(THIRD DRAFT)

(14)

CHAPTER 15

INSOLVENCY COURTS

Introduction

1 The judicial administration of insolvency matters in England and Wales is long overdue for drastic rationalisation and simplification. The striking feature of the present system is the diversity of the tribunals by which such matters are heard and determined. This unsatisfactory situation is the result of a long series of historical accidents by which the essential homogeneous nature of insolvency procedures has gradually become totally obscured and unrecognisable.

2 We believe that a good modern insolvency law requires the restoration of this principle primarily to ensure that in the whole field of insolvency matters justice is done to all the multifarious parties and interests with which it is from time to time concerned. We are also incidentally satisfied that a more uniform approach to the subject will lead to a more economic use of the manpower available for decision-making in this field.

The Principles of Insolvency Jurisdiction

3 The judicial administration of the insolvency jurisdiction, originally confined to bankruptcy matters, has always been conducted by and within a unique system; this uniqueness corresponds to and reflects the special characteristics and needs of the social and commercial problems which the existence of an insolvency will necessarily create. As we have sought to emphasise in earlier Chapters of this Report, the fact and the consequences of insolvency, its effect upon the status of the insolvent, the administration of his, or its,

assets, and the adjudication upon the mutual rights of have always tended to give rise to situations of difficu complexity.

4 The Court which administers an insolvency case must exercise a jurisdiction of a substantially universal application, and yet it must satisfy the criterion of being, so far as possible, a "neighbourhood court" relative to the geographical location of the insolvent and his creditors. To this end it needs to be locally based, yet must, so far as practicable, be unfettered by pecuniary limits upon its jurisdiction.

5 That court must also be clothed with a very wide judicial discretion. The exercise of its jurisdiction must almost invariably be concerned with business matters and frequently with the analysis of business accounts, culminating in the making, by the court itself, of decisions or judgments of an essentially business character. Its philosophical orientation in this respect is akin to that of the Commercial Court of the Queen's Bench Division. It is interesting to recall that until 1921, bankruptcy jurisdiction was entrusted in the High Court to the King's Bench Division from which it was then transferred to the Chancery Division.

6 The jurisdiction, as originally exercised in bankruptcy, and in more recent times in winding up also, exhibits three specific and important characteristics~~which are peculiar to itself:~~

(a) The Court possesses the power to compel insolvents or, where corporate, their officers, and other relevant witnesses to submit to a detailed and not infrequently intensive examination, the answers to which

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Rider to Page10, Para. 23.

(b) High Court in London.

23. The High Court has a special "Companies" section, which forms part of the Chancery Division, amd somewhat resembles that special section already referred to in para. 19 as dealing with bankruptcy matters. Although this section is called "the Companies Court", it is not s court separate and distinct from the High Court; it has been described as "a way of describing the High Court when dealing with matters originating in the chambers of the Bankruptcy Registrar dealing with company matters, and "the Companies Judge" is a way of describing a High Court judge when trying such matters.

24. The Companies Court, and the Companies Court Judge, when the terms are used in thèses senses, exercise several distinct jurisdictions, the existence of which are relevant to our proposals for the unification and the harmonisation of the bankruptcy, winding up and analogous procedures, so as to produce so far as practicable one code and one court administer it, and one category of judicial person to presi over it.

25. There are three distinct aspects of jurisdiction affecting companies, which are exercised through the Companies Court by the Companies Judge. The first of th is the winding up jurisdiction relating to insolvent companies, amd conferred by certain parts of the Companies Acts (and connected Acts, such as those dealing with insurance companies; interwoven with this is a jurisdicti to deal with certain aspects of the affairs of solvent companies, in principle arising from disputes betwe n the

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CHAPTER 15

INSOLVENCY PRACTITIONERS Qualifications Dent m

Introduction

732. In earlier chapters we have put forward detailed proposals for a comprehensive and integrated insolvency system for all classes of debtor; ~~a~~ this system ~~which~~ is designed to deal with the problems of the eighties and, in particular, to enable businesses in trouble to be rescued more easily. The success of any insolvency system is very largely dependent upon those who administer it. If they do not have the confidence and respect, not only of the courts, and of creditors and debtors, but also of the public generally, then complaints will multiply and, if remedial action is not taken, the system will fall into disrepute and disuse. The history of insolvency law is replete with periods when there has been public dissatisfaction with its administration, [not only in this country (for which, see Chapter 2) but also in other countries.] DM PA

RP [We have referred to dissatisfaction in Ch.] Public Concern.

