

Payment of preferential debts out of assets subject to floating charge not permitted

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Introduction Companies (Winding-up Amendment) Act Comment

Introduction

The Supreme Court recently considered whether, within the meaning of Section 237 of the Companies (Winding-up Amendment) Act, preferential creditors have any claim against the moneys received by receiver-managers for the sale of assets subject to a charge.

Joint official liquidators applied for an order regarding whether there was any entitlement for preferential debts to be paid, pursuant to Section 237, to creditors of one or more of the Baha Mar Companies in priority to the claims of holders of debentures under any floating charge created by such companies.

Companies (Winding-up Amendment) Act

Section 237 provides:

"Notwithstanding anything contained in this Act, in a winding up there shall be paid in priority to all other debts –

(a) All rates, taxes, assessments or impositions imposed or made under the provisions of any Act, including sums due in respect of...

(b) Any sum due by the company to an employee whether employed in The Bahamas or elsewhere, in respect of –

(c) Wages of any workman or labourers in respect of services rendered to the company during two months before the relevant date;

(d) Any sum due and payable by the company on behalf of an employee in respect of an employee in respect of medical health insurance premiums or pension fund contributions;

(e) Where a contract of employment has been terminated as a consequence of the company being wound up, any sum due by the company to any former employee in respect of –

(i) Severance pay; and

(ii) Earned vacation leave...

(2) the debts referred to in subsection (1)-

(a) rank equally among themselves and shall be paid in full, unless the assets are insufficient to meet them, in which case they shall abate in equal proportions; and

(b) so far as the assets of the company available for payment of general creditors are insufficient to meet them, have priority over the claim of holders of debentures under any floating charge created by the company, and be paid accordingly out of any property comprised or subject to that charge."

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The joint official liquidators submitted that the winding up began before the crystallisation notice was served and that the preferential debts were payable pursuant to Section 237(b) in priority to claims of holders of debentures under any floating charge.

However, the joint receiver-managers submitted that as a result of the crystallisation notice:

- the floating charge created under the debenture was converted into a fixed charge before the commencement of the winding up of the Baha Mar companies in official liquidation;
- there were no assets subject to a floating charge at the commencement of the winding-up proceedings; and
- there was no entitlement for preferential debts to be paid pursuant to Section 237(2)(b) to any creditors of any one or more of the Baha Mar companies in priority to the claims of the holders of debentures under any floating charge created by such companies.

Section 195(2) of the act provides that the winding up was deemed to have commenced at "the time of the presentation of the petition for the winding up".

The UK case of *Re Griffin Hotel Co Ltd* ([1940] 4 All ER 324) interpreted the provisions of Section 264 (4)(b) of the UK Companies Act 1929, which is equivalent to the section in the Bahamian statute which addresses payment of preferential debts payable in a winding up. In the ruling Judge Bennet stated that:

"S.264 (4) (b) operates only if at the moment of the winding up, there is still floating charge created by the company, and it gives the preferential creditors a priority only over the claims of the debenture-holders on any property which at that moment of time is comprised in or subject to the charge."

Judge Winder, who rendered the Supreme Court ruling, also considered the cases of *Re Brightlife Ltd* ([1987] 1 Ch 200) and *Re JD Brian Ltd (in liquidation) t/a East Coast Print and Publicity* ([2015] IESC 62) among others, before concluding that the words 'in a winding up', as referred to Section 237 (1) of the act, have been found to refer to the process which follows the making of an order to wind up a company. The court held that it is in relation to that proceeding that the distribution of the company's assets and preferential debts were to be considered, not at the time of filing the petition. The court further held that the courts also found that the language of the section under review did not prohibit the crystallisation of a floating charge so long as the crystallisation could take place before the making of the winding-up order.

Comment

The Supreme Court therefore determined that a floating charge which crystallised before the making of a winding-up order takes priority over other creditors, and the commencement of the winding up at the time of the presentation of the petition has a bearing merely on the understanding of certain key periods under the act. Further, 'in a winding up' must apply to circumstances in which a winding-up order has been made.

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