GRATUITOUS ALIENATIONS AND THE IMPLICATIONS OF *MACDONALD V CARNBROE ESTATES LTD*

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I. INTRODUCTION

A gratuitous alienation, in simple terms, is a disposal of property for no or inadequate consideration. Where the party disposing of the property is insolvent and subsequently enters certain insolvency processes,[1] the transaction may be validly challenged under legislative provisions.[2] This is also true in (virtually) all other legal systems[3] but Scots law has had particular difficulty with situations in which a purchaser has provided some, but inadequate, consideration.[4] However, in *MacDonald v Carnbroe Estates Ltd*,[5] the UK Supreme Court (UKSC) sought to offer some clarity regarding this aspect of the law and in doing so has overturned controversial pre-existing authorities.[6]

While the decision in *MacDonald v Carnbroe* has generally been welcomed,[7] there are implications of the judgment that remain unclear and need to be explored. The present contribution will seek to do this. In particular, there is still uncertainty with respect to the appropriate remedy (or remedies) where a party has made some payment for property in a transaction that has since been successfully challenged. The UKSC indicated that in some instances a court can, and should, take account of consideration paid in devising a remedy and remitted the case to the First Division to determine the appropriate remedy in the instant case. Before drafting the present article, we decided to await the court's decision; however, we understand that this will not be forthcoming as the case has now settled. While this is disappointing from the perspective of future legal certainty (if not for the parties involved), it gives greater scope here to consider the consequences of the UKSC's decision for the law of gratuitous alienations.[8]

This article will first examine the case of *MacDonald v Carnbroe* itself, before identifying and discussing various implications that arise from it. In particular, the following will be considered in turn: (1) the likely preferred remedy for parties involved in a transaction at an undervalue and what the law considers the primary remedy to be where some consideration has been paid; (2) the relevance of the decision for non-corporate insolvency and its application to unfair preferences; (3) the impact of the case on common law challenges (which remain available despite the statutory provisions); (4) issues relating to the ranking of

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[1] Namely, liquidation or administration for corporate insolvencies, and sequestration, the granting of a protected trust deed, or the appointment of a judicial factor (following the death of an insolvent debtor) under s.11A of the Judicial Factors (Scotland) Act 1889, for non-corporate insolvencies.

[2] See Insolvency Act 1986 s.242; Bankruptcy (Scotland) Act 2016 s.98. It should be noted, however, that common law challenges to gratuitous alienations remain possible and these merely require the debtor's insolvency, without the necessity of entry into a formal insolvency process. D. W. McKenzie Skene, *Bankruptcy* (Edinburgh: W. Green, 2018) paras 14-14 ff; J. St Clair and Lord Drummond Young, *The Law of Corporate Insolvency in Scotland*, 4th edn (Edinburgh: W. Green, 2011) paras 10-01 ff; W. W. McBryde, *Bankruptcy*, 2nd edn (Edinburgh: W. Green, 1995) ch 12.

[3] See e.g. R. Bork, *Corporate Insolvency Law: A Comparative Textbook* (Cambridge: Intersentia, 2020) ch 6. See also UNCITRAL Legislative Guide on Insolvency Law (2004) 141 ff.

[4] See e.g. St Clair and Drummond Young, *Law of Corporate Insolvency in Scotland* (2011) paras 10-07-10-08; McKenzie Skene, *Bankruptcy* (2018) paras 14-32 ff.

[5] [2019] UKSC 57; 2020 SC (UKSC) 23.

[6] The earlier leading cases on remedies for such transactions were *Short's Tr v Chung* 1991 S.L.T. 472 and *Cay's Tr v Cay* 1998 SC 780.

[7] See e.g. J. Hardman, "Caveat Emptor: Clarity for Statutory Gratuitous Alienations in Scotland" (2020) 31(6) ICCLR 363; and D. Blyth and T. Blank, "A New Approach to Balancing Competing Interests in Gratuitous Alienations" (2020) 13(2) CR&I 55; K. G. C. Reid and G. L. Gretton, *Conveyancing 2019* (Edinburgh: Edinburgh Legal Education Trust, 2020) pp.168-173; albeit that these sources note some difficulties too.

[8] Nevertheless, space precludes examination of a few relevant issues. For some of the implications of the court's interpretation of "adequate consideration", see Hardman, "Caveat Emptor: Clarity for Statutory Gratuitous Alienations in Scotland" (2020) 31(6) ICCLR 363.

a gratuitous alienee's claim; (5) the heightened importance of good faith for remedies in gratuitous alienation cases, and what this may tell us about the rationale or policy of the law in this area; (6) the expanded role of judicial discretion and how this may be appropriately exercised; and (7) whether English law can provide lessons with respect to the Scots law position on remedies.

II. FACTS AND BACKGROUND

MacDonald v Carnbroe involved an insolvent company, Grampian MacLennan's Distribution Services Ltd ("Grampian"),[9] and the sale of its principal asset, a site consisting of a warehouse, vehicle workshop and yard with a gatehouse, to Carnbroe Estates Ltd ("Carnbroe").[10] The property had been valued in March 2013 at £1.2 million on the open market and at £800,000 if there was a 180-day restricted marketing period.[11] Subsequently, Grampian suffered financial difficulties and was sold to a new owner, but this was followed by further financial problems. Grampian owed more than £500,000 to NatWest (a creditor with a standard security over the site, as well as a floating charge over Grampian's property and undertaking), and HMRC was owed a similar amount. The loan payments to NatWest fell into arrears. Grampian's owner discussed the sale of the site with a businessman he had known for more than 30 years, who was the sole director and shareholder of Carnbroe, and who was aware of Grampian's situation.[12] Following negotiations, it was agreed that Carnbroe would purchase the property at a reduced price of £550,000 in an off-market quick sale, due ostensibly to the risk of NatWest enforcing its security and because buildings on the site required repairs and upgrading.

The sale of the property to Carnbroe took place in July 2014,[13] but rather than paying Grampian, most of the agreed price was paid to NatWest to satisfy the loan secured over the property and to obtain a discharge of the standard security.[14] This was followed by Carnbroe acquiring a loan from Bank of Scotland, for which security was granted over the site. HMRC remained unpaid and requested tax that was due from Grampian but this was not paid and HMRC petitioned for Grampian's winding up. A provisional liquidator was appointed in September 2014 and the following month Grampian formally entered liquidation. The joint liquidators subsequently challenged the sale to Carnbroe and raised proceedings in November 2014.

In January 2017, the Lord Ordinary (Woolman)[15] held that the sale was for adequate consideration, a valid defence against a gratuitous alienation action.[16] This was despite the consideration being below open market value: Grampian "had very limited options" and "was in a perilous financial position", so a quick off-market sale was permissible.[17] However, the liquidators appealed to the Inner House, whereupon the First Division held that there had been a gratuitous alienation and reduced the disposition of the property.[18] The First Division concluded that a quick sale was not justified. There was no realistic prospect that Grampian's business could continue in existence after the sale of its assets and so it was not a case in which a quick sale would save the business.[19] In such circumstances, the interests of creditors prevail over any need to pay debts as they fall due. Following this decision, Carnbroe appealed to the UK Supreme Court.

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[9] See company details on Companies House (https://find-and-update.company-information.service.gov.uk/) (company number SC089369).
[10] For the facts generally, see paras [2]-[13].
[11] See also para [12] where there are details about valuation evidence, including expert suggestions that the open market value of the property at the transaction date was £740,000 or £820,000. The experts noted that a price of £550,000 was not inappropriate in some circumstances involving an off-market sale by a "financially distressed vendor".
[12] Paras [6]-[7].
[13] The disposition was dated 24 July 2014 (para [9]) but it is unclear how soon after this registration in the Land Register took place.
[14] The amount paid to NatWest was £473,604.68. The remainder of the payment price was not paid to Grampian until after completion of the proof in June 2016.
[15] [2017] CSOH 8.
[16] See Insolvency Act 1986 s.242(4)(b).
[17] [2017] CSOH 8 per Lord Ordinary (Woolman) at paras [30]-[31]. And see para [14] of the UKSC judgment.
[18] [2018] CSIH 7; 2018 SC 314. And see paras [15]-[17] of the UKSC judgment.
[19] [2018] CSIH 7 at paras [27]-[30] per Lord Drummond Young (with whom the other judges agreed).

