

## Lessons from Scotland: environmental regulators' claims as contingent debts or liquidation expenses in insolvency proceedings (and the future toppling of a Celtic giant?)

Blanca Mamutse

### **Abstract**

This paper examines two 2018 judgments of the Scottish Court of Session relating to the insolvency of Dawson International plc and Doonin Plant Ltd, which are notable for a number of reasons. In contrast to established cases involving the disclaimer of environmental obligations, the *Dawson* and *Doonin* decisions do not involve a collision between environmental protection legislation and insolvency legislation. They raise issues regarding the status of a regulator's claim for clean-up costs, where a company has entered insolvency proceedings prior to enforcement action being taken/concluded. In upholding environmental interests through a statutory interpretation approach rather than a policy-oriented approach, *Dawson* and *Doonin* mark a clear separation from English precedent that is at least two decades old, deepening intrigue as to whether the outcomes in *Dawson* and *Doonin* have increased the likelihood of the standing English authority being over-ruled in the near future.

### **A. Introduction**

*Nimmo, Administrator of Dawson International plc*<sup>1</sup>, and *Nimmo and Friar as the joint liquidators of Doonin Plant Ltd*<sup>2</sup> are the newest additions to Scottish case law on the standing of environmental clean-up responsibilities, where a company enters administration/liquidation proceedings. The cases represent a welcome shift from the disclaimer cases, which centred on largely similar themes.<sup>3</sup> They shed more light on the courts' approach to treating environmental remediation obligations as contingent debts or liquidation expenses, and office-holders' exposure to liability for such obligations. These two judgments also come soon after the *Scottish Coal* decision<sup>4</sup>, which departed from the leading English authority on disclaimer (*Re Celtic Extraction*),<sup>5</sup> by ruling that liquidators did not have power to disclaim land and statutory licences/permits; inviting interest as to whether the reasoning in the Scottish decisions will be followed by English courts in future. Scope for adoption of the *Dawson* and *Doonin* decisions is intensified by the fact that compared to *Scottish Coal*,<sup>6</sup> the *Dawson* and *Doonin* cases did not involve any notable differences between

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<sup>1</sup> [2018] CSOH 52.

<sup>2</sup> [2018] CSOH 89.

<sup>3</sup> *Re Mineral Resources Ltd* [1999] 1 All ER 746; *Re Celtic Extraction* [1999] 4 All ER 684; *Environment Agency v Hillridge Ltd* [2003] EWHC 3023; *Nimmo and Friar, Joint Liquidators of the Scottish Coal Company Ltd* [2013] CSOH 124.

<sup>4</sup> *Scottish Environment Protection Agency v Joint Liquidators of the Scottish Coal Company Ltd* [2013] CSIH 108.

<sup>5</sup> (n.2).

<sup>6</sup> (n.4), [124]

English and Scottish insolvency law.<sup>7</sup> Furthermore, the environmental legislation considered in both judgments applies in both England and Scotland. Aside from the prospects of future take-up of these decisions, they open a window into the courts' understanding of their role in this domain, and how far this constitutes a break with established precedent.

The decisions are outlined below in chronological order, with substantial attention to the complexity of the facts and argument behind the judgments. The space of three months between the handing down of the judgments meant that the *Dawson* decision could inform counsel's submissions in the *Doonin Plant* case.<sup>8</sup>

### **B. *Nimmo, Administrator of Dawson International plc***

This was an application for directions, in circumstances where one company's actions had produced environmental damage, a related company had voluntarily engaged in remediation efforts with respect to the damage, and both companies had now collapsed.

Between 1980-2000, Dawson International plc ('DIP') was overall parent company in a corporate group with subsidiaries including POS, a knitwear manufacturing company that owned a factory in Berwick-upon-Tweed ('the site'). POS's manufacturing activities at the site involved use of the solvent tetrachloroethylene. This solvent incurred several spillages over an extended period, resulting in tetrachloroethylene penetrating the ground at the site and migrating into the groundwater contained in an aquifer under Berwick-upon-Tweed from which neighbouring landowners abstracted water for business activities. In 1992, POS was prosecuted over a spillage at the site, and was convicted of an offence under the Water Resources Act 1991. Following the conviction, POS executed various measures to combat pollution of the groundwater and potentially the River Tweed. These included installation of equipment for treating and decontaminating the groundwater under the site, which was flowing into the aquifer, and indemnifying a neighbouring landowner against costs of decontaminating any water that this landowner abstracted from the aquifer.

In 1997, POS entered a business transfer agreement to sell its entire undertaking, property and assets to another subsidiary in the group with effect from January 1998. The sale included heritable property relating to the business, and liabilities of the business. The purchaser, DITL, indemnified POS against all liabilities of the business – present, future, contingent, disputed. Operations on the site were closed by POS in the late 1990s, but since the closure date was uncertain, the noter averred that it was unclear whether those operations were part of the business comprised in the business transfer agreement. Although the business transfer agreement required POS's heritable property to be conveyed to DITL, the site was not

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<sup>7</sup> (n.1), [77]; (n.2), 51.

