Neutral Citation Number: **[2020] EWHC 2839 (Ch)**

Case No: **CR-2017-006113**

**IN THE HIGH COURT OF JUSTICE**
**BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES**
**INSOLVENCY AND COMPANIES LIST (ChD)**

Royal Courts of Justice, Rolls Building
Fetter Lane, London, EC4A 1NL

Date: **22 October 2020**

**Before** :

**Mrs Justice Falk**

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**Between :**

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| **The Official Receiver** | **Claimant** |
| **- and -** | |
| **(1) Sunetra Atkinson (DISCONTINUED)** | **Defendants** |
| **(2) Camila Batmanghelidjh** | |
| **(3) Erica Jane Bolton** | |
| **(4) Richard Gordon Handover** | |
| **(5) Vincent O'Brien** | |
| **(6) Francesca Mary Robinson** | |
| **(7) Jane Tyler** | |
| **(8) Andrew Webster** | |
| **(9) Alan Yentob** | |

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**Lesley Anderson QC and Gareth Tilley** (instructed by **Womble Bond Dickinson (UK) LLP**) for the **Claimant**
**Rupert Butler and Natasha Jackson** (instructed by **Leverets**) for the **Second Defendant**
**Daniel Margolin QC and Daniel McCarthy** (instructed by **Joseph Hage Aaronson LLP**) for the **Third Defendant**
**George Bompas QC and Catherine Doran** (instructed by **Bates Wells**) for the **Fourth and Sixth to Ninth Defendants**
**Andrew Westwood** (instructed by **Maurice Turnor Gardner LLP**) for the **Fifth Defendant**

Hearing date: **22nd October 2020**

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# RULING

**Mrs Justice Falk** **Thursday, 22 October 2020**
(**3:30** pm)

Ruling by **MRS JUSTICE FALK**

1. This is my decision on the defendants' challenge to certain of the submissions in the Official Receiver's skeleton argument, namely whether the Official Receiver should be permitted to allege that specified loan repayments were preferences voidable under section 239 Insolvency Act 1986 and that there were breaches of duty under sections 172, 173 and 174 Companies Act 2006, being the duty to promote the success of the company, the duty to exercise independent judgment and the duty to exercise reasonable care, skill and diligence.

2. The Official Receiver makes a single allegation against all the defendants that they caused and/or allowed Kids Company to operate an unsustainable business model, an allegation which is supported by a series of particulars set out in the report. Nothing in the report contains an allegation that section 239 was engaged or that there were any specific breaches of duty. So far as the defendants are concerned, these are allegations raised for the first time in the skeleton argument served two weeks before the start of the hearing.

3. The particular relevance of these matters is that, if they are made out by the Official Receiver, they are matters to which the court must have regard under Schedule 1 to the Company Directors Disqualification Act 1986 (the "CDDA"): see section 9 and paragraphs 1 and 8 of Schedule 1 (as in force at the relevant time).

**The legal principles**

4. The starting point is rule 3 of the Insolvent Companies (Disqualification of Unfit Directors) Proceedings Rules 1987. That provides for evidence in support of an application for disqualification, in the form of one or more affidavits (or a report in the case of the Official Receiver), to be filed with the application. Rule 3(3) provides that the affidavit or report must include a statement of the matters by reference to which the respondent is alleged to be unfit to be

concerned in the management of a company. In this case the relevant parts of the report complying with rule 3(3) are paragraphs 8 to 11 of Mr Hannon's first report.

5. This requirement in rule 3(3) obviously reflects both good practice and indeed the requirements of natural justice and fairness. A disqualification order involves penal consequences, and the defendants must know and have proper notice of the case they have to meet: see the comments of the Sir Nicholas Browne-Wilkinson VC in *Re Lo-Line Electric Motors Ltd* [1988] (Ch) 477 at pp 486-487, which were discussed further by Dillon LJ in *Re Sevenoaks Stationers (Retail) Ltd* [1991] (Ch) 164 at pp176-177. As Lewison J said in *Secretary of State for Trade and Industry v Goldberg* [2003] EWHC 2843 at [51], the substance of the case that the defendant is required to meet must be set out. In *Re Grayan Building Services Ltd* [1995] (Ch) 241 Hoffmann LJ also commented at p253 that it is the conduct specified under rule 3(3) with which the court is solely concerned.