III. DECISION

The principal issues raised by the appeal to the UKSC were (i) the interpretation of "adequate consideration" (in the Insolvency Act 1986, s.242(4)(b), which provides a defence to a gratuitous alienation action); (ii) whether the Inner House was entitled to interfere with the Lord Ordinary's evaluation that the consideration was adequate consideration; and (iii) whether the court has any discretion regarding the remedy available to it (under s.242(4)).[20] Issues (i) and (ii) can be dealt with together (below) under adequate consideration, while (iii) must be considered separately.

The UKSC unanimously allowed the appeal but only to remit the case to the First Division to identify the appropriate remedy. The judgment was given by Lord Hodge with whom the other four justices agreed.[21] After detailing the facts of the case and the decisions of the lower courts,[22] Lord Hodge discussed the historical development of the relevant statutory provisions for insolvency (non-corporate and corporate),[23] before considering the specific issues in the case.

1. Adequate Consideration

Upon reviewing earlier authorities,[24] including cases since the statutory reforms of 1985,[25] Lord Hodge stated that "adequate consideration" involves an objective test, and "regard must be had to the commercial justification of the transaction in all the circumstances on the assumption that hypothetical people in the position of the insolvent and the transferee would be acting in good faith and at arm's length."[26] The hypothetical purchaser would not have knowledge of the seller's financial problems unless they were known in the relevant market. It did not matter for this purpose that the owner of Grampian informed the owner of Carnbroe about Grampian's financial problems.[27] Importantly, however, an insolvent seller is expected to manage its assets to protect the interests of creditors.[28] Related to this, Lord Hodge considered that the objective purpose of a sale is also relevant. An off-market sale may achieve a low price but a quick sale of this type may be in the interests of creditors in some circumstances, such as where an insolvent party has liquidity issues and the sale would allow it to trade out of insolvency.[29]

If there is no prospect of the sale preserving liquidity or otherwise enabling the insolvent to remain in business, and the company "is ceasing or has ceased to carry on business and is, in reality, winding up its business in an informal way", as in *MacDonald v Carnbroe*,[30] the consideration's adequacy depends on the circumstances of the insolvency and, more generally, whether there is prejudice to the insolvent party's creditors.[31] Lord Hodge stated that where directors of an insolvent company can place the property on the

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[20] This third issue regarding the interpretation of the words in section 242(4) arose during the hearing – see para [1].
[21] Lords Reed, Wilson, Briggs and Sales.
[22] Paras [2]-[18].
[23] As well as statutory provisions, including the 1621 Act (c. 18) and later legislation, he discussed the common law position (which was built upon the *actio Pauliana* in Roman law) and remains relevant – paras [19]-[28]. For detailed discussion of the law's development in this area, see J. MacLeod, *Fraud and Voidable Transfer* (Edinburgh: Edinburgh Legal Education Trust, 2020) ch 4.
[24] Paras [29] ff. H. Goudy, *A Treatise on the Law of Bankruptcy in Scotland*, 4th edn by T. A. Fyfe (Edinburgh: T. & T. Clark, 1914) 25 and 47 and G. J. Bell, *Commentaries on the Law of Scotland*, 7th edn (Edinburgh: T. & T. Clark, 1870) II, 179 are cited. In various cases over the centuries, the courts have had to contend with what constitutes adequate consideration, and a number of these cases are referred to in *MacDonald v Carnbroe* see e.g. *Earl of Glencairn v Birsbane* (1677) Mor. 1011; *Miller's Trustee v Shield* (1862) 24 D. 821; *Gorrie's Trustee v Gorrie* (1890) 17 R 1051; *Tennant v Miller* (1897) 4 S.L.T. 318; *Abram Steamship Co Ltd v Abram* 1925 S.L.T. 243.
[25] *Kerr v Aitken* [2000] B.P.I.R. 278 and *Lafferty Construction Ltd v McCombe* 1994 S.L.T. 858. These reforms in the Bankruptcy (Scotland) Act 1985 s.34, and the Companies Act 1985 s.615A, led in turn to the Insolvency Act 1986 s.242 for corporate insolvencies. See further below.
[26] Para [32]. For a subsequent case involving adequate consideration, see *O'Boyle's Trustee v Brennan* [2020] CSIH 3.
[27] Para [32]. However, this knowledge may be of relevance for determining the remedy – see further below at IV.5.
[28] Paras [33]-[34].
[29] Paras [34]-[35].
[30] Where the business's key assets were being sold: as well as the site itself, Grampian's vehicles had already been sold.
[31] Paras [36]-[37].

market and undertake a proper marketing exercise, adequate consideration ought to be measured against the likely outcome of this approach. However, if a full marketing exercise would not have been possible, the consideration obtained should be measured against the price (after deduction of expenses), that would have been obtained by a liquidator of the company, or by the holder of security, rather than the open market price.[32] In the case, the court considered that there was no justification for an off-market sale at a price so far below market value on the ground of urgency.[33] There was a lack of evidence that Grampian attempted to put the property on the open market and, even if an open market process was not possible, Carnbroe had not led evidence that a sale by NatWest or a liquidator would have been likely to achieve a net price comparable to, or less than, the price Grampian accepted.[34] Consequently, the Inner House was entitled to interfere with the Lord Ordinary's assessment of the consideration's adequacy and was correct in determining that there had been a challengeable gratuitous alienation.

2. Remedies

Section 242(4) of the Insolvency Act 1986 provides that upon a successful challenge the court "shall grant decree of reduction or for such restoration of property to the company's assets or other redress as may be appropriate". Lord Hodge recognised that reduction could be harsh on a purchaser in good faith and at arm's length who had paid (substantial) consideration.[35] He also noted that "[i]t is not realistic in a commercial negotiation to expect a purchaser to ask a seller why he or she is not demanding a higher price."[36] Earlier decisions of the Inner House, particularly *Short's Tr v Chung*[37] and *Cay's Tr v Cay*,[38] had determined that reduction was not to be subject to any redress for the purchaser (beyond a claim in the seller's insolvency).[39] The insolvent estate would therefore receive not only the returned property but the payment made by the purchaser, creating an "uncovenanted windfall" for the seller's creditors as a whole.[40] This was criticised by commentators, who had even questioned whether it would be compatible with Article 1 of Protocol 1 to the ECHR (protection of property).[41] Lord Hodge referred to "anomalous results" identified by counsel to which the pre-existing law could give rise, as a party who had paid some consideration would be in a worse position than if it had been gifted the property for no consideration or declined to purchase the property or paid full value, and there would be no windfall to creditors in these scenarios.[42]

In examining the limited authorities from before the arrival of the modern statutory regime, Lord Hodge noted that annulment was the only remedy if it was possible.[43] He went on to say that, while the

[32] Paras [37]-[40].
[33] Paras [40]-[41].
[34] Paras [40]-[42].
[35] Paras [45], [51], [53], [57] and [65].
[36] Para [45]. See also counsel for Carnbroe's argument at para [18].
[37] 1991 S.L.T. 472.
[38] 1998 SC 780.
[39] See the coverage of these cases in *MacDonald v Carnbroe* at paras [46]-[48]. They involve the equivalent non-corporate insolvency provisions but given the similarity in the law, they were used as authority for the corporate insolvency provisions too – see e.g. *Baillie Marshall Ltd v Avian Communications Ltd* 2002 S.L.T. 189.
[40] Para [51].
[41] See St Clair and Drummond Young, *Law of Corporate Insolvency in Scotland* (2011) para 3.10. Lord Hodge (at para [66]) held that ECHR issues did not arise in the context as the statutory wording could be interpreted to avoid such a situation. Earlier cases had determined that the windfall would not breach ECHR in any event: *Johnston's Tr v Baird* [2012] CSOH 117; *Accountant in Bankruptcy v Walker* [2017] CSOH 78. For further consideration of this point, regarding the law as it stood, see e.g. McKenzie Skene, *Bankruptcy* (2018) paras 14-32 ff. And see J. Ulph and T. Allen, "Transactions at an Undervalue, Purchasers and the Impact of the Human Rights Act 1998" [2004] JBL 1 for discussion of human rights and the equivalent English law in this area.
[42] Para [52]. And if a gratuitous transferee or purchaser/transferee who has made a substantial but inadequate payment sells to a bona fide third party for full value, then the court could grant "other redress", which could consist of payment of the shortfall of consideration to the insolvent's estate to reach adequate consideration.
[43] Para [59]. See *Tennant v Miller* (1897) 4 S.L.T. 318; *Thomas v Thomson* (1866) 5 M. 198; and Bell, *Commentaries*, II, 217 (referring to fraudulent preferences).

