House of Lords has however now been granted in *Family Housing Association* v. *Donnellan* (Ch.D., 12 July 2001), and so the whole question may well be aired in the future.

And so to conclude: the Grahams are blessed, and Pye has learnt a hard lesson. The owner of land, even when registered as proprietor at the Land Registry, has responsibilities towards that land that he ignores at his peril. The House of Lords was in no mind to develop or reinterpret the jurisprudence and instead chose to reaffirm the orthodox version. The result may seem unfair, but the House of Lords was unrepentant; it reached the only possible conclusion that it could properly have done on its chosen terms. Thank goodness that the Land Registration Act 2002 will soon come into effect and then the present unsatisfactory jurisprudence will largely fade away into a twilight zone of harsh decisions and lucky breaks.

LOUISE TEE

THE UNCERTAIN FLIGHT OF *BRITISH EAGLE*

IN a winding-up, the property of the insolvent company must be liquidated and the proceeds distributed *pari passu* amongst its unsecured creditors. This being mandatory, a company cannot by contract arrange to do things differently, and a provision purporting to do so will be void (*British Eagle International Airlines* v. *Compagnie Nationale Air France* [1975] 1 W.L.R. 758). The scope of this common law rule of public policy is, however, notoriously uncertain. Neuberger J.'s judgment in *Money Markets International Stockbrokers Ltd.* v. *London Stock Exchange Ltd.* [2002] 1 W.L.R. 1150, based on a thorough and erudite review of the authorities, suggests some helpful clarifications.

Prior to April 2000, the London Stock Exchange ("LSE") was owned and controlled exclusively by its members. The LSE's rules provided, *inter alia*, that membership would terminate were a member declared a "defaulter"—being unable to pay its debts to other members. The LSE had been incorporated as a limited company, structured to give effect to the organisation's mutual character. Only "B" shares carried voting rights. Clause 8.03 of the articles of association required new members to acquire "B" shares; conversely, a shareholder ceasing to be a member would be required to dispose of its shares. "B" shares could only be transferred to firms that were members of the LSE, and not for any consideration.

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Money Markets International Ltd. ("MMI") was a member firm of the LSE. In February 1999 it was the subject of a winding-up petition. The next day, MMI was declared a defaulter, stripped of its membership, and in accordance with article 8.03, required to dispose of its "B" share for no consideration. Whilst MMI's liquidation was still ongoing, the LSE agreed to "demutualise", whereupon each "B" share became a liquid asset worth approximately £2.8 million. The liquidator of MMI argued that article 8.03 was void as a fraud on the insolvency laws, because it compulsorily deprived the insolvent company of the "B" share, which ought to have been available for its creditors.

Following the House of Lords' decision in *British Eagle*, the rule of public policy in question has often been referred to as the "*pari passu* principle". Yet the "deprivation provision" in *Money Markets International* did not offend *pari passu*, for no creditor was put in a preferential position. Neuberger J. accepted a broader basis for the rule, namely that it avoided provisions which deprived the insolvent of assets and thereby harmed unsecured creditors. Offending *pari passu* is just one way in which such harm could occur. Another, as in the instant case, is the removal of an asset for inadequate consideration. This analysis lends support to those who contend (*e.g.* Mokal, (2001) 60 C.L.J. 581) that the principle at play in *British Eagle* was not simply one of distribution, but was rather a more general rule about the protection of insolvency law's mandatory character.

LSE's principal argument was that article 8.03 constituted an inherent limitation on MMI's interest in the share. In insolvency proceedings, what constitutes the company's "property" is largely defined by reference to its pre-insolvency entitlements. Thus, the argument runs, a provision derived not from a collateral contract, but inherent in the property interest itself, does not deprive the company of anything it would otherwise have had. The interest is itself defined by the provision. It has long been established that a beneficial interest may be expressed to subsist only for so long as the beneficiary remains solvent, and that its determination does not offend insolvency law (*Brandon* v. *Robinson* (1811) 18 Ves. Jun. 429, 433). Less certain was whether this reasoning could be extended to a case where the "property" itself constitutes a bundle of contractual rights—as is the case with a share.

