Michaelmas Term
[2019] UKSC 57
On appeal from: [2018] CSIH 7

JUDGMENT

MacDonald and another (Respondents) *v* Carnbroe Estates Ltd (Appellant) (Scotland)

before

Lord Reed, Deputy President
Lord Wilson
Lord Hodge
Lord Briggs
Lord Sales

JUDGMENT GIVEN ON

4 December 2019

Heard on 2 May 2019

Appellant
Lord Davidson of Glen Clova QC
Jonathan Brown
(Instructed by Levy & McRae Solicitors LLP (Glasgow))

Respondents
Kenneth McBrearty QC
Susan Ower
(Instructed by Harper Macleod LLP (Glasgow))

LORD HODGE: (with whom Lord Reed, Lord Wilson, Lord Briggs and Lord Sales agree)

1. This appeal concerns the Scots law of gratuitous alienations on insolvency. It raises three principal questions. First, there is a question as to the interpretation of the term "adequate consideration" in section 242(4)(b) of the Insolvency Act 1986 ("the 1986 Act"). Secondly, there is the question whether the Inner House was entitled to interfere with the Lord Ordinary's evaluation that the consideration given by Carnbroe Estates Ltd ("Carnbroe") amounted to adequate consideration under that statutory provision. Thirdly, a question arose during the hearing as to the interpretation of the words in section 242(4) that empower the court to grant a remedy. The court invited and received written submissions from counsel for both parties. The question is whether the court has any discretion as to the remedy it may give.

Factual background

2. Grampian MacLennan's Distribution Services Ltd ("Grampian") was, as its name suggests, a distribution services company. It carried on business from a site at 9 Stroud Road, Kelvin Industrial Estate, East Kilbride ("the Property"). The Property, which was Grampian's principal asset and centre of operations, consisted of a warehouse, a vehicle workshop and a yard with a gatehouse. Grampian purchased the Property in August 2005 for £630,000. The buildings on the Property had been constructed in the 1970s and by 2014 were in need of further maintenance, repair and upgrading. Grampian's shareholders until June 2014 were Derek and Hazel Hunter, and Derek Hunter ("Mr Hunter") was the sole director.

3. In March 2013 DM Hall, chartered surveyors, ("DM Hall") valued the Property at £1.2m on the open market with the valuation falling to £800,000 if one were to assume a restricted marketing period of 180 days. By early 2014 Grampian was in financial difficulty. In May 2014 Mr Hunter consulted an insolvency practitioner to obtain advice as to whether he should put Grampian in members' voluntary liquidation. At that time Mr Hunter believed that the sale of the Property would enable Grampian to pay all its creditors and make a distribution to the shareholders. His belief was supported by the DM Hall valuation of March 2013. Shortly before the consultation in May 2014, Carnbroe had intimated through its solicitors an interest in purchasing the property for £950,000. In mid-2014, another company, Bullet Express Ltd, also expressed an interest in acquiring the Property at a price of £900,000.

4. Mr and Mrs Hunter chose not to pursue those expressions of interest in the Property but instead sold their shares in Grampian to Mr Kevan Quinn ("Mr Quinn"), who became its sole shareholder and director with effect from about 16 June 2014. At this time, Grampian's total liabilities marginally exceeded £1m. Sums in excess of £500,000 were due to HM Revenue and Customs ("HMRC") and sums over £500,000 were due to National Westminster Bank plc ("NatWest"), which together were Grampian's principal creditors. NatWest held a standard security over the Property in respect of a LIBOR loan, which I mention below. It also held a bond and floating charge over Grampian's property and undertaking. Grampian had to pay monthly loan payments to NatWest of about £4,600.

5. In his witness statement, which was accepted as his evidence in chief and truthful and on which he was not cross-examined, Mr Quinn explained that he had taken over Grampian in the hope that he could save it and make money out of it. He narrated that shortly after his takeover, Grampian's invoice factor withdrew its factoring facility which caused the company's cash flow to collapse. He was not able to obtain alternative funding. He explained that once he realised how bad Grampian's position was, he tried to deal with it in as responsible a way as he could. He sold off the company's trucks, which were on hire purchase, to reduce outgoings, and then sought to sell Grampian's only other asset, the Property. With the collapse in its cash flow, Grampian could not pay the loan payments to NatWest, which fell into arrears. He sought to sell the Property to prevent it from being re-possessed by NatWest.

6. Mr Quinn entered into discussions to sell the Property with James Gaffney ("Mr Gaffney") who was a successful businessman whom he had known for over 30 years and with whom he had had business dealings throughout that time. Mr Gaffney tried to "chisel" the price by pointing out that the electrical system of the building needed immediate attention, and that there was an issue about the presence of asbestos which would have to be addressed at some time. Mr Gaffney was aware of Grampian's predicament and mentioned that he could buy the Property after it had been repossessed.

7. Mr Gaffney also gave evidence in a written witness statement which was accepted as truthful. He stated that Carnbroe was one of his family companies and that he negotiated with Mr Quinn on its behalf. Mr Quinn had explained to him Grampian's financial difficulties on a number of occasions. Mr Quinn was looking for a quick sale because of mortgage arrears and the risk that the Property would be repossessed. The price of £550,000 reflected the quick sale. The buildings needed repairs and refurbishment, including re-wiring and asbestos removal.

8. That is all the direct factual evidence that was led about the circumstances which led up to the sale of the Property to Carnbroe. The parties sought to adopt an

economical and proportionate approach to the proof, which is to be commended. In a Joint Minute of Admissions the parties agreed as true the contents of the affidavits of the liquidators and two other witnesses to fact on their behalf. The reports of and other documents prepared by the two expert valuation witnesses, Mr Iain Prentice of Colliers International Valuation UK LLP, whom the liquidators called as a witness, and Mr Alastair Buchanan of J & E Shepherd, who gave evidence at Carnbroe's request, were admitted as their evidence in chief. Both expert witnesses gave brief oral evidence in chief and were cross-examined in a succinct manner. The Joint Minute of Admissions also proposed detailed findings of fact on matters which were not in dispute. No evidence was led as to the likely price which NatWest could be expected to obtain if it had called up its standard security and sold the Property or which a liquidator of Grampian would be likely to have obtained on its sale in a winding up.

9. Grampian transferred the Property to Carnbroe by a disposition dated 24 July 2014 in which the consideration was stated to be £550,000, having agreed an off-market sale. Entry was given to the Property on that date. Immediately before the sale, Grampian owed NatWest £473,604.68 under the LIBOR loan which was secured over the Property. Carnbroe did not pay the agreed consideration of £550,000 but instead, on 18 August 2014, its solicitors paid the sum of £473,604.68 to NatWest in repayment of the LIBOR loan to Grampian and to obtain a discharge of the standard security over the Property. Carnbroe did not pay the balance of the stated purchase price to Grampian until 9 June 2016, after the completion of the proof before the Lord Ordinary in this case.

10. Carnbroe funded the purchase of the Property by a loan of £600,000 from the Bank of Scotland plc ("the Bank"). In support of its lending, the Bank obtained a report from DM Hall dated 23 June 2014, which confirmed the valuation in its March 2013 report, namely £1.2m on the open market and £800,000 on the assumption of a restricted marketing period of 180 days. On 28 July 2014, solicitors for the Bank questioned the discrepancy between the purchase price of £550,000 and the DM Hall valuation. Carnbroe's solicitor replied by email to the effect that because NatWest were calling for payment under threat of enforcing their securities, there was no willing seller and no willing buyer for the Property and that Grampian did not have the option of a 180 day marketing period. The solicitor stated that he had spoken with DM Hall who had confirmed that, as a result, the assumptions made in their valuation did not apply. The Bank then made a loan of £600,000 to Carnbroe which was secured over the Property.