question of restitution of the defender did not arise in the case of an alienation which was wholly gratuitous, where the sale was at an undervalue the law did not allow for general *restitutio in integrum*. He considered, however, that the earlier law was "not wholly inflexible" with regard to restitution and allowed a partial restitution in the context of annulment of a preference.[44] It is true that the case law indicates some flexibility but it is unclear to what extent this is true where reduction of an alienation is possible. As regards the modern statutory provisions on gratuitous alienations, Lord Hodge not only identified the possibility of interpreting the statutory wording widely but also drew upon policy-focused reasoning by noting that if there was no flexibility in remedies then it would deter "rescue transactions" involving the purchase of assets from distressed companies, undermining the wider "rescue culture".[45] Consequently, although the UKSC held that the court does not have a "general equitable jurisdiction" regarding remedies for gratuitous alienations and the primary remedy is annulment of the transaction by reduction or restoration, the statutory words are broad enough to allow the courts, in certain cases, to formulate a remedy to give some protection to good faith purchasers for consideration paid.[46] As regards the latter point, the earlier cases were overturned.[47] Interestingly, our review of archival materials indicates that taking account of consideration paid in determining the appropriate remedy aligns with the Scottish Law Commission's perception of the pre-existing law, and arguably also the modern regime they were proposing, when producing their report that led to the 1985 reforms (referred to above and in section IV.2. below).[48]

In *MacDonald v Carnbroe*, the UKSC remitted the case to the First Division to determine whether it would be appropriate to qualify reduction to take account of all or part of the consideration paid by Carnbroe.[49]

IV. IMPLICATIONS

In suggesting that in some circumstances a court can and should take into account the consideration paid by a purchaser in a transfer at an undervalue, the UKSC's judgment poses questions as to what remedies are available and which is most appropriate in prevailing circumstances. While there is a strong argument

[44] Paras [60]-[61]. See also McBryde, *Bankruptcy* (1995) para 12-96, and the discussion below.
[45] Para [62].
[46] Paras [53], [63]-[65].
[47] Para [65]. *Short's Tr v Chung* and *Cay's Tr*, in particular. An argument that there had been parliamentary endorsement of those decisions due to later legislation, namely the 2016 Act, was rejected, as consolidation legislation (such as the 2016 Act) does not constitute endorsement of earlier case law (see paras [55]-[57]). A parliamentary endorsement argument was also rejected in *MacMillan v T Leith Developments Ltd* [2017] CSIH 23, 2017 S.C. 642 (a floating charges and diligence case referred to by Lord Hodge); see A. D. J. MacPherson, "The Circle Squared? Floating Charges and Diligence after *MacMillan v T Leith Developments Ltd* 2018 Jur. Rev. 230, 233.
[48] See e.g. *Scottish Law Commission Papers*, L3/244H, Note of Meeting held on 23 September 1976, p.4; L3/244H, Gratuitous Alienations (Draft) Paper by A. E. Anton Dated 17 September 1976, p.1; L3/244I, Bankruptcy – Reduction of Gratuitous Alienations and Illegal Preferences Outside EEC Bankruptcy Convention Paper by A. J. Sim Dated 8 December 1976, p.4; L3/244R, Note of Meeting on 17 December 1979 – Gratuitous Alienations, Reduction of Preferences and Equalisation of Diligences, p.3; and see also L3/244S, Bankruptcy Report – Chapter 13 Voluntary Gifts and Preferences – Instructions to Draftsman Dated 10 June 1980. They appear to have considered that, under the existing law, reduction could be qualified to take into account the amount of consideration paid. We are grateful to the Scottish Law Commission, and particularly Professor Frankie McCarthy, Charles Garland and Gordon Speirs, for giving us access to the Scottish Law Commission's archived materials. See also Scottish Law Commission, *Report on Bankruptcy and Related Aspects of Insolvency and Liquidation* (Scot Law Com No 68: 1982) para 12.9, which appears ambiguous regarding the pre-existing law on this point, but can be read as consistent with the position indicated in the above documents. As noted by Lord Hodge (paras [22] and [62]), the recommendations in the Scottish Law Commission's *Report* (para 12.19), which gave rise to the wording on remedies in the 1985 Act, are not clear regarding the flexibility of the remedies. However, it may be reasonable to conclude that there was a desire for continuity with the earlier law in this matter, particularly in the absence of a provision which was inarguably to the contrary. Archival documents held by National Records of Scotland relating to the Bankruptcy (Scotland) Act 1985 (files with references AD63/1820/1-10 and SOE10/88-91) do not shed further light on remedies and there is an absence of discussion of the legal situation where some consideration is paid, which could be read as an indication that the matter was viewed as uncontroversial.
[49] Paras [69]-[70].

that a good faith purchaser does deserve protection for consideration paid, to avoid an unmerited windfall to the insolvent estate and to avoid unfair penalisation of the purchaser, there was a greater element of certainty in the pre-existing law.[50] Much work is therefore required to clarify exactly how the law now stands and how it might operate in practice in future cases. To that end, the following sub-sections explore a number of the key implications of *MacDonald v Carnbroe* for the law of gratuitous alienations and beyond.

1. A Preferred Remedy?

Of course, the decision of the UKSC has had immediate implications for the case itself. Although there has not been a further decision of the Inner House regarding the appropriate remedy, the UKSC's judgment has clearly impacted upon the case's outcome by way of settlement. While we do not know the terms of the settlement, the alienated property's title sheet on the Land Register of Scotland discloses that Carnbroe recently (re-)acquired the site for £700,000, this further disposition presumably being necessary as a result of the reduction of the original transaction and return of the property to Grampian.[51] It is unclear whether Carnbroe simply made an additional payment to reach an acceptable value for the property and/or how litigation expenses featured in the settlement. Nevertheless, it appears to show that the preferred outcome was for Carnbroe to have ownership of the property and for the liquidators to receive a further payment.

More broadly, this approach will often be the best option for the parties involved. The acquirer will frequently have entered into occupation of the premises, they may be operating a business from there, they may have carried out repairs, maintenance and improvements or refurbishments and, if they are required to return the property, there is likely to be further expenditure involved, including due to (almost) inevitable disruption. It is unknown whether these types of costs will be taken into account by the courts in determining the amount of redress for the acquirer, given that the UKSC focused expressly on consideration paid and stressed that there was no general equitable jurisdiction for remedies.[52] If they are not to be included in the court's assessment, the restoration of the property to the insolvent's estate in return for the earlier consideration paid or an equivalent "payment" by the liquidator (or equivalent) for the return of the property will frequently be less attractive for the acquirer. Although in some instances the alienee's expenditure on the property would be of benefit to the liquidator or equivalent (and the creditors), they may prefer to have liquid funds that can be distributed rather than the return of the alienated property which would require to be marketed and then sold in order to obtain such funds, without any guarantee that a commensurate level of payment for the property will be received. In addition, by the time the alienation has been successfully challenged, the liquidator may not have available funds to give to the alienee to cover the consideration they have paid.

