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Judgment: approved by the Court for handing down (subject to editorial corrections) | ***Delivered:*** **5/10/12**

2011/149766/149767/140124

IN THE HIGH COURT OF JUSTICE IN NORTHERN IRELAND

CHANCERY DIVISION (BANKRUPTCY)

BETWEEN:

ANDREW HUTCHINSON
LESLIE ROSS
JONATHAN FINCH

Applicants.

and

BANK OF IRELAND (UK) PLC

Respondent.

MASTER KELLY

[1] In this case Mr Hutchinson, Mr Ross and Mr Finch ("the applicants") seek to set aside statutory demands issued against them by the respondent bank ("the bank") on foot of personal guarantees ("the guarantees")executed by them in favour of the bank, in the sum of £1,400,000. The guarantees and the £1,400,000 relate to facilities extended by the bank to property development companies of which the applicants were directors. The case for the applicants is substantively made out on their individual grounding affidavits. Mr Hutchinson appears to be a chartered surveyor with (by his own admission) a long standing involvement in the fuel distribution business and he describes Mr Ross as a chartered town planner and Mr Finch also as a chartered surveyor. The case for the bank is made out on the affidavit of Mr

Jed Murray, Senior Business Manager in the bank's Challenged Lending Team.

[2] The applications were filed on 22nd December 2011 and first mentioned before the court on 30th January 2012. Following an exchange of affidavits the substantive hearing took place on 25th June 2012. There was no oral evidence given by the deponents and the matter was disposed of by way of counsels' submissions. Mr Shields appeared for the applicants and Mr Gowdy for the respondent. I was greatly assisted by their careful conduct of the case and helpful oral and written submissions.

Background to the applications.

[3] The background to this case appears relatively straightforward but the evidence is obfuscated somewhat by the differing roles the applicants held in their dealings with the bank at the various relevant times. The principal loans to which the guarantees apply relate to facilities secured by the applicants on behalf of their companies in their capacity as company directors. They executed the personal guarantees as individuals.

[4] Briefly, the applicants say that in 2005 the bank approached them via a Mr Niall Devlin from the bank in an effort to attract their business. They were it seems customers of another bank around this time. The applicants say at this time they had a business known as Tamlaght Estates. It is not clear whether this company was a limited company but in any event it is submitted that it held a small property portfolio. The applicants state that both they and the bank had a mutual interest in property investment. They say the bank was actively seeking their business for this purpose and that two limited companies were set up of which the applicants were directors and to which the bank provided funding. The companies were known as Tamlaght Developments Ltd and RBT Properties Ltd. This does not appear to be a matter of dispute.

[5] Following the formation of these two companies the affidavits show a significant amount of property development business was pursued by RBT Properties Ltd and Tamlaght Developments Ltd with financing from the bank. Almost none of this formed part of the hearing, but it is noteworthy that the property development involved seemed to be on a significant commercial scale and included plans for a nursing home, hotel, retail unit and filling station. From their own evidence the applicants appear to be experienced businessmen.

[6] The main thrust of the applicants' case is what they claim to be an unsatisfactory chain of events involving themselves and the bank regarding the purchase of two sites by their property development companies in or about 2006. They allege the bank actively encouraged them to try to purchase

these sites as they were adjacent to a site which the applicants' company was already interested in acquiring, with funding from the bank. The acquisition of all three sites they contend would have maximised their development potential to the mutual benefit of the companies and the bank. They allege that Mr Devlin informed them that these sites were being developed by a company known as Rosslan which was an existing customer of the bank and apparently in financial difficulties. They further allege that Mr Devlin encouraged them to approach Rosslan directly to purchase these sites for which the bank would provide funding. The applicants said they did in or around November 2006 and entered into a contract with Rosslan for those said sites.

[7] The applicants argue that during 2007, the exact date is unclear, Rosslan's financial situation led to enforcement action being taken by the bank. This would appear to mean that the bank had placed Rosslan into Receivership. The applicants say that following this Mr Devlin approached them and that an agreement was reached with the bank whereby the applicants would pull out of their existing (and apparently binding) agreement for the purchase of the Rosslan sites and deal directly with the bank, the inference being that they could now purchase the same sites directly from the bank or with the consent of the bank for a lower sum.

