to me, his desire to help [the bankrupt] in his difficulties'. At p134, Slesser LJ considered the terms of the resolution of the committee of inspection, noting that by its terms, the business 'is not to be carried on for such time as would be necessary for the purpose of a beneficial winding-up – it is to be carried on for the present'. He concluded that the conduct of the trustee in carrying on the business was contrary to the provisions of s.56(1) BA 1914.

74. The language of Schedule 5 of the 1986 Act, so far as material in this case, reflects that of its predecessors. That being so, in my judgment the cases of Re Sneezum, Re Batey and Clark v Smith remain instructive on the issue of the scope of the powers under consideration in this application.

75. In my judgment, Schedule 5 does not authorise a trustee in bankruptcy to carry on a bankrupt's business, with or without the assistance of the bankrupt by way of appointment under s.314(2), indefinitely. The carrying on of the bankrupt's business is only authorised 'so far as may be necessary for winding it up beneficially'. The 'it' in context, must be the business. In this regard I note that a similar conclusion was reached in Re Batey per Cotton LJ at p.42:

'The power is given simply for the purpose of the beneficial winding-up of the business, not the estate'

76. The most obvious examples of continued trading of a business for the purpose of winding it up beneficially are (1) where there is outstanding 'work in progress' and the most effective way of collecting in book debts is to complete the same, and (2) where continued trading is with a view to a sale of the goodwill at the best price

reasonably obtainable. In a similar vein, see Re Sneezum per James and Mellish LJJ at pp 473 and 475 respectively.

77. Ms Rogers submitted that the court should take a wider view of such powers in the light of the 'rescue culture'. In my judgment the rescue culture cannot be prayed in aid as a means of ignoring the clear wording of Schedule 5. Where long-term or indefinite trading of a bankrupt's business is envisaged, which is not for the purpose of winding it up beneficially, this should be achieved either by the bankrupt exiting the bankruptcy via a trading IVA, or by a sale of the goodwill of the business to a bankrupt or a third party, on deferred consideration terms if appropriate.

78. The Respondent raised a further point on vires. He maintained that the Trustee was only granted by the Secretary of State power to trade the business himself, and not power to appoint the Respondent to trade it under s.314(2)(b). In this regard reference was made to the wording of the sanction itself, which provided:

'I hereby grant sanction for the trustee to continue the business of the bankrupt, trading as a cleaning contractor… for the period of 24 October 2014 to 23 October 2015, in order that he may maximise realisations for the benefit of creditors.'

79. In my judgment there is little in this point. In reality, no trustee is in literal terms likely to be trading a bankrupt's business personally. The sanction granted must be read constructively and in context. The sanction was issued on 24 October 2014 as a matter of urgency, within 30 minutes of the Trustee's last response to enquiries raised on behalf of the Secretary of State about his application: a response in which he had made clear that the Respondent would be actively involved in the day to day running of the business. It is authority to trade under Schedule 5 para 1. Read constructively, in my judgment the sanction granted by the Secretary of State to carry on trading must be read as including sanction to appoint the bankrupt to assist in that process.

80. Since 25 May 2015, all the powers in Schedule 5 have been exercisable without the need for sanction, albeit the power to carry on any business of the bankrupt remains subject to the requirement that it be 'necessary for winding it up beneficially.'

81. Against that backdrop, I turn to consider the facts.

Who was trading?

82. The Respondent maintains that since the date of bankruptcy, he has been trading the business in his own right. As put at paragraph 40 of Mr Fennell's skeleton argument: 'The reality is that R has carried on the trading since the bankruptcy and A has not'.

83. The factors relied upon in support of this contention may be summarised as follows:

(1) The business is not a separate asset. The assets making up the business are a combination of tangible assets, book debts, work in progress, the benefit of uncompleted contracts, and goodwill. Whilst the Respondent accepts that the Trustee has 'allowed' the Respondent to 'use those assets', he maintains that 'it does not follow' that he 'has to account for all monies generated by their use, less the costs of the business and a sum needed to meet his reasonable domestic needs': Respondent's skeleton argument, para 39.

(2) At the outset, the Trustee told the Respondent to send a communication to all customers, saying: "I am writing to let you know that following my recent unfortunate bankruptcy, my trustee has given permission for me to re-launch my business under his supervision while we sort out how I am going to get my affairs back into order".

(3) The Respondent, and not the Trustee, entered into contracts with customers and invoiced them as "EA Robinson trading as Anglesey Contract Cleaning", with payments being made into the trading accounts maintained by the Trustee.

(4) The Trustee did not employ the employees; the Respondent employed them and told the Trustee how much to pay them every month, and how much to pay HMRC in respect of PAYE/NIC.

(5) The Trustee did not account to HMRC for VAT relating to the business in his own name; the Respondent was registered trader for VAT purposes.

(6) The Trustee did not account to HMRC for any income tax due from the trading, maintaining that it was the Respondent's income for tax purposes, which the Respondent then accounted for by self-assessment.

(7) The Trustee instructed the Respondent to disclose his own name on any business stationery, including websites.

