Thursday, 19 February 2015

(10.30 am)

Opening submissions by MR DICKER (continued)

MR DICKER: My Lord, I was just finishing the Commonwealth authorities.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: There are two. The first is a decision from Hong Kong called Peregrine Investment Holdings Limited. I just need to show your Lordship the judgment. For your Lordship's note, the reference is 1E, tab 147. The judge in that case simply referred to Bower v Marris, Humber Ironworks and said that such authorities and the principles in them also applied in Hong Kong. There's no further analysis.

MR JUSTICE DAVID RICHARDS: Right.

MR DICKER: My Lord, the other case I did want to show your Lordship was a decision from the Second Circuit Court of Appeals in the United States, called Ohio Savings Bank & Trust Company v Willys Corporation. Your Lordship has that in bundle 1B, tab 64.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: My Lord, picking it up on page 2 of the report in the right-hand column, the last full paragraph:

"This appeal involves the legality of an order instructing the receiver in an equity receivership as to

the application to be made of the dividend payments being payments upon interest-bearing debts. The court below instructed that such payments should be applied first to the payment of the interest and then towards the discharge of the principal. From this order the Willys Corporation, the debtor, and the protective committee for the first preferred stockholders of that corporation have appealed. They insist the order referred to is erroneous in law, claiming that such payment should be applied to the reduction of the face amount of the principal of the claims as allowed, and the interest which accumulated during the receivership should be paid last."

The opinion of the court is given by Circuit Judge Rogers. It starts at the top of page 3.

If your Lordship goes to page 4, the last -- it's column 1, the last full paragraph and the last four lines of that, he says:

"The only disagreement between the appellants and the appellees" --

MR JUSTICE DAVID RICHARDS: Sorry, page 4?

MR DICKER: Yes, page 4, column 1, just below -- just above the bottom, last four lines.

MR JUSTICE DAVID RICHARDS: I'm with you, yes.

MR DICKER: "The only disagreement between the appellants

and the ...(reading to the words)... amount of interest so payable."

Then the two methods are identified in the right-hand column:

"Method 1, the dividend payments to creditors treated ...(reading to the words)... balance of the payment then being applied to reduce the principal of the claims."

My Lord, dropping a paragraph, the judgment continues:

"The question involved in the appeal is to the extent to which the principal of the claims has been paid by the five dividends aggregating 100 per cent of such principal. The contention of the appellants is the principal has been paid in full and that only interest remains to be paid."

My Lord, the familiar argument.

Then the next paragraph:

"This brings us to enquire into the rules applicable to the payments already made and those which remain to be made because of the interest which may be due thereon."

There's a reference to United States authorities, first Story v Livingston:

"The correct rule in general is the creditor should

calculate interest whenever a payment is made. To this interest the payment is first to be applied ...", et cetera.

Then in the next paragraph, number 2:

"... and that is understood to be the rule in all the federal courts before and since that time."

Various authorities referred to.

Halfway down column 1, 1835, the question came before Chancellor Walworth in New York in Stone v Seymour:

"He states that ..."

Then if your Lordship goes down in the quotation to the hole-punch, it says:

"These rules prevailed in the Roman or civil law, now settled law of France, Spain, Holland, Scotland, England and the United States. The last of these principles is also supported by all of the English and American cases in which the rule has been settled as to the computation of interest."

Then:

"We shall not review the New York cases which have since been decided", and then there's a very long list of those cases.

More relevantly, for present purposes, halfway down column 2 on page 5, he says:

"The rule in the United States on this subject prevails also in England."

Your Lordship has seen a reference to Bromley v Goodere.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: Over the page, the first paragraph, a reference to Bower v Marris.

Then dropping a paragraph:

"The authorities show the rule laid down by Lord Chancellor Hardwicke in 1743 is still the law of the English courts."

A reference to Warrant Finance Company's case, Humber Ironworks, Whittingstall v Grover, which your Lordship hasn't seen but will, similarly re Calgary and Medicine Hat Land Limited:

"The same doctrine prevails in the Chancery Court of Ireland and in the Court of Session of Scotland."

That's Gourlay v Watson.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: The conclusion in column 2, the first full paragraph, the last two lines:

"It seems to us the order made in the court below which followed method number 2 was justified" --

MR JUSTICE DAVID RICHARDS: Sorry, the second column?

MR DICKER: My Lord, I am sorry. The second column. It's

the first full paragraph. Then the last two lines of that paragraph.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: Then, finally --

MR JUSTICE DAVID RICHARDS: Just before we leave this -- are you about to leave this case?

MR DICKER: I was just going to show your Lordship one more passage. It's in the paragraph beginning number 5:

"The court ought to have in mind that prior to the order appealed from ...(reading to the words)... by the decision in Calgary and Medicine Hat Land Company Limited."

My Lord, as I say, your Lordship hasn't yet seen that.

MR JUSTICE DAVID RICHARDS: No.

MR DICKER: That was all I was proposing to show your Lordship from that judgment. It continues basically by dealing with the Calgary and Medicine Hat Land Company case.

MR JUSTICE DAVID RICHARDS: The Ohio Savings Bank & Trust Company -- no, it was the Willys Corporation was in receivership, is that right?

MR DICKER: My Lord, yes.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: That appears to be the position.

MR JUSTICE DAVID RICHARDS: Yes. We see that, yes. So this must -- the jurisdiction must have been some equitable jurisdiction to appoint a receiver. It's not a bankruptcy under the bankruptcy code and just so I know the context of it?

MR DICKER: My Lord, I can't answer the precise -- I can't tell your Lordship at the moment the precise nature of the receivership here.

MR JUSTICE DAVID RICHARDS: No.

MR DICKER: What your Lordship will see in a minute is that the rule in Bower v Marris is not limited to bankruptcy in companies winding up.

MR JUSTICE DAVID RICHARDS: No, I appreciate that.

MR DICKER: And, in a sense -- certainly one of the cases, the last one mentioned in the judgment, Calgary and Medicine Hat Land Company, is an English decision on a debenture holder's action for enforcement of his debenture.

MR JUSTICE DAVID RICHARDS: Yes, okay. That's fine. Thank you very much. Yes, actually I think it was some equity receivership proceeding. That appears in the headnote.

MR DICKER: Mr Fisher points out, just at the top of page 2, column 1, line 3:

"The court was asked to appoint receivers and authorise them to continue the operation of the

defendant's business in such matter and to such extent as the court might direct ... preserve and protect the property and assets of the defendant from being satisfied ... [then] receivers were appointed by the district courts on the creditor's bills."

MR JUSTICE DAVID RICHARDS: Okay. Thank you.

MR DICKER: My Lord, as I say, it's not entirely clear to us to what extent receivership embodied principles of insolvency law. It certainly --

MR JUSTICE DAVID RICHARDS: It looks like it.

MR DICKER: It certainly envisaged distributions being made.

MR JUSTICE DAVID RICHARDS: Yes, exactly.

MR DICKER: My Lord, I mentioned just now that the rule applies outside of bankruptcy and companies winding up. There are two streams of authorities that we refer to in our skeleton argument. The first concerns debenture holders' actions and that's paragraphs 111 to 114 of our skeleton. The main authority being the Calgary and Medicine Hat Land Company case.

MR JUSTICE DAVID RICHARDS: I see.

MR DICKER: My Lord, the second concerns the administration of deceased estates and payment of legacies. That's paragraph 115 to 119 in our skeleton.

My Lord, York deal at some -- in some detail, particularly, with the second stream of cases. That's

paragraph 72 to 81 of their skeleton, the main case being a case called Whittingstall v Grover. My Lord, if your Lordship was content with this, I was going to leave it to Mr Smith to deal with both of those.
MR JUSTICE DAVID RICHARDS: Certainly.
MR DICKER: What your Lordship will, however, see from Whittingstall v Grover in due course, just to flag the point, is an analysis by Mr Justice Chitty in the context of administration of deceased's estates which essentially says the reason why statutory interest is given at the prescribed rate in that context is because the court effectively prevents the creditor from taking proceedings and obtaining its own judgment, and equity effectively has to compensate the creditor for the fact that it's preventing it from obtaining its remedies at law. So it gives it a corresponding right and that right ended up being enshrined in the rules, still present in CPR today.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: But passing over both of those and leaving those to my learned friend Mr Smith, my next task was to draw together some points in relation to interests on debts that do not otherwise carry interest; in other words, statutory interest at the Judgments Act rate.
Just to remind your Lordship of the statutory

position, your Lordship will recall the 1824 and 1825 Acts introducing a right to interest on debts that didn't otherwise carry interest.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: At that stage ranking after creditors' entitlement to interest reserved or otherwise payable. Your Lordship will also recall that the 1883 Act entitled all creditors to interest at 4 per cent, so effectively elevating that to the first line, and then said anyone else with a higher rate of interest is entitled to it on the basis he's got to be paid in full before the surplus is provided to shareholders. So there's a slight tweak in that respect.
The submission at this point is that in our submission it's clear that the rule in Bower v Marris applies not just to contractual interest, it also applies to interest under statute, including the creditors' entitlement to interest under section 129, section 132, et cetera.
Now, the starting point is, I think, there is common ground between us and Wentworth, at least in this respect. They say it would not make sense for Bower v Marris to apply in one situation but not in the other; in other words, it wouldn't make sense for it to apply, for example, in relation to contractual interest

but not also to apply in relation to statutory interest.
My Lord, just so your Lordship has the reference. It's paragraph 79 and paragraph 80 of their skeleton.
My Lord, at that point obviously the direction of argument diverges. Wentworth says it's not payable, it's not applicable in relation to statutory interest and, therefore, it can't be applicable to contractual interest either. We obviously put it the other way round. We start with contractual interest. We say it's perfectly plain that Bower v Marris applies in relation to a creditor who's entitled to contractual interest. It has to, otherwise he wouldn't receive the interest which he otherwise would have received absent insolvency, and that's one of the fundamental principles of the insolvency regime.
My Lord, we also say that it's not -- it's clear that it's not in any event limited just to contractual interest, it's also applicable to any right a creditor has outside of the insolvency regime, whether that right is contractual or statutory, including a right to interest pursuant to a judgment. Your Lordship has seen that most clearly stated in Tahore Holdings Property Limited. That the Australian case, the reference was 1D/135.
MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: Your Lordship may remember Mr Justice Barrett saying although the cases talk about contractual interest, it applies equally, regardless of the source.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: The next point is obviously the justification for giving creditors a right to interest at the Judgments Act rate is the existence of a moratorium. They are effectively to be put into the position that a creditor would have been in had he obtained judgment.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: Put another way, if a creditor had obtained judgment the day before and was entitled to rely on the rule in Bower v Marris, why on earth should it make any difference that he would have obtained judgment the day after but couldn't as a result of the moratorium?
The next point is every case that has considered the point has either held or indicated that the rule applies in both situations.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: Put another way, there is certainly no case which anyone has found which suggests the rule does not apply to statutory interest at the Judgments Act rate.
Can I just remind your Lordship of three authorities your Lordship so far has seen on that? The first is Bower v Marris itself. Your Lordship may remember

Lord Cottenham's reference to section 132 of the 85 Act, not drawing any distinction in this respect between claims as to contractual interest and claims to interest at the prescribed rate. It may just be worth looking at that passage. It's bundle 1A.
MR JUSTICE DAVID RICHARDS: He referred to the 1885 Act.
MR DICKER: 1825.
MR JUSTICE DAVID RICHARDS: 1825, sorry.
MR DICKER: That was the --
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: The passage then perhaps for your Lordship's note, it's at the bottom on page 357.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: He refers to section 132.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: He doesn't draw a distinction in that section between the various parts of section 132. He doesn't say that the rule in Bower v Marris only applies where you are dealing with interest reserved or only applies where you're dealing with interest reserved or otherwise payable at law, but does not apply to interest at the prescribed rate. It's effectively treated and referred to as one.
So that's the first point.
The second -- the first case.

The second is the decision of Mr Justice Blair in the Attorney General of Canada v Confederation Trust case.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: My Lord, again, the reference 1D, tab 133. My Lord, that was concerned with specifically concerned with a provision providing for interest (inaudible) that didn't otherwise carry interest, and Bower v Marris applied. That's why my learned friends say that case must have been wrongly decided.
The third is Hibernian Transport. Ignoring, as it were, the wrinkle caused by the question of whether the bankruptcy rules also applied in corporate consultancy, Mrs Justice Carroll -- I think I misdescribed her yesterday -- held that in bankruptcy, where there is a similar provision for interest at the prescribed rate on all debts, whether or not they carry interest, Bower v Marris applies. So that's the third case.
The fourth case, one your Lordship hasn't yet seen, outside of insolvency but to identical effect, Whittingstall v Grove in relation to the administration of deceased's estates.
We say that must be correct as a matter of principle. If the rule applied to creditors entitled to contractual interest but not Judgments Act interest, it

would be treating them differently. Creditors with contractual rights to interest would effectively be compensated for additional delay in the way that creditors entitled to statutory interest would not, effectively causing -- giving rise to a difference in treatment, contrary to Lord Justice Giffard's comment at the end of Humber Ironworks, that there is no justification for treating them differently.
Secondly, if creditors entitled to interest at the Judgments Act rate did not receive interest calculated on the basis of the rule, then they would not receive interest at an effective rate of 8 per cent, effectively the amount they receive when they eventually receive it would be worth less as a result of the time value of money.
We say that can't be what the legislature intended.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: My Lord, the final point on this is Wentworth has a technical reason why they say the rule in Bower v Marris can't apply to statutory interest at the Judgments Act rate. The reason the argument is that they say the rule in Bower v Marris requires interest to have accrued and statutory interest -- at least statutory interest under the Judgments Act rate cannot have accrued unless and until there is a surplus.

My Lord, we say that argument is incorrect. There's no difficulty in regarding creditors' rights to statutory interest as a contingent right at the date of commencement, the contingency being the occurrence of a surplus. That's precisely how it was analysed in Attorney General of Canada v Confederation Trust. The reference is paragraph 25. We say there is no theoretical problem, once a surplus has arisen, in conducting the calculation by applying hindsight; in other words, doing exactly the same as one does in relation to the process of collective enforcement, but in relation to the surplus. One has a contingent right pursuant to the statute to interest at the Judgments Act rate. It's true it's contingent on there being a surplus, but once a supplies arises, there is no theoretical difficulty in saying that we will treat interest as having accrued up to and on the date of each dividend payment and applying Bower v Marris on that basis.
MR JUSTICE DAVID RICHARDS: Can I just see in the Confederation Trust case.
MR DICKER: Yes, 1D/33. Reminding your Lordship, at paragraph 17 it sets out section 95(2).
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: Paragraph 25, Mr Justice Blair says

section 95(2) applies, and then:

"To say this not to give the provision retroactive effect ...(reading to the words)... debts and obligations and the costs associated with liquidation."

He's dealing with a slightly different argument there. One of the arguments was that section 95 didn't apply at all because it only came into force after the start of the liquidation. He says effectively it's a continuing liquidation and there's no difficulty in analysing it this way, but for our purposes what we rely on, which we say is correct as a matter of analysis, is the statute gives you a right. It may be it's conditional, contingent on there being a surplus, but once the right arises, there's no difficulty in looking back and saying, "We now know effectively you had a claim to interest accrued on the principal as at the date and performing the calculation accordingly".

MR JUSTICE DAVID RICHARDS: So the Wentworth argument is that Bower v Marris can apply only where interest has accrued due at the relevant payment dates; is that right?

MR DICKER: Yes.

MR JUSTICE DAVID RICHARDS: They say, "Well, this doesn't accrue due at the dates of the payments of the dividends, it only accrues due once there is a surplus".

MR DICKER: Correct.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: So they draw a distinction. It's a fallback argument for them.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: They draw a distinction between claims to interest as a matter of contract.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: And claims to interest where your only right to interest is under the statutory scheme.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: The argument effectively on Wentworth's part is: Bower v Marris is all about remission to your contractual rights.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: So that's fine, it covers contract, but the logic of it in the remission to contractual rights is you have an underlying right to interest which is accruing and that, they say, is a critical part of one's ability to apply the rule in Bower v Marris.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: Now, we say in response: not so, the rule in Marris is effectively a rule that governs how you calculate interest in an insolvency. It's not simply an application of parties' contractual rights, although the

rule may be justified on the basis it reflects those rights and provides creditors what they would otherwise have been entitled to, and, as a rule of calculation, there's no difficulty in saying not merely we'll treat prior dividends as having been applied notionally first in respect of interest, if you can do that there is no reason why you can't also say, as part of the calculation, we will to the extent necessary treat interest as having been accrued up to the relevant date of principal. We now know, given that there is a surplus, that that as a matter of statute is the interest to which you were entitled.

MR JUSTICE DAVID RICHARDS: This particular argument, the Wentworth argument on this point, was that actually advanced in the Attorney General v Confederation Trust case?

MR DICKER: No.

MR JUSTICE DAVID RICHARDS: No.

MR DICKER: My Lord, moving on to the section in our skeleton dealing with policy and principle. It's paragraphs 120 and 121. I think I can take this fairly shortly.

Just to add a little structure and a few additional points. The first point we say is the easiest situation concerns a creditor with a contractual right to

interest. As the authorities repeatedly state, the rule ensures the creditors receive the full amount they would have received had the company not gone into liquidation.

Now, just dealing with a point your Lordship I think raised with me yesterday. In many cases obviously the amount that the creditor would be entitled to receive absent insolvency will be a matter of effectively express stipulation in this respect. It's obviously common, particularly for finance documents, to contain an express provision entitling the creditor to apply payments as it wishes, not how the debtor wishes.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: So it will often be enshrined in the terms of the contract itself. But if that's not the case and the debtor makes a general payment on account, on the authorities the creditor is entitled to apply that first interest, if he wishes.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: Failing that, if neither -- if it's a general payment on account and the creditor has not applied it, the default rule is that the court will treat it as having been applied to interest.

The fourth point, which I think your Lordship raised yesterday, is what if the debtor says to the creditor, "Here's a payment, apply it in respect of principal".

