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COMMENCEMENT OF BANKRUPTCY

PART I

1. Jurisdiction to make a debtor bankrupt is conferred on the Bankruptcy Court by notice of the debtor being proved to have committed one or more "acts of bankruptcy", as principally defined in s.1(1)(a) to (h) of the Bankruptcy Act 1914; other such acts are prescribed by other statutes for the purposes of "criminal bankruptcy" and under the administration order provisions.

2. Each of the acts of bankruptcy represents an overt act or omission by the debtor, or some event involving his affairs, which evidence or are deemed to evidence his being in a state of insolvency. The Commission of the act of bankruptcy must be strictly proved by the petitioning creditor, otherwise his petition will be dismissed. By far the most frequently used act of bankruptcy is the debtor's failure to comply with a bankruptcy notice; this can only be founded on a final judgment or order for the payment of a sum of money (now of not less than £200) whether sued for in contract or in tort or awarded in respect of costs. The bankruptcy notice provisions (ss. 1 (1)(g) and 2) originally allowed the debtor seven clear days after service upon him (almost invariably personal service) to pay or compound for his debt; this period has just been extended by s.5 of the Insolvency Act 1976 to ten days. The period is probably still too short, and if any new form of "salvage" procedure is to be introduced to save insolvent debtors from actual bankruptcy it will need to be still further extended; see ILRC20, paras. 16 to 23.

3. It is however not essential for the petitioning creditor to found his bankruptcy petition on a judgment or order; if he can prove that the debtor has committed some act of bankruptcy (other than non-compliance with a bankruptcy notice) he can found a petition on a non-judgment debt of at least £200 so long as it is liquidated (s.4) and not, or not substantially, disputed. Until the 1976 Act took effect, the minimum debt under either procedure was £50, now £200. The Court does not favour the use of bankruptcy petitions to litigate disputed debts; although it will entertain limited litigation as to the debt which has not terminated in a judgment or order, yet if the debt is bona fide disputed, either as to its subsistence or as to the debtor possessing a sufficient set-off, counterclaim or cross-demand, it will usually adjourn the petition until the dispute is disposed of in the ordinary courts, or may even dismiss the petition.

4. The debtor need not reserve his disputing of the debt to the hearing of the petition; he can object to the bankruptcy notice on the ground that he has such a set-off, counterclaim or cross-demand; and if he can within a very limited time show good grounds, the court will stay the operation of the notice until the dispute has been litigated.

5. A creditor's petition must be presented within three months from the date of the act of bankruptcy relied upon. It is in form an application to the court to administer, by means of the bankruptcy procedure, the assets of a debtor who is, or is deemed to be, insolvent; it is not intended as, but is widely used as, a method of debt-collecting. However, its "collective" character, as a process being presented in the interests of creditors generally, is emphasised by the court's general unwillingness to allow the petition debt to be paid off out of the debtor's own monies (as distinct from ostensible third party monies) or to allow the petition to be withdrawn or dismissed without the court's leave. Furthermore, if another creditor with a difficient debt can show that the petitioning creditor is not proceeding with due diligence, he can, but only within the three months following the act of Bankruptcy, apply to be "substituted" as petitioning creditor (s.111).

6. When the petition comes on for trial before the Registrar in chambers, it is supported and opposed by affidavit evidence filed by either party (infrequently by oral evidence) on which the parties may cross-examine the deponents. The whole proceedings take place in chambers, under conditions of confidentiality (see ILRC 20, para 10), and are generally marked by requirements of considerable strictness of proof of the matters required to be proved by the petitioning creditor, a rule historically justified on the ground that bankruptcy was a quasi-penal procedure. This ground is perhaps now of lesser validity.

7. No creditor other than the petitioning creditor should generally be present (but see ILRC 20 paras 14 and 17); the debtor's actual state of solvency or insolvency may be relevant and may be canvassed, but in general without any participation by other creditors as parties, only as affidavit witnesses on one side or the other. The debtor's actual state of solvency or insolvency may of course be proved by his having already executed a deed of arrangement or some other form of contractual composition (itself an act of bankruptcy), for which purpose he has circulated a statement of his assets and liabilities; or he may be ordered by the court to swear and file such a statement of affairs eg. as a ground for an adjournment of the petition.