(8) The Trustee did not take out employers' liability or third-party insurance in relation to the business, instead relying on the Respondent's insurance.

(9) Employees came and went between 2014 and 2019 and the Trustee usually took no part in the recruitment process. The Respondent would tell the Trustee that he had hired someone after doing so. The only exception appears to have been in 2016, when the Respondent took on a substantial new contract and the Trustee expressed concern that he might become liable under TUPE.

(10) The Respondent renewed contracts with existing customers and took on new customers between 2014 and 2019.

84. The Trustee's position is that (1) he was running the business, having obtained sanction for that very purpose and that (2) he appointed the Respondent to assist in the process of running the business. He maintains that, viewed objectively, the section 314(2)(b) power has been used, even if the sanction granted by the Secretary of State did not contain express reference to that power. He maintains that the extensive correspondence between the parties clearly demonstrates that it was the Trustee was trading the business, using the Respondent as his appointee.

Discussion and Conclusions

85. On the evidence which I have heard and read, I am satisfied that at all material times from the date of his appointment, the Trustee was trading the business, using the Respondent as his appointee pursuant to section 314(2)(b) IA 1986. I so find.

86. Addressing the specific points summarised at paragraph 83 above: with regard to (1), I accept that the mere fact that a trustee has 'allowed' a sole trader bankrupt to use the

assets of his sole trader business post-bankruptcy does not of itself lead inexorably to the conclusion that the trustee is trading the business using the bankrupt as his appointee pursuant to s.314(2)(b) IA 1986. The evidence, however, has to be considered as a whole. On the evidence as a whole, the position is clear.

87. Points 2, 3, 4, 7, 9 and 10 are in my judgment entirely consistent with the Respondent acting as appointee under s.314(2)(b).

88. Points 5 and 6 are ultimately red herrings.

89. With regard to point 5: on the evidence before me, I am satisfied that the Respondent's income was dealt with for tax purposes by way of self-assessment on the advice of HMRC; I so find. The trading income generated by the business was at all material times reflected in the receipts and payments accounts for the bankruptcy. Any tax payable in respect of the Respondent's self-assessment tax returns was paid by the Trustee out of the trading income.

90. With regard to point 6: as a corollary of point 5, it is entirely unsurprising that the Respondent declared the VAT as well. From the evidence before me it is clear (and I so find) that the Trustee had to intervene with HMRC to ensure that the Respondent enjoyed the use of a VAT registration number post-bankruptcy for this very purpose. The Trustee explained to HMRC that 'the business continues to trade under my supervision'. It was only as a result of his intervention that HMRC permitted the Respondent to use a VAT registration number post-bankruptcy. Again, any VAT payable was paid by the Trustee out of trading income of the business.

91. With regard to point 8; on the evidence before me I am satisfied that at the outset of the bankruptcy, the Trustee expressly directed the Respondent to ensure that his name was included on the policy of any insurance taken out in respect of the business. The fact that the Respondent may not have complied with this direction in all respects is neither here nor there; the direction was given.

92. The suggestion that the Respondent was trading in his own right was unsustainable on the evidence. The contemporaneous correspondence spoke for itself. Whilst the Respondent dealt with the day to day operation of the business and the Trustee for the most part maintained a 'light touch' supervisory approach, ultimately it was the Trustee who was in control. From the outset, the Respondent accounted to the Trustee for trading income. Payments were only made out of that trading income with the consent of the Trustee. The Trustee called for ongoing accounting information and the Respondent would provide it.

93. The Respondent sought to explain away these arrangements, saying that he was simply seeking to comply with his duties under the Insolvency Act 1986 to cooperate with his Trustee. Reading the attendance notes and correspondence in evidence as a whole, this explanation simply does not ring true and I reject it. The Respondent knew full well what arrangements would be required if the business was to continue trading and he welcomed those arrangements.

94. The Trustee told the Respondent that he was seeking permission to trade in their first conversation on 23 October 2014. The Trustee's telephone attendance note of that

conversation, the accuracy of which was not challenged and which I accept, provided as follows (with emphasis added):

> 'Mr Robinson telephoned as he is very anxious about his business collapsing and what can I do to prevent it.
>
> I told him that the Official Receiver had organised an urgent appointment for me so that I could look into matters quickly and based on the information which he had provided this should be an annulment matter and that I had already applied to the insolvency service for a sanction to continue the business so I would be ready if we could do so.
>
> *I explained that **if** we were to continue **it would have to be done on the basis that it was under my control** and the surplus on the business would be used to pay off creditors in due course. **After that** he would be able to **have his business back** and carry on as before. All this was assuming that the business was profitable which we need to check out.*
>
> *Mr Robinson seemed very pleased that this was possible and said that this is what he would like to do*. I said I would write to him as soon as possible to confirm how all this would move ahead and [Mr Davis of the Trustee's firm] would come and see him shortly'.