I mentioned a decision called Nemichand which addressed that. I ought to just show your Lordship the reference. It's bundle 1D, tab 62A.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: It's a decision of the Privy Council from 1921. The relevant paragraph is paragraph 3 of the commendably short judgment. Paragraph 3:
"The law as to payment being applied as to principal or interest laid down by the board in the case of ..."
Then there's the reference to that:
"Shortly restated it is this: a creditor to whom principal and interest are owed is entitled to appropriate any indefinite payment which he gets from a debtor to the payment of interest a debtor might make in making a payment stipulate that it was only to be applied only to principal. If he did, so the creditor need not accept the payment on these terms. Then he must give back the money or the cheque by which the money is proffered. If he accepts it, he would then be bound by the appropriation proposed by the debtor."
That's the position outside of insolvency.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: We say, obviously, outside of insolvency, if the creditor returned the money, what he would then be able to do, obviously, is issue proceedings, obtain judgment,

obtain a Judgments Act rate, interest, enforce, et cetera. Plainly, obviously, he can't do that in insolvency, nor, for obvious reasons, can he sensibly decline to received dividend payment.
So one way or another -- some more complicated than others -- outside of an insolvency, a creditor is entitled effectively to the application of the rule in Bower v Marris.
My Lord, the next point is this: it's not only a creditor with a contractual right to interest who may be prejudiced if the rule does not apply. Consider a creditor who's entitled to statutory interest at the Judgments Act rate. The legislature has said that he ought to have interest at 8 per cent, but if Wentworth and the administrators are right, that's not in reality what he gets. On their case the amount of interest he receives is effectively crystallised on each dividend payment, although it may not in fact actually be paid for years. So one has a situation in which a dividend, say of 50 per cent, is paid at the end of year 1. The interest for that year is 8 per cent at the amount of the dividend payment. Now, assume that it takes another ten years to pay the final dividend. Wentworth and the administrators' case is that first year's interest crystallised at the end of the process, was effectively

capped at the end of the first year, although only payable in the event some ten years later and therefore worth considerably less as a result of the time value of money.
My Lord, we do say why on earth would the legislature have wanted to go to the trouble of specifying interest at 8 per cent if it was effectively content for that right to be watered down as a result of further time passing before that amount of interest is eventually paid?
My Lord, the third point is the rule ensures equality of treatment of creditors. This is a slightly different point. One of the consequences of Wentworth's and the administrators' approach is that the treatment of creditors will differ depending on when they prove for their debts and whether they receive any interim dividends. So take a case of a creditor who does not prove until just before the final dividend, he will receive principal and interest on the full amount right up to the date of final dividend. Now, compare a creditor who received interim dividends. He will only receive a sum in respect of interest accrued up to the date of each dividend, effectively degraded by the time value of money.
So one of the consequences of their approach is that

the amount that creditors actually receive will differ depending on whether and, so if, when, they prove their debts and received interim dividends. On their case it's better, assuming there is a surplus, not to prove your debt until the last possible moment. You will then preserve effectively interest at 8 per cent right up to the date you prove and get your dividend. Again, we say the legislature can't have intended creditors to be treated differently, depending on whether they prove early or late, and there will certainly be an unfortunate incentive so far as the administration of insolvencies was concerned if there was any incentive for creditors effectively to say, "We're not going to prove. We're not going to receive dividend as a result. We're going to delay doing it as long as possible so that we continue to receive statutory interest".
My Lord, that's obviously contrary to the intention of having a winding-up order being concluded as reasonably practicable.
My Lord, the fourth and final point is it ensures the debtor or its shareholders do not benefit from the time taken to conduct the insolvency.
Again, there are two aspects to this. The first of course is to the extent that creditors with contractual rights to interest get less than they otherwise would

have done, that sum inures for the benefit of shareholders so a creditor with a contractual right loses the shareholder gains. But it also prevents the debtor or its shareholders from obtaining the benefit of any interest earned on the state or increase in the value of its asset in the meantime.

My Lord, one example of this is the facts in Hibernian. Your Lordship may remember, at the time the company went into liquidation there was a deficiency. The only reason there turned out to be a surplus was because of interest earned on the assets during the course of the administration -- the course of the liquidation.

MR JUSTICE DAVID RICHARDS: Yes, I remember.

MR DICKER: As I say, one of the consequences of Wentworth and the administrators' case is that if interest is capped in the way that they say it is, then the benefit of that interest effectively goes to the shareholders or the debtors.

One can illustrate that easily. Take the present situation. We have had a final dividend. According to the administrators and Wentworth, therefore, the amount of interest the creditors will receive is now a fixed amount, but it may take, as a result of this application, two or three years, depending of how far it

goes, before the surplus is eventually distributed. In the meantime the 6 billion, or whatever it is, of cash that the administrators hold will no doubt be earning interest --

MR JUSTICE DAVID RICHARDS: Although not at 8 per cent, I wouldn't think.

MR DICKER: Although not at 8 per cent. There are, as I understand it, assets held through affiliates in a form of securities and things of that sort which may well increase in value.

MR JUSTICE DAVID RICHARDS: Mmm.

MR DICKER: But that interest will effectively go, on their case, to shareholders and --

MR JUSTICE DAVID RICHARDS: The point you're making now is not in any way dependent on whether the creditor has a right to interest, apart from the administration. Your first point under this heading relates to those who have a right to interest as a matter of contract or perhaps judgment or something.

MR DICKER: Correct.

MR JUSTICE DAVID RICHARDS: This point applies irrespective of whether you have a right outside the administration.

MR DICKER: Absolutely. Both are prejudiced by delay.

MR JUSTICE DAVID RICHARDS: What about the -- in respect of the first lot? If Wentworth and the administrators are

right and Bower v Marris doesn't apply to statutory interest, then the effect of that is a creditor receives in total less interest than he would have done if Bower v Marris had been applied, may he not be remitted to his rights and so have a non-provable claim for the balance?

MR DICKER: Your Lordship's example assumes a creditor who isn't otherwise entitled to --

MR JUSTICE DAVID RICHARDS: No, someone who is. Someone who is. So you have a right to contractual interest which, if Bower v Marris doesn't apply to statutory interest, by which I mean under rule 2.88, will be able to say, "I haven't received my full contractual entitlement" because Bower v Marris should be applied to if we're just dealing with the position outside the administration rules.

MR DICKER: My Lord, if it's not within 2.88, then in our submission the logic must be that it's then a non-provable claim --

MR JUSTICE DAVID RICHARDS: So that would take care of that first example you gave. I mean, it would mean they were further down the waterfall. I think Mr Trower submits that rule 2.88 deals completely with interest.

MR DICKER: Well, and that --

MR JUSTICE DAVID RICHARDS: No non-provable claims for

interest.

MR DICKER: And so do Wentworth.

MR JUSTICE DAVID RICHARDS: And so do Wentworth as well, yes.

MR DICKER: So addressing that argument, we say creditors end up at the end of the day with less than they otherwise would have received.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: No chance for a non-provable claim, but your Lordship's earlier point is exactly right. All creditors are prejudiced if Bower v Marris doesn't apply. They are prejudiced in slightly different ways and for slightly different reasons. The contractual creditor because he's not getting to what he bargained for.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: The creditor who didn't otherwise have a right to interest is entitled to interest at the Judgments Act rate; he is prejudiced because he's not getting an effective rate of 8 per cent which we say the legislature plainly intended that he should receive.

My Lord, it's no answer in our submission for Wentworth to say, "Okay, at the moment 8 per cent happens to be a high rate of interest". Your Lordship can't, as it were, decide what the answer as a matter of

law is depending on whether on any particular date prevailing interest rates are just below or just above 8 per cent.

My Lord, there's then a separate set of issues -- points concerning what may be called policy and principle so far as third parties are concerned. It's effectively the effect of Wentworth and the administrators' case on, for example, co-obligors.

MR JUSTICE DAVID RICHARDS: Right.

MR DICKER: One of the points dealt with in Bower v Marris.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: My Lord again, my learned friend Mr Smith is going to deal with that.

MR JUSTICE DAVID RICHARDS: Okay.

MR DICKER: That's another issue.

My Lord, so that concludes, although I'm conscious at some length, the statutory history, the authorities, both in this jurisdiction and elsewhere, and draws some of the themes together.

The next stage is arguments as to why, according to Wentworth and the administrators, things changed in 1986.

MR JUSTICE DAVID RICHARDS: Yes. Could I just ask one question. Can you just remind me where the equivalent provisions to 2.88 and interest are in bankruptcy now?

MR DICKER: Yes.

MR JUSTICE DAVID RICHARDS: It's in the rules, is it, or is it in the Act?

MR DICKER: No, it's in the legislation.

MR JUSTICE DAVID RICHARDS: Is it in very similar terms?

MR DICKER: Yes.

MR JUSTICE DAVID RICHARDS: Thank you.

MR DICKER: It's also in very similar terms in relation to winding up as well. My Lord, it's 328 in relation to bankruptcy.

MR JUSTICE DAVID RICHARDS: Thank you.

MR DICKER: My Lord, can I --

MR JUSTICE DAVID RICHARDS: Yes, that's helpful. Thank you.

MR DICKER: I'll come back to this in a moment, but just to emphasise a point which I hope I have made.

We say Bower v Marris isn't simply the application of a contractual entitlement.

MR JUSTICE DAVID RICHARDS: No.

MR DICKER: That's not how Lord Hardwicke -- that's not how Lord Cottenham dealt with it in Bower v Marris. Your Lordship may remember him saying, "It's not a question of appropriation, it's a question of how I construe the statutory scheme".

We say it's effectively a judge-made rule as to how the insolvency scheme works which -- one of the

justifications for which, but not the only justification -- is that it ensures creditors receive the full amount that they would have received absent the insolvency. There is this distinction between ourselves and Wentworth. They effectively say, "It's no more than your contractual entitlement".

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: We say that's not how it's analysed in the cases. The way it's analysed in the cases is it's effectively part of the operation of the statutory scheme. It's there because it effectively is the just, the right result. Part of the reason why it's the just or right result is that it ensures creditors being paid in full. But it's broader than that and obviously the broader bit, we say, also encompasses the right to statutory interest at the Judgments Act rate.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: Turning now to 1986. One starts with the legislative materials leading up to the Act. Can I just show your Lordship how this is dealt with by Wentworth and the administrators. So far as Wentworth is concerned, their skeleton argument is paragraphs 12 and 14. My Lord, they refer in paragraph 12 to the Cork Report, paragraph 1392, concluding:

"There should be one set of rules relating to

interest on debts in all forms of insolvency proceedings. In preparing the rules, simplicity and certainty are essential."

In line with that sentiment it recommended, paragraph 1394, that in the event of being a surplus after the payment of all admitted debts and liabilities, "... interest should run on all such debts and liabilities until a final dividend has occurred, the rate being that currently applicable to judgment debts at the commencement of the insolvency."

Then you will see in 14 they emphasise the words "until a final dividend is declared" saying:

"The essence of the recommendation that interest should run 'until a final dividend is declared' was enacted, with a slight variation that interest under rule 2.88(7) runs until the final dividend has been paid..."

So that's what they say in relation to the Cork Report.

The administrators, in paragraphs 87 to 92, refer in 87 to the Cork committee, set out the changes which were made in 88 and then say, in 91:

"As a result of the Cork Committee's recommendation, the mandatory direction that the surplus be applied in paying interest (rather than principal), which had

formed part of the bankruptcy legislation since 1883, became part of the winding-up legislation. For the first time, the corporate liquidation regime was brought into line with bankruptcy regime."

Then 92, the last sentence:

"As a result of the introduction of the mandatory direction requiring the surplus to be applied ... a default rule could no longer apply as it was plainly not what the legislature's choice of words indicated its intention to be."

So the administrators' position is essentially Bower v Marris had been abolished by the 1883 Act. What the Cork Report says is we need to bring company liquidation in line with bankruptcy, we need to include a mandatory direction. As a result of including a mandatory direction, Bower v Marris disappeared from company liquidation as well.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: My Lord, that's what they say the Cork Report was doing. We respectfully invite your Lordship to look at the terms of the discussion. It's in bundle 4, tab 3. My Lord, obviously this is not a statute.

MR JUSTICE DAVID RICHARDS: No.

MR DICKER: It would be unfair of the authors to construe it as if it was. Looking at what they discussed. There

are three main sections to the report. Just identifying them. The first starts just above 1363, "Interest-bearing debts", which deals with section 66(1) of the 1914 Act. I'll come back to that.

The second your Lordship will see at 1382, "Non-interest-bearing debts". That deals with the position up to the date of the receiving order or commencement of the winding-up.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: So pre-insolvency.

The third, "Statutory interest out of surplus assets" obviously deals with our situation, but one needs to look at all three.

So far as the first is concerned, there is a long discussion about the effect of section 66(1) of the Act of 1914. Your Lordship may recall, if you look at 1364, the last sentence summarises the effect of 66.1:

"The interest in excess of 5 per cent is postponed and ranks for dividend only after the debt which have been proved have been paid in full."

1365:

"Sub-section 2 designed to prevent avoidance by creditors."

Then there's a reference to that.

1368, the second sentence:

"This section was believed not to be applicable and was therefore never applied in companies winding up. This belief was shown to be erroneous in 1967."

1369, the second sentence:

"The section is now applied in companies winding up and since for many years ...(reading to the words)... secondly, on the liquidation of an ordinary trading company which has an overdraft with its bank."

The long of the short of it is summarised at 1378:

"No doubt section 66 has proved impracticable to apply in companies winding up ... is a source of delay, expense and embarrassment ... highly unsatisfactory ... not only is the law unclear but that in particular recent interpretations have found to be virtually unworkable."

Essentially the exercise of stripping out the sum above 5 per cent was too time-consuming and so expensive that it was almost impossible for liquidators to perform.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: In 1379, the last sentence:

"Now that money lending transactions and all credit...(reading to the words)... retaining this section in personal insolvency."

1380, the last sentence, firmly of the view this

section has long outlived its usefulness and needs complete repeal.

1381:

"The repeal of section 66 would enable exorbitant rates of interest ...(reading to the words)... exorbitant credit agreements on the application of the liquidator."

As your Lordship knows, that indeed is what happened.

The next paragraph, 1382, as I said, deals with pre-insolvency interest:

"In cases where there is no express provision for interest ...(reading to the words)... [and they say] this rate has been in force since 1883."

Then dealing with the surplus:

"Section 33(8) of the Act of 1914 provides that if after all the proving creditors have been paid in full, the bankrupt's estate still has a surplus it is to be applied first in paying interest from after the date of the receiving order at the rate of 4 per cent per annum on all debt proved in the bankruptcy, any balance belonging to the bankrupt."

Then they draw the distinction between bankruptcy and companies winding up:

"There is no similar provision in the winding-up

code."
In other words, no provision or interest on debts that don't otherwise carry interest.
They make the point section 66 of the ct of 1914 -- sorry:
"Unlike section 66, the provisions of section 33(8) are not imported into the Companies Act."
That's effectively Rolls-Royce.
MR JUSTICE DAVID RICHARDS: Hmm, hmm.
MR DICKER: Dropping four lines:
"Provided that there is a surplus after the proving creditors have been paid in full, therefore the company is to be treated as no longer insolvent. This means that the creditor who is entitled to interest on the debt for which he has proved may recover interest accruing after the presentation of the winding-up petition as if there had been no winding-up at all."
In 1385 they make the point that:
"It is essentially unfair that interest is not payable on debts that do not otherwise carry interest."
There's a reference to the Vice Chancellor in Rolls-Royce saying he reached the conclusion with some regret:
"It seems fair a creditor should be compensated for being kept out of his money."

1386:
"Our attention has been drawn to this anomaly ...(reading to the words)... in the same way both administrations, and we agree."
Then their proposals, 1395. They recommend.
"Firstly, section 66 should be repealed. Secondly, the court's power ...(reading to the words)... applicable to judgment debts at the commencement of the insolvency."
E:
"These rules should be applicable in all forms of insolvency proceedings."
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: My Lord, we say it's perfectly clear what the authors of the report had in mind. What they had in mind was getting rid of section 66(1) which was unworkable and embarrassing. They recommended that the entitlement of interest on debts that didn't otherwise carry interest present in bankruptcy was extended to corporate insolvency, and they recommended the same rules should apply in both sets of insolvency proceedings.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: My Lord, the suggestion that the authors wanted either to cap interest as at the date of final dividend,

which is what Wentworth say, or that the authors of the Cork Report wanted to assimilate company winding-up to bankruptcy and thereby abolish the rule in Bower v Marris, we say receives no support from anything in the report at all.
My Lord, there's one other document which is at tab 1 of the same file which is the DTI Revised Framework for Insolvency Law, presented in 1984. My Lord, paragraphs 85 to 88. 85:
"The review committee identified numerous instances where ...(reading to the words)... subject to the discretion of the court as to excessive agreements."
My Lord, so far as the 86 Act and rules are concerned, there was obviously no change in the fundamental features of the collective -- the process of collective execution. By that I mean there was nothing in the 86 Act that affected how payments of dividends as part of that process were to be treated. It simply continued to say: the assets of the debtor are to be pari passu in respect of proved debts. So nothing that might mean that a payment of a dividend had a different effect after 1986 than it did before. Nothing to suggest that if there were previously general payment on account, somehow they were no longer.
What the Act did do was, as recommended, repeal

section 66(1) and insert instead a provision for challenging extortionate credit transactions, which is section 343.
Secondly, giving a right to interest at the Judgments Act rate into corporate insolvency. Again, copying across the position in bankruptcy into corporate insolvency.
Thirdly, amending the rules so the same provisions applied in each, obviously updating and revising the language as necessary.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: My Lord, we say no fundamental change, certainly not in either bankruptcy or particularly corporate insolvency, and certainly not in the way that my learned friends suggest.
My Lord, I mention Wentworth saying that no evidence the drafters of the Cork Report or the 1986 legislation had Bower v Marris in mind at all. Just in that respect, your Lordship may like to note one of the members of the committee, David Graham QC, was obviously counsel in re Lines Brothers number 2 who shortly afterwards argued Bower v Marris.
My Lord, coming to the operation of the rule in 2.88(7) and (9), we say its operation is straightforward and it works in the way as it did prior to the 1986 Act,

subject right to changes I've mentioned.
Firstly, all creditors are entitled to interest at a minimum of the Judgments Act rate, whether or not their debts carry interest. That's compensation for the moratorium.
Secondly, creditors that have a right to interest at a greater rate are entitled to interest at that rate. This ensures the creditors' claims to interest are satisfied in full in accordance with their full package of rights before any surplus is distributed to shareholders.
Thirdly, we say nothing in the changes to suggest that interest would not be calculated in the same way as it had been since 1743.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: We say nothing in the language of rule 2.88 which means that the calculation cannot be performed in exactly the same way as it had been performed for the last 250 years.
It may help if your Lordship were just to take rule 2.88. My Lord, starting with 2.88(7), there are three points. The first is the rule says:
"Any surplus remaining after payment of the debts proved shall, before being applied for any purpose, be applied in paying interest on those debts ..."

