

Re: Permacell Finance – Can the floating charge holder participate in the prescribed part for any shortfall?



December 2008

The Northern Irish equivalent of the Enterprise Act is the Insolvency (NI) Order 2005. This piece of legislation made several changes to insolvency law. Probably the most high profile change was to remove the preferential status of the main Crown departments, with the “*quid pro quo*” being the introduction of a “*prescribed part*” to ensure that a fund is set aside out of the floating charge holder’s potential windfall for the benefit of unsecured creditors.

Article 150A (which applies to floating charges created on or after 27 March 2006) provides that the liquidator, administrator or receiver shall set aside the prescribed part and “shall not distribute that part to the proprietor of a floating charge except in so far as it exceeds the amount required for the satisfaction of unsecured debts”.

However until *Permacell*, it seemed that there was nothing to prohibit a secured creditor, whose security was inadequate to discharge its outstanding debt, from sharing in the prescribed part distribution.

Facts

Permacell entered liquidation following administration. The prescribed part which became available for distribution to unsecured creditors totalled £379,000. The private debenture holder suffered a shortfall totalling £918,850 following the realisation of the assets caught by its floating charge. Other unsecured creditors totalled approximately £3,104,000.

The Birmingham High Court was asked to decide if the floating charge holder could participate with the other unsecured creditors in the distribution of prescribed part - the argument advanced being that, ordinarily, a secured creditor can prove for any shortfall and therefore ought to be treated equally amongst other creditors of the same class.

The Court’s Ruling

His Honour Judge Purle QC decided that the floating charge holder was **not** entitled to participate in circumstances such as those encountered in this case. His judgement appears to have given effect to the parliamentary intention, namely to give floating charge holders the benefit of increased realisations through the abolition of Crown preference, but without having a detrimental effect on the unsecured distribution process.

Comment

This decision should accord with the practice already adopted by many Insolvency Practitioners faced with this type of scenario already. The Insolvency Service (Dear IP no. 30) in April 2004 interpreted the prescribed part provision to operate in this manner, however, quite prudently it highlighted that ultimately, it was for the courts to decide. The decision is therefore welcome clarification in this area.

NB: since writing, a reported High Court decision (*Re Airbase Services (UK) Limited*) has reached the same conclusion as in *Permacell*.

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