Provisional Liquidation in the Public Interest and the Perils of Crowdfunding "a Spectacular Investment"

Re BBH Property 1 Ltd unreported 10 August 2017 Ch D

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Introduction

In John Le Carré's first novel, *Call for the Dead*, the quintessential anti-hero, George Smiley, critiques the 20th Century political desire to harness the power of the masses by posing the simple question:

> "When had mass philosophies ever brought benefit or wisdom?"[1]

Whilst Le Carré was, of course, addressing the threat then posed by communism, Smiley's question has peculiar pertinence in the modern world. Thus, it is notable how many recent technological innovations seek to exploit the power of the collective to address pressing social, economic and cultural needs. Crowdfunding is but one example. It requires a body of people to pledge financial commitment (as opposed to political allegiance) to a specific project that purports to provide a mutually beneficial return. Investment is invariably secured through emotive entreaties for projects that are often characterised as socially or culturally significant and which would not otherwise receive funding from conventional lenders.

Although it presents itself as a much-needed alternative to the hegemony of financial institutions, crowdfunding provides a burgeoning carapace for those seeking to exploit and mislead unwary investors. Against this backdrop, the recent decision of Roth J in *Re BBH Property 1 Ltd*[2] merits careful consideration.

Facts

Thirteen companies were involved in one of two crowdfunding projects. The first was a project to acquire, develop and promote a former convent in Woodchester, Stroud, Gloucester into a hotel and music venue. The second involved the acquisition and development of a sizeable property in Norway so as to create an ambitious "eco-resort" including a central hotel and 224 houses. In both cases, the people behind the investment schemes were Matthew and Charlotte Roberts who had individually or together been directors of 12 of the 13 companies (the exception being Music Show Ltd).

The projects were crowdfunded by investors sourced through introducer companies. In doing so, prospective investors were provided with various representations that their funds would be invested in the companies purchasing the properties. The crowdfunding involved numerous rounds of fundraising often through different vehicles with the activities of one company often funded by another.

Amongst the most notable representations was the statement made by BBH Property 1 Ltd on the front page of its investment brochure characterising the UK project as "a spectacular investment secured by a spectacular asset". Similarly, the Norwegian investment was separately described as "an amazing secured investment". Further, it was stated repeatedly that the various companies were asset-backed by actual properties that investors would own outright via shares in the purchasing company.

In reliance upon the various representations, a large number of individual investors were induced to pay significant sums into the investment schemes to fund the projects. For example, some £5.8 million was raised from investors in respect of the UK project.

As it transpired, the purported representations were said to be false. The central complaint was that investors were induced to invest on the basis that their monies would be used to acquire property which would be transferred to the companies in which they would hold shares and would be secured accordingly. Security was not put in place and the investors' monies were dissipated without the companies acquiring the properties.

A significant portion of the money was diverted to companies controlled by Mr and Mrs Roberts or for other purposes. Equally, some of the relevant properties are under the control of RSM Tenon acting as fixed charge receiver for Saving Stream Security Holding Ltd under a charge granted to it to secure bridging finance of £3.6 million. It would appear that the investors may receive little return on the funds invested.

Issues

The Secretary of State for Business, Energy and Industrial Strategy (Secretary of State) presented petitions to wind up the 13 companies pursuant to s.124A of the Insolvency Act 1986 (IA 1986) on the basis that it was expedient in the public interest to do so. The first hearing of the petition was listed for 20 September 2017. On 10 August 2017, the High Court heard an application made by the Secretary of State for an order that a provisional liquidator be appointed pending the determination of the various petitions.

Four of the companies had appointed individual investors as directors who, in turn, sought to appoint a different provisional liquidator in respect of the relevant four companies. The Secretary of State's counsel, Mr Mark Mullen, successfully argued that it was in the public interest that the Official Receiver be appointed as provisional liquidator of all the companies.

Applicable Law

Pursuant to s.135 of the IA 1986 and r.7.33 of the Insolvency (England and Wales) Rules 2016 (SI 2016/1024), the Court may appoint a provisional liquidator at any time after presentation of a winding-up petition and before the making of a winding-up order. The jurisdiction to appoint provisional liquidators can be exercised if a winding-up petition had been presented and was likely to be successful. "Likelihood" in this context was interpreted by the Court in *Revenue and Customs Commissioners v Winnington Networks Ltd*[3] as meaning that the petitioner had demonstrated

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an entitlement to present the petition; that a material part of the petition was not capable of dispute; and that the petitioner had given full and frank disclosure.

In the more recent case of *Secretary of State for Business Innovation and Skills v New Horizon Energy Ltd*,[4] Norris J made clear that, in determining whether a petition was capable of serious dispute, the Court could consider information from the pre-petition investigation. Having established that the petition was likely to succeed, the Court still had to be satisfied that appointing a provisional liquidator was the right course of action. The Court's power to appoint a provisional liquidator pending hearing of the petition is not restricted to cases where there is a danger to assets or unlawful trading though that may often be the case in such applications.

Application to the Facts

In the present case, the 13 companies had not kept proper account records; lacked transparency; and had misapplied invested funds. Accordingly, the winding-up petitions were not capable of serious dispute such that the Court was satisfied that winding-up orders were likely to be made.

Turning to whether all the circumstances merited the appointment of a provisional liquidator pending the hearing of the petitions, the Court adopted a multi-factorial analysis. First, it was noted that since none of the companies were trading, the appointment of a provisional liquidator would not endanger legitimate business. Further, there existed a danger that the companies' assets would be dissipated or otherwise be seized by third parties if a provisional liquidator were not appointed. Placing all of the companies in the hands of a provisional liquidator would enable the companies to be administered consistently.

Whilst the directors appointed by investors were indeed acting on behalf of investors to assist with realising recoveries, their investigations were only at a preliminary stage. In any event, if the companies were wound up, then any agreement reached prior to insolvency would likely be set aside. Equally, the Official Receiver had agreed to liaise with the relevant investor appointed directors regarding the investigatory work that had been carried out.

Ultimately, Roth J noted that the Court was required to balance the directors' position against the vital necessity for there to be a single person in control of all the companies. Notwithstanding any potential cost saving of allowing the investor appointed directors to in turn apply to appoint a provisional liquidator in respect of four of the companies, all the companies had to be administered consistently. In this regard, the Court again noted the importance of having a single focal point for the investigation of all the companies and to act as a single point of contact for investors. Accordingly, Roth J ordered the appointment of the Official Receiver as provisional liquidator for all the companies.

Conclusion

Whilst the decision of Roth J to appoint the Official Receiver as provisional liquidator of all the companies is not unsurprising in the circumstances, it provides a timely reminder of the powers available to the Court when faced with multiple petitions of connected companies where a winding-up petition is likely to be made.

The background facts to the application also disclose the ways in which investors may be exposed to significant financial risk through purportedly "secure" crowdfunding projects. Crowdfunding is equally subject to the old adage: "if it seems too good to be true, it probably is".

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[1] John Le Carré, *Call for the Dead* (London: Hodder & Stoughton, 1961).

[2] *Re BBH Property 1 Ltd* unreported 10 August 2017 Ch D.

[3] *Revenue and Customs Commissioners v Winnington Networks Ltd* [2014] EWHC 1259 (Ch); [2014] B.C.C. 675.

[4] *Secretary of State for Business Innovation and Skills v New Horizon Energy Ltd* [2015] EWHC 2961 (Ch).