

# Directors' Fiduciary Duties Survive Post-Insolvency

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In *Byers and Others v Chen Ningning (British Virgin Islands)* [2021] UKPC 4, the Privy Council held that the former director of an insolvent company owed fiduciary duties to the company in respect of payments alleged to constitute unfair preferences. This is a cautionary tale for directors of companies which become insolvent, who should be well aware of their continuing fiduciary duties and the need to take into account the interests of the insolvent company's creditors. It is also equally important for directors of insolvent companies to remember that they cannot evade their duties through delegation to an employee or a de facto director or by "*stand[ing] by idly and allow[ing] a company's assets to be depleted improperly*".

The claim was brought by the joint liquidators (the "Liquidators") of Pioneer Freight Futures Ltd ("PFF") based upon the alleged misfeasance of one of PFF's former directors, Miss Chen Ningning ("Miss Chen"). The appeal addressed a number of issues, including the changing nature of the duties of a director once the insolvent administration of a company becomes inevitable. That same issue fell to be considered by the English High Court in a number of cases heard last year, which we discussed in our "[Civil Litigation Review: 2020](#)".

PFF was a company incorporated in the British Virgin Islands (the "BVI") and until September 2008 was one of the largest traders of forward freight agreements ("FFA") in Asia. Miss Chen was the ultimate beneficial owner of a group of companies known as the Pioneer Group. Miss Chen became PFF's sole director in the course of 2007, following the resignation of the other two directors. PFF began to experience severe financial difficulties in 2008 due to a catastrophic collapse in the freight market and ceased trading in FFAs as a result. In 2009, it entered into a loan agreement with Zenato Investments Ltd ("Zenato"), a company owned and controlled by a business acquaintance of Miss Chen. Pursuant to the loan agreement, Zenato advanced US\$13 million to PFF in May 2009.

In October 2009, PFF lost an action that had been brought against it in the High Court in London by a FFA counterparty, Marine Trade. On the last day of the trial, PFF conceded that it was commercially insolvent, and the judge held that an event of default

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had occurred under the terms of the contract with Marine Trade and that any liability of Marine Trade to PFF was suspended whilst PFF remained indebted to Marine Trade (the “Marine Trade Judgment”). Shortly after the Marine Trade Judgment, PFF repaid its indebtedness to Zenato. However, PFF was insolvent at all times following the Marine Trade Judgment and therefore also at the time that the repayments were made to Zenato.

Subsequently, PFF applied in the BVI for the Liquidators’ appointment. Shortly after, the Liquidators began proceedings against Miss Chen in the High Court of Justice of the BVI, claiming the loan amount plus interest for breach by Miss Chen of her fiduciary duties as a de jure, de facto or shadow director of PFF, or as someone else whose role in the affairs of PFF (including as sole authorised signatory on its bank accounts) justified the imposition of fiduciary duties, for causing and procuring the repayments to Zenato. They also sought an order against Miss Chen pursuant to various sections of the 2003 Act for restoration of the funds paid to Zenato on the basis that the repayment of the loan constituted an unfair preference and was therefore a voidable transaction under the 2003 Act.

The trial judge, Bannister J decided in favour of Miss Chen, making his poor opinion of the merits of the Liquidators’ claims clear. The Court of Appeal agreed with the trial judge and dismissed the appeal on all grounds. The Liquidators subsequently appealed to the Privy Council on the following grounds:

- The judge ought to have found that Miss Chen was a de jure director of PFF at the time of the payments to Zenato and remained a de jure director of PFF until its liquidation. Even if Miss Chen was not a de jure director of PFF at the time of these payments, she was a de facto or shadow director because she retained responsibility for important aspects of PFF’s affairs and, in particular, its bank account and the payments it made. Irrespective of the precise nature of her directorship, Miss Chen owed fiduciary duties to PFF and, once it became clear that PFF was insolvent, to PFF’s unsecured creditors.
- The judge was wrong not to find that Miss Chen acted in breach of these fiduciary duties, as she permitted Zenato’s loan to be repaid in full when she knew that PFF was insolvent. At the time of the repayment, Zenato was only entitled to prove pari passu with PFF’s other unsecured creditors in the insolvency and, by allowing PFF to repay its loan in full, Miss Chen acted in breach of her duty to the company to have proper regard to the interests of all its creditors.
- The judge ought to have found that Miss Chen actually arranged or at least consented to the repayment of the Zenato loan and that the evidence that Miss Chen

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was involved in the payments to Zenato and did give her permission for them to be made was overwhelming and ought to have been accepted.