11. The sale of the Property and the repayment of NatWest's LIBOR loan left the other principal creditor, HMRC, unpaid. HMRC wrote to Grampian on 6 August 2014 requiring payment of tax that was due. On Grampian's failure to pay, HMRC presented a petition for winding up Grampian founding on that debt. Mr MacDonald was appointed provisional liquidator on 12 September 2014 and on 21 November

2014 he and Ms Coyne were appointed as joint liquidators at a meeting of Grampian creditors. The liquidators raised the present proceedings on 28 November 2014.

12. I can summarise the valuation evidence shortly. Mr Prentice's evidence was that the open market value of the Property at the date of the transaction was £820,000. Mr Buchanan's evidence of the open market value at that date was £740,000. The experts both made their valuations on the assumption that the bargain was between a willing seller and a willing buyer at arm's length. They both assumed a proper period of marketing, which Mr Prentice thought would take between 12 and 24 months and Mr Buchanan thought would be 24 months. Both advised that it was appropriate to apply a discount of between 25% and 30% if there were a restricted marketing period of six months. Neither considered that a consideration of £550,000 was inappropriate if there were an immediate off-market sale by a financially distressed vendor, in accordance with the factual assumptions which Mr Buchanan was requested to address and addressed in his report.

13. The question which has become of central importance in this case is whether there was an objective justification for such an urgent off-market sale, which caused so radical a reduction in the value of the Property in comparison with the open market value.

The judgments of the Scottish Courts

14. After a two-day proof, the Lord Ordinary held in an opinion dated 18 January 2017 ([2017] CSOH 8) that Carnbroe had established that the sale of the Property was made for adequate consideration. He recorded the submission which counsel made on behalf of Carnbroe that Grampian was fighting for its survival and that Mr Quinn had to make a quick decision. He continued:

> "30. While the purchase price fell short of the open market value, Grampian had very limited options. It was in a perilous financial position. It could not afford the leisure of a lengthy marketing period. NatWest was threatening to call up the standard security and to use other diligence against it in terms of the bond and floating charge it held. There was no other offer on the table. The earlier expressions of interest were just that. There was no solid proposal to accept.
>
> 31. Carnbroe's offer presented an opportunity to obtain a quick sale. To place the property on the open market would have involved significant expense. There would have been advertising costs and an estate agency fee of 1% to 1.5%. There

> was no clear indication that a sale would be achieved within the standard marketing period of 12 to 24 months. According to the surveyors' evidence, a stigma can attach to a property that remains on the market too long. It might be the subject of vandalism."

He went on the state that Mr Quinn and Mr Gaffney were not "associates" in terms of the relevant legislative definition, but their long business relationship justified close scrutiny of the transaction. The expert surveyors had agreed that a price of £550,000 was not inappropriate if the Property had been marketed on a closed basis for six months.

15. The liquidators appealed to the Inner House. In an opinion and interlocutor dated 23 January 2018 the First Division (the Lord President, Lord Drummond Young and Lord Malcolm) ([2018] CSIH 7) allowed the reclaiming motion, reduced the disposition of the Property and ordered Carnbroe to execute a disposition of the Property in favour of the liquidators. In the opinion of the Court, which Lord Drummond Young delivered, the First Division recorded its view (para 11) that the most important issue in the appeal was whether it was correct to assert that a quick sale was justified because Grampian had an immediate need for funds. The First Division concluded that it was not. Analysing the facts found by the Lord Ordinary, the Court identified four factors which were of central importance, namely Grampian's severe financial difficulties when the finance house withdrew its invoice factoring facility, Grampian's balance sheet insolvency, the sale of the trucks on which Grampian depended to provide its distribution service, and the sale of the Property which was its principal place of business and depot (paras 27-29). The First Division concluded that on an objective analysis there was no realistic prospect that Grampian's business could continue in existence after the sale of those assets (para 30). In consequence, this was not a case in which the achievement of a quick sale of the Property would save the company's business.

16. In its legal analysis of the principles of insolvency law the First Division (paras 12-20) stated that a person, once he or she became insolvent, owed a fiduciary duty to have regard to the interests of his or her creditors and as a result, if a debtor alienates property once he or she is insolvent, he or she must obtain full consideration for the property alienated. The First Division pointed out that under the current and prior statutory provisions relating to gratuitous alienations the burden of proving that full consideration had been given rested on the recipient of the insolvent debtor's property. The same principles applied to a corporate insolvency in which directors of an insolvent company owed analogous fiduciary duties to have regard to the interests of the company's creditors as a body. As a result, the courts should take a relatively strict view of the adequacy of consideration (para 24).

17. The First Division distinguished balance sheet insolvency (ie an excess of liabilities over assets) with cash flow insolvency (ie the inability of a trading entity to meet its debts as they fall due). It recognised both that an urgent forced sale, necessitated by a trading entity's need for cash to maintain liquidity in order to continue to trade, would generally result in a lower price than a sale in ordinary market conditions and that the need to maintain liquidity and stay in business could be a relevant factor in deciding whether the consideration paid was adequate. But if an insolvent trading entity's business was about to come to an end, there was no need to maintain liquidity and the paramount importance of the interests of the creditors prevailed over any need to pay debts as they fall due. The First Division stated (para 25):

> "For these reasons we are of opinion that the need for a forced sale to provide immediate liquidity is not normally a factor that should be taken into account in determining the adequacy of consideration obtained for a sale of the debtor's assets in any case where the debtor has ceased business or is about to cease business."

As a result, if a trading entity sold its principal asset, such as its principal place of business, the court would have to scrutinize the company's commercial situation in order to determine whether it was realistic for it to continue to trade (para 26).

18. Carnbroe appeals to this court with this court's permission. In presenting Carnbroe's appeal, Lord Davidson of Glen Clova QC makes three submissions. He submits that the central issue is whether the insolvent company's financial distress justified an urgent sale and that the Lord Ordinary reached a conclusion which was open to him on the evidence. The First Division therefore erred in interfering with his evaluation. It erred in placing a gloss on the statutory words and requiring a strict approach to the assessment of any departure from open market value when the alternative facing Grampian was a sale by the standard security holder or a sale by a liquidator, both of which could be categorised as a forced sale. The Lord Ordinary made no findings as to the likely outcome of such sales, which were the appropriate comparators. Secondly, the First Division erred in identifying the applicable legal policy. Lord Davidson does not challenge the proposition that an insolvent company is in substance a trustee for its creditors but submits that a countervailing consideration is that the law should facilitate commercial transactions and promote commercial certainty. What the statute requires is the striking of a just balance between the creditors' interests and the interests of those contracting at arm's length with an insolvent company. The test of "adequate consideration" takes account of both interests. He refers by way of analogy to statutory provisions in English law (section 238 of the 1986 Act) and in Australian law (sections 588FB, 588FC and 588FF of the Corporations Act 2001) and submits that the test is whether the transaction was a commercial one which was satisfactory in all the circumstances

rather than, as the First Division held, a strict approach to the words "adequate consideration". Thirdly, he submits that the First Division's judgment lacks commercial practicability: a purchaser in a commercial deal looks after its own interests and is entitled to exploit a vendor's financial distress to obtain a favourable price in an arm's length transaction. Sales at less than open market value are the norm where there are problems with liquidity. But the purchaser cannot know whether the vendor in pursuing an urgent sale has a realistic possibility of preserving its business or is otherwise acting in the interests of its creditors. If the First Division's analysis were correct, prudence would require the purchaser to refuse to deal with a company in distress and instead wait to see if a formal insolvency eventuated which would enable it safely to purchase from a liquidator.

