APPEAL COURT REF NOS. 2014/1822; 2014/1826; 2014/1839

IN THE COURT OF APPEAL (CIVIL DIVISION)

ON APPEAL FROM THE HIGH COURT OF JUSTICE,

CHANCERY DIVISION

COMPANIES COURT (MR JUSTICE DAVID RICHARDS)

IN THE MATTER OF LEHMAN BROTHERS INTERNATIONAL (EUROPE) (IN ADMINISTRATION)

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

BETWEEN:

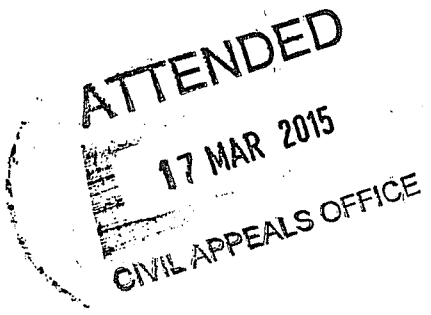
(1) THE JOINT ADMINISTRATORS OF LEHMAN BROTHERS LIMITED (IN ADMINISTRATION)

(2) THE JOINT ADMINISTRATORS OF LB HOLDINGS INTERMEDIATE 2 LIMITED (IN ADMINISTRATION)

(3) LEHMAN BROTHERS HOLDINGS INC

Appellants

-- and --



(1) ANTHONY VICTOR LOMAS

(2) STEVEN ANTHONY PEARSON

(3) PAUL DAVID COPLEY

(4) RUSSELL DOWNS

(5) JULIAN GUY PARR

(In their capacity as Joint Administrators of Lehman Brothers International (Europe) (In Administration)

(6) CVI GVF (LUX) MASTER SARL

(Joined by order of Patten LJ dated 2 September 2014)

Respondents

SKELETON ARGUMENT OF

SIXTH RESPONDENT

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(1) INTRODUCTION

1. This Skeleton Argument is filed on behalf of CVI GVF (Lux) Master Sarl, ("CVI"). It is concerned solely with the appeal, by the Appellants, in respect of paragraph (iii) of the Order of David Richards J dated 19 May 2014, which concerned claims denominated in a foreign currency. [App/C/6]

2. The circumstances which give rise to the relevant issue can be illustrated as follows. A liquidator has paid all proved debts and statutory post-insolvency interest in full, leaving a surplus. For the purposes of proof, claims denominated in US dollars were converted into sterling as at the date of the winding up order. The sterling sums received by creditors with claims in US dollars, if converted into US dollars at the date of payment, were, however, less than the full amount to which they are otherwise entitled, whether by contract, tort or otherwise, given the depreciation in sterling since the date of the winding-up order. A similar issue arises in a distributing administration.

3. The amounts at stake are considerable. The Administrators have estimated that the shortfall to creditors with claims denominated in a foreign currency as against their contractual rights may amount to as much as £1.3 billion. The surplus is estimated to be sufficient to discharge that shortfall in full. The issue is whether, in such circumstances, the surplus is to be applied in discharging the unpaid balance to which such creditors are contractually entitled or is it instead to be distributed to the shareholders.

4. CVI submits that it would be contrary to justice and common sense if a company's assets could be, and were required to be, distributed to shareholders who would receive a £1.3 billion windfall when creditors had not received, and would as a result never receive, the full amount to which they were contractually entitled. It would be even more extraordinary in this case, given that LBIE is an unlimited liability company.

5. David Richards J concluded, not surprisingly, that the surplus is to be applied first in discharging the remaining liability owed to creditors, holding that, in such circumstances, a creditor has a non-provable claim for the unpaid balance, which ranks ahead of any distributions to shareholders; see the Judgment at [88] to [111]. His conclusion was correct. [App/C/4] Permitting or requiring the surplus to be paid to the shareholders, prior to payment in full of such liabilities, would be contrary to the fundamental principles of company and insolvency law and contrary to legislation and to a consistent and longstanding line of authority at the highest level.

(2) FUNDAMENTAL FEATURES OF INSOLVENCY PROCEEDING

6. The fundamental features of a liquidation (or distributing administration) can for present purposes be summarised as follows:

(1) The company's debts and liabilities must be satisfied in full before any assets can be distributed amongst its shareholders.

(2) A liquidation is a process of collective enforcement of provable debts. It is concerned with distributing the assets of the company amongst its creditors in satisfaction of their provable debts.

(3) To enable the company's assets to be distributed pari passu in satisfaction of provable debts, such debts need to be ascertained and valued by reference to a common date and currency of account.

(4) Debts are discharged only to the extent that they are paid out of dividends.

(5) If there is a surplus, after all provable debts have been satisfied in full, it is applied first in payment of post-insolvency interest and then in discharge of any remaining liabilities which were, for whatever reason, non-provable.

(6) In the case of corporate insolvency and unlike in bankruptcy, there is no statutory provision for discharge. The insolvency process leaves the legal rights of creditors unaffected, save to the extent of actual payment. If any liabilities have not been satisfied in full, whether provable or non-provable, the company remains liable but, when all the assets have been distributed, there is nothing more against which the liability can be enforced.

(7) When a company is wound up shareholders are liable to contribute to its assets to any amount sufficient for payment of its debts and liabilities. In the case of a company limited by shares, their liability is limited to the amount (if any) unpaid on their shares. In the case of an unlimited liability company, their liability is unlimited.

(8) If there is a surplus after all debts and non-provable liabilities have been satisfied in full, it is to be distributed amongst its shareholders.

(3) RECENT AUTHORITY

7. In *Wight v Eckhardt Marine GmbH* [2003] UKPC 37 Lord Hoffmann summarised these features at [26] and [27] as follows: [Auth/1C/75]

> *"Winding up is, as Brightman LJ said in Re Lines Bros Ltd [1983] Ch 1, 20, "a process of collective enforcement of debts" ...*
>
> *The winding up leaves the debts of the creditors untouched. It only affects the way in which they can be enforced. When the order is made, ordinary proceedings against the company are stayed ... The creditors are confined to a collective enforcement procedure that results in pari passu distribution of the company's assets. The winding up does not either create new substantive rights in the creditors or destroy the old ones. The debts, if they are owing, remain debts throughout. They are discharged by the winding up only to the extent that they are paid out of dividends. But when the process of distribution is complete, there are no further assets against which they can be enforced. There is no equivalent of the discharge of a personal bankrupt which extinguishes his debts. When the company is dissolved, there is no longer an entity which the creditor can sue. But even then, discovery of an asset can result in the company being restored for the process to continue."*

8. See also for example: *Financial Services Compensation Scheme Ltd v Larnell (Insurances) Ltd* [2006] QB 808 per Lloyd LJ at p.816; *Cambridge Gas Transportation Corpn v Official Committee of Unsecured Creditors of Navigator Holdings plc* [2006] UKPC 26 per Lord Hoffmann at [14] and [15]; and *Parmalat Capital Finance Ltd v Food Holdings Ltd* [2008] UKPC 23 per Lord Hoffmann at [8]. [Auth/1C/78] [Auth/1C/82] [Auth/1C/83]

(4) EFFECT OF THE FUNDAMENTAL PRINCIPLES

9. A creditor whose claim is denominated in a foreign currency is entitled to be paid in that currency. His contract had nothing to do with sterling: he bargained for payment in his own currency and only his own currency; *Miliangos v George Frank ((Textiles) Ltd* [1976] AC 443 per Lord Wilberforce at p.465F-H. [Auth/1B/54]

10. The effect of a liquidation (or distributing administration) on a creditor with a claim denominated in a foreign currency can be summarised as follows:

    (1) The creditor is entitled to prove in respect of his claim and to participate in the process of collective enforcement by which the assets of an insolvent company are distributed *pari passu* amongst its proved debts.