[8] Having pulled out of the contract with Rosslan, the applicants allege that having been led to believe they could purchase these sites through the Receivership, they had to engage in a bidding process which saw the sites eventually sold to a third party in what they believe to be contentious circumstances. The manner in which this bidding process was conducted they imply was unsatisfactory if not unlawful and clearly left them feeling aggrieved. It is their contention that the statutory demands are an attempt by the bank to avoid litigation with the companies which would reveal impropriety on the part of the bank. I pause there to clarify two matters. The first is that the bank chose not to respond to these issues in the course of the proceedings and I will return to that later, and the second is that while more grievances are outlined in the applicants' affidavits, it is this particular grievance which was the focus of the hearing and central to the application.

[9] While the exact chronology of the above events is somewhat vague, there are a number of facts which do not appear to be in dispute. It is not a matter of dispute that during this period of time Tamlaght Developments Ltd and RBT Ltd obtained company loans from the bank and said loans were payable on demand. It is also not in dispute that each applicant executed three personal guarantees to the bank for company loans that were repayable on demand. Nor is it a matter of dispute that each guarantee imposed an unconditional and irrevocable continuing obligation on the guarantor to repay on demand the sums referred to therein, or that all three guarantees were limited to specific sums:-

(i) Guarantee 17th May 2006 was limited to an amount not exceeding £400,000.00 for RBT Properties Ltd together with interest fees and charges.

(ii) Guarantee 20th October 2006 was limited to an amount not exceeding £500,000 for RBT Properties Ltd together with interest fees and charges

(iii) Guarantee 16th April 2007 was limited to an amount not exceeding of £500,000 for Tamlaght Developments Ltd together with interest fees and charges.

Each applicant completed the "Personal Guarantors Certificate Concerning Independent Legal Advice" section of the guarantee in his own handwriting stating that prior to executing the guarantee he had been advised by his solicitor as to the nature and terms and effect of the guarantee. In the case of the latter two guarantees the applicants' solicitor also confirmed this in writing to the bank.

[10] The applicants' evidence as to how these guarantees came to have been sought from them is negligible. There appears to be no mention at all of the circumstances in which they arose in the applicants' grounding affidavits. As appears, the issue was raised for the first time in Mr Hutchinson's second affidavit, the contents of which were adopted by Mr Finch and Mr Ross. Yet in his second affidavit Mr Hutchinson refers only to the third guarantee. In this affidavit he attributes the execution of the third guarantee to the purchase by one of the companies of a property in Dunfanaghy at auction on 2nd March 2007, at which a non-refundable deposit in excess of £100,000 was paid and a binding contract signed. This purchase at auction he says took place on the strength of an understanding the company had that the bank would fund it. However, there does not appear to be any evidence that the bank had at that stage given any commitment to do so and when the bank eventually issued a letter of offer on 30th March 2007 it was accompanied by a requirement for the applicants to sign a personal guarantee. The applicants say that as there was a binding contract in place they had no alternative but to execute the guarantee in order to secure the bank's loan to the property development company. With the exception of this particular incident, the applicants offered no other evidence in respect of any of the guarantees. There is no evidence that they objected to having to give them or of any attempt on their part to negotiate terms.

[11] Mr Murray in his affidavit for the bank states that as at 27th June 2011 the bank demanded repayment of facilities from Tamlaght Developments Ltd and RBT Properties Ltd. As at that date Tamlaght Developments Ltd seems to have been indebted to the bank in the sum of £559,026.66 and €1,386,756.61. As appears, RBT Properties Ltd was indebted to the bank as at the same date in the sum of £2,082,536.13. On 28th June 2011 the bank called in all three

guarantees from the applicants. The total amount claimed on foot of the guarantees is £1,400,000 and this is the sum claimed on the individual statutory demands.

[12] Each of the guarantees has two identical clauses upon which the bank relies.