<sup>8</sup> (n.2), [11].

conveyed to DITL and in 2001 POS contracted to sell the site to another company. The sale agreement for the site required POS to 'retain all liability and responsibility for remediation of the Known Contamination' (defined as tetrachloroethylene contamination of the aquifer).<sup>9</sup> POS also indemnified the purchaser for any liability that it may be subjected to for the 'Known Contamination'.

The purchaser company DITL entered receivership in 2010, and the site was sold to the second respondent in these proceedings, TTL (current owners of the site). POS was dissolved in January 2012, hence ceased to exist. Joint administrators were appointed to DIP and DITL in August 2012. In investigating the corporate group's affairs, the noter discovered that in the period since 1998, remediation work had been conducted at the site, most recently through use of a pump-and-treat system. The legal basis for performing this remediation work was questionable, since from mid-2001 the site had not been in the ownership of any company within the group headed by DIP. Water abstraction and discharge licences relating to the site had however been held in DIP's name.

At the time of these proceedings, the noter held £3,296,529.18 in the administration, to meet administration expenses and creditor claims. The largest claim submitted belonged to the Pension Protection Fund ('PPF', third respondent), for £10,366,153 in respect of DIP's staff pension plan. DIP's administration had now been ongoing for over 5 years, and the noter sought to conclude it and distribute funds to the creditors of the company. However, the tetrachloroethylene contamination raised the possibility that DIP retained some form of liability to the Environment Agency (first respondent), under the Environmental Protection Act 1990 or the Water Resources Act 1991, with respect to either/both the cost of remediating the contaminated land at the site, and the cost of maintaining the pump-and-treat system for an unspecified future period. Such liability could cause a considerable delay in making any distribution in the administration proceedings. At worst, accounting for either cost as an administration expense that ranked ahead of ordinary unsecured creditors such as the PPF, would substantially diminish the amount available for distribution to such creditors. The site's location also suggested to the noter that English law would govern the existence and quantification of any potential liability on DIP's part. However, Scots law governing administration would apply to determining whether any such liability should be characterised as an administration expense, or as a provable debt in the administration.

The Environment Agency had not asserted a claim in the administration, but had indicated that further investigations would be necessary to establish whether a claim existed. The emergence of a claim against DIP would depend on the outcome of those investigations and the subsequent designation of the site as 'contaminated land' and a 'special site' – a process which could take several years. The Environment Agency had also affirmed that relevant

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<sup>9</sup> (n.1), [7]

English environmental legislation imposed a duty upon the noter to keep the pump-and-treat system in place for an indefinite period, regardless of the expense; and failure to fulfil these obligations would result in the noter incurring liability for the remediation costs in his personal capacity as well as *qua* administrator. Yet, the noter had been advised by specialist environmental consultants that the pump-and-treat system was no longer yielding appreciable benefits and could therefore be closed down. These circumstances left the noter in a difficult position as to how to conclude the administration and distribute assets to creditors. He interpreted the Environment Agency's contention that the prospect of liability under Part 2A of the Environmental Protection Act 1990 prevented him from distributing DIP's assets, as implying that the costs of remedial work would constitute an administration expense. He was concerned that sustaining the pump-and-treat system indefinitely, without making a distribution, would prejudice the interests of the general body of creditors by reducing the amount available for distribution while increasing the fees payable to the noter and advisers. Furthermore, while the noter was conscious that treating 'a far-off claim'<sup>10</sup> which could not presently be valued as an administration expense might occasion a significant delay to resolution of the administration, he wanted to avoid prejudicing the Environment Agency's interests if it were found to be a major creditor of the administration.

The noter accordingly sought directions under Insolvency Act 1986, Schedule B1, paragraph 63 as to the appropriate course of action in concluding the administration, specifically:

- (i) Whether either/both the noter and DIP were 'appropriate persons' under the Environmental Protection Act 1990 or the Water Resources Act 1991 (the '1990/1991 legislation') in terms of liability to the Environment Agency for costs of remediating the site and the costs of treating the groundwater or the aquifer under the site.
- (ii) Whether, in line with his duties under the 1990/1991 legislation on one hand, or Scots law governing insolvent administrations on the other, the noter could/should permanently disconnect the pump-and-treat system and proceed to conclude DIP's administration.
- (iii) Whether, in the event that DIP or the noter were liable to the Environment Agency under the 1990/1991 legislation as an 'appropriate person' for the costs in direction (i) above, if that liability should be classed as an administration expense or as a debt for which the Environment Agency ranked as an ordinary unsecured creditor in the administration.
- (iv) Whether, in the event that any liability in direction (i) above should be classed as an administration expense, the noter may/should require the Environment Agency and all other would-be creditors of DIP regarding administration expenses, to submit claims to the noter for the full value of their claims together with supporting evidence of DIP's indebtedness and the status of the debt as an

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<sup>10</sup> *Ibid*, [13].

administration expense, within 28 days of the noter's invitation to such creditors to submit such claims and evidence.