95. It is perfectly clear from the foregoing exchange that the Respondent would not be trading in his own right.

96. At a later stage, having considered the accounting information initially provided, the Trustee wrote to the Respondent by email dated 29 October 2014, saying (with emphasis added):

"this is probably the mail you have been waiting for. I am happy in principle for you to recommence trading ***under the aegis of the bankruptcy***. It will not surprise you to know that there is quite a lot to do to bring matters into order but you appear to be able to deal with your own administration and given that part of the object of the exercise is to work towards getting you your annulment in due course, the more of the tasks you can undertake the better as this will help in keeping my firm's costs down."

97. Again, this email made clear that if trading were to recommence, it would be 'under the aegis of the bankruptcy'.

98. A few months later, by email dated 22 April 2015, the Trustee wrote to the Respondent stating (with emphasis added) "I think the moment has come to talk about where all this is going … The issue is how are we going to get you out of bankruptcy ***and back to trading in your own right***?

99. Notably, the Respondent did not respond to this email by stating that he was already trading in his own right.

100. There were numerous other examples of such references in the correspondence in evidence. In the interests of brevity, I shall not list them all.

101. The suggestion that the Respondent was trading in his own right after the bankruptcy order made no sense. There would have been no point in the Trustee seeking, as a matter of urgency, sanction to trade, if the Respondent's account of events was correct. As at the date of bankruptcy, save for his own personal tools of trade, the Respondent had no assets with which to trade. Post-bankruptcy trading was only made possible by using, with the permission of the Trustee, the equipment, book debts, WIP and other assets of the bankruptcy estate which had vested in the Trustee. As the Trustee explained in oral evidence, the book debts and money generated by WIP had to be 'fed back' into the business, in order to keep it going. Moreover, but for the intervention of the Trustee, the Respondent would have no VAT registration number to trade under. As a bankrupt, he would have no business bank account available to him either (indeed, the Respondent confirmed that, even as at 2018, he was refused a business bank account). It was the Trustee who applied for permission to open a bank account for the business, arranged the opening of that account and sought renewed permission each year to keep it open. As a bankrupt, the Respondent could not obtain credit of more than £500. Without the blessing of his Trustee, the Respondent could not have used any trading style of the business either, as this vested in the Trustee as part of the bankruptcy estate.

102. I also remind myself that at no time prior to instructing solicitors in 2017 did the Respondent suggest that he was trading the business in his own right.

103. Overall, on the evidence which I have heard and read, I am satisfied that at all material times from the date of his appointment as Trustee until 31 July 2019, it was the Trustee trading the business, with the day to day assistance of the Respondent as his appointee under s.314(2). I am further satisfied that the Respondent was at all material times aware that his continued involvement in the business was on behalf of the bankruptcy estate under the supervision of the Trustee and not in his own right. I so find.

Was the trading for authorised purposes?

104. I turn next to the question whether the Trustee exercised his power to trade for purposes permitted by Schedule 5.

105. In his application for sanction sent to the Insolvency Service on 22 October 2014, the Trustee addressed the estimated benefit to the estate from continued trading as follows: 'Realise value of business by sale back to the bankrupt and realisation of substantial book debts'. His stated 'reason for the continuance of trading', which was 'to maximise realisations', must be read in that context. According to the sanction application form, therefore, his initial aim was to maximise realisations by trading on (1) to realise the book debts and (2) to achieve a sale back to the Respondent.

106. A reasonable period of trading (which in the context of a business of this size would in my judgment be up to twelve months) for the purpose expressed in the application for sanction would fall comfortably within Schedule 5.

107. In the event, however, whilst I am satisfied that the Trustee did not intentionally misrepresent the purpose of continued trading in his application for sanction, it is clear (and I so find) that he rapidly lost sight of that purpose and pursued others instead.

108. From the evidence which I have heard and read it is clear (and I so find) that

(1) from the grant of sanction on 24 October 2014 until 10 October 2015, the Trustee continued trading the business with a view to the Respondent achieving either a s.282(1)(b) annulment or an IVA;

(2) from the date of the Respondent's automatic discharge on 10 October 2015 until June 2017, the Trustee continued trading the business initially with a view to the Respondent achieving either an informal IVA or a s.282(1)(b) annulment and latterly (having been advised that an informal IVA was not feasible) with a view simply to a s.282(1)(b) annulment;

(3) the Trustee did not trade with a view to achieving a sale back to the Respondent until June 2017.

109. By his letter to the Respondent dated 4 June 2017, which I am satisfied is an accurate account of events, the Trustee described a 'sale-back' as a 'new strategy'. The letter of 4 June 2017 provided inter alia as follows:

> 'As you know, your business known as Anglesey Cleaning vests in the bankruptcy estate and since the bankruptcy I have effectively been trading it with you acting as special manager…'

110. Pausing there, the Respondent was plainly not a 'special manager' in the technical sense. The Trustee has since corrected this error of terminology. The Respondent was an appointee under s.314(2). To continue with the letter (with emphasis added):

> 'I have endeavoured to allow you a free reign and have interfered as little as I can, whilst at the same time ensuring as far as possible that the business continued successfully and to this end I have continued to monitor it and maintain a level of involvement. ***You will recall that the object of the exercise was to "trade out" and ultimately pay off your creditors and obtain an annulment of your bankruptcy. We even discussed the possibility of exiting the bankruptcy by entering into an individual voluntary arrangement but unfortunately you appeared not to be ready for that and once you received your discharge, that was no longer a possibility***.

