

**IN THE SUPREME COURT OF GIBRALTAR**

**Case No:2019/COMP/002**

**BETWEEN:**

IN THE MATTER OF ELITE INSURANCE COMPANY LIMITED  
(IN ADMINISTRATION)

AND IN THE MATTER OF THE INSOLVENCY ACT 2011

AND IN THE MATTER OF THE INSOLVENCY RULES 2014

Mr Tom Smith QC and Raymond Triay (instructed by Triay & Triay)  
for the Applicants

**JUDGMENT**

**RESTANO J:**

**Introduction**

1. Edgar Lavarello and Dan Yoram Schwarzmann in their capacity as Joint Administrators of Elite Insurance Company Limited (In Administration) (“Elite”) have made an application for directions on the operation of the rules of insolvency set-off contained in the Insolvency Act 2011 (“the Act”). The application was heard on 1 July 2020 by way of a remote hearing which I directed following a request made by the Applicants on the grounds that the application raised a novel point of law which warranted the appearance of specialist London Leading Counsel whose attendance in court would have not have been practicable given the ongoing difficulties with international travel due to the Covid-19 pandemic.
2. The application has been made under section 71(2)(e) of the Act and the Joint Administrators seek a direction as to the correct

interpretation of sections 135 to 140 of the Act as they apply to administrations under the Act and which they say means that the rules of insolvency set-off are engaged from, and the account for set-off purposes is taken as at the date on which the statement of distribution of dividend is issued to creditors. Alternatively, they seek directions confirming that it is appropriate for the Applicants to treat the rules contained in sections 135 to 140 of the Act as modified pursuant to the power under section 72(2) of the Act to the same effect.

3. The application is supported by the witness statement of Edgar Lavarello dated 23 June 2020 which sets out the background to the application and which can be summarised as follows: Elite was authorised to carry on various types of insurance business in several countries until 1 February 2019 when its authorisation to conduct insurance business was withdrawn. The Company was placed into administration in Gibraltar on 11 December 2019. On 9 February 2020 the Joint Administrators issued their proposals for achieving the purposes of administration which were approved at a meeting of creditors on 3 April 2020. As part of their investigations, the Joint Administrators have been considering the impact that the rules of insolvency set-off might have on claims which are made by Elite against creditors or on claims by creditors against Elite. The investigations have resulted in the Joint Administrators establishing that at least one party currently holds multiple 'After the Event' insurance policies with Elite which means that money may become due to, or due from Elite in relation to various policies. The Joint Administrators have also established that Elite carried out significant insurance business in France and that this book of business is such that there is a significant possibility that mutual debts, credits and other mutual dealings exist between Elite and other insurance undertakings which might be said to be amenable to set-off. It is therefore a matter of significant practical importance that the Joint Administrators understand

how the rules of set-off are intended to operate in an administration under the Act.

#### The statutory framework

4. Sections 135 to 140 of the Act come under the heading “liquidation and bankruptcy” and contain the rules on insolvency set-off. In particular, section 135 contains the core provision which provides as follows:

(1) This section applies where before the relevant time there have been mutual credits, mutual debts or other mutual dealings between a debtor and a creditor claiming or intending to claim for a debt in an insolvency proceeding.

(2) Subject to section 136 and subsections (3) to (6) –

(a) where this section applies, an account shall be taken of what is due from each party to the other in respect of the mutual dealings, and the sum due from one party shall be set-off against the sums due from the other party; and

(b) only the balance, if any, of the account owed

(i) To the creditor may be claimed in the insolvency proceedings; or

(ii) To the debtor shall be paid to the liquidator or bankruptcy trustee, as part of the assets of the debtor.

5. The “relevant time” as referred to in section 135 (1) of the Act is defined in section 2 of the Act both for liquidations and administrations. In the case of a liquidation not preceded by an administration, the relevant time is the commencement of the liquidation. This means that wherever there have been pre-liquidation dealings with a company which has gone into liquidation, an account is automatically taken and set-off occurs. This allows the insolvent debtor’s creditor to use his indebtedness to the debtor as a form of security and instead of having to prove with other creditors for the whole of his debt in the insolvency, he can set off pound for pound what he owes the

company in the liquidation and prove for or pay only the balance: *Stein v Blake* [1996] AC 243, 251. The position under English law is materially the same: see Rule 14.25 of the English Insolvency Rules 2016 (“the English Rules”).

6. Section 72 of the Act extends the above rules to administrations and states as follows:

72 (1) The administrator of a company may make a distribution

- (a) to a secured creditor or a preferential creditor without the leave of the Court; and
- (b) to any other creditor, with the leave of the Court.

(2) Where the administrator makes a distribution under subsection (1), sections 135 to 140 and sections 198 to 208 apply with such modifications as may be specified in the Rules or, to the extent that modifications are not so specified, with such modifications as are appropriate.

7. Rule 14.24 of the English Rules deals with set-off in administrations in England & Wales and insofar as this is material, it provides as follows:

(1) This rule applies in an administration where the administrator intends to make a distribution and has delivered a notice under rule 14.29.

(2) An account must be taken as at the date of the notice of what is due from the company and a creditor to each other in respect of their mutual dealings and the sums due from the one must be set off against the sums due from the other.

...

### Submissions

8. Mr Smith submits that the set-off rules in administrations are similar in Gibraltar and in England & Wales in that insolvency set-off does not apply immediately upon a company’s entry into administration but only comes into play if and when it becomes a distributing administration, specifically when the

administrator has delivered a notice of intention to make a distribution to creditors. The English Rules, however, specifically identify the set-off date as the date when the set-off account is taken. The English regime therefore makes it clear that the account is taken at the date of notice of intention to distribute, and is not backdated to the date of commencement of the administration or some other point. Mr Smith points out that the analogue provision in Gibraltar (section 135(2)(a) of the Act) does not specify when the taking of the account should take place only “that an account shall be taken of what is due from one party to the other in respect of the mutual dealings”. In particular, it does not refer to the account being taken “as at the date of the notice” as provided for in rule 14.24(2) of the English Rules.