Even though the outcome noted above is likely to be favoured in many instances, the apparent continued prioritisation of reduction or restoration where possible in *MacDonald v Carnbroe*[53] raises questions as to whether a court could simply order the acquirer to make a further payment to reach the level of "adequate consideration" ("further payment approach"), as opposed to ordering reduction/restoration with a balancing repayment of consideration to the alienee ("annulment and return of consideration approach"), especially if the liquidator disagrees with the further payment approach. The law still seems to prioritise returning particular property to the estate over restoring lost value more broadly. Lord Hodge suggested that if reduction is granted, the court might provide that the liquidator makes a payment to the transferee

[50] There was also the possibility that in some instances, deserving parties might have been able to recover losses (e.g. for consideration paid) if their solicitors had acted negligently in failing to advise that the transfer could be challenged subsequently as a gratuitous alienation. Similarly, it was pointed out in criticism of the floating charge case of *Sharp v Thomson* (1997) SC (HL) 66 (which is unconnected to gratuitous alienations) that the purchasers could have sued their solicitors for professional negligence in the circumstances – see e.g. K. G. C. Reid, "Equity Triumphant: *Sharp v Thomson*" (1997) 1 EdinLR 464 at 468.

[51] Title Number LAN86957. Some details about the property are also available at https://scotlis.ros.gov.uk/property-summary/LAN86957. The date of entry is given as 13 August 2021, with a registration date of 2 September 2021.

[52] See e.g. at paras [65] and [69].

[53] See e.g. para [49].

in exchange for the reduction (repaying all or part of the consideration).[54] This was, however, only given as an example and in the context of qualifying the reduction that the First Division had already ordered. The judgment could be interpreted in a way that does allow for an alternative approach in the circumstances, and this is arguably supported too by Lord Hodge referring to "restoring property *or value* to the insolvent's estate" when discussing the devising of a suitable remedy.[55] Cases where some consideration has been paid could be viewed as an exception allowing for the primary remedy to be departed from in some instances. This would, however, seem to be getting closer to a general equitable jurisdiction, which was firmly rejected by the UKSC. It would also raise issues as to how a court should react if an alienee desires the further payment approach but the liquidator seeks annulment and return of consideration. Should the primary remedy of reduction (or restoration) still apply, qualified by the return of consideration paid, which may not be fair or just to the alienee due to expenditure they may have incurred since the transfer?

Despite drawbacks for a liquidator if property is restored, as noted above, if the value of the property has increased substantially since the alienation, whether as a result of improvements by the alienee or otherwise, it may be more attractive for the liquidator to have it returned rather than receive the payment of an extra amount to reach adequate consideration as assessed at the time of the alienation. In the event that the courts are unable or unwilling to order the further payment approach, the parties could always agree an out of court settlement in terms of which the purchaser would pay an additional sum to reach what is agreed to be an acceptable price.[56] By contrast, if the value of the property has substantially dropped,[57] the alienee may prefer the annulment and return of consideration approach, which would be less popular with the liquidator. If, for example, the property had suffered accidental damage, such as fire damage,[58] the property could be returned, with the alienee having the advantage by receiving their consideration back. However, depending on the timing and the amount of the property's lost value, perhaps the liquidator would simply not challenge the transaction in such a situation, meaning the damaged property would remain with the alienee.

It might be queried why "reduction", "restoration" and "other redress" are not simply properly alternative options, rather than there being an implicit hierarchy, especially given the use of "or" between the different remedies in the statutory wording. This would enable a court to select the most appropriate remedy or remedies based on the prevailing circumstances. The court did interpret "or" as the equivalent of "and/or" (i.e. as both conjunctive and disjunctive), thus justifying a combination of the options.[59] While identifying primary remedies has the merit of a greater degree of certainty, a more flexible approach might allow a fairer and more proportionate response, which would enable a court to require the alienee to make an additional payment (or, if that is not possible, to return the property in return for consideration paid). On the other hand, the annulment and return of consideration approach does avoid the need for the court to determine exactly what would constitute adequate consideration. In addition, having a more flexible approach would likely mean that the courts would be called upon more frequently to dispose of gratuitous alienation actions by exercising their discretion. There is perhaps merit in a default remedy which looms over parties and helps them negotiate a settlement based on the situation at hand. Even if a party has not paid anything for alienated property, it is always open to the parties to agree that rather than returning the property, the alienee will simply pay an acceptable amount for the property acquired.

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[54] Para [69].

[55] Para [65]. Albeit that value here may be more focused on instances where the property itself cannot be returned.

[56] Although adequate consideration is assessed at the time of the alienation, the new value of the property may have relevance in the negotiations, as without an agreement for the alienee to retain it, the property (with its current value) would be returned to the insolvent's estate.

[57] The reduction in value would have to be significant for this to be the case, given that the sum already paid was at an appreciable discount on the value of the property, but this could occur, for example, if land was contaminated with the result that there were substantial remedial costs.

[58] If there was an insurance policy held by the alienee, questions could be raised as to whether they could keep the insurance proceeds. A flexible approach ought to require those proceeds to be given to the insolvent's estate.

[59] See para [53] for this inclusive use of "or". It is possible to interpret "or" in legislation in this inclusive sense or in an exclusive sense, but while the former seems to be more common, it depends on context – see e.g. Office of the Parliamentary Counsel, *Drafting Guidance* (2020) para 3.7.

2. Application to Non-Corporate Insolvency and Unfair Preferences

The impact of the UKSC's decision is not limited to s.242 of the Insolvency Act 1986 and corporate insolvency law. Non-corporate insolvency law in Scotland has equivalent rules for sequestration (and comparable processes, such as protected trust deeds), and these are found in the Bankruptcy (Scotland) Act 2016, s.98. The predecessor of section 98 was section 34 of the Bankruptcy (Scotland) Act 1985, which introduced the modern statutory regime for challenging gratuitous alienations,[60] and substantially the same regime was applied to corporate insolvency first in the Companies Act 1985[61] and then in section 242 of the 1986 Act.[62] However, the construction of the remedies provision in s.98(5) of the 2016 Act differs from its predecessor (s.34(4) of the Bankruptcy (Scotland) Act 1985) and the equivalent provision in s.242(4) of the 1986 Act. It states that the court "must grant decree— (a) of reduction, or (b) for such restoration of property to the debtor's estate, or such other redress, as may be appropriate." The separation of reduction and restoration into (a) and (b) and the inclusion of the latter with "such other redress", could be interpreted to mean that there is even less of an apparent hierarchy of remedies here, allowing them to be viewed as simply alternatives available to the court.[63] And while the use of (a) and (b) might instead be read as establishing a hierarchy between them, that would seem to be at odds with the ordinary meaning of "or", and should require an express statement, as is the case with the hierarchy of objectives for administrators in the 1986 Act, Sch B1, para 3. Within other provisions in s.98, such as section 98(6), which provides that the court is not to grant decree in the event that the person seeking to uphold the alienation establishes, for example, that at any time after the alienation the debtor was absolutely solvent or that the alienation was for adequate consideration, "or" is undoubtedly being used to present alternative defences, without a hierarchy.

As an aside in relation to s.98 of the 2016 Act, it appears there is an error in how the provisions have been laid out. Section 98(7) states that subsection (6) is "without prejudice to any right acquired, in good faith and for value, from or through the transferee in the alienation". This protection of third party rights should place a limit on the potential remedies a court may give under s.98(5), *not* the potential defences in s.98(6), and is assumed to be a drafting error. The issue could be easily resolved by replacing the reference to s.98(6) with a reference to s.98(5) in subsection (7).[64] This is not a problem with the equivalent provisions for corporate insolvency, as the material on remedies and the defences are contained within the same sub-section, along with the protection for good faith acquirers for value, which states that the subsection is without prejudice to their rights. That approach was previously adopted in the Bankruptcy (Scotland) Act 1985, but the drafters of the 2016 Act decided to separate (into s.98(5)-(7)) the provisions previously combined in s.34(4) of the 1985 Act.

