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BTI v Sequana: Guernsey at the forefront of developments in directors' duties

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On 5 October 2022, the Supreme Court handed down their landmark judgment in the long-running case of *BTI v Sequana*[1]. It is "*a momentous decision for company law*" (in the words of Lady Arden who gave one of the leading judgments) that addresses fundamental questions and provides welcome guidance for directors of companies. The decision also confirms Guernsey's role at the forefront of legal developments in this field.

Background

In May 2009, a company called AWA distributed a dividend of €135 million to Sequana, its only shareholder. Although AWA was solvent, both on a balance sheet and cash flow basis, there was a real risk that AWA might become insolvent at some point in the future as a result of environmental clean-up liabilities.

More than nine years later in October 2018, AWA went into insolvent administration. BTI, who took an assignment of AWA's claims, consequently sought to recover substantial damages from AWA's former directors on the basis that they had breached their duty owed to creditors of the company by authorising the dividend to Sequana.

Both the High Court and the Court of Appeal dismissed BTI's claims on the basis that, although there was a real risk of insolvency at the time of the dividend being paid, the company was not yet insolvent, nor was insolvency imminent or even probable.

Case summary

BTI appealed to the Supreme Court, who were able for the first time to consider various aspects of what has become known as the "creditor duty" or the "rule in West Mercia", including the point in time at which directors must begin to consider the interests of the company's creditors, the duty's exact content and its inter-relationship with other key principles of company law such as ratification and payment of dividends.

The key conclusions of the Supreme Court were that:

1. There is a "creditor duty" under English law, whereby a company's directors' duties include an obligation to consider the interests of the company's creditors in certain situations.
2. It is not, however, a free-standing duty; it merely adjusts the well-established fiduciary duty of a director to act in good faith in the interests of the company.

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3. The "creditor duty" is engaged not when there is a mere 'real risk' of insolvency (as in this case), but rather when the directors know, or ought to know, that the company is insolvent, is bordering on insolvency, or that an insolvent liquidation or administration is probable.
4. Once the duty is engaged, the greater the company's financial difficulties, the greater the weight that should be given to the interests of creditors when balancing them against the interests of shareholders, i.e. a 'sliding scale' approach was preferred; it is not binary. Once insolvent liquidation becomes inevitable or irreversible, however, the creditors' interests will have become of paramount importance, over and above the interests of the shareholders.

Carlyle endorsed

Of particular note from a Guernsey law perspective is the express endorsement by Lord Reed and Lord Briggs of key aspects of Lt Bailiff Hazel Marshall KC's judgment in the 2017 Guernsey case of *Carlyle Capital Corporation Ltd v Conway and others* (in which this firm acted for the successful independent director defendants).

In *Carlyle*, Lt Bailiff Marshall KC adopted a nuanced approach to the issue of "paramountcy" (i.e. once the creditor duty is engaged whether the creditors' interests immediately become paramount or whether a more fact specific approach is appropriate), which differed from the approach taken in certain English cases before that time and which the Plaintiffs had relied upon. Lt Bailiff Marshall KC's nuanced approach found favour with their Lordships who quoted the relevant passages from her judgment in full.

The Supreme Court's decision as to when the creditor duty is engaged was also consistent with Lt Bailiff Marshall KC's approach to that issue in *Carlyle*.

Such endorsements are clear evidence of the central part Guernsey has played in developing this fundamentally important area of the law.

Please do not hesitate to contact Gareth Bell or David O'Hanlon for any assistance you may require in relation to directors duties or related issues.

[1] *BTI 2014 LLC v Sequana SA and others* [2022] UKSC 25

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