6. So, the starting point is that the Official Receiver is limited by reference to the allegations in his report. However, each of the Vice Chancellor, Dillon LJ and Lewison J in the cases just mentioned recognised that this is not an immutable rule. The court has a discretion to allow the Official Receiver to add further allegations or change their nature, provided that can be done without injustice to the accused director. Whether that is possible depends on the circumstances of the case, but it might be the case, for example, if proper notice has been given or an adjournment can be allowed to permit any further evidence to be obtained.

7. Having proper notice of the case to be met includes, in particular, an opportunity to produce evidence in the light of that knowledge. It must be borne in mind that, as a Part 8 claim, there are no pleadings. In essence the report and the other affidavit evidence relied on by the Official Receiver is all the defendants have to go on. So, just as pleadings must mark out the parameters of the case advanced, identify issues and the extent of the dispute and make clear the general nature of the case, so must the report. It must set out the essential facts relied upon.

8. I would add to this that pre-action correspondence between the parties provides relevant context. In addition, any response to a Part 18 request for further information is obviously relevant.

9. It is also worth bearing in mind that the Official Receiver will have had access to or power to obtain significant documentation during the investigation phase. The normal rules for disclosure of documents do not apply and, furthermore, the Official Receiver has an opportunity to file a second report in response to the defendants' evidence, in which allegations made can be modified or added to.

10. The nature of the procedure means that caution is required in determining whether the court should exercise its discretion to allow additional or altered allegations: see *Goldberg* at 56, where Lewison J concluded, having regard to the nature of disqualification proceedings, that he should be cautious before allowing a change in the thrust of the allegations as originally set out.

11. Furthermore, where dishonesty is alleged, that allegation must be made fairly and squarely: *Goldberg* at 53. I also accept that where, as here, the allegation as understood was framed as one of incompetence, rather than want of probity, it would be particularly unfair to allow changes to be made which engage the question of probity without proper notice. Among other things, if the director had been aware at an earlier stage that such an allegation or series of allegations might be made, then it might have affected his or her decision whether to fight the case or to provide a disqualification undertaking, which, as I will note later, potentially has different implications to a finding by a court of the matters alleged. In any event, it could certainly affect the evidence that he or she wishes to adduce.

12. It is also worth referring to the discussion of the principles to apply by Laddie J in *Re Finelist* [2004] BCC 877 at [17] to [19]. In particular, he emphasised the importance of being able to ascertain with clarity what are the criticisms and also on what evidence the applicant intends to rely, rather than the applicant making general allegations which require the respondent to put forward his

own account, and then relying on that to try to support the case for a disqualification order, (citing on that point *Re Sutton Glassworks Ltd* [1996] BCC 174, 176).

13. I should address one further preliminary point. Section 9 CDDA provides that the court shall have regard to the matters contained in Schedule 1. In my view this does not require the court to look beyond the matters before it. The court is required to determine only those issues that are properly before the court. If, for whatever reason, the Official Receiver has not properly placed before the court a particular matter to which it says the court should have regard, then it is not for the court to choose for itself to make findings on those issues.

14. I note that there is some consideration of this point in *Mithani on Directors' Disqualification* at Div III, Chapter 2, paragraph 349, footnote 8, by reference to what appears to be an unreported case, with the suggestion that the court can have regard to a particular matter referred to in the Schedule (that is, Schedule 1 to the CDDA) if the charge brought against the defendant relates directly or indirectly to that matter. However, I am not persuaded that the "directly or indirectly" language, even if correct, would permit the court to have regard to matters that, for reasons of procedural fairness or otherwise, are not in fact properly before it.

**The Official Receiver's position**

15. In summary, the Official Receiver's position is that there would be no procedural unfairness in allowing him to seek to establish breaches of duty, or that there were voidable preferences. The Official Receiver does not resile from the single allegation that has been made and accepts that establishing these additional matters is neither necessary nor sufficient to establishing unfitness: see *Goldberg* at [27], citing the *Barings* decision in the Court of Appeal (*Baker v Secretary of State for Trade and Industry* [2001] BCC 273 at [35]).

16. However, the single allegation in this case is supported by a number of particulars. In practice that means that there are multiple individual allegations, albeit that the Official Receiver accepts that,

unless the central allegation of causing or allowing the operation of an unsustainable business model is made out, his case will fail.

17. What Ms Anderson, for the Official Receiver, says that the Official Receiver is seeking to do is to emphasise or enhance those particulars. There is, she says, no attempt to introduce new facts, no additional documents would be required not currently before the court and, to the extent that the defendants wish to give evidence-in-chief in respect of those matters, there would be no objection to them doing so. She points out that there was also advance notice in the form of a skeleton argument served in advance of the trial, and she makes the point that it is not the case that all legal submissions must be reflected in the Official Receiver's report.

