**Trinity Term**
**[2016] UKSC 30**
*On appeal from: [2015] CSIH 12*

# JUDGMENT

# Brown and another, the Joint Administrators of Loanwell Limited (Respondents) *v* Stonegale Limited (Appellant) (Scotland)

# Brown and another, the Joint Administrators of Oceancrown Limited (Respondents) *v* Stonegale Limited (Appellant) (Scotland)

# Brown and another, the Joint Administrators of Questway Limited (Respondents) *v* Pelosi (Appellant) (Scotland)

**before**

**Lord Neuberger, President**
**Lord Sumption**
**Lord Reed**
**Lord Carnwath**
**Lord Hodge**

## JUDGMENT GIVEN ON

## 22 June 2016

**Heard on 15 February 2016**

*Appellant*
Alan Summers QC
David Massaro
(Instructed by Halliday Campbell WS)

*Respondents*
Kenneth McBrearty QC
Susan Ower
(Instructed by Pinsent Masons LLP)

**LORD REED: (with whom Lord Neuberger, Lord Sumption, Lord Carnwath and Lord Hodge agree)**

1. These three conjoined appeals concern section 242 of the Insolvency Act 1986, as amended. Where section 242(1) applies, and a company enters administration, an alienation by the company is challengeable by the administrator. In terms of section 242(2), section 242(1) applies where by the alienation, any part of the company's property is transferred or any claim or right of the company is discharged or renounced, and the alienation takes place on a relevant day as defined by section 242(3) (that is to say, within a specified time before the date when the company enters into administration). In terms of section 242(4), on a challenge being brought under subsection (1), the court shall grant decree of reduction or for such restoration of property to the company's assets or other redress as may be appropriate, but the court shall not grant such a decree if the person seeking to uphold the alienation establishes that it was made for adequate consideration.

2. These proceedings were brought under section 242(1) by the joint administrators of Oceancrown Ltd, Loanwell Ltd and Questway Ltd, in respect of alienations made by each of those companies of four properties in Glasgow during November 2010, nine months before the companies went into administration. The alienations took place on relevant days as defined. The administrators are the respondents to the present appeals.

*The facts*

3. The facts, as found by the Lord Ordinary, are as follows. Oceancrown and the other companies in administration were part of a group of companies controlled by Ralph Norman Pelosi ("Mr Pelosi senior"). He was the beneficial owner of their shares, the sole director of Oceancrown and Loanwell, and a shadow director of Questway. He was also the 99% owner (subsequently 100%) of another company, Strathcroft Ltd. The nominal director of that company was John Anderson. Norman Ralph Pelosi ("Mr Pelosi junior") was the sole shareholder and director of a further company, Stonegale Ltd. He is the appellant in one of the appeals, and Stonegale is the appellant in the others.

4. A secured facility in the region of £17.3m had been made available to Oceancrown by Anglo-Irish Bank. The other companies in the group had cross-guaranteed the debt. Oceancrown owned a commercial property at 278 Glasgow Road, Rutherglen. It also owned properties at 110 and 260 Glasgow Road. Loanwell

owned a property at 210 Glasgow Road. Questway owned a property at 64 Roslea Drive, Glasgow. The bank held standard securities over each of these five properties.

5. Mr Pelosi senior had concluded an agreement with Clyde Gateway Development Ltd for the sale of 278 Glasgow Road for £2,467,500 inclusive of VAT: a sum far in excess of an earlier valuation of the property at the sum of £762,000. Subsequent events were, in the Lord Ordinary's words, "machinations designed to protect the 'profit' on the sale of number 278" (para 44), by keeping it out of the hands of the bank.

6. On 19 August 2010 Robert Frame, a solicitor of Miller Becket and Jackson ("MBJ"), a Glasgow firm of solicitors, wrote to the bank's solicitor, Mr Gillespie of McClure Naismith, in relation to the release of the properties from the bank's securities, giving "details of the properties and the relevant sale price". According to the details stated, the sale price of 278 Glasgow Road was £762,000; the sale price of 110 Glasgow Road was £200,000; the sale price of 210 Glasgow Road was £934,000; and the sale price of 260 Glasgow Road was £450,000. Mr Gillespie was subsequently informed that 64 Roslea Drive was also to be sold, at a price of £68,000. The total sale price of the five properties, as stated, was £2,414,000. Mr Gillespie passed this information on to the bank, and prepared discharges of the standard securities. These were duly executed by the bank, and Mr Gillespie was authorised to deliver them to MBJ in exchange for the free proceeds of sale. In reality, as explained earlier, the actual sale price of 278 Glasgow Road was £2,467,500, and no sales had been agreed in respect of the other properties.

