

<p>1 Friday, 20 February 2015 2 (10.30 am) 3 MR JUSTICE DAVID RICHARDS: Mr Zacaroli, just before you 4 start your submissions, can I raise a logistical issue 5 as regards Monday. As you may know, there is the Global 6 Law Summit taking place in London, I think it's Monday, 7 Tuesday, Wednesday, and on Monday afternoon there is 8 a session here in the Rolls Building, not only here in 9 the Rolls Building but on this floor. They are not, 10 I think, going to be using this court but there are 11 going to be quite a lot of -- upwards of about 200 12 delegates outside and they are going to have a session 13 outside before going into various courts. I have been 14 wondering how best we can cope with that. It occurs to 15 me there are two alternatives. One is to press on with 16 usual court hours, as if they weren't there, which is 17 possible, I think, given we have double doors and so on. 18 I would hope that the noise outside would be kept to 19 a minimum, but one doesn't know and there is the 20 difficulty you have 200 people out there and quite a lot 21 in here and so on. 22 The alternative, which on balance I think may be 23 preferable, would be to sit at, let's say, 9.30 on 24 Monday go and on with a break at some point to 1.30 or 25 2 o'clock. I mean, I'm quite -- I would welcome your</p> <p style="text-align: center;">Page 1</p>	<p>1 overview for a moment, so far as construction is 2 concerned, broadly we say that the rule, 2.88(7), 3 requires interest to be paid at a defined rate on 4 a defined sum for a defined period. Those words neither 5 permit nor require that interest is calculated on the 6 basis that the proved debt has not in fact been paid or 7 that interest will be payable long after the proved debt 8 has been paid, or that what is being paid is actually 9 principal, not interest, all of which are 10 characteristics of the Bower v Marris rule. 11 I will develop those points shortly. 12 So far as the second point is concerned, why 13 Bower v Marris is irrelevant, and, again, just to 14 summarise what we'll be dealing with in some detail when 15 we go to the cases, but the proposition for which 16 Bower v Marris stands as authority is that payments made 17 under a process of law, such as dividends under the 18 Bankruptcy Act, but also other examples, are not 19 appropriated towards discharge of principal or interest, 20 they're not appropriated at all. They are treated as 21 being payments on account in the event that any surplus 22 arises, such that the creditors' right, which is a right 23 under the general law, to appropriate payments when the 24 debtor has not appropriated them, survives and is 25 exercisable.</p> <p style="text-align: center;">Page 3</p>
<p>1 views on that. You might want to just have a word about 2 it in the mid-morning break and come back to me. I have 3 a slight inclination in favour of sitting early and just 4 finishing before they all arrive, but if you could give 5 some thought to that, the precise hours, I would have 6 thought if we started at 9.30, I think we would need 7 certainly -- certainly I think our transcribers would 8 need some -- a half hour break or something in the 9 middle and what time we finish, you just might like to 10 think about. But perhaps I can leave that with you all. 11 It would be helpful if you can tell me after the 12 mid-morning break what your views are about it. 13 Opening submissions by MR ZACAROLI 14 MR ZACAROLI: My Lord, we will do. Thank you. 15 MR JUSTICE DAVID RICHARDS: Thank you very much. 16 MR ZACAROLI: My Lord, I propose to deal with issue 2 under 17 three broad topics. First of all, the construction of 18 the rule itself as a matter of construction. 19 Secondly, to explain why Bower v Marris is 20 irrelevant to that question of construction. 21 Thirdly, to deal with the fact that Bower v Marris, 22 even where it does apply, can only apply in respect of 23 interest-bearing debts and the impact that has on the 24 second topic. 25 To unpack those three broad points by way of</p> <p style="text-align: center;">Page 2</p>	<p>1 The ordinary rule of appropriation as between 2 solvent debtors and creditors therefore applies and 3 operated on a presumption that the creditor would wish 4 to satisfy interest first, but it's a presumption and is 5 not always so. 6 Now, that proposition, for which Bower v Marris is 7 authority, has relevance when one is considering 8 a creditor's entitlement once there is a surplus to 9 pursue whatever pre-existing claim it had on the 10 assumption that the debtor is now solvent. That was the 11 basis on which interest from an insolvency surplus was 12 payable under every English case, every Australian case 13 that my Lord has had to consider, that has ever 14 considered the point. It was not the case in two 15 examples, re Hibernian in Ireland and the 16 Confederation Trust case in Canada. We distinguish 17 those cases on the basis they were wrongly decided, 18 there was no proper analysis and the arguments weren't 19 put. So I'll always exclude those two cases in my 20 general propositions about the cases that have 21 considered this idea. 22 But the proposition is simply irrelevant to 2.88(7) 23 because the legislation in 1986 proceeded on a different 24 basis. It's no longer a question of allowing 25 pre-existing claims to be reasserted once the debtor is</p> <p style="text-align: center;">Page 4</p>

<p>1 solvent, whether company or individual. Instead there's 2 a direction as to how to apply the surplus, i.e. paying 3 interest at a defined rate on a defined sum for 4 a defined period.</p> <p>5 Turning to the third topic, just by way of overview. 6 If and where the Bower v Marris calculation applies, it 7 can only logically apply to creditors with 8 interest-bearing debts. There are two reasons for that. 9 The first one is a technical reason: because for 10 a creditor to be able to appropriate a payment to one 11 payment or -- one liability or another, both those 12 liabilities must exist at the time the payment is made. 13 In the case of a non-interest-bearing debt, there is no 14 interest accrued at the date that dividends are paid in 15 the bankruptcy.</p> <p>16 The second reason is a broader reason and really 17 goes back to the rationale underlying Bower v Marris and 18 Bromley v Goodere, which is that creditors' contractual 19 rights should be satisfied before the bankrupt gets 20 anything. So the whole rationale for the rule, as 21 applied in bankruptcy, in the early part of the 22 19th century, was it was based upon satisfying 23 creditors' rights.</p> <p>24 Now, that is both a freestanding point, that 25 whatever else may be the case, it can't apply to</p> <p style="text-align: center;">Page 5</p>	<p>1 be such a non-provable claim in relation to interest, 2 but we say that the only way out of the dilemma, if 3 my Lord sees that as a dilemma or some sort of prejudice 4 being suffered, the only way out of it is by a further 5 round of claims, non-provable claims for those with 6 interest-bearing debts.</p> <p>7 Now, there are, as my Lord will see, many areas of 8 disagreement, but two main areas of disagreement with 9 the Senior Creditor Group about the application of 10 Bower v Marris. First of all, we disagree fundamentally 11 with their description of the so-called rule in 12 Bower v Marris. They refer to it as essentially a rule 13 which dictates the calculation of interest payable in an 14 insolvent estate. We disagree with that fundamentally. 15 We say it is as I have already stated and I will come 16 back to develop it in due course.</p> <p>17 Secondly, and it follows from that, we disagree with 18 the repeated assertion that our case involves the 19 abolition of the rule in Bower v Marris, whether in 1883 20 in bankruptcy or in 1986 for companies. The point is 21 that Bower v Marris is simply a facet of a creditor's 22 rights in relation to interest against a solvent debtor, 23 and where the rules, as they did in 1883 with bankruptcy 24 and 1986 for companies and bankruptcy, do not proceed on 25 the basis of remitting creditors to their contractual</p> <p style="text-align: center;">Page 7</p>
<p>1 creditors with non-interest-bearing debts, but it also 2 reinforces the point we make that the draughtsmen can't 3 have intended that this Bower v Marris-type of 4 calculation would have any application under 5 rule 2.88(7) because it creates unworkable difficulties. 6 I will develop those when we get to the third topic, but 7 that's our broad proposition there.</p> <p>8 Now, by way of perhaps footnote at this stage, if 9 my Lord is ultimately persuaded by an argument that 10 creditors who would have had some right under the 11 general law to appropriate payments towards interest as 12 opposed to principal first, had the debtor been solvent, 13 if those creditors' rights have been prejudiced by the 14 insolvency regime as a whole, and that my Lord is 15 concerned about that, the only way logically that that 16 can be addressed is through a non-provable claim that 17 comes after 2.88(7). I'm not submitting that my Lord 18 should find that. Of course we say there shouldn't be 19 one for a variety of reasons, but logically the only way 20 out of this is that it comes in afterwards and only in 21 respect of interest-bearing debts.</p> <p>22 One of the slightly odd features of the submissions 23 of both parties or both sides in this so far as -- 24 I think we agree there's an element of common ground 25 that actually there are good reasons why there shouldn't</p> <p style="text-align: center;">Page 6</p>	<p>1 rights, it simply has no part to play. It's not 2 abolished, it's just irrelevant.</p> <p>3 The rest of my submissions will fall into the 4 following parts. First of all, I'll take each of those 5 three broad topics in turn. That will take 6 a considerable amount of time. We'll have to go through 7 many of the cases that my Lord has seen and many that 8 my Lord has not seen.</p> <p>9 MR JUSTICE DAVID RICHARDS: Right.</p> <p>10 MR ZACAROLI: Secondly, I'll pick up on the point that the 11 word "rate" in rule 2.88(9) incorporates Bower v Marris 12 into the calculation process. I'll deal, I think, at 13 the same time with the sub-issue about interest on 14 a compound basis, continuing to compound and accrue on 15 a compound basis after the debt has been paid.</p> <p>16 The third thing is I'm going to respond briefly to 17 my learned friend's three basic propositions from 18 Wednesday about how the rule works -- about how the 19 construction works, how the construction of the present 20 rule works.</p> <p>21 Fourthly, I'll deal with some point of principle and 22 policy and then, fifthly, I'm going to take issue 39 23 which really follows on from those point of policy and 24 principle.</p> <p>25 MR JUSTICE DAVID RICHARDS: Right.</p> <p style="text-align: center;">Page 8</p>

<p>1 MR ZACAROLI: So then, turning to the first topic, which is 2 construction. All parties agree that question 2 in the 3 application is actually a question of construction of 4 the rule. Before I get to looking at the words 5 themselves, the specific words themselves, I want to 6 place the rule in context, which requires seeing what 7 the existing regime was that Parliament was faced with 8 when enacting the 1986 Insolvency Act and rules. 9 This is familiar ground so I can take it quickly, 10 although I do want to go back over the Bankruptcy Act in 11 a little detail to correct what we says a misconception 12 as to how they worked. 13 First of all, as my Lord well knows, in winding up 14 there was no statutory regime for payment of interest if 15 a company turned out to be solvent at all. There was 16 a judge-made rule from Humber Ironworks that interest 17 stop running at the date of winding up, but, if there 18 was a surplus, creditors were remitted to their 19 contractual rights. 20 On the other hand, in bankruptcy there was already 21 a long history of statutory provision of one kind or 22 another for post-bankruptcy interest, it's actually 1824 23 but the Act was replaced within a year by the 1825 Act, 24 which is the one we're going to look at. 25 Can I my Lord to take up the bundle 3A, just to go</p> <p style="text-align: center;">Page 9</p>	<p>1 MR ZACAROLI: If there's any surplus, it shall be applied in 2 payment of interest from the date of the receiving order 3 at the rate of £4 per centum per annum. 4 Then section 65 over the page: 5 "The bankrupt shall be entitled to any surplus 6 remaining after payment in full ...(reading to the 7 words)... as by this Act provided and of the costs, 8 charges ...", et cetera. 9 Now, at this point we suggest there's 10 a misconception in my learned friend Mr Dicker's 11 analysis of the rules here or the sections here. He 12 submitted that in section 65 what Parliament was doing 13 was preserving the rights of creditors who might have 14 a higher contractual rate of interest to be paid before 15 it goes back to the bankrupt. My Lord, first of all, as 16 a matter of construction of the section, that ignores 17 the crucial words "as by this Act provided". The only 18 interest as by this Act provided for the post-bankruptcy 19 period is section 40, sub-section 5. There is no other 20 provision. 21 My learned friend's reading would have the 22 slightly -- well, we would say very -- odd intention to 23 be imputed to Parliament that, having the started with 24 an Act which gave creditors a contractual right of 25 interest as a priority over everybody else,</p> <p style="text-align: center;">Page 11</p>
<p>1 quickly back to the statutory provisions. Tab 10 is the 2 1825 Act. Section 132 is in the last page of the tab, 3 I think. 4 MR JUSTICE DAVID RICHARDS: Yes. 5 MR ZACAROLI: The section that's following features. They 6 won't be unsurprising to my Lord. First of all, the 7 surplus is to paid to the bankrupt after all creditors 8 who have proved have been paid. That's the first aspect 9 of the rule. Secondly, it requires, before that 10 happens, that interest to be paid on those debts with -- 11 which bear interest at such rate as they carry, but only 12 if there's anything left after that, so on 13 a subordinated basis there's a right of 4 per cent 14 interest for all non-interest-bearing debts. 15 MR JUSTICE DAVID RICHARDS: Yes. 16 MR ZACAROLI: Turning on then to the 1883 Bankruptcy Act. 17 That provision remained in substantially the same form 18 in the interim Acts, and we needn't look at those, but 19 there was a substantial change in 1883. 20 MR JUSTICE DAVID RICHARDS: Right. 21 MR ZACAROLI: Tab 27 of the bundle. 22 MR JUSTICE DAVID RICHARDS: Yes. 23 MR ZACAROLI: The two relevant sections are section 40, 24 sub-section 5, on page 302. 25 MR JUSTICE DAVID RICHARDS: Yes.</p> <p style="text-align: center;">Page 10</p>	<p>1 subordinate -- altered that priority by subordinating 2 them to the creditors but said nothing about it. 3 MR JUSTICE DAVID RICHARDS: Yes. 4 MR ZACAROLI: Mr Dicker referred to no authority to support 5 his construction of the rule in that way. In a moment 6 I'll show my Lord a case which is inconsistent with that 7 construction, but, before I do that, I want to deal with 8 the other aspect of interest which comes in in the 9 1914 Act. 10 So if my Lord turn on to tab 36. We first of all 11 have the same provisions as in the 1883 Act but this 12 time section 338, which is the only provision providing 13 for interest for the post-bankruptcy period. It's the 14 4 per cent flat rate for all. 15 Then section 69 is the mirror of section 35 of the 16 1883 Act and refers to the surplus going to the bankrupt 17 after payment in full of his creditors with interest as 18 by this Act provided. The same words appear. 19 MR JUSTICE DAVID RICHARDS: Yes. 20 MR ZACAROLI: The other provision, which is new -- 21 MR JUSTICE DAVID RICHARDS: Sorry, that's in section 69? 22 MR ZACAROLI: 69. 23 MR JUSTICE DAVID RICHARDS: Yes, absolutely. 24 MR ZACAROLI: So then there's another provision which is 25 new. It in fact came in in the Bankruptcy Act 1890 and</p> <p style="text-align: center;">Page 12</p>

<p>1 is then incorporated into this consolidated statute in 2 1914 and that's section 66(1). My Lord was shown the 3 section. 4 MR JUSTICE DAVID RICHARDS: Yes. 5 MR ZACAROLI: "Where a debt has been proved and the debt 6 includes interest ...(reading to the words)... have been 7 paid in full." 8 Now, no submission was made about that but lest it 9 be thought that that section somehow continues to apply 10 to interest in the post-bankruptcy period, it does not. 11 It is dealing with proof. It's dealing with an excess 12 over the proved debt. 13 MR JUSTICE DAVID RICHARDS: I see. 14 MR ZACAROLI: Excess in the proved debt over 5 per cent. 15 To make one obvious point: a creditor with, let's 16 say, 4.5 per cent rate of interest would not fall within 17 section 66(1) but would be being done out, as it were, 18 of 0.5 per cent per annum per interest. No way 19 section 66 can deal with that possibility. 20 Now, there is authority that makes good both these 21 propositions. First of all, that the surplus after 22 payment of the 4 per cent statutory and secondly that 23 section 66(1) is dealing only with the pre-bankruptcy 24 interest period. 25 The case is re Baughan, in bundle 1B, at tab 74.</p> <p style="text-align: center;">Page 13</p>	<p>1 the Moneylenders Act." 2 We will see that section but it's in the same in 3 material terms as section 66(1) of the Bankruptcy Act. 4 MR JUSTICE DAVID RICHARDS: Right. 5 MR ZACAROLI: There then at page 315, paragraph 8 in this -- 6 about seven lines down, there's a number 8 in brackets, 7 it then falls to be considered how the balance of 8 approximately £692 shall be applied. That's the 9 surplus -- the surplus in the hands of the trustee: 10 "The possible claimants to this fund are the four 11 money ...(reading to the words)... under section 33(8)." 12 Then reading down a few lines, just above the break, 13 six lines above the break: 14 "The precise direction which the official receiver 15 required and which was argued before his Lordship was an 16 order directing him to what person or persons he should 17 paid the sum of £692 then in his possession being the 18 surplus remaining in his hands." 19 Now, taking up briefly the second case, which is 20 dealt with -- summarised at page 317, the top half of 21 the page, about eight lines down, there's a reference to 22 "the said Alfred Harvey Bennett". 23 MR JUSTICE DAVID RICHARDS: Yes. 24 MR ZACAROLI: He was the trustee of the marriage settlement. 25 So the question for the opinion of the court on this</p> <p style="text-align: center;">Page 15</p>
<p>1 MR JUSTICE DAVID RICHARDS: Yes. 2 MR ZACAROLI: In fact this was two different cases that came 3 on together. In the headnote, at page 313, the second 4 paragraph, it is said: 5 "in two bankruptcy cases the official receiver as 6 trustee ...(reading to the words)... valuable 7 consideration had been satisfied." 8 So those are the two cases. 9 The decision, as noted in the "Held" below: 10 "The money lenders were creditors for their excess 11 interest as a debt provable in bankruptcy and though 12 postponed to other debts it took precedence over the 13 payment of statutory interest under section 33(8)." 14 Then so far as settlement trustee's claim was 15 concerned: 16 "They were not a creditor whose proof for trustee in 17 bankruptcy was bound ...(reading to the words)... to the 18 creditor's claim to statutory interest." 19 Now, looking at the facts briefly, on page 314, 20 towards the bottom of the page, the learned judge, 21 Mr Justice Romer, deals with the first case, the money 22 lender's case. Reading from the bottom, six lines up: 23 "Four proofs by money lenders were admitted for sums 24 totalling £2,000-odd. Of this sum, the amount of 25 ...(reading to the words)... pursuant to section 9(1) of</p> <p style="text-align: center;">Page 14</p>	<p>1 matter is. 2 "... whether the official receiver should apply the 3 surplus ...(reading to the words)... to the creditors 4 who have proved." 5 If we can pick up the judgment at page 320 and deal 6 with case 1, the money lenders first, and then I'll come 7 back to the judgment and deal with case 2. The so the 8 money lenders' claim is dealt with at page 320, the 9 second paragraph of the judgment. Mr Justice Romer 10 says: 11 "The claim by the money lenders on the first 12 application to interest in excess of 5 per cent under 13 section 9(1) ... analogous provisions are contained in 14 section 66(1) of the Bankruptcy Act 1914." 15 You will see the Moneylenders Act section 9 is there 16 in the footnote and it's materially the same, postponing 17 the right to proof. 18 MR JUSTICE DAVID RICHARDS: Right. 19 MR ZACAROLI: For the excess. 20 "It is, I think, clear that the amount due to 21 a money lender ...(reading to the words) ... is whether 22 the excess interest is subordinated further to the 23 statutory interest." 24 The question of subordination is not so important. 25 The important point is it is quite clear that this is</p> <p style="text-align: center;">Page 16</p>

<p>1 talking only about interest due at the date of the 2 adjudication of bankruptcy, or the receiving order. 3 MR JUSTICE DAVID RICHARDS: Yes. 4 MR ZACAROLI: In fact, at the bottom of the page, he 5 decides, page 321, the bottom two lines: 6 "The result of that is that no creditors are 7 entitled to ...(reading to the words)... for the payment 8 of statutory interest." 9 Therefore, at page 327, he concludes, at the bottom 10 of the page, the fourth line from the end: 11 "As I have said earlier in this judgment, excess 12 interest due on money lenders' loan is a debt, and 13 a provable debt. As was stated by the present Master of 14 the Rolls In re A Debtor, Section 9(1) ...(reading to 15 the words)... postponed under section 42(2) of the 16 Bankruptcy Act." 17 That's the matrimonial causes matter. 18 Picking up then case 2, the matrimonial case, this 19 is the aspect which deals with all -- the only interest 20 available to creditors under the Bankruptcy Act is 21 4 per cent -- in relation to post-bankruptcy period is 22 the 4 per cent as provided. 23 MR JUSTICE DAVID RICHARDS: Right, yes. 24 MR ZACAROLI: So case 2 is described, first of all, at 25 page 322 of the judgment. In the middle of the middle</p> <p style="text-align: center;">Page 17</p>	<p>1 MR JUSTICE DAVID RICHARDS: Yes. 2 MR ZACAROLI: Clearly indicating that only -- the statute is 3 only requiring 4 per cent in order to satisfy claims of 4 creditors in full. 5 So with the help of, among other things, that 6 authority, Mr Justice Romer at page 327, says, in the 7 middle paragraph: 8 " I have accordingly come to the following 9 conclusions as to the position of ...(reading to the 10 words)... next in paying dividends to him." 11 MR JUSTICE DAVID RICHARDS: Yes. 12 MR ZACAROLI: Now, it's evident from the report of the 13 Cork Committee that they took the same view as to the 14 operation of the Bankruptcy Act in both respects. If 15 I can ask my Lord to turn that up. It's in bundle 4. 16 MR JUSTICE DAVID RICHARDS: The position therefore is that 17 after 1883 the bankruptcy legislation did not make 18 provision for the payment of post-bankruptcy interest, 19 except to the extent of the statutory 4 per cent? 20 MR ZACAROLI: Yes. 21 MR JUSTICE DAVID RICHARDS: So that was clearly a change 22 from the 1825 section? 23 MR ZACAROLI: Yes. 24 MR JUSTICE DAVID RICHARDS: Yes, I see. Right. 25 MR ZACAROLI: There's no possibility --</p> <p style="text-align: center;">Page 19</p>
<p>1 paragraph, Mr Justice Romer says: 2 "These provisions and authorities conveniently took 3 consideration ...(reading to the words)... or money or 4 money's worth have been satisfied." 5 And it's that phrase "have been satisfied" which is 6 picked up in the judgment later on. 7 MR JUSTICE DAVID RICHARDS: Yes. 8 MR ZACAROLI: I'll come to the consideration of 9 Mr Justice Romer on page 327 in a moment, but, first of 10 all, he cites a case at page 325, a decision of 11 Mr Justice Clauson In re Howes from 1934. He notes at 12 the top of that paragraph: 13 "He, Mr Justice Clauson, there held where the assets 14 of a bankrupt are sufficient to satisfy in full 15 ...(reading to the words)... debts proved in the 16 bankruptcy." 17 Then the principle which he's applying he cites at 18 the bottom of the page, seven lines up: 19 "The principle appears to be well-established by the 20 older cases and the ...(reading to the words)... to meet 21 the claim of Sir Charles Cottier's executors." 22 Although it's not dealing with the surplus being 23 remitted to the bankrupt there, the partner is 24 essentially in the of the bankrupt, in the same 25 position.</p> <p style="text-align: center;">Page 18</p>	<p>1 MR JUSTICE DAVID RICHARDS: Do we know why? 2 MR ZACAROLI: Well, we don't know why. I'm not sure if it's 3 available. 4 MR JUSTICE DAVID RICHARDS: No, I just wondered. Anyway ... 5 MR ZACAROLI: I will, when I come to policy and principle 6 arguments, suggest some reasons why. 7 MR JUSTICE DAVID RICHARDS: Sometimes this is referred into 8 a judgment but it's not here. 9 MR ZACAROLI: We haven't found anything which explains it, 10 but that undoubtedly was the position. 11 MR JUSTICE DAVID RICHARDS: Right. 12 MR ZACAROLI: The Cork Report extracts are in volume 4 at 13 tab 3. First of all, to pick up a quick reference at 14 paragraph 1364 on page 310, my Lord has seen this 15 paragraph. I'm just reminding my Lord of the last 16 sentence at 1364. This is dealing with section 66(1). 17 You will see as described in the last sentence: 18 "The interest in excess of 5 per cent is postponed 19 and ranks for dividend only after all the debts which 20 have been proved have been paid in full." 21 So it picks up the point I made that that's only 22 dealing with pre-bankruptcy interest, provable interest. 23 MR JUSTICE DAVID RICHARDS: Yes. 24 MR ZACAROLI: Then, more importantly, paragraph 1383, 25 section 33(8) of the Act of 1914 provided that:</p> <p style="text-align: center;">Page 20</p>

<p>1 "If, after all the proving creditors have been paid 2 in full, the bankrupt's estate still has a surplus, it 3 is to be applied first in paying interest from after the 4 date of the receiving order at the rate of 4 per cent 5 per annum on all debts proved in the bankruptcy. Any 6 balance then belongs to the bankrupt." 7 Now, it's important to remember, and I'll come back 8 to this again when I'm dealing with policy and 9 principle, that in bankruptcy there is no possibility of 10 the creditor claiming against the bankrupt after he has 11 had his discharge because the debt has been discharged, 12 which includes the interest payable on it. 13 MR JUSTICE DAVID RICHARDS: I see. Right. 14 MR ZACAROLI: So one of the things you might want say is in 15 the bankruptcy context non-provable debts just 16 re-asserted against the bankrupt once he has his 17 discharge, and that's true of many of them. 18 MR JUSTICE DAVID RICHARDS: But not true of interest on 19 a debt which is discharged in the course of the 20 bankruptcy. 21 MR ZACAROLI: Precisely. 22 MR JUSTICE DAVID RICHARDS: Right. 23 MR ZACAROLI: Can we keep the Cork Report open because 24 I want to move now to having summarised the position 25 that the legislature was faced with, namely a remission</p> <p style="text-align: center;">Page 21</p>	<p>1 the interest after the presentation of the winding up 2 petition as if there had been no winding up at all. On 3 the other hand, the creditor who is not entitled has no 4 means of recovering interest, even if later there is 5 a surplus." 6 Thirdly, the committee picked up on the anomalous 7 position that there was a distinction or different 8 approach in bankruptcy and winding up. That 9 paragraph 1386. They refer to it as the anomaly that 10 has been drawn to their attention by many different 11 bodies. 12 Fourthly, they note, in 1385, citing the decision of 13 the Vice Chancellor Pennycuik in Rolls-Royce that the 14 purpose of interest post-bankruptcy, post-liquidation is 15 to compensate creditors for being kept out of their 16 money during the period of the administration of the 17 estate. 18 My Lord found exactly the same in the Waterfall 1 19 judgment. You needn't look at it but the reference, if 20 you want it, is paragraph 86 of the Waterfall 1 21 judgment. It's the compensation for being kept out of 22 money during the period of administration of the estate. 23 MR JUSTICE DAVID RICHARDS: Yes. 24 MR ZACAROLI: Now, one major consideration in formulating 25 proposals was to keep matters simple and certain. You</p> <p style="text-align: center;">Page 23</p>
<p>1 to contractual rights in winding up and a flat rate of 2 interest but no more for all creditors in bankruptcy, 3 that was the starting point before 1986; what then did 4 the Cork Report and the White Paper which followed it 5 recommend? I know my Lord has been taken through the 6 entirety of the paragraphs that I'm going to refer to so 7 I'm not going to ask my Lord to read them again but pick 8 up highlighted points. 9 The first is, as my learned friend pointed out, 10 there's a lot of dissatisfaction with the generally 11 confused position under the 1914 Bankruptcy Act, in 12 particular section 66(1) and sub-section 2 which deal 13 with what has happened if you have been paid interest in 14 the period prior to bankruptcy at the greater rate; that 15 sort of thing. 16 MR JUSTICE DAVID RICHARDS: Yes. 17 MR ZACAROLI: That's undoubtedly true, but other matters 18 which were of concern to the committee, first of all, is 19 the inequality of the position in winding up, that 20 creditors with contractual rights got interest as if 21 there was no winding up at all and others got nothing. 22 That's paragraph 1384. They pick up on this just after 23 halfway through paragraph in the middle of the line: 24 "This means that the creditor who was entitled to 25 interest on the debt for which he has proved may recover</p> <p style="text-align: center;">Page 22</p>	<p>1 see that from paragraph 1392 under the subheading, "Our 2 proposals". 3 MR JUSTICE DAVID RICHARDS: Yes. 4 MR ZACAROLI: "We have taken the following matters into 5 consideration. We consider there should be one set of 6 rules relating to the interest on debts in all forms of 7 insolvency proceedings. In preparing the rules 8 simplicity and certainty are essential." 9 The conclusion, therefore, the recommendation, was 10 to take the current bankruptcy position and extend it 11 across the board. You see that in recommendations at 12 1395, (c): 13 "During the insolvency, in the event of there being 14 a surplus after ...(reading to the words)... at the 15 commencement of the insolvency." 16 So you will see the recommendation then did change. 17 The recommendation then was just the Judgments Act rate, 18 so exactly the position that had applied in bankruptcy. 19 MR JUSTICE DAVID RICHARDS: Yes. 20 MR ZACAROLI: The other point to note is a clear intention 21 in that very paragraph that the interest should run 22 until a final dividend is declared. 23 Finally, one point to just go on. In the middle of 24 paragraph 1392 on this same page, one of the other 25 problems they identified is the unequal treatment of</p> <p style="text-align: center;">Page 24</p>