The Environment Agency and TTL both averred that the Note should be refused. The Environment Agency's position was that the noter was not entitled to seek direction from the Scottish courts on whether DIP was an 'appropriate person' or to seek direction as to the costs of countering/treating groundwater under the site or aquifer, and furthermore had not provided the court with the information required to determine that question. Similarly, TTL saw the orders sought as falling outside the Court of Session's jurisdiction, as they included matters governed by English law, specifically whether DIP was an appropriate person under the 1990 Act and whether the noter could permanently turn off the pump-and-treat system. On the other hand, the PPF generally accepted the noter's position, and rejected the notion that the Environment Agency had any standing in the proceedings, or that if any statutory liabilities were imposed they would constitute debts capable of being claimed in the administration. Hence, the noter's obligations were to use the available assets in the administration only for the benefit of current creditors and to stop funding the operation of the pump-and-treat system. Even if it were to be established that DIP and the noter should use the available assets for the purpose of any remedial works in relation to the site, such sums would not constitute expenses of the administration, as they would not be expenses arising from acts/decisions taken by the noter during the administration. Rather, they arose from events which occurred before the administration.

Lord Clark began with the first/primary issue: whether the Environment Agency could have a claim in the administration. He recognised the Environment Agency's position as being that, subject to the site being designated as contaminated land and a special site, it had a right to have the contamination remedied. The Agency was evidently asserting that it was a contingent creditor. This activated the application of the principles laid down in *Liquidator of Ben Line Steamers Ltd, Noter*<sup>11</sup> and *Re Nortel GmbH*,<sup>12</sup> in particular the three-part test formulated in the latter case, for determining whether a company is subject to liability pursuant to a statutory provision 'which was in force before the insolvency event'.<sup>13</sup> The components of the test had been fulfilled: (a) the companies had taken 'steps' with some legal effect by assuming control of the contaminated premises, failing to remediate the contamination and knowingly permitting the continued contamination. (b) These steps subjected them to a legal duty/relationship which rendered them vulnerable to the specific liability in question, in that the Environment Agency could serve notices under the 1990/1991 legislation. (c) It was consistent with the regime imposed by the 1990/1991 legislation to conclude that these steps gave rise to an obligation from which a contingent liability arose; otherwise, a company could knowingly cause contamination and avoid any liability by

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<sup>11</sup> [2010] CSOH 174.

<sup>12</sup> [2013] UKSC 52.

<sup>13</sup> *Ibid*, [77].

entering insolvency proceedings before enforcement was initiated.<sup>14</sup> In keeping with *Liquidator of Ben Line Steamers Ltd*: as a result of the companies' acts/omissions, there were existing obligations before the administration, whose enforceability depended on the occurrence of future events (i.e. the designation of the site as contaminated land and as a special site, and the issuing of a Works Notice).

Notably, Lord Clark did not consider the previous decisions *Re Mineral Resources Ltd*<sup>15</sup> and *Re Celtic Extraction Ltd*<sup>16</sup> as being of any assistance. In *Mineral Resources*, the point whether the Environment Agency could prove that it was an ordinary creditor was *obiter*. That matter turned on its own facts, and the judgment did not have the effect of preventing the Environment Agency from claiming in proceedings based on the 1990/1991 legislation. The present case was also distinguishable from *Celtic Extraction*, where the English Court of Appeal rejected the argument that the costs of continued compliance should be classed as an administration expense. Here in the *Dawson* case, it was the position prior to administration which drew into question whether the Environment Agency could claim as a creditor. Lord Clark therefore concluded that the Environment Agency could claim as a creditor of DIP. Hence, he rejected the PPF's arguments on the Environment Agency's lack of standing, as well as its contention that directions (ii) and (iv) should be upheld instead of directions (i) and (iii).

The question whether the orders sought in the note were a proper subject for directions by the court centred on the Insolvency Act, Schedule B1, paragraph 63, and whether an administrator's right to seek directions was confined to matters concerning proper interpretation of insolvency law governing the administration. 'Questions of the kind raised, which affect the treatment of claims or potential claims, can be suitable issues for directions.'<sup>17</sup> Paragraph 63's application could be determined by addressing each of the directions consecutively, to consider which function of an administrator it was said to be connected with, and whether a connection did in fact exist.

Lord Clark saw no difficulty in concluding that direction (i) fell within the scope of paragraph 63. The functions of administration clearly included distributing assets to creditors, and managing the administration process to completion. The issues on which a potential creditor claim was founded could be regarded as matters arising in connection with these functions. Direction (ii) likewise fell within the scope of paragraph 63: it was plain that any duties under the 1990/1991 legislation were a vital feature of this direction and thus that it was somewhat dependent on direction (i). Finding that the companies were not 'appropriate persons' would affect the administrator's obligations and his ability to distribute money to creditors. The answer to the question whether the noter/DIP were 'appropriate persons' obviously affected

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<sup>14</sup> (n.1), [78].

<sup>15</sup> (n.3).

<sup>16</sup> (n.3).

<sup>17</sup> (n.1), [87].

aspects of the administrator's performance/fulfilment of these functions. Furthermore, the questions underlying directions (i) and (ii) could not be viewed as the type of commercial or administrative decisions that the courts are generally reluctant to entertain.<sup>18</sup>

Lord Clark noted the protracted history of the matter, and that the only obstacles to the distribution of assets and completion of the lengthy administration were the issues raised in the directions. The directions sought would have the effect of preventing any further delay in completion of the administration. Public funding constraints in the Environment Agency's ability to conduct the necessary investigations/analysis did not provide a solid basis for hindering conclusion of the administration and protecting the interests of the general body of creditors.

