IN THE COURT OF APPEAL, CIVIL DIVISION
ON APPEAL FROM

Nos 7924 and 7945 of 2008 and No 429 of 2009

THE HIGH COURT OF JUSTICE
CHANCERY DIVISION
COMPANIES COURT
MR JUSTICE DAVID RICHARDS
IN THE MATTER OF LEHMAN BROTHERS INTERNATIONAL (EUROPE) (IN ADMINISTRATION) and others
AND IN THE MATTER OF THE INSOLVENCY ACT 1986
B E T W E E N:

(1) THE JOINT ADMINISTRATORS OF LEHMAN BROTHERS INTERNATIONAL (EUROPE) (IN ADMINISTRATION)
(2) THE JOINT ADMINISTRATORS OF LEHMAN BROTHERS LIMITED (IN ADMINISTRATION)
(3) THE JOINT ADMINISTRATORS OF LB HOLDINGS INTERMEDIATE 2 LIMITED (IN ADMINISTRATION)

Applicants

and

(1) LEHMAN BROTHERS HOLDINGS, INC
(2) LYDIAN OVERSEAS PARTNERS MASTER FUND LIMITED

Respondents

REPLACEMENT OUTLINE SUBMISSIONS OF LEHMAN BROTHERS HOLDINGS, INC

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1. LBHI appeals against paragraphs (i), (ii), (iii), (v), (vi), (viii), (ix) and (x) of the order of Mr Justice David Richards. LBHI adopts the submissions of LBHI2 and makes the further submissions set out below.

Paragraph (v): non-provable non-statutory interest ([127][1])

2. The Judge held that, in a winding up immediately following an administration, creditors with interest-bearing debts are entitled to claim interest for the period of the administration as a non-provable liability.

3. The premise of the Judge's reasoning was that, where there is a surplus, creditors are remitted to their contractual rights.

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[1] Unless otherwise stated, sections and rules referred to in this skeleton argument are those in the Insolvency Act 1986 (the **Act**) and the Insolvency Rules 1986 (the **Rules**) respectively; and paragraphs in square brackets refer to paragraphs in the judgment below.

4. The premise is false. It is inconsistent with the statutory scheme which comes into effect upon winding up. The effect of that scheme is that the company's liabilities are ascertained at the date of the winding up and its property is divided among creditors pro rata according to the value of their claims at that date, as determined in accordance with the Rules. As a result, creditors' rights are not necessarily the same as their original contractual rights: *Re Dynamics Corporation of America* [1976] 1 WLR 757, 761G-H **[JA/1B/55]**; *Re Lines Bros Ltd*, unreported, 18 April 1981 at 25-26 **[JA/1B/56**]; [1983] 1 Ch 1, 26E-F **[JA/1B/57]**; *Re Danka Business Systems plc* [2013] Ch 506 at [32], [37] **[JA/1C/91]**.

5. This can be illustrated by reference to a future debt, contingent debt, currency claim and interest claim. For example, suppose:

   (1) A company owes a creditor a debt of £1,000, which falls due for payment 20 years after the company went into liquidation. In accordance with r 4.94 (r 2.105 in administration), the amount of the admitted proof for the purpose of dividend is £1,000/1.05^{20} = £376.89. If dividends are paid on the date that the company goes into liquidation, and the company is able to pay all the debts proved, the creditor receives £376.89, not £1,000.

   (2) A company owes a creditor a debt of £1,000, which is payable 20 years after the company went into liquidation in the event that a remote contingency takes place. In accordance with r 4.86 (r 2.81 in administration), the liquidator estimates the likelihood that the contingency will occur at 10%. He therefore estimates the value of the debt at 10% x £1,000 = £100, which he discounts for accelerated receipt (at, say, 5% pa), giving £100/1.05^{20} = £37.69. The proof is admitted for that amount. If dividends are paid on the date that the company goes into liquidation, and the company is able to pay all the debts proved, the creditor receives £37.69, not £1,000.

   (3) A company owes a creditor a debt of $1,000, which is equivalent to £500 when converted in accordance with r 4.91 (r 2.86 in administration). Suppose that £500 is equivalent to $1,100 when converted on the date of payment. If the company is able to pay all

the debts proved, the creditor receives $1,100, not $1,000.