<p>1 different classes of creditors and they are trying to 2 address that as well. 3 MR JUSTICE DAVID RICHARDS: What is that actually 4 a reference to? 5 MR ZACAROLI: I assume that's talking about the fact that 6 creditors with a right of interest get interest, but 7 those without don't. Maybe not. I thought that's what 8 it was referring to. 9 MR JUSTICE DAVID RICHARDS: That's not -- no, that's not 10 right, is it, in bankruptcy? Sorry, is this bankruptcy 11 or winding up? 12 MR ZACAROLI: This is just generally formulating proposals. 13 MR JUSTICE DAVID RICHARDS: I suppose it could be -- so you 14 think -- hold on. Yes, I think it must be 15 a reference -- it probably is a reference to the 16 winding-up petition, yes. 17 MR ZACAROLI: But point is that inequality of treatment 18 amongst creditors is an important factor. 19 MR JUSTICE DAVID RICHARDS: Yes. 20 MR ZACAROLI: Then turning to the White Paper, because the 21 White Paper did move on from that recommendation in one 22 very important respect. That's at tab 1. First of all, 23 just to pick up a reference in paragraph 85, the review 24 committee identified numerous instances where the 25 present law in relation to the payment of interest is</p> <p style="text-align: center;">Page 25</p>	<p>1 bankruptcy and winding up. It's exactly the same 2 formulation. 3 MR JUSTICE DAVID RICHARDS: Yes. 4 MR ZACAROLI: So the first point to note is it follows the 5 Cork Committee's recommendation in not adopting the old 6 Companies Act regime but taking the bankruptcy regime of 7 a rate of interest payable to all, with the uplift if 8 there was a contractual rate of that rate. So it does 9 not leave creditors to claim as if there had been no 10 winding up at all. 11 It spells out how the payments from the surplus are 12 to be made: 13 "In so doing, we say that it provides new rights 14 that are substantially different to creditors' 15 pre-existing contractual or other rights to interest as 16 against the solvent company." 17 We summarise some of these in paragraph 17 of our 18 initial skeleton, but just to run through them quickly. 19 The most obvious one is that provides a rate of interest 20 at the judgments rate to all creditors, even those who 21 had no right of interest before. 22 The second is, and linked to that, if the creditors 23 had a rate of, say, 4 per cent under his contract, it 24 gave that creditor an uplift if the judgments rate was 25 higher.</p> <p style="text-align: center;">Page 27</p>
<p>1 unsatisfactory. Particular areas of concern were the 2 provision of section 66 of the Bankruptcy Act and 3 then -- and interest payable out of a surplus on claims 4 for the period between the commencement of proceedings 5 and the winding up and the date of payment in full. So 6 they think they're considering the issue of interest 7 payable until the date of payment in full. 8 MR JUSTICE DAVID RICHARDS: I see, yes. 9 MR ZACAROLI: Then the important paragraph is 88. The 10 proposal now is that the judgments rate should be 11 a minimum rate and that if there's a higher contractual 12 rate, then that rate should be applied instead. 13 MR JUSTICE DAVID RICHARDS: Yes. 14 MR ZACAROLI: We say it's important to note that all that is 15 being incorporated here, from what was the position in 16 relation to companies, is the rate of interest, if 17 provided by a contract, was being enhanced. So a higher 18 contractual rate was being substituted for the 19 Judgments Act rate, nothing more. 20 MR JUSTICE DAVID RICHARDS: Yes. 21 MR ZACAROLI: I'll come back to that when dealing with the 22 question whether rule 2.88(9) somehow incorporates 23 Bower v Marris because it uses the word "rate". 24 Now, if I can finally go to rule 2.88(7) itself. As 25 my Lord knows, this is in the same form as the rule in</p> <p style="text-align: center;">Page 26</p>	<p>1 The third point is this, and we do say this is new 2 in 1986: there is, for the first time, form of one-off 3 compounding because what interest is being paid upon is 4 the proved debt and the proved debt includes principal 5 and interest up to the date of the winding up. 6 MR JUSTICE DAVID RICHARDS: Yes. 7 MR ZACAROLI: That was not the case in companies -- under 8 companies liquidation before. It was simply a remission 9 to your contractual rights. On a proper analysis it 10 wasn't the case in bankruptcy prior to 1883 either. Of 11 course these particular changes had already happened in 12 bankruptcy some 100 years previously. 13 MR JUSTICE DAVID RICHARDS: Yes. 14 MR ZACAROLI: But what I'm detailing here is the differences 15 from creditors' contractual rights. 16 MR JUSTICE DAVID RICHARDS: Yes. 17 MR ZACAROLI: There are other respects in which the rights 18 here are potentially different from contractual rights. 19 Whether these are good points or not will depend upon 20 my Lord's answer to subsequent questions. 21 MR JUSTICE DAVID RICHARDS: Right. 22 MR ZACAROLI: But, for example, in relation to future debts, 23 it is common ground amongst all parties in relation to 24 issue 8 that where a dividend is payable on a future 25 debt after the time at which that debt has fallen due</p> <p style="text-align: center;">Page 28</p>

<p>1 for payment there is no discounting back on the value of 2 that debt to the date of administration for the purposes 3 of dividend. So a £100 debt due in three years' time, 4 if there's a first and final dividend paid three years 5 and one day after the administration, the creditor 6 receives £100. If the answer to question 8 is as the 7 administrators and we say it is, interest is payable 8 from the date of administration. That could never have 9 been the position absent an administration. 10 Sorry, it is us and them. 11 MR JUSTICE DAVID RICHARDS: Yes. 12 MR ZACAROLI: Similarly, on question 7, depending on 13 my Lord's answer to that question -- which is, when does 14 interest begin to run in relation to a contingent 15 debt? -- if on this one we are wrong and on this we side 16 with the administrators, if we're wrong on that, then 17 interest is payable from the date of administration, 18 even though, under -- absent the insolvency, that could 19 never have been the case. You couldn't get interest 20 until the debt has fallen due. So two other potential 21 ways in which creditors' contractual rights have 22 changed. 23 Lest it be said that some of these benefits could 24 have been obtained by creditors going off and getting 25 a judgment, not true necessarily. It depends.</p> <p style="text-align: center;">Page 29</p>	<p>1 MR JUSTICE DAVID RICHARDS: Very well. 2 MR ZACAROLI: It's easier to understand some of our points 3 there once I have been through the rest of the 4 submissions. 5 So now looking at what the rule actually requires to 6 be done, and I've made these points briefly in opening 7 and actually making them more extensively doesn't take 8 much longer. We say as a matter of construction the 9 rule does not permit interest to be paid to creditors on 10 the basis that prior dividends are treated as having 11 discharged interest before principal. What the rule 12 does is it directs the surplus to be applied first only 13 when all the proved debts have been paid in full; 14 secondly, at a defined rate, minimum 8 per cent, on 15 a defined sum. The defined sum is the amount of the 16 proved debt on the basis that's now been paid. 17 MR JUSTICE DAVID RICHARDS: Yes. 18 MR ZACAROLI: Then for a defined period. The defined 19 period, leaving aside any wrinkles about contingent and 20 future debts for a moment, leading that aside, the 21 defined period is the date between the date of 22 administration and the date or dates on which the debt 23 was in fact paid in whole or part. We get that from the 24 word "periods", periods of the debts outstanding. That 25 caters for the fact that there will be in many cases</p> <p style="text-align: center;">Page 31</p>
<p>1 A creditor with a debt denominated in a foreign 2 currency, for example, would not get Judgments Act rate 3 of interest on that debt. They would get a commercial 4 rate, and not true of course in relation to future or 5 contingent debts. You can't get a judgment with 6 interest before the date that the debt's fallen due. 7 MR JUSTICE DAVID RICHARDS: Yes. 8 MR ZACAROLI: So the overall point we make here is that 9 there is a bundle of rights given by rule 2.88 which 10 substantially alter, for better, and potentially worse, 11 the pre-existing rights of creditors against the solvent 12 debtor. The only concession to the contractual rights 13 is the rate point, which I've already dealt with, 14 although we say this as well: the fact that the 15 draughtsman has identified one particular facet of 16 contractual rights, namely the rate, and decided to 17 incorporate that, but otherwise not adopt a remission to 18 the contractual rights, would support our view that 19 actually that's all that comes in from the contractual 20 world from the non-insolvency world; you look at this 21 rule alone to determine what's payable. 22 Just in passing, one question posed: does the rate 23 in 2.88(9) incorporate the right to appropriate on 24 Bower v Marris basis? I'll deal with that later, but we 25 say "no".</p> <p style="text-align: center;">Page 30</p>	<p>1 interim dividends, so the debt will cease to be 2 outstanding in part before it ceases to be outstanding 3 in whole. 4 The phrase "for the period during which they have 5 been outstanding" must mean up until the date the 6 dividend is finally paid because the relevant surplus is 7 that remaining after payment of the debts proved. What 8 has to have been outstanding is those debts proved. 9 I don't think there's disagreement about this. I think 10 everyone accepts that's what the word must mean there. 11 Now, to apply the Bower v Marris approach to 12 calculating interest, if that's what it is, would 13 require the following. It requires an assumption to be 14 made that what has been paid to date is statutory 15 interest already, not the proved debt, or at least not 16 just the proved debt. 17 Secondly, it requires the proved debt to be treated 18 as if it hasn't been paid in full. 19 Thirdly, it permits interest to be paid long after 20 the proved debt has in fact been paid in full. 21 Fourthly, it requires that what is being paid 22 pursuant to the rule is in fact the proved debt itself 23 and not interest. 24 We say these are all simply incompatible with the 25 rule as we have noted.</p> <p style="text-align: center;">Page 32</p>

<p>1 Just to take a very simple example, to put that -- 2 give that some colour. Imagine a proved debt of £100. 3 It's outstanding for five years after the date of 4 administration. After five years there will be £40 5 interest owing at 8 per cent a year. The proved debt is 6 then paid in full, so £100 is paid after five years. 7 There is then a further delay of two years before 8 there's sufficient surplus to pay any interest. 9 Interest now amounts -- well, on the other side's case, 10 the Senior Creditor Group's case, the £100 is taken to 11 have discharged £40 of interest and £60 of principal, 12 leaving £40 principal unpaid and further interest of 13 £6.40. So the £20 which is then payable -- of that £20, 14 £6.40 is paid in relation to interest accruing since the 15 date that the dividend was actually paid and the 16 remainder, £13.60, is used to discharge such part of the 17 outstanding proved debt itself. 18 So, first of all, one is paying interest for a lot 19 longer after the date the dividend was finally paid and 20 you're paying something which isn't interest, you're 21 paying the proved debt. 22 Now, it really is that simple, my Lord, in terms of 23 construction. We haven't really, with respect, heard 24 a response to that on the meaning of the words. The 25 other side's cases, York's and Senior Creditor Group's</p> <p style="text-align: center;">Page 33</p>	<p>1 included a quite lengthy passage on the appropriate 2 rules. 3 MR JUSTICE DAVID RICHARDS: Yes. 4 MR ZACAROLI: I'm not going to take my Lord through those. 5 To the extent that it's necessary, Mr Trower will do 6 that. I just make the following very short point, that 7 no case has construed the rule we are considering or 8 anything substantially like it. Thus, there is no 9 authority which has any bearing on the interpretation of 10 rule 2.88(7) for that reason. In fact, as I will hope 11 to make good in going through the authorities, none of 12 the cases are in fact construing a statutory rule as to 13 how interest from a surplus should be calculated at all. 14 They are all concerned with something else, which is 15 this rule of appropriation. 16 There is not a single case and not a single writer 17 that anyone has found writing on the regime since 1986, 18 which is now nearly 30 years, that has suggested 19 rule 2.88(7) works in this way, in the Bower v Marris 20 way. Equally, no one has suggested it works the other 21 way. It hasn't been considered; I accept that, but it 22 is telling that no one has considered this point before. 23 My learned friend was taken to a sentence in 24 a footnote in Gore-Browne. It's worth just looking at 25 that again. It is in bundle 2, I believe. It's tab 7.</p> <p style="text-align: center;">Page 35</p>
<p>1 cases, we say are remarkably thin in responding to this 2 argument. Their case on construction starts we say from 3 a peculiar position and involves three basic 4 propositions. These are set out by my learned friend 5 Mr Dicker in the first day's transcript, page 63 for 6 my Lord's note. 7 The three points they make are, first of all, that 8 features of rule 2.88 on which we rely were also 9 features of the previous regimes. Secondly, the 10 arguments we make were advanced and rejected under the 11 previous regimes. Thirdly, under the prior regimes the 12 courts construed the statutory scheme as providing 13 a mode of calculation for interest which proceeded on 14 the basis that dividends were treated as notionally 15 discharging interest before principal. 16 Now, again, it will be more helpful, I submit, to 17 deal with the answer to those fully once I've been 18 through all the cases, but, in short, we say all three 19 propositions are wrong. The previous regimes were 20 fundamentally different and, as I pointed out in my 21 overview at the beginning, SCG and York's case 22 misconstrues what the rule in Bower v Marris was all 23 about. 24 So far as the principles of statutory construction 25 are concerned, the administrators in their skeleton have</p> <p style="text-align: center;">Page 34</p>	<p>1 MR JUSTICE DAVID RICHARDS: Yes. 2 MR ZACAROLI: The relevant passage is on page -- the numbers 3 are obscured but it's the page after 59-26. 4 MR JUSTICE DAVID RICHARDS: Yes. 5 MR ZACAROLI: Paragraph 18F and the sentence that the 6 footnote relates to is that beginning five lines down or 7 six lines down: 8 "Such interest is itself provable as part of the 9 debt to the extent that it is payable in respect of 10 a period preceding the commencement of the liquidation." 11 So the text is dealing with pre-administration or 12 liquidation interest. 13 MR JUSTICE DAVID RICHARDS: Yes. 14 MR ZACAROLI: The footnote refers to insolvency rule 4.93(1) 15 which is indeed dealing with pre-insolvency interest. 16 MR JUSTICE DAVID RICHARDS: Yes, I see. 17 MR ZACAROLI: So it's the prohibition -- sorry, it's 18 allowing the proof in relation to pre-administration 19 interest. 20 MR JUSTICE DAVID RICHARDS: So the equivalent of 2.88 -- 21 MR ZACAROLI: -- is 2.88(1). 22 MR JUSTICE DAVID RICHARDS: Sorry, can you just repeat that? 23 MR ZACAROLI: The equivalent for administration is 24 rule 2.88(1). 25 MR JUSTICE DAVID RICHARDS: What is the equivalent of -- for</p> <p style="text-align: center;">Page 36</p>

<p>1 the statutory interest?</p> <p>2 MR ZACAROLI: I see. Ah, that's section 189, I believe.</p> <p>3 MR JUSTICE DAVID RICHARDS: Is it?</p> <p>4 MR ZACAROLI: Yes. That's in the Act.</p> <p>5 MR JUSTICE DAVID RICHARDS: Thank you.</p> <p>6 MR ZACAROLI: Yes, 189, sub-paragraph 2 and then 4 is the</p> <p>7 rate.</p> <p>8 MR JUSTICE DAVID RICHARDS: I see. In Gore-Browne they deal</p> <p>9 with further down the page.</p> <p>10 MR ZACAROLI: Yes.</p> <p>11 MR JUSTICE DAVID RICHARDS: Yes, I see.</p> <p>12 MR ZACAROLI: So we would suggest that the authorities of</p> <p>13 the sentence in the footnote is somewhat diminished by</p> <p>14 the understanding of its author that it was dealing with</p> <p>15 provable interest.</p> <p>16 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>17 MR ZACAROLI: In a sense, it's irrelevant for provable</p> <p>18 interest because we know interest stops running at the</p> <p>19 date of the bankruptcy or winding up or administration,</p> <p>20 so the only relevance of knowing to which part interest</p> <p>21 or principal was the dividend first payable will be for</p> <p>22 the benefit of a creditor who has some tax interest in</p> <p>23 that. That's likely the only circumstances because</p> <p>24 interest doesn't keep running so it's irrelevant -- the</p> <p>25 proved debt can't increase in value because dividends</p> <p style="text-align: center;">Page 37</p>	<p>1 Humber Ironworks.</p> <p>2 MR JUSTICE DAVID RICHARDS: Quite.</p> <p>3 MR ZACAROLI: He took my Lord to Wight v Eckhardt. It's</p> <p>4 worth looking at that briefly again. That can be found</p> <p>5 in bundle 1D at tab 132. He read to you the passage at</p> <p>6 paragraph 27 that Lord Hoffmann referred to</p> <p>7 Humber Ironworks and Lines Brothers in paragraphs 23</p> <p>8 through 26. Perhaps my Lord will just remind yourself</p> <p>9 of paragraphs 23 to 26.</p> <p>10 MR JUSTICE DAVID RICHARDS: Certainly. (Pause)</p> <p>11 Yes.</p> <p>12 MR ZACAROLI: So Humber Ironworks, the "different" point, is</p> <p>13 the different Lines Brothers case altogether.</p> <p>14 My Lord, my final point on construction is this,</p> <p>15 that we saw that one of the aims of the Cork Committee</p> <p>16 was simplicity and certainty. I am going to come back</p> <p>17 to deal with complications that arise if Bower v Marris</p> <p>18 is included only for some creditors within 2.88(7) and</p> <p>19 the problems that creates, but actually there's a wider</p> <p>20 point to be made about the lack of certainty and</p> <p>21 simplicity which is created if Bower v Marris is</p> <p>22 applicable at all. This arises because the essence of</p> <p>23 the Bower v Marris approach is that interest remains</p> <p>24 outstanding after the date the final dividend has been</p> <p>25 paid, potentially indefinitely.</p> <p style="text-align: center;">Page 39</p>
<p>1 are appropriated towards interest first because interest</p> <p>2 must stop running at the date of bankruptcy.</p> <p>3 MR JUSTICE DAVID RICHARDS: It could be relevant to a claim</p> <p>4 against a co-obligor.</p> <p>5 MR ZACAROLI: Indeed could be, yes. Yes, as we say, none of</p> <p>6 this deals --</p> <p>7 MR JUSTICE DAVID RICHARDS: Was Joint Stock Discount</p> <p>8 Company, I forget, concerned with co-obligors, or not?</p> <p>9 MR ZACAROLI: I just have to remember which one it was. One</p> <p>10 of them was.</p> <p>11 MR JUSTICE DAVID RICHARDS: The reference is to number 2.</p> <p>12 (Pause)</p> <p>13 MR ZACAROLI: Yes, this is the two estates one.</p> <p>14 MR JUSTICE DAVID RICHARDS: It is. So, actually, understood</p> <p>15 in that context, the point made in the footnote is</p> <p>16 a perfectly sensible point.</p> <p>17 MR ZACAROLI: Yes.</p> <p>18 MR JUSTICE DAVID RICHARDS: But it's not actually concerned</p> <p>19 with post-liquidation interest.</p> <p>20 MR ZACAROLI: Correct, yes.</p> <p>21 My learned friend Mr Dicker yesterday then referred</p> <p>22 to the fact that there are a number of authorities since</p> <p>23 1986 which have cited Humber Ironworks or</p> <p>24 Lines Brothers, although he frankly conceded to my Lord</p> <p>25 that none of those cases considered this point on the</p> <p style="text-align: center;">Page 38</p>	<p>1 Now, before -- well, in describing the problems that</p> <p>2 gives rise to, it is helpful to look at a very clear</p> <p>3 exposition in one of the Australian cases as to why it</p> <p>4 is that back in the 19th century the judges adopted</p> <p>5 a rule that interest stopped running at the date of</p> <p>6 bankruptcy or winding up. It's because it creates</p> <p>7 complications, if you're trying to make a pari passu</p> <p>8 distribution thereafter, if you don't know when interest</p> <p>9 stops running. I will be taking my Lord to the case in</p> <p>10 more detail later on but can I for the moment pick up</p> <p>11 a passage in it.</p> <p>12 It's MacKenzie v Rees, bundle 1B, tab 71. It's</p> <p>13 a case from 1941. It's in the High Court of Australia</p> <p>14 and much of the case is taken up with a debate as to</p> <p>15 whether the relevant debts were interest-bearing or not.</p> <p>16 The case is authority -- all the judges in the case</p> <p>17 agreed -- for the proposition that interest stops</p> <p>18 running at the date of the winding up or the bankruptcy,</p> <p>19 as in England. It's not a Bower v Marris case at all,</p> <p>20 but it does deal with that basic rule.</p> <p>21 Page 9 in the judgment of Mr Justice Dixon, just the</p> <p>22 second paragraph, a third of the way down the page, he</p> <p>23 says:</p> <p>24 "The principal rule, namely that excluding</p> <p>25 intermediate interest ...(reading to the words)... might</p> <p style="text-align: center;">Page 40</p>

<p>1 lead to many difficulties."</p> <p>2 He then cites Browne v Wingrove.</p> <p>3 Then he says:</p> <p>4 "The principle is accepted in the United States of</p> <p>5 America and the principle upon ...(reading to the</p> <p>6 words)... of the estate would be seriously complicated.</p> <p>7 One must not forget that 2.88(7) doesn't operate</p> <p>8 only where -- I suggest rarely where -- there is so much</p> <p>9 surplus that everyone gets paid in full, certainly in</p> <p>10 one go. Indeed, sub-rule 8 recognises that by saying</p> <p>11 that all interest payable under paragraph 7 ranks</p> <p>12 equally whether or not the debts on which it's payable</p> <p>13 rank equally. So there is another form of pari passu</p> <p>14 distribution of statutory interest. So all the</p> <p>15 arguments that led to the interest stopping at the date</p> <p>16 of bankruptcy apply with equal force to requiring</p> <p>17 interest to stop accruing at the date of final dividend</p> <p>18 being paid because only then do you have fixed and</p> <p>19 ascertained claims to interest which can be distributed</p> <p>20 on a pari passu basis.</p> <p>21 Precisely the same argument works to stop interest</p> <p>22 at a compound rate compounding beyond that date.</p> <p>23 My Lord, I'm about to move on to the second topic,</p> <p>24 that is the rule in Bower v Marris, so it might be</p> <p>25 a convenient moment.</p> <p style="text-align: center;">Page 41</p>	<p>1 of appropriation because it mean the creditor's right to</p> <p>2 appropriate remains.</p> <p>3 The principles of appropriation are well-known.</p> <p>4 They are that where two or more liabilities are due from</p> <p>5 the debtor, first of all, the debtor can choose which</p> <p>6 one he is paying. The creditor may agree to accept that</p> <p>7 or not.</p> <p>8 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>9 MR ZACAROLI: But if the debtor does not appropriate, then</p> <p>10 it's up to the creditor to decide how to appropriate the</p> <p>11 payments. In the absence of appropriation by either,</p> <p>12 the law applies certain presumptions and always has</p> <p>13 done.</p> <p>14 In the case of principal and interest, it has long</p> <p>15 been the case that if there's no appropriation the</p> <p>16 starting presumption is that it's appropriated towards</p> <p>17 interest first because that's in the creditor's best</p> <p>18 interest usually. That's a relevant question wherever</p> <p>19 the distribution of interest from an insolvency estate</p> <p>20 is by reference to the contractual rights of the</p> <p>21 creditors alone, but irrelevant under 2.88(7) for the</p> <p>22 reasons we've already given.</p> <p>23 Although I said the principles of appropriation are</p> <p>24 well-known, it may be worth just looking at those for</p> <p>25 a moment to see how they have applied both in two</p> <p style="text-align: center;">Page 43</p>
<p>1 MR JUSTICE DAVID RICHARDS: I think that would be</p> <p>2 a convenient moment. I'll rise now for five minutes.</p> <p>3 (11.43 am)</p> <p>4 (Short break)</p> <p>5 (11.48 am)</p> <p>6 MR ZACAROLI: My Lord, I believe the consensus in relation</p> <p>7 to Monday is that we start at 9.30 and continue until</p> <p>8 2.00 with a half hour break after two hours.</p> <p>9 MR JUSTICE DAVID RICHARDS: Yes. Fine. Let's do that. The</p> <p>10 only thing I was just thinking about in the break was at</p> <p>11 2 o'clock they are going to be setting up chairs and</p> <p>12 things outside. We will say at the moment we'll do</p> <p>13 exactly that, but it may be that we'll have to rise</p> <p>14 a bit earlier than 2 o'clock because I know they are</p> <p>15 going to be setting things up out there. Fine. Good.</p> <p>16 Thank you very much indeed.</p> <p>17 MR ZACAROLI: My Lord, turning to the second topic which</p> <p>18 will be the largest of them, Bower v Marris and its</p> <p>19 application throughout the English-speaking world.</p> <p>20 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>21 MR ZACAROLI: Our core propositions, just to remind my Lord</p> <p>22 very quickly, are that the Bower v Marris rule is merely</p> <p>23 that payments which are required to be made by law from</p> <p>24 an estate, such as a bankruptcy estate, are not thereby</p> <p>25 appropriated either way. That is an aspect of the law</p> <p style="text-align: center;">Page 42</p>	<p>1 different debts cases and then in interest and principal</p> <p>2 cases, just a few references. We can start, my Lord,</p> <p>3 with Chitty which is in bundle 2, tab 2. If my Lord</p> <p>4 turns to page 1587 at the bottom of the pages, there's</p> <p>5 a subheading, "B. Appropriation of payments":</p> <p>6 "Where several separate debts are due from the</p> <p>7 debtor to the creditor the debtor may, when making</p> <p>8 a payment, appropriate the money paid to a particular</p> <p>9 debt or debts and if the creditor accepts the payment so</p> <p>10 appropriated he must apply it in the manner directed by</p> <p>11 the debtor. If, however, the debtor makes no</p> <p>12 appropriation when making the payment, the creditor may</p> <p>13 do so."</p> <p>14 Then paragraph 21068, one page on:</p> <p>15 "Appropriation as between principal and interest.</p> <p>16 Where there is no appropriation by either debtor or</p> <p>17 creditor in the case of a debt bearing interest, the law</p> <p>18 will, unless a contrary intention appears, apply the</p> <p>19 payment to discharge any interest due before applying it</p> <p>20 to the earliest items of principal."</p> <p>21 So clearly operating on a presumption.</p> <p>22 A couple of authorities. One goes way back before</p> <p>23 Bower v Marris and that's Clayton's case. Clayton's</p> <p>24 case is a very long case. I am only going to take</p> <p>25 my Lord to one paragraph in it. I'm hoping that the</p> <p style="text-align: center;">Page 44</p>