My Lord, we say this simply reflects the basic ranking of claims; in other words, the waterfall is: proved debts followed by interest followed by non-provable claims and then any residue to the shareholders. That has been a feature of the statutory regime since 1542.
My Lord, secondly, 2.88(7) requires the surplus to be applied in paying interest on those debts.
My Lord, we say, again, there's absolutely nothing new in that. Obviously the surplus is to be applied in paying interest on the debts which have been proved.
What is said, however, is that the reference to "those debts" is to the proved debts and the argument is that because those proved debts have been repaid, you can't apply the rule in Bower v Marris.
My Lord, that argument was equally an argument which arose under the earlier legislation. Interest was being paid on the debts, and the debts under the earlier legislation were equally the proved debts. This is no more than an aspect of what I've called the appropriation fallacy. Put another way, the rule doesn't say how interest is to be calculated. It simply says, "You pay interest in respect of proved debts". Under the previous legislation the authorities held, "Fine, pay interest in respect of proved debts but you

calculate it in the following way", namely by treating prior dividends as having applied first in relation to interest. No reason why you can't do exactly the same under 2.88(7).
The third point is that 2.88(7) says, "Well, you pay interest in respect of the periods during which they have been outstanding since the relevant date". My Lord, similarly, we say: nor does this cause any difficulty. You obviously pay interest depending on the periods for which the debts have been outstanding. The question is how do you calculate the amount of interest which is payable? My Lord, again, equally a point which arose in relation to earlier legislation or earlier interpretation of how the statutory scheme worked. It gave rise, so far as Mr Justice Mervyn Davies was concerned, to a point he raised at the end of his judgment. It was essentially the same point. He said, "Well, you have paid proved debts in full. How is it that interest could continue running? There's nothing left outstanding". To which the response was, "That's simply not how you calculate the amount of interest payable". So there's nothing in this either.
Now, my Lord, there's a danger in looking simply at 2.88(7) and ignoring 2.88(9). Your Lordship knows 2.88(9) includes the phrase "the rate applicable to the

debt apart from the administration", and so far as that is concerned, as your Lordship knows, our submission is this can naturally be read as encompassing every factor which determines the total amount of interest payable as, indeed, the administrators' skeleton so clearly confirms.
If those words "naturally encompass every factor, including the default rule" i.e. the rule in Bower v Marris, what on earth is the difficulty in applying rule 2.88(7) and (9) in exactly the same way as it had operated for the last 250 years? Equally, what on earth is the reason why Parliament wanted to change the rule, if they had wanted to change it? Why on earth change it in such a subtle manner as the administrators and Wentworth effectively contend it was changed? If you want to change the position, in our submission, you would not have done it in this way.
My Lord, I wonder whether that's a convenient time for the break?
MR JUSTICE DAVID RICHARDS: Yes, certainly. I'll rise for five minutes.
(11.45 am)
(Short break)
(11.50 am)
MR DICKER: I now need to deal, finally, with the two

arguments that are made against us and the third possibility which your Lordship identified.

The first argument is that the statute required dividends to be applied in respect of proved debts and thus discharged principal and interest therefore has to be calculated on that basis.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: In other words, payments of dividend amounted to an actual appropriation of principal.

My Lord, I mentioned to your Lordship that was Wentworth's position in its reply position paper. It also appears to be the administrators' position. The answer to it in our submission is very short. All of the authorities, back to Bromley v Goodere, hold that payments of dividends do not amount to an actual appropriation in respect of principal. In the event of a surplus, they are treated as having constituted payments generally on account and the amount of interest is calculated on that basis.

My Lord, as I'm sure Mr Smith will develop, one obvious consequence of an argument that dividends actually discharge principal arises if you are dealing with a co-obligor whose liabilities are necessarily co-extensive with those of the debtor.

So that argument, in our submission, is wrong. It's

essentially the one repeatedly raised in the authorities -- raised, I think, three or four times by Mr Jessel QC -- and rejected.

So that's the first.

The second is the complete and exhaustive code or the "occupy the field" argument. I confess it took us a little time to understand quite how this argument works but, as we understand it, it works as follows. Firstly, Wentworth accepts that in the event of a surplus, the court treats the dividends as having been paid generally on account. In other words, it's not suggesting that the effect of the scheme is that there has been an actual appropriation to principal, thereby trying to avoid the co-obligor problem. In other words, it accepts, at least in this court -- I think there's a footnote reserving its rights -- that Bower v Marris was correctly decided, at least to that extent, but it says this is irrelevant and it's irrelevant because rule 2.88 contains a complete and exhaustive code as to the calculation of interest. Its terms require interest to be calculated on the basis that dividends discharged principal.

So, in other words, this isn't an argument that principal was in fact discharged; it's an argument that on the construction of the rule, the rule requires you

to proceed effectively as if principal had been discharged.

My Lord, I have already answered the submission that the 1986 Act was intended to be a complete and exhaustive code in part. There was one point in particular I did want to just make and it's this. One might ask where does Wentworth get the fact that the rule is a complete and exhaustive code from? The answer appears to be that they rely on the fact that it "cuts across creditors' rights". That's the only basis that we can identify they rely on for saying it's a complete and exhaustive code. We say that's incorrect. No reason to regard the provisions in 2.88 as in any way different from all the other provisions in the statutory insolvency regime; in other words, they provide creditors with rights in the event of an insolvency but they don't affect, they don't discharge, they don't extinguish creditors' underlying rights.

In a sense, one could equally say the same about every provision of the Insolvency Act. It cuts across creditors' rights. Now, in one sense that's obviously correct. One's ability to enforce against an insolvent company is restricted by the effect of the moratorium. You only get payments of dividend pari passu. But one doesn't conclude from that that creditors' rights have

otherwise been extinguished. Far from it. There's absolutely no reason why this cutting across idea should operate differently in the event of a surplus.

My Lord, just to echo a comment your Lordship made in a paragraph 110 in the Waterfall 1 judgment. Your Lordship said:

"Contractual rights are compromised by the insolvency regime only for the purpose of achieving justice among creditors thorough a pari passu distribution."

They're not intended effectively to enable the debtor to benefit.

My Lord, your Lordship might also like to note that so far as this -- the argument based on cutting across rights are concerned, in substance none of the changes referred to in 86 were new. They had all existed in one form or other in one or other of the previous regimes. None of the changes actually prejudiced creditors, so if there was prejudice to creditors, it's only a result of the change alleged by my learned friends. One can overstate the extent to which, in substance, they provided any actual benefit to creditors over and above that outside of the insolvency. One has the obvious point that although creditors have a right to interest, even on debts that didn't otherwise carry interest, as

the cases indicate, one can regard that simply as compensation for preventing them from obtaining their own individual judgments carrying such interest.

My Lord, I made the point that in our submission the complete exhaustive code argument, occupy the field, is contrary to the overarching principles applicable to the scheme. Your Lordship may like to note Wentworth's skeleton seeks to deal with Wight v Eckhardt at paragraph 20. The submission made there is Lord Hoffmann was only concerned with the position if the company was insolvent. In effect, when he said creditors' rights aren't affected he was only dealing with an insolvent company. The implication being it is entirely consistent with Lord Hoffmann to say, "Yes, but in the event of a surplus their rights are affected". That seems, with the greatest respect, topsy turvy. You don't affect their right in the event of an insolvency. Underlying rights remain. It's only when you get to a situation where there's a surplus, not mentioned by Lord Hoffmann, but suddenly creditors lose their rights.

My Lord, Wentworth relies only, I think in this respect, on Danka Systems. Your Lordship may recall that's a case which effectively holds if you have a contingent claim, you can't reserve the full amount and simply wait indefinitely for what happens.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: My Lord, all that -- that is entirely consistent with the insolvency regime. Obviously if you are going to have a liquidation, you have to estimate contingent claims, otherwise all you have is a run-off.

MR JUSTICE DAVID RICHARDS: Yes. I mean, Danker was a solvent company, wasn't it?

MR DICKER: Yes.

MR JUSTICE DAVID RICHARDS: It's consistent with a liquidation regime for a solvent, as much as for an insolvent, company.

MR DICKER: Your Lordship is quite right, but if you're going to give companies the ability to wind up their affairs and to do so otherwise than by way of a run-off, then logically you need a process of estimation.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: My Lord, it remains the case that what you are trying to do is produce the best estimation you can of the value of the claim and pay that estimation. You may or may not ultimately get it right. Hindsight will help you deal with changes in the meantime. If it hasn't happened by the time of eventual distribution, it's too late. There is nothing in Danka Systems which suggests that rather than try and making the best estimate you can, the regime can lead to a position in which

knowingly the creditor can end up with less than his full entitlement.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: My Lord, those are the two arguments that, as we understand it, are made.

The third is the argument your Lordship identified which I think I described as a theoretical possibility.

MR JUSTICE DAVID RICHARDS: Hmm, hmm.

MR DICKER: The argument is that, as I understand it, the suggestion is that Wentworth does not need to argue the rules provide a complete and exhaustive code. They could just argue that rule 2.88 did not incorporate Bower v Marris, leaving open the possibility of a non-provable claim for the shortfall.

Now, obviously one reason Wentworth don't run that argument is because to the extent it would give rise to a non-provable claim, their economic position isn't assisted, but there are, in our submission, more serious analytical problems with the argument.

They are these. One could understand a legislature that decided as a matter of policy, "We think a debtor ought to be entitled to apply payments first in respect of principal, rather than interest". One may not agree with the policy but if that's what the legislature decided, then that's what would have to happen.

Now, if that was the view the legislature had taken, the logical position would be to say Bower v Marris is abolished. The rules do provide a complete and exhaustive code. They occupy the field. There's no non-provable claim.

What would be necessary for the theoretical argument to work is a very different legislature intention. What the legislature would effectively have to intend was that what you want to do is adjust the priority regime. We're entirely happy for contractual rights so far as they relate to numerical percentage, compounding or anything else, to rank equally under 2.88(9), but we're effectively going to subordinate the right to the creditor to interest calculated on the basis payments, applied defer in respect of interest.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: My Lord, we say that makes absolutely no sense at all. You can easily imagine a situation in which you have two creditors, the first of which says, "I'm happy to bargain for a simple rate of interest and I'm happy to do so on the basis that I will be able to apply payments in respect of interest first". You could equally imagine a creditor who says, "I want a right to compound interest", and you can also imagine a situation in which economically those two results will produce

exactly the same outcome.

Why on earth would the legislature effectively want to say, "We're going to carve one thing and one thing only out of rule 2.88 and that one thing which we're going to subordinate is the ability of a creditor to apply payments first to interest"? My Lord, there's no logic in it. It doesn't make commercial sense and there is absolutely no indication anywhere that that is what the legislature had in mind.

My Lord, that's why we say. No doubt Wentworth and the administrators, as we understand it, are not running that argument. And why, in any event, it is incorrect.

My Lord, one further and final point. Whichever of the two -- whichever of the second and the third argument are adopted, they both share the same -- this feature: they both proceed on the basis that dividend payments were not in fact applied in respect of principal and didn't in fact discharge principal, so they are both methods of calculation. The first occupies the field. The second leaves open the possibility of a non-provable claim, but they're both methods of calculation.

Now, the only difference between that method of calculation and that which existed for the previous 250 years is previously the method of calculation said

you apply payments first in respect of interest. Wentworth's argument is essentially now for some reason the legislature decided to change the method of calculation and to say, "I'm sorry, although that's how it was done for the previous 250 years, now you're going to have to calculate it in a different way". My Lord in other words, all of the early steps in the argument are effectively identical. We're both talking about a method of calculation. The only difference is we say it should be done in the way it's been done for the last 250 years. Wentworth say, "I'm sorry, everything changed in 1986. It now needs to be done in the reverse of the way it had previously been done". My Lord, again, we say nothing to indicate that that was intended.

My last word on question 2 is this: there is no subsequent case after the 1986 Act that gives any support to such a change having occurred. There are a large number of cases which have continued to cite cases such as Humber Ironworks, Joint Stock Discount Company, re Lines Brothers, at the highest level. We refer to some of them in paragraph 148 and paragraph 149 of our skeleton. Wight v Eckhardt is an obvious example.

MR JUSTICE DAVID RICHARDS: Yes, but have they been -- have they been cited in this context or for other propositions?

MR DICKER: No, I can't say that, but what I can say is that when Lord Hoffmann summarised the effect of the statutory regime in Wight v Eckhardt and no doubt had Humber Ironworks in mind, it would be extraordinary if he summarised the effect of the scheme in the way he did if he didn't at least proceed on the basis that Humber Ironworks was correct, both in relation to the insolvent position and also the solvent position.

MR JUSTICE DAVID RICHARDS: Shall we just look at Wight v Eckhardt in the light of that.

MR DICKER: My Lord, it's 1D at 132. If my Lord goes to paragraph 27 -- sorry, I should just start at 148:

"The cases referred to in the opinion of their Lordships ..."

Your Lordship will note Humber Ironworks.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: At 27:

"The winding up leaves the debts of the creditors untouched ...(reading to the words)... can result in the company being restored for the process to continue."

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: My Lord, one might think it's a remarkable state of affairs if my learned friends are right. One has an underlying debt. Central to that underlying debt is the interest which it accrues. On my learned friend's case that is the one aspect which the legislature have decided effectively to in part extinguish. There's no similar extinguishment, apparently, about any other non-provable claims.

Again, it simply doesn't make sense.

The final reference to one textbook is to Gore-Browne. It's bundle 2, tab 7. If you have tab 7, it's 18F, if my Lord has that? The relevant bit is, if your Lordship just goes six lines down, there's a sentence towards the end beginning:

"Such interest is itself provable if part of the debt to the extent it is payable in respect of a period preceding the commencement of the liquidation".

Then the relevant bit is footnote 3. There's a reference:

"A dividend paid in respect of principal and interest is attributed first to the interest: Joint Stock Discount Company."

So it's not perhaps the clearest of references but the editors of Gore-Browne appear to regard that aspect of Joint Stock Discount Company as still good law.

MR JUSTICE DAVID RICHARDS: So rule 4.93(1) is -- yes, where a debt -- yes, I see. It's the equivalent for

winding-up, isn't it? Yes.
MR DICKER: My Lord, subject to my Lord --
MR JUSTICE DAVID RICHARDS: Paid in respect of principal -- yes, thank you.
MR DICKER: My Lord, on any basis it's an odd state of affairs. If we have ended up in a position where creditors' claims aren't satisfied in full, one might have expected that to be a major discussion in the textbooks, in learned articles, as to what is the reason for this exception to the otherwise overarching principle that applies. No indication of that. To the extent there are indications, everyone seems to think we're carrying on as we have always done.
MR JUSTICE DAVID RICHARDS: My recollection is that Robin Potts used to write the section on liquidations in Gore-Browne.
MR DICKER: Your Lordship would know.
MR JUSTICE DAVID RICHARDS: Just interesting, given that he was counsel in re Lines Brothers.
MR DICKER: Yes. It's also interesting -- I think that, if I may say this, it is remarkable, your Lordship may think, how consistent the approach is throughout the Commonwealth on this issue over the last 200 years. It's also, when one gets to re Lines Brothers, interesting again, your Lordship might think, it was

a matter of common ground between the very experienced counsel in that case.
My Lord, that's all I was proposing to say in relation to question 2.
MR JUSTICE DAVID RICHARDS: Just so it doesn't completely slip my mind. In re Lines Brothers the state of the rules at that stage -- I've just forgotten -- did the rules make express provision for the payment of contractual and similar interest?
MR DICKER: There was no similar express provision.
MR JUSTICE DAVID RICHARDS: There was no express provision dealing with it at all?
MR DICKER: Absolutely.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: That's the reason for the administrators' distinction between 1883 --
MR JUSTICE DAVID RICHARDS: I was just trying to remember because it was -- what was said to be a solvent liquidation, therefore the bankruptcy rules didn't apply and there was just nothing express applicable.
MR DICKER: One had to effectively go back to almost Bromley v Goodere: how does the scheme work as a whole? The general operation of the scheme by reference to the principles governing it are: members come last; how do we achieve that? Creditors have to be paid in full.

MR JUSTICE DAVID RICHARDS: It will be said it's a remission to rights type of case. I just wanted to be clear about that. Thank you.
MR DICKER: Yes.
My Lord, question 3 I've already, I think, dealt with and I wasn't proposing to say any more about.
My learned friend, Mr Trower, referred to a subsidiary issue about whether compounding continues beyond the date of the final dividend, which your Lordship may remember.
MR JUSTICE DAVID RICHARDS: Yes, I do remember.
MR DICKER: It's essentially on -- the well, the issue assumes a creditor entitled to compound interest, either as a matter of contract or otherwise, and the administrators ask: does the interest continue to compound in full under rule 2.88(9), following payment in full of principal, or, if not, does the creditor have a non-provable claim for the shortfall?
Our first submission is the point simply doesn't arise because it assumes they're right on question 2.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: But if the issue does arise, our submission is of course interest must continue to compound. Interest has been compounding right up to the date of final dividend. It's common ground, given the answer to

question 3. Why on earth would it cease to compound? Why on earth would you cease to be entitled to interest on the accrued interest after the payment of final dividend? What magic is there in payment of final dividend to stop that occurring? That's the short point.
We also say that if that's not right, and mirroring the structure of our submissions elsewhere, there must be a non-provable claim for the shortfall. My Lord, we deal with it, just so your Lordship knows, fairly briefly in paragraphs 187 to 189 of our skeleton argument.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: My Lord, that only leaves question 39.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: I can deal with that, I hope, relatively shortly. Question 39 arises after one has answered what rule 2.88(7) and (9) provide, and also other questions.
It asks whether a creditor may have been entitled to any further compensation for delay and, if so, what form this compensation takes? Obviously the importance of this question depends in part on the answers to the earlier ones. As my learned friend Mr Trower mentioned, if Bower v Marris doesn't apply, then the amount of the shortfall potentially subject to a non-provable claim,

the subject matter of question 39, is much larger than it otherwise would have been.