Discussion

i) The statutory provisions

19. Section 242 of the 1986 Act enables among others the liquidator of a company to challenge a gratuitous alienation in Scotland if the alienation took place not earlier than two years before the commencement of the winding up or not earlier than five years before that date if the alienation favours an associate of the company. Subsection (4) provides:

> "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 -
>
> > (a) that immediately, or at any other time, after the alienation the company's assets were greater than its liabilities, or
> >
> > (b) that the alienation was made for adequate consideration, or
> >
> > …
>
> Provided that this subsection is without prejudice to any right or interest acquired in good faith and for value from or through the transferee in the alienation."

20. Several points may be made about the section 242. First, the liquidator or creditor is entitled to make the challenge if the alienation occurs at a date not less than two years before the commencement of the winding up or five years before that date if the transferee is an associate of the insolvent company: section 242(3). Secondly, subject to the next point, the court must give at least one of the remedies specified (section 242(4)). Thirdly, to prevent the court from giving such remedies, the transferee of the alienation must establish one of the listed circumstances (section 242(4)(a)-(c)). In this case the circumstance which Carnbroe asserts is that the alienation was made for adequate consideration. The burden is thus placed on the transferee to establish that the consideration given for the alienation was "adequate". Fourthly, as I shall show when I discuss case law below, the test as to whether the consideration is adequate is an objective test. Fifthly, where a remedy is given against the transferee, the subsection protects any right or interest which a third party has acquired in good faith and for value from or through the transferee (the proviso in section 242(4)). This is relevant to the interest of the Bank in this case.

21. Subsection (7) preserves the Scots common law of challenges to gratuitous alienations by providing that a liquidator and an administrator have the same right as a creditor has under any rule of law to challenge an alienation of a company made for no consideration or no adequate consideration.

22. Section 242 of the 1986 Act applies to corporate insolvency a regime for challenging gratuitous alienations which was introduced in section 34 of the Bankruptcy (Scotland) Act 1985, which governs the bankruptcy of natural persons and partnerships in Scotland, following a recommendation of the Scottish Law Commission in their 1982 *Report on Bankruptcy and Related Aspects of Insolvency and Liquidation* (Scot Law Com No 68). The relevant provision in bankruptcy is now section 98 of the Bankruptcy (Scotland) Act 2016, but I will focus on the predecessor statute in discussing the genesis of the relevant provisions. Essentially the same regime was introduced into corporate insolvency by section 75 of and paragraph 20 of Schedule 7 to the Bankruptcy (Scotland) Act 1985 which inserted section 615A into the Companies Act 1985. Thereafter, it was replaced by the provision in the 1986 Act. I therefore refer to the new regime for gratuitous alienations as "the 1985 statutory reforms". In chapter 12 of the report which led to the 1985 statutory reforms, the Scottish Law Commission set out its proposals to make more consistent the rules of Scots law, both common law and statutory, in relation to the challenges to gratuitous alienations and unfair preferences to creditors on insolvency.

23. Scots common law has built on the principle of the actio Pauliana in Roman law which allowed a challenge to a gift made by an insolvent donor on the basis that the gift was a fraud upon his or her creditors. Under Scots common law it is not necessary to prove an intention to defraud if the creditor mounting the challenge can

show three things: (i) the debtor was absolutely (ie balance sheet) insolvent at the time of the challenge and was either insolvent (in that sense) at the time of the alienation or was made insolvent by it, (ii) the alienation was made without onerous consideration, and (iii) the alienation prejudiced the challenging creditor. As it was difficult for a creditor to prove such insolvency at the date of the alienation, the Scottish Parliament by the 1621 Act (c 18) ("the 1621 Act") strengthened the creditor's position in challenges to alienations which an insolvent made to a "conjunct and confident person" (ie a close relative, business partner, employee etc to whom money or assets were often secretly transferred) "without true, just and necessary causes" by creating factual presumptions which the transferee had to rebut. The 1621 Act, which the Scottish courts interpreted liberally, had the effect that, if the creditor could establish that the debtor was insolvent at the date of the challenge, it was presumed both that the debtor had been insolvent at the date of the alienation and that the alienation was made without onerous consideration. It was not necessary that the alienation be wholly gratuitous as the challenge could be made to an alienation which was for a materially inadequate consideration in money or money's worth. Under both the common law and the 1621 Act the challenger of the transaction did not have to prove that the debtor or the transferee was aware of the debtor's insolvency or that the debtor was seeking to harm his creditors: *McCowan v Wright* (1852) 14 D 968, 970 per the Lord Justice-Clerk (Hope). Under the 1621 Act the challenger had to prove only the debtor's insolvency at the date of challenge and that the challenger was prejudiced by the transaction if it was at an undervalue. Nor is it necessary when alleging fraud at common law, as a general rule, to prove that there was fraud or complicity on the part of the recipient of the alienation: *McCowan v Wright* (1853) 15 D 494, 496-504 per the Lord Justice-Clerk (Hope), 509 per Lord Cockburn, 512-515 per Lord Wood. A successful challenge led to the annulment of the alienation; where there had been a purchase at an undervalue there was no requirement that the retransfer of the property to the debtor's estate was conditional upon the repayment of the consideration which the transferee had paid: *Tennant v Miller* (1897) 4 SLT 318.

24. Both Scots common law and the 1621 Act protected a third party who took the alienated property from the transferee in good faith and for value; in such a circumstance the only remedy for the creditor or insolvency practitioner was to claim the sale proceeds from the transferee. The common law and the statutory provisions have been applied to companies as well as other debtors: *Abram Steamship Co Ltd v Abram* 1925 SLT 243; *Bank of Scotland v R W Forsyth Ltd* 1988 SC 245.

25. Alongside these provisions concerning gratuitous alienations, Scots common law allowed creditors of an insolvent to challenge as fraudulent preferences voluntary preferences which the insolvent granted to a creditor during insolvency. Such fraudulent preferences could take the form of a grant of security for a prior debt or facilitating a creditor's attempt to execute diligence or obtain a decree to enforce the debt. The common law was reinforced by another Act of the Scottish

Parliament in the Act 1696 (c 5) ("the 1696 Act"), which nullified all deeds which a bankrupt granted within 60 days before or during his insolvency and which gave a preference to a creditor over other creditors. Like the 1621 Act, the courts gave this Act a broad interpretation.

26. The Scottish Law Commission's expressed aim in promoting the reform proposals was to achieve a consistent and logical scheme for the annulment of alienations and unfair preferences. There is no suggestion of an intention fundamentally to alter the law in relation to gratuitous alienations on the repeal of the 1621 Act. Section 242 of the 1986 Act reflects many of the Commission's recommendations. The wording of the remedies which the court was empowered to give in section 242(4) tracks the Commission's recommendation in para 12.19 of the report but there is no discussion in the report of any prior case law on the nature of the remedy or remedies open to the court and no statement of policy to explain the recommendation. The report thus gives no guidance as to whether it was envisaged that the court would enjoy a discretion in devising a remedy. I return to this matter in paras 44 - 69 below.

27. Both before and after the 1985 statutory reforms, the consequence of the annulment of an alienation by reduction was and is that the property is transferred back to the insolvent's estate. If the court is not empowered to or does not impose conditions on the reduction, the transferee who has paid a substantial but inadequate consideration may only have a claim in unjustified enrichment against the insolvent's estate for repayment of the consideration paid. In making that claim the transferee ranks as an ordinary creditor and may receive only a dividend or nothing at all, depending upon the balance between the insolvent's assets and the debts due to secured creditors and other creditors. A claim for the recovery of the transferred asset itself or the proceeds of its sale ranks as a postponed debt: rule 4.66(2)(a) of the Insolvency (Scotland) Rules 1986 (SI 1986/1915), which has now been replaced by rule 7.27 of the Insolvency (Scotland) (Receivership and Winding Up) Rules 2018 (SSI 2018/347).