<p>1 principles for which the case stands are well-known.</p> <p>2 MR JUSTICE DAVID RICHARDS: I think so.</p> <p>3 MR ZACAROLI: The part that we're concerned with -- it's in</p> <p>4 bundle 1A at tab 13A. It's one part of a very large</p> <p>5 case called Devaynes v Noble. It's a long report but</p> <p>6 Clayton's case begins being dealt with on page 781 of</p> <p>7 the English reports and the passage is at 791.</p> <p>8 Of course the point here was about whether payment</p> <p>9 were to be appropriated on the basis of "first in first</p> <p>10 out" or some other basis. So that was what the case was</p> <p>11 about.</p> <p>12 One sees that from what the Master of the Rolls says</p> <p>13 at 26 July, page 791; that the principles which are</p> <p>14 being applied are stated very shortly at page 792 in the</p> <p>15 first full paragraph:</p> <p>16 "This state of the case has given rise to much</p> <p>17 discussion ...(reading to the words)... or the priority</p> <p>18 in which they were incurred."</p> <p>19 In the case of a running account, the decision in</p> <p>20 the case was that the presumption is that each payment</p> <p>21 made in is appropriated to the first one out.</p> <p>22 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>23 MR ZACAROLI: So from way before Bower v Marris, the general</p> <p>24 principle is one of relying on presumptions.</p> <p>25 Then, skipping forward a few years to the Mecca in</p> <p style="text-align: center;">Page 45</p>	<p>1 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>2 MR ZACAROLI: My Lord was shown one of the -- a case on</p> <p>3 a similar line yesterday from India.</p> <p>4 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>5 MR ZACAROLI: It's a tax case about appropriation of</p> <p>6 principal or interest.</p> <p>7 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>8 MR ZACAROLI: You will see from the headnote:</p> <p>9 "For the purpose of the Indian Income Tax Act the</p> <p>10 income derived ...(reading to the words)... has not</p> <p>11 credited as a receipt of interest."</p> <p>12 The principles are discussed briefly in the judgment</p> <p>13 of Lord Macmillan at page 157. At the top of the page:</p> <p>14 "Now where interest is outstanding on a principal</p> <p>15 sum due and the creditor ...(reading to the words)... it</p> <p>16 also applies where the income tax officer is concerned."</p> <p>17 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>18 MR ZACAROLI: While we're in this bundle, there's one other</p> <p>19 case which shows that the presumption can be the other</p> <p>20 way in relation to principal and interest. My learned</p> <p>21 friend Mr Smith showed my Lord a debenture trust case.</p> <p>22 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>23 MR ZACAROLI: There's another debenture trust case which in</p> <p>24 fact was referred to in the one he looked at. This case</p> <p>25 is called Smith v Law Guarantee and Trust</p> <p style="text-align: center;">Page 47</p>
<p>1 the 1890s, I think. It's bundle 1A, tab 50.</p> <p>2 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>3 MR ZACAROLI: This is a decision of the House of Lords. The</p> <p>4 headnote reads:</p> <p>5 "When a debtor pays money on account to his creditor</p> <p>6 and makes no ...(reading to the words)... the creditor</p> <p>7 expressed, implied or presumed."</p> <p>8 That point is made good in the judgment of</p> <p>9 Lord Macnaghten at page 293, towards the bottom of the</p> <p>10 page:</p> <p>11 "Now, my Lords, there can be no doubt what the law</p> <p>12 of England is on this subject ..."</p> <p>13 It repeats the same principle there.</p> <p>14 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>15 MR ZACAROLI: Then 294, seven lines down, at the end of the</p> <p>16 line:</p> <p>17 "Where the election is with the creditor it is</p> <p>18 always his intention ...(reading to the words)... there</p> <p>19 are no circumstances pointing in the opposite</p> <p>20 direction."</p> <p>21 The cases I've shown my Lord were not cases where</p> <p>22 the appropriation was between principal and interest,</p> <p>23 but the next case is. The next case is at bundle 1B,</p> <p>24 tab 66. It's Income Tax v Maharajadhiraja. It's</p> <p>25 a Privy Council appeal from India.</p> <p style="text-align: center;">Page 46</p>	<p>1 Society Limited. It is at tab 54A of bundle 1B. The</p> <p>2 facts of this case were that the trust debenture by its</p> <p>3 terms required payments to be appropriated towards</p> <p>4 interest first before capital.</p> <p>5 MR JUSTICE DAVID RICHARDS: Right.</p> <p>6 MR ZACAROLI: Payments were made. They were made,</p> <p>7 however -- it was held, pursuant to an order of the</p> <p>8 court, but the subsequent court decided that those</p> <p>9 payments had not been appropriated by that order in any</p> <p>10 particular manner. The judge at first instance held,</p> <p>11 and I don't believe this was appealed but it's certainly</p> <p>12 common ground in the Court of Appeal, that although the</p> <p>13 contract required the payments to be appropriated</p> <p>14 towards interest first, that was a provision solely for</p> <p>15 the benefit of the debenture holders and they could</p> <p>16 therefore waive it. When it transpired that company was</p> <p>17 insolvent, it remained insolvent, it was in their</p> <p>18 interests to appropriate towards capital because an</p> <p>19 appropriation towards interest gave rise to a tax</p> <p>20 liability.</p> <p>21 MR JUSTICE DAVID RICHARDS: I see.</p> <p>22 MR ZACAROLI: So that was the point in the case.</p> <p>23 MR JUSTICE DAVID RICHARDS: Yes, I see.</p> <p>24 MR ZACAROLI: The Court of Appeal decided that</p> <p>25 notwithstanding that term in the contract, since there</p> <p style="text-align: center;">Page 48</p>

<p>1 hadn't been an appropriation because this was made by 2 operation of law, it remained for the creditors to 3 appropriate. They didn't bother to ask the debenture 4 holders themselves because they took the view that they 5 would only answer one way, namely it's in our interests 6 to appropriate towards capital, so let's please do that. 7 MR JUSTICE DAVID RICHARDS: Yes. 8 MR ZACAROLI: I needn't read the headnote. I've described 9 the case, I hope, sufficiently. 10 Page 571 of the report is reciting what happened in 11 front of the judge. At the bottom of the page, it says: 12 "Mr Justice Byrne held that the provisions in the 13 trust deed for payment ...(reading to the words)... in 14 their hands it would after be treated differently." 15 Then in the Court of Appeal 16 Lord Justice Vaughan Williams, at page 574, middle 17 paragraph, next to the second hole-punch: 18 "In this state of things these orders of 15 June 19 1896 and 21 July 1897 ...(reading to the words)... 20 payments should not be immediately appropriated." 21 So the court was considering earlier orders which 22 may or may not have amounted to an appropriation. But 23 they decided they hadn't: 24 "If the payments had been made simply generally on 25 account, it may well be ...(reading to the words)..."</p> <p style="text-align: center;">Page 49</p>	<p>1 a surplus. 2 MR JUSTICE DAVID RICHARDS: No. 3 MR ZACAROLI: There is also no doubt in this case that the 4 entitlement to post-bankruptcy interest was based purely 5 on such rights as the creditors had to interest against 6 the debtor, assuming it to be solvent. It's all about 7 contractual rights or similar. 8 There's a passage that my learned friend read to you 9 but I want to highlight at page 50 which I'll come back 10 to the point here later on in my submissions, but what 11 he says at page 50, about four paragraphs up from the 12 bottom: 13 "All bankrupts are considered in some degree as 14 offenders ...(reading to the words)... is given for 15 delay of payment." 16 I'll come back to that very important background 17 context for these cases later on. 18 Then the actual decision in the case, I can 19 highlight two passages which get to the crux of it. The 20 judgment takes us through all of the old 21 Bankruptcy Acts, but at page 51 he's dealing with the 22 Act of Elizabeth 13 which is an Act prior to there being 23 any discharge for the bankrupt. So there was no 24 discharge for the bankrupt at this stage. Page 51, the 25 first full paragraph:</p> <p style="text-align: center;">Page 51</p>
<p>1 should now be attributed to capital." 2 MR JUSTICE DAVID RICHARDS: Yes. 3 MR ZACAROLI: Now, I am turning to the application of this 4 principle in the bankruptcy cases. We start with 5 Bromley v Goodere. 6 Again, my Lord has seen this decision so I can take 7 it, I hope, quite quickly. Just a couple of points 8 about it. First of all, there is of course no 9 discussion anywhere in the decision, the judgment of 10 Bromley v Goodere about the appropriation of payments or 11 and order in which payments should be dealt with. 12 That's something which appears only in the order itself. 13 MR JUSTICE DAVID RICHARDS: Yes. 14 MR ZACAROLI: In fact, there is no analysis in any case from 15 the 19th century in relation to bankruptcy about how 16 this works, other than in Bower v Marris. That is the 17 only place one finds any analysis of the topic. 18 The other point to mention of course is that there 19 was no statutory provision at all dealing with interest 20 post-the date of bankruptcy at the time of 21 Bromley v Goodere. So it's entirely judge-made law. 22 MR JUSTICE DAVID RICHARDS: Yes. 23 MR ZACAROLI: So whatever the rule is here, it cannot have 24 been a rule as to the construction of a statutory 25 provision dealing with the payment of interest from</p> <p style="text-align: center;">Page 50</p>	<p>1 "The Act goes on to take notice of the surplus 2 ...(reading to the words)... from him again by the 3 creditors." 4 Then over the page he deals with the Act of Ann 4th 5 and 5th which introduced the concept of a discharge. At 6 page 52, the first full paragraph, he says: 7 "Consider, therefore, the effect of the discharge; 8 the certificate is not to operate as a discharge of the 9 fund before vested in the assignees but to extend only 10 to any remedy to be taken against the person of 11 a bankrupt of his future effects." 12 In essence, therefore, it leaves -- the creditors 13 are free to claim against the surplus, precisely what 14 they would have claimed against the bankrupt before the 15 discharge. That's the only difference it makes. On any 16 view one is dealing here with a case where one requires 17 full satisfaction of creditors before anything can go to 18 the bankrupt. 19 You see that in fact from the order itself, at the 20 top of page 53, just before the paragraph break: 21 "The requirement is pari passu all creditors until 22 they receive full satisfaction." 23 MR JUSTICE DAVID RICHARDS: Yes. 24 MR ZACAROLI: As I mentioned, no other case contains any 25 analysis of the point until you get to Bower v Marris.</p> <p style="text-align: center;">Page 52</p>

<p>1 So can we go then to Bower v Marris. I don't think 2 I need to show my Lord the statutory provision again. 3 My Lord is now well familiar with it. 4 MR JUSTICE DAVID RICHARDS: Hmm, hmm. 5 MR ZACAROLI: Bower v Marris is at tab 17 of this bundle 6 MR JUSTICE DAVID RICHARDS: Yes. 7 MR ZACAROLI: It's a small point but worth noting that the 8 case is authority for the question of appropriation as 9 between -- as it arose in the claim by the creditor 10 against the solvent co-obligor. So everything else is 11 technically obiter. And the headnote refers to it as 12 (inaudible), but I'm not taking much of a point on that. 13 It's clearly well-reasoned judgment, but it's worth 14 noting it is actually obiter dicta. 15 Turning to the decision -- the judgment of the 16 Lord Chancellor, Lord Cottenham. I am going to pick up 17 a number of points on the way through this judgment so 18 I'm not going to read all of it, but the first point to 19 notice is that when he refers to the argument that there 20 should be appropriation towards interest first, at the 21 very beginning of the judgment, at the bottom of 22 page 354, over to the top of page 355, where he says: 23 "... insist the amount is to be calculated by 24 applying the amount ...(reading to the words)... 25 discharge pro tanto of the principal."</p> <p style="text-align: center;">Page 53</p>	<p>1 discharge to part of the principal whilst any interest 2 remained due." 3 It's an implicit recognition that it's for the 4 creditor to decide that any creditor would do it that 5 way. 6 The third point to note is what the argument 7 advanced was, and this is very important for the next 8 point, which is when the Lord Chancellor says: 9 "The doctrine of appropriation has nothing to do 10 with it", he's not saying the doctrine of appropriation 11 has nothing to do with this case. What it has nothing 12 to do with is the argument that is being immediately 13 presented to him. We'll see how that works. 14 The middle paragraph, page 355, he says: 15 "The question so far as it's a question of principle 16 turns upon the accuracy ...(reading to the words)... was 17 upon each payment discharged." 18 So that's the argument that he's faced with. 19 His response: 20 "In the first place as this mode of payment is 21 regulated by Acts of Parliament, the doctrine of 22 appropriation which is founded upon the intention 23 expressed or implied of a debtor or creditor cannot have 24 any place in the consideration of the present question." 25 The present question being have the payments so made</p> <p style="text-align: center;">Page 55</p>
<p>1 He says: 2 "This is no doubt the ordinary mode of calculation." 3 Now, it's clear, we submit, that what he's saying 4 there is the ordinary mode of calculation in accordance 5 with the general principles of law, not some ordinary 6 mode of calculation in bankruptcy, because he has not 7 yet referred to any authority and the whole of this part 8 of the judgment is in fact argued or reasoned as 9 a matter of principle because he doesn't turn to 10 authority until the top of page 358, where he says: 11 "If there had been no decision on this subject, 12 I should have thought these reasons conclusive in favour 13 of the mode of calculation." 14 He then turns to look at cases like 15 Bromley v Goodere. 16 He goes on to say that it is the general course of 17 dealing in cases of mortgages, bonds and other 18 securities; emphasising that he is talking here about 19 a general principle of law applicable where a debtor 20 owes money to his creditor. 21 The second point to note is that he clearly 22 understands that this is -- the general law operates on 23 the basis of a presumption as to the creditor's interest 24 because he goes on to say immediately: 25 "No creditor would apply any payment to the</p> <p style="text-align: center;">Page 54</p>	<p>1 already been appropriated towards principal? No, 2 because they're made in regulation of Acts of 3 Parliament. 4 MR JUSTICE DAVID RICHARDS: Right. 5 MR ZACAROLI: As put later by Lord Justice Selwyn, in 6 process of law. It's the same concept. 7 He then goes on to recognise that the question of 8 appropriation is therefore a matter of entitlement for 9 the creditor. So he says: 10 "The estate of the obligor under administration is 11 liable to pay all the ...(reading to the words)... and 12 he is entitled [that's the creditor] to apply all 13 payments on account to the interest due before he would 14 be bound to apply any part of it towards the discharge 15 of the principal." 16 That is simply a classic statement of the state of 17 law as it then existed under the general rules of 18 appropriation. 19 He confirms or it can be confirmed that that is what 20 he is talking about at page 357, when, about five lines 21 down, at the end of the line, he asks rhetorically: 22 "Why should such payments [that is, made pursuant to 23 the Act] have a different effect than they would have if 24 made by a solvent obligor?" 25 If made by a solvent obligor, they could only have</p> <p style="text-align: center;">Page 56</p>

<p>1 had the effect of leaving the creditor with the option 2 of appropriating. 3 MR JUSTICE DAVID RICHARDS: Yes. 4 MR ZACAROLI: Now, the next point to note from this decision 5 is that it is essential to the reasoning of the case 6 that the creditor had an existing interest-bearing debt. 7 First of all, if you look at the top of page 356, the 8 passage we have already looked at, where he talks about 9 the entitlement of the creditor: 10 "... is to apply all payment on account to the 11 interest due." 12 Secondly, when he's talking about the rule of 13 convenience at the bottom of page 356, that interest 14 stops at the date of commission, about eight lines from 15 the bottom, there's a passage which begins: 16 "The trains stops at the date of the commission and 17 though subsequent interest becomes due it is not 18 provable under the commission." 19 Again, only talking about interest which is pursuant 20 to a pre-existing right. 21 Then at the top of page 357 he makes it absolutely 22 clear: 23 "The bankrupt continues indebted for the principal 24 and interest accrued since the commission." 25 MR JUSTICE DAVID RICHARDS: Yes.</p> <p style="text-align: center;">Page 57</p>	<p>1 bottom of page 355, "the doctrine of appropriation 2 cannot have any place in the consideration of the 3 present question", have been taken out of context by 4 York and the Senior Creditor Group, have been assumed to 5 mean that the case itself has nothing to do with the 6 doctrine of appropriation. And that is wrong. They are 7 very clearly directed only at the argument that he's 8 been presented with at that time. 9 My learned friend Mr Dicker referred to a sentence 10 or a line on page 358, in the middle of page 358, where 11 he refers to Bromley v Goodere and the order that was 12 made in that case. So the reference to 13 Bromley v Goodere is next to the first hole-punch. 14 MR JUSTICE DAVID RICHARDS: Yes. 15 MR ZACAROLI: "The order appears to have been framed by 16 himself...(reading to the words)... justice of the case 17 without the aid which the statute now affords." 18 My Lord, the only thing he can be referring to there 19 is that the statute now provides that there is a right 20 to interest payable once all the debts have been paid to 21 creditors. 22 MR JUSTICE DAVID RICHARDS: Yes. 23 MR ZACAROLI: That simply wasn't there at the time of 24 Lord Hardwicke's decision. So he isn't saying, "I'm now 25 construing this statute as giving this right to interest</p> <p style="text-align: center;">Page 59</p>
<p>1 MR ZACAROLI: He asks why should it be different with 2 a solvent obligor? That can only be relevant to whether 3 in relation to the solvent obligor there's an obligation 4 to pay interest. 5 Then at the bottom of the page, 357, again, the 6 middle of that paragraph, he talks about interest 7 stopping at the date of the commission because it's 8 supposed the estate will be deficient. So interest can 9 only be stopped if it's already due or otherwise would 10 have been due. 11 Then, finally, at the bottom of the page: 12 "The creditor in that case will not have received 13 interest upon his debt to the same extent as he would if 14 there had been no bankruptcy. If there had been no 15 bankruptcy he would only receive interest if he was 16 entitled to it." 17 So it is absolutely clear that the reasoning in this 18 case is founded upon the fact the creditor has a right 19 to interest and therefore in the background that 20 interest is accruing and that creditor has a right of 21 appropriation in relation to payments made to him at 22 a time when both principal and interest are owing under 23 his contract. 24 MR JUSTICE DAVID RICHARDS: Yes. 25 MR ZACAROLI: So, in short, we submit that the words at the</p> <p style="text-align: center;">Page 58</p>	<p>1 in a way which must be calculated in this way". That's 2 not what is happening here. He's simply saying the 3 creditor remains entitled to his rights and in that 4 context the general law give this right of appropriation 5 and there has been no appropriation so far. 6 The final point that I want to pick up on from the 7 case is at page 359, the second paragraph on that page: 8 "It is true that in certain cases the dividend has 9 been considered...(reading to the words)... in justice 10 and defeat the contract between the parties." 11 Now, my learned friend Mr Dicker yesterday accepted 12 that this rule in Bower v Marris is always subject to 13 there being a contrary agreement between the parties. 14 Now, that contrary agreement is not one which is an 15 agreement reached after bankruptcy; it's a contrary 16 indication in the agreement between the parties. So in 17 a case where the debtor and creditor have previously 18 agreed that all payments shall be appropriated 19 pari passu towards interest on the principal outstanding 20 at any time, that clearly governs. 21 MR JUSTICE DAVID RICHARDS: Yes. 22 MR ZACAROLI: Which emphasises that this is a question of 23 general law. That's irrelevant unless one is actually 24 saying that what one is doing is looking to see what the 25 general law of appropriation is. It's only then that it</p> <p style="text-align: center;">Page 60</p>

<p>1 becomes relevant to the contract and creates a different 2 outcome.</p> <p>3 My Lord, on the first day, page 88 of the 4 transcript, Mr Dicker said to my Lord that there are -- 5 having looked at Bower v Marris, he said: 6 "There are a very large number of bankruptcy cases 7 I could show your Lordship but I think that's all I need 8 to".</p> <p>9 Now, this chimes with a very eloquent way my learned 10 friend expressed the case throughout, that there is this 11 rule in Bower v Marris as if everyone has known about 12 this rule all along and it's well understood and has 13 always been applied, up until some change happened in 14 1986.</p> <p>15 My Lord, the truth is very different.</p> <p>16 The Bower v Marris judgment was delivered on 17 7 August 1841. It so happens it was a Saturday. They 18 worked much harder in Victorian days. If I may be 19 permitted a little colour, at this point, just a little; 20 the infamous Marshalsea debtors' prison in which 21 Charles Dickens' father had been imprisoned a mere 22 17 years before was still open for business.</p> <p>23 MR JUSTICE DAVID RICHARDS: Right.</p> <p>24 MR ZACAROLI: This is 28 years before bankruptcy becomes 25 decriminalised in 1869.</p> <p style="text-align: center;">Page 61</p>	<p>1 jurisdiction that my Lord has been shown that applies 2 English law -- I'm leaving aside America -- any 3 jurisdiction where the principle has been applied to the 4 distribution of interest from a corporate or personal 5 insolvent's estate, until Lines Brothers.</p> <p>6 MR JUSTICE DAVID RICHARDS: Really?</p> <p>7 MR ZACAROLI: So between Humber Ironworks and 8 Lines Brothers -- I should have made that clear, 9 a period of 100 years -- there is no case when the 10 principle has been applied in the context of the 11 distribution from an insolvent's estate.</p> <p>12 There's a danger here of my Lord being shown a lot 13 of authorities. Those that referred to the 14 Bromley v Goodere, they are all Bower v Marris or prior.</p> <p>15 The rest of the cases my Lord has been shown are from 16 Australia, Canada, Ireland, they are all post-1986. So 17 in asking yourself what was the legislature in England 18 faced with in 1986, was it faced with this long-standing 19 rule that everyone knew about, that this was how you 20 always distributed from a bankruptcy estate? We would 21 suggest absolutely not.</p> <p>22 Moreover, there's no reference to the Bower v Marris 23 case at all or the principle of appropriation in it in 24 any edition of Williams. Williams, the leading 25 bankruptcy textbook for the whole of the 20th century;</p> <p style="text-align: center;">Page 63</p>
<p>1 Now, it's not irrelevant colour because there are 2 two points that spring from this. First of all, as I'll 3 come back to when looking at broader policy and 4 principle arguments, it is very important to look at 5 general statements in the old cases about everyone must 6 be satisfied in full before the bankrupt gets anything 7 in that context. The debtor was regarded as an 8 offender, a criminal, who was deliberately not paying 9 his debts, who was thrown into prison, therefore making 10 it impossible for him to pay his creditors but, 11 nevertheless, being punished for that. That's the 12 context.</p> <p>13 More important for the present moment, since 14 judgment was given in Bower v Marris, on 7 August 1841, 15 neither the case nor the principle of appropriation 16 applied in it has been applied or even referred to in 17 any bankruptcy case in England. You have not been shown 18 one. The parties no doubt between us have been 19 scrabbling around to find any reference to it. There is 20 no bankruptcy case which has applied the principle or 21 even referred to it.</p> <p>22 In fact, leaving aside the Scottish decision of 23 Gourlay v Watson, which wasn't a bankruptcy case but was 24 something similar and was in Scotland anyway, there is 25 no case at all, whether bankruptcy or company, in any</p> <p style="text-align: center;">Page 62</p>	<p>1 not one of its editions contains any reference to it.</p> <p>2 My learned friend Mr Smith refers to two textbooks, 3 one Mr Robson from 1884 and one Mr Wace from 1904, 4 I think it was. The second one is a rather tentative 5 reference to, "It's conceived that this is the way you 6 do it".</p> <p>7 MR JUSTICE DAVID RICHARDS: Right.</p> <p>8 MR ZACAROLI: That book has never seen the light of day 9 since. I'm not sure who Mr Wace was. It's certainly 10 not of the calibre of Williams throughout the rest of 11 the century.</p> <p>12 Mr Robson, then, in 1884 -- my Lord was shown the 13 passage. He says, "As to the old law, this was how it 14 was done under Bower v Marris", I agree it's an 15 ambiguous concept but at least on one view he's talking 16 about what the "old law" was. There is another reason 17 to question the authority of that statement anyway. 18 It's worth just picking the book up at bundle 2, tab 12, 19 page 291.</p> <p>20 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>21 MR ZACAROLI: The footnote G is referable to the text, 22 halfway down the page: 23 "The Act of 1883 also provides if there is any 24 surplus it shall be ...(reading to the words)... on all 25 debts proved in the bankruptcy."</p> <p style="text-align: center;">Page 64</p>

