1(52)

44th Mtg
16.7.80

INSOLVENCY LAW REVIEW

Minutes of the Fortyfourth Meeting of the Review Committee on 16 July 1980

Present:	P J Millett	(in the chair)
	J S Copp	
	G Drain	
	AIF Goldman	
	J M Hunter	
	D McNab	
	T R Penny	
	C A Taylor	
	T H Traylor	(Secretary)
	E L Reeves	(Assistant Secretary)
In attendance:	J R Endersby	
	D Graham	
	G A Weiss	

1 The Committee met at 10.00 am. In para 9 of the minutes of the fortythird meeting held on 25 June lines 2 and 3 were amended to read "....the powers of the Court when setting aside voidable transactions should be set out, referring.....", and "excuse" in para 34 should have read "exercise". The minutes as amended were agreed and signed.

MATTERS ARISING

2 With regard to para 9 of the minutes of the fortythird meeting, Mr Millett pointed out that the intention had been to include a discretionary power not to set a transaction aside. Mr John Hunter said that this had been covered by para 10.

3 Mr Taylor, referring to para 42, thought that trading with insufficient assets would be a matter of opinion and hard to prove. The Secretary said that on reflection the matter was already covered by the proposed provisions and insufficiency of assets would be no more than an example. Mr Millett (in the chair) agreed.

ORAL EVIDENCE

4 The Secretary said that the Chairman had indicated that he would be available on both 8 and 15 September. The CLCB had agreed to meet the Committee on the morning of 8 September and it was thought that the lawyers could be seen on the afternoon of that day. [This has since been confirmed]. The Committee agreed that these arrangements could go ahead. The Secretary added that CCAB could not meet the Committee on 4 September but were available on the morning of 15 September; the Committee agreed to see them then.

5 The Committee took the view that no other oral evidence should be taken until October. This would include the Department of Trade and the revenue departments.

6 In addition to Inland Revenue, Customs and Excise and DHSS it was felt that Department of Employment should be seen on preferential creditors. It was agreed that delegations from these departments should be seen separately.

7 It was agreed that when taking oral evidence the Committee would be able to seek views on the Interim Report which would have been published by then. The Secretary asked members to provide him with a note of topics which they would wish to discuss with those due to give oral evidence in September as soon as possible.

SECRETARY'S REPORT

8 The Secretary said that apologies for absence had been received from Sir Kenneth Cork, Mr Avis, Mr Muir Hunter, Mr Walker-Arnott and Mr Jack.

9 Papers circulated since the last meeting had been ILRC 119 and 123 to 128, a letter and papers from the Hundred Group of Chartered Accountants (now numbered C202), and briefs and comments from members on items on the agenda. Placed before the members were comments by Mr Walker-Arnott on group trading, the clause from the lost 1973 Companies Bill extending s.332(3) and a revised list of ILRC papers (up to 128).

10 Meetings fixed for August were as follows: Working Group 1 on 12 August; Working Group 2 on 15 August; the Legal Panel on 18 August; and the main Committee on 20 August.

11 The Secretary said that a further Companies Bill was being prepared primarily to implement the next EEC Directive on company law. For this reason the Bill would need to reach the "Second reading" stage by December. The Department wished to include something on s.332 in the Bill, but felt that new proposals, such as the Committee's ideas on "Wrongful trading", should be left over until after the Final Report had been submitted. Therefore, they were proposing to implement the Jenkins' recommendation (Clause 107 of the lost 1973 Bill, put before the Committee) extending s.332(3) to cover all fraudulent trading, irrespective of whether or not the company was in liquidation. The Department would, however, first seek the Committee's views. The Committee agreed that the proposed clause would be welcome. In addition, if penalties had not been increased, they should be.

PARTNERSHIP BANKRUPTCY

12 The Committee reverted to this (see paras 43 to 45 of the minutes of the fortythird meeting) and had before it a note from Mr John Hunter.

13 Mr John Hunter, referring to the text books, suggested that the problem was an accounting rather than a legal one. Mr Millett pointed out that no evidence had been adduced to the contrary and he thought that the present law was fair and sensible. The Committee agreed that no change should be recommended although reference might be made to the views of the academics.