    (2) For the purposes of such *pari passu* distribution and to determine how much he should receive in competition with the other creditors in respect of their proved

claims, the creditor's claim is converted into sterling as at the date of the winding up order.

(3) The creditor's claim is treated as having been paid to the extent of any sums that he receives, for this purpose converting any sterling dividends that he receives into the relevant foreign currency as at the date of payment.

(4) The creditor's contractual right to be paid the full amount of his claim in the foreign currency is not discharged or otherwise affected by the process of collective enforcement of proved debts against an insolvent debtor.

(5) In respect of any part of his contractual entitlement as remains unpaid, the company remains liable to the creditor, and the creditor has a non-provable claim ranking immediately after the payment of all proved debts and post-insolvency interest in full.

(6) The creditor is entitled to payment of such part of his contractual entitlement as remains unpaid out of any surplus before any distributions are made to shareholders.

11. The right to prove a debt in an insolvency process and to receive dividends *pro rata* with other creditors in respect of proved claims, does not amount to a compromise of a creditor's legal entitlement or involve the exchange of such entitlement for a right to prove. That legal entitlement remains untouched, save only to the extent that it is discharged through payment; see *Wight v Eckhardt* at [27]. **[Auth/1C/75]**

(5) THE DISTINCTION BETWEEN PROVABLE AND NON-PROVABLE CLAIMS

12. For the purposes of distributing the debtor's assets in an insolvency process, a distinction is drawn between provable debts and non-provable liabilities. Non-provable liabilities are payable after provable debts and statutory interest: *In re Nortel GmbH* [2013] UKSC 52 at [39]. The distinction between provable and non-provable debts exists for three related main reasons: **[Auth/1C/96]**

(1) The distribution of the company's assets amongst its creditors in respect of their provable debts requires the identification of a cut-off date by which the existence of such claims is to be assessed. As Lord Neuberger said in *Re Nortel GmbH* at [35] "*there* **[Auth/1C/96]**

has to be a cut-off date to determine the class of creditors who are to participate in the distribution of the company's available net assets". Only claims which 'existed', in the required sense, prior to the cut-off date are provable.

(2) A claim may also be excluded from proof on policy or other grounds. Thus, for example, unliquidated claims for damages arising otherwise than by reason of contract or promise were, prior to 1986, not provable in bankruptcy or corporate insolvency, originally because they were regarded as arising from personal wrongdoing by the bankrupt; see *Re T&N Ltd* at [77][1]. [Auth/1C/79]

(3) Certain claims or parts of claims are excluded from proof on the basis that they are regarded as incompatible with the *pari passu* distribution of the debtor's assets in respect of proved debts. Thus, for example, a right to interest under a contract in respect of the period after the date of the winding-up order is not provable.

13. The statutory test for distinguishing between provable and non-provable claims has changed as, over the last three hundred years, the legislature has progressively widened the class of provable debts and narrowed the class of non-provable liabilities. A short summary of the history was given by David Richards J in *Re T&N Ltd* [2005] EWHC 2870 at [76] to [85]. But any claim or part of a claim which does not satisfy the requirements for a provable claim will be a non-provable claim. For example, at present: [Auth/1C/79]

(1) Any liability to which a company becomes subject otherwise than by reason of an obligation incurred before the date on which the company went into liquidation is not provable in a liquidation or distributing administration within r.13.12(1)(b). Prior to the decision in *Re Nortel GmbH* there was, for example, a long line of cases which held that a claim for costs in litigation where the order for costs was only made after the date when the company went into liquidation was not provable; see Lord Neuberger at [87] to [90]. Those authorities dealing with orders for costs have now been overruled. However, it remains the case that where, for example, the liability derives from an obligation under an enactment, r.13.12(1)(b) excludes from proof any debt or liability to which the company became subject after the insolvency date which did not arise by reason of any obligation under an enactment incurred before that date. In *Re Nortel GmbH* Lord Neuberger set out at [77] the requirements which have to be satisfied for [Auth/3/21] [Auth/1C/96]

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1 See also r.12(3)(2) of the Insolvency Rules 1986 (the "1986 Rules") which provides for certain categories of non-provable claims in an insolvency process

an obligation under an enactment to be treated as having been incurred before the relevant cut-off date.

(2) Even following the amendment to the Rules following the decision in *Re T&N Ltd*, unliquidated claims for damages in tort are only provable if "*all the elements necessary to establish the cause of action exist at that date except for actionable damage*"; see r.13.12(2)(b). [Auth/1C/79] [Auth/3/21]

(3) The position in relation to interest in respect of the period after the date of the winding up order is slightly different. Prior to 1986 a right to interest in respect of the period after the winding up order was regarded as a non-provable claim. However, in the event of a surplus after payment of all provable debts, it was payable in priority to any other non-provable claims. The position is now addressed by s.189(2) of the 1986 Act and r.2.88(7) of the Rules. As referred to above, as Lord Neuberger indicated in *Re Nortel GmbH* at [39] post-insolvency interest ranks after all proved debts but before other non-provable liabilities. [Auth/3/20] [Auth/3/21] [Auth/1C/96]

(6) NON-PROVABLE CLAIMS AND MAINTENTANCE OF CAPITAL

14. The consequences of incorporation, limited liability and the eventual dissolution of the company also inform the analysis. It would be contrary to fundamental principles of company law, including the principles relating to maintenance of capital, for the company's assets to be distributed to its shareholders when the company had not satisfied, and as a result of such a distribution would not be able to satisfy, its liabilities in full. This is particularly so where, as in this case, the company is an unlimited liability company, as shareholders would be able to cap their unlimited liability by operation of the insolvency regime. See *Oakes v Turquand* (1867) LR 2 HL 325 at 349-355 and *Ayerst (Inspector of Taxes) v C&K Construction Ltd* [1976] AC 167 per Lord Diplock at p.176F. [Auth/1A/7] [Auth/1B/53]

(7) THE PRIORITY OF NON-PROVABLE CLAIMS TO ANY SURPLUS

15. The treatment of non-provable claims in the event of a surplus after payment of all proved claims, prior to the introduction of the 1986 Act, was clear from the authorities. The authorities established that, in the event of a surplus, creditors are remitted to their rights apart from the insolvency, and such rights are required to be satisfied in full before any distributions are made to shareholders.

