



June 2017

The Companies (Accounting) Act, 2017 – Welcome clarity on where floating charges, once crystallised, rank in relation to the claims of preferential creditors

□ Introduction

The Companies (Accounting) Act, 2017 (the **Act**) was signed into law by President Michael D. Higgins on 17 May 2017 and came into operation on 9 June 2017. Sections 92 and 98(d) of the Act provide clarity and certainty on the issue of whether the claim of the holder of a floating charge, once crystallised, ranks in priority to the claim of a preferential creditor following the High Court and the Supreme Court decisions of *In the Matter of Re In the Matter of JD Brian Limited (In Liquidation)* (the **JD Brian case**).¹

□ Overview of the JD Brian Case

In the JD Brian case the subject companies entered into various debentures with Bank of Ireland (the **Bank**) which included a clause that provided for the crystallisation of a floating charge where the Bank served a notice of crystallisation, which the Bank had duly served. Subsequently an order was made to wind up the companies and a liquidator was appointed. The Revenue Commissioners disputed the Bank's claim that the floating charges had validly crystallised and ranked in priority to Revenue's preferential claim.

¹ *In the Matter of Re In the Matter of JD Brian Limited (In Liquidation) T/A East Coast Print & Publicity, and In the Matter of JD Brian Motors Limited (In Liquidation) T/A Belgard; and In the Matter of East Coast Car Parks Limited (In Liquidation), and In the Matter of the Companies Acts 1963-2009 [2011] 3 IR 244; [2015] IESC 62*

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▣ The High Court Decision

In the High Court, Ms. Justice Finlay Geoghegan found that:

- a) The inclusion of crystallisation clauses in a debenture were valid under Irish law and crystallisation of a floating charge can occur provided that, once crystallised, a company is restricted in its use of the charged assets post crystallisation.
- b) The proper construction of Section 285(7) of the Companies Act, 1963 is that preferential claims rank in priority to the claim of the Bank, as debenture holder, irrespective of whether the floating charge crystallised prior to the commencement of winding up. In interpreting Section 285(7) in such a way that reflected the position in England (under Section 175(2) and Section 251 of the Insolvency (England) Act 1986), Ms. Justice Finlay Geoghegan departed from what had been the position of the Irish courts in *Re Griffin Hotel Co Limited*² (applied in *Re Brightlife Limited*³) where the Irish courts had found that if a floating charge crystallises before the appointment of the receiver or liquidator then the debenture holder has priority over the preferential creditors.
- c) On the facts of this case, the crystallisation notice given by the Bank would not have the effect of converting the assets subject to the floating charges into fixed charges as the debentures did not expressly provide for a restriction on dealing with the assets after the service of notice.

▣ The Supreme Court Decision

In the Supreme Court Ms. Justice Laffoy overturned the High Court decision on appeal on the following grounds:

- a) In reaffirming the position in *Re Griffin* and *Re Brightlife*, Ms. Justice Laffoy found that the correct interpretation Section 285(7) of the Companies Act, 1963, as it applied to the facts of this case, was that once the floating charges crystallised before the commencement of the winding up, the Bank's claim was no longer a claim secured by a floating charge, but now a claim secured by a fixed charge, providing the Bank with priority over Revenue's claim as preferential creditor.
- b) The crystallisation notice served on the companies was a valid notice and it succeeded in converting the floating charges over the companies' assets into fixed charges prior to the commencement of the wind-up.

Ms Justice Laffoy concurred that the determinative factor in the crystallisation of a floating charge was the intention of the parties in restricting the use of the assets which were the subject of the

² [1941] Ch 129

³ [1987] 1 Ch 200

crystallised floating charge. Based on the facts, she found that the companies would not be entitled to use the assets in the ordinary course of their business without the consent of the Bank. A valid notice of crystallisation can occur in cases where (1) there is an express provision for the crystallisation of a floating charge in the debenture and (2) a bank has provided notice of the crystallisation of the floating charge in writing to the company prior to the winding up of the companies

The Companies (Accounting) Act, 2017

The Company Law Review Group (**CLRG**) reviewed the JD Brian case in 2015. The CLRG was of the view that the law as it stood following the Supreme Court's interpretation of the law at the time required legislative action to prevent floating charge holders "leap-frogging" the claims of preferential creditors by crystallising the floating charges.

Section 92 of the Act was drafted on foot of the CLRG recommendations and amends Section 621(7)(b) of the Companies Act 2014 (previously Section 285(7)(b) of the Companies Act, 1963) to provide that preferential debts in a winding up shall:

"so far as the assets of the company available for payment of general creditors are insufficient to meet them, have priority over the claims of holders of debentures under any floating charge created by the company".

Section 98(d) of the Act similarly amends Section 440 of the Companies Act 2014 in relation to receivers appointed under powers contained in floating charges. The effect of this amendment ensures clarity in relation to this element of the priorities of payments in the liquidation of companies.

Conclusion

The amendments under the Act have the effect of bringing Irish law in line with the position in England under the Insolvency (England) Act 1986.

There is now welcome certainty that the priority of claims of preferential creditors are unaffected by the crystallisation of floating charges.

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