A potential point of distinction between corporate and non-corporate insolvency in relation to remedies involves policy. It was noted earlier that Lord Hodge drew on the rescue culture as part of policy-focused reasoning to support a more flexible interpretation of the statutory provisions on remedies.[65] The rescue culture is relevant primarily in the context of corporate insolvency, with which this case was concerned, since bankruptcy law, although it encompasses a number of entities (such as partnerships other than limited liability partnerships) to which the rescue culture may be relevant, is in practice concerned largely with insolvent individuals, the vast majority of whom are consumers. The rescue culture might therefore be seen as justifying a different approach in the case of corporate insolvency. On the other hand, it should not be forgotten that one of the main aims of the Scottish Law Commission in recommending

[60] Following the recommendations in Scottish Law Commission, *Report on Bankruptcy and Related Aspects of Insolvency and Liquidation* (1982) paras 12.15 ff.
[61] Bankruptcy (Scotland) Act 1985 s.75 and Sch 7 para 20 inserted s.615A into the Companies Act 1985.
[62] See Lord Hodge's discussion of the history of the provisions at para [22].
[63] If reduction were the primary remedy, and was possible in given circumstances, then "other redress" would not be available if, for example, consideration had been paid, since that remedy is only included with restoration of property in (b) and is not mentioned in (a).
[64] The issue and its solution are also discussed in K.G.C. Reid and G.L. Gretton, *Conveyancing 2020* (Edinburgh: Edinburgh Legal Education Trust, 2021) p.205, n 2.
[65] Para [62].

reform to the law of challengeable transactions was to harmonise the law in its application to all types of debtors.[66] We should therefore be hesitant about any divergence involving the two kinds of debtor on the basis of this policy matter alone. And, indeed, the law may also not wish to discourage parties from entering into transactions with financially distressed individuals, as those transactions could ultimately enable the individuals to avoid an insolvency process.

The promotion of the rescue culture is a relatively recent development when set against the long history of the law on gratuitous alienations, and it may indeed point to a different approach than that which is suggested by focusing solely on the principle that insolvent debtors are effectively required to act as trustees for their creditors. It is true that the main statutory regime for corporate rescue, namely administration, ostensibly prioritises the rescue of the company as a going concern. However, it also in fact allows, indeed requires, a different objective to be pursued where this would result in a better outcome for the creditors as a whole, even if a rescue would be practicable.[67] Thus, it may also be seen as subsidiary to that wider principle and not justification for a different approach.

Finally in this part, the UKSC's decision also has significance for unfair preferences, as there is equivalent wording regarding the remedies for successful challenges to these too, in section 243(5) of the 1986 Act for corporate insolvencies, and in s.99(6) of the 2016 Act for non-corporate insolvencies.[68] It is more difficult in the context of unfair preferences to ascertain when a party may obtain special redress. However, it could be of use if a security is granted to secure both newly provided funds (which would not be challengeable) and pre-existing debt claims (which could be challengeable). An absolute reduction of the security would appear disproportionate and unfair to the creditor, and so a court could order that the security only extends to the debt comprised in the new funds.[69]

3. Common Law

As noted above, it remains possible to challenge a gratuitous alienation at common law, and the decision in *MacDonald v Carnbroe* may also have implications for such a challenge. At common law, while reduction is normally the appropriate remedy where available, sometimes it may not be possible, in which case a different remedy may be sought.[70] What is less clear, however, is whether reduction (or restoration) is always to be regarded as the primary remedy where available. McBryde states that "[t]he ***normal*** remedy was reduction without *restitutio in integrum* although it is difficult to be certain about the position with gifts, particularly a gift for some, though inadequate, consideration."[71] He also suggests that it "might have been sensible to seek a monetary payment to reflect the shortfall in the true and just price, but authority is sparse." The implications of this are two-fold. If reduction or restoration without *restitutio in integrum* can be regarded as the primary remedy where available, this might make a common law challenge more attractive to a challenger if it may avoid the flexibility now available in a statutory challenge as a result of the UKSC decision. It might, for example, allow for reduction (or restoration) without the requirement to make any repayment of consideration. On the other hand, the uncertainty in the existing cases over the position involving some but inadequate consideration could leave the way open for the court to develop the law and adopt a more flexible approach in a similar (or even more expansive) way than in *MacDonald v Carnbroe*.[72] Certainly, many of the same arguments could be utilised in such a situation and the UKSC's decision would

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[66] See e.g. Scottish Law Commission, *Report on Bankruptcy and Related Aspects of Insolvency and Liquidation* (1982) para 12.29 and Draft Bill cl.33 and Sch 6 para 4.

[67] Insolvency Act 1986, Sch B1, para 3.

[68] See para [49] for Lord Hodge's recognition of the equivalence.

[69] This may also be supported by earlier case law e.g. *Thomas v Thomson* (1866) 5 M 198.

[70] See McBryde, *Bankruptcy* (1995) para 12-52 and paras 12-94-12-98 and references there cited; McKenzie Skene, *Bankruptcy* (2018) para 14-46 and references there cited.

[71] McBryde, para 12-96. Emphasis added.

[72] When developing their recommendations that led to the 1985 Act, the Scottish Law Commission seem to have considered that remedies under the common law would be limited to gratuitous elements of transactions and so protection could be provided for those who had made some payment – see *Scottish Law Commission Papers* cited above at n 48. And see D. C. Coull, "The Prevention of Fraud Prior to Bankruptcy: A Comparative Study" (PhD Thesis, University of Aberdeen, 1974), pp.26-27.

no doubt be influential. It may also be noted that creditors with the right to challenge could take a different view of the best way to proceed to an insolvency officeholder, and could seek to raise a common law action if it was thought that it could allow for a more favourable outcome.

A further point of disparity between statutory and common law challenges involves the provisions relating to postponed debts, where there has been a successful challenge of a gratuitous alienation. These provisions only apply where there has been a successful challenge under the statutory provisions, not common law challenges, and are discussed next.[73]

4. Ranking of the Defender's Claim

In *MacDonald v Carnbroe*, Lord Hodge noted that if the court was not empowered to impose conditions on the reduction of an alienation, or did not do so, a transferee who had paid a substantial but inadequate sum would have only a claim in unjustified enrichment against the insolvent estate for repayment of the inadequate consideration.[74] That claim would rank as an ordinary claim, with a claim for the recovery of the transferred asset itself or the proceeds of its sale ranking as a postponed debt in terms of rule 4.66 of the Insolvency (Scotland) Rules 1986 (now rule 7.27 of the Insolvency (Scotland) (Receivership and Winding Up) Rules 2018).[75]

Lord Hodge dismissed an argument by the liquidator that it was the purchaser's claim for repayment of the (inadequate) purchase price which was a postponed debt under these provisions.[76] Yet the provisions are not without problems. McBryde, discussing the corresponding earlier provisions for sequestration, noted that there was an argument that under them, the claim of an alienee for the return of partial consideration was a postponed debt.[77] Lord Hodge, however, considered that this argument was misconceived. He said:[78]

> ...the postponed debt is the transferee's right to reclaim the property which had been alienated or the proceeds of sale of that property. It addresses the right of a transferee to reclaim the property, which had been alienated and restored to the insolvent estate, if a surplus emerged in a winding up. It does not address the claim in unjustified enrichment of a transferee which has paid an inadequate consideration for the repetition of the sums which it has paid which is inconsistent with any right to a reconveyance of the property to the transferee. The provision does not therefore support a contention that Parliament intended to penalise the gratuitous alienee in relation to a claim for unjustified enrichment.

The provisions relating to sequestration, which are replicated in modified form in the corporate insolvency rules, were included in the draft bill attached to the Scottish Law Commission's report on which the Bankruptcy (Scotland) Act 1985 was based.[79] However, the report contains no discussion of them, either in the context of gratuitous alienations or in the context of postponed debts, and so provides no insight into their purpose or interpretation. Archived documentation does indicate though that the Commission's focus regarding postponed debts here was a donee's right to a distribution in relation to property that was returned to the insolvent's estate by reduction (or restoration), and this was considered to reflect the deferral

[73] See Insolvency (Scotland) (Receivership and Winding Up) Rules 2018 (SSI 2018/347) r.7.27; Bankruptcy (Scotland) Act 2016 s.129(4)(c).
[74] Para [27].
[75] Para [27]. The equivalent provision in sequestration is s.129(4)(c) of the Bankruptcy (Scotland) Act 2016, originally s.51(3)(c) of the Bankruptcy (Scotland) Act 1985. The wording of these provisions, however, is not exactly the same for reasons which will become apparent.
[76] Para [54].
[77] McBryde, *Bankruptcy* (1995) para 12-96.
[78] Para [54].
[79] Scottish Law Commission, *Report on Bankruptcy and Related Aspects of Insolvency and Liquidation* (1982) Draft Bill, cl.48(3).

of the donee's interests to those of the "onerous creditors" but also their prioritisation over the insolvent debtor.[80]

The equivalent wording in the corporate insolvency rules is somewhat clumsy, referring to a creditor's right to "*any alienation* which has been reduced or restored to the company's assets under s.242 or to the proceeds of sale of such *an alienation*" (emphasis added).[81] The reference to an alienation – rather than the property alienated – is awkward. This may, however, simply be the result of a less than perfect attempt to mirror the corresponding provisions in sequestration in the context of corporate insolvency where there is usually no vesting in the officeholder: the corresponding provisions in sequestration refer to the creditor's right to anything vesting in the trustee by virtue of a successful challenge under the statutory provisions or the proceeds of sale thereof.[82] This can be seen more clearly to refer to the property vesting in the trustee having been restored to the debtor's estate as a result of the successful challenge.