We have therefore been trading on through the bankruptcy which has meant that any funds raised to pay costs and creditors are subject to the prior payment of valorem duty or "Secretary of State" fee. At 15% of realisations this is a tax which really is unsustainable in a long-term trade out position. Unfortunately, at the beginning of the bankruptcy we believed that the business was far more profitable than it turned out to be because of the errors you had made with regard to your tax assessments. It really did have a serious knock-on effect and it was only when we examined the HMRC claim in detail that the dreadful truth emerged.

I am now of the opinion, based on trading at your current level, that any attempt to trade out within the bankruptcy would in fact take many years, if indeed it could be achieved at all. Robert Freestone concurs with me in this view. ***As a result, a new strategy is needed to decide what exit which we should pursue to bring about an ultimate release of your business from the bankruptcy process***.

The trading exercise has not been valueless, however. We have achieved a position where you are up-to-date with your VAT, your PAYE and your self-assessment tax. It is extremely important that this remains the case.

It is clear that the business is profitable and does have a value, especially if you are relieved of the costs of bankruptcy which are not insubstantial. It is also likely that if it were put on the market then you would be the only real buyer, although not impossible. By the same token, the business is clearly of immense value to you and your family and indeed fills a substantial need for your customers and your staff as well. You are currently 53 years of age and accordingly have plenty of working lifetime left ahead of you and I would not wish to deprive you of the opportunity of continuing to make the best of the business you created.

The answer must be for you to buy the business off me as trustee. In that respect, we cannot ignore that there are significant assets. Your fixed assets are not particularly substantial - various vehicles which are long past their prime but you do have a very substantial list of book debts. In April of this year they totalled just short of £40,000. Those debts of course belong to the bankruptcy estate. In addition to that value, I believe there is a value to the goodwill at between £20,000 and £30,000. Taking into account your share of the equity in the property, possibly £80,000 or more, I believe this would represent a fair return to your estate and provide the creditors with a reasonable dividend on their claims.

> Obviously raising the money is the issue which needs resolving. In the right climate I think you should be able to raise a further loan on the property. On the assumption that your wife is willing to participate in any arrangements, perhaps by acquiring your share of the house, this could also provide a contribution to the cost of purchase of the business and the balance would have to be paid on a monthly basis out of business turnover. This is not as far-fetched as it might seem because of course they would be the saving of the costs of bankruptcy.
>
> I have no doubt that you will find this somewhat confusing at first sight and you will need some time to assimilate the content. It does seem to me that it represents the best way forward and I believe that it also represents a "fair deal" in terms of how much you should be required to repay your creditors in the light of current circumstances.
>
> You should expect to receive the possession proceedings papers shortly; I do not want you to be taken by surprise and we therefore need to resolve the way forward in general as quickly as we can. If a deal can be reached then hopefully the sale of your home can be avoided.
>
> Please let me know if you have any questions; I think that probably we shall need to meet once you have thought about it so we can finalise arrangements.'

111. That the sale back was a 'change of tack' in 2017 is also confirmed by the Trustee's Progress Report for the year ending 19 October 2017, which at paragraph 8 provided (with emphasis added):

> 'trading is producing results, albeit slowly… The trustee has concluded that it would be too onerous and impracticable for the debtor to trade out completely and is therefore ***now*** looking at the possibility of selling the business back to the debtor for a reasonable consideration.'

112. By June 2017, therefore, it is clear that the Trustee had decided upon a sale of goodwill of the Business back to the Respondent as a 'new strategy'. This replaced the strategy of 'trading out of bankruptcy' via an informal IVA or a s.282(1)(b) annulment, which in turn had replaced the dual strategy in place, prior to automatic discharge, of a formal IVA or a s282(1)(b) annulment.

113. The question is whether any of the earlier strategies prior to June 2017 fell within the purposes permitted by Schedule 5. In my judgment they did not. It is no part of a trustee's function to carry on trading the business of a bankrupt in the hope that it will assist the bankrupt in achieving a 282(1)(b) annulment or an exit via an IVA. Whilst on the evidence which I have heard and read, I am satisfied that at all material times the Trustee acted honestly, in good faith, and with the very best of intentions, in

trading in bankruptcy with a view to the Respondent achieving an IVA (formal or informal) or a s.282(1)(b) annulment, he acted for a purpose other than that permitted by Schedule 5. I so find.

114. The question is with what consequence. In Clark v Smith 1940 1 KB 126, the Court of Appeal agreed with the judge's finding at first instance that the business was being carried on for a purpose other than in accordance with s.56 of the Bankruptcy Act 1914. Slesser LJ then asked (at p134): 'But what is the consequence of that?'. He concluded that it was only persons interested in the bankruptcy estate who could complain about a business being operated otherwise than in accordance with the relevant Act. The reference in Re Batey to given acts being 'ultra vires' was held to relate only to matters as between the trustee and persons interested in the disposal of the estate.

