

4

THE IMPACT OF THE DRAFT E.E.C. BANKRUPTCY  
CONVENTION ON DEEDS OF ARRANGEMENT

N O T E

This Note relates only to the English law.

Deeds of Arrangement are in essence a contract made between a debtor and his creditors, usually with the addition of a trustee or trustees who are to administer the deed. There are a number of forms of arrangement, some of which are described in Section 1 of the Deeds of Arrangement Act, 1914; the "hammering" of a stockbroker brings into existence a Deed of Arrangement pursuant to the Stock Exchange Rules.

The English law controls or affects Deeds of Arrangement in various ways, both under the Bankruptcy Act, 1914, and the Deeds of Arrangement Act, 1914. For example, a deed whereby a debtor conveys or assigns all his property to a trustee for the benefit of creditors generally is an act of bankruptcy, as is also a deed assigning part of the debtor's property with intention to defeat or delay his creditors or some of them. (See B.A. Section 1(1)(a) and (b)).

A general assignment by a debtor subsequently adjudged bankrupt of his present or future book debts, or a class thereof, may become partially or wholly void unless registered as a conditional Bill of Sale (B.A. Section 45).

A Deed of Arrangement of one of the species specified in the D. of A.A., which is made by (a) by or on

behalf of a debtor for the benefit of his creditors generally, or (b) by or on behalf of an insolvent debtor for the benefit of any three or more of his creditors, is void unless duly registered by the trustee ( D. of A.A. Secs. 1 and 2).

Deeds which are expressed to be or are in fact made for the benefit of a debtor's creditors generally are void unless duly assented to by a majority in number and value of the creditors (this means the actual creditors, not merely those disclosed by the debtor) (D. of A.A., Sec.3).

A Deed which constitutes an act of bankruptcy (vide supra) may be relied upon to found a bankruptcy petition if it is presented within 3 months of the Deed, and the Deed will become void in any bankruptcy arising on such a petition or on any petition presented within that 3 months. This period of risk may be reduced to one month by a notice given by the Deed Trustee to the creditors (D. of A.A., Sec.24).

Deed trustees are guilty of an offence if they pay deed creditors other than rateably, unless they are by law preferential (ibid, Sec.17). Issues arising in the administration of a deed which is expressed to be or which is in fact made for the benefit of the debtor's creditors generally are adjudicated upon in the Bankruptcy Court (D. of A.A., Sec.23).

If a deed of arrangement/<sup>survives</sup>~~provides~~ the foregoing hazards or risks of invalidity, it becomes fully effective

as an absolute assignment of the property comprised therein, upon the trusts therein declared, and cannot thereafter be challenged, and those trusts will be enforced by the Court.

The consideration for the deed is constituted by the debtor's assignment of his property, the trustee's covenants to administer, the creditors' release (either absolute or, usually, conditional) of the debtor from his debt, and the ~~debtor's~~<sup>creditors'</sup> mutual agreement inter se.

The Deeds of Arrangement Legislation does not apply at all to limited companies whose modes of composition are regulated explicitly by the Companies Act, 1948.

The question then arises whether a Deed of Arrangement which becomes valid and unimpeachable under the present English law can be impeached under any provision of the Uniform Law (A~~nd~~ 1.) if it becomes incorporated in English law. The only Article which seems to be relevant is Article 4, which specifies the transactions which are invalid against the bankrupt's creditors within various suspect periods.

My opinion, prima facie, is that since a Deed of Arrangement is a transaction effected for valuable consideration between all the parties thereto, and as respects the first category those parties include an assenting majority of the creditors of the debtor, it should not be impeachable at all, and could not be under Article 4(A)(1) or (2).

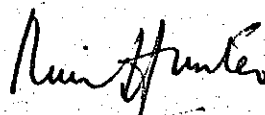
I am not so sure about (B)(1)(b) insofar as the

payment of the debts is not to be made "in any of the forms there provided for, otherwise than as a payment by way of composition". I also have some doubt about the effect of (B)(2) as to whether such a deed could be described as "a charge created by contract", but I do not think this can be intended to apply to a collective "charge".