Thus, directions (i) and (ii) were appropriate subjects for directions, notwithstanding respondents' arguments that they fell outside the court's jurisdiction, that the Environment Agency had no standing in these proceedings, and that any amounts applied towards remediation of the site could not amount to administrative expenses.

### ***C. Nimmo and Friar as the joint liquidators of Doonin Plant Ltd***

This matter also involved an application for directions. However, in contrast to the *Dawson* case, it centred on the implications of a single company's collapse in circumstances where it had not undertaken any remediation of unlawful waste deposits linked to its operations, despite being called upon by the regulator to do so.

Doonin Plant Ltd ('DPL') carried on a waste management business at various sites including a former colliery ('Armadale site'/'the site'). It held licences under the Environmental Protection Act 1990 ('EPA 1990') for certain waste management activities. The licence for the Armadale site was suspended in 2006, and the company and one of its former directors were convicted of breaching the EPA 1990 in respect of deposits made at the site. In December 2012, the Scottish Environment Protection Agency ('SEPA') issued a notice demanding that DPL remove unlawful waste deposits from the Armadale site by March 2013. Following DPL's liquidation in July 2015, SEPA issued another notice demanding DPL's removal of controlled waste from the site within 6 months, and action to eliminate/reduce the consequences of the waste deposits within 12 months. DPL did not undertake any remediation work with respect to either notice. The liquidators did not carry out any waste management activities at the site. The liquidators succeeded in realising all of DPL's assets save for the Armadale site. They estimated the cost of remediation work to comply with the notices to be in the region of £2.3-£3.7 million, against the company's funds of £600,000 before payment of liquidation expenses; and further expenses/services that had yet to be quantified. DPL's financial position

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<sup>18</sup> *Re T & D Industries* [2000] 1 WLR 646, 657.

thus fell ‘far short of the expenditure which would be required to comply fully with the ... notices’.<sup>19</sup>

The liquidators sought directions regarding whether the funds they had gathered should be applied towards remediation, in particular:

1. Whether the obligations to comply with the notices, or SEPA’s right to perform the remediation and recover the costs from DPL, constituted ordinary unsecured debts in liquidation; or if not
2. Whether the liquidators were obliged to ensure that the available funds were directed towards fulfilment of DPL’s obligations, and if so,
3. Whether the remediation costs would constitute ‘expenses of the liquidation’ under the Insolvency (Scotland) Rules 1986. Linked to this, the liquidators requested an order under the Insolvency Act 1986 s.156, that their expenses and remuneration should be accorded priority over that liquidation expense.

The parties’ arguments proceeded as follows:

Issue	Liquidators	SEPA
1.	<p><b>To be answered in the negative</b></p> <p>The obligations under the notices did not create debts to SEPA.</p> <p><b>To be answered in the affirmative</b></p> <p>SEPA’s reasonable expenses of remediating the site constituted a contingent debt owed at the liquidation date.</p>	<p><b>To be answered in the negative</b></p> <p>Obligations to comply with notices were not a debt owed to anyone, and were incapable of being enforced by private law action. Unlawful non-compliance constituted a criminal offence. Civil liability for SEPA’s remediation expenses could only flow from its service of the notices and its performance of the remediation work. Based on SEPA’s policies and limited resources it was apparent that at the date of DPL’s liquidation, there had been no real prospect of SEPA performing the works, so as to give rise to the contingent debt.</p>
2.	<p><b>To be answered in the negative</b></p> <p>Since SEPA’s remediation expenses were a contingent debt, issues 2 and 3 fell away.</p> <p>Even if the expenses were not a contingent debt, the liquidators were not bound to perform the obligations under the notices, as these were requirements imposed on DPL through SEPA’s exercise of its statutory powers.</p> <p>No requirement had been imposed on the liquidators, and it would be improper for them to give the obligations</p>	<p><b>To be answered in the affirmative</b></p> <p>A company’s private law obligations persisted between its liquidation and dissolution, even if there was no specific means of enforcing them. This was also true of its statutory obligations. The requirements imposed on DPL by the notices arose or continued after the date of its liquidation.</p>

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<sup>19</sup> (n.2), [8].