Lord Hodge's interpretation of these provisions and their relationship to the remedies available on a successful challenge is not, however, without difficulty. St Clair and Drummond Young accepted that the interpretation of s.242(4) adopted by the previous case law, but rejected by Lord Hodge, was "obviously what Parliament intended", because if restoration of the status quo was what was sought, it was difficult to see why the legislature would have provided for the creditor's right to be a postponed debt.[83] The provisions do not sit easily with an approach where some or all of an inadequate consideration may be returned to the transferee: why should the transferee have a claim, albeit postponed, to the property returned to the estate if they have received the return of their consideration? The provisions arguably fit better with an approach whereby property is returned to the estate without *restitutio in integrum* and the transferee is given the right to reclaim the property (or the proceeds of its sale) if there is a surplus. Nevertheless, if consideration is returned, an alienee should forego any right to the property, as otherwise they could theoretically obtain a windfall due to the combination of the returned payment and the property itself (albeit that this would be unlikely in reality given that the estate will almost certainly have been exhausted before postponed creditors could receive distributions).

It is also somewhat odd that the provisions refer only to a creditor's claim to anything returned to the debtor's estate as a result of a statutory challenge and not one at common law. Was this merely an oversight? Or does it support the argument that the outcome of a statutory challenge might be different from that of a common law challenge with the result that this provision was required in the context of a statutory challenge? It is difficult to be certain, but it seems as if the Scottish Law Commission in fact did not wish to make provision for the common law when constructing the proposed statutory regime for gratuitous alienations, instead leaving relevant ranking outcomes to the common law itself.[84]

Another argument, not put to the court in *Carnbroe,* is that the return of substantial but inadequate consideration to the transferee might be treated as an expense of the relevant insolvency process.[85] While this could explain the priority status of such a payment (ahead of unsecured claims), it does not seem to fit naturally within the description of expenses set out in legislation. The corporate insolvency provisions refer to "fees, costs, charges and other expenses incurred in the course of" the liquidation or administration,[86] while the bankruptcy legislation refers to "outlays…. of the trustee in the sequestration in the administration of the debtor's estate".[87] Can it truly be said that a payment that is part of unwinding a challengeable

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[80] See e.g. *Scottish Law Commission Papers*, L3/244H, Note of Meeting held on 23 September 1976, p.4.
[81] Insolvency (Scotland) (Receivership and Winding Up) Rules 2018 (SSI 2018/347) r.7.27.
[82] Bankruptcy (Scotland) Act 2016 s.129(4)(c), previously s.51(3)(c) of the Bankruptcy (Scotland) Act 1985.
[83] St Clair and Drummond Young, *Law of Corporate Insolvency in Scotland* (2011) para 10-07.
[84] Indeed, the 1985 Act provisions on gratuitous alienations which emerged from the Scottish Law Commission's project did not directly deal with the common law. It had earlier been suggested by the Commission's Working Group that gratuitous alienations should not be challengeable at common law: Scottish Law Commission, *Memorandum No 16, Insolvency, Bankruptcy and Liquidation in Scotland* (1971) para 24; however, this was rejected in the subsequent report – Scottish Law Commission, *Report on Bankruptcy and Related Aspects of Insolvency and Liquidation* (1982) paras 12.15-12.16. See also the *Scottish Law Commission Papers* cited above at n 48.
[85] This argument was posited by Professor Gretton in correspondence with the authors.
[86] See, respectively, Insolvency (Scotland) (Receivership and Winding Up) Rules 2018 (SSI 2018/347) r.7.28(1) and Insolvency (Scotland) (Company Voluntary Arrangements and Administration) Rules 2018 (SI 2018/1082) r.3.50(1).
[87] See Bankruptcy (Scotland) Act 2016 s.129(1)(b).

transaction (entered into and completed before the insolvency process) is an expense incurred in the insolvency process or an outlay in the administration of a debtor's estate? While it seems unremarkable that the expenses incurred in bringing proceedings to challenge a prior transaction of the debtor are expenses in the relevant insolvency process,[88] it may be a step too far to extend this to the obligation to repay substantial but inadequate consideration arising as result of a successful challenge. Nevertheless, the argument remains untested.

Returning to the case itself, Lord Hodge noted that it was well-established that where a challenge is successful, the defender may not set off sums due to them by the insolvent for different purposes against their liability under the statutory provisions since that would defeat the purpose of the statutory provisions.[89] He did not, however, see that as an impediment to adopting the position that a purchaser defender might in certain circumstances receive the return of some or all of the consideration paid. That position could, of course, arguably be said to be distinguishable on the basis that the inadequate consideration due to the purchaser is part of the same transaction. Yet it could equally be seen as functionally equivalent to set off, with the result that the same rules should apply.

5. The Relevance of Good Faith

The court in *MacDonald v Carnbroe* indicated that whether a purchaser has a right to receive their money back, and how much of their money they can get back, depends on whether or not they are in good faith and at arm's length.[90] Consequently, there may now be a greater distinction between good faith and bad faith alienees in the context of gratuitous alienations. This may be regarded as strange given that, as Lord Hodge himself accepted, the statutory provisions apply irrespective of whether or not the seller and/or the transferee are aware of the insolvency,[91] and while the seller's knowledge of their insolvency is required to establish the fraud necessary to justify a challenge at common law, the transferee's knowledge is not relevant.[92] It may, however, reveal something of the rationale or policy of this part of the law of gratuitous alienations.[93]

In contrast to the pre-Carnbroe position, the law now considers that, in some circumstances, the general body of creditors are less deserving of a windfall than the alienee is of receiving protection for money paid. The law here focuses on preserving the estate as it existed before the relevant transaction, rather than expanding it. Those alienees in good faith will actually receive a priority compared to other creditors (who will simply have a claim against the insolvent's estate) if the court considers that they should receive some or all of their money back, while those in bad faith are not considered to merit protection or are less worthy of it. The policy position may indeed "punish" those in bad faith by not returning

[88] See, in the context of corporate insolvency, D. McKenzie Skene, "Corporate Insolvency", *Stair Memorial Encyclopaedia* (Reissue) (2008) para 390.
[89] See para [50], citing *Raymond Harrison & Co's Tr v North West Securities Ltd* 1989 S.L.T. 718; *John E Rae (Electrical Services) Linlithgow Ltd v Lord Advocate* 1994 S.L.T. 788; *Cay's Tr v Cay* 1998 S.C.L.R. 456.
[90] Paras [64]-[65].
[91] See para [32].
[92] Cf Lord Hodge's statement at para [44] that the knowledge of the transferor is not relevant at common law. It is respectfully suggested that this is not, in fact, correct: see McBryde, *Bankruptcy* (1995) para 12-36 and McKenzie Skene, *Bankruptcy* (2018) para 14-44 and authorities there cited.
[93] More generally, Bork, *Corporate Insolvency Law* (2020) para 6.29 suggests that the policy behind transactions at an undervalue is "based on the conviction that someone who has received a performance without consideration is not – or not in the same way as a person who granted a compensating counter-performance – worthy of protection of trust". He suggests that it is not based upon the principle of equal treatment of creditors, as the recipient is not necessarily a creditor. Nevertheless, avoiding the deprivation of assets from an insolvent's estate, to protect the interests of creditors, is also an important component of gratuitous alienations. Where there is some form of compensating counter-performance, albeit an inadequate one, this may justify protection being given for consideration paid, especially since there is generally no deprivation of assets in comparison to the pre-transaction position, once alienated property is returned.