- As to the Liquidators' claim under the 2003 Act, the judge was wrong to reject it as he did on the basis that if Miss Chen was not liable for breach of fiduciary duty, then it followed that she was not liable under the provisions of the 2003 Act.

The findings of the Privy Council on the substantive issues in the case are set out below.

**Existence of Fiduciary Duties.** The judge had been entitled to find that Miss Chen continued to be a director after 29 May 2009 (i.e. the date of her letter of resignation). He had found that she had originally intended to resign from that date but that she had in fact remained a director until early August given that she continued to act, in relation to the business and affairs of PFF after 29 May 2009, in the same way as she did before that date. Although the Privy Council acknowledged the well-established principle that a director who had given the company proper notice of resignation was not entitled to withdraw that notice unless he or she had obtained the company's consent, the Privy Council explained that Miss Chen, in her capacity as sole shareholder of PFF's parent company (which, in turn, was the sole shareholder of PFF) and as ultimate beneficial owner of PFF, had in fact been able to consent to the withdrawal of her notice of resignation and that consent was binding on the company, according to the principles set out in *Duomatic Ltd, Re* [1969] 2 Ch. 365, [1968] 11 WLUK 45 and *Ciban Management Corp v Citco (BVI) Ltd* [2020] UKPC 21, [2021] A.C. 122, [2020] 7 WLUK 463.

The Privy Council considered that the judge had erred in finding that Miss Chen had ceased to be a director in early August. The judge's finding was based on a mistaken belief that it was common ground that Miss Chen had resigned before the payments to Zenato were in contemplation. However, there was no evidence that she had resigned at that time.

The Privy Council considered that the judge's conclusion was wrong, and that this error was "a highly material" one and "of fundamental importance to the outcome of this appeal". It was therefore appropriate for the Privy Council to intervene. The Privy Council explained that the key question was not whether there was positive evidence that Miss Chen continued to be a de jure director after the beginning of August 2009 but whether there was any evidence that she ceased to be a de jure director at about this time. The Privy Council held that there was no such evidence; the judge erred in law in making the finding that he did and the Court of Appeal also erred in failing to identify and correct the Judge's error. Miss Chen had in fact continued to be a director after August and had therefore continued to owe fiduciary duties.

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**Breach of Fiduciary Duty.** As to the question of whether, by failing to intervene to prevent the Zenato payments, Miss Chen acted in breach of her fiduciary duties to PFF, the Privy Council noted that Miss Chen was a de jure director of PFF and the sole authorised signatory on the account from which the Zenato payments were made. The Privy Council stated at paragraph 91 of the judgment that *“when making or authorising payments from PFF’s account, Miss Chen had a fiduciary duty to act honestly and in good faith in what she believed to be the best interests of PFF and, through PFF, an insolvent company, in the best interests of its creditors. Similarly, she had a duty to exercise her powers as a director for proper purposes, that is to say, once PFF became insolvent, for purposes which would further the interests of PFF’s creditors. Further, in light of PFF’s insolvency, the normal principle that Miss Chen, as the ultimate owner of PFF, could waive or ratify any such breach of duty was displaced.”*

The Privy Council then stated at paragraph 92 of the judgment that *“Miss Chen could not evade these duties to PFF and, through PFF, to its creditors, simply by delegating to an employee or a de facto director her authority to make payments from PFF’s account. It has been held in a number of cases, correctly, in the Board’s opinion, that a director may not knowingly stand by idly and allow a company’s assets to be depleted improperly. [...] To the contrary, a director who knows that a fellow director is acting in breach of duty or that an employee is misapplying the assets of the company must take reasonable steps to prevent those activities from occurring.”*

The Privy Council concluded that, even if another employee was the one responsible for repaying the loan, and by this time the employee in question was in charge of PFF’s affairs as sole de facto director, Miss Chen was still aware of these payments and had *“a fiduciary duty to PFF to take all reasonable steps to intervene to prevent a payment being made from a trading account of which she was sole signatory for an improper purpose”*. The Privy Council held at paragraph 93 of the judgment that *“[t]he repayment of the whole of the Zenato loan was undoubtedly improper”* and that *“[Miss Chen’s] inaction amounted to a breach of her fiduciary duty to PFF”*.

The Privy Council therefore held that the current appeal should be allowed on the basis that Miss Chen owed fiduciary duties to PFF at the time of the repayment of the Zenato loan, and her failure to intervene to prevent that repayment amounted to a breach of duty.

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Please do not hesitate to contact us with any questions.

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