	under the notices ‘a priority which the statutory scheme does not accord to them’.	DPL remained bound to comply with the requirements under the notices to the extent that this was possible with the available assets, notwithstanding the liquidation.
3.	<p><b>To be answered in the negative</b></p> <p>Since the liquidators were not obliged to use the funds gathered for DPL to comply with the obligation under the notices, this issue did not arise.</p> <p>Any payment towards compliance would not fall within the Insolvency Rules’ definition of ‘liquidation expense’.</p> <p>Although a legislative provision enacted for the purpose of giving effect to an EU Directive should be given ‘a conforming interpretation’, this interpretation could not run counter to the legislation. In particular, such an interpretative exercise could not empower the court to make decisions on issues it was not equipped to evaluate, such as the importance of environmental preservation, weighed against the equal and expeditious distribution of available assets among the unsecured creditors of an insolvent company.</p> <p>The EPA 1990 did not expressly provide for the obligations under the notices to bind liquidators instead of, or alongside a company like DPL. Nor could such liabilities be implied on a proper construction of the relevant provision. Adopting SEPA’s approach ‘would make liquidations unworkable’<sup>20</sup> in circumstances where companies had equally substantial obligations to comply with notices (the specific policy concerns of liquidators are elaborated below).</p>	<p><b>To be answered in the affirmative</b></p> <p>The interpretation of EPA 1990 liabilities should be in line with the Waste Framework Directive (‘WFD’). It could be reasonably concluded that the statutory intent was for funds expended under the provisions of the EPA 1990 regarding compliance with notices, to constitute liquidation expenses, as outlays properly incurred in connection with the liquidators’ functions under the Scottish Insolvency Rules.</p> <p>The UK’s compliance with its obligations under the WFD required that there should be an ‘effective means’<sup>21</sup> of ensuring that depositors of unlawful waste bear responsibility for its removal and remediation. ‘That is so even if the person becomes insolvent’.<sup>22</sup> Hence, in the event of liquidation a company should still be obliged to remove and remediate waste, and the expense should be a liquidation expense. Otherwise polluters would generally escape liability. Indeed, companies could enter voluntary liquidation in order to escape their liabilities to comply with notices.</p>
s.156 order	In the event of affirmative answers to Issues 2 and 3, the liquidators sought an order conferring priority to their remuneration and expenses, over the costs of compliance with the notices.	In the event of affirmative answers to Issues 2 and 3, SEPA would not oppose the application for this order.

Lord Doherty did not consider this careful framing of the issues to be crucial to the outcome of this case. He rejected the notion that Issue 1 should be considered first, and Issues 2 and 3 would not arise if it was answered in the affirmative. Strictly speaking, the starting point should be whether expenditure to comply with the notices should be a liquidation expense.

<sup>20</sup> Ibid, [28].

<sup>21</sup> Ibid, [37].

<sup>22</sup> Ibid.

If so, it would be unnecessary to consider Issue 1. For convenience, however, he dealt with the issues following the order in which they had been presented.

### *Issue 1*

While it was common ground that at the liquidation date the obligations to comply with notices were not debts owed to SEPA, the question was whether SEPA's statutory right to complete the work and claim its remediation expenses gave rise to a contingent debt. It was thus necessary to turn to the three-part test articulated in *Re Nortel GmbH*.<sup>23</sup> DPL's unauthorised deposit of waste had very significant legal effects which brought it squarely within the EPA 1990 regime, hence part (a) of the test was satisfied. However, part (b), which requires that the company's actions create 'a real prospect of ... liability being incurred', was unfulfilled since the unlikelihood of SEPA carrying out the necessary remedial work meant that there was no real prospect of the company becoming liable to reimburse SEPA. Part (c) of the test, i.e. whether it is consistent with the relevant liability regime to conclude that the company's actions gave rise to an obligation, was also unsatisfied since it was inconsistent with the regime under the relevant EPA 1990 provision that SEPA's reasonable expenses of remediation should give rise to a contingent debt. Instead, the regime imposed by the provision envisaged that money spent by a company on these remedial costs should be a liquidation expense. Consequently, **Issue 1 was answered in the negative** as regards both the obligations to comply with notices, and liability for SEPA's reasonable costs of remediation.

### *Issue 2*

DPL's obligations to comply with notices remained notwithstanding the liquidation; the question being what priority should be accorded to them. To determine whether the liquidators were obliged to incur the remediation costs, it was necessary to begin by establishing whether such costs were liquidation expenses. Accordingly, **the resolution of Issue 2 was dependent upon the outcome of Issue 3.**

### *Issue 3*

The court accepted that the wording of the relevant EPA 1990 provision did not make clear that liability for compliance with notices was a company obligation which liquidators were obliged to meet as part of the liquidation, and that the resulting expenditure would constitute a liquidation expense. The critical issue was therefore whether the legislature could reasonably have intended that liquidators' costs of compliance with a notice would amount to a liquidation expense which would rank ahead of provable debts.

The court considered the nature of obligations which could be imposed under a notice, in light of the aims and objectives of the WFD that Part II of the EPA was intended to implement.

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<sup>23</sup> (n.12), [77]

The approach was thus similar to that followed in the interpretation of domestic legislation implementing an EU Directive. The relevant provisions of the WFD and the EPA 1990 promoted objectives of ‘the protection of human health and the environment against harmful effects caused by the collection, transport, treatment, storage and tipping of waste’.<sup>24</sup> The polluter-pays principle also represents one of the main objectives of the WFD. The court accordingly concluded that the legislature must have reasonably intended a liquidator’s expenditure in complying with a notice to be a liquidation expense. Otherwise it was highly likely that insolvent polluters ‘would frequently escape paying for the damage to the environment which their conduct has caused’.<sup>25</sup>

Compared to previous decisions *Re Mineral Resources Ltd*<sup>26</sup> and *Scottish Environment Protection Agency v Joint Liquidators of Scottish Coal*<sup>27</sup>, Lord Doherty considered that in this instance the court’s analysis did not involve ‘weighing the relative importance of protection of the environment on the one hand and the expeditious and equal distribution of available assets on the other’.<sup>28</sup> Instead, it centred on accurately characterising the position of liabilities to comply with notices, in an insolvency; the nature of which indicated that they should be liquidation expenses. This conclusion did not contradict the statutory scheme in the Insolvency Rules, rather it clarified where these liabilities fell within this scheme. Contrary to the view expressed in *Re Celtic Extraction Ltd*, treating environmental obligations to comply with SEPA notices as a liquidation expense meant applying a company’s assets in accordance with the statutory liquidation regime, and did not provide a means of shifting the burden of payment from the polluter itself to the polluter’s unsecured creditors.