28. There are three principal innovations in the 1985 statutory reforms which are relevant in this case. The first is that the presumptions in the 1621 Act which applied only to alienations to "conjunct and confident persons" have been extended to all gratuitous alienations, including those in which a purchaser at arm's length buys an asset from the insolvent at an undervalue. The second is the introduction of new time limits for the challenge: the difference between associates and other transferees now lies only in the provision of different time limits in section 242(3) (para 20 above). The third is the specification in section 242(4) of the different remedies available to the court in place of a statutory statement that the transaction was a nullity.

ii) Adequate consideration

29. As I have said, before the 1985 statutory reforms to the Scottish law of insolvency, an alienation could be challenged not only if it was wholly gratuitous but also if it was at an undervalue. What amounted to a relevant undervalue before 1985? The leading Scottish textbook on bankruptcy before the 1985 statutory reforms was *Goudy, A Treatise on the Law of Bankruptcy in Scotland*, 4th ed (1914), which provided a commentary on both the common law and the Bankruptcy (Scotland) Act 1913, which was repealed in 1985. Goudy answered the question by explaining what was not an undervalue. His analysis of the prior case law was that at common law consideration for an alienation was not an undervalue if it was "fairly equivalent to what is received" (p 25) and similarly, under the 1621 Act if, it was "fairly adequate for what was given" (p 47). Support for Goudy's view can be found in *Bell's Commentaries on the Laws of Scotland*, 7th ed (1870), vol ii, p 179 which, in a commentary on the 1621 Act, stated:

> "In proving the consideration of the deed, every case must depend on its own circumstances. It may be observed, however, in general, 1. That it is not in all cases necessary to prove that the highest price possible has been got for the subject; but quite sufficient if what is commonly called a fair price has been received, ie a price, which, in the whole circumstances of the case, indicates a fair and *bona fide* transaction."

The Lord Justice-Clerk (MacDonald) in the Second Division of the Inner House used the concept of "fair consideration" in *Gorrie's Trustees v Gorrie* (1890) 17 R 1051, 1054. See also *Glencairn v Birsbane* (1677) Mor 1011, in which a defence that adequate consideration had been given was held to be relevant in the face of an assertion by the pursuer that he would have paid more, and *Miller's Trustee v Shield* (1862) 24 D 821, in which, in a challenge to an allegedly unfair preference under the 1696 Act, the First Division treated the transfer of goods for an "adequate" sum as causing no prejudice to the insolvent's creditors (p 828 per Lord Curriehill).

30. The courts have adopted a similar approach to adequate consideration since the 1985 statutory reforms. The leading Scottish authority on the meaning of "adequate consideration" in section 242 of the 1986 Act is the opinion of Lord Cullen, when he was a Lord Ordinary, in *Lafferty Construction Ltd v McCombe* 1994 SLT 858. Both the appellant and the respondents accepted his statement as the proper approach to adequacy under section 242(4)(b). He stated, at p 861:

> "In considering whether alienation was made for 'adequate consideration', I do not take the view that it is necessary for the

> defender to establish that the consideration for the alienation was the best which could have been obtained in the circumstances. On the other hand, the expression 'adequate' implies the application of an objective standpoint. The consideration should be not less than would reasonably be expected in the circumstances, assuming that persons in the position of the parties were acting in good faith and at arm's length from each other."

31. Lord Eassie expressed a similar opinion in relation to the identical term in the equivalent provision in section 34(4) of the Bankruptcy (Scotland) Act 1985 in *Aitken's Trustee v Aitken*, 26 November 1999, reported as *Kerr v Aitken* [2000] BPIR 278, in which he stated, at p 282:

> "In my opinion the expression 'adequate consideration' means the giving of a consideration which might objectively be described as being a reasonable prestation for the property conveyed by the bankrupt to the transferee had the transaction taken place between parties acting at arm's length in ordinary commercial circumstances."

The only qualification which I would make to Lord Eassie's formulation is that I would not speak of "ordinary commercial circumstances", but, like Lord Cullen, would look to the circumstances of the case, which might (as I discuss in para 34 below) in an appropriate case include the seller's need to obtain a prompt sale to protect its cash flow in a liquidity crisis.

32. Both judges correctly emphasise the objective nature of the test and that regard must be had to the commercial justification of the transaction in all the circumstances on the assumption that hypothetical people in the position of the insolvent and the transferee would be acting in good faith and at arm's length. In my view, the requirement that the hypothetical parties are acting at arm's length means that the hypothetical purchaser would not have knowledge of the seller's financial distress unless the insolvent's financial embarrassment was known in the relevant market. It would not be a relevant consideration that the actual vendor had disclosed its financial embarrassment to the purchaser and that the purchaser had exploited that disclosure in its negotiation of the purchase price. There is nothing to suggest that the 1985 statutory reforms sought to innovate in this regard. As a result, the statutory provisions apply during the specified period before formal insolvency (in this case liquidation) whether or not the insolvent is aware of his, her or its insolvency and whether or not the transferee or purchaser is so aware.

33. One of the relevant circumstances is the fact of the bankrupt's insolvency. As Lord Drummond Young records in para 13 of the Inner House's opinion [2018] CSIH 7, by reference to *Bell's Commentaries*, (above), (pp 171-172), the restoration to the bankrupt's estate of assets gratuitously alienated is based on the principle that on the occurrence of insolvency, it is the creditors who have the real interest in the bankrupt's assets and the bankrupt must manage those assets in such a way as to protect their interests. There is an analogous principle in United Kingdom company law which, on the occurrence of insolvency, requires company directors to have regard to and act in the interests of the company's creditors as part of their fiduciary duties owed to the company as a whole: *West Mercia Safetywear Ltd v Dodds* [1988] BCLC 250; Companies Act 2006, section 172(3). The mischief which led to the enactment of the 1621 Act was the practice of bankrupts of creating secret trusts in favour of family members or close associates to protect their assets from their creditors. That mischief remains relevant. But the current statutory regime and the common law extend to business transactions at arm's length and require the insolvent vendor to obtain an adequate consideration for its assets in the interests of its creditors, if a successful challenge is to be avoided.

34. Another relevant consideration, as the Inner House states, is the objective purpose of the sale. As is clear from the expert evidence in this case, there is generally a close relationship between the time which is spent on marketing a commercial property and the price at which it will sell. Such property, if sold in a hurry, will usually obtain a significantly lower price than if it were exposed to the market for a longer period. On the occurrence of insolvency, the requirement that the insolvent has regard to the interest of creditors points towards the hypothetical vendor in the objective assessment having to carry out an adequate marketing exercise to obtain a good price for the property. If the insolvent's property is not exposed to the market but is disposed of by private sale, there is an obvious risk of an inadequate price. But there may be circumstances in which an insolvent, acting in the interests of its creditors, needs to achieve a quick sale. An example of such a sale is where the insolvent is facing a liquidity problem and needs to obtain cash to pay its debts promptly in the hope of trading out of insolvency and preserving its business as a going concern. In such a circumstance, it may be objectively reasonable for the insolvent to accept the lower price from a quick sale of an asset in order to gain the chance of saving the business, as that outcome is likely to be in the interests of its creditors.