8. If the Court is satisfied that the petitioning creditor has proved all the necessary elements in his case, it will either make a receiving order or afford the debtor a last opportunity of procuring the debt to be paid off out of third party monies. Logically, once the three months from any proved act of bankruptcy has expired, the Court would be entitled to allow the debtor to pay the debt out of his own monies, but the theory supporting the general refusal of the Courts to permit this is that by reason of the currency of the petition, other potential petitioning creditors may have refrained from commencing proceedings. This rule requires reconsideration.

9. If the court makes a receiving order, it must be advertised in the "London Gazette" and a local newspaper, so that all creditors of the debtor become aware of it; after the date of the order, everyone is deemed to have notice of it (s.~~147~~ 137) and therefore deals with the debtor at the risk of the transaction being set aside as invalid. Gazette entries and advertisements, however, take some time to appear, and there is therefore a period when this risk exists with no public means of acquiring knowledge of it. This creates an injustice of this to bankers and other persons who may be holding money or property of the debtor which they may deliver up to him or who may

otherwise deal with him. It was sought to remedy this by the obscure section 4 of the Bankruptcy (Amendment) Act 1926, which was intended to provide a restricted degree of protection in respect of transactions between the date of the receiving order and its gazetting, but this is inadequate and unsatisfactory (see Williams, notes to ss.45, 46 and s.4 of 1926, pp 403-5).

10. A more effective protection at least so far as concerns bankers and analogous persons may be provided by preliminary examination of the debtor by the Official Receiver, which takes place immediately after the receiving order; at this, the debtor is required to disclose inter alia all his bank accounts so that the Official Receiver can give sheet notice to the bankers. But this protection is only effective if the debtor attends on the Official Receiver (he may even not attend on the making of the receiving order), and if he makes a true and full disclosure.

11. The debtor may apply for, and be granted, a stay of advertisement pending appeal; despite the potentially serious consequences to third parties described above, and frequent judicial warnings, such stays of advertisement are frequently granted and are continued sometimes for very long periods. It is not known to what extent such stays of advertisements in fact expose persons to subsequent claims by the trustee in bankruptcy, who successfully sue to set their transactions with the bankrupt aside.

12. No leave is needed to appeal against a receiving order, and although the appeal is graded, for the purpose of fixing hearing dates, as an "interlocutory appeal" (and therefore expedited), bankruptcy appeals frequently take too long to come on, probably longer in the case of appeal from county courts to the Chancery Divisional Court of two judges (who unlike the Court of Appeal do not sit together continuously). Due to these delays, bankruptcy administrations may be seriously and excessively delayed.

13. In addition to a stay of advertisement, the debtor may apply for, but is more rarely granted, a complete or partial stay of proceedings in the bankruptcy (s.113). Such a stay suspends the duty to file a statement of affairs, but does not differ greatly from a stay of advertisement; for during the latter stay, the Official Receiver cannot convene a meeting of creditors. In the absence of any stay, the Court may proceed with the bankruptcy notwithstanding a pending appeal against the judgment on which the debt is founded; but this is generally discouraged, if the appeal is reasonably close to hearing; the same view applies, more strongly, to the appeal against the receiving order.

14. In the absence of an appeal, or any stay, the Official Receiver will through the Department of Trade gazette and advertise the receiving order, and will also give notice directly to all the debtor's creditors and debtors of whose existence and whereabouts he is aware, and will convene a first meeting of creditors at which he presides (Sched. I). This meeting must decide by a vote whether the debtor should be adjudicated bankrupt and if so, who should be the trustee

in bankruptcy and whether a composition should be envisaged.

There is however an anomaly here, for even if they do not vote for an adjudication, the Official Receiver still has a discretion to apply to the court to adjudicate the debtor bankrupt. This he does by an application in chambers; other persons can however apply if he does not. The debtor must be given notice, but need not attend. He can, however, oppose the adjudication, on grounds either that he is appealing against the receiving order, or against the judgment debt on which the petition is based, or that he can pay his debts in full, or that he desires to propose a composition under the Act (s.16)

15. If the court finds sufficient ground for an adjudication, it will make an order (which is also gazetted and advertised), which has the effect of divesting the debtor of his property (ss. 18 and 53) and vesting it in either the trustee already nominated by the creditors, or in the Official Receiver ex-officio. Only then does the debtor become "a bankrupt" and suffer the civil and criminal consequences of that status.

(Part II, to follow, will deal with public and private examinations and bankruptcy administration. Part III will deal with discharges).

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