consideration to them and determining that a windfall to the estate should be prioritised over their interests. This may dissuade those in bad faith from entering into transactions at an undervalue.[94]

The fact that good faith alienees may have consideration returned, while other creditors do not receive the same privilege, needs to be justified. For example, why should the alienee receive protection but not a party that has paid for goods (or services) from the debtor but does not receive the goods (or services) before the debtor enters an insolvency process? Likewise, a supplier could have provided goods (or services) to the debtor but not received payment prior to the debtor's liquidation or equivalent. In each of these instances, the debtor's estate has not only the goods but also sums received or funds which could (or should) have been used for payment by the debtor. Of course, insolvency law requires a broader view whereby there may be individual unfairness or loss to certain creditors, but this is a necessary consequence of balancing the interests of all stakeholders and providing solutions favourable to the creditors as a whole.[95] Why are gratuitous alienations a partial exception to this? Firstly, the transaction at an undervalue situation can usually be separated from these other situations on the basis that it was a transaction that had been completed by the time the insolvency process commenced,[96] and parties may have proceeded on the basis that the completed transfer was valid.[97] Secondly, the challenge to the transaction involves returning the position (at least regarding the value in the estate) to what it was at the point immediately prior to the transaction taking place. This unwinding should (arguably) not be limited to one side of the transaction alone and if a transaction is being undone and there is a good faith alienee who cannot be blamed for what has occurred, they should at least receive the consideration they paid. Thirdly, the parties in the other scenarios could have taken steps to prevent the company obtaining a windfall (e.g., by withholding payment until goods are supplied or through retention of title), whereas this is more difficult to do where a transaction has been completed, as is ordinarily the case with a gratuitous alienation. Fourthly, a gratuitous alienation requires an active step to challenge the transaction after the insolvency process has commenced, and property returned to the insolvent estate through the challenge could create a windfall in comparison to both the pre-transaction position and the position before the commencement of the insolvency process if the consideration is not returned or otherwise protected. With the other situations, there is no challenge by the liquidator or equivalent and the position at the start of the insolvency process does not change to become more favourable for the debtor's asset base and their creditors.

Unfortunately, in relation to the specific case of *MacDonald v Carnbroe*, the Inner House has not had the opportunity to decide upon the extent to which Carnbroe's knowledge of Grampian's circumstances may have rendered them in bad faith. However, in light of what is known about the extent of the purchaser's knowledge, it is certainly possible that they would not have received all of their money back following reduction. Perhaps, when considering this matter, the courts should recognise that there is likely to be a spectrum of knowledge that a party may have regarding the financial position and prospects of the counterparty, as well as a range of possible circumstances that may make them more or less complicit in depriving the debtor's creditors of assets, rather than a binary good faith and bad faith division. Thus, at one end of the spectrum, a connected party with full knowledge of the surrounding circumstances and who has colluded with the seller should not expect repayment of sums paid.[98] At the other end of the spectrum, there may be cases where the purchaser has no knowledge of the seller's circumstances at all. Even then, however, there may be lingering feeling that a purchaser who is getting something for well below its true value should have some concerns and should not perhaps be surprised if the transaction is later the subject of challenge. This is despite Lord Hodge's assertion that it is not realistic in a commercial negotiation to

[94] See Lord Hodge at para [64] on this, including with respect to the position before the Bankruptcy (Scotland) Act 1985. Such an approach is not unique: in the context of director disqualification, for example, it is an accepted part of the policy of the law to discourage unfit behaviour on the part of directors.

[95] This is perhaps exemplified by *Burnett's Tr v Grainger* 2004 SC (HL) 19.

[96] In the sense that both parties have performed their respective parts of the transaction. However, it should be acknowledged that in some cases, as in *MacDonald v Carnbroe*, the transferee may not have entirely fulfilled their obligation at the relevant time.

[97] Indeed, the transaction is only voidable rather than void.

[98] See para [64].

expect a purchaser to ask a seller why he or she is not demanding a higher price,[99] perhaps on the basis that one should not look a gift horse in the mouth. Indeed, in the instant case, the low price rang alarm bells with Carnbroe's lender, causing them to ask questions.[100]

Yet, even penalising a party at arm's length who has taken some advantage of a seller's difficult circumstances, of which they have some knowledge or to which they might have turned a blind eye, may be questionable. It seems that the more a party knows about the property and the seller, the more likely they may be considered to be in bad faith and not able to get some or all of their money back. This may be viewed as incentivising knowing less about the seller, which is at odds with usual commercial practice. Consequently, a degree of knowledge of the seller's financial circumstances should not by itself deprive a purchaser of the return of their consideration.

6. Exercising Judicial Discretion

The greater level of flexibility given to the courts by *MacDonald v Carnbroe* can be viewed as part of a wider trend in Scotland and throughout the UK towards courts having more discretion in insolvency matters and a larger number of cases coming before the courts asking them to exercise their powers. This is true in relation to restructuring plans (in the new Part 26A of the Companies Act 2006),[101] which have already generated a significant amount of case law (albeit outside Scotland).[102] Other areas of insolvency law have also witnessed recent cases regarding the exercise of discretion by the courts, including with respect to remedies.[103] While facilitating flexibility and pragmatic solutions is largely welcome, particularly in insolvency scenarios that are often fraught with competing interests and conflicting principles, this needs to be balanced against the greater certainty that comes from clear rules. That is equally true for the remedies applicable to gratuitous alienations.

Consequently, there is some advantage to having a "default" remedy, as indicated by the UKSC, which can be departed from in certain circumstances. Parties involved in disputes relating to challengeable transactions would have a better understanding of the potential outcome than if there is no standard remedy. However, if this is the law, it would be preferable for there to be a statutory provision stipulating it. A provision could state that there is a presumption that the court will simply order reduction or an equivalent restoration of property, with an express rule that a party seeking to have the court depart from this by qualifying the remedy or granting an alternative remedy (including taking account of consideration already paid as well as, possibly, other expenditure) must rebut the presumption and convince the court it is appropriate in the circumstances. This would strike a suitable balance between certainty and flexibility. Even if no statutory provision to this effect is introduced, there appears to be scope for the courts to develop equivalent rules. They already recognise that there is a default remedy, and parties desiring an alternative should have to show why the default remedy (alone) is not suitable.

In a situation where an alienee has no knowledge of the transferor's problems and there is no collusion, they should be able to easily rebut the presumption in favour of the default remedy and obtain the return of consideration paid (if the property is retransferred) or to make a further payment to reach full value for the property. The appropriateness of one of these remedies over the other could be contended for by the parties to the case, and may include not only taking account of consideration paid but also post-transaction expenditure. Furthermore, there may be situations where the liquidator (or equivalent) argues that an additional payment by the alienee is preferable to the default remedy of reduction. As well as the situations noted earlier, there are other examples. For instance, if a security right is acquired in good faith and for value from the alienee, the security holder is protected and would continue to have the ability to

[99] Para [45].
[100] Para [10].
[101] Inserted by the Corporate Insolvency and Governance Act 2020 s.7 and Sch 9 para 1.
[102] See e.g. *Re Virgin Active Holdings Ltd* [2021] EWHC 1246 (Ch); *Re Gategroup Guarantee Ltd* [2021] EWHC 775 (Ch); *Re DeepOcean 1 UK Ltd* [2021] EWHC 138 (Ch); *Re Virgin Atlantic Airways Ltd* [2020] EWHC 2376 (Ch).
[103] See e.g. *Royal Bank of Scotland Plc v Donnelly* 2020 CSOH 106, which considered *inter alia* the exercise of discretion regarding the remedy of reduction of a debtor's discharge in a non-corporate insolvency process (granting of a trust deed that became a protected trust deed).

enforce against the property even if it was returned to the transferor's estate.[104] As such, the consideration should not be repaid and, more than that, there could still be loss to the estate if the secured creditor enforced and the property was sold, as the estate would only have received the earlier inadequate consideration for it.[105]