16. This makes good sense. If a right has not been fully satisfied through the insolvency process, and a surplus remains, there is no reason why a court would restrain a creditor

whose claim has not been satisfied in full from obtaining or executing judgment against the company.

17. The position can be seen most clearly from the authorities dealing with claims for post-liquidation interest, i.e. interest accruing after the commencement of the liquidation under a pre-liquidation contract which provides for interest to be payable on the debt. The leading authority is the oft-cited decision of the Court of Appeal in *Re Humber Ironworks and Shipbuilding Company* (1869) LR 4 Ch App 643. The judgments deal both with the position where the company is insolvent and unable to pay its proved debts in full and also with the position where there is a surplus: [Auth/1A/12]

(1) Where the company is insolvent, nothing is allowed in respect of interest after the date of the winding up order. Selwyn LJ explaining at p.646-7 that "*I think the tree must lie as it falls; that it must be ascertained what are the debts as they exist at the date of the winding up, and that all dividends in the case of an insolvent estate must be declared in respect of the debts so ascertained*".

(2) The position is different where there is a surplus. In this event, the creditors are remitted to their rights under their contracts. Selwyn LJ said at p.646 "... *I have already guarded myself from being supposed to say that the Court takes upon itself to alter the rights of the creditors to any further extent, or to deprive them of the right they have to interest at the full rate of £20 per cent if and when there is a surplus to pay it*". As Giffard LJ said at p.647, "*as soon as it is ascertained that there is a surplus, the creditor whose debt carries interest is remitted to his rights under the contract ...*". In the event of a surplus, therefore, a creditor is entitled to be paid from the surplus and after payment of all proved debts in full, any post-insolvency interest to which he is entitled under his contract.

(3) Furthermore, the creditor is entitled to calculate the amount of interest which he is owed in accordance with his contractual rights in the ordinary way. This includes being able to calculate the interest owed in accordance with his contractual rights and thus on the basis that any payments, although expressed to have been paid in respect of the principal due on his proved claim, are to be treated in the ordinary way and in accordance with the normal equitable rule as having been appropriated first in payment of any accrued interest.: per Selwyn LJ at p.645.

(4) Such an outcome was regarded as the just one. Selwyn LJ commented at p.645 "*It is satisfactory that in forming that decision we are not fettered by any rule which obliges us to depart from what appears to us to be the justice of the case*".

18. The decision in *Re Humber Ironworks* has been cited and approved by subsequent authority at the highest level, including by the Court of Appeal in *Re Lines Bros Ltd* [1983] Ch 1 and [Auth/1B/57] by Lord Hoffmann in *Wight v Eckhardt* at [23] and [24]. It has never been suggested that its [Auth/1C/75] analysis of what happens to the rights of a creditor in the event of a surplus is incorrect: see, for example, *Re W.W. Duncan & Co* [1905] 1 Ch 307 per Buckley J at p.315 and *Re Fine* [Auth/1A/32] *Industrial Commodities Ltd* [1956] 1 Ch 256 (in which Vaisey J commented at p. 262 that "... [Auth/1A/46] *it seems to me that when the time comes for dealing with the surplus it must no longer be deemed to be an insolvent company, but has to be treated as a company which is, and was, and always has been, solvent*" and referred in support of this at p.263 to the judgment of Giffard LJ in Re Humber Ironworks.

19. The position in relation to other types of non-provable claims was similar. Creditors were entitled to have their claims or the balance of their claims satisfied in full after all proved debts and post-insolvency interest had been paid and before any surplus could be distributed to shareholders. One example concerns the position in relation to future rent under a lease prior to more recent legislative intervention, although the analysis is more complicated. Future rent was regarded as not provable. Nor, prior to the introduction of a statutory power to disclaim, could the company divest itself of its obligations under the lease or convert the landlord's claim into a provable claim for damages. The authorities held that, in the event of a surplus, the lessor was entitled to an injunction restraining the liquidator from making a distribution to shareholders without first making proper provision for his claim to future rent.

(1) In *Gooch v London Banking Association* (1886) 32 Ch D 41 Pearson J, following what he [Auth/1A/21] regarded at p.43 as "*common justice and common sense*", granted an injunction to restrain a company in liquidation from distributing assets among its shareholders without setting aside sufficient assets to provide for future rent and other liabilities under a lease which were non-provable.

(2) The same result was reached by the House of Lords (Scotland) in *Lord Elphinstone v The* [Auth/1A/22] *Monkland Iron and Coal Company Ltd* (1886) LR 11 App Cas 332 where it was held that a lessor could obtain an interdict against the liquidator dividing the surplus among the shareholders until some provision had been made to meet his future claims. Lord

Watson commented at p.336 "*When a limited company is in the course of being wound up voluntarily, I do not think a creditor, who is asserting future or even contingent claims against the company, can justly be said to resort to an extraordinary remedy when he seeks to have the liquidators judicially interpelled from dividing the surplus assets among the shareholders without making any provision to meet his claims when they shall arise*". Lord Herschell L.C. stated at p.344 "*If any liability to the appellant existed on the part of the respondent company, he was entitled to have provision made for it by the liquidators before the assets of the company were distributed among the shareholders*".

(3) In *Re Park Air Services* [2000] 2 AC 172 Lord Millett referred to the old authorities at p.185 and explained that the position changed with the introduction into corporate insolvency of a right to disclaim onerous property by s.267 of the Companies Act 1929. The right is now contained in s.178 of the 1986 Act. A disclaimer extinguishes the lease as between the landlord and the tenant, thereby bringing to an end both the tenant's liability to pay rent and the landlord's right to receive it. Instead the landlord is given a statutory right to prove for the loss or damage which he has sustained in consequence of the operation of the disclaimer. S.178(6) expressly provides that any person who has sustained loss and damage is deemed a creditor of the company and entitled to prove for such loss and damage in the liquidation. [Auth/1B/69] [Auth/3/16] [Auth/3/20]

20. A further example is the decision of Harman J in *Re Islington Metal & Plating Works* [1984] 1 WLR 14 which considered the treatment of claims for unliquidated damages in tort. The Judge held that, under the Companies Act 1948, demands in the nature of unliquidated damages could not be admitted to proof while the company remained insolvent. In a subsequent judgment he dealt with the question whether, once all the company's unsecured creditors had been paid in full, any surplus moneys then in the hands of the liquidators should go to the tort claimants or to the shareholders. He held that it should be paid to the tort claimants, saying at p.24F that he was "*glad to be able to reach this result*" and avoid "*the gross injustice*" which would be caused by ruling out such a claim. [Auth/1B/58] [Auth/3/17]

(8) FOREIGN CURRENCY CLAIMS

21. The authorities in relation to foreign currency claims are less extensive no doubt partly because, prior to the development of international trade and increasing foreign exchange fluctuations, the problem was not a material one, and partly because, prior to the decision of the House of Lords in *Miliangos v George Frank (Textiles) Ltd* [1976] AC 443, it was [Auth/1B/54]

assumed that an English court was not entitled to give judgment for a sum of money expressed in a foreign currency. However, the authorities prior to the introduction of the 1986 Act indicated that a similar approach applied to foreign exchange claims as applied in any other situation in which, as a result of the operation of the rules governing provable claims, the creditor's claim had not been satisfied in full.