733. We discussed the role of the Official Receiver in the previous Chapter. preceding ? We are satisfied that the training given to Examiners in the Insolvency Service and the experience gained by them is such as to enable them in due course to become Official Receivers in whom the public can have every confidence. We have been particularly impressed by those who attended before us to give oral evidence and by those whom most of us have seen carrying out their duties in the Courts.

? not required purpose

734. In this Chapter we are concerned with the qualifications, powers and duties of private practitioners who act as liquidators, trustees, receivers and administrators in insolvency matters; for simplicity we refer to them collectively as insolvency practitioners. We do not intend to refer to legal practitioners as such, although it is not unknown for solicitors to act as receivers, and solicitors were at one time occasionally appointed in the provinces as "unofficial" Official Receivers.

* always accountants

735. From the evidence submitted to us and from our own experience, we are satisfied that the majority of insolvency practitioners carry out their duties in a manner which gives no cause for ~~complaint~~ comment. However, we have received a number of representations, usually relating to isolated cases, which indicate that the manner in which some insolvent estates are administered does give cause for concern. A number of matters have been brought to our attention as being in need of change. One area which has been criticised is the law - or lack of it - relating to the qualifying requirements ~~of~~ for insolvency practitioners. We have received a number of suggestions whereby the law might be strengthened, so as to ensure that insolvent estates are administered only by competent practitioners. It is perhaps of significance that many of these proposals have been put forward by insolvency practitioners themselves.

(1) QUALIFYING REQUIREMENTS

General

736. When one considers the many and varied matters with which the insolvency practitioner must be familiar, it is clear that certain qualifications, knowledge and experience are essential for many tasks. For example, he must be familiar with the law regulating the relations of debtor and creditor, and the acts and defaults of a debtor; the organisation of courts dealing with insolvency matters and the proceedings in connection therewith; the investigation of the business dealings and transactions of an insolvent debtor; the pursuit and recovery of assets fraudulently disposed of in order to defeat creditors; the rescission of voluntary conveyances and other transactions amounting to voidable preferences; and the rules relating to the distribution of the insolvent debtor's assets among his creditors. It is perhaps surprising ~~astonishing~~ alarming that apart from ~~two or three~~ a few notable exceptions, which are referred to below, almost anyone may act as an

GW Insert "skills"

insolvency practitioner.

737. Any fit person can be appointed to act as a receiver or manager, or a liquidator in a compulsory winding up, or a trustee in bankruptcy. A body corporate is not qualified to act, and an undischarged bankrupt is also barred, save that he may act as a receiver or manager with the approval of the Court. Apart from these, there are no other statutory restrictions. In the case of a trustee in bankruptcy, section 19(1) of the Act of 1914 specifically provides that he may be a creditor of the bankrupt. In the case of a voluntary winding up, whether "members" or "creditors", the only restriction is that relating to a body corporate.

738. We understand that the practice of the Companies Court, when considering the appointment of a liquidator in a compulsory winding up, is to appoint an accountant of at least five years' standing, although exceptions have been made in suitable cases.

739. We have been told that many trustees in bankruptcy, although professional accountants, are inexperienced in insolvency matters and require constant guidance from the Department of Trade, leading to delays and additional costs to the Insolvency Service.

740. Officials of the Department of Trade have drawn our attention to cases where clearly certain persons should not have been allowed to act as receivers and managers of companies, such as the directors of "one-man companies". We have already referred to similar criticism at paragraph 439. As one official put it to us, "He knew of cases where they are wearing so many hats that they are not quite sure what they are doing."

741. The Blagden Committee recommended that the trustee in bankruptcy should have some professional qualification, especially as an accountant. They also recommended that a creditor should be excluded from acting on the ground of possible lack of impartiality.