7. On 10 November 2010 Oceancrown disponed 278 Glasgow Road to Strathcroft. The consideration was recorded in the deed as being £762,000. On the same day, Strathcroft disponed the same property to Clyde Gateway for £2,467,500. Mr Frame witnessed the execution of both dispositions. The Lord Ordinary found that "Strathcroft was involved in the whole matter only in order to provide a short-lived intermediary between Oceancrown and Clyde Gateway. … It was a cog in Mr Pelosi's machine" (para 47).

8. On 16 November 2010 Mr Frame received a letter signed by Mr Anderson on behalf of Strathcroft, authorising MBJ to send the bank the sum of £2,414,000 "in respect of purchases of [the five properties]". Mr Frame transmitted the money as instructed. Once the bank received the funds, the executed discharges were delivered. The Lord Ordinary found that "the money was paid to MBJ then to the bank on the instructions of Mr Pelosi senior. Strathcroft had no real involvement in that" (para 47). He also found that "the bank was misled in relation to the funds it received" (para 39). "The bank, acting on the information from MBJ, treated the funds as the sale price of all the subjects, but that was not an accurate understanding" (para 41). "Everyone, apart from the bank and the bank's solicitor, knew that the

funds were the sale price of only 278 Glasgow Road. ... Had the bank known the true facts, namely that 278 was sold for almost £2.5m, the same overall reduction in bank indebtedness would have occurred, but only the standard security over 278 would have been discharged" (paras 39-40). "Everything depended upon the bank and the bank's solicitor being unaware of the truth. No doubt they assumed that they could trust the information provided by MBJ" (para 42).

9. As a consequence of the fact that "the bank was misled into using part of the sale price of 278 Glasgow Road to discharge all the standard securities" (para 40), the four remaining properties, with an agreed value of £1.525m, were now free of the bank's standard securities. It only remained to place them entirely beyond the bank's reach.

10. On 24 November 2010, 110, 210 and 260 Glasgow Road were disponed to Stonegale, and 64 Roslea Drive was disponed to Mr Pelosi junior. It is those dispositions which are challenged in the present proceedings. The dispositions, witnessed by Mr Frame, contained a date of entry of 16 November 2010, and recorded the consideration given as being in accordance with the figures given to Mr Gillespie. In reality, nothing was paid. The following year, Mr Pelosi junior disponed 64 Roslea Drive to a third party for £125,000.

11. In the proceedings before the Lord Ordinary, a document was produced which purported to be a loan agreement in the sum of £1,584,000, signed by Mr Pelosi junior and dated 16 November 2010. It narrated that it had been entered into between Strathcroft and Stonegale to enable the latter to finance the purchase of the properties at 110, 210 and 260 Glasgow Road. In evidence, Mr Pelosi junior confirmed that he had signed the loan agreement on 16 November 2010. The Lord Ordinary found that the document was a sham (para 44), "concocted purely for the purpose of the defence of these proceedings" (para 46).

*The proceedings below*

12. Before the Lord Ordinary, it was argued that the four dispositions under challenge were made by the companies for adequate consideration, namely the reduction in their contingent liabilities (under their cross-guarantees of Oceancrown's obligations) which resulted from the payment made by Strathcroft to the bank. That reduction in indebtedness, of £2,414,000, was in excess of the open market values of all five properties, and therefore constituted adequate consideration. That argument assumes that the open market value of 278 Glasgow Road was the £762,000 at which it had been valued by a surveyor: an assumption which is contradicted by the fact that Clyde Gateway paid almost £2.5m for it in an arm's length transaction whose bona fides is not disputed. More fundamentally, the

argument disregards the fact that the four other properties were all disponed gratuitously in subsequent transactions.