22. The treatment of foreign currency claims in the context of the proof of debts in relation to an insolvent company, following the decision of the House of Lords in *Miliangos*, was first considered by Oliver J in *Re Dynamics Corporation of America* [1976] 1 WLR 757. His approach was as follows: **[Auth/1B/55]**

(1) He identified the need for a common unit of account for provable debts: "*It is, of course, necessary in a liquidation, if a proportionate distribution among creditors of the available assets is to be achieved, that the claims of all creditors be reduced at some stage to a common unit of account*" (p.761D).

(2) He referred to the need to value provable claims as at the date of the winding up: "*I take it to be well established that the purpose of both the Bankruptcy Act 1914 and its predecessors, and of the winding up provisions of the Companies Act 1948 and its predecessors, was to ascertain the liabilities of the bankrupt or of the company, as may be, as at the date of the bankruptcy or liquidation, and to secure the division of the debtor's property among the claimants pro rata according to the value of their claims at that date*" (p.761G-H).

(3) He drew an analogy with the position in relation to post-insolvency interest saying that it was no doubt for this reason that: "*a creditor claiming in respect of an interest bearing debt due and payable before the bankruptcy or winding up, cannot, in general, claim interest beyond the date of the bankruptcy or winding up*". In this context he referred to the decision of the Court of Appeal in *Re Humber Ironworks* and quoted a lengthy extract from the judgment of Giffard LJ (p.762C to 763B). Although he was, obviously, concerned solely with provable debts in the context of an insolvent company, he did not suggest that the approach of the Court of Appeal in *Re Humber Ironworks* to a situation where there was a surplus was incorrect.

(4) He explained that such an approach was necessary if a *pari passu* distribution of the assets of an insolvency company was to be achieved: "*It is only in this way that a rateable, or pari passu, distribution of the available property can be achieved ...*" (p.764E-F).

(5) He applied this approach to proofs of debt in respect of foreign currency claims: "*What the court is seeking to do in a winding up is to ascertain the liabilities of the company at a particular date and to distribute the available assets as at that date pro rata according to the amounts of those liabilities. In practice the process cannot be immediate, but notionally I think it is, and, as it seems to me, it has to be treated as if it were, although subsequent events can be taken into account in quantifying what the liabilities were at the relevant date. In the context of a liquidation, therefore, the relevant date for the ascertainment of the amount of liability is the notional date of discharge of that liability and … that date must, in my judgment, be the same for all creditors and it must be "the date of payment" for the purposes of any judgment which has been entered for the sterling equivalent at the date of payment of a sum expressed in a foreign currency*" (p.774G to 775A).

23. Further consideration of such issues was given by the Court of Appeal in *Re Lines Bros* [1983] 1 Ch 1, in circumstances where a liquidator had been able to pay all proved debts in full (for these purposes converting foreign currency claims into sterling at the exchange rate applicable at the date of liquidation, leaving a surplus). The surplus was not, however, sufficient to pay in full both post-insolvency interest and the balance owed in respect of the foreign currency claims. The creditor challenged the liquidator's approach to the admission of foreign currency claims to proof. Its argument was, in essence, that the practice of converting foreign currency claims for the purposes of proof at the date of the commencement of the liquidation was, following the judgment of the House of Lords in *Miliangos*, now incorrect. It argued, in short, that, in the light of that judgment, *pari passu* distribution of the assets of an insolvent company required, in effect, a re-calculation of the relative value of such claims as at the date of each dividend payment. [Auth/1B/57] [Auth/1B/54]

24. The argument was rejected, the Court holding that the old practice of converting foreign currency claims for the purposes of proof by reference to the exchange rate as at the commencement of the liquidation was correct.

(1) Lawton LJ stated at p.14F-G "*Ever since Re Humber Ironworks and Shipbuilding Co., LR 4 Ch App 643 it has been the practice to value the fund as at the date of liquidation. I can see no reason why a different date should be fixed merely because one or more of the liabilities is stated in a foreign currency*".

(2) Brightman LJ also referred to *Re Humber Ironworks* and also to *Re WW Duncan & Co* and explained at p20F that liquidation is "… *akin to execution because its purpose is to enforce, on a pari passu basis, the payment of the admitted or approved debts of the company*".

(3) Brightman LJ also justified this approach on the basis that the policy underlying the decision in *Miliangos,* that the foreign currency debtor should not be entitled to impose on the foreign currency creditor the risk of a fall in the value of sterling, did not apply where a company was insolvent and creditors were in competition with each other (p.16C-G). It was on this basis that he concluded that claims for post-insolvency interest should also have priority (p.21G-H).

(4) Oliver LJ's judgment was to the same effect saying that "*... the submission to proof of a foreign debt is part of the statutory scheme of collective enforcement and thus subject to the same universal rule for ascertainment and quantification as any other debt*" (p.24F-G).

25. The court also considered the position in the event of a surplus. Brightman LJ dealt with this at p.20H to 22A, having made it clear at the start of his judgment that this was a separate issue:

(1) He referred to the principle that, in the event of a surplus, creditors are remitted to their contractual rights: "*... when the problem arises for decision, it may be relevant to observe that the view has repeatedly been expressed in relation to interest that once the provable debts have been satisfied in full, so that the company has in that sense a surplus of assets, the duty of the liquidator is to discharge the contractual indebtedness of the company in respect of such debts to the extent that the contractual indebtedness exceeds the provable indebtedness. '[A]s soon as it is ascertained that there is a surplus, the creditor whose debt carries interest is remitted to his rights under his contract ...' per Giffard LJ in In Re Humber Ironworks and Shipbuilding Co., LR 4 Ch App 643, 647; and Selwyn LJ to the same effect, at p.645*" (p.21D-E).

(2) He suggested that, given this, a liquidator may be under a duty to make good the shortfall before distributing the surplus: "*It may well be the duty of the liquidator, in the case of a wholly solvent liquidation, if a foreign currency creditor has been paid less than his full contractual currency debt, to make good the shortfall before he pays anything to shareholders*" (p.21F-G).

Oliver LJ, whilst also making it plain that the point should be left open for decision, said that certainly for his part he did not dissent from the proposition that the answer in a solvent situation may well be found in the way suggested by Brightman LJ (p.26F).