Clause 25:

> "Every obligation of the Guarantors arising under this guarantee shall be discharged in the same currency as that of the corresponding principal debt of the Customer. All payments to be made hereunder by the Guarantors shall be made to the Bank without any set-off our (sic) counterclaim and without any deduction for or on account of any present or future taxes, levies, collected, withheld or assessed unless the Guarantors are compelled by law so to do. If so compelled the Guarantors shall pay such additional amounts as may be necessary in respect of their obligations hereunder in order that the net amounts after such taxes, levies, imposts, duties, deductions, witholdings or other charges shall equal the respective amounts due hereunder."

Clause 28(ii):

> "The Guarantors hereby agree that in any litigation relating to these presents the aforesaid obligation or any security therefor (sic) they shall waive the right to interpose any defence based upon any claim of laches or set-off or counterclaim of any nature or description."

In other words the Guarantees contain a "no set-off" clause.

[13] In my view the case for the applicants is summarised in the second affidavit of Mr Hutchinson sworn on 23rd April 2012 the contents of which have been adopted by Mr Ross and Mr Finch. At paragraphs 3-8 of his affidavit Mr Hutchinson argues:

> "3. I have been shown the affidavit of Mr. Murray and I note that rather than reply to the matters set forth in my previous affidavit, Mr. Murray seeks only to rely upon two clauses within the Deeds of Guarantee, being respectively Clauses 25 and 28(ii). It is claimed that by reason of these clauses I and the other alleged guarantors should be prevented from making the defences previously set out.
>
> 4. I dispute this on a number of grounds.
>
> 5. Firstly, I am advised and believe that the clauses sought to be relied upon by the Bank are unlawful by reason of the Unfair Contract Terms Act 1977. I am advised and believe that the burden of proof lies upon the Bank to demonstrate the lawfulness of the terms under this legislation and in the current circumstances. I expand upon this below.
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> 6. Secondly, I believe that the matters I have previously set out in my affidavit of 22 December 2012, and in particular what I believe to be the

bad faith and breach of duty by the Respondent, are such as to discharge these guarantees in their entirety or to entitle the guarantors to rescind the guarantees in their entirety. I believe that in these circumstances the particular clauses sought to be relied on upon by Mr Murray.

7. Thirdly, I am advised and believe that as a matter of interpretation the particular clauses relied upon by Mr. Murray do not have application to the current circumstances. I am advised and believe that Clause 28(ii) applies only to "litigation" and that the current process (where the Respondent has failed to issue proceedings by Writ) is not included in the definition of litigation for the purposes of the Clause. I am further advised and believe that even if Clause 25 has application to debts of the principal debtor/company, it does not address my entitlement to raise a counterclaim on my own account against the Bank. Myself, Jonathan Finch and Leslie Ross have substantial claims distinct from those of the principal debtors under the guarantee. For example, we have suffered loss in respect of the shop that we intended to be operated at the Bushmills site. We had purchased this shop unit with the intention of developing a convenience retail store. The shop would generate profit which might reasonably have been in the range of £147,000 p.a. Due to the actions of the Respondent this opportunity was lost. There are loans that were made to the principal debtor companies (by other businesses connected with us) which have will now likely be prejudiced by the actions of the Respondent, in the sum of over £900,000.00.

8. Expanding on the issues relating to the Unfair Contract Terms Act 1977, I am advised that the Court may take into account the following matters in assessing the reasonableness of these terms:

a. the strength of the bargaining positions of the parties relative to each other, taking into account (among other things) alternative means by which the customer's requirements could have been met;
b. whether the customer received an inducement to agree to the term, or in accepting it had an opportunity of entering into a similar contract with other persons, but without having a similar term;
c. whether the customer knew or ought reasonably to have known of the existence and the extent of the term (having regard, among other things, to any custom of the trade and any previous course of dealing between the parties)."

[14] It seems to me that the applicants' case is therefore that:

(1) The bank acted in bad faith towards RBT Ltd and/or Tamlaght Developments Ltd.
(2) The bank was negligent and in breach of its fiduciary duty to them, and
(3) The "no set-off" clause was (a) invalid pursuant to the Unfair Contract Terms Act 1977, (b) that they weren't aware of this term, (c) that their attention should have been specifically drawn to it by the bank and (d) such a term is draconian in effect.