The court also addressed the specific policy arguments raised by the liquidators with respect to Issue 3, that treating liabilities to comply with notices as a liquidation expense would deter insolvency practitioners from accepting appointment as liquidators. These arguments ran as follows: firstly, if expenses of compliance with notices enjoyed priority over liquidators’ remuneration unless the court ordered otherwise, insolvency practitioners would not run the risk that the court might decline to make such an order. Secondly, contractors who were needed to carry out the work involved with liabilities to comply with notices would probably only accept engagement subject to liquidators being held personally liable under the contracts. Thirdly, in situations such as the present, where the company’s funds would not stretch to cover all the compliance work required, liquidators would be faced with the difficult task of identifying which aspects of the work should take precedence over others. In rejecting these warnings, Lord Doherty followed the approach of the Inner House in *Scottish Environment Protection Agency v Joint Liquidators of Scottish Coal*,<sup>29</sup> where similar arguments

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<sup>24</sup> (n.2), [64].

<sup>25</sup> *Ibid*, [65].

<sup>26</sup> (n.3), 756-757.

<sup>27</sup> (n.4), [144].

<sup>28</sup> (n.2), [66].

<sup>29</sup> (n.4), [78]-[79].

were adopted by the same liquidators. He observed that although an affirmative answer to Issues 2 and 3 could make liquidators' work more challenging, these particular difficulties did not render the liquidation process unworkable. He highlighted ways in which the difficulties were all surmountable, namely that there was no real risk of a court refusing to confer priority to a liquidator's remuneration above expenditure for compliance with notices, if it was necessary to ensure that a liquidator was remunerated. In addition, liquidators negotiating contracts could be expected to protect their own interests as well as those of the company. Finally, it could be anticipated that liquidators' decisions concerning the deployment of limited available resources would be made in consultation with SEPA. **Thus, Issues 2 and 3 should be answered in the affirmative.**

Turning to the s.156 application, the court concluded that it was appropriate to order that the liquidators' remuneration and expenses should be paid from DPL's assets in priority to the expenses of complying with the SEPA notices.

#### ***D. Immediate lessons from these developments***

Starting from very different factual bases, both cases plainly go some way towards elucidating the circumstances in which responsibility for environmental clean-up may constitute a contingent debt or liquidation expense. The *Dawson* decision demonstrates how a regulator such as the Environment Agency can become an unsecured creditor in insolvency proceedings concerning a company which was carrying out remediation activity on its own initiative rather than by virtue of any regulatory intervention. Insolvency officeholders who find themselves in situations where notices have not been issued against the company (or necessary investigations have not yet even been conducted by regulator/s), may note the implications of this decision in considering whether the circumstances point towards the existence of a provable claim.

*Doonin* shows how obligations to comply with notices, that a company has not honoured by the time of its insolvency, may be treated as liquidation expenses. Although the judgment makes clear that the question of designating the claim as a liquidation expense should have been uppermost among the issues, the sequencing of the issues raised in argument made it possible for the court to signal the barriers to establishing a contingent debt, i.e. the failure of parts (b) and (c) of the *Re Nortel* test. The part (b) barrier was factual – resource constraints on the regulator's own ability to perform the remedial work and seek reimbursement from the company; whereas the part (c) barrier was interpretational – unsecured creditor status was inconsistent with the EPA 1990 liability regime because the legislature must have intended liquidation expense status. Notwithstanding Lord Doherty's indication in this case that the courts would rarely refuse to confer liquidators' remuneration priority over liquidation expenses, insolvency practitioners find themselves on uncomfortable ground in that until clear guidance emerges regarding the type of situation in which their s.156

applications could be refused, the boundaries of the courts' willingness to favour such applications will be tested over time.

It may be noted that the parallel themes in *Dawson* and *Doonin* – whether unenforced obligations constitute contingent claims in insolvency, and the effects of a regulator's inability to undertake the remediation – echo questions considered in recent environmental insolvency decisions of Canadian appellate courts. These judgments have applied a three-pronged test aimed at determining whether a regulatory obligation amounts to a provable claim;<sup>30</sup> the third prong of which captures the *Dawson* and *Doonin* themes. This third component considers whether a monetary value can be attached to environmental obligations that are not expressed in monetary terms, such as clean-up requirements.<sup>31</sup> The general principle that a contingent claim will be included in the insolvency proceedings if it is not 'too remote or speculative' is accordingly applied to this environmental context to establish if it is sufficiently certain that the contingency will materialise, i.e. that the regulator will perform the remediation and seek reimbursement.<sup>32</sup> Thus, the approaches in *Dawson* and *Doonin* can be aligned with the principles in these high-profile judgments, a factor which may increase their value as persuasive authorities for English courts.

### **E. Broader lessons from these developments**

Read in light of established authorities relating to the tension between environmental protection and insolvency law, the recent judgments also touch on points of wider interest. Two decades on from the decision in *Re Celtic Extraction*, the conjunction of *Scottish Coal* and these 2018 decisions raise questions as to whether *Celtic Extraction's* significance has diminished.