<p>1 It refers to section 40, sub-section 5: 2 "This provision is altered by Bankruptcy Act 1890, 3 section 23" -- 4 MR JUSTICE DAVID RICHARDS: Sorry, where are we? 5 MR ZACAROLI: I am looking at footnote G, section 40, 6 sub-section 5. 7 MR JUSTICE DAVID RICHARDS: Where does it say -- 8 MR ZACAROLI: G is on the left-hand column. 9 MR JUSTICE DAVID RICHARDS: I have that, yes. 10 MR ZACAROLI: So he cites section 40 sub-section 5. He then 11 says: 12 "This provision is altered by the Bankruptcy Act 13 1890, section 23, for the benefit of creditors whose 14 debts carry higher interest that 4 per cent." 15 That's just plainly wrong. 16 MR JUSTICE DAVID RICHARDS: Oh dear. 17 MR ZACAROLI: It's worth -- what he's talking about is in 18 fact the section of the Bankruptcy Act 1890 which became 19 section 66(1) which is about the 5 per cent interest 20 that's capped for proving creditors and then there's an 21 uplift -- they are entitled to the excess as a matter of 22 proof once everyone has been paid in full. I can show 23 my Lord that section very quickly. It's bundle 2 -- 24 bundle 3A, tab 29. Within the tab, it's page 628, 25 section 23 is there set out. You'll see it's exactly</p> <p style="text-align: center;">Page 65</p>	<p>1 applied in the way my learned friends contend, but any 2 rule there may have been had been pretty much forgotten 3 about, apart from Lines Brothers, for over 100 years. 4 MR JUSTICE DAVID RICHARDS: Was Lines Brothers decided 5 before or after the Cork Committee reported? 6 MR ZACAROLI: Afterwards. 7 MR JUSTICE DAVID RICHARDS: Lines Brothers was after? 8 MR ZACAROLI: I'm pretty sure because 1982 is the 9 Cork Report and Lines Brothers number 2 was -- it's 10 reported in 1984 and I'm pretty sure it was decided in 11 1983 or 1984. I am reminded, December 1983, January 12 1984. 13 MR JUSTICE DAVID RICHARDS: That's Lines Brothers? 14 MR ZACAROLI: Lines Brothers number 2. 15 MR JUSTICE DAVID RICHARDS: And the Cork Report was ...? 16 MR ZACAROLI: June 1982. 17 MR JUSTICE DAVID RICHARDS: Because Mr Dicker made the point 18 that David Graham QC was a member of the Cork Committee. 19 If Lines Brothers had been decided before the report, it 20 might have featured. 21 MR ZACAROLI: I see, yes. It is the wrong way round. It 22 makes a very large assumption anyway, or a number of 23 assumptions. 24 MR JUSTICE DAVID RICHARDS: Hmm, hmm. 25 MR ZACAROLI: I am reminded that Mr Graham was also the</p> <p style="text-align: center;">Page 67</p>
<p>1 the same as what becomes section 66(1). I am sorry, 2 it's page 623. 3 MR JUSTICE DAVID RICHARDS: I'm getting there gradually. 4 (Pause) 5 Oh, yes. You mentioned it had come in at this 6 stage. 7 MR ZACAROLI: In re Baughan, the case we looked at, shows 8 that's just about provable interest. 9 So when he goes on to say "as to the mode of 10 calculating interest on the old law", it may be that 11 he's again, rather like the editor of Gore-Browne, not 12 necessarily wrong because he's talking about the 13 provable interest, but, anyway, he's clearly wrong in 14 the first sentence which undermines to some extent the 15 rest. 16 MR JUSTICE DAVID RICHARDS: Yes. 17 MR ZACAROLI: Be that as it may, that and Mr Wace's 18 reference are the only references you will see in any 19 textbook to Bower v Marris throughout that entire 20 period. That is 1880 through to 1986. 21 MR JUSTICE DAVID RICHARDS: Yes. 22 MR ZACAROLI: So when one comes to the question of what 23 policy reason could there have been in 1986 for 24 abolishing the rule in Bower v Marris, well, we question 25 whether there was ever any such rule that was ever</p> <p style="text-align: center;">Page 66</p>	<p>1 editor of Williams. 2 MR JUSTICE DAVID RICHARDS: Was he? Right, along with 3 Mr Muir Hunter, I think. 4 MR ZACAROLI: Yes. 5 Now, I have made the point about no references for 6 100 years, but of course the really important date for 7 that purpose is 1883 because that's the date when 8 there's a significant change in the law relating to 9 bankruptcy in post-administration which -- I've already 10 shown my Lord how that works. 11 MR JUSTICE DAVID RICHARDS: Yes. 12 MR ZACAROLI: Importantly, therefore, the premise of 13 Bromley v Goodere, that creditors must be satisfied in 14 full before surplus goes back to the bankrupt, and the 15 underlying premise in Bower v Marris Bower v Marris, 16 which is to the same effect, creditors' rights must be 17 satisfied before anything goes back, those are 18 completely -- substantially removed because the 19 principle is now not creditors must get everything they 20 could have got as a matter of contract before the 21 surplus goes to the bankrupt. Now the principle is 22 creditors must get what the statute requires them to get 23 by way of statutory interest before the bankruptcy gets 24 the surplus. 25 So, so much for the bankruptcy cases. Now the</p> <p style="text-align: center;">Page 68</p>

<p>1 company cases. The statutory framework here, as my Lord 2 knows, that there is no provision until 1986 dealing 3 with the payment of interest from a surplus once it 4 arises so we're in the judge-made rule period. There's 5 then the quartet of cases involving Humber Ironworks and 6 the Joint Stock Discount Company. On proper analysis, 7 we say that each of those cases supports the proposition 8 we say you get out of Bower v Marris, namely that there 9 is simply no appropriation when the payments are made 10 pursuant to a statutory regime pursuant to law which 11 leave the creditor free to exercise his contractual 12 rights. That's a phrase which crops up more than once 13 in the judgments in these four cases. 14 So if we start with 1A, tab 27, which is the first 15 Humber Ironworks case. 16 MR JUSTICE DAVID RICHARDS: Just give me a moment. Yes 17 I have it. Tab 27. 18 MR ZACAROLI: The case is most often cited for the famous 19 "the tree lies where it falls" quote, and the idea that 20 interest stops running at the date of winding up, which 21 is the first case in winding up where that was decided. 22 MR JUSTICE DAVID RICHARDS: Right. 23 MR ZACAROLI: It's also very clear that the basis upon which 24 creditors could claim interest once the company was now 25 surplus, is, as Lord Giffard put it, memorably by</p> <p style="text-align: center;">Page 69</p>	<p>1 So, properly read, entirely consistent with the way 2 we say Bower v Marris should be read. 3 MR JUSTICE DAVID RICHARDS: Yes. 4 MR ZACAROLI: There's nothing in Lord Justice Giffard's 5 judgment which really touches on this point because he 6 wasn't dealing with the appropriation of payments. 7 Just to pick up on one point. When 8 Lord Justice Giffard says, at the end of his judgment -- 9 he adds another reason, pages 647 to 648: 10 "I do not see with what justice interest can be 11 computed in favour of creditors whose debts carry 12 interest ...(reading to the words)... and so obtaining 13 a right to interest." 14 That is a reason he's putting forward as to why all 15 interest stops running at the date of winding up for the 16 purposes of proof. 17 MR JUSTICE DAVID RICHARDS: Right. 18 MR ZACAROLI: Because that's what he's been talking about 19 above. 20 MR JUSTICE DAVID RICHARDS: Yes, I see. 21 MR ZACAROLI: In the immediate preceding sentence he's made 22 it clear -- 23 MR JUSTICE DAVID RICHARDS: Yes. 24 MR ZACAROLI: He's made it clear in the preceding sentence, 25 of course, there's no interest out of a surplus to</p> <p style="text-align: center;">Page 71</p>
<p>1 remission to their contractual rights. 2 MR JUSTICE DAVID RICHARDS: Yes. 3 MR ZACAROLI: Lord Justice Selwyn alone deals with the 4 Bower v Marris issue at page 645. So what he says 5 there, at the bottom paragraph, where there's a surplus: 6 "Whatever manner the payments may have been made, 7 whether originally made in respect of capital or in 8 respect of interest, still in as much as they have all 9 been paid in process of law [picking up the concept from 10 Bower v Marris] and without any contract or agreement 11 [so, again, subject to contrary intention amongst the 12 parties] the account must, in the event of there being 13 a surplus, be taken as between the company and creditors 14 in the ordinary way. That is in the manner pointed out 15 in Bower v Marris by treating the dividends as ordinary 16 payments on account and applying each dividend in the 17 first place to the payment of the interest due at the 18 date of such dividend and the surplus, if any, to the 19 reduction of principal." 20 So only relevant where there is interest due at the 21 date of the dividend. Described as being in the 22 ordinary way, a phrase used in Bower v Marris to 23 describe the way in which it's been used for bonds, 24 securities and debentures, et cetera, i.e. the general 25 law principles.</p> <p style="text-align: center;">Page 70</p>	<p>1 someone who had no right to it in the first place. 2 MR JUSTICE DAVID RICHARDS: Yes. 3 MR ZACAROLI: My Lord, then turning to the next of the four 4 cases, the Joint Stock Discount Company case, which is 5 tab 28. This is the proof against two estates case. 6 MR JUSTICE DAVID RICHARDS: Yes. 7 MR ZACAROLI: I can take this very shortly. At page 88, 8 Lord Justice Giffard refers to Mr Jessel's argument 9 about appropriation having already happened and says 10 that's a mistake: 11 "The rule which has been made has no such effect 12 ...(reading to the words)... or the particular winding 13 up." 14 That's the rule about interest stopping at the date 15 of winding up: 16 "But it is not meant at all to interfere with the 17 rights of the creditor." 18 So here one falls back to it is the creditor's 19 rights which are being respected: 20 "If he can get payment from other sources to combine 21 and retain ...(reading to the words)... not only his 22 principal but all his interest." 23 So the only principle he's applying is there is no 24 appropriation because matters are paid in a process of 25 law. There's no appropriation and therefore the</p> <p style="text-align: center;">Page 72</p>

<p>1 creditor's rights remain, as they did in <i>Bower v Marris</i></p> <p>2 against the co-debtor.</p> <p>3 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>4 MR ZACAROLI: Similarly, in the <i>Humber Ironworks</i></p> <p>5 <i>Shipbuilding</i> number 2, tab 29. This is the security</p> <p>6 case. This is the creditor with rights of security, as</p> <p>7 well and provable rights.</p> <p>8 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>9 MR ZACAROLI: He refers, page 92, to the <i>Joint Stock</i></p> <p>10 <i>Discount Company</i> number 2 which I think is the one we</p> <p>11 just looked at. Yes, it is.</p> <p>12 MR JUSTICE DAVID RICHARDS: Hmm, hmm.</p> <p>13 MR ZACAROLI: "The creditor proves in the winding up as in</p> <p>14 bankruptcy for whatever the amount of...(reading to the</p> <p>15 words)... amount to an appropriation in any shape or</p> <p>16 form."</p> <p>17 So that's the key point we get from <i>Bower v Marris</i></p> <p>18 as well, no appropriation.</p> <p>19 Then page 93, the way he puts it here is very</p> <p>20 important, the last four lines before the last little</p> <p>21 paragraph:</p> <p>22 "Although the proof in terms is in respect of</p> <p>23 principal, that does not amount to any appropriation or</p> <p>24 preclude the party who has proved from appropriating the</p> <p>25 sum received for the payment of interest so long as the</p> <p style="text-align: center;">Page 73</p>	<p>1 MR JUSTICE DAVID RICHARDS: That's it.</p> <p>2 MR ZACAROLI: Yes. Which is a concession, as my Lord knows.</p> <p>3 There's no decision there at all.</p> <p>4 MR JUSTICE DAVID RICHARDS: No.</p> <p>5 MR ZACAROLI: I'm going to deal separately with cases in</p> <p>6 other fields, like the debenture actions and the</p> <p>7 testamentary cases, because there's a similar principle</p> <p>8 at play. Well, it's the same principle of appropriation</p> <p>9 at play, but I'll deal with those separately.</p> <p>10 I'm now going to turn to the foreign cases. In all</p> <p>11 of them, except the two I've already mentioned,</p> <p>12 <i>Hibernian and Confederation Trust</i>, the conclusion is</p> <p>13 entirely consistent with our analysis of <i>Bower v Marris</i>.</p> <p>14 They don't contradict it whatsoever. In all of them,</p> <p>15 again excluding those two, the relevant statutory</p> <p>16 provision relating to post-liquidation interest or</p> <p>17 post-bankruptcy interest operated on the basis that the</p> <p>18 claims of the creditor against the now solvent debtor</p> <p>19 were to be satisfied before anything else happened.</p> <p>20 So in all of them, to the extent that they</p> <p>21 considered <i>Bower v Marris</i> at all, which is not all of</p> <p>22 them by any means, but to the extent that they did, they</p> <p>23 were applying it as a principle of appropriation.</p> <p>24 MR JUSTICE DAVID RICHARDS: Yes, all right.</p> <p>25 MR ZACAROLI: In the two cases which don't fit with that</p> <p style="text-align: center;">Page 75</p>
<p>1 train is due."</p> <p>2 Very clearly the creditor's right to appropriate</p> <p>3 remains.</p> <p>4 Then the last of the quartet is the re <i>Joint Stock</i></p> <p>5 <i>Discount Company</i> number 2. Here the point is put most</p> <p>6 clearly by Sir Richard Baggallay QC, which is the</p> <p>7 successful counsel whose arguments were accepted, having</p> <p>8 responded yet again to Mr Jessel's arguments. Page 13</p> <p>9 is the note of the argument. He refers again to the</p> <p>10 <i>Joint Stock Discount Company</i> case. He refers to the</p> <p>11 argument about appropriation, and then says:</p> <p>12 "But that is an appropriation simply for the</p> <p>13 convenience of the court and not such as to deprive the</p> <p>14 creditor of his right to appropriate the payment in any</p> <p>15 way he thinks most beneficial, according to the</p> <p>16 principle laid down in <i>Bower v Marris</i>."</p> <p>17 So there we have an extremely clear statement of the</p> <p>18 <i>Bower v Marris</i> principle, as one which simply preserved</p> <p>19 the creditor's right to appropriate.</p> <p>20 MR JUSTICE DAVID RICHARDS: Yes, I see.</p> <p>21 MR ZACAROLI: The judgment doesn't give us much help. It's</p> <p>22 a very short judgment of Lord Romer.</p> <p>23 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>24 MR ZACAROLI: My Lord, that's the English cases on the</p> <p>25 subject. Until <i>Lines Brothers</i> --</p> <p style="text-align: center;">Page 74</p>	<p>1 thesis, there was no argument and no analysis of any</p> <p>2 substance to the point.</p> <p>3 Now, I'm afraid I will go to a number of these cases</p> <p>4 that my Lord has seen but it's important to make that</p> <p>5 point good. In a sense, I'm looking for a negative but</p> <p>6 I shall go through them hopefully quite quickly.</p> <p>7 The first is one we saw briefly this morning,</p> <p>8 <i>MacKenzie v Rees</i>, bundle 1B, tab 71. The reason for</p> <p>9 showing my Lord this case, apart from the fact that it's</p> <p>10 cited in my learned friends' skeletons, is it's not</p> <p>11 a case which deals with <i>Bower v Marris</i> at all, but it's</p> <p>12 a very important case in Australia as the reasoning</p> <p>13 underlines what is happening when creditors are coming</p> <p>14 against the insolvent company under the Australian</p> <p>15 legislation to claim interest. What is happening is</p> <p>16 that they are essentially having another run. The claim</p> <p>17 that they had at the outset is suspended and they come</p> <p>18 back in with their claim once there's a surplus. So</p> <p>19 nothing like the current position in England. It's very</p> <p>20 much you have your contractual right which we're now</p> <p>21 going to respect.</p> <p>22 As I mentioned this morning, earlier on, one of the</p> <p>23 main debates in the case was whether or not the relevant</p> <p>24 debts carried interest at all, but that's not a concern</p> <p>25 for us.</p> <p style="text-align: center;">Page 76</p>

<p>1 MR JUSTICE DAVID RICHARDS: No.</p> <p>2 MR ZACAROLI: Picking up Mr Justice Dixon's judgment at</p> <p>3 pages 10 and 11. So page 10, he is referring here to</p> <p>4 the principle that interest stops running. We have seen</p> <p>5 that this morning, that passage about interest stops</p> <p>6 running at the date of bankruptcy.</p> <p>7 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>8 MR ZACAROLI: At the bottom of page 10, about four lines</p> <p>9 from the bottom, he says:</p> <p>10 "It is possible, I think, to give effect both to the</p> <p>11 principle and to the form...(reading to the words)...</p> <p>12 thus the wide language of section 81.1 [I will come back</p> <p>13 to that in a moment] may be taken as covering the</p> <p>14 intermediate interest [by which he means interest</p> <p>15 between the date of bankruptcy and the surplus arising,</p> <p>16 that intermediate period] so that it is not altogether</p> <p>17 excluded as a claim against the assets and, at the other</p> <p>18 end, section 118 may be regarded as conferring upon the</p> <p>19 debtor...(reading to the words)... allowed only if and</p> <p>20 when a surplus is attained."</p> <p>21 MR JUSTICE DAVID RICHARDS: I'm just going to re-read this</p> <p>22 passage to myself, sorry. (Pause)</p> <p>23 Yes, thank you.</p> <p>24 MR ZACAROLI: It is helpful to see the statutory background.</p> <p>25 I should perhaps have taken my Lord to it first.</p> <p style="text-align: center;">Page 77</p>	<p>1 "The bankrupt shall be entitled to any surplus</p> <p>2 remaining after payment in full of his creditors and of</p> <p>3 the costs, charges and expenses of the bankruptcy."</p> <p>4 The form of the legislation thereafter in Australia</p> <p>5 relevant to the later cases changes slightly and some of</p> <p>6 the cases considering whether the fact the legislation</p> <p>7 has changed in a particular respect has altered this</p> <p>8 rule and they all decide it hasn't, but that's the</p> <p>9 underlying basis of the jurisprudence in Australia.</p> <p>10 MR JUSTICE DAVID RICHARDS: I see. So just remind me, under</p> <p>11 the Bankruptcy Act 1914 was there express provision --</p> <p>12 yes, of course there was. There was a provision for the</p> <p>13 payment of interest. Sorry, yes. So there was nothing</p> <p>14 in the Commonwealth Bankruptcy Act?</p> <p>15 MR ZACAROLI: That's right, yes.</p> <p>16 The second decision, one I think my learned friend</p> <p>17 did take you to, is Midland Montagu v Harkness, in</p> <p>18 bundle 1C, at tab 119.</p> <p>19 MR JUSTICE DAVID RICHARDS: I don't think I have seen this</p> <p>20 one.</p> <p>21 MR ZACAROLI: I am sorry, I thought you had. I think it may</p> <p>22 have been mentioned in passing. I can be quite short</p> <p>23 then. It's not one that seems to be relied upon, but</p> <p>24 this is a case which did consider the rule in</p> <p>25 Bower v Marris and applied it in Australia, if</p> <p style="text-align: center;">Page 79</p>
<p>1 MR JUSTICE DAVID RICHARDS: No, don't worry.</p> <p>2 MR ZACAROLI: I have them. They're appended to our</p> <p>3 skeleton. I don't know if my Lord still has them there?</p> <p>4 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>5 MR ZACAROLI: It's annex 2 to our skeleton. We're dealing</p> <p>6 here with the Commonwealth Bankruptcy Act of 1924 in</p> <p>7 Australia and the first page of the annex is section 81.</p> <p>8 MR JUSTICE DAVID RICHARDS: Sorry, page --</p> <p>9 MR ZACAROLI: It's annex 2.</p> <p>10 MR JUSTICE DAVID RICHARDS: Just give me a moment. Right</p> <p>11 yes, I see. Yes, I have it.</p> <p>12 MR ZACAROLI: It should be the Australian Commonwealth</p> <p>13 Bankruptcy Act.</p> <p>14 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>15 MR ZACAROLI: Section 81.1:</p> <p>16 "All debts and liabilities, present and future,</p> <p>17 certain or contingent, to which the bankrupt is subject</p> <p>18 at the date of the...(reading to the words)... deemed</p> <p>19 to be debts provable in bankruptcy."</p> <p>20 That's the first of his termini, debts provable.</p> <p>21 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>22 MR ZACAROLI: But then the judge-made rule says that</p> <p>23 interest stops running for the purposes of proof.</p> <p>24 Section 11.8 is the second of the two termini he's</p> <p>25 referred to over the page:</p> <p style="text-align: center;">Page 78</p>	<p>1 I remember rightly.</p> <p>2 MR JUSTICE DAVID RICHARDS: In relation to a scheme, yes.</p> <p>3 MR ZACAROLI: It was a scheme which applied -- let me get</p> <p>4 the facts right -- the position in companies to the</p> <p>5 scheme and the company law itself referred on to the</p> <p>6 bankruptcy law in relation to interest. In the</p> <p>7 headnote -- yes, there were a number of companies</p> <p>8 subject to schemes of arrangement.</p> <p>9 MR JUSTICE DAVID RICHARDS: Perhaps I'll just read the</p> <p>10 headnote to myself to see what the context of this is.</p> <p>11 MR ZACAROLI: Yes. (Pause)</p> <p>12 MR JUSTICE DAVID RICHARDS: Yes, I see. I'm just reading</p> <p>13 headnote. (Pause)</p> <p>14 Yes.</p> <p>15 MR ZACAROLI: My Lord, the relevant statutory provision</p> <p>16 which at the end of that cross-referral process applied</p> <p>17 was 82.3(b) of the Bankruptcy Act 1966, which you can</p> <p>18 see copied out at page 330 of the report.</p> <p>19 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>20 MR ZACAROLI: What the learned judge says is that that</p> <p>21 sub-section does no more than enact in statutory form</p> <p>22 a principle as to the proof of liabilities carrying</p> <p>23 interest which has been part of the general rule of</p> <p>24 bankruptcy since 1789, citing MacKenzie v Rees.</p> <p>25 MR JUSTICE DAVID RICHARDS: Yes.</p> <p style="text-align: center;">Page 80</p>

<p>1 MR ZACAROLI: What he finds is that no change in the law was 2 intended by the introduction of that statute. 3 So what the decision stands for is an application of 4 the principle in Bower v Marris in the context of 5 a statutory regime which mirrored very much that scheme 6 applicable in England to companies pre-1986; that is, 7 there is no provision for interest out of the surplus as 8 such in the statute. 9 MR JUSTICE DAVID RICHARDS: Yes. 10 MR ZACAROLI: I am not going to take my Lord to all the 11 cases referred into the skeleton which my Lord hasn't 12 been taken to. I will make that general proposition 13 that in none of them is there anything which contradicts 14 this basic principle. 15 MR JUSTICE DAVID RICHARDS: I'm with you. 16 MR ZACAROLI: The one case worth reminding my Lord of is 17 Tahore Holdings, 1D, tab 135, which you were taken to. 18 MR JUSTICE DAVID RICHARDS: Yes. 19 MR ZACAROLI: My learned friend Mr Dicker described this 20 case as one which applied Bower v Marris to a case where 21 the right to interest arose by way of a judgment. So it 22 was a judgment of interest. That's not quite right. It 23 is true that the interest in this case arose because of 24 a judgment, not because of a contract, but actually the 25 case doesn't apply Bower v Marris. It's merely dealing</p> <p style="text-align: center;">Page 81</p>	<p>1 MR ZACAROLI: My Lord, the next case to go to is the case of 2 Gerah Imports v The Duke Group Limited. 3 MR JUSTICE DAVID RICHARDS: You just touched on re Tahore 4 just before we rose. I had looked at that before, but 5 a point you make about this case is that there's no 6 discussion of Bower v Marris or the principle in 7 Bower v Marris at all. 8 MR ZACAROLI: No. 9 MR JUSTICE DAVID RICHARDS: But consistently with your 10 submissions, would Bower v Marris be applied in Tahore? 11 MR ZACAROLI: Yes, we accept that. We don't draw 12 a distinction between a pre-existing right to interest, 13 which is derived from the law, as opposed to derived 14 from a contract. 15 MR JUSTICE DAVID RICHARDS: Yes, quite. I'll just make 16 a note of that, yes. (Pause) 17 Just give me one moment. 18 MR ZACAROLI: The next case is Gerah Imports v The Duke 19 Group Limited, bundle 1D at tab 137. 20 MR JUSTICE DAVID RICHARDS: Yes. 21 MR ZACAROLI: My Lord was taken to this, again so if I can 22 take this quite briefly. 23 MR JUSTICE DAVID RICHARDS: Yes, I was. 24 MR ZACAROLI: Paragraph 13 of the judgment is where you see 25 the relevant section of the Companies Act, the amount of</p> <p style="text-align: center;">Page 83</p>
<p>1 with the principle of the right to interest coming back 2 in once there's a surplus. 3 The judgment critically was a pre-insolvency 4 judgment, so at the time of the insolvency the creditor 5 had a right to interest -- 6 MR JUSTICE DAVID RICHARDS: Yes, I'm with you. 7 MR ZACAROLI: The principle for which it was cited by my 8 learned friend Mr Smith, I think, was that interest in 9 these circumstances isn't limited to contractual 10 interest and includes interest arising under, for 11 example, a judgment. We don't disagree with that. The 12 question is what right did the creditor have to interest 13 at the date of the bankruptcy or winding up or 14 administration. If he already had a Judgments Act 15 judgment and therefore a Judgments Act interest in 16 favour of him, he was like a creditor with a contractual 17 right. 18 MR JUSTICE DAVID RICHARDS: I'm with you. 19 MR ZACAROLI: We don't draw a distinction. 20 My Lord, is that a convenient moment? 21 MR JUSTICE DAVID RICHARDS: Yes, certainly. 2 o'clock 22 (1.00 pm) 23 (Luncheon Adjournment) 24 (2.00 pm) 25 MR JUSTICE DAVID RICHARDS: Yes, Mr Zacaroli.</p> <p style="text-align: center;">Page 82</p>	<p>1 the debt of a company including a debt that includes 2 interest is to be computed for the purposes of the 3 winding up as at the relevant date. 4 MR JUSTICE DAVID RICHARDS: Yes. 5 MR ZACAROLI: One of the questions in this case was whether 6 the previous law about allowing a second round of proofs 7 once there was a surplus was somehow changed because of 8 the statutory provision. 9 MR JUSTICE DAVID RICHARDS: Yes, I see. 10 MR ZACAROLI: Paragraph 19, there's this quite helpful 11 description of what goes on here as a second round of 12 proofs. That's really based upon the judgment of 13 Mr Justice Dixon in MacKenzie v Rees at paragraph 20, 14 which he then cites. 15 MR JUSTICE DAVID RICHARDS: Yes. 16 MR ZACAROLI: At paragraph 22, in particular, the key 17 passage he cites is that one we saw before about the 18 principle is really one about determining the order in 19 which debts are to be discharged. So very clear in this 20 case, which he did apply Bower v Marris in the sense 21 that he approved a paragraph in the liquidator's 22 affidavit which said, "Should I do it on this basis?" 23 which included Bower v Marris reference. So he approved 24 that. He did it in the circumstance that what was 25 happening was a second round of proofs, the original</p> <p style="text-align: center;">Page 84</p>