Greater difficulties arise with (C)(1), where transactions even for valuable consideration may be declared invalid if they have occasioned detriment to the bankruptcy creditors and if the persons receiving payment knew of the suspension of payments. This might provide a remedy for a dissenting <sup>or non-assenting</sup> creditor under a deed who had failed to exercise his rights under the Bankruptcy Act within either 3 months or one month (vide supra); the question also here turns on what is to be the meaning or equivalent in English law of the expression "the suspension of payments" (as presently translated, but the new translation will presumably use "cessation of payments"). Plainly, the summons to a meeting at which the creditors are to be asked to accept a deed constitutes a suspension of payment, both generally and in the context of English law (see B.A. 1(1)(h)).

Having regard to these areas of uncertainty, I advise that we should consider a specific exception, (comparable to the one in Article 4(A)(1)) which protects a Deed of Arrangement which has become valid under the general English law.

I have reason to think that similar out-of-court arrangements or compositions are known within the Common Market State; there is certainly in Italy a similar deed called "Privata Scrittura", and there would therefore be other forms of such composition instruments which would need, and could be covered by, the same protection.



Muir Hunter

5th November, 1973.



E.E.C. DRAFT BANKRUPTCY CONVENTION

DEEDS OF ARRANGEMENT

FURTHER NOTE

1. A deed of arrangement in English law is a contract between a debtor (an individual or partnership, not a company) and his or their creditors.

It is also a juridical act or event, in respect of :

- (a) the declaration of insolvency constituted by the summoning of the meeting of creditors and/or by declarations made thereat by or on behalf of the debtor;
- (b) the assignment by the execution of a deed of all, or a class, of the debtor's property;

2. Events (a) and (b) above are already acts of bankruptcy under English law and, we believe, acts evidencing practical insolvency under Scottish law; event (a) will also constitute under the Convention evidence of a cessation of payments by the debtor of which all creditors will have received notice.

Event (b) will under the Convention confirm the cessation of payments (if still in doubt).

3. Will event (b) constitute a void or voidable act under Article 4 of the Uniform Law, in the event of bankruptcy supervening thereafter?

4. Under Paragraph B (1)(a), does the term "payments of debts which had not fallen due when the bankruptcy was opened" cover payments made by a deed trustee? We think not.

5. Under Paragraph B(1)(b), are payments by the deed trustee

capable of being held to be "unusual", and are therefore capable of being avoided? We think not.

6. Under Paragraph B(1)(c), the performance of a contractual obligation by payment of a composition by a deed trustee might be held to be an unusual manner of performance and therefore void: certainly, if (hypothetically) payment was in specie.

7. Under Paragraph (C)(1), payments made by the debtor of debts which have become due and acts "for valuable consideration" done by the debtor are voidable as against the general body of creditors, (i) if they have prejudiced the general body of creditors, and (ii) if the other party knew of the cessation of payments.

8. Do the distributions made by the trustee under a deed constitute "payments"? Probably not; compare note on paragraph B(1)(a) above.

9. Does the execution of a deed constitute a "prejudice" to the general body of creditors? The answer to this question depends upon whether the general body of creditors have ~~consented~~ assented to the execution of the deed, and have assented to it after it has been executed. If they have done, then there is no longer any "general body of creditors" capable of being prejudiced thereby.

10. But the last proposition is dependent on the deed being for the benefit of the debtor's creditors generally: see Deeds of Arrangement Act, 1914, s.1 (1)(a). In the case of a deed made for the benefit of a group smaller than the general body of creditors (see ibid s.1(1)(b) (three or more creditors)), there might be a case for proving prejudice to the others, and hence a case for the avoidance of such a deed; see e.g. the standard deed required to be executed by insolvent stock-brokers under the Stock Exchange Rules,



and comparable deeds used by other trade associations.

11. Could a deed of arrangement be set aside by means of a "Paulian action"? If that action is correctly defined in C.P. 7.18/38/39, a deed of arrangement would not seem to be an act or transaction capable of being invalidated thereunder, at least in the case of a deed for the benefit of creditors generally.

12. The formal validity of an English deed under the present English statute (Deeds of Arrangement Act, 1914) would presumably still depend upon its registration (s.2) and the receipt of a majority of assents (s.3). But its invalidation under the bankruptcy law, despite its formal validity, would depend on the form of that law, and the continued subsistence, or the replacement, of the "act of bankruptcy" constituted under the Bankruptcy Act, 1914, s.1(1)(a).

13. If a petition (in England) were to be capable of presentation solely by virtue of proof of a cessation of payments (e.g. under the definition proposed in C.P. 7.21/22), then the deed could be invalidated thereby (see para. 2 above).

*presented at 20<sup>th</sup> Meeting.*

16 May, 1975.