9. Mr Smith further submits that the Act’s failure to expressly specify that the set-off account must be taken at the set-off date may well be because the insolvency set-off rules which apply to liquidations and bankruptcies aimed at realising and distributing assets are extended to administrations by virtue of section 72(2) of the Act with such modifications as may be appropriate. This is to be contrasted with the position in England & Wales where there is a specific statutory scheme catering for administrations.
10. In Mr Smith’s submission, despite this omission the most logical and straightforward combined reading of sections 2, 72 and 135 of the Act is that the set-off account should be struck when the administrator makes a distribution. Indeed, he submits that there are many practical and conceptual difficulties with a set-off account in an administration being taken at an earlier stage such as the commencement of the administration rather than when administrators make a distribution. In particular, if the set-off date is backdated to the commencement of the administration, this would have the effect of freezing positions and could well prevent the administrator from trading or selling receivables and rescuing the company as a going concern which

is one of the statutory objectives of administration: see section 46 of the Act. This is supported by Lightman and Moss on the *Law of Administrators and Receivers of Companies*, (6<sup>th</sup> ed., Sweet & Maxwell) at paragraph 22-079 which states that the emphasis in administrations is on the rescue of a company as a going concern unlike liquidations which concern terminal insolvency proceedings aimed at the realisation and distribution of assets. Thus, if mandatory and self-executing set-off applied at the commencement of the administration in relation to all debts (including prospective and contingent debts) that might serve to undermine ongoing trading and the objective which lies behind administrations.

### Analysis

11. Whilst there is no express statement in the Act that a set-off account must be taken when a distribution is made in an administration, in my view a combined reading of the relevant provisions makes it plain that this is the case. Section 135 is only triggered when an administrator makes a distribution within the meaning of section 72(2) of the Act. Where section 135 has effect, it applies where there have been mutual dealings pre-administration and an account must be taken of what “is due” in respect of those pre-administration dealings. This means that only those pre-administration debts which remain due as at the date from which section 135 has effect (i.e. the date of distribution) are included in the set-off account. This means that the legislative intention must have been for the set-off account to be struck when the administrator makes a distribution to creditors, more specifically the date when a statement of distribution of dividend is issued to creditors in accordance with rule 118 of the Insolvency Rules 2014 (“the Rules”).
12. This construction is consistent with the emphasis on rescue in administrations as it means that the set-off rules are only engaged once the administrator has concluded that the rescue of

the company is not possible and that the administration should be used instead to make distributions to creditors. Were the set-off rules to apply at an earlier date, it would have the effect of freezing positions for example under running accounts or hedging agreements which might then prevent the administrator from being able to continue to trade and which would be at odds with the aims of administration.

### Jurisdiction

13. The Applicants have made this application pursuant to section 71(2)(e) of the Act which provides that an administrator of a company may “apply to the Court for directions in respect of the administration of the company”. This jurisdiction is materially the same as the power to give directions under English law (see paragraph 63 of Schedule B1 to the English Insolvency Act 1986) and which has been recognised as being expressed in very wide terms.
  
14. In *Re Lehman Brothers International Europe* [2013] EWHC 1664 (Ch) the English High Court granted an application for directions made by the Joint Administrators of Lehman Brothers International Europe confirming that they could perform their obligations under a settlement agreement with the trustee appointed in the United States for the liquidation for Lehman Brothers Inc. That, however, was a slightly different sort of case as it concerned obtaining the court’s blessing for the performance of an agreement entered into by the Joint Administrators and not the determination of a point of statutory construction. In *Lehman Brothers International (Europe) (In Administration) v Burlington Loan Management Limited and others* [2015] EWHC 2269 (Ch) an application for directions was made for the purposes of clarifying the entitlement of creditors to interest on their debts pursuant to rule 2.88 of the Insolvency Rules 1986 for periods after the commencement of

the administration of Lehman Brothers International Europe. In my view, the circumstances which gave rise to that application are more akin to the present application in that they both involved the resolution of a point of statutory construction. Further, I do not consider that there is any objection in principle why this application should not be entertained. Although this application is wide in its terms in that it seeks clarification on a general question of statutory construction, it concerns one which affects the running of this administration and I therefore consider that it falls within the scope of the directions jurisdiction contained in section 71(2)(e) of the Act.

15. This application has proceeded without any creditor or debtor being notified about this application. Mr Smith submits that whilst two books of business have been identified as being affected by the way in which the rules of insolvency set-off operate, the far-reaching nature of the direction sought means that there are a large number of creditors who could potentially be affected by this application and that it would not have been practicable to proceed in any other way. In my view, this means that any interested party who wishes to challenge this judgment should have the opportunity to do so in due course and the order to be drawn up consequent on this judgment should provide for that.

### Conclusion

16. I consider that the rules of set-off contained in sections 135 to 140 of the Act apply in an administration where the administrators first make a distribution under section 72 (1) of the Act. Further, properly construed these provisions mean that the account for set-off purposes is taken as at the date on which the statement of distribution of dividend is issued to creditors in accordance with rule 118 of the Rules.

17. For the reasons given above, the order to be drawn consequent of this judgment should reflect the fact that I grant liberty to



apply so that creditors or debtors of Elite should have the opportunity to challenge this decision should they so wish. Further, the Joint Administrators should use their best efforts to bring this judgment to the attention of Elite's creditors and debtors.

**Mr Justice Restano**  
**Puisne Judge**

Date: 8 July 2020