26. The decision of the Court of Appeal in *Re Lines Bros* has also been cited and approved by subsequent authority at the highest level, including by Lord Hoffmann in *Wight v Eckhardt* [Auth/1B/57] [Auth/1C/75]

at [26] and in *Cambridge Gas* at [15]. It has never been suggested in any of the cases that Brightman LJ's analysis of the position in the event of a surplus is incorrect. [Auth/1C/82]

(9) THE SCOPE OF THE PARI PASSU RULE

27. The Appellants submit that that payment of the surplus in discharge of the unpaid part of any foreign currency claims would amount to a breach of the *pari passu* rule.

28. The submission is misconceived. The *pari passu* rule is the rule that assets of a company are applied *pro rata* in respect of its provable debts. The rule is not infringed by the existence, in the event of a surplus, of a non-provable claim for the unpaid balance of any currency conversion claim ranking after payment of all provable debts in full and before any distribution to shareholders, any more than it is infringed by the existence of a right to payment of post-insolvency interest in similar circumstances.

(10) THE EFFECT OF THE 1986 ACT AND RULES

29. The enactment of the 1986 Act and Rules did not change any of the fundamental features of a liquidation referred to above or affect the position of non-provable claims including any unpaid part of a foreign currency claim, although it codified certain matters.

30. Three potentially relevant changes that were made were as follows:

    (1) The dividing line between provable and non-provable claims was changed once more so as to enlarge still further the scope of provable claims. Most significantly, claims for unliquidated damages in tort were made provable, provided, as initially enacted, that the cause of action had accrued prior to the date on which the company went into liquidation; see r.13.12(2) prior to its amendment in 2006. However, the fact that actionable damage is an essential ingredient of a cause of action in tort meant that, even after the introduction of the 1986 Act, many tort claims still continued to be non-provable even under the new regime, as Sir Donald Nicholls V-C explained in *Re Kentish Homes* [1993] BCLC 1375 at p.1382. [Auth/3/21] [Auth/1B/61]

    (2) The position in relation to post-insolvency interest was expressly dealt with in s.189(2) (for liquidations) and r.288 (for administrations). The rules codified the existing law that the surplus is, before being applied to any other purpose, to be applied in paying any post-insolvency interest to which a creditor was otherwise entitled. However, it [Auth/3/20] [Auth/3/21]

also changed the law by providing that post-insolvency interest was also payable out of the surplus on provable debts which did not accrue interest, thereby remedying the injustice identified as long ago as 1869 by Giffard LJ in *Re Humber Ironworks* at p.648. [Auth/1A/12] It also provided that the rate of interest payable was the greater of the rate applicable apart from the insolvency and the rate specified in s.17 of the Judgments Act 1838. [Auth/3/5]

(3) The requirement to convert foreign currency claims into sterling as at the date of the insolvency for the purposes of proof was reflected in r.4.91 (liquidation) and r.2.86 [Auth/3/20] [Auth/3/20] (administration). This was statutory confirmation of the decisions of Oliver J in *Re* [Auth/1B/55] *Dynamics Corpn* and of the Court of Appeal in *Re Lines Bros* in relation to the proof of [Auth/1B/57] foreign currency claims against an insolvent company.

31. Subject to such matters, the 1986 Act and Rules did not make any changes in relation to the fundamental features of an insolvency, to the relative ranking of provable and non-provable claims, or to the entitlement of a creditor to be satisfied in full before any surplus was distributed to shareholders.

32. The Cork Report, in the context of considering amendments to the regime as regards [Auth/4/9] interest, made specific reference to the fact that once there is a surplus the company is treated as being no longer insolvent with the result that "*the creditor who is entitled to interest on the debt for which he has proved may recover the interest accruing after the presentation of the winding up petition as if there had been no winding up at all*" [1384].

33. So far as creditors with a claim denominated in a foreign currency are concerned, r.2.86(1) [Auth/3/21] expressly provides that it operates "*For the purpose of proving a debt incurred or payable in a currency other than sterling*". The rule takes effect for, but only for, the purpose of giving effect to creditors' rights in the insolvency; see *Finance Services v Larnell* per Lloyd LJ at [Auth/1C/78] p.816. It does not alter the fundamental fact that corporate insolvency leaves the debts unaffected, merely having the effect that when the assets are distributed there is nothing left against which the liability can be enforced.

34. In *Re Barings (No.6); Hamilton v Law Debenture Trustees Ltd* [2001] 2 BCLC 159 Morritt V-C [Auth/1B/72] held at [34] to [37] that post-liquidation exchange rate losses would be payable in priority to any payment to the holders of perpetual notes.

35. The position in the event of a surplus of a creditor with a non-provable claim for damages in tort following the introduction of the 1986 Act was expressly considered by David Richards J in *Re T&N Ltd*: [Auth/1C/79]

(1) He held that the effect of r.13.12, as originally enacted, was that a creditor with a claim for unliquidated damages in tort could only prove if his cause of action had accrued by the date of the commencement of the insolvency. [Auth/3/21]

(2) He rejected a suggestion that the 1986 Act had changed the position of creditor with a non-provable claim, such that the surplus might now be capable of being distributed to shareholders so as to leave them unpaid. He said at [107] "*It would indeed be extraordinary if a company's assets could be, and were required to be, distributed to shareholders without paying tort claims which had accrued since the liquidation date, or other claims not provable in a liquidation, such as costs incurred in litigation against the company before the liquidation date but not then the subject of an order. In my judgment that is not the position if there is a surplus which would otherwise be distributed to shareholders, I see no reason why the court would not give leave to a tort claimant to obtain or execute judgment*"[2].

36. The position is the same in relation to any other claims or parts of claims which are not provable and in respect of which the creditor has not been satisfied in full by the process of collective execution in respect of provable debts. Even after the introduction of the 1986 Act there remain, as explained above, various possible categories of claims which are not provable. One example is a liability pursuant to an enactment which by the cut-off date did not satisfy the requirements identified by Lord Neuberger in *Re Nortel GmbH* at [77] to have constituted an obligation incurred prior to that date. The fact that it was not provable would not make it any less a liability of the company, as and when it eventually arose, which, if the company had not gone into insolvency proceedings, it would have had to pay. [Auth/1C/96]

(11) LAW COMMISSION AND CORK REPORT

37. The Appellants submit that the Law Commission and the Cork Report both recommended, however, that foreign currency claims should be converted into sterling as

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2 The position of creditors with claims in tort was subsequently altered. R.13.12(2) was amended by r.4 of the Insolvency (Amendment) Rules 2006 (SI 2006 No. 1272) which amended the Rules to provide that a claim for damages in tort is provable provided that "*all the elements necessary to establish the cause of action exist at that date except for actionable damage*". [Auth/3/23]

at the date of winding up and argue that they intended that this should remain the position even where one was dealing with a surplus after payment of all proved debts and post-insolvency interest. This is incorrect.