(4) A company owes a creditor a non-interest bearing debt, or a debt which bears interest at a rate which is lower than the rate specified in s 17 of the Judgments Act 1838 (the **Judgment Rate**). If there is a sufficient surplus remaining after payment of the debts proved, the creditor receives interest on the debt at the Judgment Rate, rather than at the lower rate (if any) applicable to the debt apart from the winding up (s 189(2), (4), r 2.88(6), (7), (9)).

6. The Judge relied on *Re Humber Ironworks & Shipbuilding Co* (1869) LR 4 Ch App 643 **[JA1A/12]** as authority for the proposition that, where there is a surplus in a winding up, a creditor is remitted to his contractual right to interest. The Judge quoted was said by Giffard LJ, namely that, as soon as it is ascertained that there is a surplus, *"the creditor whose debt carries interest is remitted to his rights under his contract"* ([127]).

7. *Re Humber Ironworks* was decided before there was a statutory entitlement to interest. The decision is no longer good law. The words of Gifffard LJ following those quoted by the Judge were "*and on the other hand, a creditor who has not stipulated for interest does not get it."* (647). The position under the Act is different - if there is a sufficient surplus after payment of the proved debts, a creditor who has not stipulated for interest does get it; and a creditor who has stipulated for interest at a rate lower than the Judgment Rate, gets it at the Judgment Rate. As the Judge rightly held, the contractual right to interest is replaced by a statutory right to receive interest out of any surplus (**Statutory Interest**) ([86], [154]). For this reason, a creditor is not remitted to his contractual right to interest.

8. The legislative history is instructive. Section 66(1) of the Bankruptcy Act 1914 **[JA/3/14]** provided as follows:

> *"Where a debt has been proved, and the debt includes interest, or any pecuniary consideration in lieu of interest, such interest or consideration shall, for the purposes of dividend, be calculated at a rate not exceeding five per centum per annum, without prejudice to the right of a creditor to receive out of the estate any higher rate of interest to which he may be entitled after all the debts proved in the*

estate have been paid in full."

9. Section 23 of the Bankruptcy Act 1890 **[JA/3/13]** was in similar terms; and these provisions were applicable in winding up[2]. Section 9 of the Moneylenders Act 1927 **[JA/3/15]** also provided that a moneylender reverted to his contractual right to interest after all the debts proved had been paid in full.[3] Thus, for nearly a century until the passing of the Act, the legislation had expressly provided that a creditor reverted to his contractual right to pre-bankruptcy interest after all the debts proved had been paid in full.

10. The fact that the provisions in the Act and the Rules relating to interest do not, in contrast to their predecessors, provide that a creditor reverts to his contractual right to interest after all the debts proved have been paid in full supports the view that the contractual right is replaced in administration or winding up by the statutory right to interest.

11. Furthermore, the effect of section 33(8) of the Bankruptcy Act 1914[4] **[JA/3/14]** was that creditors were not remitted to their contractual rights with respect to post-bankruptcy interest[5]. Having regard to the fact that the 1986 Act was intended to create a single unified system relating to interest in winding up and bankruptcy, creditors are likewise not remitted to their contractual rights with respect to post-winding up interest.

12. If an unpaid contractual liability to pay interest did survive the insolvency process, a bankrupt would not be released from such a liability upon his

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[2] *Re Theo Garvin Ltd* [1969] 1 Ch 624, 656A **[JA/1A/49]**.

[3] *"Where a debt due to a moneylender in respect of a loan made by him after the commencement of this Act includes interest, that interest shall, for the purposes of the provisions of the Bankruptcy Act, 1914, relating to the presentation of a bankruptcy petition, voting at meetings, compositions and schemes of arrangement, and dividend, be calculated at a rate not exceeding five per cent. per annum, but nothing in the foregoing provision shall prejudice the right of the creditor to receive out of the estate, after all the debts proved in the estate have be paid in full, any higher rate of interest to which he may be entitled…"*

[4] *"If there is any surplus after payment of the foregoing debts, it shall be applied in payment of interest from the date of the receiving order at the rate of four pounds per centum per annum on all debts provided in the bankruptcy."* See also Schedule 2, rule 18: *"… a creditor shall in no case receive more than twenty shillings in the pound and interest as provided by this Act."*