Firstly, it is notable that the courts in *Dawson* and *Doonin* drew clear lines of differentiation with *Celtic Extraction* on the facts, and based on developments in the law since 1999. In *Dawson*, the court distinguished the present circumstances from *Celtic Extraction* on the ground that the latter judgment was concerned with determining whether the costs of continued compliance ranked as an administrative expense. Therefore, it could not help determine whether the facts leading up to the administration established that the Environment Agency could claim as a creditor. The court in *Doonin* echoed the point previously made in *Scottish Coal*,<sup>33</sup> that European law on interpretation of Directives had been clarified since *Celtic Extraction*. Thus, the relevant provision of the Environment Protection Act 1990 ('EPA 1990') should be examined 'through the prism of the [Waste Framework]

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<sup>30</sup> *Newfoundland and Labrador v AbitibiBowater Inc* 2012 SCC 67; *Re Nortel Networks Corporation* 2013 ONCA 599; *Orphan Well Association v Grant Thornton Ltd* 2019 SCC 5.

<sup>31</sup> *Abitibi*, *ibid* [30]-[31].

<sup>32</sup> *Abitibi*, *ibid* [36]; *Nortel*, (n.30) [31]; *Orphan Well*, (n.30) [138]-[140].

<sup>33</sup> (n.3), [46].

directive' which it was enacted to implement, taking account of objectives including the polluter-pays principle.<sup>34</sup> This led to the conclusion that the legislature must reasonably have intended a liquidator's expenditure to comply with a notice should be a liquidation expense, even though the language of the 1990 Act provisions did not make this explicit.

Secondly, policy considerations may be seen as playing a more muted role in *Scottish Coal* and *Doonin*, compared with the *Mineral Resources* and *Celtic Extraction* decisions, which were based 'partly on the grounds of policy and partly on the grounds of statutory construction'.<sup>35</sup> In *Doonin*, Lord Doherty managed to sidestep the policy arguments surrounding the relative weight attached to 'protection of the environment on one hand and the expeditious and equal distribution of available assets on the other',<sup>36</sup> focusing instead on interpreting the EPA 1990 in line with the purpose of the Waste Framework Directive. He emphasised however that he was not casting doubt on the judiciary's competence to evaluate these issues, and that persuasive arguments in favour of maximising environmental protection could well have carried the day if it had been necessary to rely on them. Similarly, *Scottish Coal* interpreted the Water Environment (Controlled Activities) Regulations 2005 in accordance with the Water Framework Directive to determine whether liquidators could disclaim statutory licences even though they lacked any express power to do so.<sup>37</sup> The 'persuasive factors in favour of giving pre-eminence to the policy of maximising environmental protection'<sup>38</sup> were treated as supplementary justification for this reasoning.

The courts therefore appear to be gravitating towards a position whereby the statutory interpretation angle in cases of this nature will tend to overshadow policy reasoning in favour of environmental protection or creditor interests. This impression is reinforced by the *Scottish Coal* and *Doonin* courts' rejection of the view expressed in *Celtic Extraction*, that enforcing 'polluter pays' in insolvency would infringe the insolvency distribution scheme by diverting funds which would otherwise be payable to the polluter's unsecured creditors. Instead, *Scottish Coal* and *Doonin* carefully affirm that applying assets towards the fulfilment of environmental obligations does not violate the statutory distribution scheme or the *pari passu* principle.<sup>39</sup> It is therefore conceivable that where possible, future cases will minimise the portrayal of a 'clash of interests'<sup>40</sup> or 'black and white contest'<sup>41</sup> between environmental and insolvency law associated with cases such as *Mineral Resources* and *Celtic Extraction*. This development would help to cool the debates regarding whether the courts should play a role

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<sup>34</sup> (n.2) [65].

<sup>35</sup> *Re Wilmott Trading Ltd* [1999] 2 BCLC 541, 544; *Re Mineral Resources* (n.3) 757-761; *Re Celtic Extraction* (n.3) [39]-[42].

<sup>36</sup> *Ibid*, [66].

<sup>37</sup> (n.4), [143].

<sup>38</sup> *Ibid*, [144].

<sup>39</sup> *Scottish Coal* (n.3), [52]; *Scottish Coal* (n.4), [145]; *Doonin* (n.2), [67].

<sup>40</sup> A. Keay and P. de Prez, 'Insolvency and Environmental Principles: A Case Study in a Conflict of Public Interests' (2001) 3 *Environmental Law Review* 90, 110.

<sup>41</sup> J. Armour, 'Who pays when polluters go bust?' 2000 *Law Quarterly Review* 200, 203.

in resolving ‘complex policy issues’<sup>42</sup> of this nature,<sup>43</sup> although the court in *Doonin* openly rebuffed the idea that courts in previous cases had overstepped the limits of their authority and strayed into legislative territory.<sup>44</sup> If the courts’ receptiveness to liquidators’ applications under s.156 Insolvency Act 1986 (indicated in *Doonin*) is added to this picture, it is not hard to infer that the judiciary are firmly asserting their role in this arena.