One can make a similar point in relation to question 3. If the rate applicable to the debt doesn't include Bower v Marris either, then, again, the shortfall is bigger and this question becomes more important.

My Lord, just so your Lordship knows, it is also potentially relevant in the context of questions 6 and 8, which your Lordship hasn't yet seen. But again, for similar reasons, if the operation of the rule for estimating contingent claims, discounting future claims, providing interest on those claims gives creditors less than they otherwise would have been entitled to, again the question arises: is there any other claim they may have effectively as a non-provable claim?

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: My Lord, the starting point, of course, are the fundamental principles which we set out in the introduction to our skeleton argument and I am not going to repeat those.

We divide our answer to question 39 in two parts.

The first part concerns a situation in which a creditor says, "I have an underlying right to payment which has not been satisfied in full and involves him

making a non-provable claim for any shortfall".

The second concerns the entitlement to interest at the Judgments Act rate under 2.88(9) which is a right derived from a statutory scheme itself. What I can't say in respect of that I have a right outside of the insolvency and the analysis therefore is different in relation to each.

Starting first, and hopefully the position will become clear, with non-provable claims in respect of what I've called underlying rights. The starting point is that where the sums paid to a creditor pursuant to the insolvency process have not satisfied his claims in full, he has a non-provable claim for the shortfall.

MR JUSTICE DAVID RICHARDS: So is this postulating that he has a contractual or other right to interest which is not fully satisfied?

MR DICKER: Correct. Absolutely.

MR JUSTICE DAVID RICHARDS: I see.

MR DICKER: One starts with the basic architecture of the scheme which is if you don't receive what you're otherwise entitled to through the collective process at level 1, you have a non-provable claim after interest has been paid. As your Lordship just mentioned, the reason for the shortfall is irrelevant. It doesn't matter whether the underlying right is contractual,

statutory, tortious or whatever.

The third point is the underlying claim which has not been satisfied may therefore be a claim for compensation for delay. So to take your Lordship's example, a creditor who has a contractual right of interest, if for whatever reason he doesn't receive full amount that he is entitled to receive as a matter of contract, there is a shortfall and on general principle he should have a non-provable claim for the amount of that shortfall.

MR JUSTICE DAVID RICHARDS: Yes. I mean, that's simply his contractual right to interest giving credit for what he has previously received.

MR DICKER: Absolutely. Your Lordship will no doubt recall in Waterfall 1 your Lordship gave admittedly a slightly unusual situation in which this may occur, where there is effectively a lacuna in the rules.

MR JUSTICE DAVID RICHARDS: Oh, yes.

MR DICKER: Paragraph 127 of your Lordship's judgment.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: As your Lordship just mentioned, the claim is based on the underlying right, and obviously all the creditor is essentially saying is, "I have a contractual or other right to interest. This is how much it amounts to. I haven't been paid it in full. I therefore have

a claim".

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: The insolvency process in a sense is irrelevant, save that it provides the measure of the delay which gives rise -- which has to be taken into account in working out how much the claim is.

My Lord, the next point is a more significant one. Because the basis for the non-provable claim doesn't matter, it doesn't matter whether it's contract, tort, et cetera, it can also include a claim for damages for delay. So one starts with the fact that a court has a common law jurisdiction to award interest as damages on claims for non-payment of debts, as well as on other claims for breach of contract or tort. So following Sempra Metals, a creditor may therefore have a claim for damages for his actual losses caused by the late payment of his debt.

My Lord, I'm sure your Lordship is familiar with Sempra Metals. I don't know whether I need to turn it up.

MR JUSTICE DAVID RICHARDS: Well, let's look at it. It's not something that I've actually come across in -- I'm aware of it, but it's not something I've come across.

MR DICKER: My Lord, it's in 1E at tab 146. My Lord, taking this as shortly as I can, held, at the bottom of

page 561, is that:

"The anomalous and unprincipled exception with regard to interest losses by way ...(reading to the words)... non-payment of debts as well as on other claims for breach of contract and tort."

My Lord, two passages from the speeches of their Lordships. First, from Lord Hope at page 581. It may be quickest if your Lordship were simply to read paragraphs 16 through to 18.

MR JUSTICE DAVID RICHARDS: Certainly. (Pause)

18 is concerned with the restitutionary cause of action.

MR DICKER: Yes.

MR JUSTICE DAVID RICHARDS: Are we --

MR DICKER: Not in detail. The only point is obviously you can have a claim in damages regardless of the underlying.

MR JUSTICE DAVID RICHARDS: Yes, I see.

MR DICKER: But no.

MR JUSTICE DAVID RICHARDS: Okay. No, absolutely.

MR DICKER: 41, if your Lordship just turns to that, just to note Lord Hope saying, 41:

"Compound interest is a necessary and very familiar fact of commercial life. As the Law Commission said, the obvious reason for awarding compound interest is

that it reflects economic reality."

Then a reference to the Scottish Law Commission endorsing the view of the Law Society in their response that:

"Simple interest never provides a full indemnity for the loss to the litigant."

MR JUSTICE DAVID RICHARDS: Hmm, hmm.

MR DICKER: That's all I think from Lord Hope.

If your Lordship goes to Lord Nicholls, there is a lengthy discussion. If your Lordship goes to paragraph 74, a section dealing generally with interest losses and damages. 84, a discussion of previous decision of the House of Lords in La Pintada. Then, at 92, the restrictive common law exception today.

Picking it up at 93, if I may:

"In La Pintada the House made clear that, contrary to the general understanding of the effect ...(reading to the words)... whether the borrowing costs comprise simple interest or compound interest."

Then 94:

"To this end, if your Lordships agree, the House should now ...(reading to the words)... such as remoteness, failure to mitigate", and so forth.

Then a discussion of remoteness, causation and the various ways in which those points may be addressed.

Then at 97:

"Common law's unwillingness to presume interest losses where payment delayed ...(reading to the words) is to be found in the statutory provisions."

Then at paragraph 100:

"For these reasons, I consider the court has a common law jurisdiction to award interest, simple and compound, as claims on damages for non-payment of debts, as well as on other claims for breaches of contract and in tort."

My Lord, Lords Scott, Walker and Mance also gave speeches but I don't think I need to show your Lordship those.

Now, we obviously accept that to the extent that such a damages claim is measured solely by the time value of money and relates to the period after the date of administration, it's not provable. The cut-off rule in respect of post-insolvency interest must plainly cover claims for damages measured by the time value of money for that subsequent period, but the consequence is we say that the creditors' underlying claim for loss and damage is nevertheless unaffected by the insolvency process. That's Lord Hoffmann in Wight v Eckhardt. If he's not been satisfied in full, he has a non-provable claim for the shortfall.

One can test it this way. Imagine a creditor who is faced with a breach of contract shortly before the company goes into administration and has a claim from damages for late payment of money, part of which pre-dates the administration, part of which post-dates it. He's plainly entitled to prove in respect of the prior period. What is it in the insolvency scheme we say that extinguishes his claim for damages in respect of the period after the commencement of the administration? What is it that prevents him from saying if there is a surplus, "I have a claim for damages which has not been satisfied in full; that is a right I have, according to the House of Lords in Sempra Metals, it hasn't been satisfied in full and I'm now entitled to shortfall".

It may be in many cases such a claim will be of limited commercial importance because the creditor either can't establish such loss, hasn't incurred it or whatever, all because the Judgments Act rate already provides adequate compensation. But if that is not the case, then we say there is a non-provable claim for damages in respect of the shortfall.

MR JUSTICE DAVID RICHARDS: I mean, I don't know if we one has actually advanced such claim in the administration of Lehmans. I mean, I don't know for sure, but I'm not

aware that Sempra Metals-type claims for damages for late payment are very common. I have remarked that I don't think I've come across one, but I'm not just from general awareness, it's not at any rate as yet I think something that crops up very much.

MR DICKER: My Lord, from my experience, for what it's worth, is along the same lines. There may be a number of practical reasons for that; one of which may be that the Judgments Act rate at the moment --

MR JUSTICE DAVID RICHARDS: The Judgments Act rate only takes you from judgment. It doesn't take you from the date of breach until the judgment.

MR DICKER: Although section 35 gives you a right to pre-Judgment Act interest.

MR JUSTICE DAVID RICHARDS: To an award of interest by the court you mean?

MR DICKER: Yes. So you can get that from the date the cause of action accrued.

MR JUSTICE DAVID RICHARDS: But it tends to be at a sort of ordinary sort of borrowing rate at -- but simple, of course, not compound.

MR DICKER: Yes.

MR JUSTICE DAVID RICHARDS: Anyway, yes. You're right here, in practice it may be that save in very exceptional circumstances, even if -- if Wentworth and the

administrators are right about how 2.88 works, nonetheless the amount of interest that creditors will get would really extinguish any possible claim they might have of a Sempra Metals type, unless there were some very special factors.

MR DICKER: And the point is simply this: as a matter of analysis, assuming such special facts, there is absolutely nothing in the scheme that would exclude such a claim and so the right of the creditors, like any other, which, according to Lord Hoffmann, continues unaffected and subject only to the complete and exhaustive code point, no reason why it shouldn't be payable as a non-provable claim. And, if one goes back to the basic position, why not? Creditors are entitled to have their claim satisfied in full. This is such a claim. There is a surplus. Why should the debtor be entitled to benefit from having gone into insolvency, getting rid of a liability for damages which it would otherwise have had to bear? Certainly nothing as a policy reason based on the fact that such a claim for damages may include a claim for compound interest, as the House of Lords indicate. There's nothing as a matter of principle objectionable to compound interest claims.

My Lord, exactly the same analysis, we say, can

apply to a claim denominated in a foreign currency. If the creditor has a contractual or statutory right to interest which for any reason has not been satisfied in full, then he has a non-provable claim for the shortfall. It doesn't matter if his underlying claim for interest is pursuant to some foreign contract, foreign judgment, foreign statute.

Similarly, if the creditor with a claim denominated in a foreign currency has a claim for damages for non-payment of his debt when it fell due for payment, then equally he has a non-provable claim for any shortfall. It doesn't matter whether the claim is governed by English law or some foreign law.

Now, the only answer, as we understand it, to this point by the administrators and Wentworth is the occupy the field; in other words, "Fine, outside of insolvency I entirely accept you have such claim but, I'm sorry, it's disappeared because the rules have effectively operated to extinguish it once and for all".

My Lord, I said there's a separate analysis required in relation to interest at the Judgments Act rate. The reason for that is of course that the right is one provided by the statute itself. So one can't begin the analysis by referring to the rights of a creditor outside of the insolvency. They're simply not relevant.

The analysis therefore must depend on the terms of the rule and the operation of the scheme as a whole.

So what your Lordship is concerned with here is how creditors' entitlement in respect of statutory interest is intended to work. We say two points one has to take into account. First, the starting point is the legislature provided that creditors are entitled to a minimum of 8 per cent interest on their debts. Obviously, as I submitted earlier, if interest stops running effectively on the date of final dividend, at the date of each dividend more accurately, for the relevant amount of the dividend, and the interest is only paid some years later, then the effective rate that the creditor receives is not 8 per cent but some lesser rate, depending on how long it's taken him to pay it. That's just a consequence of the time value of money. You have accrued entitlement to, say, £100 interest. If it's not paid for five years, the £100 in effect is no longer worth 8 per cent. It's been diminished over time. We say it would be very odd if the legislature had intended to provide for interest at 8 per cent in the way for which the administrators and Wentworth contend, given the consequence of delay; in other words, without accounting for it.

The second point again I've already mentioned is the

possibility of unequal treatment between creditors.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: Again, it's the same argument at the sort of non-provable level. Assume a creditor with a contractual right to interest. If we're right in our earlier submissions, he is entitled to compensation for the time it takes to distribute the surplus. He may be entitled because he's got an underlying contractual right to interest. He may be entitled because he has a claim for damages. It doesn't matter. If, however, Wentworth and the administrators are right that the amount of interest payable to a creditor who is only entitled to interest at the Judgments Act rate is effectively fixed forever with each payment of dividend -- so you get to the final dividend, you have a fixed sum, it can never go up; those creditors effectively will not be treated equally. They will not receive any compensation for the delay in the distribution of the surplus. Other creditors will. They won't.

We say the legislature can't have intended that result either, so the only question is how does the statutory scheme avoid it?

Now, the way it avoids it, we say, is as follows. The first point is the creditors' right to interest at

the Judgments Act rate is a right which they are given pursuant to rule 2.88(7). It's a statutory right like any other. What 2.88(7) requires is that any surplus remaining after payment of the debts proved be applied in paying interest on those debts; in other words, it requires the surplus to be applied in payment of interest after you have paid proved debts in full.

The second point is that the right, as I have already submitted, is a form of contingent right conferred on creditors at the commencement of the administration. It's a right to interest contingent on there being a surplus.

Thirdly, the right we say is also a liability of LBIE's. My Lord, in making that submission we're echoing the approach your Lordship took in the Waterfall 1 judgment.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: It's paragraph 71 where your Lordship dealt with an argument of: is the obligation an obligation on LBIE or is it simply a duty of the administrators?
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: Your Lordship said, effectively, well, it can be both. There's no reason it can't be an obligation on the part of LBIE and also involve a duty on the part of the administrators.

MR JUSTICE DAVID RICHARDS: Yes. I mean, to be clear, that was a question of the construction of the subordination agreement.
MR DICKER: Yes. Well, echoing that, if I may, applying that here, we say that the same point can be made in relation to 2.88(7). It gives creditors rights and it imposes an obligation on LBIE. The right is to distribution of the surplus on payment of final dividend. That effectively is the stage, we say, at which the obligation arises on LBIE.

Now, it might be said, "Well, how does that work? You're not suggesting, are you, that the administrators were in breach of duty for failing to distribute the surplus on payment of final dividends?" The short answer to that is, "No, of course not", but we're dealing with two different things. Just as we are in relation to the underlying insolvency, there's no problem in saying that when LBIE went into administration it owed sums of money. It's perfectly consistent to say that at the same time as saying but of course the administrators weren't in breach for failing to pay a dividend on day two. The two issues are different.

Now, the next stage is we say the mere fact that there is a dispute as to how the surplus should be

applied, which requires determination by the court, doesn't mean the debt or liability doesn't exist. So one could test it this way: the creditors could have issued proceedings the day after final dividend had been paid, seeking a declaration that they were entitled to the surplus and seeking an order for payment by LBIE of the amount due.

Now, it's true the court would have to decide the dispute. Having decided the dispute, the court would effectively be declaring what the rights of the parties were as at the date of final dividend. The court would be declaring that as at that date, final dividend having been paid, these creditors were entitled to the following so far as surplus was concerned.

We say the consequence of this is essentially to give rise to another non-provable claim for damages. If we're right in our analysis of how the statutory scheme works, creating rights and obligations, and if we're right that the obligation effectively arose, so far as LBIE was concerned, on the date of final dividend, in the sense that's when LBIE came under an obligation to apply the surplus, one has another non-provable claim for damages for any subsequent delay .

Now, the answer that's put forward, as we understand it, is essentially, "Hang on, rule 2.88(7) doesn't

actually say when the surplus is to be distributed". So if there isn't a particular date when the surplus is to be distributed, there can't be an obligation on LBIE to distribute it and there can't therefore be a breach of that obligation and there can't be any question of a damages claim for delay in payment.

Now, it's perfectly true, of course, that 2.88(7) doesn't specify a day when the surplus has to be applied, but what it says is it has to be applied after payment of the final dividend. We know when the final dividend occurred so there's no difficulty effectively of identifying the relevant date.

My Lord, the final point is this: one alternative would have been for the creditors to have applied for permission to commence proceedings for a declaration that they were entitled to payment of the surplus and for an order for payment.

MR JUSTICE DAVID RICHARDS: Payment of the surplus ...?

MR DICKER: And for an order for payment. Payment essentially for the amount to which they were entitled; in other words, to seek an order that when the dispute is resolved it will be found that they were entitled to the surplus and should be paid. The only reason it's not being distributed is because there is this dispute that needs to be resolved.

MR JUSTICE DAVID RICHARDS: Yes.

MR DICKER: So one alternative for creditors would be to issue -- everyone to issue proceedings and then to say either, "I am entitled to pre-judgment interest from the date I commenced my proceedings". As your Lordship says, there may be an issue about precisely what the rate of interest would be. That would be a way of creditors alternative of getting some form of compensation for this delay.

Alternatively, if your Lordship thought that wasn't necessarily sufficient, to say, "Well, at the moment there's the moratorium but I can lift the moratorium and effectively I can permit judgment to be entered into". The difficulty with that, of course, is it's quite difficult to work out what the terms of the judgment would be.

The final stage then is this: the whole process of the insolvency scheme is to avoid creditors having to take those sorts of steps, actually to issue proceedings, given the cost, delay, et cetera, that's involved. Again, applying the same logic that applies to the statutory interest provision in the first place, namely it's compensation for not having had judgment yourself, you can apply exactly the same reasoning at this point and say this is another justification why we

ought to construe the scheme in the way I've submitted; in other words, construe it as saying on payment of final dividend LBIE came under an obligation to distribute the surplus and essentially interest should run from that date.

The reason for this is, just going back to the underlying position, at the moment we have a situation where there may be 6 billion sitting with the administrators. According to the administrators and Wentworth, the amount of interest to which creditors are entitled is fixed so they will receive the same amount however long it takes to distribute that surplus. We say that needs to be addressed and this is the way in which it can be addressed and plainly it should be addressed. Parliament can't have intended essentially the debtor, the shareholders, to benefit from this delay, to receive the interest earned on that money until it becomes possible to distribute the surplus.

My Lord, I think it's York in its skeleton refers to the sort of perverse incentive that might give shareholders to delay the eventual distribution of the surplus. If creditors and their entitlement to interest was fixed and if any money earned on the surplus would go to them, rather than creditors, it would effectively give them, one might say, a free ride. Indeed, one may

say it's worse than that. It would effectively reward them for the journey and pay them per mile.

MR JUSTICE DAVID RICHARDS: Well, I mean, I think the main point I'm taking from this submission is that there will inevitably be a delay between the date of the payment of the final dividend and the payment of interest under rule 2.88. You say, well, if we apply the Bower v Marris principle, that deals with that issue.

MR DICKER: Yes.

