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Liquidators: A duty to deal with trust assets?

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Does a liquidator of a company have a duty under English law to deal with "trust assets", (i.e. assets which are held by the company on trust and not beneficially owned by it)? This article argues that, under English law, there is no such duty. This argument is supported by the wording of the UK Insolvency Act 1986, and the 'Berkeley Applegate' cases. Although there is Australian authority which holds that the liquidator has a duty to "act responsibly" in relation to trust assets, its correctness (and in any event, its applicability to English law) is doubtful.

Introduction: liquidators' duty to deal with trust assets

When a company goes into liquidation, an issue that is often faced by the liquidator is how to deal with property which is held (or arguably held) on trust by the company.

Undoubtedly, the liquidator is under a duty to ascertain which of the putative trust property is actually owned beneficially by the company; and which is owned beneficially by third parties.

The former category would form part of the company's assets available for distribution to creditors and (if there is a surplus) to shareholders.

What about the latter category of assets ("trust assets")? Those assets would not form part of the pool available to creditors. In practice, a liquidator may often *choose* to deal with trust assets (e.g. identifying the correct beneficiaries and distributing the trust fund to them). However, a question that arises is whether the liquidator has a *duty* to administer trust assets.

This question is of practical importance, not only to liquidators, but also to financial regulators. This is because companies which go into liquidation may be holding large sums on trust for members of the public (such as investment firms holding client monies on trust). If the legal position is that liquidators have *no* duty to deal with trust assets, there could be thorny issues as to how such beneficial owners could recover their assets (in the event the liquidators decline to administer the trust).

Despite the importance of the subject, it has been little explored in the case law. This question was broached recently in *Re Beaufort Asset Clearing Services Ltd* [2022] EWHC 636 (Ch) (in which one of the authors appeared as counsel). The company was part of an investment banking group, which had held significant assets on trust for clients, and was now in liquidation.

Sir Anthony Mann, sitting as a judge of the English High Court, described the issue of whether the liquidator was under any duty to administer the trust assets as a "potentially significant question" [27]. The Financial Conduct Authority worried that a negative answer would leave a "significant hole in client protection" in relation to FCA-regulated companies which hold assets on trust [24]. However, the judge declined to grapple with the question, as it was academic on the facts.

This article will discuss the position in English law. The correct view appears to be that a liquidator has *no* duty to deal with trust assets.

Liquidators' functions under the UK Insolvency Act 1986

When a compulsory winding up order is made, the primary functions of the liquidator are set out in s.143(1) of the UK Insolvency Act 1986 ("IA 1986"). They are: "... to secure that the assets of the company are got in, realised and distributed to the company's creditors and, if there is a surplus, to the persons entitled to it."

(See, similarly, s.107 in relation to a voluntary winding-up.) Additionally, the liquidator has the function of investigating the causes of the company's failure and, if necessary, reporting wrongdoing to the appropriate authorities (*Re Pantmaenog Timber Co Ltd* [2004] 1 AC 158, [11], [64], [67], [77]).

Under s.144, as part of that duty, a liquidator "shall take into his custody or under his control all the property and things in action to which the company is or appears to be entitled".

In addition to those duties, the liquidator has the "powers" in ss.167, 168, and Schedule 4 of IA 1986. They include (at paragraphs 5 and 13 of Schedule 4) the "power to carry on the business of the company so far as may be necessary for its beneficial winding up" and the "power to do all such other things as may be necessary for winding up the company's affairs and distributing its assets."

It is important to note that these are *powers* and not duties. Indubitably, *if* a liquidator chooses to exercise one of these powers, she will be under a duty to act properly in relation to the exercise of that power. But that does not mean that she is under a *duty to exercise* those powers. The liquidator is entitled not to exercise those powers, if, after due consideration, she does not believe that it would be beneficial for the winding up to do so.

Thus, from the statutory wording, the duties on a liquidator are primarily limited to those in s.143(1), i.e. getting in, realising, and distributing the company's assets. The liquidator also has an additional duty to investigate the causes of the company's failure (which, as explained in *Pantmaenog Timber*, is reflected in various provisions of IA 1986, such as ss.143(2) and 218(3)). However, there is nothing in the statutory wording which extends those duties to dealing with trust assets.

The position of a liquidator can be contrasted with that of an administrator. An administrator is a person appointed under Schedule B1 of IA 1986 "to manage the company's affairs, business and property" (paragraph 1(1)). Under paragraph 59(1), the administrator may do anything necessary or expedient for the management of the affairs, business, and property of the company. Hence, the administrator's duty has been held to include discharging the duties of trustees of a pension fund,[1] and administering statutory 'CASS' trusts for the protection of customers of the business.[2]

The role of an administrator is wider than that of liquidator: an administrator is expressly charged with managing the company's affairs, business, and property, whereas the statute imposes no such duty on the liquidator. This makes sense, because the point of liquidation is to wind down the company's business, rather than revive it.

The *Berkeley Applegate* litigation

That there is no obligation on a liquidator to deal with trust assets is supported by the *Berkeley Applegate* trilogy of cases.

The first decision[3] held that certain assets held by the company (an investment firm in liquidation) were held on trust for clients.

In the sequel,[4] the liquidator applied for payment of his remuneration for administering the trust assets. The judge held that, although there was no statutory basis for remuneration of work done in relation to trust assets (rather than the company's assets), the court had a discretionary jurisdiction to so order, which it then decided to exercise.

