Neutral Citation Number: [2005] EWHC 259 (Ch)

Case No 5799 of 2004

IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION
COMPANIES COURT

IN THE MATTER OF VP DEVELOPMENTS LIMITED (IN COMPANY VOLUNTARY ARRANGEMENT)

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

Royal Courts of Justice
Strand,
London,
WC2A 2LL

Date: 1 March 2005

Before :

The Hon Mr Justice Laddie

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Between :

PENWITH DISTRICT COUNCIL **Petitioner**

- and -

V P DEVELOPMENTS LIMITED **Respondent**

- -

Mr Jeremy Goldring (instructed by **Pinsent Masons**) for the **Petitioner**

Mr Hugh Sims (instructed by **Donald Pugh**) for the **Respondent**

Hearing dates: 4 February, 2005

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Judgment

The Hon Mr Justice Laddie :

1. I have before me two cross-proceedings. One is a creditor's winding up petition. It was presented on 21 September 2004 by Penwith District Council ("the Petitioner") against V P Developments Ltd ("the Company"). The Petitioners seeks a compulsory winding up order. The application is brought by the Company. It applies for the striking out or a stay of the Petition. The Petitioner is represented by Mr Jeremy Goldring and the Company is represented by Mr Hugh Sims.
2. The facts underlying the current dispute are spread over a number of years. The Company carried on business as a building contractor and maintenance specialist. In the late 1980s it entered into a number of building contracts with the Petitioner relating to a number of projects under which it carried out renovations and other building work to flats and houses owned by the Petitioner. After the works were completed, disputes arose between the parties. In substance the Company said that the calculations made by the Petitioner to determine what it owed the Company under these contracts were incorrect. As a result, the Company said that it had been significantly underpaid by the Petitioner. Each of the contracts between the Company and the Petitioner contained an arbitration clause. In late 1993 the Company commenced eight arbitrations. Those arbitrations and the amounts sought in them are as follows:
    a. Penbeagle£27,710.78
    b. Bodriggy£19,737.03
    c. Lanuthnoe £8,057.21
    d. Pendarves £2,937.38
    e. Alverton B2(b)£367,311.00
    f. Alverton A2(a)£132,601.25
    g. 2 Jobbing Works Contracts £38,000 (approximately)
3. The progress of those arbitrations is a matter of some importance to the issues I have to decide. In the Penbeagle and Bodriggy arbitrations, on 28 May 1998 the Petitioner's appeal to the High Court against the interim award of the Arbitrator on a preliminary issue succeeded. A costs order was made in the Petitioner's favour in the sum of £21,000 plus interest at 8% per annum. The Arbitrator then dismissed the Company's claims in the Penbeagle and Bodriggy arbitrations on 21 July 1999, and ordered the Company to pay the Petitioner's costs. At the same time certain orders were made in the Lanuthnoe arbitration. I am told that the total value of the costs awarded in the Petitioner's favour as a result of these orders are estimated to be in the region of £100,000-£150,000. Those costs have not yet been assessed and, according to the Petitioner, a division of costs between the three arbitrations will require detailed analysis. The Company's claim in the Lanuthnoe arbitration is now dependent on a narrow ground. The Petitioner says that it is bound to fail. This is disputed by the Company. However, the Company has taken no further steps in this arbitration since 1999. In the Pendarves arbitration, costs have been awarded to the Petitioner and have been assessed. These costs represent the principal element in the Petition Debt. The Alverton B2(b) arbitration continues. On 2 September 1999, the Arbitrator ordered that security be provided by the Company in the Alverton A2(a) arbitration in the sum of £55,000 with costs to the Petitioner. The Company has failed to give the necessary security, with the result that that arbitration has been stayed. The Company has taken no further steps in it since 2 September 1999. As far as the 2 Jobbing Works Contracts

are concerned, the Company has taken no steps since issuing Notices to Refer in March 1996. I understand that the Penbeagle arbitration was not a complete failure for the Company. An award of £700 was made in its favour but, notwithstanding this, in substance it lost, hence the costs order against it.