**General observations**

18. I will start with some general observations. It is stating the obvious to say that this is a very substantial case, which has involved an enormous amount of work on all sides. The Official Receiver conducted a lengthy investigation over many months, and instigated proceedings over three years ago on the basis of reports totalling over 600 pages in length and with very extensive exhibits. A further report was filed in March this year in response to the defendants' evidence. In total, the Official Receiver has had more than five years since the company's collapse to formulate its case.

19. These are very significant proceedings for the defendants in many respects. They are not normal adversarial proceedings but proceedings with potentially penal consequences which may significantly impact their reputations and indeed livelihoods. They are no doubt very stressful and involve significant personal, not to mention at least potential financial, cost. It is entirely appropriate for the court to be cautious and Ms Anderson rightly accepted that.

20. The Official Receiver's case has been founded on a single allegation of causing and/or allowing Kids Company to operate an unsustainable business model. Further, an express confirmation was given in a letter written by the Official Receiver's solicitors on 7 July 2017, shortly before the

proceedings commenced, to Bates Wells, at that stage acting for all the defendants other than the second and fifth defendants, in which it was stated that it was not suggested that there was a want of probity on the part of the Bates Wells' clients or any allegation of dishonesty or self-serving conduct on their part.

21. Prior to the Official Receiver's skeleton being served there had been no allegation of breach of any statutory duty or any allegation that there were preferences that were voidable under section 239. There has been no good explanation of why such matters were not raised earlier, if they were to be relied on.

22. The defendants have prepared their cases over many months on the basis of the single allegation and a clear understanding that there was no allegation of want of probity or any allegation of breach of statutory duty or voidable preference. Indeed, they will have made an important decision, whether to fight the case or to provide a disqualification undertaking, on the basis that they were facing that single allegation, supported by the particulars as stated in the report. Their affidavit evidence has also been prepared on that basis.

23. I agree with Mr Margolin's observation that multiple allegations of breach of duty does have a different look and feel to the single allegation previously made, albeit supported by the particulars as mentioned, an allegation which was understood to be one of incompetence and not something suggesting want of probity or breach of particular duties. Describing the additional allegations as an enhancement to the particulars does not, in my view, properly address that point.

24. There was nothing to prevent the Official Receiver from including in the report specific allegations of breach of duty or voidable preference to which, if the court finds the allegations are made out, it must have regard under Schedule 1 to the CDDA. I do not accept that these matters should simply be left to legal submissions, rather than being reflected in the report. The Official Receiver can and indeed must set out the essential facts relied on and the allegations, being the matters by reference to which the defendants are said to be unfit.

25. It is worth noting that in *Re Pinemoor Ltd* [1997] BCC 708 Chadwick J gave guidance at p710 that care should be taken to distinguish between facts that can be established by direct evidence, inferences which the court is invited to draw from those facts, and matters which are said to amount to unfitness; in other words, all those matters ought to be set out.

26. If, as here, the Official Receiver wishes to ask the court to have regard to specific breaches of duty or preferences pursuant to section 9 and Schedule 1 CDDA, then in my view that should be made clear. That, as I understand it, is standard practice and I consider that it properly reflects the provisions of the legislation, the nature of the proceedings and rule 3(3). It is not simply a matter for legal submissions, as I think Ms Anderson had to recognise in accepting that the defendants should be given an opportunity to give evidence in respect of them. The requirement is to set out the substance of the case.

27. It is also not a sufficient answer to offer an opportunity to examine the defendants in-chief on these issues. I do not consider that that addresses the points I have already made about the case for which the defendants have prepared over a lengthy period and have decided to come to court to defend.

**Preferences: section 239 Insolvency Act**

28. Although the loan repayment to Ms Atkinson in December 2014 is referred to in the report and can obviously be relied on as a factual matter, the report contains no allegation of any preference in relation to that payment. The Official Receiver has now rightly accepted that such an allegation cannot be advanced in respect of that payment, and that the effect of this is that no allegation in respect of preference can be made against Mr O'Brien, who resigned before the date on which the further payments relied on as preferences were made.

29. The Official Receiver has also now accepted that, in light of the responses to the Part 18 request made on her behalf, no allegation in respect of preferences will be maintained against Ms Bolton.

30. The allegation against the other defendants relates to loan repayments made in April 2015 and is made in the report in the following terms, namely (and reading from paragraph 9.6) that the directors:

> "... caused or allowed payments to connected persons to a value of £150,000 and to unconnected persons to a value of £400,000, in preference to the general body of unsecured creditors of Kids Company."