GROUP TRADING

14 The Committee had before it ILRC 119 and 128, notes from the Secretary on the Accountants' Panel and Legal Panel views, comments from Mr Copp, Mr McNab and Mr Walker-Arnott, and the submission from the One Hundred Group of Chartered Accountants (C202).

15 Mr Millett thought that the Committee should do no more than refer to the grievances which were felt, the evidence received and possible solutions. The Secretary pointed out that in Parliament it had been stated that the Committee would be reporting on this problem. In view of the absence of the Chairman and Mr Walker-Arnott it was decided to defer further consideration until the next meeting. Further comments from members were welcomed.

DISPOSITION OF PROPERTY AFTER COMMENCEMENT OF WINDING UP

16 The Committee had before it ILRC 123. The Secretary said that no comments had been received from members.

17 With regard to the three headings of complaint in para 7, on (a) Mr Endersby thought that there might be a case for laying out broad directions. Mr Millett however thought that over the years the Courts had made it clear what s.227 was about (the object was to try and preserve the assets for the creditors and to prevent the assets being dissipated or being paid out to existing creditors not pari passu); it was unnecessary to spell it out. On (b) Mr Millett said that the Courts have made it clear that they can act, and on (c) Mr Millett said that the Court in practice would always validate transactions in favour of persons who reasonably could be ignorant of the presenting of a petition.

18 Mr Millett thought that s.227 worked well and Mr Weiss agreed, but added that application to the Court was not made often enough. Mr Millett thought that s.227 was still needed in company cases. Mr Goldman however saw no necessity for it if the Committee's other recommendations were implemented. During the discussion which followed it was noted that Mr Muir Hunter in introducing ILRC 98 (Initiation of insolvency proceedings) at the thirtysecond meeting had said that it was intended to apply to both individual and corporate debtors; and that the Committee had reached decisions on advertisement at the thirty-fifth meeting (para 25 of the minutes). It was noted that if s.227 was repealed, antecedent transaction provisions would apply up to the making of an order, that a company would have the right to apply for an administrator if it wished to make dispositions and it could be provided that all dispositions made should be void except in favour of bona fide persons for value without notice. It was agreed therefore that s.227 was no longer required.

HANDLING AND INVESTMENT OF FUNDS BY LIQUIDATORS, TRUSTEES AND RECEIVERS

19 The Committee had before it ILRC 126 and 127, and a set of forms required by liquidators and trustees.

20 Mr Weiss thought that this was an area where savings in staff and costs could be made. Mr Taylor stressed the need for control and for there to be a positive disincentive against liquidators protracting liquidations. The Committee were reminded that in the liquidation of assets procedure it was being proposed that the trustee should report to the Court annually as to why the liquidation had not been finalised and it was suggested that this idea might be applied to all insolvency procedures; this met with approval.

21 As to recommendation (1) (that the liquidator etc, should be able to pay moneys directly into approved accounts and draw them out without intervention of the Department) this was agreed by the Committee. "Approved account" was a matter for the Rules and it might well be any institution approved under the Banking Act 1979. On the question of security, it was thought that compulsory bonding would provide a sufficient safeguard. It might be that the Department would wish for these accounts to be at the Bank of England; collectively there would be a large sum and interest could be paid into the Insolvency Services Account, whereas the individual estate account could produce only a small amount of interest. This was a matter which needed to be raised with the Department in oral evidence.

22 Recommendations (2) to (4) were then accepted.

23 Mr John Hunter pointed out that certain changes were needed in the text of the paper before it went into the Report. S.362 applied also to voluntary liquidations whilst s.343 applied also to compulsory liquidations.

TRADE PROTECTION ASSOCIATIONS

24 The Committee had before it ILRC 124. Mr Weiss said that this arose from complaints that practitioners control trade protection associations and thereby get votes to become a liquidator and then a member of the association sits on the committee and votes the remuneration.

25 It was felt that the recommendation that a liquidator etc, must be a member of a specified professional body would to some extent be a safeguard in that complaints could be addressed to the appropriate disciplinary committee. Mr Weiss pointed out however that the bulk of the complaints were against the employee of the trade association.

26 It was agreed that attention should be drawn to the abuse, that it should be a requirement that interest should be declared, that it should be pointed out that legislation on canvassing already existed, and that such legislation should be enforced more strictly.