MR JUSTICE DAVID RICHARDS: I think these alternative ways of putting it are much more difficult because you would only be entitled to an award of interest from the date on which the interest became payable, but it may be right that interest is due from the date of the final dividend but it's not going to be payable from that date precisely because the administrators have to take various steps before they can make payment. So I'm not sure you have a complete cause of action for payment from that date.

MR DICKER: My Lord, your Lordship is entirely right that this is an alternative argument. If am right on Bower v Marris, I don't need this.

MR JUSTICE DAVID RICHARDS: I appreciate that, yes.

MR DICKER: Can I just add this final word on your Lordship's point.

MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: It goes back to a comment made in a series of Canadian cases, including Attorney General of Canada v Confederation Trust. Picking up the words of Lord Justice Selwyn that no one should be prejudiced by the time taken to realise the assets, they add the additional point that of course no one should be prejudiced either by the time taken to distribute them. That they regard as the underlying principle for the operation of the insolvency scheme.
We say one needs to try and construe rule 2.88 in a way that gives effect to that. Your Lordship is absolutely right, what in effect one does need to do is to say this money needs to be treated as effectively having become payable. Then creditors shouldn't be prejudiced simply because there's a dispute with the shareholders as to whether or not they're entitled to it and therefore, if it's not paid, they ought to be treated as having a claim for damages for late payment.
Your Lordship is right, our primary argument is question 2.
MR JUSTICE DAVID RICHARDS: Yes.
MR DICKER: My Lord, I'm conscious I've taken slightly longer than the about a day I indicated but --
MR JUSTICE DAVID RICHARDS: That completes your submissions

on these issues.
MR DICKER: It does.
MR JUSTICE DAVID RICHARDS: So I hear next from Mr Smith.
Mr Smith, how long do you anticipate being?
MR SMITH: Perhaps a couple of hours, my Lord.
MR JUSTICE DAVID RICHARDS: Can I just say -- I hesitate to move everyone around and it slightly depends on how long everyone is going to be. I appreciate Mr Zacaroli will be a little while tomorrow. It's much easier for me if the counsel on his feet is here, as it were, rather than down there (Indicated) so if you're going to be much of the afternoon, it doesn't necessarily mean your entire teams need to switch over, but it's a help to me anyway.
MR DICKER: I was certainly proposing to move down. I do recall, I think, the McKillen trial in front of your Lordship, trying to cross-examine the witness.
MR JUSTICE DAVID RICHARDS: It wasn't terrific, was it? On the whole I managed with McKillen to move people around so I had that in mind actually, Mr Dicker. Good. Thank you. 2 o'clock.
(1.00 pm)
(Luncheon Adjournment)
(2.00 pm)
Opening submissions by MR SMITH
MR JUSTICE DAVID RICHARDS: Yes, Mr Smith.

MR SMITH: My Lord, perhaps I can begin by gratefully adopting everything Mr Dicker has said. I intend to emphasise a few points and add some additional points in relation to issues 2 and 3. I'm not proposing to add anything in these submissions in relation to issue 39. We rely on our written materials for that and also on Mr Dicker's submissions.
MR JUSTICE DAVID RICHARDS: Right.
MR SMITH: I'm going to endeavour not to repeat Mr Dicker and I won't, with one or two small exceptions, take your Lordship back to the authorities Mr Dicker has taken you to.
MR JUSTICE DAVID RICHARDS: Right.
MR SMITH: My Lord, perhaps if I can begin just by making some general remarks on the rule in Bower v Marris. Mr Dicker has obviously explained the policy reasons why the Bower v Marris approach should be applied for the purposes of calculating interest payable under rule 2.88.
MR JUSTICE DAVID RICHARDS: Yes.
MR SMITH: The first point in our submission is the rule makes commercial sense. It treats the principal on which interest continues to run as having been paid last. Therefore, by operation of the rule, it ensures that a creditor is compensated for any late payment that

is made as whole as possible. In our submission there's an inherent commercial sense to that.
Similarly, it places the creditor as close as possible to the position he would have been in if the same payments had been made by a solvent debtor. That of course is one of the main points made by Lord Cottenham in Bower v Marris itself.
Now, the way in which Wentworth and the administrators have put their case as to why the Bower v Marris approach should not be followed in relation to rule 2.88 seems to us to raise two related issues. The first is the extent to which Bower v Marris and the other authorities which have applied the same approach are relevant authorities for the purposes of rule 2.88. That, it seems to us, is principally a question of understanding the relevant statutory schemes and other distribution schemes which were in place at the time of those authorities and seeing if there are or are not relevant points of distinction in relation to the position under rule 2.88.
Obviously the technique of Wentworth and the administrators is to seek to distinguish the authorities as far as they can until they reach a residue they can't distinguish which they then say are wrongly decided. On the other hand, what we would say is that subject to

actually some fairly minor differences, the authorities have all concerned schemes for the distribution of estates which are materially the same as that which applies under the 1986 Act and the 1986 rules.

So, my Lord, that's the first issue.

The second principal issue, as we see it, is the extent to which the terms of rule 2.88 itself can be said to exclude the application of the Bower v Marris approach and actually require a different approach to be taken to the calculation of statutory interest. So that is obviously principally a question of the construction of the rule, but in approaching construction we suggest it's approached against the background of the existing authorities and also the forms of the statutory provisions which have been considered in those cases.

So, my Lord, I'm going to focus on those two issues in these submissions.

The starting point is perhaps to understand the legal basis of Bower v Marris approach itself; in other words, how does it work legally? In our submission it can be summarised as follows. First and foremost, it rests on the foundation that dividend payments made in respect of proved debts are not treated as having been appropriated to the proved debt when they are made. That is essentially the argument which was put in

Bower v Marris and which was roundly rejected by Lord Cottenham.

Secondly, rather, such payments are treated as having been ordinary payments on account made by the debtor. They're not treated as having been appropriated between principal or interest when they are made.

Accordingly, and this is the third point, if and when there is a surplus such that a right to post-insolvency interest arises at that point, for the purposes of calculating such interest the creditor is then entitled to treat the dividend payments previously made as having been applied first in discharge of interest before discharge of principal.

Now, in our submission that isn't an overly complicated approach. It's also not a rule which depends on a contractual right to have the proceeds applied in a normal way or on the fact that the right to interest is a contractual right, rather in our submission it reflects the ordinary way in which payments made by a debtor to his creditor fall to be treated where there is no appropriation by the debtor.

Now, my Lord, following from that, an important point at the outset is to identify what is the correct treatment of dividend payments for the purpose of calculating post-insolvency interest, whether

subsequently found to be a surplus so that a right to that interest arises. Now, in our submission the authorities very clearly demonstrate that for these purposes dividend payments are treated as ordinary payments on account. That's a point we would suggest is fairly conclusively shown by the authorities. Mr Dicker has shown you, I think, Humber Ironworks, page 645, Lord Justice Selwyn, which is in tab 27 of the authorities bundle 1A. There's also Lord Rommily, Master of the Rolls, in re Joint Stock Discount Company number 2, which is in tab 14, authorities bundle 1A. There's Whittingstall v Grover, Mr Justice Chitty, which we'll come to. And of course re Lines Brothers number 2, where it was common ground between everyone, and the judge agreed, that the payments were treated as ordinary payments on account.

My Lord, in addition there's also a Scottish case, Gourlay v Watson, which Mr Dicker took your Lordship to briefly yesterday.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: I was just going to take your Lordship back to that, if I may.

MR JUSTICE DAVID RICHARDS: Just so I understand it, I've just opened up what Lord Justice Selwyn said in Humber Ironworks.

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: Sorry, tab --

MR SMITH: 1A, tab 27. It's the passage at the bottom of page 645.

MR JUSTICE DAVID RICHARDS: What I see him as saying is really that it's -- in the event of there being an ultimate surplus, the account must be taken as between the company and the creditors in the ordinary way; that is, as pointed out in Bower v Marris.

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: I mean, it seems to me idle to say that when the payments are made they're not payments of principal.

MR SMITH: Yes, I don't think --

MR JUSTICE DAVID RICHARDS: Clearly they are.

MR SMITH: No.

MR JUSTICE DAVID RICHARDS: It's more that ex post facto, isn't it, they are deemed -- this is the argument -- to be ordinary payments on account?

MR SMITH: Yes. Your Lordship says "deemed". I think the word we have used is "treated". It's for the purposes of calculating insolvency interest they are treated as ordinary payments on account, absolutely.

MR JUSTICE DAVID RICHARDS: Yes, I see.

MR SMITH: Now, I was just mentioning to your Lordship the

cases where I think that point is picked up and essentially repeated and reiterated.

There's also the Scottish decision in Gourlay v Watson which your Lordship will see in authorities bundle 1B at tab 51. My Lord, I think the easiest place to probably pick up the facts are on page 764.

MR JUSTICE DAVID RICHARDS: Right.

MR SMITH: Your Lordship will see, on page 764, there's a rather long footnote which basically sets out the opinion of the Lord Ordinary who was the judge below.

MR JUSTICE DAVID RICHARDS: Just before we get to that, just remind me what this concerned, in the sense of -- it was a trust deed --

MR SMITH: It was.

MR JUSTICE DAVID RICHARDS: -- for the proof of creditors?

MR SMITH: It was. It was a slightly unusual set of facts. What happened was that three brothers had established a trust over their shares of the estate of their deceased father, and the purpose of the trust was essentially to meet the liabilities of the estate.

MR JUSTICE DAVID RICHARDS: Right.

MR SMITH: Their own liabilities, and then with the residue back to them. So that was the nature of it. It was essentially a trust for the benefit of creditors.

MR JUSTICE DAVID RICHARDS: Right.

MR SMITH: I think your Lordship probably picks that up --

MR JUSTICE DAVID RICHARDS: It's in the headnote, I see.

MR SMITH: It is in the headnote. It's also on page 764, the first paragraph.

MR JUSTICE DAVID RICHARDS: Right, yes.

MR SMITH: The first paragraph in the opinion of the Lord Ordinary he refers to the three brothers of the name Wilson:

"... the disponent assigns to the trustees their respective shares of the estate left ...(reading to the words)... and these creditors all signed a document consenting to the arrangement which the deed embodied."

Then, my Lord, there's this point, the terms of the trust deed conferred certain powers on the trustee, including all powers and privileges competent to the office of a trustee under a sequestration.

Then the Lord Ordinary said this:

"I gather that the kind of arrangement contemplated was a gradual liquidation in which it was ...(reading to the words)... the hands of the trustees a surplus £9,500 which forms the fund in medio in this action."

Then he then goes on in the next paragraph to describe essentially the claims on that fund.

Your Lordship will see, towards the end of that

paragraph, there's a reference to Messrs James Watson & Co. They say:

"The payments made to account made by the trustees ...(reading to the words)... is still due to them."

So essentially they were making a Bower v Marris point and saying actually there's still outstanding interest owed us to because it falls to be calculated in accordance with the Bower v Marris principle.

My Lord, the claim for interest is described further over the page on page 765. Your Lordship sees how it was put. At the top of the page, it sets out:

"James Watson & Co did so and argued..."

Then the basis on which it was put appears towards the end of that paragraph, where it's said:

"Even in a sequestration if there should ultimately be a ...(reading to the words)... after the date of the sequestration."

Then there's reference in the footnote at the bottom of the page to section 52 of the Bankruptcy (Scotland) Act 1856 which basically set out the rights of a creditor. It's really the last bit of that which is relevant. If your Lordship sees right at the bottom of the page, it says:

"And if there be any residue of the estate [over the page] after discharging the debts ranked, he should be

entitled to claim out of such residue the full amount of the interest on his debt in terms of law."

MR JUSTICE DAVID RICHARDS: So a sequestration, because the trustees had all the powers and privileges competent to the office of a trustee under a sequestration, that is a bankruptcy?

MR SMITH: It is, yes, the equivalent.

MR JUSTICE DAVID RICHARDS: So effectively he's saying he's got all the powers of a trustee in bankruptcy.

MR SMITH: Exactly. Although it's formally established as a trust, how it's worked is that the powers applicable in a sequestration or a bankruptcy have been incorporated in. So for all intents and purposes it works as if it was a bankruptcy.

Your Lordship sees, just going back to the text in page 765, it says:

"The creditors are accordingly entitled, there being a surplus, to principal and legal interest, unless they had done something to disentitle them."

MR JUSTICE DAVID RICHARDS: I'm awfully sorry, just repeat what you said then.

MR SMITH: So I'm back in the actual main body of the text on 765. The last sentence of the main body of the text.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Your Lordship sees it says:

"The creditors are accordingly entitled there being a surplus, to principal and legal interest, unless they had done something to disentitle them."

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Now, there is just a point on the reference to "legal interest" which I ought to just explain. It's actually dealt with in a much later Scottish case which your Lordship will find in bundle 1E. It's 1E, tab 158A. It might be worth your Lordship turning it up. It's just one paragraph. It's tab 158A in that bundle. It's a decision of the Outer House Court of Session, in the cause of the official liquidation of Weir Construction (Contracts) Limited.

The facts don't matter at all but there is, at paragraph 8 of the opinion of Lord Hodge, an explanation of what legal interest is. Essentially it appears to be the position under Scottish law that essentially it was an interest rate of 5 per cent a year which was due as a matter of law in the absence of a contractual rate.

MR JUSTICE DAVID RICHARDS: Yes, I see.

MR SMITH: So, my Lord, that is relevant because in our submission the 5 per cent interest which was the subject of Gourlay v Watson was on analysis not a contractual rate, in the sense of a rate provided for under the contract but was interest allowed at law or legal

interest.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Now, my Lord, just looking at the decision itself, there's first of all a speech of Lord Young which your Lordship sees at the bottom of page 766. Just turning over to page 767, the final paragraph at the bottom of that page, he basically said, as your Lordship sees from the first sentence of that paragraph:

"The doctrine of appropriation of payment by a debtor making it in my opinion inapplicable."

Essentially his view was that because in that case the debt plus interest was a single and indivisable debt, there was no room for appropriation. His analysis was basically it was a single debt. That was the correct construction of the debt and because it was a single debt no question of appropriation arose.

He therefore had a slightly different analysis to the other two judges who approached it in a different way. The way they approached it is set out firstly in the speech of Lord Traynor which your Lordship sees at the bottom of the page, page 768. He says:

"First of all, I think the payments made to Watson & Co by Wilson's ...(reading to the words)... I would have agreed with the Lord Ordinary."

Then he says:

"The rule of law which applies is too well-established to have gone back on."

Then he says:

"My difficulty, however, has arisen on the view the trustee were not entitled ...(reading to the words)... creditors' interests and to the advantage of the debtors."

Then he says this:

"I agree with Lord Moncrieff, whose opinion I have read, that this case must be ...(reading to the words)... cannot appropriate those payments to any specific part of those claims."

So that's his approach and essentially he agrees with Lord Moncrieff and then elaborates on the point, as your Lordship sees at the bottom of page 769. He also begins by saying:

"This case must be treated as that of a trust for the distribution of an estate which was actually in all likelihood insolvent at the commencement of the trust."

Then he refers to the view of the Lord Ordinary, who considered there was an appropriation by the debtor.

Then he says this, and Mr Dicker may I think have taken your Lordship to this passage yesterday.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: He begins by saying:

"I do not think that is a correct view of the case. If a solvent debtor is desirous ...(reading to the words)... their being appropriated towards extinction of principal."

So he's basically saying there's no appropriation because at the time they're made there's no claim to interest or any contemplation of a claim to interest so almost by definition there can't be any appropriation.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: The he goes on to say:

"But if it transpires that there is a surplus sufficient to pay ...(reading to the words)... of his debts in terms of the law."

MR JUSTICE DAVID RICHARDS: The Bankruptcy Act 1856, is that a Scottish Act?

MR SMITH: That's the Scottish one I think we looked at in the footnote.

MR JUSTICE DAVID RICHARDS: Oh is it? Right.

MR SMITH: That's the one back in the footnote on page 765. So it's the Bankruptcy (Scotland) Act 1856.

MR JUSTICE DAVID RICHARDS: Thank you, yes.

MR SMITH: Your Lordship sees the terms of that.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Of course we make the point section 52 is not dissimilar to rule 2.88.

Your Lordship will see he also refers to Warrant Finance Company's case which is actually re Humber Ironworks, the first re Humber Ironworks decision of 1869.

MR JUSTICE DAVID RICHARDS: Right.

MR SMITH: My Lord, one other small point which might be worth making in relation to Gourlay v Watson. It obviously post-dates the 1883 Bankruptcy Act but there's no suggestion there that Bower v Marris had ceased to be part of the bankruptcy law of England following that Act. On the contrary, reference is made specifically to the analogy of the law of bankruptcy, both here and in England.

So, my Lord, that was the first additional case I wanted to show your Lordship.

There is a second one, also mentioned by Mr Dicker, which is the re Calgary Medicine Hat Land Company case, which your Lordship will find in the same authorities bundle, tab 58.

MR JUSTICE DAVID RICHARDS: Lord Traynor didn't think that Humber Ironworks had much to do with it. Still, there we are. They took different views. Sorry, the next one is ...?

MR SMITH: The next one is re Calgary Medicine Hat Land Company, which is another one Mr Dicker referred to.

It's at tab 58. It's a decision of the Court of Appeal in 1908. Basically it was a debenture case. It concerned a debenture holder's action. It probably makes sense for your Lordship just to read the headnote actually. It's a relatively short headnote which summarises the facts quite neatly. (Pause)

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Your Lordship sees it concerned a debenture. Essentially what had happened is that the Master had certified the sums in respect of principal but he hadn't certified anything in respect of interest, and payments had then been made accordingly pursuant to the Master's certification. There then was a surplus and the question was whether the payment which had been made previously had been appropriated to principal or not.

If your Lordship goes to page 656, your Lordship will see in the middle of the page the argument made by Mr Hughes KC for the debenture holders he said:

"These are merely payments on account generally. Ordinary payments on ...(reading to the words)... interest at the date of dividend and then in reduction of capital (see Bower v Marris)."

Then, my Lord, page 658, there's the judgment of the Master of the Rolls, where he sets out in the middle of the page:

"Counsel for the appellants, the company, the contend that the effect of the orders was ...(reading to the words)... no complete appropriation of the payments as between principal and interest."

Then he goes on to say:

"I cannot treat them as finally appropriating the dividends ...(reading to the words)... stated in the Master's certificate. That is all."