There are similar references elsewhere in the report, including, in particular, paragraph 11.6.

31. I should perhaps clarify that, as against defendants other than Mr O'Brien and now Ms Bolton, the Official Receiver can maintain the allegation as stated in the report, namely that the defendants chose to pay particular creditors in preference to others. The question is whether he can maintain that the transactions were voidable under section 239.

32. Nothing in the report addresses the requirement in section 239(5) that:

> "The court shall not make an order under this section ... unless the company which gave the preference was influenced in deciding to give it by a desire to produce ... the effect mentioned in subsection (4)(b)."

The effect so mentioned is that the relevant creditor is put in a better position in the event of the company going into insolvent liquidation.

33. Under section 239(6) the existence of such an influence is presumed unless the contrary is shown in relation to preferences given to connected persons. Although the report does refer separately to connected and unconnected persons, it draws no distinction between them in this respect and it refers to no evidence to suggest that there was in fact any such desire, which the Official Receiver would have to demonstrate positively in the case of unconnected persons. It is also inaccurate in terms of the requirements of the Act because it assumes that Mr O'Brien was connected when in fact he was not at the date of the relevant repayment, because he had resigned on 31 March 2015 (see section 249 for the relevant definition).

34. The Official Receiver's analysis accompanying the report in relation to preferences is far from definitive, simply suggesting that, as compared to some of the payments, a challenge to the

December 2014 onward connected party transactions would "appear to have more of a chance of success".

35. I do not accept Ms Anderson's submission that it would not have been possible to make any allegation in respect of section 239(5) in the report. The Official Receiver should have set out his contention that section 239 applies and, if appropriate, acknowledge that he is relying on inference, rather than facts that can be established by direct evidence. That is also consistent with the need for the case to be presented fairly and in a balanced way: see *Re Finelist* at [19]. The defendants would then have had a proper opportunity to respond to that allegation in their evidence and, if appropriate, the Official Receiver could then have responded to that, either by withdrawing the allegation or challenging the defendants' evidence.

36. In the circumstances, I am not persuaded by the Official Receiver's submissions that there would be no injustice in permitting the Official Receiver to seek a finding that there were voidable preferences.

37. It is notable that the Official Receiver was asked for clarification about the position on section 239 more than once in pre-action correspondence, and never confirmed that he was alleging that section 239 was engaged. On my reading of the correspondence, the defendants were not properly put on notice. The correspondence uses language similar to that contained in the report or, in the case of the final letter I was shown before the proceedings commenced, the letter sent on 7 July 2017 already referred to, simply says that the fact that preferential payments were made was a consequence of the business model. That does not come close to an allegation that section 239 applied. There has been no further reference to it, including none in the second report produced in response to the defendants' evidence.

38. I accept that the question of preference is addressed to some extent in the defendants' evidence. But that was not done with reference to the requirements of the key ingredient set out in section 239(5).

39. As already indicated, I do not think it is appropriate to allow the point to be dealt with as oral evidence-in-chief, particularly in light of the pre-action correspondence and the defendants' understanding of what the Official Receiver was alleging.

40. In the circumstances, therefore, I do not think it would be fair to allow the question of voidable preferences under section 239 to be raised now.

**Breaches of statutory duty**

41. As already mentioned, the Official Receiver seeks to rely on section 172 Companies Act 2006, which is the duty to promote the success of the company; section 173, the duty to exercise independent judgment; and section 174, the duty to exercise reasonable care, skill and diligence.

42. The question of breach of duty was, like the question of preferences, also raised in pre-action correspondence, although only on behalf of Mr O'Brien. His solicitors specifically raised the issue of breach of duties and set out his position in some detail, including in relation to the specific provisions of the Companies Act now relied on.

43. The Official Receiver's solicitors chose not to engage with this, despite the clear statements by Mr O'Brien's solicitors that he had not breached any of the duties and that there was no allegation in the correspondence that he had breached any particular duty.

44. Section 172 raises particular concerns as far as all the defendants are concerned, because it is an allegation of breach of fiduciary duty and, as such, carries a flavour of lack of probity, stigma or moral taint and in most, although I accept not all, cases, involves a want of good faith. Honest mistakes are not ordinarily caught by section 172 because the benchmark it sets is one of acting in a way the director considers, in good faith, would be most likely to promote the success of the company. It is of particular concern that in places the Official Receiver's skeleton appears to suggest that there was a deliberate flouting of responsibilities to creditors.