7. Lessons from English Law?

The decision adopted by the UKSC moves Scots law closer to English law in relation to the remedies available where there is a transaction at an undervalue.[106] In England and Wales, upon a successful challenge, section 238(3) of the 1986 Act states that the court "shall… make such order as it thinks fit for restoring the position to what it would have been if the company had not entered into that transaction." While the use of "shall" suggests that the court must make an order for "restoring the position", the accompanying term "as it thinks fit" has been held to give the court discretion as to whether it should make an order at all and what that order should be.[107] The statutory wording therefore gives a broad scope to courts to formulate an appropriate remedy based on the circumstances. The specific remedies given in s.241(1) are non-exhaustive, and in seeking to achieve the general goal of placing both parties back into the position they were in before the transaction, the court's order should take account of any consideration paid.[108]

Unlike the apparent position in Scots law, there is no default remedy or presumption in English law regarding the remedy to be provided.[109] Yet an order should not place the debtor in a more beneficial position (i.e. provide a windfall) and it is recognised that an order to pay a further sum to reach full value for the property or to retransfer the alienated property and return the purchaser's consideration may not be sufficient to restore the position to what it would have been if the transaction had not taken place.[110] For example, recognition must be given to the fact that the alienee may have made improvements to the property or incurred other equivalent expenses, and, on the other side, the (lost) potential for the debtor to have acquired extra income or profits by virtue of having a larger asset base.[111] Company X may have sold

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[104] See the comments of Lord Hodge (paras [67]-[68]) who noted that if the secured creditor of the alienee had not been discharged, then, as a good faith acquirer of the security right (for value) from the alienee (Insolvency Act 1986 s.242(4)), their security would be protected and there would be no cause to qualify the annulment of the transfer "as the interested parties themselves can achieve substantive restitutio in integrum". However, as suggested in the following sentence in the main text here, the return of the property rather than a further payment could be disadvantageous for the insolvent's estate.

[105] This is assuming that there are insufficient funds left over to give to the insolvent debtor's estate after the secured creditor has been paid in full, e.g. where the security is for all sums due and the debt is (considerably) greater than the amount of the inadequate consideration paid, which may be the case especially if further debt has been incurred since the original transfer.

[106] For discussion of the English law position, generally, see e.g. K. van Zwieten, *Goode on Principles of Corporate Insolvency Law*, 5th edn (London: Sweet & Maxwell, 2018) paras 13-11 ff; A. Keay and P. Walton, *Insolvency Law: Corporate and Personal*, 4th edn (Bristol: LexisNexis, 2017) ch 38. See also the comparison of English law with Scots law in Blyth and Blank, "A New Approach to Balancing Competing Interests in Gratuitous Alienations" (2020) 13(2) CR&I 55.

[107] See e.g. *Re Paramount Airways Ltd* [1993] Ch 223 at 239 per Nicholls VC; and *Singla v Brown* [2008] Ch 357. And see D. Milman and P. Bailey, *Sealy & Milman: Annotated Guide to the Insolvency Legislation*, 24th edn (London: Sweet & Maxwell, 2021) pp.329-330; van Zwieten, *Goode on Principles of Corporate Insolvency Law* (2018) para 13-42, where it is also noted that a court will not make an order if the company would have been in "an even worse position if the transaction had not been carried out", citing *Re MDA Investment Management Ltd, Whalley v Doney* [2004] 1 BCLC 217. See too Keay and Walton, *Insolvency Law: Corporate and Personal* (2017) para 38.7.

[108] Section 241(1) provides some examples of orders, including requiring any transferred property to be vested in the company (s.241(1)(a)). See also s.241(2). As noted in van Zwieten, *Goode on Principles of Corporate Insolvency Law* (2018) para 13-43, there is no express reference to the court's ability to impose conditions on orders; however, such conditions are justified by the generality of s.238.

[109] *Ramlort Ltd v Reid* [2004] EWCA Civ 800 per Parker LJ at [125]; *Walker v WA Personnel Ltd* [2002] BPIR 621; van Zwieten, *Goode on Principles of Corporate Insolvency Law* (2018) para 13-42.

[110] See van Zwieten, *Goode on Principles of Corporate Insolvency Law* (2018) para 13-42.

[111] See *Phillips v Brewin Dolphin Bell Lawrie Ltd* [2001] 1 WLR 143; *Weisgard v Pilkington* [1995] BCC 1108; van Zwieten, *Goode on Principles of Corporate Insolvency Law* (2018) paras 13-42, 13-45 ff and 13-139 ff.

property worth £1,000,000 to Y for £500,000. If the property had remained in X's estate (or indeed if X had received the extra £500,000 for the property) it could have been used to generate further revenue for the company's business.[112] Yet, in the meantime, Y may have carried out a refurbishment of the property and X was able to earn interest on the money it did receive, and the value of the alienated property may have increased or decreased in value.[113]

Given that Scots law has now moved in the direction of giving a greater element of discretion to the courts, it could be contended that in devising an appropriate remedy in future, the issues addressed by English law should be taken into account in determining how much the alienee should pay to retain the property or in deciding how much the alienee should be paid in return for the property being transferred back into the debtor's estate. They could also be used to decide which of the remedies is most suitable in the circumstances. However, there is a considerable difficulty in doing this at present. Lord Hodge focused on consideration when discussing potential redress for the alienee, so it may mean that other financial issues are not relevant in such an assessment, but the position cannot be regarded as definitively settled. If a court were to take these issues into account, it would become a more challenging exercise to determine what exactly the remedy should be than if consideration alone is involved. If it is desirable to provide further discretion to the courts in this area, then statutory amendments would allow for the policy preference to first be ascertained, and then to implement a framework specifying what courts may take into account when devising a remedy.

V. CONCLUSION

As well as clarifying the meaning of adequate consideration, the UKSC decision in *MacDonald v Carnbroe* has overturned existing authorities and changed the law of gratuitous alienations regarding remedies. Specifically, there is now some flexibility to give effect to consideration paid by an alienee in certain circumstances. There is not, however, a general equitable jurisdiction available to the courts, unlike the apparent position in English law, and annulment by reduction or restoration apparently remains the primary remedy but may be qualified to provide redress for an alienee who was in good faith and paid consideration. Yet, as has been shown above, the parties themselves may often prefer for the alienee to make a further payment to reach an appropriate level of adequate consideration, rather than for the alienated property to be returned to the insolvent's estate. If the parties are in dispute though, and reduction or restoration remain possible, it is unclear whether the further payment approach can be ordered by the courts. In addition, while Lord Hodge's judgment only focused on consideration, there are various other forms of expenditure and financial issues that the law could take into account in devising a suitable remedy, and this is the approach adopted by English law. It may be, however, that *MacDonald v Carnbroe* precludes this approach.

The case, and the consequent new legal position, have been utilised above to identify the applicable rationale and policies in this area of law, which justify prioritising the return of consideration over other claims. Related to this, there is also now a greater distinction between good faith and bad faith in the law of gratuitous alienations, involving a spectrum of behaviour that may correspond to varying remedies, particularly how much, if any, consideration ought to be repaid.

Although the law prior to *MacDonald v Carnbroe* was subject to significant criticism, the likely outcome for cases was more certain than the new position (and there remain questions about issues such as the priority status of consideration claims and the common law position). The change brought about by the UKSC may prompt a more fundamental review of what the law in this area ought to do. Should we in fact be moving towards a general equitable jurisdiction regarding remedies? Should there remain default remedies which can be departed from if it is demonstrated to the court that this would be appropriate or fairer in the circumstances? Is greater flexibility desirable? In any event, it may be difficult for the courts to achieve this alone, and amendments to the statutory provisions in both the Insolvency Act 1986 and the

[112] See also the examples at van Zwieten, *Goode on Principles of Corporate Insolvency Law* (2018) paras 13-42 ff.

[113] As acknowledged in Keay and Walton, *Insolvency Law: Corporate and Personal* (2017) para 38.7, taking account of matters such as changes in the value of transferred property when deciding upon an appropriate order is not straightforward.

Bankruptcy (Scotland) Act 2016 would allow for policy preferences to be fulfilled and for greater clarity to materialise.