[5] *Re Howes* [1934] 1 Ch 49 **[JA/1A/40]**; *Re Baughan* [1947] 1 Ch 313 **[JA/1A/43]**.

discharge[6]. He would be liable to be adjudged bankrupt for a second time on the petition of a creditor in the first bankruptcy who had not been paid contractual interest in full. Contractual interest would continue to accrue in the second bankruptcy, and the bankrupt would be exposed to further bankruptcies based on unpaid contractual interest. This would undermine one of the main aims of the bankruptcy regime, namely to enable the bankrupt to be freed from debts, contracts, liabilities, engagements and contingencies of every kind.[7]

Paragraph (vi): extent of member's liability under s 74(1) ([150]-[178])

13. The debts and liabilities referred to in s 74(1) do not include Statutory Interest, for 3 reasons.

14. First, the words "debts and liabilities" in s 74(1) cannot be read literally, so as to refer to all the company's debts and liabilities. This is because, in a winding up, there are debts and liabilities which the company is not obliged to pay, and the reference to "payment" in s 74(1) makes it clear that a member is not required to contribute an amount in respect of a debt or liability which the company is not obliged to pay. Such debts and liabilities include the discounted element of future and contingent debts; secured liabilities where the creditor has not given up his security and proved[8]; and non-enforceable debts, such as those which are statute-barred; *Re Art Reproduction Co Ltd* [1952] Ch 89) **[JA/1A/44]**.

15. Furthermore, if "debts and liabilities" included those to which the company became liable in the winding up, there would be no need to refer in s 74(1) to the expenses of the winding up.

16. The company's assets are applied in discharge of its liabilities at the date of the winding up order (*Re General Rolling Stock* (1872) LR 7 Ch App 646) **[JA/1A/15]**; the contribution to the company's assets to an amount sufficient

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[6] Interest in respect of the period after the commencement of the bankruptcy is not a bankruptcy debt and the bankrupt is not therefore released therefrom: ss 281(1) **[JA/3/20]**, 382(1)(d) **[JA/3/20]**; *Muir Hunter on Personal Insolvency* Vol 1, para 3-2698 **[JA/2/2]**; [156].

[7] *Ex p Llynvi Coal and Iron Co In re Hide* (1871) LR 7 Ch App 28, 32 per James LJ **[JA/1A/14]**,.

[8] The position of secured creditors is governed by rr 4.88 and 4.95-4.99 **[JA/3/21]**.

for the payment of its debts and liabilities is therefore limited to its liabilities at the date of the winding up order.

17. Secondly, the natural meaning of s 189(1) **[JA/3/20]** and r 2.88(7) **[JA/3/21]** is that Statutory Interest is payable *to the extent* that there is a surplus remaining after the payment of the debts proved (**Surplus**), such that the company has no liability to pay Statutory Interest independently of a Surplus. It is for this reason that the liability to contribute to the assets does not extend to creating a Surplus without which no Statutory Interest is payable.

18. The creation of Statutory Interest followed a recommendation in the Report of the Review Committee on Insolvency Law and Practice Cmnd 8558, 1982 (the **Cork Report**), at para 1395(c) **[JA/4/9]**. The Cork Report gives no support to the view that Statutory Interest is payable where there is no Surplus. It is doubtful that Parliament intended to create a liability which will be not be paid in full in all but rare cases where there are sufficient assets to pay interest at 8% pa or more on all proved debts (cf *Re Toshoku Finance UK plc* [2002] 3 All ER 961 at [30], per Lord Hoffmann) **[JA/1C/74]**.

19. The description of statutory interest in *Re Lines Bros Ltd* [1984] BCLC 215 at 223e is apposite **[JA/1B/59]**. The provision which created statutory interest in that case was s 33(8) of the Bankruptcy Act 1914 **[JA/3/14]**, which provided that "*If there is any surplus after payment of the foregoing debts, it shall be applied in payment of interest from the date of the receiving order at the rate of four pounds per centum per annum on all debts proved in the bankruptcy*." This is similar in structure to r 2.88(7) **[JA/3/21]**. Mervyn Davies J said that statutory interest cannot be regarded as a debt or liability of the company because the liquidator's obligation to pay interest out of a surplus is pursuant to a statutory direction to him, being an obligation which is part of the statutory scheme for dealing with a company's assets which comes into operation on the outset of the winding up.

