INSOLVENCY BULLETIN

Volume 3, Issue 12 October 2022

AT LAST, A DECISION ON SEQUANA

When does a director's duty to promote the success of a company become fettered by a conflicting duty to consider the interests of that company's creditors? In *BTI 2014 LLC (Appellant) v Sequana SA and Ors (Respondents) 2019/0046 UKSC* the Supreme Court has had its first opportunity to consider the nature of creditor duty and where that duty sits within corporate decision making.

In 2009, Sequana SA ("Sequana") received a €135 million dividend from AMA, a company it owned. AMA had a long term contingent liability in respect of pollution related litigation in the US. That contingent liability was " *a real risk, although not a probability, that AMA might become insolvent at an uncertain but not imminent date in the future".* Even so, in 2009 AMA was solvent on both a cash flow and a balance sheet basis. Almost 10 years later AMA entered insolvent administration. The assignee of AMA's claims ("BTI") attempted to recover the dividend payment by arguing that AMA's directors had not considered or acted in the interests of its creditors.

The Existing Law

Under S172(1) Companies Act 2006, a director has a duty to promote the success of a company, although under S172(3) CA 2006 such a duty is *"subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company".*

The rules on dividend payments are governed by Part 23 CA 2006 which identifies that dividends are payable from distributable profits. The "Rule in West Mercia" confirmed that under the common law a director's duties shift towards creditors in the proximity of insolvency.

The Position "Post-Sequana"

The Supreme Court stated that there is an enduring list of cases confirming creditor duty, supported by S172(3) CA 2006. Creditors have an interest in a company's assets which increases when a company approaches or enters insolvency, giving that duty a "*coherent or principled justification".* Creditor duty is one aspect of a director's fiduciary duty.

Creditor duty was not engaged in this case, and so BTI's appeal to the Supreme Court failed, as when the dividend payment was made by AMA insolvency was not likely or even probable. Creditor duty is engaged when a director *"knows or ought to know that the company is bordering on insolvency or is insolvent. The greater the company's financial distress then the more the directors should take into account creditor interest."*

The Supreme Court also confirmed that an otherwise lawful dividend can be subject to creditor duty, because Part 23 CA 2006 is subject to any law to the contrary (in this case the common law) and also because *"it cannot be the case that the directors of a company which is cash-flow insolvent…could lawfully distribute a dividend."* Shareholders cannot ratify a decision which is in breach of creditor duty.

Editor's Note

The responsibility to be fully aware of a company's financial status before authorising distributions lies with its directors. It would be wise, particularly in the current economic environment, to seek advice and determine whether a company is on the edge of insolvency or insolvent, before making such decisions.

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