<p>1 creditor's claim was re-admitted once the surplus arose.</p> <p>2 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>3 MR ZACAROLI: So entirely consistent with the way we put our</p> <p>4 case. Entirely dependent upon there being some interest</p> <p>5 accruing by the contract in that case.</p> <p>6 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>7 MR ZACAROLI: There are a couple of other Australian cases</p> <p>8 referred to in --</p> <p>9 MR JUSTICE DAVID RICHARDS: Just to interrupt you, again</p> <p>10 nothing expressly in the legislation providing for</p> <p>11 post-liquidation interest?</p> <p>12 MR ZACAROLI: No. My Lord, that is clear in this case</p> <p>13 because you have paragraph 19 talking about the rule at</p> <p>14 common law and the question is whether section 439(1)</p> <p>15 has changed that.</p> <p>16 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>17 MR ZACAROLI: There were a couple of other cases cited in</p> <p>18 probably footnotes or in passing in my learned friends'</p> <p>19 skeletons. I'm not going to take my Lord to those.</p> <p>20 They weren't relied upon. They do not have a --</p> <p>21 contradict the basic proposition. If my Lord is taken</p> <p>22 to them, then maybe I'll have to deal with it but we</p> <p>23 don't need to go there.</p> <p>24 That deals with Australia.</p> <p>25 My learned friend mentioned in passing the case of</p> <p style="text-align: center;">Page 85</p>	<p>1 Bower v Marris; what it entailed and why it would extend</p> <p>2 the situation which existed in this case, that the</p> <p>3 statute proceeded on the basis that all creditors were</p> <p>4 entitled to interest at the judgments rate, whether or</p> <p>5 not they had a contractual right.</p> <p>6 Again, one is looking for a negative. There is</p> <p>7 nothing in here which analyses underlying rationale in</p> <p>8 Bower v Marris and purports to extend it to that case in</p> <p>9 any reasoned way.</p> <p>10 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>11 MR ZACAROLI: I don't need to show my Lord any particular</p> <p>12 passage because it's a negative. There is nothing in</p> <p>13 here which deals with that.</p> <p>14 It appears that it was a fairly speedy decision,</p> <p>15 given the day after the argument, so not much time taken</p> <p>16 for consideration.</p> <p>17 The short point is it's of no persuasive authority</p> <p>18 at all.</p> <p>19 MR JUSTICE DAVID RICHARDS: No, I follow. Sorry to -- the</p> <p>20 statutory regime in Ireland at the time provided for</p> <p>21 post-liquidation interest.</p> <p>22 MR ZACAROLI: Yes.</p> <p>23 MR JUSTICE DAVID RICHARDS: Unlike, for example, in</p> <p>24 Lines Brothers.</p> <p>25 MR ZACAROLI: Yes.</p> <p style="text-align: center;">Page 87</p>
<p>1 Peregrine v Hong Kong. No need to take my Lord to that.</p> <p>2 There is nothing in it which takes us any further either</p> <p>3 way. There is no relevant statutory provision. It's</p> <p>4 simply an application of Bower v Marris. It was</p> <p>5 a double estate case so it was a question of proving</p> <p>6 against one and being entitled to prove against the</p> <p>7 other.</p> <p>8 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>9 MR ZACAROLI: Then Ireland, and the one case we need to deal</p> <p>10 with is the case of Hibernian. This is in bundle 1C,</p> <p>11 tab 107. This is the second judgment of</p> <p>12 Ms Justice Carroll; the first judgment having determined</p> <p>13 that in the context of that case the approach taken in</p> <p>14 Rolls-Royce that the Bankruptcy Act was not incorporated</p> <p>15 was not to be followed. Her judgment was overturned and</p> <p>16 therefore --</p> <p>17 MR JUSTICE DAVID RICHARDS: On that point?</p> <p>18 MR ZACAROLI: On that point. What appears in this judgment</p> <p>19 was not dealt with at all by the Court of Appeal.</p> <p>20 MR JUSTICE DAVID RICHARDS: No, right.</p> <p>21 MR ZACAROLI: It was certainly not approved, not expressly</p> <p>22 overturned, but obviously rendered moot by the fact that</p> <p>23 the original judgment itself was overturned. So given</p> <p>24 that state of the authority already, one doesn't find in</p> <p>25 this decision any analysis of the rule in</p> <p style="text-align: center;">Page 86</p>	<p>1 MR JUSTICE DAVID RICHARDS: And the relevant provision is --</p> <p>2 MR ZACAROLI: It's at page 267, at the top of the page. The</p> <p>3 section is -- it's section 304 it looks like of the</p> <p>4 original 1857 Act but it's been amended by section 86 of</p> <p>5 the Bankruptcy Act 1988.</p> <p>6 MR JUSTICE DAVID RICHARDS: So it's still the provision at</p> <p>7 the top of the page, is it?</p> <p>8 MR ZACAROLI: That's correct, yes.</p> <p>9 MR JUSTICE DAVID RICHARDS: With interest at the rate</p> <p>10 currently payable on judgment debt?</p> <p>11 MR ZACAROLI: Yes, yes.</p> <p>12 Now, we would say that must be wrong on the analysis</p> <p>13 of Bower v Marris as we put forward insofar as it</p> <p>14 relates to creditors who had no contractual right to</p> <p>15 interest, because there was no right to interest</p> <p>16 accruing at the time that dividends would have been paid</p> <p>17 prior to the surplus arising.</p> <p>18 MR JUSTICE DAVID RICHARDS: Sorry, I'm just wondering where</p> <p>19 she deals with this. So you get -- so all creditors got</p> <p>20 interest at the judgment rate.</p> <p>21 MR ZACAROLI: Yes. There doesn't appear to be a reference</p> <p>22 to entitlement to a higher contractual rate.</p> <p>23 MR JUSTICE DAVID RICHARDS: No. But at page 269 she says</p> <p>24 that after payment of the statutory interest, the</p> <p>25 contractual creditors are entitled to be paid the</p> <p style="text-align: center;">Page 88</p>

<p>1 balance due for contractual interest giving credit for 2 the statutory interest. 3 MR ZACAROLI: Yes. 4 MR JUSTICE DAVID RICHARDS: In that context, she applies 5 Bower v Marris, as I read it. 6 MR ZACAROLI: My Lord, I am terribly sorry, I am looking at 7 the wrong decision. It's my fault entirely. 8 MR JUSTICE DAVID RICHARDS: Ah, right. 9 MR ZACAROLI: It should be tab 108. 10 MR JUSTICE DAVID RICHARDS: This not the one that was 11 overruled -- 12 MR ZACAROLI: No, this is the judgment that was overruled. 13 MR JUSTICE DAVID RICHARDS: This is the judgment? 14 MR ZACAROLI: This is the judgment that said that the 15 Rolls-Royce approach doesn't apply. 16 MR JUSTICE DAVID RICHARDS: So this is the second judgment? 17 MR ZACAROLI: No, the first judgment was the one which said 18 Rolls-Royce didn't apply; that was overruled. The 19 second judgment, which is tab 108 -- I am very sorry -- 20 therefore becomes -- 21 MR JUSTICE DAVID RICHARDS: That's where we are. What she's 22 done here, at 107, is this right, is to say creditors in 23 the event of a surplus after payment of proved debts get 24 interest at the rate currently payable on judgment 25 debts.</p> <p style="text-align: center;">Page 89</p>	<p>1 MR JUSTICE DAVID RICHARDS: Right. 2 MR ZACAROLI: This is a decision purely on the question of 3 how interest was to be computed in relation to creditors 4 whose debts did not carry interest, and her decision 5 is -- her conclusion is at the end of the decision at 6 page 273. 7 MR JUSTICE DAVID RICHARDS: Sorry to interrupt you again, 8 but the decision on appeal from the case -- from the 9 decision in 107 occurred after this? 10 MR ZACAROLI: Yes, that's right. 11 MR JUSTICE DAVID RICHARDS: So it sort of removed both these 12 decisions in effect. 13 MR ZACAROLI: Yes. It removed the first one, so the premise 14 for the second one just disappeared. 15 MR JUSTICE DAVID RICHARDS: I'm with you, yes. 16 MR ZACAROLI: That's 112, my Lord, if you want the 17 reference. 18 MR JUSTICE DAVID RICHARDS: Thank you. 19 MR ZACAROLI: So this is the question about whether those 20 not entitled to contractual interest would also be 21 treated on the Bower v Marris basis, and the answer was 22 "yes". But the reasoning is crisp, to say the least. 23 MR JUSTICE DAVID RICHARDS: Yes. 24 MR ZACAROLI: She relies on page 272 on a report from the 25 Bankruptcy Law Committee which says that they took the</p> <p style="text-align: center;">Page 91</p>
<p>1 MR ZACAROLI: Yes. 2 MR JUSTICE DAVID RICHARDS: Then, if contractual creditors 3 still have an entitlement to interest, they're entitled 4 to be paid that, applying Bower v Marris? 5 MR ZACAROLI: Yes. 6 MR JUSTICE DAVID RICHARDS: Right. 7 MR ZACAROLI: The reasoning for that may well be because 8 although there is a statutory right to interest in 86, 9 as we've just seen at page 267, which is everyone has 10 the judgments rate, the surplus provision, which is -- 11 I was going to say the surplus provision is different, 12 but it's -- I'm not entirely sure at the moment why it 13 is she thought that there was a contractual right to 14 interest. 15 MR JUSTICE DAVID RICHARDS: Well, I suppose because -- no. 16 Well -- 17 MR ZACAROLI: It doesn't really matter because she's not 18 construing any English Act. 19 MR JUSTICE DAVID RICHARDS: No. 20 MR ZACAROLI: The terms of the section are materially 21 different to the English Bankruptcy Act, for example, 22 which wouldn't have allowed such right for the reasons 23 we went through this morning. 24 MR JUSTICE DAVID RICHARDS: Right. Okay. So 108. 25 MR ZACAROLI: 108 is the correct decision.</p> <p style="text-align: center;">Page 90</p>	<p>1 view that in England interest was to be computed as 2 running interest, referring to Bower v Marris, 3 et cetera, and Bromley v Goodere. She says, at the 4 bottom of page 273: 5 "If statutory interest is payable it seems to me it 6 should be computed as running interest following 7 Bower v Marris." 8 Therefore, you apply them to interest first. 9 MR JUSTICE DAVID RICHARDS: Yes. 10 MR ZACAROLI: I make the same point I did before. It's of 11 no persuasive value. 12 MR JUSTICE DAVID RICHARDS: The crisp reasoning -- well ... 13 (Pause) 14 MR ZACAROLI: The previous paragraph she just says the 15 amendment to the Act, which we saw before, section 86, 16 which gives interest at the judgments rate to all, she 17 says that, at the bottom of page 273: 18 "The amendment removes the judicial discretion 19 ...(reading to the words)... interest is payable it is 20 payable on the running interest basis." 21 MR JUSTICE DAVID RICHARDS: Yes, I see. 22 MR ZACAROLI: Without having understood or analysed what it 23 is that gives rise to this principle of appropriation in 24 Bower v Marris, which clearly wouldn't work to interest 25 which hadn't accrued --</p> <p style="text-align: center;">Page 92</p>

<p>1 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>2 MR ZACAROLI: -- at the time of dividends.</p> <p>3 MR JUSTICE DAVID RICHARDS: This Bankruptcy Law Committee,</p> <p>4 we don't know -- this was obviously some time in the</p> <p>5 1980s, I take it.</p> <p>6 MR ZACAROLI: One suspects, because the Act is dated -- is</p> <p>7 1986 or 1988 -- the 1988 Act, yes.</p> <p>8 MR JUSTICE DAVID RICHARDS: So it led to that, in other</p> <p>9 words?</p> <p>10 MR ZACAROLI: Yes.</p> <p>11 MR JUSTICE DAVID RICHARDS: It's interesting that they were</p> <p>12 on to Bower v Marris but the Cork Committee was not.</p> <p>13 Thank you.</p> <p>14 MR ZACAROLI: That's Ireland.</p> <p>15 Canada, the one decision which is inconsistent with</p> <p>16 our proposition is Confederation Trust which is at 1D,</p> <p>17 tab 133. Now, my Lord saw this but the question is</p> <p>18 summarised on page 2 of the report in the fifth line:</p> <p>19 "The dispute was over whether the interest was to be</p> <p>20 paid in accordance with...(reading to the words)...</p> <p>21 utilising an interest first or a principal first focus</p> <p>22 as a starting point."</p> <p>23 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>24 MR ZACAROLI: So the first question was whether section</p> <p>25 95(2) applied at all because it came into effect after</p> <p style="text-align: center;">Page 93</p>	<p>1 inaccurate summary of the principle in Bower v Marris as</p> <p>2 applied in, for example, the quartet of cases about</p> <p>3 Humber Ironworks in 1870 for the reasons that I went</p> <p>4 through this morning. It is true that one ends up with</p> <p>5 a situation that generally interest under the English</p> <p>6 legislation prior to 1883 and bankruptcy and still in</p> <p>7 companies winding up until 1986, it is true that</p> <p>8 generally the interest was applied first -- the</p> <p>9 dividends were applied to interest before principal but</p> <p>10 not because that was the rule that had to be applied on</p> <p>11 distribution of assets from insolvency estate; it was</p> <p>12 because of the rule that the dividends themselves were</p> <p>13 not appropriated having been paid pursuant to law and</p> <p>14 therefore the creditor's right to appropriate remained</p> <p>15 with the presumption that that was the result. So</p> <p>16 that's a very condensed and inaccurate summary.</p> <p>17 The second sentence doesn't make sense because -- at</p> <p>18 least the last part of it "to protect the contractual</p> <p>19 relationship between the parties" is only relevant to</p> <p>20 those who have a contractual right to interest.</p> <p>21 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>22 MR ZACAROLI: So for those two reasons, those two sentences</p> <p>23 are equally of no persuasive authority before this</p> <p>24 court. Importantly, of course, the arguments that</p> <p>25 my Lord is hearing from this side of the court weren't</p> <p style="text-align: center;">Page 95</p>
<p>1 the insolvency proceedings had started, but it was held</p> <p>2 to apply, even though the right to interest was a future</p> <p>3 contingent right. My Lord saw that paragraph yesterday.</p> <p>4 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>5 MR ZACAROLI: That didn't matter. It was -- the Act</p> <p>6 applied.</p> <p>7 MR JUSTICE DAVID RICHARDS: Right.</p> <p>8 MR ZACAROLI: The second question then is dealt with at</p> <p>9 page 9, paragraph 29 and following. Mr Justice Blair</p> <p>10 says:</p> <p>11 "The traditional rule in insolvency situations is</p> <p>12 that dividends are to be applied first to the payment of</p> <p>13 interest and then to the payment of principal. This is</p> <p>14 said to prevent injustice, promote equity amongst the</p> <p>15 creditors and protect the contractual relationship</p> <p>16 between the parties."</p> <p>17 Now, I should remind my Lord that section 95(2)</p> <p>18 provided a rate of interest at 5 per cent for all claims</p> <p>19 provable in the winding up, so there's -- some creditors</p> <p>20 would have had a right to interest before that, others</p> <p>21 not. So, like the Irish provision, it covers the</p> <p>22 ground.</p> <p>23 Now, the first point to note about that sentence or</p> <p>24 those two sentences is that "the traditional rule in</p> <p>25 insolvency situations is that" is a very condensed and</p> <p style="text-align: center;">Page 94</p>	<p>1 made in that case.</p> <p>2 MR JUSTICE DAVID RICHARDS: But might you not say that</p> <p>3 insofar as he is condensing the sort of Bower v Marris</p> <p>4 history, that line of authority -- it was part of your</p> <p>5 point -- is to protect the contractual relationship</p> <p>6 between the parties?</p> <p>7 MR ZACAROLI: True. The point is that it doesn't work. It</p> <p>8 doesn't lead to his conclusion.</p> <p>9 MR JUSTICE DAVID RICHARDS: I follow that. I see.</p> <p>10 MR ZACAROLI: That's all I meant. I am sorry, that is</p> <p>11 indeed the rationale underlying Bromley v Goodere and</p> <p>12 Bower v Marris.</p> <p>13 MR JUSTICE DAVID RICHARDS: Quite.</p> <p>14 MR ZACAROLI: It does not lead to the conclusion that those</p> <p>15 without a right to contractual right should get it.</p> <p>16 MR JUSTICE DAVID RICHARDS: I follow that. I see that, yes.</p> <p>17 Right.</p> <p>18 MR ZACAROLI: The rest of the judgment deals with points of</p> <p>19 more general principle. True enough you might say in</p> <p>20 paragraph 33, for example, that those policy</p> <p>21 considerations might be said to apply equally, although</p> <p>22 I'll come on to those arguments later and explain why,</p> <p>23 but I'm not saying that there's anything particularly</p> <p>24 wrong about how he construed the policy behind the</p> <p>25 Canadian legislation. The key point is in the technical</p> <p style="text-align: center;">Page 96</p>

<p>1 analysis part of this decision, which is just in 2 paragraph 29, he's wrong. The analysis -- he doesn't 3 deal with the analysis in Bower v Marris and he doesn't 4 deal with the arguments we're presenting here and 5 therefore my Lord gets nothing from this decision that 6 helps in this case. 7 MR JUSTICE DAVID RICHARDS: Yes. 8 MR ZACAROLI: My Lord, that's Canada. There was another 9 case later on that my learned friend may have touched 10 on. It's in their skeleton. It simply followed this 11 case without any discussion, so nothing more to be got 12 at of that. 13 That leaves us with Scotland. 14 The case of Gourlay v Watson. This is at bundle 1B, 15 tab 51. This involved a sequestration. It appears, as 16 my Lord noted with Mr Smith yesterday, it had the 17 attributes -- some of the attributes of a bankruptcy 18 although it doesn't appear to be a bankruptcy. 19 The relevant bankruptcy legislation which is -- 20 seems to be applied by analogy is section 52 of the 21 Bankruptcy (Scotland) Act 1856 which is copied at the 22 bottom of page 765. 23 MR JUSTICE DAVID RICHARDS: Yes. 24 MR ZACAROLI: That section, the relevant part of it is, is 25 at end of the page:</p> <p style="text-align: center;">Page 97</p>	<p>1 MR JUSTICE DAVID RICHARDS: The passage where it cropped up 2 was in the judgment itself on page 765. So we've only 3 got a relatively small part of the judgment as such 4 there, I think. This is all judgment, is it, or is it? 5 No, I'm not sure it is. 6 MR ZACAROLI: The judgment starts at the bottom of page 766. 7 MR JUSTICE DAVID RICHARDS: So what is this that we're 8 looking at here, I wonder? 9 MR ZACAROLI: This is just the -- 10 MR JUSTICE DAVID RICHARDS: I see. At 765 this is the 11 argument. 12 MR ZACAROLI: Yes. 13 MR JUSTICE DAVID RICHARDS: Sorry, yes, I see. Well, what 14 Mr Smith showed me was if you see on 765, at the bottom 15 of that bit, it says: 16 "The creditors were accordingly entitled, there 17 being a surplus [then over the page] to principal and 18 legal interest." 19 "Legal interest means allowed by law, not 20 contractual", I have jotted down. I was just 21 wondering -- you're reading in terms of law as meaning 22 or at any rate including contractual interest and you 23 may be right. 24 MR ZACAROLI: That's what I've assumed, but it would also 25 include, as I understand it from Mr Smith's submissions</p> <p style="text-align: center;">Page 99</p>
<p>1 "If there be any residue of the estate after 2 discharging the debts ranked then he shall be entitled 3 to a claim out of such residue, the full amount of the 4 interest on his debt in terms of law." 5 He being the creditor. 6 So that pretty much mirrors the first part of the 7 applicable rule in 1825 in England because it's simply 8 remitting someone to the right he has at law to 9 interest -- 10 MR JUSTICE DAVID RICHARDS: What, this section is, is it? 11 MR ZACAROLI: The last words of that section. So the bit 12 I've just read out. In Bower v Marris the creditors 13 were entitled -- who had an interest-bearing debt were 14 entitled to interest, and then there was the -- 15 MR JUSTICE DAVID RICHARDS: I wasn't sure whether this -- 16 I think Mr Smith took me -- gave me some explanation as 17 to what was meant in Scotland by "legal interest". 18 I don't know whether interest on his debt in terms of 19 law carries this rather more technical meaning. 20 MR ZACAROLI: My Lord, even what Mr Smith was showing you 21 was, I think, legal interest being pursuant to some 22 pre-sequestration. 23 MR JUSTICE DAVID RICHARDS: I see; is that right? 24 MR ZACAROLI: Yes. He wasn't, and I'm pretty sure he was 25 not telling --</p> <p style="text-align: center;">Page 98</p>	<p>1 yesterday, what they call in Scotland legal interest, 2 being something which is payable pursuant to -- I don't 3 know exactly what it was -- it's a pre-bankruptcy right. 4 MR JUSTICE DAVID RICHARDS: It was explained by Lord Hodge 5 I think you're right, that it's a sort of judgment. I'm 6 not sure. 7 MR ZACAROLI: Exactly, yes. 8 MR JUSTICE DAVID RICHARDS: It gets quite involved. I'm not 9 sure I know the answer straight off. 10 MR ZACAROLI: I'm certainly not professing to explain to 11 my Lord the law of Scotland. 12 MR JUSTICE DAVID RICHARDS: No. All right. Anyway, 13 let's -- 14 MR ZACAROLI: At the top of page 767 Lord Young is 15 considering the case of interest with a contractual 16 right. The first paragraph at the top of page 767. 17 MR JUSTICE DAVID RICHARDS: Yes. 18 MR ZACAROLI: "It is not a matter of doubt that a creditor 19 in any ...(reading to the words)... becomes due at the 20 date of payment." 21 MR JUSTICE DAVID RICHARDS: Yes. 22 MR ZACAROLI: Then at the bottom of that page: 23 "The doctrine of appropriation by payment of 24 a debtor ...(reading to the words)... to pay certain 25 interest-bearing debts."</p> <p style="text-align: center;">Page 100</p>

<p>1 So I have understood this case to be a case about 2 interest-bearing debts. 3 MR JUSTICE DAVID RICHARDS: It may well be, yes. 4 MR ZACAROLI: As such, my Lord, it's not a bankruptcy case 5 It's an example of the principle of appropriation which 6 we saw applied in Bower v Marris being applied in this 7 Scottish sequestration, where creditors had accrued 8 rights to interest from -- prior to the date of the 9 sequestration. 10 MR JUSTICE DAVID RICHARDS: Yes. 11 MR ZACAROLI: The reference to English bankruptcy law is 12 very short, at page 770. It's the paragraph beginning 13 in the middle of the page: 14 "The analogy of the law of bankruptcy, both here and 15 in England, is in accordance ...(reading to the 16 words)... the full amount of the interest on his debt in 17 terms of law." 18 He cites the Warrant Finance Company case. 19 MR JUSTICE DAVID RICHARDS: Yes. 20 MR ZACAROLI: I'm reminded this is a trust case. It's 21 a trust deed which applies the principle of 22 sequestration. That's how one gets there. 23 My learned friend Mr Smith said this case is notable 24 because it's after 1883. It's true. It's in 1900. But 25 the suggestion that the 1883 Bankruptcy Act and the</p> <p style="text-align: center;">Page 101</p>	<p>1 the will on the legacy. 2 MR JUSTICE DAVID RICHARDS: Yes. 3 MR ZACAROLI: That right to interest accrues due before 4 payments are then made under these cases to the relevant 5 beneficiary. So all of these cases are examples of at 6 the time a payment is made the legatee has, at the same 7 time, the right to the legacy and interest accrued on 8 it. The principle which the cases are authority for is 9 that such payments made under a will do not constitute 10 an appropriation towards principal or interest in the 11 same way that payments made under bankruptcy legislation 12 don't, because they're made not so much in compulsion of 13 law but by someone other than the deceased, obviously, 14 by the testator. They don't amount to an appropriation 15 and therefore the creditor's right to appropriate one or 16 the other remains. They are therefore perfectly 17 consistent with the operation of the principle as 18 applied in Bower v Marris itself. 19 The first case is called re Prince, Hardman and 20 Willis. It's bundle 1B, tab 68. The headnote states 21 simply that: 22 "Where there are insufficient funds to pay legacies 23 when due ...(reading to the words)... due to them at the 24 time of payment on account of such legacies." 25 The facts were that Mr Prince died in 1917. That's</p> <p style="text-align: center;">Page 103</p>
<p>1 change that had made to English bankruptcy law was 2 brought to the attention of the judges in Scotland is 3 without any foundation. There's no reason why they 4 would have been shown the 1883 Bankruptcy Act. It had 5 nothing to do with the case. 6 The only reference into English law is in fact to 7 the case involving companies, the Warrant Finance 8 Company case. So the coincidence of the date being 9 after 1883 is irrelevant. 10 MR JUSTICE DAVID RICHARDS: Yes, I see. 11 MR ZACAROLI: My Lord, we can keep that bundle. At the risk 12 of straying into yet more remote areas of law, I'm going 13 to turn to the testamentary cases. There are two types 14 of -- two different categories of testamentary case to 15 consider. One is where interest is payable on legacies; 16 the other is where interest is payable on debts. There 17 are three cases in the bundles dealing with legacies, 18 one dealing with debts. The latter is 19 Whittingstall v Grover. 20 So far as legacies are concerned, my Lord may know 21 this. Interest is payable on legacies after the 22 executor's year, so a year after the death, at a fixed 23 rate to creditors, whether or not they had a right to 24 interest -- there's no right to interest of course. 25 It's a gift from the will so it's interest payable from</p> <p style="text-align: center;">Page 102</p>	<p>1 the first paragraph on the left below the headnote. 2 MR JUSTICE DAVID RICHARDS: Yes. 3 MR ZACAROLI: In the judgment of Mr Justice Clauson, he says 4 towards the middle of the first paragraph: 5 "The executors made certain payments in the years 6 1933 and 1934 to the legatees without professing to 7 appropriate between principal and interest." 8 Then in the last paragraph, he says: 9 "I have been referred to Bower v Marris, a decision 10 of Lord Cottenham, and from that case I clearly infer 11 that if the payer of a sum of money is a debtor and the 12 payee is a creditor, the payee has the right to treat 13 any sum paid to him without any appropriation in respect 14 of the debt primarily as a payment of interest due." 15 We would say that's a perfectly respectable summary 16 of the proposition one gets from Bower v Marris. 17 MR JUSTICE DAVID RICHARDS: Yes. 18 MR ZACAROLI: He then says: 19 "I feel bound to hold that the principle laid down 20 in Bower v Marris ...(reading to the words)... of the 21 principle of the legacies." 22 The second case to look at is re Morley's Estate, 23 the same bundle, tab 70. 24 MR JUSTICE DAVID RICHARDS: The right to interest on 25 legacies, the source of that right is what?</p> <p style="text-align: center;">Page 104</p>