35. An analogous example is the case of *John E Rae (Electrical Services) Linlithgow Ltd v Lord Advocate* 1994 SLT 788, in which an insolvent company, in order to continue to trade, needed certificates from the Inland Revenue that exempted it from the requirement that persons who employed it as a contractor or subcontractor should deduct tax from payments made to it. To obtain those certificates from the Inland Revenue the company granted a bond in respect of past tax liabilities of an associated company, whose business had been transferred to the company, arising from underpayments of income tax and national insurance

contributions in respect of payment made to subcontractors. The liquidator raised an action under section 242 of the 1986 Act in which he sought reduction of the bond and repayment of sums which had been paid to the Revenue under it on the basis that it was an alienation in favour of the associated company. But Lord Clyde rejected the liquidator's challenge. Adequate consideration had been given because the company, in return for undertaking to pay the associated company's debt, had obtained in effect the right to continue trading and had thus staved off its imminent demise. That approach may be questioned where there is no evidence to show that the projected cash flow advantage, which the certificates gave the company, was measurable in money or money's worth and, as so measured, was adequate as Lord Cullen's formulation envisages. But if there is such evidence, that approach accords with the section.

36. Where there is no question of a sale to preserve a company's liquidity or otherwise in the hope of enabling it to remain in business, and where the insolvent company is ceasing or has ceased to carry on business and is, in reality, winding up its business in an informal way without the involvement of a liquidator or an administrator, what is an adequate consideration?

37. The answer, in the context of the objective exercise which the law mandates, will depend upon the circumstances of the insolvency. The aim of the common law and section 242 is to make sure that the creditors of the insolvent company are not prejudiced by an alienation by that company which brings into the insolvent estate materially less than would be obtained in an arm's length transaction between bona fide commercial parties in the circumstances of the case. Where the directors of the insolvent company, mindful of their duty to creditors, have an opportunity to place a property on the market and carry out a proper marketing exercise to enhance the price which the property will command, "adequate consideration" should be measured against the likely result of such an exercise. Where the insolvent company is not able to support such a marketing exercise, the adequacy of the consideration achieved on a sale is to be measured by comparing the consideration which the insolvent company has accepted against the likely outcomes which a formal insolvency would achieve through the sale or other disposal of the asset by a liquidator or administrator, taking into account the fees which the insolvency practitioner would charge for effecting the sale. Where the asset in question is the subject of a security with a power of sale, it would be relevant also to consider the likely outcome of that sale. The aim of the common law and section 242 in that context is to make sure that the creditors of the insolvent company are not prejudiced by an alienation by that company which brings into the insolvent estate materially less than would be obtained by the formal insolvency process or the sale by the security holder.

38. A liquidator is under a fiduciary duty to the company, and possibly its creditors as a class, to exercise the professional care and skill of an insolvency

practitioner in realising the assets of an insolvent company: *Hague v Nam Tai Electronics Inc* [2008] UKPC 13; [2008] BCC 295; *Oldham v Kyrris* [2003] EWCA Civ 1506; [2004] BCC 111; see by analogy *Lightman & Moss on the Law of Administrators and Receivers of Companies*, 6th ed (2017), para 12-042. The liquidator must take reasonable care in choosing the time at which to sell the property and must also take reasonable care to obtain the best price that the circumstances of the case, as he reasonably perceives them, permit: *In re Charnley Davies Ltd (No 2)* [1990] BCLC 760, 775-776 per Millett J; *Silven Properties Ltd v Royal Bank of Scotland plc* [2003] EWCA Civ 1409; [2004] 1 WLR 997, para 25 per Lightman J. The holder of a standard security is under a statutory duty when selling the security subjects:

> "to advertise the sale and take all reasonable steps to ensure that the price at which all or any of the subjects are sold is the best that can reasonably be obtained."
>
> (Conveyancing and Feudal Reform (Scotland) Act 1970, section 25)

39. In my view, where the directors of an insolvent company are conducting an informal winding up by disposing of the company's assets and are unable as a result of circumstances beyond their control to carry out a full marketing exercise, the sale should be measured against that standard. Lord Davidson accepts the approach of comparing a private sale with a sale in a winding up or a sale by the holder of the standard security in his submission to the court that the Inner House has erred in adopting a comparison with the open market value. But it is necessary to have regard to these duties imposed on the insolvency practitioner and the holder of a standard security when making the comparison which he advocates.

iii) The application of the law to the facts of this case

40. It is clear from the evidence of Mr Quinn that after Grampian's invoice factor withdrew its factoring facility, he was not able to obtain alternative funding and so disposed of the assets by which Grampian carried on its business. The sale of the Property, which was Grampian's distribution centre, following the sale of its vehicles was in effect part of an informal winding up of the business. There is no justification for the off-market sale of the Property at a price so far below market value on the ground of urgency. There was no evidence that Grampian had sought NatWest's agreement that it should place the property on the open market. Even if one can infer from Mr Quinn's evidence that such a marketing exercise was not possible, Carnbroe has not established that there was adequate consideration as it led no evidence to support the view that a sale by NatWest or a sale by the liquidator

with NatWest's consent would have been likely to achieve a price net of expenses which was comparable to or less than the sale price which Grampian accepted. The Inner House was therefore entitled to interfere with the Lord Ordinary's assessment as to whether there had been adequate consideration.

41. In reaching this view, I have sympathy for the predicament of the Lord Ordinary as Carnbroe ran its defence on the basis that an urgent sale was required to preserve Grampian's business and it does not appear from the pleadings and written submissions which were provided to this court that the liquidators' legal team challenged this submission. It does not appear that they argued, as they did in the Inner House, that the evidence did not support the justification of the discounted price on the basis of urgency because Grampian's business was at an end. If there were such a failure, it might in other circumstances have justified a modification of an award of expenses. But in this case Carnbroe's failure to pay the whole of the contracted purchase price until after the proof had been completed caused the Lord Ordinary to award expenses in favour of the liquidators, notwithstanding that they lost before him. There is therefore no basis for interfering in the award of expenses at first instance.

42. Absent evidence that the £550,000 which Carnbroe eventually paid for the Property was equivalent to the price which NatWest or a liquidator would be likely to obtain for the Property after deduction of the likely expenses of sale and other costs incurred as a result of a delay in achieving the sale, Carnbroe failed to establish that the Property had been sold for adequate consideration. I therefore agree with the conclusion of the Inner House, albeit for reasons which are not precisely the same.

43. That would be sufficient to dispose of the appeal if the question of remedies had not arisen in debate. I therefore turn to that question.

iv) The statutory remedies

44. To provide context for discussing the remedies which the court can give to reverse a gratuitous alienation, it may be useful to summarise the position. First, at common law and under the 1986 Act it is not a condition of a challenge to a transaction that either the transferor or the transferee has knowledge of the transferor's insolvency. Where the alienation that is wholly gratuitous is made by an insolvent to his or her family or to a close business associate one would expect in the normal course that the insolvent transferor and the transferee would have some knowledge of the transferor's financial difficulty. But no such knowledge need be proved. Secondly, the 1985 statutory reforms for the first time have imposed on a transferee, who is not an associate of the insolvent transferor, the burden of establishing the circumstances in section 242(4) which exclude the court's power to

reverse the alienation. This is a point to which I will return in para 62 below. Thirdly, the test for “adequate consideration” is an objective test which takes account of all the circumstances, including circumstances of which one or both of the parties to the transaction may not have been aware, such as the transferor’s insolvency and the objective purpose of the transaction.

45. There is therefore a significant risk that a bona fide purchaser without knowledge of the seller’s insolvency or the reason why the seller is willing to sell at a price substantially below open market value may be exposed to a challenge which he or she cannot defend. It is not realistic in a commercial negotiation to expect a purchaser to ask a seller why he or she is not demanding a higher price. It was this concern that caused the court during the hearing to raise the question of the court’s discretion in giving a remedy under section 242(4) of the 1986 Act. In response, counsel referred the court to three cases which addressed the equivalent provision in personal bankruptcy (section 34(4) of the Bankruptcy (Scotland) Act 1985), which provided that on a challenge being brought “the court shall grant decree of reduction or for such restoration of property to the debtor’s estate or other redress as may be appropriate”.