PROOFS OF DEBT AND PROVABLE DEBTS

27 The Committee had before it ILRC 125 and a note from Mr John Hunter.

28 As regards proofs of debt, it was agreed that something like Form 60A was required in all forms of insolvency proceedings. Where there was likely to be a Court action, a formal proof could be called for.

29 The Committee then considered provable debts.

30 It was suggested that unliquidated claims in tort should be provable just as are unliquidated claims under contract. Mr Graham indicated that he was doing some research into the theory behind the distinction. It was agreed that something like the New Zealand provision (or the Republic of Ireland provision) should be included subject to whatever Mr Graham discovered in his research. Mr John Hunter pointed out that the victim of a tort by an insolvent company was in a worse position than a victim of a tort by a bankrupt.

31 The suggestions by GKN (C29) could not be accepted.

32 As to fines and costs, Mr Graham offered to look into the present position, but it was thought that these were not a matter in which the Committee should get involved.

33 With regard to foreign currency debts the proposal by the Senate of the Inns of Court and the Bar and the Law Society (C186) that Re Dynamics should be confirmed was agreed (with Mr Taylor dissenting on the grounds of uncertainty), and a rider by Mr Graham was also agreed that, if there was a surplus after creditors had been paid, a foreign creditor who had been compelled to accept an earlier date for conversion should be topped up before payment was made to shareholders.

RECEIVERSHIPS UNDER FLOATING CHARGES

34 This item which covered the remaining undiscussed paras of ILRC 73 (paras 94 et seq) was deferred and members were asked to retain the brief for the next meeting.

NEXT MEETING

35 It was agreed that the Committee would meet next at 10.00 am on Wednesday, 20 August. The agenda would include Group Trading, Receiverships (para 34 above), the Family Dwelling and whatever other papers were ready.

44th agenda
43rd Mins

INSOLVENCY LAW REVIEW COMMITTEE

FORTYFOURTH MEETING

Meeting to be held in the Conference Room, 2-14 Bunhill Row, on Wednesday 16 July 1980 at 10.00 am.

A G E N D A

1 Minutes of the meeting on 25 June.

2 Matters arising.

3 Secretary's report.

4 Partnership bankruptcy (ILRC 120) (see minutes of 43rd Mtg, paras 43-45).

5 Group Trading (ILRC's 119 and 128).

6 Disposition of property after commencement of winding-up (ILRC 123).

7 Handling and Investment of Funds by liquidators, trustees and receivers (ILRC's 126 and 127).

8 Trade Protection Associations (ILRC 124).

9 Proofs of Debt and Provable Debts (ILRC 125).

10 Receiverships (ILRC 73 paras 94-108) - see 'brief' attached.

11 Any other business.

12 Agenda for next meeting (20 August).

T H TRAYLOR
Secretary
1 July 1980

ILRC 44th MEETING

Brief for Item 4

Partnership Bankruptcy (ILRC 120, DT6)

1 This was a late addition to the agenda of the last meeting. The paper suggests that no changes in the law are required - a proposal which is supported by the CCAB. It was decided to raise the matter again at the next meeting in order to deal with any notes which had been sent in by members.

2 Attached is a note by John Hunter.

Trevor Traylor

T H TRAYLOR
10.7.80

PARTNERSHIP BANKRUPTCY

(Note by John Hunter)

Lindley on Partnership (14th edn. p. 768) points out that the principle adopted in bankruptcy of making each estate pay its own creditors often produces results strangely at variance with the doctrine of equality, and with an accountant's notions of right and wrong. This is illustrated by an example quoted from an old text book on partnership accounts and a copy of this is attached.