However, this enhanced air of authority is somewhat weakened by the courts’ use of the same premise to support their reasoning in the policy-driven judgments as well as the judgments more strongly grounded on statutory interpretation. This premise can be traced to the disclaimer cases *Mineral Resources* and *Wilmott Trading*, where Neuberger J saw the danger of solvent companies resorting to voluntary liquidation to relinquish burdensome obligations as a factor supporting the conclusion that a waste management licence was not capable of being disclaimed.<sup>45</sup> In *Dawson*, the court turned to the idea that ‘Otherwise, a company could knowingly cause contamination...’ to support its conclusion that part (c) of the *Re Nortel* test for contingent debts had been fulfilled,<sup>46</sup> entitling the Environment Agency to prove a claim in the administration. In *Doonin*, the court discerned that ‘Otherwise, it is very likely that polluters who become insolvent would escape paying for the damage to the environment’, in interpreting the EPA 1990 to find that compliance with a notice must have been intended to constitute a liquidation expense.<sup>47</sup> In adverting to this danger time and again, the courts have succeeded in emphasising the value of their judgments as a safety net against companies’ deliberate evasion of environmental obligations through insolvency. On the other hand, the force and clarity of this rationale may be compromised if it becomes increasingly recurrent in environmental insolvency cases, notwithstanding the disparity between the issues involved.

#### **F. Could the impact of these developments be overstated?**

While *Dawson* and *Doonin* add impetus to expectations of English judges reviewing the standing of *Celtic Extraction*, it is arguable that quite apart from this duo, the permanence of this Court of Appeal authority was never guaranteed. It may be recalled that the *Scottish Coal* outcome created anticipation of a Supreme Court appeal which would have the effect of re-opening *Celtic Extraction*.<sup>48</sup> Furthermore, the appeal court decision in *Celtic Extraction* itself, stemmed from a contrasting judgment based on similar facts (*Re Mineral Resources*), and the

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<sup>42</sup> Armour, *ibid* 204.

<sup>43</sup> Keay and De Prez, (n.36) 111.

<sup>44</sup> *Doonin*, (n.2) [66].

<sup>45</sup> *Mineral Resources*, (n.3) 760-761; *Wilmott*, (n.3) 548, 554.

<sup>46</sup> (n.1), [78].

<sup>47</sup> (n.2), [65].

<sup>48</sup> P. Cranston, ‘The impudence of liquidators: the scope and limits of disclaimer’ (2014) 1 Corporate Rescue and Insolvency 3, 8.

policy reasoning in *Mineral Resources* was strongly endorsed at first instance in *Scottish Coal*<sup>49</sup> – underscoring *Celtic*'s vulnerability.

*Celtic Extraction* also appeared to lack finality in that it left an important question unresolved: whether the Environment Agency would be entitled to claim as an unsecured creditor if a licence was successfully terminated through disclaimer.<sup>50</sup> This gave rise to a conundrum whereby a regulator might be unable to prove any claim at all in an environmental liquidation. The complexity surrounding the question whether a regulator could claim for the costs connected with a company's post-liquidation failure to comply with its obligations was similarly acknowledged but left unsettled, in *Mineral Resources* and *Scottish Coal*.<sup>51</sup>

The reasoning in *Celtic Extraction*, that upholding the polluter-pays principle would infringe the *pari passu* principle or the insolvency distribution scheme, has been marked with scepticism since the time of the decision.<sup>52</sup> Furthermore, it was corroded by legislative requirements introduced soon after the decision, which precluded environmental regulators from issuing landfill permits unless they were satisfied that operators had made adequate financial provision for fulfilment of obligations under their permits, including closure and after-care of sites.<sup>53</sup> This dulled the prospects of future cases based on an identical conflict of environmental and insolvency law coming before English courts,<sup>54</sup> helping to free subsequent decisions from deferring to *Celtic Extraction*.

## G. Conclusions

The recent judgments present unusual and rather involved sets of issues, adding diversity to the case law in this subject area. Since the facts of *Dawson* and *Doonin* are quite distinct from each other, as are their outcomes regarding the status which they recognize for the environmental claims, it is difficult to draw firm conclusions about their impact on future cases. However, they may be credited with producing further movement on this front by demonstrating that statutory interpretation – rather than the policy reasoning admitted to have been strongly influential in *Mineral Resources*<sup>55</sup> – can bring about a more advantageous treatment of environmental obligations. At the same time, they have further curtailed *Celtic Extraction*'s relevance to Scots law, and reignited the possibility of its departure from the English legal landscape.

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<sup>49</sup> (n.3), [51]; Cranston, *ibid*.

<sup>50</sup> *Ibid*, [38]

<sup>51</sup> (n.3), 758-760; (n.4), [146].

<sup>52</sup> Keay and de Prez, (n.40) 103-105.

<sup>53</sup> Council Directive 1999/31/EC of 26 April 1999 on the landfill of waste, Article 8.

<sup>54</sup> B. Mamutse and V. Fogleman, 'Improving the Treatment of Environmental Claims in Insolvency' 2013 J.B.L. 486, 494.

<sup>55</sup> D. Neuberger, 'Company Law Reform: The Role of the Courts', Chapter 3 in J. de Lacy (ed), *The Reform of United Kingdom Company Law* (Cavendish, 2002), 76.