46. In the first, *Short’s Trustee v Chung* 1991 SLT 472, a man purchased two flats at a significant undervalue from an insolvent and conveyed them for no consideration to his wife. The insolvent’s permanent trustee successfully challenged the sales as gratuitous alienations. Before the Lord Ordinary and on a reclaiming motion to the Second Division the wife, whose husband had died before the challenge, submitted that the court had a discretion under section 34(4) to make an appropriate order, which, she submitted, was not a reduction of the dispositions but an order for payment of the difference between the price which her husband had paid and the market value of the flats at the date of the alienation. It does not appear that the wife, who as the ultimate transferee was the defender of the action, argued that it was inequitable to reduce the dispositions because she would not be able to recover the (inadequate) consideration paid. This may be because her husband had paid the consideration and she had been a gratuitous disponee of the flats from him. It is not clear from the report that she had title to seek repetition of the price which he had paid. The argument of her counsel was that it was inequitable to reduce the dispositions (a) because the wife would rank as a postponed creditor in the insolvency under section 51(3)(c) of the Bankruptcy (Scotland) Act 1985, which governed her right to recover the properties or the proceeds of their sale and (b) because the properties had increased in value significantly since the date of the alienation. The Second Division (the Lord Justice-Clerk (Ross) and Lord McCluskey and Lord Sutherland) upheld the trustee’s contention that the section did not give the court a general equitable discretion and that the statutory words, “or other redress as may be appropriate”, were designed to enable the court to make an appropriate order in a case where reduction or restoration of the property was not available as a remedy. In the opinion of the court, which Lord Sutherland delivered, it is stated at p 476:

> "The starting point in a case of this nature for interpretation of section 34(4) is that the original alienation has been avoided and the transaction has been vitiated. This is not a good starting point for an argument which is based solely on equity. It is in our opinion clear from a reading of section 34(4) that the general purpose is to provide that as far as possible any property which has been improperly alienated should be restored to the debtor's estate. In the case of a disposition of heritable property this can easily be done by reduction of that disposition. We consider that the reference to 'other redress as may be appropriate' is not intended to give the court a general discretion to decide the case on equitable principles but is designed to enable the court to make an appropriate order in a case where reduction or restoration of the property is not a remedy which is available."

47. The Second Division (the Lord Justice-Clerk (Cullen) and Lord McCluskey and Lord Morison) confirmed this approach in the second case, *Cay's Trustee v Cay* 1998 SC 780. In that case an insolvent transferred to his wife £34,885.11, which were the proceeds of sale of his share of a fishing licence. In response to a challenge by the insolvent's permanent trustee, she argued (i) that she had given adequate consideration because she had undertaken in return to pay and had paid certain of his debts amounting to over £20,000 and had undertaken to use the balance of the sum transferred to pay household bills. The court accepted that the undertaking to pay £20,000 towards the insolvent's debts was consideration but rejected the submission that the use of the balance to pay household bills could be treated as consideration as she was under a pre-existing statutory duty to aliment her insolvent husband. The court held that the undertaking to pay and payment of £20,000 was not adequate consideration and rejected her alternative argument that she was entitled to set off that sum against the demand for repayment of the sum which she had received, holding that section 34(4) did not confer a general equitable jurisdiction on the court. The court stated at p 788:

> "We consider the court in *Short's Trustee v Chung* correctly held that the section did not create any general discretion to decide on equitable principles to order something less than a full return of the alienated property."

48. The third case, *Baillie Marshall Ltd v Avian Communications Ltd* 2002 SLT 189, is an opinion of Lord Kingarth in the Outer House on a challenge to an unfair preference under section 243 of the 1986 Act, in which subsection (5), providing for remedies, is in substantially the same terms as section 34(4) of the Bankruptcy (Scotland) Act 1985 and section 242(4) of the 1986 Act. In this case an insolvent company transferred its assets and business to the defender for a consideration which

included the payment of the debts of the transferor company's trade creditors but not its other creditors. The liquidator did not seek to annul the alleged unfair preferences to recover funds from the trade creditors who had been paid their debts but concluded for payment by the defender of damages measured by the alleged loss to the remainder of the unsecured creditors. Lord Kingarth held that such a remedy was not available under section 243. Referring to *Short's Trustee v Chung* and *Cay's Trustee v Cay*, he stated, at para 22:

> "It seems to me to be reasonably clear, notwithstanding the apparent width of the language of subsection (5) (in particular 'or other redress as may be appropriate') that the purpose of the section as a whole is to enable the liquidator (amongst others) to undo, so far as possible, what was done when the preference was created … and, so far as possible, to restore the asset position of the company, diminished by the transaction which created the preference, for the benefit of the general body of creditors. There would appear to be no doubt that the primary remedies envisaged are reduction and restoration of property, and … that the words 'or other redress as may be appropriate' properly fall to be construed as relating to redress of the same character, and do not give the court a general equitable jurisdiction."

49. I am satisfied that the provisions in the 1986 Act providing remedies against gratuitous alienations (section 242(4)) and unfair preferences (section 243(5)) and the equivalent provisions in the bankruptcy legislation do not confer a general equitable jurisdiction. It is clear from the law before the 1985 statutory reforms that the principal remedy available in challenges to both gratuitous alienations and unfair preferences was the annulment of the impugned transaction. That remains the primary remedy after the 1985 statutory reforms. There is a strikingly contrasting juxtaposition in the Bankruptcy (Scotland) Act 1985 of the remedies made available to reverse gratuitous alienations and unfair preferences (sections 34(4) and 36(5) respectively) and the wider power which section 35 conferred on the court to recall an order made against the insolvent on divorce for the payment of a capital sum. In contrast with sections 34(4) and 36(5), the court was enabled under section 35, when deciding whether to order the repayment of the whole or part of a sum paid or property transferred, to have regard to the whole circumstances including the financial and other circumstances of the person against whom the order would be made. This conferred a general equitable jurisdiction which the statutory remedies for gratuitous alienations and unfair preferences do not entail.

50. It is also well established that the transferee of a gratuitous alienation or the recipient of an unfair preference cannot set off sums due to it by the insolvent for different purposes as that would defeat the purpose of sections 242 and 243 of the

1986 Act: *Raymond Harrison & Co's Trustee v North West Securities Ltd* 1989 SLT 718, 724E; *John E Rae (Electrical Services) Linlithgow Ltd* (above), 791; *Cay's Trustee* (above), 787-788.

51. But commentators on the statutory provisions have criticised the disproportionate consequence of annulling the transaction when the transferee has paid a significant albeit inadequate sum for the alienated property and is made to rank as an ordinary creditor in relation to his claim for unjustified enrichment: *St Clair and Drummond Young, The Law of Corporate Insolvency in Scotland*, 4th ed (2011), para 3.10. An order for the restoration of the property to the insolvent company, which leaves the transferee to prove in competition with other creditors for the price which it originally paid, not only is harsh on the transferee but also gives the general body of creditors an uncovenanted windfall as the company would not have received the price but for the impugned sale.