20. Thirdly, if s 189(2) **[JA/3/20]** imposes a liability on a company to pay Statutory Interest independently of the Surplus, the equivalent provision in bankruptcy would impose a like liability on a bankrupt to pay such interest

(**Bankruptcy Interest**)[9]. The bankrupt would not be released from this liability upon his discharge[10]. He would be liable to be adjudged bankrupt again on the petition of any creditor in the first bankruptcy, save where Bankruptcy Interest had been paid in full. Bankruptcy Interest would continue to accrue, and the bankrupt would be exposed to further bankruptcies based on unpaid Bankruptcy Interest. This would undermine the policy of bankruptcy law.

21. The Judge gave 2 reasons for finding that Statutory Interest is a liability for the purpose of s 74(1) ([164]) **[JA/3/20]**. The first was that s 189(2) was not intended to have the effect that what was previously a liability of the company should cease to be so for the purposes of s 74(1). However, the right to receive Statutory Interest from the Surplus exists where the company had no previous liability to pay interest. So the fact that there may have been a previous contractual liability to pay interest (possibly at a different rate to that at which Statutory Interest is payable) is no guide to whether Statutory Interest is a liability within s 74(1). The second reason was that s 74(1) extends to making calls for the payment of non-provable liabilities, ranking behind Statutory Interest, so calls can be made in order to fund the payment of Statutory Interest. This assumes that Statutory Interest is a liability within s 74(1); that Statutory Interest is payable where there is no Surplus; and that the debts and liabilities referred to in s 74(1) include non-provable liabilities and those to which the company becomes liable in the winding up.

Paragraph (viii): proof by LBIE, acting by its administrators, in a distributing administration or liquidation of LBL or LBHI2 in respect of those companies' liabilities under s 74(1) ([195]-[226])

22. The opening words of s 74(1) are *"When a company is wound up"*. For this reason, s 74(1) has no application unless and until the company is wound up.[11] The provisions relating to the liability to contribute under s 74(1) (the

[9] Section 328(4): *"Any surplus remaining after the payment of the debts that are preferential or rank equally under subsection (3) shall be applied in paying interest on those debts in respect of the periods during which they have been outstanding since the commencement of the bankruptcy."* **[JA/3/20]**

[10] See footnote 4 above.

[11] *Financial Corporation Ltd v Lawrence* (1869) LR 4 CP 731, 737-738 **[JA/1A/13]**; *Re China*

Statutory Liability) are also expressly limited to the winding up.[12]

23. The Judge said that *"the obligation of contributories under section 74(1) arises only in a liquidation"*. He also said, in explaining why the contributory rule applies only in winding up, that it is a rule dictated by the nature and the purpose *"of the obligation imposed on contributories by the legislation in a winding up"* ([167], [170], [182]). The Judge was right; and it is because the obligation to contribute arises only in a liquidation that the Statutory Liability is provable only when the company is wound up.

24. This analysis is reinforced by a consideration of the features of the regime under which the Statutory Liability is imposed; the consequences if the Statutory Liability is provable before the company is wound up; and whether it is fair and sensible to treat the Statutory Liability as provable before the company is wound up (cf *Re Nortel GmbH* [2014] AC 209 at [58]-[63], [77], [86]) **[JA/1C/96]**.

<u>The Statutory Liability cannot be dealt with before the company is wound up</u>

25. It is well established that the moneys paid in respect of a Statutory Liability to meet a call:

    (1) are payable only on a winding up of the company;

    (2) are never under the control of the directors of the company and cannot be charged, disposed of or in any way dealt with by them;

    (3) are not part of the capital of the company;

    (4) form a statutory fund which only comes into existence when the company is wound up;

Steamship Company, ex p Mackenzie (1869) LR 7 Eq 240 242-243 **[JA/1A/10]**; *Whittaker v Kershaw* (1890) 45 Ch D 320, 326 **[JA/1A/25]**; *Re H L Bolton Engineering Co Ltd* [1956] Ch 577, 582 **[JA/1A/47]**; *Mace Builders (Glasgow) Ltd v Lunn* [1987] Ch 191, 199; **[JA/1B/60]** *Re Shoe Lace Ltd* [1993] BCC 609, 622D **[JA/1B/63]**; *Re Esal (Commodities) Ltd* [1997] 1 BCLC 705, 716d **[JA/1B/64]**.