45. In the circumstances, and bearing in mind the case the defendants have prepared to meet, I do not consider that it would be just to allow the Official Receiver to seek to rely on a breach of section

172. Not only does it raise or at least appear to raise a question of probity, but it is also of questionable relevance to the allegation that the Official Receiver continues to maintain as the single allegation, namely causing or allowing the operation of an unsustainable business model.

46. In essence, it moves away from an allegation understood to be one of incompetence to one that would at least be perceived as being qualitatively different, and potentially encompassing something more than incompetence.

47. I am also very conscious that there are difficult questions as to exactly how section 172 might operate in this case. Not only is the law still developing on the question of exactly how creditors' interests should be taken into account where a company is or is likely to become insolvent – see *BTI 2014 LLC v Sequana SA* [2019] BCC 631 at [222] – but there is the added question of whether it makes a difference that Kids Company was a charitable company, where the focus is ordinarily on its charitable purposes rather than the interests of members, and also the question of whether a mistaken but honest belief as to priorities as between charitable purposes and creditors might be treated differently from a deliberate flouting of rules, or at least from an action that is not in good faith.

48. These difficulties present another reason why the court, in my view, should not be drawn into making findings that are not strictly necessary to determine the allegation made. This is particularly the case where the evidence has not been prepared with reference to those issues.

49. As far as section 174 is concerned, the position is somewhat less acute because it is not a question of breach of fiduciary duty, with the connotations and consequences that that may involve. Furthermore, the test in section 174, with its objective and subjective elements which look at the general knowledge, skill and experience that may reasonably be expected of any director, and also the general knowledge, skill and experience that the particular director has, are clearly of some relevance in determining unfitness for disqualification purposes: see, for example, the discussion in

*Walters and Davis-White, Directors' Disqualification and Insolvency Restrictions*, 3rd edition, in chapter 5, for example, at 5-74 and 5-76.

50. However, ultimately the test to be applied is one of unfitness and not whether the relevant director acted with care and skill. As Ms Anderson recognised, a finding of breach of that duty is neither necessary nor sufficient. Furthermore, an allegation of a breach of section 174 is not clearly relevant to the single allegation made in this case as put by the Official Receiver. The Official Receiver's report makes no allegation of any such breach.

51. In addition, whilst perhaps not involving the same level of stigma as a breach of fiduciary duty, the allegation still involves an allegation of breach of statutory duty, and as such is significant and qualitatively different to the allegation as previously put and understood.

52. In the case of the fifth defendant, Mr O'Brien, who is a chartered accountant and also regulated by the Financial Conduct Authority, the concern was also raised by his counsel that a finding of breach of statutory duty might give rise to immediate regulatory or disciplinary issues.

53. In the circumstances, I have concluded that it would not be appropriate to seek to prevent any party referring the court to the tests in section 174, because of their potential relevance to the question of unfitness. But I have concluded that it would be unfair to allow the Official Receiver to ask the court to make findings that there have been breaches of section 174 in circumstances where he has not made those allegations on a timely basis, in a way that gives the defendants a proper opportunity to consider their position and to respond.

54. I do not accept that there has been no unfairness on the basis that the allegation of incompetence that has been made implies something worse than negligence. An allegation of incompetence is not necessarily the same as an allegation of failure to exercise reasonable care.

55. In relation to section 173, unlike section 174, this can be regarded as an aspect of directors' fiduciary duties and indeed is specifically acknowledged as such in section 178(2) Companies Act. In that respect, at least to some extent, it also carries a flavour of lack of probity.

56. I take Ms Anderson's point that part of the Official Receiver's case has always been that the trustee defendants deferred too much to Ms Batmanghelidjh and the defendants have had the opportunity to respond to that case, so, in that respect, there would be no unfairness.

57. However, I do not accept that that is the same as an allegation of a breach of section 173. To take one example, it is not necessarily a failure of independent judgment to reach the conclusion that delegation to a particular individual should occur or to take a decision about the particular level of supervision or interference that is appropriate.

58. Finally, in relation to all the alleged breaches of duty, I have also taken into account the possibility that, if the court were asked to and did make findings of breach of duty, that might potentially expose the defendants to civil liability in respect of those breaches in a way that would contrast with the position were the defendants to have accepted disqualification undertakings. As I understand it, such undertakings are generally given in terms which do not permit reliance on the matters accepted by the defendant for purposes unrelated to the disqualification legislation.

**Conclusion**

59. In conclusion, for reasons of procedural fairness, I have decided that the Official Receiver is not permitted to seek findings of breaches of sections 172, 173 or 174 of the Companies Act 2006, or that there were preferences voidable under section 239 of the Insolvency Act.