742. The Jenkins Committee recommended:

(a) that section 367 of the Act of 1948 should be amended to disqualify, without exception, undischarged bankrupts from acting as receivers or managers, and that a similar disqualification should extend to acting as liquidator of a company; and

(b) that section 188 of that Act should be extended to empower the Court to disqualify persons from acting as receivers, managers or liquidators for the same reasons and in the same manner as it may disqualify persons from acting as company directors.

743. A variety of qualifying requirements have been put to us for consideration; they include the following alternatives (?)

(a) appointments should be limited to members of recognised professional bodies;

(b) appointments should be limited to members of recognised accountancy bodies;

(c) insolvency practitioners should be professionally qualified and officially approved;

(d) they should be registered and licensed by the Secretary of State for Trade;

(e) they should be members of a licensed professional body of insolvency practitioners (that is, a

separate, specialised profession);

(f) appointments should be limited to persons having at least five years' experience in insolvency practice with a reputable firm; and

(g) the appointment of a receiver or manager should be restricted to those who are eligible for appointment as auditor.

The case against change

744. Officials of the Department of Trade have described to us the difficulties which arose when it was decided to write down qualifications for company secretaries in the Companies Acts. Having produced a short list of suitable bodies, the Department was inundated with claims from other organisations that they should be added to the list. Difficulties also arose regarding people left out who had been doing the job previously. In the event, there is a short list in the statute (section 79, Companies Act 1980) followed by a further subsection saying that the directors could in fact appoint anybody else if they were satisfied that the person was suitably qualified. The proviso would appear to have the effect of making the whole provision pretty meaningless.

745. We were also told of the problems arising where the Department has a discretionary role, such as was originally the method for approving individuals to be eligible to act as auditors of companies. The work is extremely labour intensive and invariably gives rise to complaints of unfair treatment, Before 1976 the Secretary of State could authorise a person to act as an auditor on the ground that he had obtained adequate knowledge and experience in the course of his employment by a member of an authorised accountancy body. This provision was repealed because it was widely felt that authorisations

ought to be on the basis of relevant professional training and examinations, and because the process of individual authorisation involved a considerable degree of subjective judgment and an unjustifiable amount of the Department's time. [We were left in no doubt that the Department would need a great deal of persuading that it was right to take on any further ~~job~~ duty of that sort.] PA Co 747 PA

GW 745A re certificate fee - automatic unless previously renewed.

[746. Section 161 of the Act of 1948 and section 13 of the Act of 1976 provide that the auditor of a company - public or private - must either:

(a) be a member of one of four specified accounting bodies (although the Secretary of State can add to or subtract from the list); or

(b) be individually authorised by the Secretary of State as having a foreign qualification equivalent to those ~~of~~ the recognised bodies.]

PA delete, matter to end of 746. ? confirmed by

747. The Department continue[s] to be involved in appraising the qualifications of British bodies which seek recognition. It is necessary in each case to try to judge the standing of the applicant and its membership by studying for example its curriculum, teaching arrangements, examinations, ethical standards and disciplinary procedures, in order to assess their relationship with those of the bodies already recognised. There are numerous accounting bodies in Britain, and there is nothing to stop appeals against rejection of recognition. The Department also has to assess the eligibility of individuals who claim to have equivalent foreign qualifications. presumably body comparability PA for 745

748. Considerations against introducing statutory qualifications would seem to include:

(a) given the wide variety of companies, it may be difficult to specify a single set of qualifications appropriate to all of them;

(b) from the numerous arguably relevant professional qualifications, it is likely to be difficult to distinguish between the suitable and the unsuitable;

(c) it is questionable whether the Department could carry out the task at (b) even if staff could be made available; and

(d) similar difficulties would arise over the assessment of the qualification of individuals.

749. It might be argued that to impose restrictions on the category of those eligible to act as insolvency practitioners would simply create a new restrictive trade practice, by limiting to a certain class of persons the right to administer insolvent estates, and that it would be reducing creditors' rights of choice without the prospect of a material benefit in checking abuse. There is also the risk that such a step would create a new bureaucracy of those required to administer the system.

Our conclusion

750. In our view, some form of control is necessary. It is essential that measures are introduced to ensure a high standard of competence as well as integrity in the persons who are eligible for appointment as insolvency practitioners. The existing system is too open to abuse to command public confidence. We do not regard arguments against control as compelling, as we think that it should be possible to establish a measure of control which would not be difficult or expensive to administer.