38. First, the Law Commission went out of its way to emphasise, both in its Working Report No.80 and also in its Final Report published in October 1983, that in its view the present law was satisfactory. Thus, for example: [Auth/4/8] [Auth/4/11]

    (1) The conclusion in the relevant section of its Final Report at [3.37] was that "*The present law relating to the conversion into sterling of foreign currency claims in relation to solvent and insolvent companies and to bankruptcy is satisfactory*". The previous paragraph of its report expressly referred to the decision of the Court of Appeal in *Re Lines Bros.*

    (2) Part VI of its Summary of Conclusions and Recommendations stated at [6.2(8)] that "*The present law relating to the conversion into sterling of foreign currency claims in relation to solvent and insolvent companies and to bankruptcy is satisfactory*".

39. The Law Commission could not conceivably have concluded that the present law relating to the conversion into sterling of foreign currency claims in relation to solvent and insolvent companies was satisfactory, whilst at the same time thinking that Brightman LJ was incorrect in *Re Lines Bros* to suggest that any creditor with a foreign currency claim was entitled to have his claim satisfied in full before any surplus was distributed to shareholders. [Auth/1B/57]

40. Secondly, the Appellants have misunderstood the relevant passages from the reports of the Law Commission. Although the relevant passages, read in isolation, are perhaps not as clear as they might be, the question that was being addressed was whether, if it turned out that a company was solvent, a different regime should be adopted for the admission of proofs, such that the assets would then be required to be distributed *pari passu* amongst the provable debts converted by reference to the exchange rate at the date of payment rather than at the date of the winding up order. The Law Commission considered that such an approach would not be desirable. There is nothing inconsistent with this and Brightman LJ's suggested approach in the event of a surplus after all proved debts and post-insolvency interest has been paid.

41. The discussion and conclusion in the Cork Report is to similar effect. At [1309] the report stated that "*We are firmly of the view that the principles stated in the two most recent cases provide an* [Auth/4/9]

appropriate solution to the problem of the conversion of foreign money claims into sterling in the context of insolvency proceedings". Although the two cases are not identified by name, it is noteworthy that the Report was published in June 1982, some four months after the Court of Appeal had delivered judgment in *Re Lines Bros.* The reference was plainly intended to be to *Re Dynamics Corp* and to that case.

42. Thirdly, whatever may have been the views of the Law Commission and the authors of the Cork Report, the 1986 Act and Rules did not alter the position, and this conclusion is confirmed by the approval in subsequent authorities of, for example, the decisions in *Re Humber Ironworks* and *Re Lines Bros.*

(12) COMPARISON WITH RULES RELATING TO FUTURE AND CONTINGENT CLAIMS AND SET-OFF

43. The Appellants submit that r.2.86 causes the mandatory conversion of the foreign currency debt into sterling and renders the sterling equivalent of the debt provable in the administration of the company, such that subsequent payment of the proved – sterling – sum together with statutory interest satisfies the creditor's claim. In effect, they submit, the Rules effect a mandatory compromise such that, in exchange for his contractual rights, the creditor obtains instead a right to prove and receive payment of a sum equal to that amount converted into sterling as at the date of the winding up order. [Auth/3/21]

44. This is contrary to the basic principle that corporate insolvency leaves debts and liabilities unaffected, merely having the effect that when the assets are distributed there is nothing left against which the liability can be enforced.

45. The Appellants seek to support their submission by reference to the rules governing the proof of future and contingent claims. They submit that the rules relating to future and contingent claims have a substantive effect, such that payment of the discounted and estimated value of such debts is payment of those debts in full, and that r.2.86 has a similar substantive effect.

46. This is incorrect. The rules governing future and contingent debts operate only so far as necessary for the purposes of proof and, save to that extent, do not otherwise affect the substantive rights of creditors. The basic position in relation to the proof of future debts is as follows:

(1) R.2.105(2) provides, similarly to r.2.86, that "*for the purposes of dividend (and no other purpose)* ..." the amount of the creditor's admitted proof is discounted in accordance with the statutory formula. [Auth/3/21]

(2) The effect of this rule was considered by the Court of Appeal in *Re Kaupthing Singer & Friedlander Ltd* [2010] EWCA Civ 518. The case concerned the operation of r.2.85 (Mutual credits and set off) and r.2.105 (Debt payable at a future time). Some of the depositors had loans from the insolvent bank, in excess of their deposits, which were repayable at a future date. R.2.85 required the respective claims and cross-claims to be set off against each other. For these purposes it also provided in r.2.85(7) that "*Rule 2.105 shall apply for the purposes of the Rule in relation to any sum due to or from the company*". The creditor argued that the bank's claim in respect of the future loan had to be discounted and then set-off against its liability in respect of the deposits. Having done this, the creditor argued, the bank would be left with a claim for the net discounted balance of its loan on which no interest would be payable, although this balance would only be payable when the loan fell due for repayment in the future. This was said to be the necessary consequence of the clear wording of the Rules and the substantive effect of insolvency set-off as described in *Stein v Blake.* [Auth/1C/85] [Auth/3/21] [Auth/3/21] [Auth/3/21] [Auth/1B/66]

(3) The Court of Appeal rejected this argument. It held that the proper approach was to discount only such part of the loan as was required to effect the set-off, leaving the balance undiscounted and payable to the company in future with interest as previously provided for under the contract. Etherton LJ stated at [34] that "*I see no difficulty in the circumstances in reading the words 'for the purposes of this Rule in r.2.85 as confining the effect of the incorporation of r.2.105 to what is necessary to calculate what should be paid by way of dividend to the creditor and, for that purpose, the making of the insolvency set-off, and as not touching at all upon what remains due to the company after the insolvency set-off has taken place*". In other words, the rules were applied so far as was necessary for the purposes of proof and no further; see Etherton LJ at [36] and [37].

47. The basic position in relation to contingent claims is as follows:

(1) R.2.81 provides for the administrator to estimate the value of any debt which, by reason of it being subject to a contingency or for any other reason, does not bear a certain value, and for the amount provable to be the estimate for the time being. [Auth/3/21]

(2) R.2.81(1) further provides that the administrator can revise any estimate previously made if he thinks fit by reference to any change in circumstances. As Lord Hoffmann explained in *Wight v Eckhardt* at [32] the "*cases on the use of hindsight to value debts which were not contingent at the date of the winding up order show that the scene does not freeze at the date of the winding up order. Adjustments are made to give effect to the underlying principle of pari passu distribution between creditors*". The creditor cannot, however, interfere with past dividends and, if all the assets have already been distributed, then it will be too late to revise any estimate. [Auth/3/21] [Auth/1C/75]

48. There is nothing in these Rules or in previous authority that suggests that the process of discounting or estimating for the purposes of proof and receipt of dividends constitutes a compromise of the creditor's rights, such that payment of the discounted or estimated amount constitutes, as a matter of law, satisfaction in full of his legal rights, as opposed to satisfaction of his right to participate in the insolvency and receive distributions *pari passu* in respect of his proved debt, nor that they should have any effect wider than strictly necessary for that purpose; compare the Judgment at [77].