13. In rejecting the argument, the Lord Ordinary focused on the latter point:

> "No one paid anything for 110, 210, 260 Glasgow Road and 64 Roslea Drive. The sellers, namely Oceancrown, Loanwell and Questway, did not receive anything in return for the dispositions under challenge. They gifted the properties to the dispones. ... That the bank was prepared to discharge the standard securities over all five properties in return for the monies forwarded to it does not create a consideration given in return for the subsequent dispositions to Stonegale. No party gave the sellers anything in return for the conveyances under challenge. Any value received was the value paid in respect of number 278. That is what was transferred to McClure Naismith. In my view nothing else alters that basic fact. All that happened was that Strathcroft, on the direction of Mr Pelosi senior, paid the bank monies which were designed to, and did persuade the bank to discharge the standard securities over the five properties, all in order to facilitate the subsequent gratuitous sales. Neither that payment, nor any consequential reduction in indebtedness, was in consideration for the subsequent transactions. It was a mechanism for allowing the inter-company transfers which it was hoped would achieve the retention of the 'profit' on 278 within the group (and regarding Roslea Drive, Mr Pelosi junior) - and free of the bank's securities." (paras 40 and 42)

The Lord Ordinary added:

> "The dispositions under challenge were gratuitous alienations. Were it otherwise the bank would have received in excess of £4m, and the overall indebtedness would have been reduced by that amount. The price obtained for 278 was used to allow the other Glasgow Road properties to be transferred without consideration to another company which, nominally at least, was owned and controlled by Mr Pelosi junior, and, in the case of 64 Roslea Drive, to him personally." (para 43)

14. Accordingly, the Lord Ordinary decided that he should reduce (ie set aside) the three dispositions to Stonegale, order the defenders to execute dispositions of

those subjects to the administrators, and order Mr Pelosi junior to repay the £125,000 which he had received for the sale of the fourth property. Before granting decree, he decided to have the proceedings put out By Order for appropriate disposal.

15. That decision was upheld by an Extra Division of the Inner House (Lord Menzies, Lord Brodie and Lord McGhie). No issue was taken with the facts found by the Lord Ordinary. The same argument was repeated, and again rejected, for the same reasons.

*The present appeal*

16. In the absence, at the relevant time, of any requirement to obtain permission to appeal to this court, the appellants took the opportunity to challenge the approach adopted by the courts below. They submitted that the administrators could have pursued a number of alternative remedies. They could have challenged the alienation of 278 Glasgow Road by Oceancrown to Strathcroft. They could have proceeded against Mr Pelosi senior as director of Oceancrown for breach of his fiduciary duty, and recovered the proceeds of his breach from the ultimate beneficiaries. If the bank was the victim of a fraudulent misrepresentation, it could have recovered damages in respect of its loss. The wrong remedy, it was argued, had been selected. The failure to challenge the transfer by Oceancrown to Strathcroft meant that the transfer by Strathcroft to Clyde Gateway could not be impeached. In any event, the £762,000 paid by Strathcroft reflected a professional valuation of the property, and therefore constituted the property's market value.

17. There are no doubt a variety of remedies which the administrators might have pursued, but the issue for this court is whether they are entitled to the remedy which they have sought. That remedy does not involve a challenge to the disposal of 278 Glasgow Road (or depend on whether the disposal of that property by Oceancrown was at an undervalue, although it plainly was), but a challenge to the other four dispositions as gratuitous alienations. The gratuitous nature of the alienations was clearly explained by the Lord Ordinary in the passages cited at para 13 above. Before the various conveyances, the companies owned five properties. A bargain was in place for the sale of one of those properties, 278 Glasgow Road, for the sum of £2.4m. After the sale was completed, £2.4m was transferred to the bank in reduction of borrowings, and the companies retained the other four properties, valued at £1.525m. Those properties were then conveyed to the appellants. The companies received nothing whatsoever in return. There was no reciprocity between those disposals and the earlier payment made to the bank. The purpose and effect of those transactions was to divert assets away from the companies' creditors: exactly what section 242 is intended to prevent. That they were gratuitous alienations is plain and obvious.

18. The appeal is therefore dismissed.