The position in other countries

751. The pattern throughout Europe is similar to that used in France, where the Court appoints the equivalent of a trustee or liquidator from a cadre of professional "syndics de faillite", a list of whom is maintained by the Court, and whose names appear on the list as a result of examination and experience. Members of the cadre are excluded from certain commercial activities.

752. Under the Canadian Bankruptcy Act, which applies to both individuals and companies, there is a licensing system for trustees in bankruptcy. Licences are granted by a Board, which conducts an oral examination concerned largely with practical insolvency problems. Boards are composed of four members: a representative of the Federal Superintendent of Bankruptcy, a representative of the Provincial Superintendent of Bankruptcy, and two lawyers specialising in insolvency law. Conflicts of interest are avoided by excluding chartered accountants from Boards. Boards have powers to revoke licences and exercise a general disciplinary jurisdiction over licensees. We understand that the applicant for a licence must demonstrate a thorough knowledge of bankruptcy law and its application and have substantial business experience, as well as satisfactory financial and other resources available in order to administer insolvent estates. In almost every instance a licensed Trustee in Bankruptcy is a chartered accountant or a limited company associated with a firm of chartered accountants.

753. A form of registration, similar to that used in Canada, is in operation in Australia and in Singapore. However, in almost every bankruptcy in Australia, the Official Receiver carries out the duties of trustee. For example, in the year ended 30 June 1979, there was a total of 3857 new bankruptcies of which 3846 estates were administered

by the Official Receiver, and 11 estates were administered by registered trustees.

754. The position in New Zealand is similar to the present position in this country; that is, bodies corporate and undischarged bankrupts are not qualified for appointment, with the proviso that an undischarged bankrupt may act under an appointment made by Order of the Court.

USA ? new Zlr

Form of control

755. There are three possible ways of restricting by statute who may act as an insolvency practitioner:

(a) by prescribing minimum qualifications for those eligible to be appointed; & prescribed books,

(b) by disqualifying certain classes of persons from appointment;

(c) by a combination of (a) and (b).

(d) giving the Dept & the power to supervise

Our proposals

756. We recommend that the system for controlling the eligibility of insolvency practitioners should combine disqualifications of certain classes of persons with a requirement of certain minimum qualifications.

757. We do not support the introduction of a licensing system on the Canadian pattern, which we regard as both unsuitable and unnecessary for use in this country. We support the Department's view that the setting up and running of examining boards would be too complex and expensive to justify the probable benefits.

Qualifications

758. We recommend that an insolvency practitioner shall, unless

falling within the transitional provisions set out below, be a member of a professional body approved by the Department of Trade. To qualify for possible inclusion in the list of acceptable professional bodies, the following conditions must be met:

(a) the body must have a written constitution which includes a satisfactory code of ethics covering both the general aspects of the profession and the specific aspect of insolvency;

(b) the members must be subject to an effective disciplinary authority body with adequate powers to deprive defaulting members of their right to practice;

(c) members who are in practice must be required to hold a current ~~practising~~ membership certificate authorising him to practise renewable annually, and to comply with that part of the code of ethics which deals with accounting before their practising certificate is renewed; and

(d) entry into the profession must be by competitive examination which includes a paper on "Insolvency".

Experience

759. In addition to being a member of an approved professional body, a person must have been in general practice for five years prior to beginning to act as an insolvency practitioner.

Examination

760. We are divided on the precise requirement for a paper on "Insolvency" in the relevant professional examinations. The majority of us consider that there should at least be an optional paper on "Insolvency". ~~and that an insolvency practitioner should have taken and passed this paper.~~

Transitional provisions

761. To cover those people who for many years have acted competently as liquidators and trustees we recommend that the Department of Trade should be authorised to approve individuals, whether qualified in any profession or not, if they have for the previous five years competently undertaken the duties of liquidator or trustee in respect of not less than an average of five administrations a year. We regard this as a duty which properly falls to be done by the Department, who are - or should be - the recipients of all complaints against insolvency practitioners.