49. Future and contingent claims obviously raise a further aspect which needs to be mentioned. A company is entitled to wind up its affairs and distribute its assets within a reasonable period and to be dissolved. It cannot be required to wait until all future debts have fallen due and all contingencies have occurred. That would not be a liquidation, but merely a run-off. Given this, if creditors with future or contingent claims choose to participate in the process, it necessarily follows that their claims will have to be discounted to present value and estimated. If they choose not to participate, they run the risk of the liquidator being permitted to distribute any surplus to shareholders and being left with no assets against which to execute their claims; see *Stanhope Pension Trust Ltd v Registrar of Companies* [1994] 1 BCLC 628 and *Re Danka Business Systems plc* [2013] Ch 506. [Auth/1B/65] [Auth/1C/91]

50. These factors are, however, irrelevant in the context of foreign currency claims, where the existence of any unpaid balance will necessarily be apparent by the time that payment of proved debts is made in full and before any distribution of the surplus is made to shareholders. The existence of a non-provable claim for any shortfall, ranking after all proved debts and post-insolvency interest and before any distribution to shareholders, is therefore not inconsistent with the entitlement of a company to wind up its affairs within a reasonable period.

51. In any event, recognising such a foreign currency claim is entirely consistent with the approach taken to a contingent claim, the value of which can continue to be revised at least until all the assets have been distributed. As Patten LJ commented in *Re Danka Business Systems plc* [2013] EWCA Civ 92 at [38]: [Auth/1C/91]

> " ... *if the contingency does occur pre-distribution to members and so creates an actual liability of the company which the liquidator has not provided for then it would obviously be open to the creditor (absent agreement) to lodge an additional proof out of time which in a solvent liquidation the liquidator would have to deal with.*"

This would not prevent the value of a contingent claim from being revised between the date of payment of the last dividend on proved debts and any distribution of a surplus to shareholders. See also *Stanhope Pension Trust Ltd v Registrar of Companies* [1994] 1 BCLC 628 per Lord Hoffmann at p.634g-h, who referred at p.634h to the possibility that a creditor might be entitled to prove for an accrued debt when the contingency only occurred after the conclusion of the winding up. [Auth/1B/65]

52. The Appellants also seek to support their submission that r.2.86 compromises the underlying rights of a creditor with a foreign currency claim, by referring to r.2.85 dealing with set-off which, they submit, also has a substantive effect. The Appellants' reliance on r.2.85 does not assist them: [Auth/3/21] [Auth/3/21]

(1) *Stein v Blake* [1996] 1 AC 243 held that, on a bankruptcy, a claim and cross-claim were mandatorily set-off against each other, with the result that all that was assignable was the amount due after the set-off had occurred. To this extent, as Lord Hoffmann said at p.251D-E it "*affects the substantive rights of the parties by enabling the bankrupt's creditor to use his indebtedness to the bankrupt as a form of security*". [Auth/1B/66]

(2) As the Court of Appeal made clear in *Re Kaupthing Singer & Friedlander Ltd*, the rules relating to set-off are however applied so far as is necessary for the purposes of proof and no further. Thus the fact that r.2.85(6) required all future claims to be discounted, before being set-off, did not have the effect of changing the parties' substantive rights in respect of any balance over and above the amount required for the purposes of the set-off. This is apparent from r.2.85(8) itself. [Auth/1C/85]

(3) The claim and cross-claim in that case were, however, both denominated in sterling. *Stein v Blake* was not concerned with the relationship between set-off and foreign currency claims. As David Richards J held at [102] to [104], there is no reason why the [Auth/1B/66]

effect of the rule should be materially different than it is in relation to future debts. Thus, for the purposes of the set-off required by r.2.85, the foreign currency claim is converted into sterling as at the date of the winding-up and the relevant claim and cross-claim are set-off. There is no reason why, subject only to the effect of such set-off, the creditors' rights should otherwise have been affected. If a creditor with a claim denominated in a foreign currency has not been paid in full, he should have a non-provable claim for the shortfall whether or not part of his claim has been the subject of insolvency set-off.

(4) The argument that the effect of insolvency set-off as described in *Stein v Blake* was to create a new cause of action in respect of the balance which did not carry any of the contractual characteristics of the original underlying claim was raised by a Respondent's notice before the Court of Appeal in *Kaupthing, Singer & Friedlander* and specifically rejected at [36] and [37]. [Auth/1C/85]

53. In any event, even if the rules governing the proof of future and contingent debts and insolvency set-off to some extent have substantive effect, that effect only extends as far as is necessary for the purpose of the relevant rule. The application of those rules does not determine whether and if so to what extent and in what circumstances r.2.86 dealing with foreign exchange claims has substantive effect, let alone require that any claim denominated in a foreign currency is treated as having been converted into sterling at the date of the winding up order so as to convert the creditor's underlying legal rights into a claim solely in respect of that sterling sum, let alone to do so once and for all and irrevocably.

(13) NOTIONAL COLLECTION AND DISTRIBUTION ON DAY 1

54. The image of collecting and *uno flatu* distributing the assets of the company on the day of the winding up does not mean that the conversion of foreign currency claims into sterling required by r.2.86 is necessarily for all purposes and all times. As Lord Hoffmann explained in *Wight v Eckhardt* at [29] the image is applied "*to give effect to the underlying purpose of fair distribution between the creditors pari passu and not as a rigid rule*". If the image was applied literally it would necessarily follow, for example, that no creditor would be entitled to post-insolvency interest. Despite this the Court of Appeal in *Re Humber Ironworks* both identified the image that the tree must lie as it falls, whilst at the same time holding that creditors reverted to their strict legal rights in the event of a surplus. [Auth/1C/75]

55. Nor does such a conclusion follow from the fact that winding up has been described as a collective process of enforcement:

(1) It is correct that in *Miliangos* the House of Lords held that, for practical reasons, if a judgment in a foreign currency requires to be enforced, the relevant amount will need to be converted into sterling as at the date that enforcement is ordered. But it does not follow that the converted amount will be treated as discharging the foreign currency liability irrespective of any further movements in exchange rates between the date of the order for enforcement and the date of receipt by the creditor. [Auth/1B/54]

(2) In any event it would be wrong to treat the date of the winding up order as equivalent for all purposes to the date of order for execution referred to in *Miliangos*. The process of collective enforcement represented by a liquidation or distributing administration is a process of collective enforcement of provable debts. Such an approach would also represent a triumph of form over substance, given that the period between a winding up order and the payment of any dividends is almost always likely to be substantially greater than that which arises on an ordinary order for execution.