I don't think we need the judgment of Lord Justice Fletcher Moulton, but then one gets to the final judgment which is Lord Justice Farwell. If your Lordship goes to page 66 in the middle of the page. He says this:

"When the Master made his certificate it was believed by all the parties ...(reading to the words)... the only account taken accordingly was that of capital."

Then over on page 663 at the top of the page, he then went on to conclude:

"In the present case each order for payment was made as a step towards final distribution ...(reading to the words)... to that inherent right of adjustment which always exists in cases of this nature."

So, my Lord, that was obviously a slightly different factual scenario, but it's a similar principle in my submission. Where payments are made in a state of

insolvency, there's no question of those payments being appropriated to interest at that time. That essentially reinforces the point which was decided in Bower v Marris itself, but your Lordship sees how it's applied and has been applied in our submission fairly consistently across the different contexts.

Now, my Lord, one then comes to the question of what is the case of the administrators and Wentworth on how dividends in respect of proved debts are to be treated for the purposes of calculating post-administration interest?

Now, like Mr Dicker, we understand that the administrators proceed on the basis that payments are appropriated to principal when they're made. If your Lordship has their skeleton argument, which your Lordship should have in bundle 6, tab 4, paragraph 35 first of all. Your Lordship sees first of all in paragraph 35:

"Rule 2.88(7) is a clear" --

MR JUSTICE DAVID RICHARDS: Sorry, paragraph ...?

MR SMITH: 35.

MR JUSTICE DAVID RICHARDS: This is the administrators'?

MR SMITH: Yes, it should be tab 4 for your Lordship.

MR JUSTICE DAVID RICHARDS: Yes, it is. Thank you.

MR SMITH: First of all, paragraph 35:

"Rule 2.88(7) is a clear and mandatory direction as to how the surplus is to be applied. In circumstances where the debts proved have been paid, and a surplus remains ... the surplus must be applied in paying interest ..."

So it says there it applies where the debt has been proved to be paid. Similarly, paragraph 37(1), the first line:

"Rule 2.88(7) proceeds on the basis that the debt proved have already been paid ..."

Then one has paragraph 107, sub-paragraph 2, which is the paragraph Mr Dicker referred to where the point may be put slightly more clearly because that's where they say:

"When dividends are applied to pay the debts proved, the principal is discharged in part."

So at least, as we understand it, the administrators' case is that the dividend payments, when made, are appropriated to the proved debt.

Now, obviously the problem with that case is that it is directly contrary to Bower v Marris and not only Bower v Marris but the Court of Appeal cases in Humber Ironworks and Joint Stock Discount Company which held that the dividend payments are not appropriated to principal. So, my Lord, in our submission, that's

a short answer to that case.

It's also inconsistent with Wentworth's position.

MR JUSTICE DAVID RICHARDS: Sorry, just let me follow this. The second -- I have paragraph 35. I just didn't -- what was the other paragraph you referred to?

MR SMITH: There were two other paragraphs. It's paragraph 37(1) and then paragraph 107(2). It's probably clearest in paragraph 107(2).

MR JUSTICE DAVID RICHARDS: Let me just re-read that.

(Pause)

MR SMITH: At least, as we understand it --

MR JUSTICE DAVID RICHARDS: So, sorry, it's dangerous to take sub-paragraphs out of the overall context.

MR SMITH: It is.

MR JUSTICE DAVID RICHARDS: But paragraph 35 is clearly a submission based on the terms of rule 2.88.

MR SMITH: Exactly, yes.

MR JUSTICE DAVID RICHARDS: So the pre-existing law, or even if admissible as background is ultimately, Mr Trower would say, beside the point because it must give way to the proper construction of rule 2.88.

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: The same, I think, is true of 37(1), but just looking at it on its own -- well, I suppose the only thing, 107(2) is preceded of course

by 107(1), which again refers to rule 2.88.

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: I agree if you read 107(2) on its own, yes -- anyway.

MR SMITH: The point for present purposes is merely to identify what they say is the correct treatment of the dividend payments when one comes to calculate statutory interest.

MR JUSTICE DAVID RICHARDS: Yes. Exactly.

MR SMITH: As we understand it, it is their case in that context that they say they are effectively treated as having been appropriated to the proved debts or having discharged proved debts.

Now, the problem in our submission obviously with that case is it's directly contrary to Bower v Marris. It's also directly contrary to Humber Ironworks and the Joint Stock Discount Company because the point of principle which on any view we suggest one gets from those cases is that dividend payments are not treated as having been appropriated to principal when one comes to calculate statutory interest.

Now, the administrators' position is also inconsistent or different to Wentworth's position. As Mr Dicker said, Wentworth has changed its position. They had originally said in their reply position paper,

paragraph 13, that the dividend payments are appropriated to principal. I don't think we need to turn it up. They have changed their position since then.

The current position is set out in their reply skeleton, first of all, at paragraph 17 of their reply skeleton which your Lordship will see in bundle 6, tab 6. It's page 5 of their skeleton, where they summarise what they say is the principle which was applied in Bower v Marris. They say:

"... the principle which was applied in Bower v Marris is merely a negative one: that payments made pursuant to a statutory scheme such as distributions of a bankruptcy estate are not appropriated towards principal ..."

So we would not disagree with that.

Then they elaborate on that a little then in paragraph 25, in particular sub-paragraph 3 of paragraph 25, which your Lordship will find on page 8 of the skeleton.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Where they say this:

"The SCG is mistaken in asserting that Wentworth's argument is one that was rejected in Bower v Marris. The argument rejected in Bower v Marris was that the

payments of dividends did constitute an appropriation towards principal. Wentworth's case does not depend on showing that there has been any particular appropriation."

So they seem to accept the Bower v Marris principle and they say their case doesn't depend on any such appropriation, but it does then raise the question of what do they say is the correct treatment of dividend payments in the hands of the creditor when you come to calculate post-insolvency interest. The logic, we would suggest, of their position appears to be that when one comes to the time of calculating post-insolvency interest, one is approaching it on the footing at that time that the payments are to be treated as payments on account. They say they're not appropriated to principal; they don't say they're appropriated to interest. So it seems their position is that when one comes to the moment of calculating statutory interest, what has gone before is treated as being -- having been payments on account.

But, my Lord, if they accept that, then we suggest it's very difficult indeed to see what is the reason for not then applying the approach in Bower v Marris.

Now, if payments haven't been previously appropriated to principal, then it's not clear why one

wouldn't approach post-insolvency interest by calculating it in the usual way, by applying the usual rule that payments are treated as having been received in discharge of interest before principal. One is approaching statutory interest from the context that one has previous payments that are payments on account.

The normal rule would be to treat those payments as being discharged first in interest rather than principal. One asks oneself, against that context, why would the legislature want to impose a different approach and, in particular, an approach which prejudices the creditor?

Now, there's no suggestion that the legislation did intend to impose such a different approach. Indeed, in our submission, one would need to find something very clear in the rule which led one to that conclusion, because not only is one approaching the calculation of statutory interest against the footing that these are payments on account, that there is a usual rule that applies, but one is also approaching it against the context of the preceding authorities. Now, in our submission, there is nothing in the rule that one could find that the legislature intended the calculation of insolvency interest to be approached other than in the usual way.

Now, just to pick up a couple of points here, one of the points which Wentworth make is a sort of quid pro quo point, if I can put it like that. What they say is that there is a reason to think the legislature intended to have a different approach and that's because it effectively gave something new in the 1986 rules. It gave a right to interest to persons whose debts didn't previously bear interest and, therefore, because it gave something new, it's not necessary surprising that it took something away at the same time, namely the right to rely on the rule in Bower v Marris.

Now, there's two points we make in answer to that. The first is there's nothing to suggest that that was the intention of the legislation. It's a slightly odd intention to attribute to the legislature that it gives with one hand a creditor a right to interest. Presumably in the case of a creditor whose debt doesn't bear interest for the purpose of putting that creditor in the position he would have been in if he'd been able to obtain a judgment. But, at the same time, it's taking something away from that creditor as part of a quid pro quo. There's nothing to suggest that was the intention of the legislature.

MR JUSTICE DAVID RICHARDS: It wouldn't be taking anything

away from that creditor because that creditor didn't have anything.

MR SMITH: He didn't in the case of corporate insolvency.

MR JUSTICE DAVID RICHARDS: Correct.

MR SMITH: But one then comes to the second point which is how it applies to bankruptcy, where in that case obviously the creditor did have a right to get interest on non-interest-bearing debts. If we're right about the 1883 Act and the question of whether there was a fundamental change in the law in 1883, but assume we are right about the 1883 Act and the rule in Bower v Marris did continue to apply, then the effect is that that creditor was deprived of something.

MR JUSTICE DAVID RICHARDS: Yes, I see.

MR SMITH: Because in his case -- in fact he's not receiving anything new because he already has a right to interest, but he's having the rule in Bower v Marris taken away.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Now, that was the first point.

The second point I just wanted to address briefly at this point is the idea of the non-provable claim which is the notion, well, the legislature took away Bower v Marris in relation to rule 2.88 but the consequence of that is a creditor in effect has a non-provable claim to the extent required to vindicate

his contractual rights.

Now, there's three points we make about that is that stage. First, it's a very odd intention on the part of Parliament, we would suggest, to abolish the rule in Bower v Marris for statutory interest but instead then, at the same time, to insert a non-provable claim further down the waterfall. It's very difficult to identify any obvious policy reason for that or any reason of principle. That first point.

The second point is the effect of that would, at least potentially, be to prejudice creditors whose debts did not bear interest as a matter of contract.

Now, assume there's no Sempra Metals-type claim for damages for late payment. Those creditors would not appear to have a non-provable claim for the vindication of their rights. They have no contractual rights to vindicate. That, however, is in the context where obviously the reason for conferring interest on the right to interest on those creditors in the first place was to put them in the same place as they would have been in if they had a judgment. That's the -- one of the points I think your Lordship made in the first Waterfall decision at paragraph 163.

MR JUSTICE DAVID RICHARDS: I think, again, one shouldn't read too much into points like that. I think the point

I was making there is that is why judgment rate has been chosen.

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: It may extend from that the intention is to put them in the same position as they would be in if they had a judgment, but I don't think I was actually addressing that part of that.

MR SMITH: I think it may be worth your Lordship looking at it, rather than me misquoting it to your Lordship. It's bundle 1E, tab 167, paragraph 163, I think, at page 55 of the judgment.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: It's in the middle of the page, the relevant passage against letter D.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Your Lordship says:

"The justification for statutory interest, even in those cases where the debts do not already carry a right to interest, is that the creditors are prevented by the liquidation regime from obtaining a judgment against the company which would then carry interest at a judgment rate."

MR JUSTICE DAVID RICHARDS: I see.

MR SMITH: Now, my Lord, we obviously submit -- well, firstly, we respectfully agree with that.

Secondly, we would submit that off the back of that it's a somewhat odd intention for the legislature to confer a judgment rate on a creditor whose debt doesn't bear interest, presumably seeking to put him as far as possible in the position he would have been in if he had obtained a judgment but which he couldn't because of the winding-up. It's very odd that if that's the intention on the one part, but then, at the same time, to deprive the creditor of one of the normal rights he would have if he had obtained Judgments Act interest which would be the right to apply the rule in Bower v Marris.

So that's second point.

Indeed, it goes slightly further because on the non-provable claim analysis, not only is the right removed at the level of statutory interest but that creditor doesn't even have a non-provable claim to vindicate his rights.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: So, my Lord, we say that would be a very odd intention.

The third point is this, that in our submission it would actually involve a perverse intention on the part of the legislature. Obviously one of the main points of the Cork Report was to remove the anomaly in corporate insolvency between debts which bore interest and debts

which didn't. That's one of the main reasons of the report and obviously the changes made in consequence of the report did remove that anomaly in relation to statutory interest. So both of them are treated equally. But if the position is that Bower v Marris doesn't apply but there's a non-provable claim for creditors who have a contractual right to interest, then the effect of that is to re-insert exactly the same anomaly, just further down the waterfall. Because one's in the position then of having exactly the same anomaly at the level of non-provable claims, because on this analysis creditors with contractual interest would have a non-provable claim to vindicate those rights but creditors without a right to contractual interest wouldn't have any such claim.

So one has exactly the same anomaly which a legislature has just reversed at the level of statutory interest. So that does seem to us to be a rather unlikely and, indeed, perverse intention on the part of the legislature.

My Lord, the next topic I was going to deal with is the idea which is put forward by Wentworth that Bower v Marris is dependent on an appropriation being made to interest at the time the dividends are paid. One of the themes that's put forward by Wentworth is

actually Bower v Marris is no more than an application of the general rules of appropriation and in effect all that is happening under the Bower v Marris approach is that a creditor is appropriating dividend payments to interest when those payments are made.

One sees that in their first skeleton argument, bundle 6, tab 2, paragraphs 49 to 50. Your Lordship sees they say first of all in paragraph 49:

"... the ... 'rule' is no more than an application of the general rule applicable between solvent parties that enables the creditor, entitled to receive both principal and interest, to appropriate payments made to it in discharge of interest before principal."

Then on the back of that, they say, in paragraph 50:

"... the application of principal to the calculation of interest payable from an insolvency surplus depends upon the fact that the relevant legislation preserved the underlying right of a creditor with an interest-bearing debt to be paid in full ..."

Then related to that, if your Lordship just go goes back a few pages, and sorry to move your Lordship around the document, but at paragraph 29, they say this:

"... the operation of the principle of appropriation in Bower v Marris depends on there being an accrued right to interest at the time of the payment of the

dividend."

MR JUSTICE DAVID RICHARDS: Is that not a different point? This is the point that Mr Dicker touched on. You married them up, I see.

MR SMITH: I understand that they're related.

MR JUSTICE DAVID RICHARDS: I see. So the so-called principle is just the general rule.

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: But the general rule can't apply because there is no accrued right to interest; is that the point?

MR SMITH: That's what they say is the position under the 1986 Act and rules, yes. As I understand it, what they basically say is that Bower v Marris -- the conceptual approach in Bower v Marris is it works on the idea that the creditor appropriates to interest at the time the dividend payment is received. They say that can't --

MR JUSTICE DAVID RICHARDS: Or thereafter? It doesn't have to do it at the time. It can treat it as a payment on account so that the creditor is free at any time thereafter to appropriate it, as I understood it.

MR SMITH: Well, I'm not sure because they --

MR JUSTICE DAVID RICHARDS: The appropriation really can't take place until there's a surplus.

MR SMITH: Well, but this is why it seems to me one has to

see it in the context of paragraph 29 because they set out -- your Lordship is right, they set out the general principle in paragraphs 49 and 50, but then it's linked in paragraph 29 to the idea that there is an accrued right to interest at the time of the payment of the dividend.

MR JUSTICE DAVID RICHARDS: Depends on there being, yes.

MR SMITH: Depends on there being.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: So they said:

"... the operation of the principle of appropriation in Bower v Marris depends on there being an accrued right to interest at the time of the payment of the dividend."

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Now, what it seems to me what they're in effect saying is that the Bower v Marris approach works on the basis that at the time the dividend payment is made there are accrued rights in respect of both principal and interest and the dividend payment as at that time is effectively appropriated by the creditor to interest.

MR JUSTICE DAVID RICHARDS: Not necessarily -- I don't read it as being at that time.

MR SMITH: Well, at the very least there has to be an accrued right to interest at the time of payment.

MR JUSTICE DAVID RICHARDS: That's right. Yes, that I understand.

MR SMITH: It may be that's the limitation, but certainly at the very least they say there has to be an accrued right to interest at the time the dividend payment is made. That, they say, is the foundation for the rule and, as I understand it, they then seek to distinguish that position with what they says the position under the 1986 Act.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Now, in my submission that isn't the correct analysis. The rule has never depended on the existence of an accrued right to interest at the time of the dividend payment. That isn't position either under the present statutory scheme or under the statutory scheme as it existed at the time of the decision in Bower v Marris.

Now, my Lord, in our submission the correct analysis is as follows: firstly, under the statutory scheme the creditor has a right to post-insolvency interest in the event of a surplus. That is a right which is conferred by the statute. It is a right to payment from the estate administered by the office holder in accordance with the statutory scheme. So that's first point, the nature of the right.

The second point is that at the time dividend payments are made, the creditor only has a contingent right to such interest under the statutory scheme. He only becomes entitled to receive payment of the interest and he only has an accrued right to such interest when the contingency is satisfied. So, in other words, where there's a surplus after paying 100p in the pound on the proved debts.

That's a point which was made quite neatly by Mr Justice Buckley in a case called WW Duncan which your Lordship will find at tab 55, bundle 1B. If your Lordship -- I don't think we need the facts of the case. I just want to pick up one particular statement by Mr Justice Buckley at page 315. In the middle of the page, he's talking about what you admit to proof for dividend in the winding-up of a company. He says:

"It's the amount of the debt at the commencement of the winding-up. That has nothing whatever to do with the payment of interest accruing due after the winding-up. If the company turns out to be solvent, there could not until the fact of the solvency was ascertained be right to claim that interest."

So, my Lord, the position we suggest is that under the statutory scheme actually as it exists now, as it existed also then, is that at the time the dividend

payments are made the creditor doesn't have an accrued right to interest. At most he has a contingent right to interest but ultimately whether that right accrues depends whether or not there's a surplus. My Lord --

MR JUSTICE DAVID RICHARDS: He must here be talking about contractual interest because at this time, 1905, there clearly wasn't, was there, any entitlement to interest if you didn't have a right to it, apart from the liquidation.

MR SMITH: You didn't, but -- you certainly didn't have a right to interest from the estate unless you had a contractual right, that's true, but the right to interest from the estate only arose in the event of a surplus.

MR JUSTICE DAVID RICHARDS: That's true, as it were, as part of the liquidation process. As a matter of legal right, interest was accruing, you just weren't entitled to payment of it.

MR SMITH: Yes, but the question for these purposes, which is what is the correct right to interest, in our submission the right to interest is one that's conferred by the statutory scheme.

MR JUSTICE DAVID RICHARDS: I mean, I think that as I understand the point which is being made, which you're now addressing, if you go back to cases like

Bower v Marris, they're all -- well, apart from Lord Cottenham -- Bower v Marris is a difficult -- is in one sense a special case, but in general these are cases where there is a contractual right to interest. Bower v Marris is a case actually concerned with contractual interest.

MR SMITH: It is.