115. Agreeing, Mackinnon LJ added (at p138) that, in giving sanction, the creditors committee and the trustee had made 'a venial and intelligible mistake as to an obscure branch of the law, but without any turpitude or illegality', adding:

> 'I am at a loss to understand why, because as between the trustee and the creditors, one of the creditors might object to the carrying on of this business by the trustee, that should afford Mrs Smith [the guarantor] any defence whatever to an action on the plain contract into which she had entered with the trustee.'

116. Mackinnon LJ went on to refer by way of analogy to two cases involving claims brought by a trustee without the sanction of the court to bring proceedings, as was then required, concluding (at p.138):

> 'The courts there decided that as between the trustee and the creditors, it might be that he had acted irregularly, but that that did not afford any defence to the person who had made a clear contract with the trustee.'

117. Applying such reasoning to present facts, it is in my judgment clear that whilst the Trustee from October 2014 to June 2017 traded the business for purposes not permitted by Schedule 5, that does not render his carrying on of the business over that period void as being ultra vires. As put by Slesser LJ in Clark v Smith at p136:

> 'as against the world, the carrying on of the business by the trustee can create legal relations between him and third parties, either as debtor or creditor, incurred in the carrying on of the business, notwithstanding that it is carried on otherwise than solely for the beneficial winding up of the estate….
>
> … I do not think it can be said that it is void as being ultra vires, because the trustee is in my opinion competent to carry on the business and to create legal liabilities as between himself and third persons with whom he deals in carrying on the business, whether he does or does not do so for the purpose of the beneficial winding-up of the estate'.

118. As confirmed by Slesser LJ in Clark v Smith, the reference in Re Batey to given acts being 'ultra vires' relates only 'to matters as between persons interested in the disposal of the estate'. In the case of an insolvent estate, the persons interested are the creditors; absent a surplus, the bankrupt himself has no interest. In the present case, there is no surplus.

Conclusions on issues (3) to (6)

119. To summarise my conclusions on issues 3 to 6:

(1) Dealing first with issue (3): On the evidence which I have heard and read, I am satisfied that at all material times from the date of sanction on 24 October to 31 July 2019, the Trustee traded the business with the assistance of the Respondent as his appointee under s.314(2) IA 1986.

(2) With regard to issue (4), it follows from my finding on issue (3) that the trading income held in the Insolvency Services Account belongs to the bankruptcy estate.

(3) With regard to issue (5): under the sanction, Schedule 5 and s.314(2), the Trustee had power to continue to trade the business (and to appoint the Respondent under s.314(2) to assist in such continued trading) for the purposes of a beneficial winding up of the business (including a sale of the goodwill of the business for the benefit of the creditors as a whole). As confirmed by Re Clark, however, the Trustee was also competent to carry on the business and to create legal liabilities as between himself and third persons in carrying on the business, whether or not he did so for the purpose of a beneficial winding up of the business.

(4) With regard to issue (6): from 24 October 2014 to 4 June 2017, the Trustee traded the business for purposes which were not permitted under Schedule 5 or the sanction. This did not render his actions void as being ultra vires however: Re Clark. From 4 June 2017 to 31 July 2019, the Trustee traded the business for a purpose which was permitted under Schedule 5, namely, the sale of the assets (including the goodwill) of the business.

Issues 7, 8 and 9

120. With regard to issue 7: on the evidence which I have heard and read, I am satisfied that on or by 29 October 2014, the Trustee and the Respondent had agreed that the Trustee would continue trading the business, with the day to day assistance of the Respondent as his appointee, on behalf of the bankruptcy estate. The continued trading agreed by the parties in October 2014 was for an indefinite period (implicitly terminable by either party), with a view to the Respondent achieving an exit from the bankruptcy via an IVA or an annulment under s.282(1)(b). The consensual arrangement reached is not set out in any one document but is evidenced by, inter alia (1) the Trustee's file note of his conversation with the Respondent on 23 October 2014 (2) the Trustee's letter to the Respondent dated 26 October 2014 (3) the Respondent's email to the Trustee dated 28 October 2014 (4) the Trustee's email to the Respondent dated 28 October 2014 (5) the Respondent's email to the Trustee dated 29 October 2014 (6) the Trustee's email to the Respondent dated 29 October

2014 (7) the Respondent's email to the Trustee dated 30 October 2014 (8) the parties' conduct and correspondence thereafter.

121. As previously indicated, I reject the Respondent's evidence that he was 'simply following instructions'. Prior to the Trustee's appointment, the OR had told the Respondent to cease trading; despite that clear instruction, the Respondent had continued to trade. This is a clear example of the Respondent exercising his own judgment, rather than blindly following instructions.