The rule was also criticised in a treatise on Joint Obligations by Professor Glanville L. Williams, published in 1949. He says (pp. 86/87) -

> "From the point of view of the practising lawyer it is useless to criticise well-established rules, but as the present work is concerned in part with the betterment of the law a few critical remarks will not be out of place. The rule under consideration has perhaps some quality of symmetry which gives it an aesthetic appeal; but here one's approbation must end. An early case calls it a 'resolution of convenience', but this it certainly is not. The rule compels the court to undertake the task (often extremely difficult) of distinguishing between joint property and separate property and joint debts and separate debts; thus so far from saving trouble it causes it. In any case it is strange that the rights of creditors should be so ruthlessly sacrificed to mere ease of administration. An illustration will show the injustice that may be caused by the rule between the two groups of creditors. A and B are partners: C advances A £1000 by way of private loan, which A in fact uses in the partnership business, and D advances £1000 to the partnership as such. A and B become bankrupt having joint estate of £10 and separate estates of £10,000 each. The rule must be applied, for the existence of joint estate of any value, however small, is enough to save it. Hence, while C will be able to prove (with the other separate creditors) against A's valuable private estate, and may well receive the whole or practically the whole of his advance, D may go practically without remedy. Such a rule might be tolerable if there were some provision, as in the case of companies, whereby outsiders who trust the firm can assess its financial position; but there is not."

There are several exceptions to the general rule, which give rise to distinctions difficult to defend on merit, such as the one referred to at paragraph 44 of the minutes of the 43rd. meeting. However, I doubt if such anomalies can be dealt with by legislation without a revision of the rule itself. Perhaps accountants are better qualified than lawyers to propose such a revision. What is described in the passage quoted in the attached extract as following out mercantile principles appears

/preferable

preferable to the present rule.

Professor Glanville Williams refers to the provisions of Rule 19 of Schedule 2 of the Bankruptcy Act 1914 which, he says, as interpreted by the courts, gives a right of cumulative proof against both joint and separate estates in the case of joint and several contracts. He is critical of the restriction of this provision to contractual obligations and concludes by making the following general proposal -

> "It seems clear that what is necessary is that the exception for joint and several contracts should be turned into the rule not only for joint and several liability but for joint liability. In other words double proof should be allowed in all cases, and joint creditors should be treated pari passu with separate creditors whether the liability is joint or joint and several and whether it is contractual or not. To achieve this result an amendment of the Bankruptcy Act would be required."

I note from Underhill's "Principles of the Law of Partnership" (10th edn. p.141) that in Scotland each firm creditor values the dividend which he considers he will get from the firm's assets, and then proves against the partner's separate estates for the balance. In Scotland a partner is liable severally as well as jointly for the debts of the firm (Partnership Act 1890, section 9).

No less than 50 pages of Lindley on Partnership are devoted to this complicated matter. In the absence of any evidence proposing changes we may perhaps be excused from dealing with the topic in our report.

8 July 1980

J.M. HUNTER

the consolidation takes place; and if a debt has been properly proved against each of several estates, the creditor will not be prejudiced by their subsequent consolidation.[21]

Comparison of the modes in which lawyers and accountants proceed in cases of bankruptcy

The principle adopted in bankruptcy of making each estate pay its own creditors often produces results strangely at variance with the doctrine of equality, and with an accountant's notions of right and wrong. This cannot be better shown than by the following extract from a work already referred to on the subject of partnership accounts:

"We will suppose A, a man worth £40,000 clear, well known in London, and of extensive credit, to embark with an inventor, B, to carry into effect some invention which requires apparently more credit than actual capital; there being what may fairly be considered a most excellent prospect of success, and of turning the concern, as the phrase is, within a short space of time, *i.e.* receiving from the anticipated profits of the concern, within the number of months in which the bills given by this partnership become due, sufficient money to meet them or take them up. Some accident intervenes, by which it becomes necessary for A, who undertakes to find the money, to raise a sum to meet the numerous bills which the firm has ventured to put afloat, in expectation of their being taken up by the success of the project. A raises upon his credit from several persons, perhaps at a distance in the country and altogether ignorant of his trading, what he himself considers only temporary loans, to the amount of £39,000, and brings this money into the firm, not as a loan but as capital. We will further suppose that this is insufficient and that the firm, after a few more struggles, stops payment for £50,000, owing to different individuals. A general meeting of all the creditors is called, at which there is a desire to settle the matter, and realise the effects as fast as possible, and for that purpose they put the matter into the hands of an accountant. If the accountant knew anything of the law of bankruptcy, he would see the difficulties; but if he simply followed out the mercantile principles, he would first take the account of the firm, and there find £50,000 debts, and we will say £4,000 assets and consequently a balance due to the firm from A and B to the amount of £46,000; of which A would be indebted £23,000 and B £23,000, or in some other proportions as the case may be; but as B is worth nothing at all, A would be answerable for the whole. The accountant would then take A's accounts where he finds A's estate worth £40,000, and that he is liable to the firm for £46,000, and to other people for £39,000, making the whole amount of his liabilities £85,000, upon which he would declare a dividend of 9s. 4½d. He would, therefore, carry over to the firm, as a creditor for £46,000, the sum of £21,647 1s.