MR JUSTICE DAVID RICHARDS: I mean, as a general proposition if on 1 March the debtor pays £1,000 and on 1 March only principal is payable, there is no outstanding interest, well, there can't be an appropriation to interest because there is no interest outstanding.

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: So as a general proposition, applying these rules to a contractual position, the proposition that there must be interest accrued at the date of payment is right, isn't it?

MR SMITH: In terms for there to be an appropriation?

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Yes, indeed.

MR JUSTICE DAVID RICHARDS: I think that is the point. I have to hear Mr Zacaroli but it may be he's not making any bigger point than that.

MR SMITH: As I understand the point that's made -- the point that's essentially made is to say that the

rationale -- the juridical basis of Bower v Marris is that it turns on the doctrine of appropriation and essentially in order for the doctrine of appropriation to apply, you need both accrued rights to principal and interest at the time the dividend is paid.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: What he basically says is, "Well, how it works is that the dividend payment is treated as being appropriated to the accrued right in respect of interest". Now, in my submission that's the point I'm addressing. And in my submission that's not basis of the rule, because so far as the right to interest is concerned, that's a right to interest which arises under the statutory scheme.

MR JUSTICE DAVID RICHARDS: Are you talking here about contractual interest or interest which doesn't arise, save under the statutory scheme?

MR SMITH: I'm talking about both. I'll come shortly to section 132 of the 1925 Act, but certainly what we say in relation to that is that the right to interest is a statutory right.

MR JUSTICE DAVID RICHARDS: Sorry? The 1825 Act, yes.

MR SMITH: Yes. My Lord, I will also come after that to Humber Ironworks because one of the things one needs to look at quite closely in the case of Humber Ironworks is

how actually the Companies Act worked at that time and how the right to interest out of the assets worked.
MR JUSTICE DAVID RICHARDS: Okay.
MR SMITH: My Lord, certainly our submission is that it's not based on an accrued right to interest because the relevant right is the right that arises under the statutory scheme. That right only accrues due where there is a surplus.
MR JUSTICE DAVID RICHARDS: Can I just put it this way, just so you can deal with it: if we start using this language of debtors and creditors appropriating payments to certain debts and so on, this is going into -- going out of insolvency, just into the general position about payments from debtors to creditors; that was the Privy Council case that Mr Dicker took me to this morning, and so on. So that's all operating in an area where, on the date of payment by the debtor, there are two elements to the debt which are then payable.
MR SMITH: Yes, correct.
MR JUSTICE DAVID RICHARDS: Now, insofar as the judges in the Bower v Marris type of cases used that approach, they are, it may be said, assuming that at the date of payment there are accrued rights to payment of principal and interest. If there aren't, then the judges are going much further than that. They're actually creating

a new doctrine that doesn't depend upon simply an application of appropriation in the ordinary course and so on.
MR SMITH: Yes.
MR JUSTICE DAVID RICHARDS: I mean, that's not a reason why it's not good law, but it's no -- it is carrying the doctrine quite a lot further.
MR SMITH: I see the distinction and obviously your Lordship, I think, starts from the proposition that in Bower v Marris, I think Lord Cottenham said in terms that this is nothing to do with the doctrine of appropriation.
MR JUSTICE DAVID RICHARDS: Well, I need to look closely at what he said.
MR SMITH: It's very important, and that point is then picked up in two or three of the other cases, where they say it's nothing to do with doctrine of appropriation.
My Lord the reason I suggest it's nothing to do with doctrine of appropriation is that the statutory right to interest isn't a right that's accrued at the time the payment is made.
MR JUSTICE DAVID RICHARDS: No.
MR SMITH: That's why it's distinct. So, my Lord, it's not an example of the application of the normal rules of appropriation.

MR JUSTICE DAVID RICHARDS: Sorry, I have Bower v Marris here. Let's just have a look at that very point, if we may, in Bower v Marris. I think page 335.
MR SMITH: Yes exactly. So the passage I obviously had in mind is the bottom of page 355.
MR JUSTICE DAVID RICHARDS: Yes.
MR SMITH: Where he says this:
"As this mode of payment is regulated by Acts of Parliament ...(reading to the words)... cannot have any place in the consideration of the present question."
So, my Lord, what he seems to be saying there is it's not a question of the doctrine of appropriation because that turns on the intention of the debtor or creditor, rather it's a question of how the Act applies. Then, ultimately, he deals with it on that basis.
I think we have put together, probably in the skeleton argument, the other various dicta one gets where they say throughout the succeeding cases it's nothing to do with the doctrine of appropriation.
MR JUSTICE DAVID RICHARDS: Well, okay. I see. So if that's right, then obviously whether or not it's accrued due for payment at the relevant date is really neither here nor there.
MR SMITH: Yes. It's a very similar -- it's very similar, I would suggest, to the approach your Lordship saw in

Gourlay v Watson actually because what they say there is the payments are made pursuant to principal at a time when there's no conception there's going to be any interest payable. How it works is that those payments are not appropriated. There can't be any question of appropriation because no interest has yet accrued due, but what does happen is where you then get a surplus which arises, the creditor is entitled then to treat payments as having been applied first in interest, rather than in discharge of principal.
So, my Lord, that's in our submission how it works.
MR JUSTICE DAVID RICHARDS: Right. Thank you.
MR SMITH: My Lord, that analysis, we suggest, applies equally in the context of the statutory scheme under the 86 Act and the 86 rules as it did to the 1825 Bankruptcy Act, and as it did to all other statutory schemes. Contrary to Wentworth's analysis, the rule isn't dependent on the debtor having accrued rights in respect of both principal and interest at the time the dividend payments were made.
My Lord, I'm not sure what time your Lordship --
MR JUSTICE DAVID RICHARDS: If it's a convenient moment, I'll rise. We'll have a five-minute break now.
(3.10 pm)
(Short break)

(3.15 pm)
MR SMITH: My Lord, I am going to deal next very briefly with section 132 of the 1825 Act --
MR JUSTICE DAVID RICHARDS: Yes.
MR SMITH: -- which your Lordship will find in bundle 3A, tab 10. Obviously your Lordship will have well in mind the 1825 Act established the familiar sort of statutory scheme for bankruptcy, creditors are entitled to proof for the debts and demands which they had contracted for when the commission was issued.
So far as section 132 itself is concerned, I think Mr Dicker has already pointed out to you the similar language to rule 2.88. It provides that interest is payable after the creditors who have proved under the commission have been paid. So it's looking at the position after payment of their proved debts. Once that happened, the bankrupt was entitled to recover the surplus, but that was subject to the assignees first paying post-bankruptcy interest.
That's obviously relevant to the point the administrators make, that the difference with rule 2.88 is it contains a mandatory direction to apply for the surplus. But, in our submission, in substance, that was exactly the position also under section 132.
Then, my Lord, also section 132 provides for the

payment of interest upon their debts. Your Lordship sees that in the middle of the passage. So, again, like rule 2.88(7), it provides specifically for the payment of interest on accrued debts.
MR JUSTICE DAVID RICHARDS: Yes.
MR SMITH: Now, my Lord, so far as the treatment of those debts are concerned, they obviously fell into two categories. The first category was where there was a rate of interest reserved or by law payable on the debt.
MR JUSTICE DAVID RICHARDS: Yes.
MR SMITH: Then essentially the second category, which was ranked lower in priority, was all other debts.
Rate of interest probably doesn't require any explanation. "By law payable thereon" appears to have been intended to capture the position where a creditor had a debt which wasn't -- which was payable on demand but where the instrument did not provide for interest. The legal position at the time being appears to be that when that creditor brought an action on the debt he would be entitled as a matter of law to interest at a rate of 5 per cent from the date of the demand. I am not going to take your Lordship to it, but for your Lordship's note that's explained in a case called re East of England Banking Company which is in tab 26 of

the authorities. It's Lord Cairns at page 18 and Sir William Page Wood at page 19 of that report.
MR JUSTICE DAVID RICHARDS: Right.
MR SMITH: My Lord, there's some significance to that because it means that the first category of interest under section 132 was not limited to a purely contractual rate, in the sense of a rate bargained for under the contract. It also extended to the rate which could have been awarded by a court at an action of law in relation to a debt which was repayable on demand.
MR JUSTICE DAVID RICHARDS: Yes.
MR SMITH: So, my Lord, the first category does go, we would suggest, somewhat broader than pure contractual interest.
The second category of interest -- sorry, the second category of claims on which interest bore plainly did extend to cases where the creditor had no contractual entitlement to interest; that was the whole purpose of that category.
Now, Wentworth say directly that that second category wasn't at issue in Bower v Marris itself directly, which was true, but the implication of their argument seems to be that there would have been a different approach in relation to the first category of interest versus the second category, where I think on

their case they say Bower v Marris applies to the first category but wouldn't apply, they would say, to the second category. I'm not sure what their position would be in relation to debts which bore the 5 per cent interest at law within the first category. But, my Lord, it would be very odd, we would say, if there had been that difference in treatment and, as Mr Dicker pointed out yesterday, Bower v Marris did not distinguish -- the Lord Chancellor in Bower v Marris did not distinguish between the two categories of debt in his judgment. He did not seem to think there was any real distinction.
Now, my Lord, just on section 132, obviously it was part of the statutory scheme which we say was essentially the same as the scheme which is in place today under the current Act. Statutory rights to interest arose under that scheme where there was a surplus. So in the same way as under the current Act, once there was a surplus there was a statutory right to interest. Those rights were statutory rights in our submission. One way to test that is to think how a creditor might have pleaded an action if the assignees had failed to make payment of interest. In our submission what the creditor would have been doing is claiming against the assignee, relying on his statutory

right under section 132.

Now, at the time any dividend payments were made, entitlement to interest pursuant to such rights was purely contingent. It was dependent on there being a subsequent surplus. My Lord, consistent with the statutory nature of the rights, as I pointed out to your Lordship, they plainly encompassed a right to interest which went beyond that, provided for in the contract itself, and in my submission one sees that in relation to both categories of right.

So, my Lord, in our submission, looking at the way section 132 worked, looking at the rights which were conferred under 132, it's inconsistent with the way Wentworth seeks to analyse the decision in Bower v Marris as being based on this idea of doctrine of appropriation and based on the idea of remission to contractual rights. In our submission that's not how it works.

My Lord, I'm not going to go back to the decision in Bower v Marris itself. Obviously subsequent case law has applied Bower v Marris. There's three main points we would emphasise to your Lordship which are really all relevant to the question of whether these authorities bear on the position under rule 2.88.

The first is clearly a number of those cases have

been concerned with interest other than as provided for under the terms of the contract. There are cases where the rule applies where the relevant obligation to pay interest arises because of a judgment rate, for example rather than merely a contractual rate. So, for example, where a creditor has obtained a judgment debt.

Mr Dicker, I think, showed your Lordship the Supreme Court of New South Wales decision in Tahore.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: But, importantly, the second category, there are also cases where the rules applicable to the administration of the relevant estate itself gave rise to an entitlement to statutory interest. So, in other words, a number of the cases where the rule has been applied are where the debt did not otherwise itself bear interest but the right to interest was in effect conferred by the statutory scheme.

My Lord, those cases, which we would suggest on analysis would include Bower v Marris, make the idea that Bower v Marris is founded on the concept of remission to contractual rights rather difficult to maintain.

Now, Mr Dicker, I think, showed your Lordship a number of examples. One other example he didn't show your Lordship is Mr Justice Chitty in

Whittingstall v Grover, which is in tab 43 of the first authorities bundle. Again, I'm afraid it's a slightly complicated and unusual set of facts. It's probably --

MR JUSTICE DAVID RICHARDS: Sorry, where?

MR SMITH: Tab 43, my Lord.

MR JUSTICE DAVID RICHARDS: Sorry, I have got out the wrong bundle.

MR SMITH: Bundle 1A.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Your Lordship sees it begins in the right-hand column, the headnote. My Lord, essentially what it was concerned with was the administration of an estate of a deceased partner in a banking business. Your Lordship sees from the headnote:

"For many years prior to 1856 A carried on a banking ...(reading to the words)... for the administration of the estate of A."

So it was a relatively complex situation where one had a testamentary estate on the one hand and a bankrupt estate on the other. The questions really related to the manner in which the testamentary estate was to be administered.

One of the main questions related to the position of separate creditors vis-a-vis joint creditors, in particular their priority in the estate of A.

Your Lordship sees that's dealt with really in the second and third paragraph of the headnote.

Then in the fourth paragraph, it said this:

"The result of the actions to administer the estate of A ...(reading to the words)... ascertaining the amount of the interest due."

It's obviously that last point which is of particular interest to us.

Then, my Lord, the two holdings:

"Held firstly, that the question of interest should be decided in accordance with the established rule as to the principal and as a consequence the separate creditors are entitled to take their interest in priority to the joint creditors."

Then this:

"Also that the dividends received ought to be accounted for ...(reading to the words)... to the reduction of the principal."

So, again, one sees the language of ordinary payments on account and then applying dividends first in payment of the interest calculated and then in reduction of the principal.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Now, so far as the judgment of Mr Justice Chitty is concerned, one can probably pick it up, I think, at

page 217, which is the last page of the report, where he begins in the second sentence at the top of the page:

"The next question which arises relates to interest ..."

MR JUSTICE DAVID RICHARDS: So that's on page ...?

MR SMITH: Page 217, the last page of the report.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Column 1, the left-hand column.

MR JUSTICE DAVID RICHARDS: The left-hand column.

MR SMITH: It begins the second sentence:

"The next question which arises relates to interest ..."

MR JUSTICE DAVID RICHARDS: I see.

MR SMITH: Having dealt with a rather complicated question about separate and joint debts, he now moves on to the interest point.

MR JUSTICE DAVID RICHARDS: Right.

MR SMITH: He says:

"After payment of 20 shillings in the pound to the joint and separate creditors ...(reading to the words)... the testate for separate creditors ..."

Then this point is important:

"... whose debts did not by law or special contract carry interest."

So he's dealing, amongst other things, with

creditors whose claims did not carry interest.

Then he goes on to refer to decision in ex parte Reeve, and a decision in ex parte Findlay.

Then he says:

"As between the separate creditors of the testator whose debt ...(reading to the words)... who do not by law carry interest on the other hand."

So there's a question of priority between the joint creditors and the separate creditors who didn't have interest as a matter of law.

Then he sets out the relevant arguments, just in the middle of that page, as to the contentions of the two creditors. Then if your Lordship picks it up, my Lord will just see in the middle of the page, left-hand column, he says:

"The orders of 1841 relating to interest were in substance repeated in the consolidated orders of 1861 and are now embodied" --

MR JUSTICE DAVID RICHARDS: I am sorry, I've lost you again.

MR SMITH: It's just in the middle of the page.

MR JUSTICE DAVID RICHARDS: In the left-hand column?

MR SMITH: Yes. Your Lordship will see, about halfway down, the sentence beginning, "The orders of 1841 ..."

NEW SPEAKER: Yes, I have it.

MR SMITH: I was picking it up there:

"The orders of 1841 relating to interest are in substance repeated in the consolidated orders of 1861 and are now embodied in the subsisting rules of court, order 55, rules 62 and 63."

My Lord, it makes it worth just having a look at those because it's helpful in understanding what the case decided. Your Lordship will wish to leave Whittingstall v Grover open. The rules themselves are in bundle 3D, tab 57. Your Lordship sees the relevant rules are rules 62 and 63. Firstly, rule 62:

"Where a judgment award is made directly ...(reading to the words)... from the date of judgment or order."

Then 63:

"A creditor whose debts do not carry interest ...(reading to the words)... as by law carry judgment."

So it's essentially providing for two things. Firstly, a contractual right to interest would be recovered, but, in addition, the creditor of the debt didn't carry interest and is entitled to recover that, subject to establishing his debt.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: So, my Lord, essentially it covered both non-contractual -- contractual and non-contractual interest.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: I've shown your Lordship it's clear from the report that Mr Justice Chitty was considering both.

Now, moving back to the report, page 217, the right-hand column, where he gets to on the question of priority is about halfway down, two-thirds of the way down. He says this:

"The sound rule therefore appears to me to be that as between the joint and separate creditors the question of interest should be decided in accordance with established rules to principal."

Then this is the important part for our purposes:

"The remaining question relates to the manner in which the dividends received ought to be accounted for in ascertaining the amount of interest due. All the dividends have been paid in process of law and the account ought to be taken in the manner pointed out in Bower v Marris and the Warrant Finance Company's case by treating the dividends as ordinary payments on account and applying each dividend in the first place to the payment of interest calculated to the day of such dividend and the surplus, if any, to the reduction in principal."

So, my Lord, that again is clearly an example of the application of the Bower v Marris principle. It was concerned not only with contractual interest but also

with the right to interest arising under statutory rules. It was also concerned as per rule 63 with a situation where interest was only payable where assets remained after satisfying the debts established.

So in many ways it was rather similar scheme to rule 2.88. It also, obviously, post-dates the 1883 Act.

Mr Dicker has also pointed to perhaps another passage I should draw your Lordship's attention to which is just slightly further up in page 217, the right-hand column. It's immediately preceding the bit I showed your Lordship. You can see a sentence:

"Nor can I find any reason which in regard to subsequent interest ...(reading to the words)... which appears on the face of the general orders themselves."

So that emphasises the point that he was clearly dealing both with contractual interest and also interest which arose as a matter of law under rule 63.

So, my Lord, that, we suggest, is a good example of the approach of treating the dividend payments as payments on account. It's an example where one is looking not merely at contractual interest and it's an example where one is looking at a right to interest which arises where there is a surplus.

Now, my Lord, that's the first category of cases.

The second category of cases is there are a large

number of cases which concern payment of interest out of a surplus after payment order discharge of the principal debts. That's the scheme which your Lordship will see in a number of these cases. It the position in Bower v Marris itself. Whittingstall v Grover is that sort of case. Gourlay v Watson was that sort of case as well, and Mr Dicker has also shown you, I think, the two Canadian cases and the Irish case. So, my Lord, again one sees in effect the same submission arising in Bower v Marris being applied in relation to those cases.

Now, my Lord, the final category of cases I just want to refer to are the company liquidation cases, such as Humber Ironworks in particular.

MR JUSTICE DAVID RICHARDS: Hmm, hmm.

MR SMITH: I think one of the points that's sort of made is that actually the position at the time of Humber Ironworks was there wasn't a statutory provision dealing with the payment of interest from the insolvency surplus as such and, therefore, it was entirely a question of remission to the contractual rights.