122. From the Respondent's first telephone conversation with the Trustee on 23 October 2014, the attendance note of which has been quoted previously in this judgment, it was clear that the Respondent was keen to ensure that his business survived. He was a very willing participant in the trading arrangements which he agreed with the Trustee in October 2014. From the contemporaneous correspondence in evidence, it is also clear that the Respondent was content for those arrangements to continue long after the Trustee began expressing concerns and actively pressing for an exit strategy to be agreed.

123. Even after the Trustee had by his letter of 4 June 2017 proposed that the Respondent buy back the business from him, and had met with the Respondent and his wife on 29 August 2017 to explain the situation face to face, the Respondent followed up the meeting with an email stating that he still wished to pay off his creditors rather than buy back the business. Again, such conduct bears no resemblance to the picture which the Respondent sought to paint, of having blindly followed the Trustee's instructions throughout, thinking that it was his duty to do so. He was exercising independent judgment throughout and, until the summer of 2017, was content for the trading arrangements initially agreed with his Trustee to continue indefinitely. I so find.

124. The consensual arrangement came to an end in 2017 when the Respondent instructed solicitors. Thereafter, a series of arrangements have been agreed between the parties' representatives pending the determination of this application.

125. With regard to issue 8: in the light of my conclusions on issue 3, the question whether the consensual arrangements in place between the Trustee and the Respondent until 2017 were contractually binding is ultimately academic; the contract argument in the application notice was put forward as an alternative to trading under s.314(2). I would add that in any event, the arrangements agreed were terminable by either party at any time.

126. With regard to issue 9: the issue of vires has already been explored. As this is an insolvent estate, the Respondent is not a person interested in the same.

Issue 10

127. In my judgment the Respondent is not 'estopped' from contending that the Trustee acted outside his powers. For reasons previously given, the correct analysis is that he is not a person interested in the estate.

128. In my judgment the Respondent is not 'estopped' from denying the existence of a contract. For the reasons previously given however it is clear on the evidence that he agreed from the outset to the trading arrangements put in place by the Trustee.

Issues 11 and 12

129. The next question is whether the Trustee has acted in breach of the rule in ex parte James and, if he has, with what result.

130. The rule in Re Condon, Ex parte James (1873-74) LR 9 Ch App 609 has recently been considered by the Court of Appeal in Lehman Brothers Australia Limited (In liquidation) v MacNamara [2020] EWCA Civ 321. In Lehman, the applicant company, which was in liquidation, was an unsecured creditor of the respondent company, which was in administration. The two companies entered into a claim determination deed, pursuant to which the applicant's claim as a creditor was agreed as £23.35m. Due to a clerical error by the respondent's administrators, that figure was deficient by £1.67m, but the deed was executed and the agreed sum duly paid to the applicant before the error was noticed. The administrators acknowledged the error but relied on a release clause in the deed to decline the request of the applicant's liquidators to correct it. The liquidators applied to the court for a direction that the administrators increase the agreed proof of debt by the deficit figure to just over £25m, under either (i) the court's inherent jurisdiction to control the conduct of its officers or (ii) the court's discretion under paragraph 74 of Schedule B1 to the Insolvency Act 1986 to grant relief where an administrator had acted so as to unfairly harm the interests of a creditor. The judge dismissed the application, holding that neither power could be used to prevent the enforcement of contractual terms freely entered into by both parties. Allowing the appeal, the Court of Appeal held, into alia, (1) that it was not a bar to relief under the court's inherent jurisdiction to control the conduct of its officers or under paragraph 74 of schedule B1 that the relief would prevent an administrator from relying on rights under a contract that had been freely entered into by both parties (2) that in exercising its inherent jurisdiction to control the conduct of its officers, the court applied a test of unfairness rather than unconscionability; and that fairness was an objective standard, calling for judgement or evaluation in its application to particular facts (3) that, on the facts of the case, no right-thinking person would think it fair for the administrators to rely on their strict contractual rights and refuse to correct the shared mistake; and that, accordingly, the liquidators were entitled to the direction which they sought, under both the inherent jurisdiction of the court to control the conduct of its officers and under paragraph 74 of schedule B1.

131. As put by David Richards LJ at [35]:

> 'The principle established by the decision of the Court of Appeal in ex p James is that the courts will not permit its officers to act in a way which, although lawful and in accordance with enforceable rights, does not accord with the standards which right-thinking people or, as it may be put, society would think should govern the conduct of the court or its officers. The principle applies to a failure to act, as much as to positive acts: see In re Hall [1907] 1 KB 875, a decision of this court. As a public authority and given its role in society, the court is expected to apply standards to its own conduct which may go beyond their legal rights and duties. A specific example is a sale of property made by the court in accordance

> with its powers: Else v Else (1872) LR 13 Eq 196. Trustees in Bankruptcy, liquidators in compulsory liquidations and administrators are all officers of the courts. … As such, they are acting on behalf of the court and they will accordingly be held to the standards by the court.
>
> [36] That the governing principle is that the court should apply to its officers though standards of conduct that society expects of the court itself is made clear in the authorities: see Ex p James LR 9 Ch App 609, 614; Ex p Simmonds; In re Carmac (1885) 16 QBD 308, 312, per Lord Esher MR; In re Tyler; Ex p Official Receiver [1907] 1 KB 865, per Vaughan Williams LJ at p869, Farwell LJ at p871 and Buckley LJ at p873.'