In short, the applicants contend that the guarantees are vitiated or rescinded and that they have a counterclaim against the bank. They argue that the burden fell on the bank to prove the validity of the clauses pursuant to the provisions of the Unfair Contract Terms Act 1977. In addition to which there is clearly an inference to actual or potential litigation between themselves and the bank although save for this application, there is no evidence that any exists.

The relevant law.

[15] The grounds that would allow the Court to set aside a statutory demand are set out in Rule 6.005(4) of the Insolvency Rules (Northern Ireland) 1991 which states:-

> "The Court may grant the application if –
>
> (a) the debtor appears to have a counterclaim, set off or cross demand which equals or exceeds the amount of the debt or debts specified in the statutory demand; or
> (b) the debt is disputed on grounds which appear to the Court to be substantial; or
> (c) it appears that the creditor holds some security in respect of the debt claimed by the demand, and either Rule 6.001(6) is not complied with in respect of it, or the Court is satisfied that the value of the security equals or exceeds the full amount of the debt; or
> (d) the Court is satisfied, on other grounds that the demand ought to be set aside".

[16] The onus is on the debtor to satisfy the court that the demand ought to be set aside on one of these grounds. The operation of the first ground is clear but frequently misapplied. Rule 6.005(4)(a) is limited to a counterclaim, set off or cross demand that the *debtor* has and does not extend to third parties. Furthermore, the court must be satisfied that the value of any counterclaim or cross demand equals or exceeds the amount claimed on the statutory demand. It will not be enough for a debtor to merely assert such a claim exists supported by his own subjective assessment of its value in order to avail of that ground. The ground relating to substantial dispute has been the subject of much argument over the years and is the ground that is most commonly relied on. The question as to what constitutes "substantial" was considered in this jurisdiction in the case of **Moore v Commissioners of Inland Revenue [2002] NI 26**. The significance of that case was not only that the demand was set aside on the grounds that there was a genuine triable issue but also this case is authority for the view that a statutory demand can be set aside conditionally i.e where the undisputed part of the debt is paid but the Demand is set aside in relation to the undisputed part. Lord Justice Girvan also concluded that an application to set aside statutory demand attracted the

protection of Article 6 of the European Convention of Human Rights. On page 6 of the judgment he states:-

> *"Although at first sight the wording of Rule 6.005 and some decided cases may suggest that a debtor served with a statutory demand bears a heavier burden than is borne by a defendant in summary judgment applications or applications to set aside judgment and that an onus of proof is thrown on him, in reality the test applicable should be no different. This is particularly so in the light of Article 6 and in the light of the severe consequences flowing from a decision not to set aside a statutory demand".*

[17] In the more recent case of **Allen –v-Burke Construction Ltd [2010] NICh9, [2011] NIJB 62** Deeny J stated:

> *"The grounds of dispute must be genuine. The grounds of dispute must not consist of some ingenious pretext invented to deprive a creditor of his just entitlement. It must not be a mere quibble."*

[18] As with (a) & (b) of Rule 6.005(4) the issue in relation to security at (c) of Rule 6.005(4) is confined to security held against property of the debtor. In **Re: a debtor (No 310 of 1998) [1999] 1WLR.452** Knox J held that the term "security" in the Insolvency Rules 1986 was to be construed in accordance with the definition of that term contained in section 383(2) of the Insolvency Act 1986 which provided that the debt was secured to the extent that security is held over any property of the debtor, whether by way of mortgage charge, loan or other security:

> *"It follows that security over the property of a party other than the debtor does not secure the debtor's liability. Thus, for example, where the debtor has guaranteed a company's debt to the creditor, security over the company's property does not secure the debtor's liability to the creditor for the same debt".*

The term "security" as used in Insolvency Rule 6.005(4) therefore has the same meaning.

Consideration and discussion.

