COLLAS CRILL

Stuck in the middle with you

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The Royal Court of Guernsey has recently handed down judgment upon an application by the liquidators of CanArgo Limited (Company), Ben Rhodes and Alan Roberts of Grant Thornton (Liquidators), for directions blessing the sale of the Company's assets which were caught between competing 'prior rights' claims of two protagonists. It was alleged by each that these rights bound the Liquidators and therefore practically prevented the sale of the assets to anyone else but themselves, or at the very least without their consent. Following a competitive bidding process, and under threat of litigation from both sides, the Liquidators sought a blessing of their decision to untangle the knot and sell to one of the competing parties.

This judgment gives excellent guidance for liquidators caught between a rock and a hard place, when the Court will 'wrap its arms around them', and how to go about things to ensure it does.

Background

The purpose of the Company was exploration and exploitation of oil and gas in Georgia through three subsidiary companies (Subsidiaries). In 2012, the Company sold 50% of its shares in each of the Subsidiaries to M. The Company entered into Joint Venture Operating Agreements (JVOAs) with M to govern how the Subsidiaries were to be run and funded.

In 2015, the Company's shareholder sold its shares in the Company on terms which included 'trailing royalty rights'. The relevant agreements included provisions that any subsequent disposal of the shares must preserve these rights. At the time of the liquidation, the royalty rights were held by A.

The Company was placed into liquidation in 2018. It had no cash and its only assets were its JV interests in the Subsidiaries. Importantly (as it turned out), the Company also had the benefit of potential claims against M under the JVOAs.

The Company's claimed liabilities comprised of debts to A, debts to the operating Subsidiaries and some other minor amounts. If A's debts were admitted in full, they would amount to approximately 99% of the Company's liabilities.

In 2018, the Liquidators opened a bidding process for the purchase of the Company’s JV interests in the Subsidiaries. The invitation to bid was limited to stakeholders of the Company. Both M and A made bids. Each asserted their respective prior rights in the course of the bidding process and each threatened action against the Liquidators if their respective rights were not protected as part of any sale.

Following the bidding process, the Liquidators entered into a conditional asset purchase agreement (CAPA) with M. Notably, the CAPA contained a condition subsequent that a direction blessing the Liquidators' decision to

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enter into the CAPA be obtained from the Royal Court.

The Liquidators subsequently sought the requisite direction from the Court but their application was opposed by A.

The Arguments

A's initial opposition was twofold:

1. the Application was not an appropriate one for the Court to grant directions on; and
2. the CAPA would compromise the Company's claim against M, which in A's view was more valuable than the consideration due under the CAPA.

Decision

Lieutenant Bailiff Marshall QC considered the scope of the Royal Court's directions powers under section 426 of the Companies (Guernsey) Law, 2008, and found:

1. It has a wide power to approve officeholders' conduct, but the power does have some limits. The purpose of the section is in respect of the future conduct of the liquidation. Whilst the Court should not bless past conduct, the condition subsequent mechanism adopted by the Liquidators was acceptable.
2. Section 426 does not enable a liquidator to surrender his/her discretion to the Court just because he/she finds himself/herself having to make a difficult decision. The objective of section 426 is to assist a liquidator to make liquidation decisions and not for the Court to take over the conduct of the liquidation. LB Marshall QC endorsed the analogy to a trustee's blessing application under the Public Trustee v Cooper jurisdiction.
3. There must be a proper and particular reason for invoking this jurisdiction. This may be easier to recognise as a matter of impression than to define and it will be fact sensitive. In this case, following the Australian decision in Idoport, the threat of litigation meant this was an appropriate case for directions.
4. A liquidator has to give full explanation of his/her decision to enter into the transaction. However, a liquidator is permitted and would be expected to exercise some discretion as to what was put before the Court. Not every 'travelling draft' need be disclosed.
5. The Court must be satisfied that the decision is the product of a competent and comprehensive consideration of all relevant matters and facts, but only relevant matters and facts, and that it is not illogical, irrational or perverse. The Court does not make any value judgment about the merits of the decision. This approach respects the fact that the power to make the decision has been confided to the liquidator and he/she is expected to exercise that power with due care and propriety.
6. Although a “proper” decision must mean a fully informed decision, there is no absolute rule that a failure to take potentially helpful legal (or other professional) advice will cause the Court to refuse to “bless” the decision. If the possibility of taking advice had been genuinely investigated and it had been found impossible or impractical, e.g. through lack of available funds or funding, the Court may accept that the decision was the best which could be taken in the material circumstances, including lack of such advice.

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7. A majority creditor's views should be taken into account by a liquidator and the Court on a directions application, however these views were not determinative. The liquidator is ultimately charged with making the decision.

The Court found that the Liquidators' decision to enter into the CAPA was reasonable in all of the circumstances and granted the directions sought.

Conclusion

In the unique circumstances of this case, the Liquidators were stuck between two parties with divergent objectives. The Liquidators were in the unenviable position where they had a job to do, no money to do it, and were being threatened with Court action if they did something, did nothing, or did something in a particular way.

A cautious bidding process, followed by a directions application blessing the CAPA enabled the Liquidators to find a way to safely chart a course to progress the liquidation in the interests of all the creditors of the Company.

The Judge spelt out concisely the principles to be taken into account when a liquidator makes an application to the Court, which will be of useful guidance for insolvency practitioners and lawyers going forward.

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