<p>1 MR ZACAROLI: My Lord, we've cited a case in our skeleton 2 which I can take my Lord to. It is in our reply 3 skeleton. My Lord, paragraph 36 of our reply skeleton. 4 I think that's tab 6 of bundle -- 5 MR JUSTICE DAVID RICHARDS: Yes. 6 MR ZACAROLI: Paragraph 36, page 10. 7 MR JUSTICE DAVID RICHARDS: Yes, I see. 8 MR ZACAROLI: Perhaps my Lord could just read paragraphs 36 9 through to 39. 10 MR JUSTICE DAVID RICHARDS: I will. (Pause) 11 Is it a right to interest -- I mean, is the interest 12 payable with the legacy or is it payable in the meantime 13 or how does it work? 14 MR ZACAROLI: It's payable after a year. 15 MR JUSTICE DAVID RICHARDS: Yes. You have the year, so no 16 interest runs then. Does it ... (Pause) 17 MR ZACAROLI: My Lord, I think it must be the case that it's 18 payable along with. We can see that, I think, from 19 re Morley's Estate. 20 MR JUSTICE DAVID RICHARDS: But it nonetheless you say it 21 accrues due during the -- 22 MR ZACAROLI: Yes. It accrues from after a year. Therefore 23 it is clearly is accruing -- 24 MR JUSTICE DAVID RICHARDS: Yes, I see. 25 MR ZACAROLI: -- thereafter, yes.</p> <p style="text-align: center;">Page 105</p>	<p>1 MR JUSTICE DAVID RICHARDS: Yes. 2 MR ZACAROLI: Secondly, subject to any contrary indication 3 in the will which mirrors the position under the general 4 law in relation to contracts, subject to different 5 agreement between the parties. 6 MR JUSTICE DAVID RICHARDS: Yes. 7 MR ZACAROLI: My Lord, the only other reference in the 8 legacy line is the other -- the third case which is an 9 older case of Thomas v Montgomery, volume 1A, tab 15. 10 It's a decision from 1828, so prior to Bower v Marris. 11 The headnote, reads: 12 "In the progress of a suit for the administration of 13 a testator's asset which are more ...(reading to the 14 words)... in reduction of one fourth of the principal." 15 There's a passage I want to draw to my Lord's 16 attention in the argument for the legatees, for the 17 successful legatees, at page 820, which explains the 18 rationale behind payments on account and how they are 19 appropriated. In the left-hand -- at the bottom of the 20 page on 820, the last paragraph in the middle of that 21 paragraph: 22 "Now a payment on account deemed to be made in 23 a case where principal and interest are due ...(reading 24 to the words)... to compensate him for the delay which 25 he has suffered."</p> <p style="text-align: center;">Page 107</p>
<p>1 I think I showed you the passage from Prince which 2 talks about interest being due. 3 MR JUSTICE DAVID RICHARDS: Where is that? 4 MR ZACAROLI: When he summarises the rule in Bower v Marris 5 he talks about it being appropriation in respect of the 6 debt primarily as a payment of interest due. We see the 7 same thing from re Morley's Estate perhaps better 8 expressed. 9 MR JUSTICE DAVID RICHARDS: Fine. 10 MR ZACAROLI: This is at tab 70: 11 "Where, owing to the nature of a testator's estate, 12 it has been impossible to realise it ...(reading to the 13 words)... previously made by the court in the matter to 14 the contrary." 15 Then he deals with this question at page -- the 16 judge does -- 496: 17 "The questions before me are really these: first, 18 what is the rule of administration which ...(reading to 19 the words)... precludes me from doing so", and refers to 20 Thomas v Montgomery and re Prince. 21 He finds there's nothing in the will in that case to 22 reach a contrary conclusion. 23 Two points to note. First of all it applies where 24 both the payments are made when interest is due as well 25 as the legacy.</p> <p style="text-align: center;">Page 106</p>	<p>1 So it's similarly adopting a presumption approach to 2 this. That's what creditors generally would want to do 3 because that's what's in their interests. The decision 4 is very short. It's the Vice Chancellor, 5 Sir Lawrence Shadwell at page 821. He notes the order 6 the Master made and then the reasoning is pretty short 7 at the end. He just says, in the last five lines of the 8 judgment: 9 "And without entering into the question of law 10 ...(reading to the words)... in this case should be 11 confirmed." 12 Then there are the interest on debts -- there is the 13 interest on debts case. There is only one case, 14 Whittingstall v Grover. That's bundle 1A, tab 43. 15 My learned friend Mr Smith took my Lord to this at 16 some length yesterday. The case deals principally with 17 the issue of priority between the joint and separate 18 estates because the deceased partner's partner 19 subsequently went bankrupt. 20 MR JUSTICE DAVID RICHARDS: Yes. 21 MR ZACAROLI: Therefore it involves that horrendous 22 complication of the interplay between estates and 23 bankruptcy. 24 MR JUSTICE DAVID RICHARDS: Yes. 25 MR ZACAROLI: We make the point in our skeleton that even by</p> <p style="text-align: center;">Page 108</p>

<p>1 the time this case was decided, the point had become 2 irrelevant because from 1883 any deceased's estate which 3 became insolvent had to be transferred to bankruptcy and 4 the rules about interest and bankruptcy applied to the 5 exclusion of anything else. So this is in fact the only 6 case on the subject because it was decided just after 7 that had happened or the bankruptcy related back some 8 30 years.</p> <p>9 MR JUSTICE DAVID RICHARDS: I see, yes.</p> <p>10 MR ZACAROLI: The first thing which happened then was that 11 one partner, Mr Whittingstall, died. That was in 1856, 12 in March 1856. His partner became bankrupt some months 13 later, in August 1856. That was Mr Smith. If my Lord 14 picks up the second page of the report where it's 15 setting out -- reciting the facts, in the middle of the 16 right-hand column, paragraph begins: 17 "By the decree made in the first of such actions [so 18 administration actions in the estate] on 26 January 1857 19 the usual accounts and enquiries were directed to be 20 taken and made." 21 So that's the second important date is that in 1857 22 a decree was issued in Chancery for accounts and 23 enquiries.</p> <p>24 MR JUSTICE DAVID RICHARDS: Right.</p> <p>25 MR ZACAROLI: The important thing to understand about that</p> <p style="text-align: center;">Page 109</p>	<p>1 MR JUSTICE DAVID RICHARDS: Right. Yes, I see. Thank you.</p> <p>2 MR ZACAROLI: This is dealt with in the judgment of 3 Mr Justice Chitty on page 217 on the left-hand side of 4 the page. The question he is dealing with here is the 5 priority as between the rights of creditors whose debts 6 did not bear interest against the separate estate and 7 the creditors of the joint estate. So it's the two 8 estates priority issue he is determining, not at this 9 point any question of appropriation. That's just at the 10 end of the judgment. At this point he's dealing with 11 the priority issue.</p> <p>12 He refers just below halfway down the page, the 13 sentence begins: 14 "Previously to the orders of 1841 ..." 15 Now, the orders of 1841 are what became --</p> <p>16 MR JUSTICE DAVID RICHARDS: Sorry, where are you?</p> <p>17 MR ZACAROLI: Page 217, left-hand side, just halfway down 18 the page.</p> <p>19 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>20 MR ZACAROLI: He says: 21 "Previously to the orders of 1841 [those were the 22 forerunner to rules 62 and 63] the court of Chancery did 23 not give ...(reading to the words)... the existing rules 24 of court merely give effect to such right."</p> <p>25 MR JUSTICE DAVID RICHARDS: Yes.</p> <p style="text-align: center;">Page 111</p>
<p>1 is that that decree operated as a judgment, treated in 2 equity as a judgment against all creditors of the 3 deceased, and giving them a right to interest because 4 it's a judgment.</p> <p>5 That's the rationale, and I'll make that good by 6 reference to Mr Justice Chitty's judgment, but it's 7 worth, first of all, picking up the rule which by this 8 time gave interest. That can be found at 3D, tab 57. 9 Mr Smith showed this to my Lord yesterday. These are 10 the rules of the Supreme Court 1853, order 55, rules 62 11 and 63.</p> <p>12 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>13 MR ZACAROLI: Rule 62: 14 "Where a judgment order is made directing the 15 account of the debt to the ...(reading to the words)... 16 4 per cent per annum from the date of the judgment or 17 order." 18 So there accrues a right to interest from the date 19 of judgment. True it is that in certain cases -- it's 20 not entirely clear what they are -- where a creditor 21 comes in subsequently and establishes his debt before 22 a judge in chambers, then there's an order of priority 23 so that the right to interest conferred by rule 62 is 24 postponed until after contractual interest has been 25 paid.</p> <p style="text-align: center;">Page 110</p>	<p>1 MR ZACAROLI: Before we deal with the rest of the judgment, 2 I think we should skip to Lord Rommily's explanation in 3 the Herefordshire Banking Company case which my Lord 4 will find at the same bundle, tab 24. We'll come back 5 to Mr Justice Chitty's judgment afterwards.</p> <p>6 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>7 MR ZACAROLI: This was a decision on rule 26 of the 8 Companies (Winding-Up) Rules 1862. Those were similarly 9 orders of court, i.e. they weren't statutory. They were 10 rules made by the judges. My Lord will remember that 11 rule 26, which gave a right of interest to creditors in 12 a winding up at 4 per cent, was held to be ultra vires.</p> <p>13 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>14 MR ZACAROLI: This judgment explains why that was ultra 15 vires but why the similar rule in equity was not.</p> <p>16 MR JUSTICE DAVID RICHARDS: Right.</p> <p>17 MR ZACAROLI: So the headnote reads shortly: 18 "Where a company is wound up under the Companies Act 19 1862 and calls have been made on the shareholders 20 ...(reading to the words)... order of November 1862 is 21 ultra vires and invalid." 22 On page 252, Lord Rommily, Master of the Rolls, 23 says: 24 "I entertain no doubt about this case. It is 25 impossible to get ...(reading to the words)... or</p> <p style="text-align: center;">Page 112</p>

<p>1 entitled to any interest in respect of it." 2 So it has very long been a key distinction between 3 testamentary cases and bankruptcy and winding-up cases 4 that in the case of deceased's estates, the decree 5 ordering the account is a judgment against all creditors 6 entitling them to interest from the date of the decree. 7 MR JUSTICE DAVID RICHARDS: Yes. 8 MR ZACAROLI: So when one goes back to tab 57 and the 9 judgment of Mr Justice Chitty -- sorry, 43, not 57 -- it 10 was in fact the case, although it's not something which 11 he relies upon, but it was in fact the case that by the 12 time any dividends were paid, those were paid in respect 13 of principal and interest which was already accruing as 14 from 1857, the date of the decree. 15 MR JUSTICE DAVID RICHARDS: Right. 16 MR ZACAROLI: Mr Justice Chitty deals with the 17 Bower v Marris point at the very end of his judgment on 18 the right-hand side of page 217. He says, 12 lines from 19 the end: 20 "The remaining question relates to the manner in 21 which the dividends received ought to be accounted for 22 in ascertaining the amount of interest due. All the 23 dividends have been paid in process of law and the 24 account ought to be taking the manner pointed out in 25 Bower v Marris. It is by treating the dividends as</p> <p style="text-align: center;">Page 113</p>	<p>1 dealing there with the question of priority between the 2 two estates. He was certainly not addressing the 3 calculation of interest on the Bower v Marris basis. 4 MR JUSTICE DAVID RICHARDS: Right. 5 MR ZACAROLI: So, properly analysed, Whittingstall v Grover 6 is perfectly consistent with the case we advance on the 7 true rule that one gets from Bower v Marris. 8 I think my learned friend Mr Smith made the point 9 that this case was also after the Bankruptcy Act 1883. 10 Irrelevant. It was dealing with a bankruptcy that 11 started long before that, so the 1883 Act was 12 irrelevant, and no suggestion that its terms were 13 brought to the attention of the judge anyway. It 14 wouldn't have needed to be. 15 The final category of cases where this principle has 16 been applied, so far as cases before this court show, is 17 the debenture holder actions. My Lord was taken to the 18 Calgary and Medicine Hat Land Company, bundle 1B, 19 tab 58. I think my Lord read the headnote. I don't 20 know if my Lord wants to remind himself of it? It's 21 a simple case of payment being made without 22 appropriation. (Pause) 23 MR JUSTICE DAVID RICHARDS: Indeed, yes. 24 MR ZACAROLI: So far as I'm concerned, there is merely one 25 passage I wish to show my Lord which shows how the rule</p> <p style="text-align: center;">Page 115</p>
<p>1 ordinary payments on account and applying each dividend 2 in the first place to interest calculated to the day of 3 such dividend and the surplus, if any, to the reduction 4 of the principal." 5 So he does make it clear in fact that it's interest 6 that's due at the date of the dividend. 7 MR JUSTICE DAVID RICHARDS: Yes. 8 MR ZACAROLI: That's perfectly consistent with our 9 interpretation of both Bower v Marris and the 10 Humber Ironworks cases. Interest was due. Payment was 11 made on account of it and principal from the deceased's 12 estate, and therefore was appropriated towards interest 13 first. 14 MR JUSTICE DAVID RICHARDS: Yes. 15 MR ZACAROLI: Just one more point to make on this judgment 16 My learned friend Mr Smith, echoing a point made in 17 my learned friend Mr Dicker's skeleton, drew attention 18 to a passage on the right-hand side of the page in the 19 middle of the page where the learned judge says: 20 "But where both sets of creditors have received 21 their principal in full...(reading to the words)... on 22 which the general orders are founded." 23 The point being made was the judge didn't 24 distinguish between interest-bearing debts and 25 non-interest-bearing debts. That's true. But he was</p> <p style="text-align: center;">Page 114</p>	<p>1 as applied here is entirely consistent with our case. 2 Page 663 in the judgment of Lord Justice Farwell. 3 MR JUSTICE DAVID RICHARDS: Yes. 4 MR ZACAROLI: It's towards the end of the first paragraph, 5 having cited Staniar v Evans and Preston Banking Co v 6 Allsup. He says: 7 "It was in fact a payment on account of and by 8 reference to the only sum of which the Master had taken 9 an account. It was not a final payment destroying the 10 creditor's rights but a payment on account without 11 prejudice" -- 12 MR JUSTICE DAVID RICHARDS: Sorry, where? 13 MR ZACAROLI: It's just above the break in the page. 14 MR JUSTICE DAVID RICHARDS: 663? 15 MR ZACAROLI: Yes. 16 MR JUSTICE DAVID RICHARDS: I see, yes. 17 MR ZACAROLI: After the reference to Preston Banking Co. 18 MR JUSTICE DAVID RICHARDS: I have it. 19 MR ZACAROLI: "It was in fact a payment on account of and by 20 reference to the only sum...(reading to the words)... 21 right of adjustment which always exists in cases of this 22 nature." 23 The way he expresses it is perfectly consistent with 24 how it was put in the Humber Ironworks cases. There is 25 no appropriation and therefore the creditor's rights are</p> <p style="text-align: center;">Page 116</p>

<p>1 unaffected.</p> <p>2 I showed my Lord this morning the other case that</p> <p>3 dealt with debentures. That was the Smith v Law</p> <p>4 Guarantee case.</p> <p>5 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>6 MR ZACAROLI: Where, as I pointed out this morning, the</p> <p>7 contract required interest to be discharged first but</p> <p>8 that was for the benefit of the debenture holders who</p> <p>9 weren't held to that and, in the circumstances, it was</p> <p>10 in their interest that it be the reverse.</p> <p>11 We make a point in our reply skeleton, not for</p> <p>12 determination in this application, but just to show</p> <p>13 my Lord what happens -- or what might, as it were,</p> <p>14 follow on from Bower v Marris applying. It's quite</p> <p>15 clear that the appropriation towards interest first is</p> <p>16 subject to anything else being inconsistent with that,</p> <p>17 i.e. a term of the contract perhaps or conduct between</p> <p>18 the creditor and the debtor subsequent to the relevant</p> <p>19 bankruptcy or administration. The point in Smith v Law</p> <p>20 Guarantee Trust was that the creditors wanted the</p> <p>21 amounts to be appropriated towards principal because it</p> <p>22 was to their tax advantage.</p> <p>23 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>24 MR ZACAROLI: We refer, again not for determination today</p> <p>25 to the fact that in this the case administrators</p> <p style="text-align: center;">Page 117</p>	<p>1 MR JUSTICE DAVID RICHARDS: Correct. At the stage when</p> <p>2 you're making distributions in respect of principal --</p> <p>3 of proved debts, it would be inappropriate to</p> <p>4 appropriate to interest.</p> <p>5 MR ZACAROLI: My Lord, not if the debt carries interest. If</p> <p>6 the proved debt include interest --</p> <p>7 MR JUSTICE DAVID RICHARDS: Pre-administration interest.</p> <p>8 MR ZACAROLI: Exactly, yes.</p> <p>9 MR JUSTICE DAVID RICHARDS: So when the distributions were</p> <p>10 made -- sorry, I missed the point. You're saying that</p> <p>11 the administrator said, "Well, we are paying this in</p> <p>12 respect of principal due at the date of administration,</p> <p>13 not interest accrued at the date of administration"?</p> <p>14 MR ZACAROLI: They don't make that clear but that must have</p> <p>15 been what they meant because the only interest which</p> <p>16 would have been payable at that date is interest within</p> <p>17 the approved debt. So it only works where the creditor</p> <p>18 has an accrued right to interest. But if the creditor</p> <p>19 did, and chose not to receive that interest --</p> <p>20 MR JUSTICE DAVID RICHARDS: Sorry, I'm getting a bit lost</p> <p>21 here. So the administrator said, "This is principal,</p> <p>22 not interest" or they said, "It's principal, not</p> <p>23 interest". So if some creditors had accrued interest as</p> <p>24 at the administration date for which they had proved,</p> <p>25 then presumably the last distribution did include</p> <p style="text-align: center;">Page 119</p>
<p>1 consciously, expressly stated at the time of making each</p> <p>2 distribution that they were appropriating to principal</p> <p>3 as opposed to interest. And going on to mention the</p> <p>4 fact that they were -- the following sentence referred</p> <p>5 to the fact that they were not withholding tax where</p> <p>6 withholding tax would apply.</p> <p>7 The point is this, simply, that one has to</p> <p>8 investigate therefore, when dividends are paid, whether</p> <p>9 the creditor, knowing that's the way in which it's being</p> <p>10 purportedly appropriated by the administrator, who would</p> <p>11 otherwise have received a smaller sum, because</p> <p>12 withholding tax would have been deducted, receives</p> <p>13 a large sum because it's been appropriated to principal,</p> <p>14 not interest. If that happens, there's a serious</p> <p>15 argument at least that there has been an appropriation.</p> <p>16 The creditor having said, "I'm taking this before</p> <p>17 principal for my tax purposes", can't then renege on</p> <p>18 that.</p> <p>19 MR JUSTICE DAVID RICHARDS: But at the time the dividends</p> <p>20 were paid, if one applies this law, there was no</p> <p>21 appropriation.</p> <p>22 MR ZACAROLI: Ah, sorry, correct.</p> <p>23 MR JUSTICE DAVID RICHARDS: There was no appropriation.</p> <p>24 MR ZACAROLI: Correct; there's no appropriation by operation</p> <p>25 of law.</p> <p style="text-align: center;">Page 118</p>	<p>1 interest.</p> <p>2 MR ZACAROLI: It must have done, yes.</p> <p>3 MR JUSTICE DAVID RICHARDS: Yes, I see. What the relevance</p> <p>4 of that -- any of that to this?</p> <p>5 MR ZACAROLI: Nothing -- that's why I say not for today's</p> <p>6 purposes, other than to recognise that that's one of the</p> <p>7 questions which arises if Bower v Marris as a -- on my</p> <p>8 learned friends' case that's one of the questions which</p> <p>9 arises because one needs to explore whether there has or</p> <p>10 has not in fact been an appropriation.</p> <p>11 MR JUSTICE DAVID RICHARDS: Does it arise? Because the way</p> <p>12 Mr Dicker puts his case, I think -- and Mr Smith -- is</p> <p>13 that there is a notional adjustment or -- I forget the</p> <p>14 word; it doesn't really matter -- of the payments</p> <p>15 previously made?</p> <p>16 MR ZACAROLI: Indeed.</p> <p>17 MR JUSTICE DAVID RICHARDS: The adjustment is between</p> <p>18 principal and accrued interest at the date of</p> <p>19 administration and post-administration interest.</p> <p>20 MR ZACAROLI: Yes.</p> <p>21 MR JUSTICE DAVID RICHARDS: I mean, I accept that I'm not</p> <p>22 anxious to hear argument on this, but I'm just slightly</p> <p>23 puzzled by what its relevance could be, I must say, at</p> <p>24 the moment.</p> <p>25 MR ZACAROLI: Its relevance could be this. I'm not</p> <p style="text-align: center;">Page 120</p>

<p>1 suggesting that the mere fact that the administrators 2 state that is enough to make the appropriation one to 3 principal as opposed to interest; that's not sufficient. 4 The question is whether there has been any agreement, 5 implicit or express, by the creditor to accept an 6 appropriation on that basis. Take the case -- and 7 there's no evidence of this, but these are hypothetical 8 cases, but take the case where the administrators would, 9 if they were paying interest, be required to withhold 10 tax because it was regarded -- 11 MR JUSTICE DAVID RICHARDS: But you must be here talking 12 about pre-administration. 13 MR ZACAROLI: I am indeed talking about pre-administration 14 interest. 15 MR JUSTICE DAVID RICHARDS: I, again, don't quite see what 16 the relevance of that is to this. 17 MR ZACAROLI: Because if it so happens that the creditor for 18 its own benefit, i.e. to get in the early distributions 19 when it wouldn't know there's going to be a surplus of 20 course, so it chooses to have a greater payment to be 21 made to it, a gross payment rather than net, withholding 22 tax, take the gross payment on the basis that that 23 relates to principal -- 24 MR JUSTICE DAVID RICHARDS: Well, I mean, what they're doing 25 is effectively saying, aren't they, "Well, we will</p> <p style="text-align: center;">Page 121</p>	<p>1 been applied demonstrates that it is in fact a rule of 2 the general law. It is not a principle about 3 distribution from insolvency estates. It's a principle 4 from the general law which is applied in the context of 5 insolvency estates in the way that we've expressed. 6 The common feature between bankruptcy, testamentary 7 cases, the debenture action cases is that the payments 8 that were made of dividends, were made without an 9 appropriation and therefore are treated as having been 10 made on account. That's why the language in each of 11 those different areas is expressed as "the creditor's 12 right are unaffected", the right to appropriate, once 13 the surplus arises, or in some cases even though there's 14 no surplus it still retains the right to appropriate. 15 MR JUSTICE DAVID RICHARDS: That is in the context of the 16 creditors receiving interest pursuant to their 17 contractual rights or it might be with the benefit of 18 a judgment or something of that sort? 19 MR ZACAROLI: Yes, a pre-existing right, i.e. an 20 interest-bearing debt. 21 MR JUSTICE DAVID RICHARDS: That's what happened in 22 Bower v Marris. 23 MR ZACAROLI: Yes. 24 MR JUSTICE DAVID RICHARDS: The odd thing about 25 Bower v Marris, just thinking about section 132 of the</p> <p style="text-align: center;">Page 123</p>
<p>1 postpone to later distributions, if there are any, the 2 payment of accrued interest", always assuming this is 3 possible? Assuming it is possible, that's all they're 4 doing. 5 MR ZACAROLI: True, but once they have appropriated, let's 6 say there's a dividend of 50p in the pound. They take 7 that 50 per cent of their claim and appropriate that 8 towards principal. Then that's -- 9 MR JUSTICE DAVID RICHARDS: I see. 10 MR ZACAROLI: Once it is appropriated, it is appropriated 11 they have now had that discharged. As I say, I'm not 12 making too much of this because it's completely 13 irrelevant to the decisions my Lord has to make, but it 14 shows what there is -- as it were, if Bower v Marris 15 were to apply, it gives rise to these further questions. 16 MR JUSTICE DAVID RICHARDS: Okay. 17 MR ZACAROLI: My Lord, is that a convenient moment to take 18 a break? 19 MR JUSTICE DAVID RICHARDS: Yes. Five minutes. 20 (3.13 pm) 21 (Short break) 22 (3.18 pm) 23 MR ZACAROLI: My final point of this second topic, which is 24 the Bower v Marris principle, is that this trawl through 25 the different contexts in which a rule such as that has</p> <p style="text-align: center;">Page 122</p>	<p>1 1825 Act, can I just get that? That's in 3A. 2 MR ZACAROLI: Tab 10. Which section are you after, 3 section 132? 4 MR JUSTICE DAVID RICHARDS: Yes. 5 MR ZACAROLI: Yes, tab 10. 6 MR JUSTICE DAVID RICHARDS: Just by way of passing, it's not 7 completely clear to me at any rate -- you may know this 8 one way or the other -- whether this Act applied to the 9 bankruptcy in Bower v Marris because Thomas Marris was 10 declared bankrupt in January 1812, the last dividend was 11 paid in 1834. I make no comment at all, except to 12 congratulate the administrators of Lehman Brothers. So 13 whether or not it in fact actually applied, but of 14 course we know that Lord Cottenham discussed the Act. 15 MR ZACAROLI: Yes. 16 MR JUSTICE DAVID RICHARDS: Now, under section -- have I got 17 this right -- 132 we have this two-stage interest. 18 First of all, we have those who have a rate of interest 19 reserved or by law payable on their debts which is 20 what -- that's the category into which the creditors in 21 Bower v Marris would fall. 22 MR ZACAROLI: Yes. 23 MR JUSTICE DAVID RICHARDS: But then we have this second 24 layer, all other creditors who have proved who are to 25 receive interest at 4 per cent. So they are creditors</p> <p style="text-align: center;">Page 124</p>