Now, in my submission that's not accurate. One has to start with the 1863 Companies Act which was the Act which was in force at the time of Humber Ironworks, which your Lordship will see in bundle 3A, tab 18.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: For these purposes I think we can probably just start with section 98 which your Lordship hopefully has on the first page of the tab.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: Your Lordship sees that that provided that as soon as may be after making an order for the winding-up of a company, the court should settle a list of contributories and then:

"... should cause the assets of the company to be collected and applied in discharge of its liabilities."

Now, that obviously on its face just refers to the liabilities of the company generally. It's not -- the statute itself didn't provide for a cut-off date. There was, in addition, to section 98, rule 26 of the order of November 1862 which your Lordship will see at the back of that tab.

MR JUSTICE DAVID RICHARDS: Sorry, where is that?

MR SMITH: It's the order of court, rule 26.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: I think Mr Dicker showed you. It's the rule, part of which was declared ultra vires, but your Lordship sees that that in effect informs or supplemented section 98 because it said what could be recovered and essentially it was interest on such dates as claimed --

MR JUSTICE DAVID RICHARDS: My eye has been caught, although I don't think it's in point, by rule 2.1.

MR SMITH: Rule 2.1?

MR JUSTICE DAVID RICHARDS: Yes. I hadn't previously seen legislation referring to Lincoln's Inn Hall. It's a very proper addition.

MR SMITH: I remember noticing that, yes. No, quite.

MR JUSTICE DAVID RICHARDS: Anyway, sorry.

MR SMITH: Back to rule 26. Obviously that in effect informed what could be recovered from the assets of the company pursuant to section 98 and it provided in the part that wasn't held to be ultra vires that the rate the debts carried could be recovered.

Now, just going back to section 98 for a moment. Section 98 obviously on its face allowed all the liabilities of the company to be paid out of the assets. What it didn't do on the face of the statute was to impose a cut-off date. Now, how that obviously subsequently worked is there was a judge-made rule developed in Humber Ironworks which in my submission effectively superimposed on top of section 98 and essentially qualified the position by holding that a creditor was to prove in the first instance for principal and interest at the date of the winding-up and only claim after that date if there was a surplus. So,

as we analyse it, that in effect is judge-made rule that superimposed on top of section 98.

Obviously once there was a surplus, that judge-made rule would cease to apply. The position then was the creditor was in effect back to his rule -- his position -- his right under section 98. So in effect once the judge-made rule had ceased to operate because there was a surplus, the creditor was then entitled to recover his post-insolvency interest pursuant to section 98.

Now, my Lord, in those submissions -- in those circumstances what we submit is the right to post-insolvency interest was in essence a statutory right. It was a right that arose under section 98. Moreover, it was a right that only arose where there was a surplus. That's the effect of the judge-made rule in Humber Ironworks. The extent of the right was delineated by statute. Moreover, my Lord, looking at the position under section 98 in light of Humber Ironworks, there was no accrued right to interest pursuant to section 98 at the time the dividend payments were made. The accrued right to interest only arose once there was a surplus and once the judge-made restriction on claiming under section 98 was lifted.

So, my Lord, as we see it, it's not really accurate

to say there's no statutory provision for interest at the time of Humber Ironworks. The position obviously not spelt out on the face of the statute in the way it is now, but, as a matter of concept, what the creditor was doing was exercising a right to claim under the statute which only arose once there was a surplus in this case.

My Lord, what the creditor wasn't doing was enforcing a contractual course of action against the company. Rather, what he had was a right to payment from the liquidation state administered by the liquidator. And in modern terminology in effect his right was a right conferred by the statutory scheme for payment from the estate held by the liquidator on the statutory trusts.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: So, my Lord, when one sees the reference to "remission to the contractual rights" and similar terms in the speech of Lord Justice Giffard, in particular, we suggest some care needs to be taken about taking those too literally. Actually when one drills down and analyses the nature of the rights, we suggest actually it's little different from the right which exists under 2.88.

MR JUSTICE DAVID RICHARDS: Well, 2.88 insofar -- well, but

it is only if you're entitled to interest by contract.

MR SMITH: It is. So there's that difference, but in terms of the basic shape and outline of the right, we say it's a right conferred by statute, it's a right that only arises where there is a surplus, and it's a right the extent of which is delineated by the statute itself.

MR JUSTICE DAVID RICHARDS: I can see that you can say there is conferred a statutory right to participate in a distribution of the estate --

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: -- in respect of post-liquidation contractual interest --

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: Which would suggest that that would rank ahead of non-provable claims.

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: I'm not sure it goes beyond that.

MR SMITH: Well, it does in the sense it's also a right that only arises where there is a surplus, because that's the effect of the judge-made rule in Humber Ironworks. What that rule does is effectively say you're limited until there is a surplus to claiming your principal and accrued interest to the date of the winding-up. Once there is a surplus, that limitation is lifted and you

then have your full right under section 98.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: So, my Lord, we do submit that actually it's essentially statutory. My Lord, that was the position under the 1862 Act. It appears to have remained essentially the same under the 1948 Act and the 1949 rules which were in place at the time of re Lines Brothers. The only differences we can see is that section 98 became replaced by section 257 of the 1948 Act and rule 26 was replaced by rule 100 of the 1949 rules.

MR JUSTICE DAVID RICHARDS: The section was section 2 ...?

MR SMITH: It became section 257 and rule 26 became rule 100 of the 1949 rules.

MR JUSTICE DAVID RICHARDS: Thank you.

MR SMITH: So, my Lord, that's what I wanted to say about the cases.

My Lord, a very short point on the 1883 Act. I think Mr Dicker mentioned there were a couple of textbooks.

MR JUSTICE DAVID RICHARDS: Yes.

MR SMITH: I should just show your Lordship briefly, they're both in the second authorities bundle. The first is at tab 12. I'm sorry, we don't seem to have the frontispiece in the bundle. It is actually a textbook

by someone called Robson. It's called a Treatise on the Law of Bankruptcy. This is its seventh edition and it was 1894.
MR JUSTICE DAVID RICHARDS: It would be quite helpful to have that.
MR SMITH: I will get that, my Lord.
The relevant passage is at page 201.
MR JUSTICE DAVID RICHARDS: Sorry, this is tab ...?
MR SMITH: I am sorry, 291. My apologies.
MR JUSTICE DAVID RICHARDS: Yes.
MR SMITH: Your Lordship sees he's dealing here with section 40. The relevant bit is in footnote G at the bottom of page 291. It begins right at the bottom of the left-hand column. He says:
"As to the mode of calculating interest under the old law, where there was a surplus (see Bower v Marris overruling re Higginbottom)."
Then he also refers to Whittingstall v Grover.
Now, we rely on that because we suggest that what that is indicating is that the Bower v Marris approach continued to apply. I think Wentworth say, well, the fact he referred to the old law means he was drawing a point of distinction. We would suggest that's not really the tenor of what he's saying here and really, looking at that, what he is more likely saying is the

same approach continued to apply.
That's one textbook.
The other textbook is tab 16 in the same bundle, where we do have the frontispiece. It's a textbook by a gentleman called Henry Wace. Your Lordship sees over the page -- sorry, this is dated 1904 so slightly later and, again, after the 1883 Act.
MR JUSTICE DAVID RICHARDS: Yes.
MR SMITH: Your Lordship sees, over the page, the very last paragraph of the commentary, before he gets on to section 41, he says:
"It is conceived that the interest is to be computed as running interest, treating the dividends as ordinary payments on account and applying each dividend in the first place to the payment of the interest which would have been due at the date of the dividend if there had been no bankruptcy, and the surplus only, if any, in reduction of the principal; Bromley v Goodere, ex parte Morris and Bower v Marris, disapproving re Higginbottom."
So that's another textbook post the 1883 Act which we say seems to suggest Bower v Marris remains good law, which also chimes with Whittingstall v Grover and the Scots case, Gourlay v Watson, which seems to have proceeded on the same basis.

My Lord, those are just two references from the textbook.
So far as the construction --
MR JUSTICE DAVID RICHARDS: Was Williams on Bankruptcy in its various editions silent on the point?
MR SMITH: Williams on Bankruptcy I don't think says anything on this point.
MR JUSTICE DAVID RICHARDS: No.
MR SMITH: I think that's true in any of its editions actually.
MR JUSTICE DAVID RICHARDS: Right.
MR SMITH: So these are the only ones we were able to find.
MR JUSTICE DAVID RICHARDS: Yes.
MR SMITH: My Lord, turning then to the 1986 Act. Obviously our primary submission is the wording at face value doesn't exclude the operation of the rules at all. Mr Dicker has dealt with that. There's one point we would just like to emphasise in response to the suggestion, I think made in particular by the joint administrators, that the Act and the rules are a code. That's a suggestion, I think, appears particularly in the joint administrators' skeleton. We would respectfully submit the Act and rules are not a code. There's a large number of examples of equitable principles operating alongside the statute.

If I can invite your Lordship just to take bundle 1E. There's a good example in the decision of the Supreme Court in the Mills v HSBC case which your Lordship will find at tab 156A of volume 1E. Your Lordship sees, I think, paragraph 1 of the judgment of Lord Walker. This decision itself concerned the rule in Cherry v Boultbee.
All I'm relying on it for is the general description your Lordship finds in paragraph 1 of the judgment. You'll see Lord Walker describes in the first sentence:
"The appeal is concerned with the long-standing principle of insolvency law, known as the rule against double proof."
Then he goes on to make the point, one sentence on:
"Like the anti-deprivation rule recently considered by the ...(reading to the words)... implicit in the Insolvency Act 1986."
So there are a number of examples of quite important rules, such as the rule against double proof, such as the anti-deprivation rule, which one doesn't find necessarily articulated in express words on the face of the statute but nevertheless exist as part of the insolvency scheme.
There's one other good example of that which your Lordship will find in Stein v Blake which is in

authorities bundle 1C, tab 120.

The example Lord Hoffmann gives is against the letter D on page 253. He is dealing here with the operation of the insolvency set-off rules in bankruptcy. The point he makes here is that, well, if you look at the wording of the statute, any creditor of the bankrupt proving or claiming to prove for a bankruptcy debt, you might think, not perhaps unfairly, that the operation of the section actually depended on the lodging of a proof, but, as per the established principles and the case law, that's not the case, and, notwithstanding that wording, the way the words are construed is to mean any creditor who would have been entitled to poof for a bankruptcy debt.

So, my Lord, in those two ways the Insolvency Act isn't a code. There are equitable principles which exist alongside it and which, if necessary, qualify the wording of both the Act and the rules.

My Lord, I'm not going to repeat what Mr Dicker said about the construction of the rules. We gratefully adopt what he said about that.

In our submission there is nothing in the rule itself which excludes the operation of Bower v Marris, both as a matter of looking at the rules in isolation but also particularly when one looks at the very similar

provisions in the other cases where the rules have been held to apply.

My Lord, there is then a point -- a separate point and a practical point in relation to the position of co-obligors and how the various arguments work where one is dealing with co-obligor situation.

The facts of Bower v Marris itself obviously concerned co-obligors. The point which the Lord Chancellor made in that case is why should the rights of the creditor against the solvent co-obligor be diminished by payments from the insolvent co-obligor being treated as having been appropriated to principal. Obviously what he had in mind there was the principle of the co-extensive liability between the joint and several creditors.

Now, that was obviously a powerful point in favour of the Lord Chancellor reaching the conclusion which he did in Bower v Marris. In our submission that continued -- that point continues to create a very significant difficulty for any argument based on dividend payments being appropriated in respect of approved debt because on that argument one runs into exactly the same problem in relation to the position of a co-obligor --

MR JUSTICE DAVID RICHARDS: You could say, couldn't you,

when you're dealing with the position of co-obligors, then that calls for a different approach?

MR SMITH: Well --

MR JUSTICE DAVID RICHARDS: You're not bound by sort of insolvency principles. I mean, I'm thinking, for example, you can prove in the estates of two co-obligors for the full amount of your claim.

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: You don't have to give credit for distributions in one or the other.

MR SMITH: Yes.

MR JUSTICE DAVID RICHARDS: Which would, on one view, seem to run contrary to --

MR SMITH: But there's two points in relation to that. Obviously what one is concerned with there is treating in effect a payment which is received by the creditor so it's not -- it's not quite the same as the creditor is simply asserting a right. One is looking for these purposes at what is the effect of the payment the creditor receives. If he's required to treat that as being appropriated to the principal in the case of the insolvent co-obligor, it is a little difficult to see, pursuant to the principle of co-extensiveness, how one has a different position if he's a solvent co-obligor.

MR JUSTICE DAVID RICHARDS: So if we were to take not

actually the Bower v Marris case of a contractual right to interest but -- no, sorry. No, sorry, I think I was going to give a bad example.

MR SMITH: My Lord, on that point we suggest really the same point which the Lord Chancellor made in Bower v Marris continues to hold good and is a serious practical obstacle to any argument based on dividend payments being appropriated in respect of the proved debt.

So far as we can see, similar difficulties would arise on Wentworth's complete code argument because in that case, as we understand it, the calculation of statutory interest on the basis that dividend payments are treated as having been appropriated to principal first and then there would in effect be a complete discharge of the insolvent co-obligor vis-a-vis the creditor. That, as I understand it, is their complete code point.

Again, it's very difficult to see how that wouldn't also work vis-a-vis the solvent co-obligor. If it's right that the insolvent co-obligor has been discharged pursuant to the complete code, why isn't the same true to the solvent co-obligor? So one has the same difficulty.

Indeed, it also seems that exactly the same difficulty arises on the third argument which is simply

the calculation without the complete code because there, again, one is in a situation where the creditor is receiving from the insolvent co-obligor a payment which has been calculated on the footing of appropriation, dividend payments to principal prior to interest. Again, it's very difficult to see why that wouldn't apply equally vis-a-vis the solvent co-obligor.

So, whichever way one looks at it, the point essentially is the Lord Chancellor's point in Bower v Marris continues to hold good and is a powerful reason as to why the arguments put forward on the other side must be wrong.

So, my Lord, that's the co-obligor's point.

The only final point I just wanted to make relates to issue 3 and, in particular, the concession made by the administrators and Wentworth in respect of issue 3. That concession is that the reference to the rate applicable in rule 2.88(9) encompasses compound interest. So that's essentially the concession which has been made.

Now, there's two points of substance which arise from this. Firstly, the concession necessarily means that Wentworth and the administrators accept that the surplus can be used not only to pay interest on the proved debts but also interest on interest. That is

what compound interest is. So by conceding one can have compound interest, that necessarily means they also accept that the wording in 2.88(7) allows the surplus to be used to pay matters other than the proved debt. Essentially in this instance it's allowed to be used to pay interest on interest.

Now, that, we suggest, directly undermines one of the main points they make in relation to rule 2.88(7) which is that there's no room of the operation of the rule in Bower v Marris because that rule by the notional re-allocation involves using the surplus to ultimately discharge a sum of notional principal which is left outstanding once one has re-allocated the dividend payments in discharge of prior interest, but exactly the same point arises in relation to compound interest. It's no bar, obviously, to the availability of compounding under rule 2.88.

So, my Lord, that's the first point.

The second point is really to ask oneself what is the logic which underpins this concession? What's the reason it's being made? If one goes back to the joint administrators' skeleton argument at paragraph 115, which is in bundle 6, tab 4, your Lordship sees what is said there in 115:

"... the word 'rate' is apt to include every factor

that determines the total amount of money that is payable by way of interest for a particular period of time, including the numerical percentage and the way in which that numerical percentage is to be applied ..."

Now, my Lord, we agree with that. That is the reason why one is allowed compound interest, but, obviously, that reasoning applies equally to the rule in Bower v Marris. The rule in Bower v Marris is another method or mode of applying a particular interest rate.

Now, the way Mr Trower sought to deal with this yesterday was to say, well, actually compound interest all goes to the computation of the rate. If your Lordship has the transcript of yesterday --

MR JUSTICE DAVID RICHARDS: Hmm, hmm.

MR SMITH: -- it's page 15, my Lord. He just touched on this point when he was opening to your Lordship. It's page 4 of the document, page 15 in the top right corner.

MR JUSTICE DAVID RICHARDS: Is this page 15 -- yes.

MR SMITH: So page 15 of the Min-U-Script transcript.

MR JUSTICE DAVID RICHARDS: Yes, thank you.

MR SMITH: He said this, beginning at line 5:

"I just want to say this: for the avoidance of any doubt we don't accept -- it won't surprise your Lordship to hear -- that the fact that compounding is appropriate when calculating the rate for the purposes of

rule 2.88(9) has any effect on the rule in Bower v Marris. They are two quite different questions. Compounding is available as a matter of construction of rule 2.88(9) [and then this] because it is a factor which goes to the computation of the rate that is permitted by rule 2.88 and properly falls within the words."

In our submission that's not how compounding works. Compounding has nothing to do with the computation of the rate or the change of the rate. The rate of interest actually remains the same but what does change is how that rate is applied and, in particular, the amount on which the interest rate is charged. Specifically compound interest you apply the same rate but on an ever-increasing mass comprising the original principal and accrued but unpaid principal.

So that isn't an explanation which deals with the concession. In my submission the original logic in the skeleton argument, which gave the reasons for the concession, is the correct logic, that one has to look at rate as not being merely the numerical rate but also the applicable mode of applying that rate. That equally applies to Bower v Marris, as it does to compounding.

My Lord, I don't think we were under any misapprehension as to what the administrators were

saying, but there is, in my submission, a possible misconception on their side as to how compound interest works.

My Lord, unless I can assist you any further, that's what we were proposing to say.

MR JUSTICE DAVID RICHARDS: Thank you very much indeed, Mr Smith.

MR SMITH: Thank you.

MR JUSTICE DAVID RICHARDS: So, Mr Zacaroli, will you be the next to address me? It's a matter for you. If you want to poison my mind for five minutes, by all means.

MR ZACAROLI: My overview will take more than five minutes.

MR JUSTICE DAVID RICHARDS: To poison my mind.

MR ZACAROLI: I wouldn't dream of it anyway.

MR JUSTICE DAVID RICHARDS: Good. All right. Thank you very much. I'll just assemble one or two things here. 10.30 tomorrow morning.

(4.12 pm)

(The court adjourned until Friday, 20 February 2015 at 10.30 am)

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