The liquidator's remuneration was then considered by Peter Gibson J in *Re Berkeley Applegate (Investment Consultants) Ltd (No 3)* (1989) 5 BCC 803. The beneficiaries argued that the remuneration should come from the company's assets and not the trust assets, on the ground that the liquidator's work in administering the trusts was a necessary part of liquidating a company which held assets on trust. They submitted that the liquidator's remuneration should be treated as expenses "incurred in the winding up" under s.115 IA 1986.[5]

However, the judge rejected this submission (805D-G): *"...it is clear that [s.115] is simply dealing with the winding up of the company, involving as it does the getting in of the assets of the company,*

ascertaining its creditors, paying its liabilities in accordance with the statutory provisions and distributing any surplus. I do not think that on any ordinary reading 'expenses properly incurred in the winding up, including the remuneration of the liquidator' would include expenses and remuneration which the liquidator has incurred and has been awarded by the court in respect of the work he has done administering the trust property held by the company as trustee..."

Thus, the judge's view was that the winding up of the company did *not* include administering trust assets; rather, it involved the getting in of the assets of the company, ascertaining its creditors, paying its liabilities. and distributing any surplus.

Although the point was only considered briefly, *Berkeley Applegate (No 3)* supports the proposition that a liquidator has *no* duty to administer trust assets. Otherwise, the judge would have held the liquidator's remuneration to have been "expenses properly incurred in the winding up."

The view from Australia

In Australia, there is a line of authority which holds that a liquidator has a duty to "act responsibly" in relation to trust assets.[6] It should be noted that in each of these cases the liquidator was arguing he was under a duty, in order to be able to control what happened to the assets in question. Some leading textbooks (in apparent reliance on such case law) also identify the existence of this duty.[7]

The genesis was in *Re Crest Realty Pty Ltd* (1977) 1 NSWLR 664. A bank refused to allow the liquidators of a company to operate a trust account in the name of the company. Needham J recognised (669D) that there was no binding authority on whether the liquidator could operate the account. He held (672F-G) that s.261(1) of the NSW Companies Act 1961[8] places upon the liquidator "the duty to act in a responsible way in the administration of the trust in the name of the company".

However, there are problems with the reasoning in *Crest Realty* (and the subsequent Australian cases).

First, and most importantly, there was no analysis of the distinction between *powers* and *duties*, which (as discussed above) is a key distinction in IA 1986, but which the Australian courts have apparently elided.

Second, the scope of the supposed duty is highly uncertain. In acting "responsibly" in relation to trust assets, is the liquidator obliged to completely step into the shoes of the trustee company (which may involve, for example, investing the assets)? Or does acting "responsibly" entail a lesser duty (e.g. limited to preservation and distribution)? The answer is unclear.

Third, if liquidators did have a duty to administer trust assets, then complying with it would be at the expense of (unsecured) creditors. In a case where a company entered liquidation but had non-trust assets available which the liquidator was able to get in and realise, and which but for having to comply with this alleged duty would be available for the general body of creditors, the costs of complying with this duty would have to be met from those assets. In effect, the creditors would be paying for the liquidator to administer non-company assets. This runs contrary to the liquidator's duty as set out in section 143 IA 1986.

Fourth, at the time of *Crest Realty*, there was no administration regime in either Australia or England. There was therefore no way of contrasting the positions of an administrator and a liquidator, in particular that a liquidator is not under an obligation to manage the company's business, but to collect, realise, and distribute the company's assets. That being the case, it is not clear why a liquidator is obliged to "act responsibly" in relation to trust assets (which, by definition, are not the company's assets available for distribution).

Re Baglan Operations

Recently, in *Re Baglan Operations Ltd* [2022] EWHC 647 (Ch), the English High Court held that the liquidator of a power plant, in exercising his power to continue or discontinue the company's business, could take into account the environment harm from shutting down the plant. Sir Alastair

Norris pointed out that there is a "public protection" aspect to the liquidator's role [47], and also that "beneficial winding up" did not refer purely to financial benefit [52].

Baglan might seem to run counter to our analysis above, since it suggests that liquidators have public functions that extend beyond realising and distributing the company's assets. However, the decision was based on a question of what the liquidator's powers were (not his duties) and the unusual facts of the case (the liquidator was appointed for the express purpose of addressing environment concerns) [46] [55] [56] [59]. It would be a colossal leap to argue from *Baglan* that liquidators generally have a duty to administer trust assets.

Conclusion

Therefore, until there is an authoritative determination (which the court in *Beaufort* declined to give), the correct position under English law appears to be that a liquidator has no duty to administer trust assets. This is corroborated by the wording of IA 1986 and *Berkeley Applegate (No 3)*. The Australian cases, which prescribe a duty to "act responsibly", are not altogether convincing.

Notes:

1 *Polly Peck International Ltd v Henry* [1999] 1 BCLC 407, at [19]-[24]

2 *Re Allanfield Property Insurance Services Ltd* [2015] EWHC 3721 (Ch), at [50]

3 *Re Berkeley Applegate (Investment Consultants) Ltd (in Liquidation)* (1988) 4 BCC 274

4 *Re Berkeley Applegate (Investment Consultants) Ltd* [1989] 1 Ch 32

5 "*All expenses properly incurred in the winding up, including the remuneration of the liquidator, are payable out of the company's assets in priority to all other claims.*"

6 *Re GB Nathan & Co Pty Ltd* (1991) 24 NSWLR 674; *Irvine v Australian Sharetrading and Underwriting Ltd* [1996] 22 ACSR 765; *Porter v Miller Street Pty Ltd* [2008] FCAFC 77

7 McPherson & Keay: Law of Company Liquidation (5th edn. 2021), [9-076]; Sealy & Milman: Annotated Guide to the Insolvency Legislation (24th edn. 2021), under s.144(1).

8 Which provided that, in a creditors voluntary winding up, a person should be nominated "*for the purpose of winding up the affairs of the company*".

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