<p>1 without any right to interest. So <i>Bower v Marris</i></p> <p>2 establishes that its principle, if you call it that,</p> <p>3 applies when you're in the first of those categories,</p> <p>4 but what about the second category? You would say not</p> <p>5 applies?</p> <p>6 MR ZACAROLI: No.</p> <p>7 MR JUSTICE DAVID RICHARDS: The reason for that is because</p> <p>8 no interest has accrued?</p> <p>9 MR ZACAROLI: Yes. Had we been there in 1832 and the point</p> <p>10 raised -- 1841 -- that's what we'd have been arguing;</p> <p>11 the same arguments that are running now would be run</p> <p>12 then on that point.</p> <p>13 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>14 MR ZACAROLI: This brings me, my Lord, on to the third topic</p> <p>15 which is indeed that rule only works where there is</p> <p>16 interest accruing. It only relates to interest-bearing</p> <p>17 debts.</p> <p>18 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>19 MR ZACAROLI: It may be worth keeping <i>Bower v Marris</i> open</p> <p>20 because --</p> <p>21 MR JUSTICE DAVID RICHARDS: I have that here.</p> <p>22 MR ZACAROLI: -- that is -- one of the submissions my</p> <p>23 learned friend made relates to it. As I said, the</p> <p>24 essential aspect of appropriation -- the essential</p> <p>25 requirement of appropriation is that there are two</p> <p style="text-align: center;">Page 125</p>	<p>1 anyway because they were not -- these aren't</p> <p>2 transcriptions of judgments, these are people in court</p> <p>3 listening and writing it down.</p> <p>4 MR JUSTICE DAVID RICHARDS: No.</p> <p>5 MR ZACAROLI: Or sometimes not. I found a report the other</p> <p>6 day of a reporter who said, "I had a terrible case of</p> <p>7 the gout and therefore missed this case, but this is</p> <p>8 what I'm told the judge said".</p> <p>9 The reason he can't possibly have been considering</p> <p>10 at all the last part of section 132 is because the</p> <p>11 context of this case was rights against a co-obligor.</p> <p>12 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>13 MR ZACAROLI: Let's assume that there had been interest at</p> <p>14 4 per cent for the creditor, where the debt did not bear</p> <p>15 interest. That could have no relevance against the</p> <p>16 co-obligor. The co-obligor could not take the advantage</p> <p>17 of the interest rate that is being paid from the</p> <p>18 bankruptcy and say, "Well, I'm owed interest as well.</p> <p>19 Therefore, as against me you're appropriating payments</p> <p>20 towards interest -- principal first rather than</p> <p>21 interest". So the whole promise of the case means it</p> <p>22 can't possibly have been considering the non-contractual</p> <p>23 rights creditor.</p> <p>24 I showed my Lord, I think, probably five or six</p> <p>25 examples in the judgment where the reasoning is premised</p> <p style="text-align: center;">Page 127</p>
<p>1 debts, two liabilities, existing at the date when the</p> <p>2 payment is made. That simply does not apply in relation</p> <p>3 to a non-interest-bearing debt in a bankruptcy case. In</p> <p>4 opening I said there were two -- that was one of two</p> <p>5 reasons why the rule couldn't apply.</p> <p>6 The other was the whole rationale of the reasoning</p> <p>7 in <i>Bower v Marris</i> is that you're respecting, giving</p> <p>8 effect to the full rights of the creditor which are its</p> <p>9 rights to interest.</p> <p>10 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>11 MR ZACAROLI: It is said against us that on page 357 of the</p> <p>12 report of <i>Bower v Marris</i> the Lord Chancellor recited</p> <p>13 section 132 or referred to section 132 without</p> <p>14 distinguishing between the contractual part of it and</p> <p>15 the non-contractual part of it.</p> <p>16 MR JUSTICE DAVID RICHARDS: Page ...?</p> <p>17 MR ZACAROLI: 357.</p> <p>18 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>19 MR ZACAROLI: Just in the second paragraph there. So what</p> <p>20 is said is <i>Bower v Marris</i> is a case where the judge was</p> <p>21 considering and deciding in relation to the</p> <p>22 non-contractual creditors or the non-interest-bearing</p> <p>23 debts. My Lord, that is simply wrong. It's a very</p> <p>24 short reference to the Act. True, it doesn't there</p> <p>25 distinguish. One has to be careful with these reports</p> <p style="text-align: center;">Page 126</p>	<p>1 on the fact that the creditor has a contractual right to</p> <p>2 interest.</p> <p>3 MR JUSTICE DAVID RICHARDS: Yes, you did.</p> <p>4 MR ZACAROLI: My learned friend Mr Dicker said yesterday</p> <p>5 that every case which has decided this point,</p> <p>6 i.e. whether it extends to non-interest-bearing debts,</p> <p>7 has concluded that the principle does apply. Well,</p> <p>8 there were four cases.</p> <p>9 The first is <i>Bower v Marris</i> itself. Wrong for the</p> <p>10 reasons I've just given. The next two are to the</p> <p>11 Attorney General of Canada v Confederation Trust, and</p> <p>12 <i>Hibernian</i>. Yes, I accept that those cases did apply the</p> <p>13 principle or what they thought was the principle in</p> <p>14 <i>Bower v Marris</i> to the case where there were debts which</p> <p>15 were not interest-bearing debts. Those cases are wrong</p> <p>16 for the reasons we have been through. I'm not going to</p> <p>17 repeat those.</p> <p>18 MR JUSTICE DAVID RICHARDS: No.</p> <p>19 MR ZACAROLI: The fourth was <i>Whittingstall v Grover</i>.</p> <p>20 As I hope I have explained to my Lord today,</p> <p>21 <i>Whittingstall v Grover</i> is a case where there was in fact</p> <p>22 interest accruing from the date of a judgment in equity</p> <p>23 which was a judgment against all creditors giving them</p> <p>24 a right to interest from that date.</p> <p>25 MR JUSTICE DAVID RICHARDS: Yes.</p> <p style="text-align: center;">Page 128</p>

<p>1 MR ZACAROLI: We said in opening that that's a freestanding 2 point; that whatever else my Lord may decide in this 3 application my Lord should not decide that any creditor 4 without a right to interest pre-administration can reap 5 the benefit of the principle in Bower v Marris. But it 6 goes further because if it doesn't apply to those 7 creditors, then it can't apply to anyone with 2.88(7) 8 without creating the source of complications which the 9 Cork Committee were set against. Indeed it makes part 10 of the rule unworkable. 11 I have already made my general submission based on 12 the passages from Mr Justice Dixon in MacKenzie v Rees 13 that applying it at all creates problems. These are 14 additional problems. 15 MR JUSTICE DAVID RICHARDS: Yes. 16 MR ZACAROLI: The first thing that it does is that it 17 creates differential treatment amongst creditors within 18 2.88(7) because it treats some creditors as entitled to 19 interest for a lot longer than others, because the 20 essence of Bower v Marris is it keeps interest rolling 21 on, even though the principal debt has been paid. 22 So the period for which the debt is outstanding 23 means something different for judgments rate creditors 24 and Bower v Marris creditors. 25 The second point is it creates complications where</p> <p style="text-align: center;">Page 129</p>	<p>1 be that they have an indefinite right to interest that 2 rolls forever, so the quantum of their claim is 3 impossible to calculate. 4 MR JUSTICE DAVID RICHARDS: Was that a problem in 5 Bower v Marris it self? 6 MR ZACAROLI: Well, it could have been. One doesn't know on 7 the facts whether there was sufficient to pay everyone 8 in full. 9 MR JUSTICE DAVID RICHARDS: No. 10 MR ZACAROLI: But it is -- it's not just a theoretical 11 problem. It's a practical problem in any case where you 12 have to distribute amongst a number of creditors, but it 13 creates this particular problem where you have some -- 14 only some creditors who are entitled to it because it 15 makes reserving for their claims very difficult. You 16 have -- let's say half your creditors have judgment 17 rates interest. You know exactly the amount they're 18 entitled to so you have £50 to distribute amongst 19 everybody. You know what percentage of that they are 20 entitled to. You don't know what percentage the rest 21 are entitled to. So you have to reserve for those 22 claims, and in reserving for those claims you can't pay 23 out the other claims unless you know there's a maximum 24 amount above which that interest can't extend. 25 MR JUSTICE DAVID RICHARDS: Just go through that. I mean</p> <p style="text-align: center;">Page 131</p>
<p>1 creditors have a contractual rate but it's less than 2 8 per cent. It does seem to us bizarre that a creditor 3 should benefit from the greater rate of interest which 4 the Judgments Act gives it but nevertheless be able to 5 say, "Ah, but I have a contractual rate to interest at", 6 let's say, "2 per cent, and I can apply dividends to 7 that part of my interest first". 8 MR JUSTICE DAVID RICHARDS: Yes. 9 MR ZACAROLI: The third problem is that -- it follows on 10 from the fact that the period for which the debt is 11 outstanding will be different between judgment rate 12 creditors and Bower v Marris creditors. That means that 13 the total amount of interest to which a Bower v Marris 14 creditor is entitled cannot be known until there is 15 a sufficient surplus to pay the very last amount of 16 principal and interest. Until that point in time, by 17 definition, every payment is going to discharge interest 18 first leaving a rump of principal upon which interest 19 still accrues. 20 So take the case of a distribution under 2.88(7), 21 when you don't have enough to pay everyone everything in 22 full, at that point in time you will not know what the 23 ultimate claim of the Bower v Marris creditor is against 24 that surplus. It entirely depends how long it is before 25 you are able to pay more distributions, if any. It may</p> <p style="text-align: center;">Page 130</p>	<p>1 the problems your contending with is where -- is 2 particularly acute when you don't have enough clearly to 3 pay everybody off. 4 MR ZACAROLI: Yes. 5 MR JUSTICE DAVID RICHARDS: You could reach a point where 6 you say, "We clearly have enough to pay everyone off". 7 MR ZACAROLI: Yes. 8 MR JUSTICE DAVID RICHARDS: So you -- so we're in the 9 position where we don't know. So, as you say, it may be 10 that interest is continuing to run, but every time -- 11 I appreciate there's going to be a gap between the date 12 of calculating the distribution and the distribution, 13 but you can draw the line then, can't you? 14 MR ZACAROLI: You could do but that means -- 15 MR JUSTICE DAVID RICHARDS: It may still run on to the next 16 distribution. 17 MR ZACAROLI: That means -- that assumes that the interest 18 you're paying, when you make an interim distribution 19 you're only paying interest up to a certain date. 20 That's one way out of it; that you say, "Okay, we will 21 pay interest only up to this date". That's a number you 22 can calculate, whether you have a Bower v Marris 23 calculation or not. The rule says you pay the interest 24 out of the surplus pari passu which means you're looking 25 at the total claims against this surplus because if you</p> <p style="text-align: center;">Page 132</p>

<p>1 waited a bit longer and got -- there was more surplus to 2 pay, then there would be more interest payable to the 3 Bower v Marris creditors. So it's the same problem 4 wherever you have an -- it's a similar problem to 5 wherever you have a distribution pari passu to be 6 made: there's not enough, and you know the size of some 7 claims but not the size of others.</p> <p>8 MR JUSTICE DAVID RICHARDS: I suppose it's that latter bit 9 I'm not quite clear about. Why don't you know the size 10 of the claims at any particular moment?</p> <p>11 MR ZACAROLI: Because you only know the size of the claims 12 for interest up to that moment in time but they're still 13 entitled to the interest from that surplus even after 14 the moment you're paying this particular dividend out.</p> <p>15 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>16 MR ZACAROLI: You have to -- you can --</p> <p>17 MR JUSTICE DAVID RICHARDS: While there is -- applying 18 Bower v Marris, while there is any principal outstanding 19 interest continues to run.</p> <p>20 MR ZACAROLI: Yes. As I say, there is a way out of it but 21 that would not then be strictly sharing the surplus 22 amongst those who are ultimately entitled to it 23 pari passu, because those who have interest running on 24 have nothing to claim that interest against. They're 25 not being paid out of the same surplus because you have</p> <p style="text-align: center;">Page 133</p>	<p>1 to the question: do the words "rate applicable apart 2 from the administration" in 2.88(9) encompass the 3 Bower v Marris calculation? As I mentioned earlier, we 4 say the answer to that is very clearly "no".</p> <p>5 First of all, we don't necessarily align ourselves 6 with the wording of the administrators' concession in 7 their skeleton. We have made our concession clear here. 8 This is issue 3. We have made our concession clear here 9 that "rate" as a matter of English language is a word 10 which is capable of covering both a simple rate and 11 a compound rate; otherwise there's an umbrella term 12 "rate of interest" within which you can have two 13 possibilities, a simple rate or a compound rate.</p> <p>14 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>15 MR ZACAROLI: We're all familiar with the concept of APR. 16 There's always a way of analysing a compound rate as 17 a simple rate on an annualised basis.</p> <p>18 I showed my Lord paragraph 88 of the White Paper 19 that followed the Cork Report --</p> <p>20 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>21 MR ZACAROLI: -- very clearly indicating that they were 22 extending the amount of interest payable beyond the 23 judgments rate to include a contractual rate of interest 24 that one might have. I suggest the draughtsman was 25 undoubtedly thinking along these lines, namely "it's</p> <p style="text-align: center;">Page 135</p>
<p>1 paid it to those who have a fixed rate.</p> <p>2 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>3 MR ZACAROLI: Where this leads, the fourth proposition, is 4 that for 2.88(9), you need to know which is the higher 5 of the Judgments Act rate or the contractual rate.</p> <p>6 If the contractual rate carries an entitlement to 7 Bower v Marris, this is the, as it were, the last 8 complication to which it gives rise, because the only 9 way in which you can measure which is the higher of, the 10 fixed judgment rate or the rate of 4 per cent, say, with 11 the right of Bower v Marris, is by knowing what period 12 of interest you're going to be paying the Bower v Marris 13 creditor for because over the course of a year it may 14 well be that 4 per cent, even with Bower v Marris, 15 doesn't get you above an 8 per cent comparison. So you 16 don't -- in many cases you will know that you've already 17 got a higher number. You don't know what it's 18 ultimately going to be, but it's a higher 19 number already. But some cases you won't know whether 20 the Judgments Act rate is or is not higher than the 21 contractual rate if you were to apply Bower v Marris to 22 it. So it renders in least some cases 2.88(9) 23 unworkable.</p> <p>24 MR JUSTICE DAVID RICHARDS: I see.</p> <p>25 MR ZACAROLI: Now, linked to that I'm going to come head-on</p> <p style="text-align: center;">Page 134</p>	<p>1 rate, nothing more".</p> <p>2 The next point is that "rate" is a fundamentally 3 different concept to the Bower v Marris calculation. 4 Bower v Marris is not the same as compounding in 5 economic effect. Indeed, it has no impact on the rate. 6 Bower v Marris is simply about the order in which you 7 treat dividends as having been paid, whether towards 8 principal or interest. In order to make the choice you 9 would need to know what interest was outstanding 10 according to the rate. So the rate is a necessary 11 pre-existing factor before you can apply Bower v Marris</p> <p>12 The third point is this, that the use of the word 13 "rate" has to be considered in the context of its place 14 in the rules and the purpose of that rule. The purpose 15 of 2.88(9) is simply to work out whether the rate apart 16 from administration was higher than the Judgments Act 17 rate. It was to preserve the right of those who have an 18 entitlement to a rate greater than the Judgments Act 19 rate to recover statutory interest at that rate. There 20 is no basis for incorporating Bower v Marris into the 21 Judgments Act rate, the rate with which that comparison 22 is to be made. So even if they were right about the use 23 of the word "rate" in 2.88(9), it couldn't possibly 24 incorporate the concept of Bower v Marris into the 25 Judgments Act rate as well.</p> <p style="text-align: center;">Page 136</p>

<p>1 The fourth point is it can only apply where the 2 relevant rate was higher than 8 per cent because, if 3 not, then it's irrelevant because the Judgments Act rate 4 would apply. So, again, the rule is about determining 5 which is the higher and only then does the contractual 6 rate apply, so a 2 per cent right of interest, if with 7 Bower v Marris it's not higher than 8 per cent, would 8 not win the battle and the Judgments Act rate remains. 9 Which leads to the last point I have already 10 made: how do you determine that? In some cases you will 11 know, but in many cases you will not know at any 12 particular point in time which is the higher of the two 13 rates if you take Bower v Marris into account. 14 Now, just one final point on this. My learned 15 friend Mr Smith argued that compounding is not a rate at 16 all. It's interest on interest which logically lead -- 17 well, logically that submission would lead to the 18 conclusion that compound interest is not within 2.88(9) 19 because if it's not a rate, then it can't be within the 20 rule at all. Of course he's not arguing that. Everyone 21 accepts that compound interest is within 2.88(9), but 22 that's because it is in fact a rate. 23 That leaves just the sub-issue within, I think, 24 issue 3: does compounding continue after the relevant -- 25 after the final dividend payment? So if you have</p> <p style="text-align: center;">Page 137</p>	<p>1 MR JUSTICE DAVID RICHARDS: Yes. 2 MR ZACAROLI: I am going to return now to my learned friend 3 Mr Dicker's three core propositions, having been through 4 all the cases, and answer them very shortly. 5 His first proposition, and this was as to the 6 construction of rule 2.88(7), his first proposition was 7 that the features of rule 2.88 which we rely upon were 8 also features of the previous regimes. My Lord, we 9 disagree. Critically the right to interest under 10 rule 2.88 is not calculated as whatever claim could have 11 been asserted against the debtor once solvent. So cases 12 considering regimes where that was the position have no 13 relevance at all to the construction of 2.88 which must 14 be undertaken on the words in the context of the 15 statute. 16 MR JUSTICE DAVID RICHARDS: Yes. 17 MR ZACAROLI: His second proposition was in substance the 18 arguments that we are making were made and rejected in 19 relation to the previous regime. Again, we say "no". 20 The arguments we are advancing could not have been made 21 in relation to all of the English and Australian and 22 Scottish cases because the regime was fundamentally 23 different. The two regimes where there was sufficient 24 similarity for the argument to have been run, i.e. in 25 Canada and in Ireland, in the two cases we've looked at,</p> <p style="text-align: center;">Page 139</p>
<p>1 a compound rate, do you carry on compounding that rate 2 and accruing interest at that compound rate after the 3 date the final dividend is paid. The answer is "no". 4 First of all, as a matter of statutory construction, 5 interest is payable for the period between the date of 6 administration and the date the dividend is paid and 7 therefore it's contrary to the statute. 8 MR JUSTICE DAVID RICHARDS: Yes. 9 MR ZACAROLI: Secondly, it creates all of the same problems 10 I've just referred you to relation to Bower v Marris, in 11 particular it means you don't know which is the higher 12 of the rates for the same reason; it's continuing, so 13 you just don't know. 14 MR JUSTICE DAVID RICHARDS: Yes. 15 MR ZACAROLI: How that works, my Lord, is because the 16 period -- interest is payable for the periods the debt 17 is outstanding, so that if you have a debt that's paid 18 by way of interim dividends, let's say one interim 19 dividend after six months, the rest after a year, what 20 that means is you treat the debt that was paid after six 21 months as a slice of the debt upon which compound 22 interest accrues during the period up until which that 23 was paid, and the remainder of the debt, the other £50, 24 has been outstanding for the whole year and therefore 25 compounds for the whole year. It's very simply done.</p> <p style="text-align: center;">Page 138</p>	<p>1 the arguments were not advanced and therefore not 2 rejected. 3 MR JUSTICE DAVID RICHARDS: Right. 4 MR ZACAROLI: The third -- his third proposition was that 5 the courts under the old regimes construed statutory -- 6 the statutory scheme as providing a mode of calculation 7 for interest which proceeded on the basis that dividends 8 were treated as notionally discharging interest before 9 principal. We say, again, wrong. They proceeded on the 10 basis that they were not construing any statutory scheme 11 about paying interest. The extent to which they 12 construe the statutory scheme was to conclude that 13 creditors were remitted to their contractual rights once 14 the surplus arose, and determining that payments made to 15 date were not appropriations at all and therefore it 16 left the creditor free to exercise his right of 17 appropriation. 18 So, in short order, that's our answer to the three 19 basic propositions. 20 MR JUSTICE DAVID RICHARDS: Thank you. 21 MR ZACAROLI: I now turn to the last of the points I was 22 going to raise under issue 2 which is questions of 23 principle and policy. 24 MR JUSTICE DAVID RICHARDS: Yes. 25 MR ZACAROLI: We were challenged, I think, to say that there</p> <p style="text-align: center;">Page 140</p>

<p>1 is no -- or by the proposition that there's no policy 2 reason why the long-standing rule in <i>Bower v Marris</i> 3 should have been abolished in 1986. Now, we first of 4 all say that the premise behind that challenge is flawed 5 because there's no question of us seeking <i>Bower v Marris</i> 6 to be abolished. We simply say it has no application to 7 the way that legislature chose to address the issue of 8 post-insolvency interest in 1986, it's just irrelevant 9 to the question.</p> <p>10 We also say the premise is flawed insofar as it 11 suggests there was a long-standing and, thus, I assume 12 well-known rule of <i>Bower v Marris</i>. I have made 13 submissions before about the length of time, about 14 a century, in which no reference to <i>Bower v Marris</i> was 15 made in the context of distributions from an insolvency 16 estate, whether corporate or personal, and whether in 17 this jurisdiction or abroad.</p> <p>18 We also disagree with the premise because it is not 19 the case that any such principle in any event was -- 20 ceased to be relevant in 1986 in bankruptcy. It had 21 already been irrelevant well over 100 years, since 1883, 22 since which time there is no case and no textbook, other 23 than one small reference in 1904, which has even cited 24 the case in a bankruptcy context.</p> <p>25 True it is the rule of appropriation that where</p> <p style="text-align: center;">Page 141</p>	<p>1 on <i>Bower v Marris</i> basis, but in many cases creditors' 2 rights are enhanced.</p> <p>3 Equally importantly, that bundle of rights 4 constituted a bundle of obligations imposed on the 5 insolvent estate that were new and different from the 6 obligations the company had had before liquidation or 7 administration.</p> <p>8 Now, there was a deliberate choice in 1986, as we 9 saw from the Cork Report -- the Cork Committee Report, 10 taken up by the legislature, a deliberate choice to 11 adopt the bankruptcy model, not the remission to rights 12 against the solvent debtor model which had been the 13 feature of company law for the last 150 years. It is 14 simply a consequence of the fact the legislature chose 15 an option which gave these creditors -- gave creditors 16 a bundle of new rights, imposed on the company new 17 obligations, and did not revert to contractual rights -- 18 that the right of a creditor against a solvent debtor to 19 appropriate, which is part of the general law, did not 20 get carried along with it.</p> <p>21 The third point is this, that what lies behind the 22 Senior Creditor Group's challenge is the assumption that 23 whatever contractual rights to interest a proving 24 creditor had against a solvent debtor must be fully 25 satisfied before anything is left for anyone behind them</p> <p style="text-align: center;">Page 143</p>
<p>1 payments are made by a solvent debtor to a creditor on 2 account the creditor has the right to appropriate -- and 3 the presumption is the appropriation will be to interest 4 before principal -- is a long-standing rule and no doubt 5 well-known.</p> <p>6 And in the only English cases that have considered 7 the proposition -- the Humber Ironworks quartet and 8 Lines Brothers, a century apart -- that was indeed the 9 relevant principle because the statute simply left 10 creditors to pursue their contractual rights against the 11 company for post-liquidation interest once there was 12 a surplus and the company was now treated as solvent.</p> <p>13 So we disagree fundamentally with the premise behind 14 the challenge, but addressing the question why is it 15 that it might have been thought that the right of 16 a solvent -- the right of a creditor as against 17 a solvent debtor to appropriate was not applicable in 18 winding up or bankruptcy from 1883 or 1986, as the case 19 may be, the fact is that both those regimes, bankruptcy 20 in 1883, companies in 1986, create for creditors 21 a bundle of new rights which in many cases enhance the 22 pre-existing rights of the creditors. In some cases 23 they didn't, I accept that. In some cases, if we're 24 right on <i>Bower v Marris</i>, it did deprive a creditor of 25 the right against a solvent debtor to the appropriation</p> <p style="text-align: center;">Page 142</p>	<p>1 in the queue. That undoubtedly was the premise behind 2 the decision in <i>Bromley v Goodere</i> and in <i>Bower v Marris</i> 3 too and therefore many of the cases around that time 4 that did the same thing.</p> <p>5 I go back here to the colour I gave earlier about 6 the context at that time, namely debtors -- bankrupts 7 were considered offenders who should be made to pay for 8 the delay caused to their creditors in getting payment.</p> <p>9 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>10 MR ZACAROLI: The comments therefore and the decisions even 11 in those cases must be seen in that context.</p> <p>12 The world today is very different.</p> <p>13 Going back to 1883 for a moment, the world in 1883 14 was different because that -- it wasn't coterminous with 15 the abolition of criminality in bankruptcy but it 16 followed shortly after that. So a bankrupt was no 17 longer a criminal in 1883.</p> <p>18 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>19 MR ZACAROLI: What Parliament did in 1883, we would say 20 beyond any doubt, is took away the contractual rights of 21 creditors if they were in excess of 4 per cent and left 22 everyone with a 4 per cent claim for post-bankruptcy 23 interest. We don't know what the policy of the 24 legislators was. We simply don't know at this distance.</p> <p>25 One possible and I submit tenable reason for that</p> <p style="text-align: center;">Page 144</p>

<p>1 decision was that there is a qualitative distinction 2 between a debtor who is refusing to pay and a debtor who 3 is insolvent, such that the administration of its estate 4 by third parties takes time before its debts can be 5 paid. In the first category, the creditor's contractual 6 rights, whatever they may be, should be asserted because 7 the debtor is simply refusing to comply with those 8 rights. In the second -- and the debtor can seriously 9 and correctly be seen as at fault in not repaying. In 10 the latter, there is no fault or at least there may well 11 be no fault on the debtor at all for the time taken to 12 distribute assets -- to get in assets, to realise them, 13 to deal with issues between creditors and end up paying 14 dividends. So one tenable reason for the distinction is 15 that when you look at a bankruptcy and take away the 16 idea of the debtor being an offender, all creditors are 17 suffering equally by the delay which follows from the 18 date of bankruptcy and they're all suffering because of 19 whatever it is within the administration of that estate 20 which is taking time.</p> <p>21 The same point can be made in relation to companies, 22 but there's an additional point in relation to companies 23 post-1986, and that is that it isn't just a debate or 24 a dispute between the creditors and the debtor which is 25 the case in bankruptcy. There are only two interested</p> <p style="text-align: center;">Page 145</p>	<p>1 against the insolvent debtor and the reason why 2 Bower v Marris would simply be irrelevant thereafter. 3 Those that -- that delay affects all creditors 4 equally, even though creditors would have had a right to 5 interest beforehand and others don't. There is that 6 distinction between them, but they're all being 7 prejudiced in the same way by the delay in the 8 administration of the estate.</p> <p>9 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>10 MR ZACAROLI: Now, hand-in-hand with this, to develop 11 a point I made a moment ago, it's wrong to assume that 12 the delay in payment of the dividend is down either to 13 the company or the debtor in bankruptcy. The delay, for 14 example, might easily be caused by creditors fighting 15 over priority issues or one creditor or some creditors 16 disputing the quantum of their claims, meaning there 17 can't be distribution to anyone until those are sorted 18 out, or it may just be delay because third parties are 19 taking advantage of the insolvency to refuse to pay up 20 and therefore time is taken to realise the assets.</p> <p>21 There's a whole plethora or reasons why administration 22 of an insolvent estate takes time and none of those can 23 be equated with the fault of the debtor or the company 24 or, certainly not, the fault of those other people 25 entitled to the priority waterfall below unsecured</p> <p style="text-align: center;">Page 147</p>
<p>1 parties. In a company you have the creditors, on the 2 one hand, in this dispute and you have everyone else who 3 is entitled to recover their investment from the debtor, 4 the corporate debtor, that falls below them in the 5 priority waterfall on the other hand.</p> <p>6 There is no way in which it would be right to 7 equate, for example, a subordinated creditor with the 8 debtor as offender under the old bankruptcy regime. 9 They're simply someone who is entitled to be paid from 10 the estate. Similarly, shareholders. You can have all 11 sorts of different layers of equity, preferential, 12 ordinary and various layers in between. They are all 13 people who have invested in this corporate personality 14 and who are entitled to be paid what they are owed or 15 entitled to in the case of an ordinary shareholder once 16 the statutory scheme has been completed. None of them 17 can properly be equated with the debtor whose fault it 18 was that creditors were not being paid timely -- in 19 a timely fashion under the Bromley v Goodere-type 20 situation.</p> <p>21 So the delay affects all of them equally, which 22 leads to the conclusion they should all have the same 23 nature of rights against the insolvent debtor. That 24 perfectly explains, we say, the decision in 1883 to give 25 all creditors the same rate of interest and nothing more</p> <p style="text-align: center;">Page 146</p>	<p>1 ordinary creditors.</p> <p>2 One reference, my Lord, if I may. My learned friend 3 Mr Dicker referred you to it, but I'm not sure he went 4 to the case. It's Danka Business Systems.</p> <p>5 MR JUSTICE DAVID RICHARDS: He mentioned it.</p> <p>6 MR ZACAROLI: Acknowledging that this is a different 7 context, the judgment is in volume 1E, tab 162.</p> <p>8 My Lord may remember this is a case about the 9 valuation of contingent plans and, in particular, 10 whether, where there's a surplus to return to members, 11 the liquidator should make a reserve for the possibility 12 of a contingency which hasn't yet fallen in, later 13 falling in, before paying every available asset back to 14 the members. The court of appeal held that he 15 shouldn't.</p> <p>16 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>17 MR ZACAROLI: There is just one short passage that I would 18 ask my Lord to look at which is in the judgment of 19 Lord Justice Patten at paragraph 36. Perhaps my Lord 20 can read 36 and 37.</p> <p>21 MR JUSTICE DAVID RICHARDS: I will, certainly. (Pause)</p> <p>22 Yes.</p> <p>23 MR ZACAROLI: The key sentence is the last one in 24 paragraph 37, the reference to the company's liabilities 25 in section 107 must be to the liabilities as determined</p> <p style="text-align: center;">Page 148</p>