4. Based upon what has happened in the arbitrations to date, the Petitioner is a creditor of the Company in respect of various cost orders made on the 22 September 1998 and 28 October 1998. They are the Petition Debt. As at 29 November 2004 that debt, taking into account interest, stood at just over £96,000. Furthermore the Petitioner has the benefit of a High Court costs order in its favour dated 21 May 1999 which, together with interest, was worth just over £29,000 as at 29 November 2004. The latter sum is not referred to in the Petition, but the Petitioner says that it will apply, if necessary, to amend the Petition to rely on this additional sum. No such amendment would alter the outcome of this dispute one way or the other and no formal application to amend is before me.
5. In addition to these assessed sums, the Petitioner has the benefit of certain other unassessed cost orders made in its favour. The Petitioner asserts that as at 29 November 2004 they would have been worth approximately £154,000. I understand that the reason there has been no assessment is that the Company has paid no part of the assessed costs and is admittedly wholly insolvent. The Petitioner has taken the not unreasonable decision not to spend further sums on assessment when there is no realistic prospect of its recovering any part of the cost of the assessment exercise let alone the costs so assessed.
6. As I have said, there is no dispute that the Company is insolvent. In mid-1994, following a meeting of its then creditors, the Company entered into a CVA and a Supervisor was appointed. At the commencement of the CVA it was apparent that the Company was unable to pay its debts as and when they fell due. At that date the estimated deficiency to creditors, ignoring the value, if any, of the claims against the Petitioner, was £505,874. One of the purposes of the CVA was to allow the Company to pursue its claims against the Petitioner. It will be appreciated from what is set out above that at the time the Company assessed the latter claims to be worth nearly £600,000.
7. As at the date of the CVA, the Petitioner was a creditor of the Company for a sum which, I understand, was trivial. The various costs orders which are relied on to support the Petition only came into existence after the CVA.
8. It will be seen that the four biggest claims made by the Company are those in the Penbeagle, Bodriggy, Alverton B2(b) and Alverton A2(a) arbitrations. By far and away the largest is the Alverton B2(b) claim which is for more than 50% of the total value of all the claims together. The Alverton A2(a) claim was also very large. It was worth more than twice the combined value of the Penbeagle and Bodriggy arbitrations.
9. In the Alverton A2(a) arbitration the Petitioner applied for security for costs. As noted above, that application was successful and no security has been forthcoming. Thus the application for security succeeded in stopping that arbitration.
10. At about the same time as it applied for security in the latter arbitration, the Petitioner also applied for security in the Alverton B2(b) arbitration. In September an order for security in the sum of £60,000 was made by the arbitrator. However in this case the Company secured funding and, in early 2000, paid the security. In the result, that arbitration is continuing. The Company appears to have decided to concentrate all the resources it can muster in the pursuit of its biggest claim.

11. On 12 July 2000, the Company served Amended Points of Claim in the Alverton B2(b) arbitration. Unfortunately the arbitrator, Mr Fox-Andrews QC, became ill and died. A new arbitrator, Mr Ian Salisbury, was appointed in April 2003. Three things then happened. First, the Petitioner made an application for an increase in security of costs in that arbitration. That application was rejected by the arbitrator on 17 March 2004. Thus the Petitioner did not manage to achieve a stay of this arbitration. Second, the Petitioner having not yet served its defence, on 24 August 2004 it applied for an extension of time to do so. The arbitrator directed the Petitioner to serve its defence and the Scott Schedule by 31 December 2004. It was some 4 weeks after it had applied for this extension of time that the Petitioner presented this Petition. Third, at about the same time the Petitioner applied to the Bristol County Court for permission to enforce the award as if it were a judgment. No doubt defending that application put a further strain on the resources available to the Company. I was not told the purpose of that application.
12. The core disputes between the parties are as follows. First, the Petitioner says that if a creditor with standing to make the application wants to have a company wound up, and if the court is satisfied that the company is unable to pay its debts, a winding up order will follow unless there is some special reason why it should not (*Re Lummus Agricultural Services* [1999] BCC 953). That it says is the position here, there being no doubt as to the Company's insolvency and its, the Petitioner's, debt. Second, and in response to this, the Company says that the court will dismiss the Petition if it is an abuse of process. In particular, a petition will be an abuse of process if it is being sought so as to secure some collateral purpose, such as to stifle related proceedings (*Re Majory* [1955] Ch 600 and *Malcolm Robert Ross (a Bankrupt)(No 2)* [2000] BPIR 636). The Company says that applies here. During the many years of the Alverton B2(b) arbitration, the Petitioner has never alleged that the Company's claim was other than serious and arguable. When the Petitioner failed in 2004 in its attempt to secure an increase in the order for security for costs, which would have stopped the arbitration, it decided to Petition as an alternative mechanism designed to achieve the same result. The Petitioner could have petitioned at any time from 1999 onwards. Its decision to petition now is only explicable on the basis that it is an attempt to stifle the Alverton B2(b) arbitration. Third, and in the alternative, the Company argues that it has a genuine and serious cross-claim, namely the claim in the Alverton B2(b) arbitration, which, if successful, will exceed the Petition Debt. If this is so, then the Petition should be dismissed (*Re Bayoil SA* [1999] 1 WLR 147). Fourth, the Petitioner argues that the Alverton B2(b) arbitration is not a relevant cross-claim and fifth, even if it is, there are special circumstances arising out of the existence of the CVA which justify ignoring it. I should mention that the Company also argues that the Petition Debt is challenged on genuine and serious grounds with the result that the Petitioner has no standing to present it. This is based upon an assertion that, as a result of various negotiations between the parties, the Petitioner has waived the debt or is estopped from relying on it. Mr Sims puts this as a distant long-stop argument. In view of my conclusions on other points, it is not necessary to consider it.
13. Although all of these points have been canvassed before me, the issue of cross-claim emerged as the most important one.
14. In *Re Bayoil*, Nourse LJ explained the difference between disputed debt cases and cross-claim cases as follows:

> "[the dismissal of the petition on the basis that the debt is disputed in good faith and on substantial grounds] is not, at any rate initially, a

> matter for the discretion of the court. It is founded on the petitioner's inability to establish the locus standi to present a petition under what is now section 124(1) of the Insolvency Act 1986. The case of an undisputed debt with a genuine and serious cross-claim is different, in that the dismissal or staying of the petition can only be a matter for the discretion of the court, albeit that its exercise may have been narrowed by authority." (p 150)

15. The formal difference between disputed debt and cross-claim cases should not hide their underlying common objective. This was explained by Ward LJ in *Re Bayoil*:

> "The practice in the disputed debt case is well-established. I appreciate that in that case the petition is dismissed because the petitioner cannot properly claim to be a creditor. That said, there seems to me to be little practical difference between the disputed debt and a cross-claim which does not constitute a set-off properly so called. In this regard I am fortified by the opinion of Lord Edmund-Davies in *Malayan Plant (Pte) Ltd v Moscow Narodny Bank Ltd* [1980] MLJ 53, 55:
>
> 'there is no distinction in principle between a cross-claim of substance (such as in the *Wools* case) and a serious dispute regarding the indebtedness imputed against a company, which has long been held to constitute a proper ground on which to reject a winding up petition.'"

16. It is against this background that I consider the cross-claim arguments.
17. Although in its evidence the Petitioner suggests that there is nothing in the Alverton B2(b) arbitration, Mr Goldring does not assert that before me. He accepts that it should be considered serious and genuine. However he says that it is not to be taken into consideration because it is not really a cross-claim at all. This is because, for there to be a cross-claim properly so called, there must be mutuality (see *Hurst v Bennett* [2001] BCLC 290). He argues that there is no mutuality here because of the existence of the CVA. The cost orders relied on as the Petition Debt are orders made against the Company on its own behalf in favour of the Petitioner. He says, by contrast, that the claim in the Alverton B2(b) arbitration is held by the Company as trustee for the creditors in the CVA. (See *In Re N T Gallaher & Son Ltd* [2002] 1 WLR 2380). It has no beneficial interest in it. If Mr Goldring is right on this point, the result would be the same even if the order for costs in favour of the Petitioner had been made in the Alverton B2(b) arbitration. That order would still be against the Company rather than against the creditors in the CVA on whose behalf the Company is acting.
18. I do not accept Mr Goldring's arguments for two reasons. First, I do not accept that there is a want of mutuality. As is explained in *Derham, The Law of Set-off* 3rd Ed at 17.93:

> "**Trustee's lien**
>
> A trustee who properly incurs a liability in the execution of the trust is entitled to be indemnified from the trust assets, and for the purposes of giving effect to the indemnity the trustee has an interest which has been described as a first charge or a lien over the assets. This is not a

mere right of retainer, but rather courts in Australia have emphasised that it confers an equitable proprietary interest in those assets which has priority over the interests of the beneficiaries. In an appropriate case the court may order a sale of trust property in order to satisfy the trustee's claim. The trustee's first charge should extend also to a trust asset in the form of a debt owing to the trustee in his capacity as such. Furthermore, it is not necessary that the trustee should first have paid the debt before claiming against the trust assets. If the trustee has not paid the debt from his personal assets he is entitled to apply the trust property in discharging it, in other words the trustee has a right to exoneration, and he has a charge on the trust property in that circumstance as well. Accordingly, when the trustee is sued by a third party for payment of a debt properly incurred in the execution of the trust, and at the same time the trustee as a result of his right of indemnity has a charge on a debt owing to the estate by the third party, there is much to be said for the view that the trustee's interest may suffice to bring about mutuality in equity for the purpose of equity acting by analogy with the Statutes. This should also be relevant to insolvency set-off. It assumes however that the trustee has a right of indemnity. In a particular case the right may be limited by the trust instrument, or it may be restricted to certain assets, as where a testator has authorised the executor to carry on business but only by utilising those assets."

19. Mr Goldring relies on the last sentence of this passage. However this takes him nowhere. The general rule is that the trustee has a right of indemnity in respect of liability properly incurred in the execution of the trust. That right may be curtailed by the terms of the trust instrument. However Mr Goldring can point to no such express or implied curtailment here. Mr Goldring does not assert that, in pursuing the arbitrations in relation to which the cost orders were made, the Company was acting otherwise than properly for and on behalf of the creditors in the CVA. In the result, the Company does have a personal interest both in the Petition Debt and the claim in the Alverton B2(b) arbitration. Its interest in the latter covers all of the Petition Debt.
20. Second, even if this is not right, the Company would be able to rely on an equitable set-off. This is explained in *Derham* at paragraph 17.90:

"Equitable set-off

A trust is not a legal entity separate from the trustee. When a trustee incurs a debt in that capacity, the trustee is personally liable. The creditor does not have direct recourse either to the trust assets or to the beneficiaries. Further, when the trust property includes a debt owing to the trustee, the trustee, although possessed of the legal title to the debt, is not the beneficial owner. Prima facie there would not be mutuality in equity as between, on the one hand, a debt incurred by a trustee, and on the other a cross-claim available to the trustee in his capacity as such against the creditor on the first-mentioned debt. Consider, however, that the trustee has entered into a transaction with a third-party out of which cross-demands arise which are sufficiently closely connected to give rise to an equitable set-off. In such a case, given that equity in any

> event has never insisted upon mutuality as a strict requirement for this form of set-off, the apparent lack of mutuality should not be a sufficient ground for denying a set-off to the third party. This was the view of Giles J. in the New South Wales Supreme Court in *Murphy v Zamonex Pty Ltd*, and in Victoria the Appeal Division of the Supreme Court in *Doherty v Murphy* accepted in a summary judgment application that a cross-claim for damages against the trustee in this situation provided an arguable defence. Nor was Giles J. persuaded to adopt a different view by the argument that the trustee in that case may have lost his right to an indemnity from the trust estate in respect of the liability because it was in breach of trust. The equitable set-off was justified on the ground that the beneficiaries of a trust should not have the benefit of the transaction without also bearing the burden of the trustee's conduct. Moreover, while in both *Murphy v Zamonex* and *Doherty v Murphy* there had been a change in trustee, that did not affect the views expressed. The new trustee takes subject to equities, so that the defendant can assert the set-off notwithstanding that the action is brought by the new trustee."

21. This passage is supported by the decision in *Murphy v Zamonex Pty Ltd* to which it refers. The facts in that case were as follows. The plaintiffs were the trustees of certain trusts. Burns Philp Trustee Co Ltd ("Burns Philp") was the former trustee. Burns Philp advanced certain moneys to the first defendant with guarantees provided by the second to seventh defendants. The plaintiffs sued for the outstanding debt and interest. The defendants mounted a cross-claim to the effect that Burns Philp was in breach of contract and certain fair trade legislation by refusing to make further advances under the loan facility. The court upheld the cross-claim against Burns Philp. The plaintiffs did not dispute that there would have been a set off had Burns Philp not been a trustee. However they argued:

> "... that it made all the difference that Burns Philp was a trustee. They submitted that because it was a trustee the defendants' entitlement to damages would not enable them to execute against the trust assets unless Burns Philp had a right of indemnity from those assets and they were abrogated to Burns Philp's right of indemnity, and then only to the extent of the indemnity. Accordingly, there was not the mutuality necessary for set-off because the beneficial title to Burns Philp's claims against the defendants lay in the unit holders rather than Burns Philp, while the subject of the defendants' claims was Burns Philp." (p 463)