52. Lord Davidson and Mr Brown in their written submission for Carnbroe point out the anomalous results to which *Short's Trustee* can give rise. They set out four circumstances. First, if an insolvent dispones heritable property gratuitously to a transferee, who holds it when the liquidator mounts a challenge under section 242, reduction is available and the company receives back the property but obtains no windfall at the transferee's expense. Secondly, if the gratuitous transferee sells the property to a bona fide third party for full value before the liquidator's challenge, the court would grant "other redress" which would be an order to account to the liquidator for the value of the alienated property obtained in that sale. This would achieve essentially the same financial outcome as reduction in the first example. If, thirdly, the transferee paid a consideration for the property which was substantial but was not "adequate consideration", reduction of the disposition would have the effects which I discussed in para 51 above: the creditors receive a windfall and the transferee is significantly worse off than if it had declined to purchase the property or if it had paid full value. Fourthly, if the purchaser/transferee in the third example has sold on to a bona fide third party for full value before the liquidator mounts a challenge, the court could only order "other redress". The court would have the power to order the payment to the insolvent estate of the shortfall of consideration in the original sale; the court would not have to order the purchaser/transferee to disgorge the whole of the onward sale price and rank as an unsecured creditor for the repayment of the price which it had paid in the original sale.

53. Is the court constrained to interpret section 242 of the 1986 Act so as to compel such a harsh and anomalous result as mentioned in para 51 above when there is a sale at an undervalue? In my view it is not. The words themselves ("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") do not compel such an interpretation. The statutory phrase does not speak of the court granting "remedy X, which failing remedy Y". I do not see the eiusdem generis principle as a helpful tool in this case

where the list comprises only two specific decrees. Further, the use of "or" cannot have been intended to be exclusively disjunctive as there will be cases where an insolvency practitioner seeks the restoration of different types of property in the same action and may have conclusions for the reduction of dispositions and the reconveyance of heritable property as well as for payment of money which has been alienated. I would read "or" in its context as being both conjunctive and disjunctive (ie "and/or"). In my view the statutory words are broad enough to allow the court to take account of the consideration which a bona fide purchaser has paid the insolvent in devising an appropriate remedy.

54. Mr McBrearty QC and Ms Ower for the liquidators in their post-hearing written submissions advance two principal arguments against this conclusion. First, they rely on rule 4.66 of the Insolvency (Scotland) Rules 1986, which has been re-enacted as rule 7.27 of the Insolvency (Scotland) (Receivership and Winding Up) Rules 2018 for the contention that the transferee, which is subjected to a reduction of a disposition under section 242, is penalised by the designation of its claim for repetition of the purchase price which it has paid as a postponed debt, giving it the lowest priority in the distribution of an insolvent estate. In my view this assertion is misconceived. Paragraph 2(i) of the relevant rule provides that a postponed debt includes:

> "a creditor's right to any alienation which has been reduced or restored to the company's assets under section 242 or to the proceeds of sale of such an alienation."

It is clear from the plain words of this provision that the postponed debt is the transferee's right to reclaim the property which had been alienated or the proceeds of sale of that property. It addresses the right of a transferee to reclaim the property, which had been alienated and restored to the insolvent estate, if a surplus emerged in a winding up. It does not address the claim in unjustified enrichment of a transferee which has paid an inadequate consideration for the repetition of the sums which it has paid which is inconsistent with any right to a reconveyance of the property to the transferee. The provision therefore does not support a contention that Parliament intended to penalise the gratuitous alienee in relation to a claim for unjustified enrichment.

55. Secondly, they submit that the Scottish Parliament has re-enacted the equivalent of section 242 in personal insolvency (section 34(4) of the Bankruptcy (Scotland) Act 1985), which was the subject of the decisions in *Short's Trustee* and *Cay's Trustee*, in section 98(5) of the Bankruptcy (Scotland) Act 2016 ("the 2016 Act"). Section 98(5) provides:

> "On a challenge being brought under subsection (2), the court must grant decree -
>
> (a) of reduction, or
>
> (b) for such restoration of property to the debtor's estate, or such other redress, as may be appropriate."

The 2016 Act is a consolidation Act which follows on the Scottish Law Commission's *Report on the Consolidation of Bankruptcy Legislation in Scotland* (2013) (Scot Law Com No 232). It is intended to restate the law but not change it. Counsel for the liquidators submit that by re-enacting section 34(4) in these terms the Scottish Parliament should be presumed to have endorsed the Inner House's approach in *Short's Trustee* and *Cay's Trustee*. They refer in this regard to the "*Barras* principle": *Barras v Aberdeen Steam Trawling and Fishing Co Ltd* 1933 SC (HL) 21; [1933] AC 402 and *R (N) v Lewisham London Borough Council* [2015] AC 1259.

56. The *Barras* principle is only a presumption and it is not without controversy. Lord Wilberforce and Lord Simon of Glaisdale doubted the validity of the principle in *Farrell v Alexander* [1977] AC 59, 74F-G and 90E-91C, Lord Neuberger of Abbotsbury has expressed strong reservations as to its propriety and its operation in *R (N)* (paras 143-148), and Lord Lloyd-Jones has expressed similar reservations in *R (Belhaj) v Director of Public Prosecutions (No 1)* [2019] AC 593, para 46. In any event, the principle cannot apply in this case as the 2016 Act is a consolidation Act: *Haigh v Charles W Ireland Ltd* 1974 SC (HL) 1, 40; [1974] 1 WLR 43, 57, per Lord Diplock; *MacMillan v T Leith Developments Ltd* [2017] CSIH 23, para 109 per Lord Drummond Young. In that paragraph Lord Drummond Young stated:

> "If all that Parliament is doing in a consolidation statute is to reproduce the existing law, with no scope for significant change, it cannot be said that there is any genuine endorsement of any cases interpreting the statutes concerned. There is no power to do so."

I agree with that statement; the re-presentation of the same statutory phrase in two sub-paragraphs in section 98(5) of a consolidation statute cannot amount to a parliamentary endorsement of prior case law.

57. Even if such a presumption applied, I am not persuaded that it would be sufficient to support the liquidators' case. It would be necessary to put in the balance

against it both the harsh and anomalous results which I have mentioned and the mismatch between the interpretation in *Short's Trustee* and *Cay's Trustee* on the one hand and the established principled approach of Scots common law on the other, both of which are matters which the senior courts have not addressed.

58. The general approach of the law is that when a person seeks to annul a transaction, for example on the basis that a contract was induced by fraudulent or innocent misrepresentation, the court will only grant decree of reduction if it is able to place the defender substantially in the position it would have been in if the parties had not entered into the impugned contract: *Boyd & Forrest v Glasgow and South Western Railway Co* 1915 SC (HL) 20, 28 per Lord Atkinson, 36-37 per Lord Shaw of Dunfermline. In *Spence v Crawford* 1939 SC (HL) 52 the House of Lords made it clear that the court has power to order monetary adjustments to restore the defender to its pre-contract position. Lord Wright stated at p 77:

> "… restoration is essential to the idea of restitution. To take the simplest case, if a plaintiff who has been defrauded seeks to have the contract annulled and his money or property restored to him, it would be inequitable if he did not also restore what he had got under the contract from the defendant. Though the defendant has been fraudulent, he must not be robbed nor must the plaintiff be unjustly enriched, as he would be if he both got back what he had parted with and kept what he had received in return. The purpose of the relief is not punishment, but compensation."

59. It appears from the limited authorities that are available that the law before the 1985 statutory reforms provided as the only remedy the annulment of the gratuitous alienation if such annulment was possible. Where the alienation was wholly gratuitous, the question of restitution of the defender did not arise. But where the insolvent had sold at an undervalue the law did not provide for a general restitutio in integrum: *Tennant v Miller* (above). Similarly, in relation to fraudulent preferences, *Bell's Commentaries* (above), (p 217), in addressing the 1696 Act (c 5) (viz para 25 above), stated:

> "It may be questioned whether the success of the reduction is to be accompanied by a *restitutio in integrum*, so that the defender shall hold the same advantages when deprived of the security, which he would have enjoyed had he never accepted it. The answer seems to be, that a *restitutio in integrum* is no part of the reduction on the Act 1696, nor necessarily implied as a condition of it; but that as the creditors are entitled to reduce only in so far as the deed is prejudicial to them, their

> success will be limited to the effect of restoring them to the full benefit of the rights they would have enjoyed had the deed never been granted."