(14) APPLICATION OF THE RULES IN A SOLVENT LIQUIDATION

56. R.4.1 provides that Chapter 9 of the Rules dealing with proof of debts in a liquidation apply wherever, and in the same way as, they apply in a creditors' voluntary winding up. The effect of this is that the rules relating to, amongst other things, estimating claims (r.4.86), set-off (r.4.90), foreign currency claims (4.91) and future debts (4.94) also apply in a solvent liquidation. This is, as explained above, a necessary consequence of the fact that a company is entitled to wind up its affairs and distribute its assets within a reasonable period and to be dissolved, and that this applies whether it is insolvent or solvent. The rules relating to discounting future claims, estimating contingent claims and set-off are all, to some extent, necessary to achieve this. Thus, if such rules did not exist, you would be unable to have a liquidation and dissolution of the company, but would instead be limited to a run-off. [Auth/3/21] [Auth/3/21]

57. The rules operate in the same way for a members voluntary liquidation as they do for a creditors' voluntary liquidation or winding up by the court, and do not operate any further than is necessary to achieve their purpose.

58. In a voluntary winding up the court may stay or restrain proceedings against the company by exercise of its powers under s.112 of the 1986 Act. However, where all provable debts have been paid in full and there is a surplus otherwise available for shareholders, there is no reason why a court would restrain a creditor whose claim had not been satisfied in full from obtaining or executing a judgment; see *Re T&N Ltd* at [107]. The statutory regime relating to members voluntary liquidations is not intended to permit or to require the assets of the company to be distributed amongst its members when there remain creditors whose debts or liabilities have not been satisfied in full. [Auth/3/20] [Auth/1C/79]

59. The effect of the Appellants' case is that a company, and its shareholders, could, by causing the company to go into a members' voluntary liquidation, become entitled to pay the sterling equivalent as at the date of the resolution to wind up and, in the event of any depreciation in sterling between the date of the resolution to wind up and eventual payment, avoid having to bear the effect of such depreciation, contrary to the contractual obligations of the company and even if this results in creditors ultimately receiving less than the full amount to which they are entitled under their contracts.

60. Such consequences would be contrary to the fundamental principles of company and insolvency law and would enable a debtor and its shareholders to benefit from insolvency. This is particularly so where the company is an unlimited liability company, as is the case with LBIE.

(15) APPELLANTS' ARGUMENTS ON THE MERITS

61. The Appellants raise various arguments on the merits to try and justify why the surplus should be distributed to members rather than applied first in discharge of any debts or liabilities of creditors which have not been satisfied in full. Unless the Appellants' arguments can in some way be limited so as to apply solely in respect of foreign currency claims, they will inevitably give priority to shareholders over all non-provable claims[3].

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[3] Thus, for example, if the company incurred an obligation under an enactment the day after the date of the winding up, such as not to be provable in accordance with the decision in *Re Nortel GmbH* **[Auth/1C/96]** the consequence of distributing any surplus to members would be that such statutory liability would never be discharged, although the company remained liable to pay it and had sufficient assets to do so. Certain of the Appellants' arguments therefore seek to focus solely on the merits as they specifically relate to foreign exchange claims. In effect, such arguments are used to try and justify, contrary to the fundamental features of the insolvency process and authority, construing r.2.86 as converting the creditor's underlying legal rights into a claim for the sterling equivalent at the date of the winding up order and doing so for all purposes, once and for all and irrevocably.

62. The Appellants' main argument is that the contrary conclusion would effectively provide the creditor with a one-way bet[4] against the company or its members (and, when the members are insolvent, the members' creditors). David Richards J rejected the one-way bet argument at [96] to [98]. He was correct to do so.

63. The suggestion that creditors with claims in a foreign currency have been provided with a one-way bet is incorrect:

(1) The creditor never agreed to take the risk of exchange rate fluctuations; that is why his claim is denominated in the foreign currency rather than sterling. The risk of any depreciation in sterling, following the date of the winding up order, should be borne by the debtor which is the defaulting party, not by the creditor who never agreed to bear that risk.

(2) Nor can it sensibly be said that the creditor faces a one-way bet if the company is insolvent. In that situation the creditor will inevitably suffer a shortfall on his claim. Furthermore, if sterling has depreciated since the winding up order, the extent of his shortfall will be increased. Thus, for example, in *Re Lines Bros* the sterling denominated creditors received 100% of their sterling claims, whilst the Swiss Franc denominated creditors received only 58.775% of their Swiss Franc claims; see at p.10B. Indeed, it was for this reason that the bank argued that to satisfy the pari passu rule all claims, following *Miliganos*, should be converted into sterling only at the date of payment. If the company is insolvent, foreign currency creditors bear not merely an insolvency risk but also an exchange rate risk. To hold that, if there is a surplus, they are entitled to payment of the unpaid balance of their claim, does not create a one-way bet. Instead, it merely partially, but not wholly, remedies the exchange rate risks that the creditor has otherwise been forced to bear. In the present case, for much of the administration and until relatively recently the Administrators' reports continued to indicate an expected shortfall.

[Auth/1B/57]

[Auth/1B/54]

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[4] The Appellants' suggestion that there is a one-way bet against the company is potentially misleading. So far as the company's other creditors are concerned, as Brightman LJ explained in *Re Lines Bros*, [Auth/1B/37] any claim would rank for payment only after payment of all proved debts and post-insolvency interest, as the other creditors did not agree to assume and should not be required to bear the exchange rate risk. The issue, to the extent it arises, is between creditors with claims denominated in foreign currencies and shareholders. In this respect, as David Richards J commented at [98], "*individual creditors may not achieve their full contractual rights when they are in competition with other creditors, but there is no justice in them not doing so when they are in competition with the debtor*".

(3) Nor can it sensibly be said that the position is unfair if the company was always and is plainly solvent. The statute permits shareholders to wind up the affairs of a solvent company and dissolve the company. To the extent that this necessarily involves ignoring, to the limited extent referred to above, the legal rights of creditors, it is neither unfair nor unjust if they are required to bear the risk of a depreciation in sterling after the date of the liquidation. At worst, this is no more than the price of exercising the statutory jurisdiction. Nor, indeed, is it one that members need necessarily bear. If they do not want to bear the exchange rate risk, there is nothing to prevent them from discharging such claims by payment of the relevant foreign currency sum prior to going into liquidation.

64. The Appellants argue that, if they are wrong, difficulties may arise in applying the Rules. There is nothing in any of these points for the reasons given by David Richards J at [99] and [105]. The working out of such issues is to form part of a further hearing before David Richards J, referred to as Waterfall II).

65. David Richards J was therefore correct to have concluded that currency conversion claims rank in LBIE's administration as non-provable liabilities, payable only after the payment in full of all proved debts and post-insolvency interest and before any distributions to members, and the Appellants' appeal in this respect should be dismissed. The contrary conclusion would be contrary to fundamental principles of company and insolvency law and to long-standing authority at the highest level. It would also be wrong to provide the members of LBIE, who agreed to accept unlimited liability, with a windfall of some £1.3 billion, despite creditors of LBIE not having received the full amount to which they are contractually entitled.

ROBIN DICKER Q.C.

South Square

RICHARD FISHER

Gray's Inn

CHARLOTTE COOKE

Amended 17 March 2015