22. The court expressed the relevant principles as follows:

> "Equitable set-off is available where the defendant establishes an equitable ground for being protected from the plaintiff's claim. That has been expressed in language to the effect that the defendant's set-off goes to the root of or impeaches the plaintiff's claim, but also in language to the effect that the counter-claim is so directly connected with the claim that it would be unjust to allow the plaintiff to recover without taking into account the defendant's counter-claim. It is

> sufficient to refer to *AWA Ltd v Exicom Australia Pty Ltd, James v Commonwealth Bank of Australia* (1992) 37 FCR 445 sub nom *Re Just Juice Corporation Pty Ltd; James v Commonwealth Bank of Australia* (1992) 109 ALR 334 and the discussion in Meagher, Gummow and Lehane, pars 3709-3710 at 817-823 without going into whether the latter approach is an illicit departure from principle and authority. Accordingly, if a court of equity will restrain A in his capacity as trustee from recovering his claim against B without allowing for B's counter-claim against A in A's capacity as trustee there will be set-off in equity. That B could not have levied execution against the trust property may be relevant to whether the court will intervene, but why should it necessarily prevent set-off? Depending on the circumstances, it may not be right for the beneficiaries to have the fruits of A's activity as their trustee without bearing the burden of A's conduct in so acting." (p 465)

23. The court then applied these principles to the facts of the case as follows:

> "in this case I consider that if there had been no question of trusteeship the defendants would have been entitled to set their claims against Burns Philp off against Burns Philp's claims against them. If Burns Philp was claiming as trustee and liable in its capacity as trustee, I consider the same set-of would be available. The claims would be just as closely related, those of Burns Philp would still be impeached by those of the defendants or it would still be unjust that the claims made on behalf of the unit holders should proceed without account being taken of the claims against the trustee for its activities on their behalf; the unit holders could not take the benefit of the transaction without bearing the burden of Burns Philp's conduct." (p 467)

24. This is consistent with the underlying principle of the cross-claim practice as explained by Ward LJ in *Re Bayoil* (see above).
25. It seems to me that Mr Goldring's approach is too narrow. The relevant question is whether the cross-claim is closely related to the Petition Debt. If it is, the court will allow one to be set off against the other. On the assumption that the cross-claim is serious and substantial, it may have the practical effect of eliminating the Petition Debt.
26. In my view the costs orders made against the Company are closely related to the claims made by the Company in all the arbitrations including that in the Alverton B2(b) arbitration. It seems to me that, were the Company to secure an award in its favour in the latter, it is inevitable that the Petitioner would seek and obtain a direction that the existing orders for costs in its favour should be set off against it. I think it is highly likely that it would obtain such a direction.
27. In the light of this, it seems to me that it would be wrong to allow this Petition to proceed unless there are special circumstances. Mr Goldring asserts that there are such special circumstances here, namely the existence of the CVA. He says it is unfair that the Petitioner may be forced to pay up on any award made in the Alverton B2(b) arbitration when it will have no prospects of recovering anything from the CVA. It is, in substance, a post-CVA creditor and therefore it will make no recovery under the CVA. He adds that success in the Petition will result in the appointment of a

liquidator, an independent officer of the court. He will be able to investigate the affairs of the Company and, in particular, will be able to determine whether or not any claim can be made against its directors.

28. I do not think that these come anywhere near being sufficiently special circumstances to justify allowing the Petition to proceed. As Nourse LJ pointed out in *Re Bayoil*, an order that a company be wound up is often its death knell. Mr Sims says that, were Mr Goldring's arguments to succeed, the Company would be penalised in the most Draconian way for having entered into a CVA. As a matter of policy, that cannot be right. Furthermore, he points out that the suggestion that a liquidator could investigate whether the Company has claims against the directors is made now for the first time. There is no material which suggests any basis for thinking such claims exist. In the end, to allow this Petition to succeed now would be likely to terminate the Alverton B2(b) arbitration. Since, for the purpose of these proceedings, Mr Goldring accepts that that arbitration is serious and substantial, its termination may well be to the significant disadvantage of most of the creditors of the Company. In such circumstances some truly compelling consideration would need to be present before it would be proper to allow the Petition to proceed. There is no such consideration here.
29. In the circumstances I do not need to determine Mr Sims' substantial argument that the pursuit of this Petition is an abuse of process. I will strike out the Petition.