I. Bad faith, negligence and breach of fiduciary duty.

[19] The applicants rely on **Bank of India –v-Trans Continental Commodity Merchants Ltd [1983] 2 Lloyds Rep 298** in support of their contention that the bank acted in bad faith towards the companies and that as

a consequence the guarantees are vitiated. In particular Mr Shields relied on the opinion expressed by Goff LJ at page 301:

> *"But as a matter of principle I cannot accept Mr. Murray's submission that a surety is discharged if a creditor acts towards the principal debtor in a manner which is irregular and prejudicial to the interests of the surety. Leaving aside what may be the special case of fidelity guarantees, I consider the true principle to be that while a surety is discharged if the creditor acts in bad faith towards him or is guilty of concealment amounting to misrepresentation or causes or connives at the default by the principal debtor in respect of which the guarantee is given or varies the terms of the contract between him and the principal debtor in a way which could prejudice the interests of the surety, other conduct on the part of the creditor, not having these features, even if irregular, and even if prejudicial to the interests of the surety in a general sense, does not discharge the surety.*
>
> *With that statement of principle I find myself in agreement, subject to the comment that I would - perhaps have preferred to state it the other way round, that is to say that there is no general principle that "irregular" conduct on the part of the creditor, even if prejudicial to the interests of the surety, discharges the surety, though there are particular circumstances in which the surety may be discharged, of which the instances specified by the learned judge provide certainly the most significant, and possibly the only, examples. I say that simply because I do not wish to be thought to be shutting the door upon any further development of the law in this field by rigidly confining the circumstances in which a surety may be discharged to the specified instances, though I freely recognize that I am unaware at present of any others. "*

As argued by Mr Gowdy, for the bank Goff LJ then goes on to state:

> *"But that merely irregular conduct on the part of the creditor, even if prejudicial to the interests of the surety does not discharge the surety"*

[20] I am not persuaded this authority assists the applicants. As appears from the evidence the bad faith, negligence and breach of fiduciary duty alleged by the applicants, principally relates to the aforementioned circumstances regarding the Rosslan site and other company transactions, which they claim give rise to potential counterclaims. However, the basis for setting aside a statutory demand pursuant to Rule 6.005(4) is predicated on grounds that the applicant has as a *debtor* and thus as an *individual*. In my opinion the applicants' argument that the statutory demands are an attempt by the bank to avoid contentious litigation with the companies which would reveal some misfeasance on the part of the bank, lacks substance and in any case falls outside the operation of Rule 6.005(4). Furthermore, it seems to me that if the companies had a legitimate grievance about this issue they could have initiated a process, including litigation, to address it. There is nothing to prevent them doing so. For the purposes of the disposal of this application however, I consider that this is a matter that concerns the limited companies

not the applicants as individuals. In the circumstances, the bank was entitled in my view not to be drawn into replying to the allegations made by the applicants within the context of this application. The only grounds therefore to support an allegation of negligence or breach of fiduciary duty appears to me to be limited to the operation of the "no set-off clause" in the guarantees.

II. The "no set-off clause".

[21] The applicants in the first instance claim that the bank should have drawn their attention specifically to clauses 25 and 28(ii) in the guarantees which excluded rights of set-off and failed to do so. It is unclear as to the basis of the applicants' claim that this particular clause should have been drawn to their attention by the bank but in any event I do not consider it to be a sustainable argument. The evidence of all three applicants contends that a significant professional relationship between the companies and the bank existed and which involved substantial commercial property development. I take the view that the applicants cannot on the one hand claim to have had such a strong professional business relationship with the bank to support the case they are making, without accepting that in doing so they are at the same time conceding that they are experienced professional businessmen on the other. Moreover, the applicants had the benefit of independent legal advice with regard to the guarantees. Indeed the solicitors who gave that advice are the applicants' solicitors in these proceedings. All three applicants in each guarantee signed the "Personal Guarantors Certificate Concerning Independent Legal Advice". This they did in their own handwriting confirming that prior to the execution of the guarantee they were independently advised on the nature, terms and effect of the guarantee by their solicitor and that the guarantee was signed voluntarily.