Compulsory bonding and indemnity insurance

762. At present, a liquidator in a compulsory winding up or a trustee in bankruptcy is not capable of acting until he has given security in the prescribed manner to the satisfaction of the Department of Trade. This is not a requirement in the case of appointments which are not subject to the jurisdiction of the Court. We recommend that the distinction should be abolished and that the appointment of all insolvency practitioners should require to be covered by insurance against all types of fraud, dishonesty and professional negligence. cf Ch. 16/§23

763. Under existing rules security may be given in each separate winding up or bankruptcy administration, or may be generally available for any administration in which the person giving security may be appointed. We understand that the Department has declined to make use of the power to take general rather than specific security.

764. We consider that there should be no delay in the ability to accept and act on any insolvency appointment by reason of a need to obtain people's cover or to agree the amount thereof with any controlling

authority, whether the Court or the Department. We can see no objection to global security covering all appointments taken by a practitioner, renewable annually, provided the amount of the cover is adequate. We have had discussions with members of the insurance profession and we believe that the insurance market will be able to write an appropriate policy. a global insurance limit?

765. We accordingly recommend that global security, as outlined above, should be a qualifying requirement for all insolvency practitioners. The insurer should be required to issue a certificate on a basis and wording to be agreed with the Department, and subsequently, to inform the Department if he is not willing to renew cover, or if any premium has not been paid.

766. Since the need to obtain cover will no longer be related to a particular appointment, the question of charging the premium to the estate will no longer arise and it will be part of the practitioner's overhead expenses.

Disqualification

767. We recommend that the following persons should be automatically disqualified from acting as insolvency practitioners:

(a) anyone in respect of whom an insolvency order is in existence;

(b) anyone who is prohibited from acting as a director of a limited company;

(c) a body corporate;

and that in any event such disqualifications should apply to specific cases, where the proposed appointee is

(d) an officer (including auditor) or former officer, or an employee or partner of an officer or former officer of the debtor company or its parent or associated company;

? JC

spouses & any person 12 related.

leave of court re auditor

(e) an employee or ex-employee of the debtor, or if it is a company, of its parent or associated companies; and

(f) a creditor, unless he undertakes not to claim in the insolvency.

(g) ~~withdrawn~~.

768. By "associated company" in the previous paragraph we include any company relationship which might be present, such as the subsidiaries and sub-subsidiaries within a group of companies.

Joint appointments

769. Cases have arisen where, because of the nature of the insolvent's business or property, it has been found desirable to appoint a particular specialist, usually as receiver or manager. We recommend that such an appointment should only be jointly with a qualified insolvency practitioner. The specialist concerned should, however, be subject to the restrictions set out in paragraph 767(a),(b), (c) and (f) above.

Discipline

770. We are mindful of the need to keep the involvement of the Department of Trade to a minimum in the control of insolvency practitioners. We recommend that it should be an offence to act as an insolvency practitioner if not qualified, punishable by a substantial fine per diem. Any interested party should be entitled to challenge the qualifications of the practitioner and to bring the matter to the attention of the Department [or the Court?].

771. The Department should have no specific obligation to supervise the work of insolvency practitioners, but it would be obliged to investigate any complaint.

772. We consider that the Department must have the right to withdraw its approval from any insolvency practitioner. We recommend that the grounds for withdrawal should include:

(a) failure to comply with any provision of the law relating to his duties;

(b) loss of his right to practice as a member of an approved body; or

(c) becoming subject to disqualification.

[What about appeal?]

Voluntary winding up

773. We have received numerous complaints concerning the administration of companies under what is at present termed a members' voluntary winding up. It would seem that abuses in this field are increasing and that all too frequently the company in question is not in fact solvent. We believe that much of the criticism of these administrations would be alleviated if voluntary liquidators were subjected to the same qualifying requirements and disqualifications as we have put forward for insolvency practitioners. An additional advantage of such a proposal is that if a company does have to transfer from a voluntary winding up to an insolvent administration, the voluntary liquidator will be qualified to continue to act, if the creditors so wish.

774. We therefore recommend that the qualifying requirements and disqualifications which we have put forward should not only apply to all types of insolvency practitioner, but should also apply to the liquidators in voluntary winding up proceedings.

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