As Neuberger J. recognised, the notion of a deprivation provision as an inherent limitation on a package of contractual rights is fundamentally at odds with the House of Lords' decision in *British Eagle*, at least where it purports to take effect once insolvency proceedings have commenced. In that case, all five of

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their Lordships (albeit the minority only in the alternative) characterised the airlines' arrangement as giving rise to bilateral choses in action, subject to a restriction that they could only be enforced via the clearing house following multilateral netting. For the minority, the restriction formed an inherent limitation on the "property" to which British Eagle could lay claim. Yet for the majority, the "property" was conceived as bilateral obligations subject to collateral restrictions. The netting provisions would therefore have the effect of depriving creditors of assets to which they would otherwise be entitled—namely, the debts—and preferring clearing house creditors to general unsecured creditors. As a result, these provisions were void.

Although there is a certain bootstraps quality to the majority's reasoning in *British Eagle*, Neuberger J. rightly felt it compelled him to reject LSE's first argument. More radically, his Lordship suggested that the principle might also strike down so-called "*ipso facto*" clauses in contracts, which purport to terminate one party's obligations on the other's insolvency, noting an observation of Professor Goode that such clauses are rendered ineffective in the US by section 541(*c*)(i) of the Bankruptcy Code. Logically, determinable equitable interests should also be rendered ineffective, but Neuberger J. recognised that their validity—and that of forfeiture provisions in leases—was firmly, albeit anomalously, recognised by authority.

LSE's alternative argument, which his Lordship ultimately accepted, was that article 8.03 was not intended to subvert insolvency law, but rather to preserve the personal character of membership of the LSE. Clearly, following *British Eagle*, that the provision was neither drafted in bad faith nor expressed to take effect upon insolvency would not suffice to ensure its validity, if it had the *effect* of depriving the insolvent company of an asset to the detriment of creditors. "Detriment" for these purposes might depend on whether a preference was conferred on any creditor, whether the asset was valuable, and what consideration was given to the company in return. Thus, deprivation provisions relating to valueless assets, or requiring fair value to be paid (*Borland's Trustee* v. *Steel Bros. & Co. Ltd.* [1901] 1 Ch. 279), will not normally be struck down. By extension, the Judge accepted that contracts expressed not to be assignable, or property the ownership of which depended on the personal characteristics of the owner, could also be treated as valueless to creditors. In each case, a liquidator could not alienate them for value. This held the key to the case's resolution. Membership of the LSE was dependent on the personal characteristics of the members, was not capable of realisation by a

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liquidator, and hence might validly be the subject of a deprivation provision. The "B" share was by the scheme of the LSE's articles designed to confer rights *ancillary* to membership, and was not transferable to a non-member. This imbued "B" share ownership with the essentially personal characteristics of membership, and sufficed to validate article 8.03's operation.

The reasoning in *Money Markets International* is not free from difficulties. It is not immediately obvious that a no-assignment clause should validate a deprivation provision. Simply because a contract is unassignable does not mean that it is valueless to the creditors. The liquidator might, after all, be able to procure the company to complete the contract. Moreover, if (as they are) parties are free to include no-assignment clauses by contract, then this provides a straightforward way for those who wish to insert an *ipso facto* clause to "work around" the common law rule which Neuberger J. outlined. That said, similarly difficult distinctions are drawn elsewhere: for example, section 365 of the U.S. Bankruptcy Code renders *ipso facto* clauses invalid, but preserves no-assignment clauses. All in all, Neuberger J.'s thorough synthesis of the law answers more questions than it raises.

JOHN ARMOUR

THE DIRECTOR'S FIDUCIARY OBLIGATIONS—A FRESH LOOK?

IT is a pillar of equity that "a person in a fiduciary position must not make a profit out of his trust which is part of the wider rule that a trustee must not place himself in a position where his duty and his interest may conflict" (*per* Lord Upjohn in *Phipps* v. *Boardman* [1967] 2 A.C. 46, 123). The House of Lords in *Regal (Hastings)* v. *Gulliver* [1942] 1 All E.R. 378 demonstrated the unrelenting nature, and some have argued inequitable severity (see, *e.g.*, Jones, (1968) 84 L.Q.R. 472), of the director-fiduciary's obligations to his company. Such "absolutism" (Lowry & Edmunds, [2000] J.B.L. 122) is necessary because human infirmity makes it difficult to resist temptation, and it is only thus that the level of conduct for fiduciaries can be "kept at a level higher than that trodden by the crowd" (*per* Cardozo C.J. in *Meinhard* v. *Salmon* (1928) 249 N.Y. 456, 464). The principle that a director is free to act as a director of or otherwise engage in a competing business, established at the turn of the 19th century by Chitty J. in *London & Mashonaland Exploration Co. Ltd.* v. *New Mashonaland Co. Ltd.* [1891] W.N. 165 and assumed correct by Lord

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