Bell went on to state, as an example, that if a creditor had renounced a security which he had held over any part of the insolvent's estate in exchange for the impugned security, he would be entitled to the full benefit of the old security when the new security was annulled, because it was only to the extent of the difference that the new security could be said to be prejudicial to prior creditors.

60. Further, in *Thomas v Thomson* (1866) 5 M 198, which concerned an application by a trustee in bankruptcy to annul a security in the form of an ex facie absolute disposition on the ground that it was a fraudulent preference, the court ordered a partial reduction only, which preserved the security in so far as it secured a debt which was not a preference. The prior law was thus not wholly inflexible and allowed a partial restitutio in integrum in the context of the annulment of the document which effected the preference.

61. Reduction was also not the only remedy under the prior law. Where the transaction could not be nullified, for example where property which an insolvent company had purchased from one of its directors at an overvalue had been sold to a third party in good faith and for value, the court allowed the liquidator to recover from the director a sum of money representing the difference between the inflated price paid and the true value of the property at the date of the transaction: *Abram Steamship Co Ltd* (above). In that context the remedy reflected the disadvantage which the company's creditors had suffered as a result of the impugned transaction and gave them no windfall.

62. The law before the 1985 statutory reforms appears to have been a partial exception to the general principle that the annulment of a transaction necessarily involved restoring the defender to its pre-transaction position. But there is only very limited case law on the point, which the Scottish Law Commission did not discuss. The 1985 statutory reforms, by imposing on a purchaser, who is not an associate of the insolvent, the burden of proving adequate consideration was paid, have increased the risk that a bona fide purchaser may suffer injustice if there is no flexibility in the remedies which the court can give. Such an outcome would also deter rescue transactions involving the purchase of assets from distressed businesses and hamper the rescue culture which statutory insolvency law has sought to promote. These considerations point towards a more flexible interpretation of the remedies provided in section 242(4). But, as I have said, there is nothing in the Scottish Law Commission's report which explains the policy behind its recommendation which has found its way into section 242 of the 1986 Act.

63. The court must therefore fall back on the statutory words, which are broad enough to allow the court in an appropriate case, and if justice requires it, to devise a remedy to protect the bona fide purchaser of property from a reversal of its purchase which would otherwise give the creditors of the insolvent a substantial windfall at its expense. The general approach to the annulment of transactions requires no more from a fraudster than that he or she compensate the victim, as Lord Wright stated in *Spence v Crawford* (para 58 above). Section 242(4) does not mandate restitutio in integrum in every case. But neither does it exclude such restitution as part of the appropriate remedy.

64. It is not open to doubt that an insolvency operates adversely on the insolvent's unsecured creditors who have paid for goods or services which they have not received or have provided goods or services and not been paid. Gratuitous alienations or unfair preferences by an insolvent can cause further harm to unsecured creditors. The pre-1985 law, by not requiring full restitutio in integrum, had the benefit of discouraging transferees from entering into transactions by which an insolvent person transfers his or her assets gratuitously or at an undervalue. Since the 1985 statutory reforms, there may be circumstances in which the court considers it appropriate to annul a transaction which was a gratuitous alienation without also ordering the repayment of the inadequate consideration, thus leaving the transferee to rank an unsecured claim for unjustified enrichment in the insolvency. For example, business associates of an insolvent might knowingly seek to obtain property at an undervalue to the prejudice of the insolvent's creditors. The words of section 242(4) of the 1986 Act leave open that option to the court. But there would in my view need to be clear statutory words to require the court in all circumstances to penalise the purchaser of property who had no knowledge or incomplete knowledge of the circumstances of the insolvent and who was not colluding to remove assets from the reach of the insolvent's creditors. There are no such words in the subsection.

65. There will be cases in which, as the commentators have suggested, it would be wholly disproportionate and unfair to annul the property transfer without giving the bona fide purchaser credit for the consideration which it has paid. In my view, section 242(4) gives the court sufficient power to devise an appropriate remedy. This does not involve a general equitable jurisdiction to take account of the personal and financial circumstances of the defender such as was envisaged by section 35 of the Bankruptcy (Scotland) Act 1985 (now section 100 of the 2016 Act). Nor does this approach call into question Lord Kingarth's conclusion that section 243 (and by analogy section 242) does not allow a liquidator to seek what was in substance damages from a defender. The question for the court is simply whether in devising a remedy for the gratuitous alienation by restoring property or value to the insolvent's estate in a particular case it should order that credit be given in some way for the consideration which a bona fide purchaser has paid. In so far as *Short's Trustee v Chung* and *Cay's Trustee v Cay* held that the court did not have this power, I respectfully conclude that they were wrongly decided and should not be followed.

66. The question of whether the subsection is consistent with article 1 of the First Protocol to the European Convention on Human Rights ("A1P1") does not arise in this context. This is because there is no need to read down the words of section 242(4) to avoid a disproportionate result as there is nothing to prevent the court in a particular case from taking account of the consideration paid by the transferee in devising the remedy. Because of that determination, I also see no reason to question the conclusion which was reached in cases in the Outer House that Parliament acted within its wide margin of appreciation in providing for remedies against gratuitous alienations and unfair preferences in the 1985 statutory reforms without creating a general equitable jurisdiction that takes account of the defender's personal and financial circumstances: *Accountant in Bankruptcy v Walker* [2017] CSOH 78; 2017 SLT 890; *Johnston's Trustee v Baird* [2012] CSOH 117.

67. There may also be cases where the purchase of the alienated property is wholly funded by borrowings and the bona fide third party lender's security is protected by the proviso to section 242(4), enabling it to recover its lending by calling up its security or by allowing the liquidator to realise the secured asset in the winding up without pursuing recovery from its borrower other than as a formality. In such case there would be no call for the court to qualify in any way its annulment of the transfer as the interested parties themselves can achieve substantive restitutio in integrum.

68. Counsel for the liquidators inform the court that the liquidators have recognised the validity of the Bank's security by virtue of the proviso to section 242(4). As a result, if the Bank still had a claim for the sums it had lent to Carnbroe, Grampian's creditors would receive no windfall through the reduction of the disposition of the Property. But in written submissions since the hearing, backed by supporting documents, counsel for Carnbroe inform the court that Carnbroe repaid its borrowings for the purchase of the Property in July 2016. Counsel also explain that Carnbroe has recently re-financed and consolidated its borrowings by taking out a facility from Together Commercial Finance Ltd ("TCFL"). Counsel state that the Bank's securities over the Property have been discharged and that there are now no securities covering the Property. But these are not, as yet, agreed facts, in part because Carnbroe's lawyers have not authorised the Bank to confirm the position to the liquidators' lawyers and in part because the re-financing by TCFL has occurred very recently. It ought to be straightforward for Carnbroe to provide documents to vouch these assertions to the liquidators and for the liquidator's advisers to search in the Land Register and at Companies House to avoid further dispute about these facts.

69. In the light of this judgment and the absence of agreed facts, it is necessary to afford the First Division an opportunity to consider whether it is appropriate in the circumstances of this case to qualify the remedy of reduction which it has given to take account of all or part of the consideration which Carnbroe gave for the

purchase, for example by requiring the liquidators to pay a specified sum to Carnbroe as a condition of the reduction.

Conclusion

70. I would allow the appeal but only to the extent that I would remit the case to the First Division to consider what is the appropriate remedy under section 242(4) in the light of the court's power to give appropriate redress.