21 *Ex p. Fuller*, 1 M. & A. 222.

3d., and to the private creditors £18,352 18s. 9d., which, distributed among the £39,000 would give them a dividend of 9s. 4½d. He would then proceed to distribute the effects of the firm, amounting to £21,647 1s. 3d., recovered from A, and the assets in hand, *viz.*, £4,000, and this, being altogether £25,647 1s. 3d., distributed among £50,000, would give a dividend of 10s. 3d. Such would be the result of the accountant's operation. But some of the separate creditors would probably be dissatisfied with this result, and strike a docket, and have the accounts taken in bankruptcy. The Court of Bankruptcy would immediately overthrow the accountant's labours, and take the accounts upon an entirely different plan. It would direct that the separate estate should be distributed amongst the separate creditors, and if there were any surplus, that it should be paid over to the joint estate. Therefore, as £40,000 would be distributed amongst £39,000, they would be all paid in full, and £1,000 passed over to the joint estate, making the assets of the joint estate £5,000, which, being distributed among the £50,000, would be exactly 2s. in the pound. Thus the Court of Bankruptcy would give the separate creditor 20s. in the pound, and the joint creditor 2s.; while, according to the mercantile principle, the separate creditors ought to have had but 9s. 4½d., and the joint creditors 10s. 3d. Such is the difference between the practice of the two classes. But if the firm had had no property at all, or the partners, in a fit of despair, had pledged all the assets for more than they were worth, the Court of Bankruptcy would have adopted the accountant's principle, and suffered the joint creditors to go in for their dividends upon the separate estate." [22]

(b) Joint Estate and Separate Estates

What property is distributable as partnership property, and what is not, depends mainly upon two questions, *viz.*:

1. Whether, as between the partners themselves, the property in question belonged to them jointly, or to some or one of them to the exclusion of the others; and
2. Whether the property in question, no matter to whom it belonged, was, at the time of the bankruptcy, in the reputed ownership of the firm, or in that of some or one only of its members.

The principles applicable to these questions having been already fully examined,[23] it is only necessary, in the present place, to notice those peculiar difficulties which are met with when it becomes necessary to distinguish joint from separate estate for the purposes of administration in bankruptcy.

It was decided in the celebrated case of *Ex p. Ruffin* [24] that agreements between partners altering the character of partnership property are binding on the trustee in bankruptcy, if made bona fide, and before the commission

[22] *Cory on Merc. Accounts* (2nd ed.), pp. 124 *et seq.*
[23] *Supra*, pp. 444 *et seq.*, and pp. 750 *et seq.*
[24] 6 Ves. 119.

ILRC 44th MEETING

Brief for Item 9

Proofs of Debt and Provable Debts (ILRC 125)

1 The Committee decided some time ago that it might be necessary to discuss these matters and summaries of the written evidence were recently sent out under ILRC 128.

2 Attached are some comments by John Hunter. With regard to John's question concerning the requirement to use the prescribed form (60A) does not Rule 7 of the Bankruptcy Rules give the answer?

> "R7(i). The forms in Appendix I, with such variations as circumstances may require, shall wherever applicable be used in proceedings under the Act."

3 I believe it is normal practice for the forms (including proxy forms, etc) to be sent out with the Notice of First Meeting by the CR. The prescribed form of Notice of the meeting actually states that a form of proof is enclosed. I would have thought that the simplified form was of benefit both to creditors and to trustees but members may feel that a detailed statement should be sufficient.