[22] It is common case that "no set-off "clauses come within the ambit of the Unfair Contract Terms Act. Mr Shields argued that the bank bears the burden of proving the reasonableness of the clauses as considered in **Skipskredittforeningen –v-Emperor Navigation [1997]CLC1151**at 1163:

> *If such a clause fails to satisfy the requirement of reasonableness in any respects then it fails in all respects, however immaterial may be the respects in which it is unreasonable to the particular case before the court."*

Mr Gowdy contended that in this case such clauses are reasonable as per **Barclays Bank plc –v-Kufner [2008] ewhc 2319 (Comm)** where Field J observed at [33] and [34]:

> *"It is common ground that by virtue of ss 13(1)(b) and/or 13(1)(c) and 2 (2) of UCTA the set-off clause is unenforceable unless the Bank can show that it is reasonable. The pertinent guidelines in Sch 2 to UCTA are: (a) the strength of the bargaining positions of the parties relative to each other taking into account alternative means by which the customer's*

requirements could have been met; and (c) whether the customer knew or ought reasonably to have known of the existence and extent of the term (having regard, among other things, to any custom of the trade and any previous course of dealing between the parties). Given that Mr Kufner was an experienced man of business with a net worth of Eur 27 million, there was no material disparity in the bargaining positions of the parties. Further, Mr Kufner does not assert in his witness statement that he did not know of the existence or the extent of the set-off clause, which is hardly surprising since he had available the services of his lawyer, Mr Knott.

[34] Is the set-off clause substantively unreasonable? Mr Nash submitted that this was an issue that was fact specific and should be decided only after a trial. I disagree. In my judgement, this issue can be fairly decided on the evidence before me. In Skips/credittforeningen v Emperor Navigation [1997] 2 BCLC 398, [1998] 1 Lloyd's Rep 66, [1997] CLC 1151, the Claimant sought summary judgement for sums due under a loan agreement that provided, inter alia: "All payments to be made by or on behalf of the Borrowers pursuant to this Agreement ... shall be made without (a) set-off The Defendant submitted that this clause was unreasonable under UCTA. Mance J rejected this submission holding that the clause was fair and reasonable. In his view "[s]uch a clause in a loan facility like the present is generally familiar, sensible and understandable". In WRM Group Ltd v Wood [1998) CLC 189 Morritt LJ agreed with this reasoning and so, with respect, do I. In my judgement, there is nothing unfair or unreasonable in requiring Kel to pay sums due under the loan agreement without set-off .Neither the set-off clause nor any other clause in the Kel loan agreement bars Kel from making a claim against the bank, and at the same time, the Bank has a legitimate commercial interest in receiving payment under the loan agreement when the same is due, instead of being kept out of its money whilst a cross-claim is litigated.

[23] In my view "no set-off" clauses within personal guarantees in the course of regulated commercial lending are difficult to find unreasonable. In such an instance the personal guarantee is a document which is created for the creditor's and/or shareholders' benefit in order to protect their respective interests. It is unsurprising therefore that it would seek to create a liability from which the Guarantor cannot resile and liquidate the debt in a manner which is most advantageous for the creditor to pursue. It seems to me however, that if the manner in which the creditor chooses to pursue the debt is to present the debtor with a statutory demand pursuant to the provisions of Article 242 of the Insolvency (Northern Ireland) Order 1989, then an interesting anomaly appears to arise. While the debtor may have contracted out of a right of set-off in executing the guarantee, Rule 6.005(4) creates in my opinion an independent statutory right to argue set-off which may render the effect of such "no set-off" clauses ineffective. Furthermore, a statutory demand is not legal proceedings. It is a statutory step required before a bankruptcy petition can issue. It is the petition which is the commencement of legal proceedings. However, an application to set aside a statutory demand is also legal proceedings but it is the creditor who is on the defensive in those proceedings.

[24] However, in the present case I think this is something of a moot point. I am not satisfied from the applicants' evidence that as individual debtors they have any claim against the bank that equals or exceeds the amounts claimed on the statutory demands. Nor is there any evidence that the applicants are solvent and in a position to discharge the liability to the bank. For the reasons set out above and elsewhere in this judgment I conclude that there is no persuasive evidence that the guarantees are vitiated or rescinded, or that any of the grounds in Rule 6.005(4) are satisfied. In the circumstances the applications are dismissed and I will now hear argument as to costs.