<p>1 in accordance with the 1986 rules, otherwise they serve 2 no useful purpose. Section 107 of course is the section 3 which tells us to distribute the company's property in 4 a voluntary winding up and in a satisfaction of the 5 company's liabilities pari passu and, subject to that, 6 distribution to the members. 7 MR JUSTICE DAVID RICHARDS: Yes. 8 MR ZACAROLI: There's an echo there, we suggest, with the 9 1883 Bankruptcy Act in relation to interest and the way 10 that's been construed subsequently in the Baughan case 11 and by the Cork Committee themselves, that once you pay 12 what the statute requires to be paid, the bankrupt gets 13 it next; there's no gap for anyone else to come in at 14 that point. 15 MR JUSTICE DAVID RICHARDS: No. 16 MR ZACAROLI: Similarly, here, you construe what is payable 17 pursuant to the statutory regime and, once you have done 18 that, it goes back to the bankrupt -- sorry, it goes to 19 the next person entitled, which would be the members 20 ultimately in the company case. 21 MR JUSTICE DAVID RICHARDS: Yes. 22 MR ZACAROLI: The question as to what rights exist in the 23 statutory scheme is a question of construction of the 24 statute and the rules. Of course my Lord has decided in 25 the Waterfall 1 judgment that one of the rights which is</p> <p style="text-align: center;">Page 149</p>	<p>1 a creditor would have against a solvent debtor to apply 2 payments on a Bower v Marris basis, if Parliament felt 3 that was right to do that in bankruptcy and provide that 4 immediately after satisfaction of creditors' proved 5 debts and that statutory interest in full the surplus 6 was returned to the bankrupt, we ask what possible 7 policy would there be in reversing that in relation to 8 companies? 9 One starts the history with the bankrupt being the 10 debtor, the offender, someone who must be made to pay 11 for delaying payment of his creditors. But in 12 a corporate context, for the reasons I've been through, 13 you can't equate any of the people in the queue, in the 14 priority waterfall below unsecured creditors, as being 15 in any sense at fault or offenders themselves. So what 16 would be the purpose in Parliament in 1986 somehow 17 meaning to introduce or allow in the corporate context 18 the creditors to have that right; more importantly, 19 perhaps, to burden those in the queue below the 20 unsecured creditors with that additional burden when the 21 bankrupt himself is not burdened with that? 22 My last task in relation to issue 2 is to deal with 23 some miscellaneous point on this issue of policy and 24 principle raised in the SCG's skeleton at paragraph 120. 25 I will have dealt with quite a bit of these points</p> <p style="text-align: center;">Page 151</p>
<p>1 left outstanding to be satisfied before a return to 2 members is the currency conversion. 3 MR JUSTICE DAVID RICHARDS: Yes. 4 MR ZACAROLI: The real point we'll come on to in issue 39 5 then is whether this interest claims can fall within the 6 same category as currency conversion claims or whether 7 there is some distinction between them. We'll come on 8 to that. 9 MR JUSTICE DAVID RICHARDS: Right. 10 MR ZACAROLI: But, taking that statement from Danka, looking 11 at the way the Bankruptcy Act was construed and dealt 12 with in relation to post-bankruptcy interest, we say 13 it's really unhelpful and distracting to try to construe 14 the statutes by reference to broad statements, such as 15 those of Lord Hardwicke in Bromley v Goodere, about 16 everyone must be satisfied in full before the rubbed 17 gets anything. That doesn't really help in construing 18 the statute today. 19 MR JUSTICE DAVID RICHARDS: Yes. 20 MR ZACAROLI: Finally, on this topic, on this subject, if 21 it's right, which we say it is, that Parliament since 22 1883 has seen fit to provide creditors with a fixed rate 23 of interest without allowing them to pursue their claims 24 for a higher rate by way of contract against the debtor 25 and thus taking away the right that a solvent --</p> <p style="text-align: center;">Page 150</p>	<p>1 generally on the way through so I'm going to pick up 2 a few additional matters. 3 Sub-paragraph 1, they say: 4 "The rule in Bower v Marris is consistent with 5 fundamental policies and principles ... it ensures that 6 all creditors, whether those with a right to interest 7 apart from the administration (whether contractual or 8 statutory) or those with a right arising under the 9 statutory scheme are compensated for being kept out of 10 their money." 11 My Lord, the fact is that the right given by the 12 statute to all creditors to be paid interest for the 13 delay caused by the distribution of dividends is what 14 compensates them for the time value of money during the 15 administration. So that point of principle has been 16 answered in 1986 for companies but long ago in relation 17 to bankruptcy to by allowing a statutory interest to 18 everybody. 19 The complaint that creditors don't get compensation 20 for delay in paying interest -- in the payment of 21 interest is simply because the statute does not provide 22 for interest upon statutory interest. It's not there. 23 It's never been there. Therefore, it would be wrong, as 24 it were, by a side-wind to say "because there's no 25 interest on interest Bower v Marris must apply" reverses</p> <p style="text-align: center;">Page 152</p>

<p>1 the correct order here.</p> <p>2 The correct order is the statute does not allow</p> <p>3 interest upon interest. It's a decision taken. There's</p> <p>4 no suggestion that the Cork -- the authors of the</p> <p>5 Cork Report ever recommended that there should be</p> <p>6 a third round of proofs for the delay caused in paying</p> <p>7 interest. Presumably a fourth round after that because</p> <p>8 of the delay on paying the interest on the interest. It</p> <p>9 would be never-ending.</p> <p>10 Sub-paragraph 3, the point here is that</p> <p>11 Bower v Marris ensures equality of treatment, namely</p> <p>12 that creditors who have their provable claims admitted</p> <p>13 and paid early are not prejudiced by comparison with</p> <p>14 creditors who have their provable claims admitted and</p> <p>15 paid later. We submit this is a bad point. If you take</p> <p>16 this example, creditor A is paid £100 after one year.</p> <p>17 Creditor B is paid £100 after five years. Interest is</p> <p>18 only payable after five years when creditor B gets paid</p> <p>19 in full. It's true that creditor B gets five years' of</p> <p>20 interest. Creditor A doesn't get five years of</p> <p>21 interest, only one year. But the short answer to that</p> <p>22 supposed disadvantage is creditor A has had his money</p> <p>23 since the end of the first year. So both are affected</p> <p>24 equally. Both are delayed in getting interest payable</p> <p>25 on the relevant outstanding period. So for the first</p> <p style="text-align: center;">Page 153</p>	<p>1 avoids prejudice in other situations, including, for</p> <p>2 example, where a creditor with security or a claim</p> <p>3 against another person who was jointly and severally</p> <p>4 liable. As Lord Cottenham stated in Bower v Marris, it</p> <p>5 would be extraordinary if a co-obligor was able to</p> <p>6 benefit from prior payments having been attributed to</p> <p>7 principle. That's not a problem because, as we accept,</p> <p>8 the creditor's rights against a co-obligor would be</p> <p>9 unaffected. He has his rights of appropriation. He has</p> <p>10 his rights of appropriation in a sense against the</p> <p>11 company in liquidation. They're just irrelevant because</p> <p>12 that's not how you determine interest is payable from</p> <p>13 the statutory fund surplus. He has his rights against</p> <p>14 the co-debtor. It is clear law that a discharge of --</p> <p>15 but from one co-debtor by operation of law does not</p> <p>16 discharge the co-debtor.</p> <p>17 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>18 MR ZACAROLI: We can provide authority if my Lord wants</p> <p>19 that. It was a point raised by Mr Smith in his</p> <p>20 submissions, that this creates problems when there is</p> <p>21 a discharge but there is clear law that discharge by</p> <p>22 operation of law does not discharge a co-debtor.</p> <p>23 MR JUSTICE DAVID RICHARDS: Right.</p> <p>24 MR ZACAROLI: My Lord, that is the end of my submissions on</p> <p>25 issue 2. I'm going to turn to issue 39.</p> <p style="text-align: center;">Page 155</p>
<p>1 year both creditor A and creditor B incur interest of £8</p> <p>2 at 8 per cent.</p> <p>3 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>4 MR ZACAROLI: They both have to wait five years for that £8</p> <p>5 to be paid.</p> <p>6 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>7 MR ZACAROLI: So there's complete equality of treatment.</p> <p>8 The next point is sub-paragraph 4. It ensures to</p> <p>9 the extent possible that creditors' existing rights to</p> <p>10 interest are given effect to and at sub-paragraph (a)</p> <p>11 they say:</p> <p>12 "Creditors with a right to interest apart from the</p> <p>13 statutory scheme are treated in the same way that they</p> <p>14 would have been treated if the payment had been made</p> <p>15 outside of solvency."</p> <p>16 My Lord, we certainly take issue with that. It's</p> <p>17 absolutely clear that the statute does not treat</p> <p>18 creditors with a right to interest apart from the</p> <p>19 statutory scheme in the same way. If you have a right</p> <p>20 to interest at 2 per cent you are given a right to</p> <p>21 8 per cent under the statute. So there's no doubt that</p> <p>22 the statute alters the rights of creditors but for the</p> <p>23 scheme.</p> <p>24 MR JUSTICE DAVID RICHARDS: Yes, I see.</p> <p>25 MR ZACAROLI: Then sub-paragraph 7, the last point, it</p> <p style="text-align: center;">Page 154</p>	<p>1 MR JUSTICE DAVID RICHARDS: Right.</p> <p>2 MR ZACAROLI: There are two different arguments that are</p> <p>3 advanced in relation to issue 39. The first is that</p> <p>4 creditors whose contractual rights were not fulfilled by</p> <p>5 payments from the statutory scheme so far should be</p> <p>6 entitled to payment from the surplus as non-provable</p> <p>7 debts. The second argument is that creditors are</p> <p>8 entitled to compensation because there's been a delay in</p> <p>9 distributing the surplus because there is a right to be</p> <p>10 paid statutory interest and when it's not paid after</p> <p>11 payment of proved debts, then there's a non-provable</p> <p>12 claim for damages based on the, I assume, Sempra Metals</p> <p>13 analysis.</p> <p>14 Much of what I have said by way of general policy</p> <p>15 and principle applies equally here and I'm not going to</p> <p>16 repeat those comments. My Lord has them.</p> <p>17 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>18 MR ZACAROLI: But the same underlying reasons why the</p> <p>19 statute doesn't give these right is explainable by those</p> <p>20 principles.</p> <p>21 So far as the first way of putting the case is</p> <p>22 concerned non-provable claims for -- non-provable</p> <p>23 liability for contractual claims. We rely on the</p> <p>24 submission that there is -- the way in which the statute</p> <p>25 provides for interest on post-insolvency period is</p> <p style="text-align: center;">Page 156</p>

<p>1 intended to be the compensation for interest -- for 2 delay in payment for that period; in other words, as we 3 put it perhaps colloquially, rule 2.88(7) in 4 administration is intended to cover the ground. It is 5 intended to be the way in which creditors are 6 compensated for this prejudice identified by the Cork 7 Committee, addressed by the Act.</p> <p>8 So far as the construction of the rule is concerned, 9 rule 2.88(7) requires that the surplus is applied in 10 paying statutory interest and in the first line of the 11 rule: 12 "Before being applied for any purpose." 13 That's the wording, "Before being applied for any 14 purpose it shall be used to discharge interest on those 15 debts in respect of the periods during which they have 16 been outstanding".</p> <p>17 MR JUSTICE DAVID RICHARDS: Yes. 18 MR ZACAROLI: So one point to make is that the logical 19 reading of "purpose" there is any purpose other than the 20 one that's just been identified, namely paying interest 21 for the period the debts are outstanding. 22 MR JUSTICE DAVID RICHARDS: Yes. 23 MR ZACAROLI: Therefore, the draughtsman was not intending 24 to include interest in any other purpose -- or any 25 purpose. We submit more broadly that it would be an odd</p> <p style="text-align: center;">Page 157</p>	<p>1 construction is the broader point that there is 2 a substantial change in creditors' rights and in the 3 obligations of the company imposed by the 1986 regime. 4 This is different to currency conversion claims because, 5 as my Lord found in Waterfall 1, the currency conversion 6 claim is simply the contractual entitlement which is 7 left standing throughout, untouched by anything in the 8 statutory process. And the loss is caused simply by the 9 fact that there is a required conversion limited for the 10 purposes of proof. That, as a matter of construction, 11 left the currency conversion or the right to be paid in 12 the foreign currency extant, therefore there could be 13 a claim for the shortfall between distributions and the 14 contractual right.</p> <p>15 MR JUSTICE DAVID RICHARDS: Yes. 16 MR ZACAROLI: I have been at length through the ways in 17 which the creditors' rights and the company's 18 obligations are changed substantively by the rules on 19 interest. 20 MR JUSTICE DAVID RICHARDS: Yes. 21 MR ZACAROLI: Those changes, those alterations, take this 22 outside of, therefore, the comment of Lord Hoffmann in 23 Wight v Eckhardt, for example, that the statutory scheme 24 has no effect on the creditors' contractual or other 25 rights; it is undoubtedly the case here that the</p> <p style="text-align: center;">Page 159</p>
<p>1 statutory intention to impute in the legislature to try 2 to deal with the problem that delay has caused in the 3 distribution of an insolvent's estate by drafting a rule 4 providing a right under this rule which gives interest 5 because of that rule, but also intended that to the 6 extent that a creditor could say, "Well, if the debtor 7 had remained outside of an insolvency proceeding and was 8 still refusing to pay me, I could have got more, 9 I should have a second bite of the interest cherry". 10 Interest is there to compensate for that delay and is 11 intended to cover the ground.</p> <p>12 Insofar as it helps at all, we say the Cork Report 13 supports this view because the Cork Report was 14 identifying the need to provide a remedy for creditors 15 who suffer because of a delay caused by the distribution 16 of the insolvent's estate and the remedy they have 17 recommended, which Parliament adopted, was rule 2.88(7) 18 and its equivalents.</p> <p>19 If the draughtsman had intended that that was not 20 everything but that interest for the same delay could be 21 claimed on a higher basis by some other creditors, then 22 it would be a very easy thing for the draughtsman to 23 say, but the draughtsman has not done so. 24 MR JUSTICE DAVID RICHARDS: Yes. 25 MR ZACAROLI: Allied to that first point about statutory</p> <p style="text-align: center;">Page 158</p>	<p>1 statutory scheme does have an effect on those rights. A 2 substantive effect not just a delaying effect, leaving 3 them to come back in once the insolvency has run its 4 course.</p> <p>5 Now, parts of these submissions -- I think in 6 particular the oddity of the draughtsman having sought 7 to provide for interest under the rules but then 8 thinking oh, well, there may be some more interest which 9 people can claim, and that be a very odd construction -- 10 it seems to be common ground, I think Mr Smith made 11 a similar submission that it doesn't make sense for the 12 draughtsman to have had that intention.</p> <p>13 MR JUSTICE DAVID RICHARDS: Yes. 14 MR ZACAROLI: Of course the submissions lead us in very 15 different directions but it's the same submission. 16 MR JUSTICE DAVID RICHARDS: Yes. 17 MR ZACAROLI: Now, the one argument of my learned friends 18 which we say shows why it is or how it is that the 19 statutory regime for interest covers the ground is the 20 suggestion that actually all creditors who could have 21 asserted a claim for late payment by way of damages can 22 share in this right to come back in at the end of the 23 process. That claim is premised upon the creditor 24 having suffered because of a delay in payment. It's 25 claiming damages for the loss caused to it by the delay</p> <p style="text-align: center;">Page 160</p>

<p>1 in the payment.</p> <p>2 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>3 MR ZACAROLI: Just expressing the way that claim works shows</p> <p>4 that it's exactly the same thing which the statute is</p> <p>5 providing. The statute has provided a remedy where the</p> <p>6 delay is caused by an insolvency process which is</p> <p>7 intended to compensate the creditor for that very same</p> <p>8 loss. We suggest it would be bizarre if Parliament had</p> <p>9 intended that having provided that remedy, there was</p> <p>10 some other parallel claim for damages caused by the very</p> <p>11 same delay for the very same reason, namely an</p> <p>12 insolvency, that the creditor could assert on some</p> <p>13 different calculated basis to the amount of interest</p> <p>14 payable under the statute.</p> <p>15 If that's right, then we also go on to say that,</p> <p>16 well, if that wasn't intended, why would the draughtsman</p> <p>17 have intended that creditors who had some other</p> <p>18 contractual basis for interest but for the insolvency</p> <p>19 should be able to assert those claims which are</p> <p>20 essentially, again, for the same loss but based on some</p> <p>21 other right that the statute has not respected?</p> <p>22 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>23 MR ZACAROLI: My Lord, that, leaves just interest on</p> <p>24 interest which I can deal with now.</p> <p>25 MR JUSTICE DAVID RICHARDS: How long will that take you?</p> <p style="text-align: center;">Page 161</p>	<p>1 get back their debt or their investment. So the</p> <p>2 subordinated creditor is as much prejudiced by the delay</p> <p>3 as the ordinary creditors. The subordinated creditors</p> <p>4 will of course have a right to interest that will come</p> <p>5 into play at some point, assuming a sufficient surplus,</p> <p>6 but members don't.</p> <p>7 Members who are entitled to the surplus as and when</p> <p>8 all debts have been paid are suffering just as much as</p> <p>9 creditors by the delay in being kept out of their</p> <p>10 investment, and there is no compensation for them by the</p> <p>11 statute at all. So combining those factors leads to the</p> <p>12 conclusion that there is no a priori reason why you</p> <p>13 should create a right of interest upon interest when the</p> <p>14 statute has not done so.</p> <p>15 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>16 MR ZACAROLI: Just by way of contrast, there is, of course,</p> <p>17 no compound interest on judgment debts so you don't</p> <p>18 gained interest on interest there.</p> <p>19 If my Lord wants a reference to a short passage</p> <p>20 which makes that clear, it's in the Novoship case,</p> <p>21 bundle 1E, tab 168. I believe it's</p> <p>22 Lord Justice Longmore and paragraphs 139 to 141. It's</p> <p>23 hopefully a fairly obvious proposition.</p> <p>24 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>25 MR ZACAROLI: So one has to ask what is it then, where is</p> <p style="text-align: center;">Page 163</p>
<p>1 MR ZACAROLI: Not long.</p> <p>2 MR JUSTICE DAVID RICHARDS: All right.</p> <p>3 MR ZACAROLI: Ten minutes.</p> <p>4 MR JUSTICE DAVID RICHARDS: Okay.</p> <p>5 MR ZACAROLI: I can deal with it hopefully shortly because</p> <p>6 I've made this submission before. The statute provides</p> <p>7 no right to interest for the delay in the payment of</p> <p>8 interest. It could have done so, it doesn't. There's</p> <p>9 no a priori reason to think that such a claim should</p> <p>10 exist because it's unfair in some way, it's unfair that</p> <p>11 they're suffering from this delay. This brings back</p> <p>12 into play some of my policy and principle points, that</p> <p>13 the delay is not the fault of the debtor any more,</p> <p>14 that's there's a qualitative difference between claims</p> <p>15 for delay interest because of delay against a defaulting</p> <p>16 debtor and one against someone who is now insolvent and</p> <p>17 the solvency regime is the thing that is causing the</p> <p>18 delay. Certainly the delay can't be laid at the door of</p> <p>19 those entitled in the queue behind ordinary creditors</p> <p>20 who get this statutory right to interest.</p> <p>21 Important to realise that delay prejudices everyone</p> <p>22 equally. By that I just don't mean the creditors who</p> <p>23 are entitled to statutory interest. It actually</p> <p>24 prejudices those lower down the order of priority as</p> <p>25 well, obviously, because everyone is having to wait to</p> <p style="text-align: center;">Page 162</p>	<p>1 it -- what is it that gives the creditors a right to</p> <p>2 have this non-provable claim for interest on interest</p> <p>3 once the statutory scheme has run its course? We say</p> <p>4 that nothing of any substance has been identified. What</p> <p>5 is relied upon is a cause of action for breach of</p> <p>6 contract or breach of -- it must be breach of contract</p> <p>7 against the company which has failed to pay interest</p> <p>8 from the surplus after, as the rule says, after payment</p> <p>9 of the debts proved.</p> <p>10 Now, the first point we make about that is that</p> <p>11 there is no date at which the company becomes under an</p> <p>12 obligation to make payment of statutory interest. All</p> <p>13 the rule does is identify a pre-condition, that the</p> <p>14 proved debts have to have been paid in full.</p> <p>15 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>16 MR ZACAROLI: The timing of that payment is, like all of the</p> <p>17 administration of the insolvency estate, under the</p> <p>18 control of the administrator, subject to the directions</p> <p>19 of the court. As is rightly accepted by Mr Smith and</p> <p>20 Mr Dicker, there is no suggestion here that the</p> <p>21 administrators are in any way in default in not having</p> <p>22 paid statutory interest to date. So there could be no</p> <p>23 claim for any breach of duty by the administrators under</p> <p>24 whose control it is to pay statutory interest.</p> <p>25 In those circumstances, we simply fail to understand</p> <p style="text-align: center;">Page 164</p>

<p>1 how it is that the company comes under some freestanding 2 obligation to make this payment on any particular date 3 that would give rise to a claim for not having paid on 4 that date.</p> <p>5 The essence of a Sempra Metals damages claim for 6 late payment is that the payment is late, i.e. there is 7 a date it should have been paid and it hasn't been. 8 That is the essential foundation of a claim in 9 Sempra Metals. That essential foundation is simply 10 missing in this scenario. For the reasons I've given, 11 there's no good reason to try and invent such a claim.</p> <p>12 Finally, picking up on some points from my learned 13 friend's skeleton for the Senior Creditor Group, 14 paragraph 461. The first argument asserted, at 461, 15 sub-paragraph 1, is that:</p> <p>16 "This would defeat the intention of the legislature 17 that all creditors should receive interest at the 18 Judgments Act rate [if there wasn't interest upon 19 interest]."</p> <p>20 My Lord, the intention of the legislature is to pay 21 statutory interest at the judgments rate for the period 22 the proved debts were outstanding.</p> <p>23 MR JUSTICE DAVID RICHARDS: Yes. I was just reading through 24 it, yes.</p> <p>25 MR ZACAROLI: The intention is to pay interest for that</p> <p style="text-align: center;">Page 165</p>	<p>1 for damages, would be compensated for such delay, but 2 creditors without such a right would not."</p> <p>3 Well, first of all, there's no breach of the 4 pari passu principle because, for reasons we've already 5 been through, there is no such right to creditors with 6 a contractual or other right to interest, but if we're 7 wrong about that, there's still no problem with the 8 pari passu principle. If there is differential 9 treatment of creditors on the basis that some have 10 a contractual right and some don't, that's explained 11 purely by their different rights and pari passu 12 treatment never has to come across existing rights of 13 creditors.</p> <p>14 Paragraph 465 draws a parallel with the 15 Judgments Act rate and the fact that under a judgment 16 they say:</p> <p>17 "Further, whilst the company remains in 18 administration creditors continue to be subject to the 19 effect of the moratorium on proceedings. Given this, 20 and in accordance with the rationale for the 21 introduction of the right to interest at the Judgments 22 Acts rate, the protection provided to creditors by the 23 entitlement to interest at the Judgments Act rate should 24 not stop when there is a delay in the distribution of 25 the sums to which they are entitled."</p> <p style="text-align: center;">Page 167</p>
<p>1 period only, for very good reasons that we've been 2 through.</p> <p>3 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>4 MR ZACAROLI: So that's the intention. That intention is 5 indeed furthered, not prejudiced, by the fact that 6 interest is paid for that period.</p> <p>7 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>8 MR ZACAROLI: The reverse could be said, equally, that if 9 you allowed interest to accrue long after that or 10 interest upon interest not provided for, then the total 11 amount being paid to a creditor by way of interest would 12 far exceed the Judgments Act rate for the period the 13 debt was outstanding. So if you had the total interest 14 paid over that period, it would be much more. So it 15 would contradict the statutory purpose.</p> <p>16 MR JUSTICE DAVID RICHARDS: Yes.</p> <p>17 MR ZACAROLI: Then it's said, sub-paragraph 2 of that 18 paragraph:</p> <p>19 "This would also have the effect that interest would 20 be paid to creditors otherwise than pari passu, and not 21 in accordance with their entitlement after proved debts 22 had been paid in full. The effect of the delay would be 23 that all creditors with a non-provable right to 24 compensation for such delay, whether as a result of 25 a contractual or statutory right to interest or a claim</p> <p style="text-align: center;">Page 166</p>	<p>1 The short answer to which I've already made, there's 2 no interest on interest under the Judgments Act.</p> <p>3 Finally, the incentive argument at paragraph 466:</p> <p>4 "Such creditors should have a right to compensation 5 in circumstances where there is sufficient cash to pay 6 the claims of creditors in full, and where a failure to 7 compensate creditors for delay in the payment of claims 8 would benefit shareholders. If no such right exists, 9 shareholders would have an incentive to extend the 10 process of administration for as long as possible so at 11 to ensure that they, rather than the creditors, received 12 any interest earned on the company's assets ... it would 13 be contrary to principle for creditors to be prejudiced 14 by and for shareholders to benefit from delay in the 15 distribution of a surplus."</p> <p>16 A number of submissions I have made cover that but, 17 frankly, that's quite a bizarre suggestion that the 18 shareholders, who are also being kept out of their 19 money, would (a) want to extend the process of 20 administration to the sum increase on the fund when if 21 they had the fund in their own hands they would be 22 earning interest on it anyway or have the use of it and, 23 (b), shareholders don't control the process, the 24 administrator does.</p> <p>25 MR JUSTICE DAVID RICHARDS: It's not in their hands, it's</p> <p style="text-align: center;">Page 168</p>

1 the administrators.

2 MR ZACAROLI: Exactly.

3 If I can be forgiven for one perhaps slightly cheeky

4 comment to finish with. The incentive in a case like

5 this, although I accept my Lord can't decide this case

6 on the basis that we happen to have a very high rate of

7 Judgments Act interest, the incentive is the reverse

8 here. The creditors will do better by arguing amongst

9 themselves for as long as possible to avoid being paid.

10 You wouldn't get that rate elsewhere.

11 My Lord, with that slightly cheeky comment, those

12 are my submissions.

13 My Lord, it is the end of a long day. I think

14 I have finished. If I think of a couple of points, with

15 consultation with my colleagues, it may be I have

16 five minutes on Monday, but I hope not.

17 MR JUSTICE DAVID RICHARDS: Very well. Thank you very much.

18 On Monday, therefore, we'll sit at 9.30. I'm not

19 able to tell you now, but I will be able to tell you

20 when we start on Monday, exactly what time we will

21 finish, but I anticipate it being somewhere between 1.30

22 and 2 o'clock. Very good. Enjoy your weekend.

23 (4.30 pm)

24 (The court adjourned until

25 9.30 am on Monday, 23 February 2015)

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