[12] See, eg, ss 148(1) (settling a list of contributories); 149(1) (ordering a contributory to pay); 150(1) (making calls); 160(1)(b), (d), 165(2), (4)(a), (b) **[JA/3/20]**; rr 4.195-4.205 (delegation of court's powers in relation to calls to the liquidator) **[JA/3/21]**; Sch 4, para 3 (compromising calls) **[JA/3/20]**.

(5) may be called for only by the liquidator to meet the special demands of the fund.[13]

26. In each of these respects, the Statutory Liability is to be contrasted with the member's contractual liability to pay unpaid capital (the **Contractual Liability**). Furthermore, the Statutory Liability is (expressly) a liability to contribute to the assets of the company; the Contractual Liability is (expressly) a debt owed to the company.[14]

27. The administrator of a company has no greater power to deal with the moneys paid in respect of the Statutory Liability than its directors. The Judge reasoned that if a company may prove for a call before it is in administration, so may a company in administration ([206]). *Re Pyle Works* **[JA/1A/24]** shows that the premise is false. It also explains why the liquidator is empowered to settle a list of contributories and to make, enforce and compromise calls under s 74(1), whereas the administrator is not.[15]

Sale or assignment

28. The distinctions drawn in *Re Pyle Works* are reflected and reinforced in recent cases. *Re Ayala Holdings Ltd (No 2)* [1996] 1 BCLC 467 **[JA/1B/62]** concerned the effectiveness of an assignment by the liquidator of the right to assert that dispositions of the company's property after the commencement of the winding up were void under s 127 and that charges on the company's property were void under s 395 of the Companies Act 1985. Knox J distinguished between property of the company, which includes rights of action against third parties vested in a company at the commencement of the winding up; and the rights and powers of a liquidator. The former can be

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[13] *Re Paraguassu Steam Tramroad Company, Black & Co's Case* (1872) LR 8 Ch 254, 262 **[JA/1A/16]**; *Re Whitehouse & Co* (1878) 9 Ch D 595, 599-600 **[JA/1A/18]**; *Re West of England and South Wales District Bank, ex p Branwhite* (1879) 40 LT 652, 653 **[JA/1A/19]**; *Re Pyle Works* (1889) 44 Ch D 524, 574, 582, 584 **[JA/1A/24]**; *Re Mayfair Property Company* [1898] 2 Ch 28, 35-36 **[JA/1A/28]**.

[14] Section 16 of the Companies Act 1862 (the predecessor of s 33 of the Companies Act 2006) provides *"all monies payable by any member to the company … shall be deemed to be a debt due from such member to the company"*. **[JA/3/9]**

[15] The administrator does have the power to call up any unpaid capital: Sch 1, para 19. **[JA/3/20]** The Contractual Liability is provable in the liquidation of the member whether or not the company is in winding up.

sold or assigned, whereas the latter cannot, because they are an incident of the office of liquidator. The right to moneys paid in respect of a Statutory Liability is of the latter kind.

29. A similar distinction was drawn in *Re Oasis Merchandising Ltd* [1998] 1 Ch 170, 181-182 **[JA/1B/67]**. The Court of Appeal held that a liquidator has no power to assign the fruits of an action for wrongful trading and said that it would be very surprising if an administrator was empowered to sell the fruits of a future wrongful trading action by the liquidator. The same is true of the fruits of a future call in respect of the Statutory Liability.

Charge

30. Moneys paid in respect of the Statutory Liability cannot be charged by the company. If they were, they would be payable to the chargee upon enforcement, rather than to the statutory fund administered by the liquidator for unsecured creditors as a whole.

31. The moneys are in the same position as the fruits of a preference or fraudulent trading action, which are received by the liquidator impressed in his hands with a trust for those creditors amongst whom he has to distribute the assets of the company.[16]

Compromise

32. The company is unable, before it is wound up, to compromise its future Statutory Liability. If it were, a full and final settlement by the company would render a subsequently appointed liquidator unable to make a call on the member in respect of the Statutory Liability.