132. The court applies the standard on an objective basis. As put by David Richards LJ at [28]:

> 'It is not concerned to ask whether the officeholder is consciously proposing to take a course which falls below the standards set by the court. It asks only whether the course proposed would or would not, on an objective basis, meet that standard. As a regulated profession, insolvency practitioners may feel aggrieved at a challenge to their conduct or proposed conduct on this basis and may be tempted to argue that the challenge is an attack on their personal integrity. This would be a misapprehension on their part.'

133. Having reviewed the authorities, David Richards LJ concluded at [68]:

> 'While the formulation of the test in the authorities, involving so many phrases with perhaps different shades of meaning, has something of the quality of dancing on pinheads, resolution of this issue lies in going back to the fundamental principle underlying the jurisdiction. The court will not permit its officers to act in a way that it would be clearly wrong for the court itself to act. That is to be judged by the standard of the right-thinking person, representing the current view of society. If one were to pose the question "would it be proper for the court to act unfairly?", only one answer is possible. It is interesting to note that fairness was introduced by some judges in the cases dealing with Ex p James at a comparatively early stage, but in general "fairness " as a test in substantive, as opposed to procedural, law has grown significantly since many of those cases were decided. Insofar as it involves a broader test than, say, dishonourable, it reflects a development in the standards of conduct to be expected of the court and its officers.'

134. At [69] David Richards LJ went on to confirm that the application of the principle in Ex p James in any case will critically turn on the particular facts of that case.

135. On behalf of the Respondent, Mr Fennell limited the scope of the relief sought by way of application of the rule in ex p James to the period following the third anniversary of the bankruptcy order; that is to say, the period from 10 October 2017 onwards. He sought a direction that all trading income generated by the business from 10 October 2017 onwards be treated as belonging to the Respondent and not to the bankruptcy estate.

136. The reasoning put forward was as follows. Mr Fennell accepted that, absent the trading arrangement, it would have been open to the Trustee to seek an Income Payments order under s.310 IA 1986, or to agree an Income Payments agreement under s.310A IA 1986. An IPO or IPA, however, would only last a maximum of three years. In this case, Mr Fennell submitted, the estate had been enriched by payments which went beyond that. The Respondent had been accounting to the Trustee for trading income from the business from 2014 until 2019; a period of five years. This, he submitted, was unfair to the Respondent.

Discussion

137. In reality, an IPO or IPA could have commenced at any time up to 9 October 2015. An IPO or IPA commenced on 9 October 2015 could therefore have run until 9 October 2018. The Trustee withdrew from the business with effect from 31 July 2019. On one analysis therefore, the trading arrangements in place exceeded the period which could have been covered by way of an IPO or IPA by less than a year.

138. Even working from Mr Fennell's calculations, however, and proceeding on the basis that the trading arrangements exceeded the maximum three year period which could have been covered by an IPO or IPA by two years, in my judgment, responsibility for those two years cannot be laid exclusively at the Trustee's door.

139. In this regard it will be recalled that, by June 2017 (less than three years after the date of the bankruptcy order), the Trustee was actively seeking to persuade the Respondent to buy the business from him. The Respondent instructed solicitors shortly thereafter and the current dispute ensued. Any sale (or even a formal transfer) of the business to the Respondent then became extremely difficult, as the Respondent claimed that the business was his in any event. Arrangements regarding the business thus became the subject of a series of 'holding' agreements between the parties' representatives, pending determination of the dispute. Having sought unsuccessfully to resolve the dispute on an amicable basis, the Trustee very properly issued a s.303 application seeking directions from the Court.

140. The question whether to apply the rule in ex p James in relation to trading income from 10 October 2017, however, does not turn on whether the Trustee has been guilty of any conscious or deliberate wrongdoing. No conscious or deliberate wrongdoing on the part of the Trustee was made out on the evidence before me. Quite the contrary; whilst the Trustee was undoubtedly guilty of errors in his handling of this bankruptcy, on the evidence before me I am satisfied that at all material times he acted honestly, with integrity and with the best of intentions. The key issue is how the

trading income from the business for the period from 10 October 2017 to 31 July 2019 should now be approached, given the somewhat unusual circumstances of this case and the dispute which has arisen. On a strict legal analysis, that income belongs to the estate. As put by Walton J in In re Clark; Ex p The Trustee v Texaco Ltd [1975] 1 WLR 559 at p563, however:

'where it would be unfair for a trustee to take full advantage of his legal rights as such, the court will order him not to do so….'

141. In my judgment, subject to the caveats addressed below, in the events which have occurred, it would be unfair for the Trustee to take full advantage of his legal rights to treat the entirety of the trading income from the business from 10 October 2017 to 31 July 2019 as an asset of the estate. Whilst the continuation of the trading arrangements beyond 2017 was plainly not the wish of the Trustee and the immediate cause of that continuation was an impasse on a sale of the business triggered by the Respondent's insistence that the business was his, the dispute which arose in 2017 must be seen in context.