Trevor Traylor

T H TRAYLOR
10.7.80

PROOFS OF DEBT AND PROVABLE DEBTS

Form of proof (Note by John Hunter)

Re C 108, under rule 2 of Schedule 2 of the Bankruptcy Act 1914, as amended by the Insolvency Act 1976, where the O.R. or trustee does not call for an affidavit, a debt may be proved by "an unsworn claim to the debt". This is not stated in the Schedule or in the Rules to require a prescribed form, although a form (60A) has been added to the prescribed forms in the Rules. Would the O.R. or trustee not be entitled to accept a detailed statement, though not in Form 60A ? This has always been the practice in N.Ireland.

Provable debts

Re C 93, claims for unliquidated damages in tort can now be proved in New Zealand under section 87 of the Insolvency Act 1967, if capable of estimation. Such claims are provable in the Republic of Ireland under section 61 of the Civil Liability Act 1961, a copy of which is attached. It would appear that under the New Zealand and R of I provisions a bankrupt, on obtaining his discharge, would be released from tortious claims admitted in the bankruptcy. Mr. Ian Fletcher, however, proposes that this should not be so, on the ground that the victim of a tort is an involuntary creditor and should not have his rights susceptible of complete cancellation through the tortfeasor's expedient bankruptcy. I think there is force in this argument.

A serious objection to the admission of such claims is that the ascertainment of the amount of the damages (which would often have to await the outcome of an action in the Q.B.D.) would delay the payment of all creditors.

8 July 1980.

J.M.H.

[Republic of Ireland]

(*b*) the traffic using the road,

(*c*) the condition in which a reasonable person would have expected to find the road.

(4) In determining whether a road authority had a reasonable opportunity to give warning that a road was a danger to traffic or had taken reasonable precautions to secure that a road was not such a danger, regard shall be had to the standard of supervision reasonable for a road of such character.

(5) In this section—

"road authority" means the council of a county, the corporation of a county or other borough and the council of an urban district;

"public road" means a road the responsibility for the maintenance of which lies on a road authority and includes any bridge, pipe, arch, gulley, footway, pavement, fence, railing or wall which forms part of such road and which it is the responsibility of the road authority to maintain.

(6) This section shall not apply to damage arising from an event which occurred before the coming into operation of this section.

(7) This section shall come into operation on such day, not earlier than the 1st day of April, 1967, as may be fixed therefor by order made by the Government.

Proof of claims for damages or contribution in bankruptcy.

61.—(1) Notwithstanding any other enactment or any rule of law, a claim for damages or contribution in respect of a wrong shall be provable in bankruptcy where the wrong out of which the liability to damages or the right to contribution arose was committed before the time of the bankruptcy.

(2) Where the damages or contribution have not been and cannot be otherwise liquidated or ascertained, the court may make such order as to it seems fit for the assessment of the damages or contribution, and the amount when so assessed shall be provable as if it were a debt due at the time of the bankruptcy.

(3) Where a claim for contribution or in respect of a judgment debt for contribution is provable in bankruptcy, no such proof shall be admitted except to the extent that the claimant has satis-

fied the debt or damages of the injured person, unless the injured person does not prove in respect of the wrong or debt.

Application of moneys payable under certain policies of insurance.

62.—Where a person (hereinafter referred to as the insured) who has effected a policy of insurance in respect of liability for a wrong, if an individual, becomes a bankrupt or dies or, if a corporate body, is wound up or, if a partnership or other unincorporated association, is dissolved, moneys payable to the insured under the policy shall be applicable only to discharging in full all valid claims against the insured in respect of which those moneys are payable, and no part of those moneys shall be assets of the insured or applicable to the payment of the debts (other than those claims) of the insured in the bankruptcy or in the administration of the estate of the insured or in the winding-up or dissolution, and no such claim shall be provable in the bankruptcy, administration, winding-up or dissolution.

Costs in certain actions in which the plaintiff is an infant.

63.—(1) Where a sum of money has been lodged in court by the defendant in an action for a wrong in which the plaintiff is an infant, an application may be made to the judge by the plaintiff to decide whether that sum of money should be accepted or the action should go to trial and—

(*a*) if, on any such application, the judge decides that the action should go to trial, and

(*b*) an amount by way of damages is awarded to the plaintiff which does not exceed the sum so lodged,

then, notwithstanding any rule of court or practice to the contrary, the costs in the action shall be at the discretion of the judge.

(2) An appeal shall lie from the order of the judge in relation to the costs in such action.