142. The trading arrangements put in place in 2014 should not have continued for such a length of time. By October 2015, the Trustee should have insisted on a sale of the business or cesser of trading. Even putting to one side the limited purposes authorised by Schedule 5 and focusing instead on the purposes of trading actually pursued in this case, post-discharge an IVA was no longer possible and by October 2015, whilst there remained hope of reducing the HMRC proof by up to £50,000, realistically a s.282(1)(b) annulment was off the table.

143. On the evidence which I have heard and read, the Respondent was in no position to buy the business back himself and carry it on in his own right in October 2015. To the extent that he sought to imply otherwise at times in his oral testimony, I reject that evidence. On a balance of probabilities, had the Trustee insisted on a sale or cesser of trading as at October 2015, this would have resulted in a sale to a third party or cesser of trading.

144. Instead of insisting on a sale or cesser of trading at that stage, however, on 10 October 2015, the Trustee wrote to the Respondent suggesting that they continue the trading arrangement for another 12 months, with a view to achieving an informal IVA or a s.282(1)(b) annulment. Whilst I am satisfied on the evidence that I have heard and read that this suggestion was motivated by a wish to assist the Respondent and not out of self-interest, it was an error of judgment on the part of the Trustee. Together with many other delays for which the Respondent must bear responsibility, this misplaced act of kindness on the part of the Trustee served to prolong the trading arrangement beyond any reasonable bounds. This forms part of the relevant backdrop to the position arrived at in 2017.

145. Once an impasse on a sale of the business had been reached in 2017, the parties agreed a series of interim arrangements with a view to ensuring the survival of the business pending resolution of the dispute which had arisen. The business continued, using assets of the estate undoubtedly, but also benefiting from the Respondent's own 'tools of the trade' and long hours which he devoted to the business, charging low sums (£14,851.86 and £11,966 in the years ending October 2018 and 2019

respectively) for his services. The Respondent's services since October 2017 have generated income for the estate significantly beyond the three-year maximum period which would have governed an IPO or IPA. In my judgment, subject to the caveats below, to allow the estate to benefit from all such income would be unjustly to enrich it at the expense of the Respondent. A right-thinking person would conclude that it would be wrong for the Trustee in such circumstances to take full advantage of his legal rights to treat the entirety of the trading income from the business from 10 October 2017 to 31 July 2019 as an asset of the estate. A right-thinking person would conclude that some adjustment should be made.

146. Subject to the caveats addressed below, I shall therefore direct the Trustee not to insist on his strict legal rights in relation to the trading income generated by the business over the period from 10 October 2017 until 31 July 2019, and instead to account for such income to the Respondent.

147. The caveats are as follows. First, the time costs charged by Mr Freestone in carrying out accounting work for the business on the instruction of the Trustee between 10 October 2017 and 31 July 2019 pursuant to the trading arrangement in place must be paid for in full out of the trading income generated over that period before accounting to the Respondent for the balance. To respectfully adopt a phrase once used by Lewison LJ in another context: the Respondent 'cannot have the penny and the bun'. On the evidence it is clear that Mr Freestone provided valuable services at reasonable cost to the business and these services must be paid for.

148. Second, to the extent that reasonable and proper time costs have been incurred by the Trustee in carrying out essential tasks for the business between 10 October 2017 and 31 July 2019 pursuant to the trading arrangements then in place, these too must be paid for out of the trading income generated by the business over that period before accounting to the Respondent for the balance. There were tasks that had to be carried out by the Trustee for the business pending resolution of this dispute and in my judgment, in the events which have occurred, these must be provided for out of trading income before accounting to the Respondent for the balance.

149. I reject Mr Fennell's submission that these time costs of Mr Freestone and the Trustee should not be accounted for out of trading income. The estate is not unjustly enriched by such sums. On the contrary, it would unjustly enrich the Respondent - at the expense of the estate - to allow him such services at no cost.

150. Third, unless the parties have already reached a contractually binding agreement to the contrary, the Respondent must also account to the Trustee for a sum representing the value of the assets making up the business. Whilst I will hear further submissions on handing down judgment on the date at which the assets should be valued for such purposes, my provisional view is that they should be valued either as at 10 October 2017 or as at the date of the bankruptcy order. Unless the Respondent is in a position to pay the same in full from other sources, the sum representing the value of the assets making up the business should be paid out of the trading income generated over the period between 10 October 2017 and 31 July 2019 before accounting to the Respondent for any balance. In the event of a shortfall, the Respondent will have to cover the same from other sources.

Issue 13

151. The issue whether the Trustee would be entitled to a quantum meruit award in respect of the time spent in connection with trading the business would only be of relevance in the event that he was disallowed his fees. As his fees have not been disallowed, it is unnecessary for me to address this issue.

Concluding Remarks

152. I shall hear from Counsel on the terms of the order sought and on costs on the handing down of this judgment.

ICC Judge Barber

4 November 2020