33. The liquidator is given the power to compromise all calls and liabilities to calls, and take any security for the discharge of any such call or liability and give a complete discharge in respect of it (Sch 4, para 3) **[JA/3/20]**. The administrator has no such power.

Dealing in the course of the member's business

[16] *Re William C Leitch Brothers Ltd (No 2)* [1933] 1 Ch 261 **[JA/1A/39]**; *Re Yagerphone Ltd* [1935] Ch 392 **[JA/1A/41]**; *Re Oasis Merchandising Ltd* [1998] 1 Ch 170, 181G-182A **[JA/1B/67]**.

34. The functions of the liquidator are to secure that the assets of the company are got in, realised and distributed to the company's creditors and, if there is a surplus, to the persons entitled to it (s 143(1) **[JA/3/20]**). This includes making and getting in any calls in respect of the Statutory Liability. This is not a function of the directors.

35. The amount of the Statutory Liability is that which is sufficient for the payment of the company's debts and liabilities and the expenses of the winding up and for the adjustment of the rights of the contributories amongst themselves (the **Adjustment**). If these moneys were payable to the company before it was wound up, the company could dispose of them without restriction. The company might not use the moneys to discharge its current debts and liabilities; and there would be no possibility of applying them in payment of the expenses of the winding up or the Adjustment. A company of doubtful solvency could remedy its financial position by receiving such moneys, thereby avoiding the only situation in which a call may be made (ie winding up) and the purpose for which the Statutory Liability is imposed (ie to contribute to the statutory fund).

Release of Statutory Liability upon discharge of the contributory's bankruptcy

36. If, before the company is wound up, the Statutory Liability was provable in the winding up of a corporate member, it would also be provable in the bankruptcy of an individual member. It would follow that the bankrupt was released from the Statutory Liability upon discharge from bankruptcy (ss 281(1), 382(1)) **[JA/3/20]**. Such a result would be a "monstrous injustice".[17] The injustice is avoided, as the Judge accepted, because s 82(4)[18] applies

[17] *Martin's Patent Anchor Co Ltd v Morton* (1868) LR 3 QB 306, 311. **[JA/1A/8]**

[18] *"The following applies if a contributory becomes bankrupt, either before or after he has been placed on the list of contributories … There may be proved against the bankrupt's estate the estimated value of his liability to future calls as well as calls already made."*

Sections 80 and 82(4) **[JA/3/20]** are derived from s 75 of the Companies Act 1862 (**Section 75**), which provides: *"The liability of any person to contribute to the assets of a company under this Act, in the event of the same being wound up, shall be deemed to create a debt (in England and Ireland of the nature of a specialty) accruing due from such person at the time when his liability commenced, but payable at the time or respective times when calls are made as hereinafter mentioned for enforcing such liability; and it shall be lawful in the case of the bankruptcy of any contributory to prove against his estate the estimated value of his liability to future calls, as well as calls already made."*

only when the company is wound up and the bankruptcy is pending ([224]-[225]).

37. Section 80[19] also applies only when a company is wound up[20]. For this reason, the Judge was wrong to rely on *Re Vaughan, ex p Canwell* (1864) 4 De G, J & S 539 **[JA/1A/3]** and *Williams v Harding* (1866) LR 1 HL 9 ([142]-[143], [196], [215]) **[JA/1A/4]**. These cases were decisions on whether a petitioner's debt was "contracted" after the passing of the Bankruptcy Act 1861 within the meaning of s 90 of that Act. They establish that the Statutory Liability has its inception at the date of, and originates with, the contract of membership; but it does not follow that the Statutory Liability is provable in the bankruptcy (*Re General Estate's Company, Hastie's Case* (1869) LR 4 Ch App 274, 278) **[JA/1A/11]** or the winding up of a member.

An analogy: s 127(1)

38. Suppose that a winding up petition is presented against a company **C**; that C then makes a disposition of its property to company **D**; and that D (but not C) is wound up by the court. C cannot prove in D's winding up in respect of D's possible future liability to C under s 127(1)[21]. This is because s 127(1) (as with s 74(1)) has no application unless and until C is wound up, and the obligation by reason of which D may become subject to a liability does not arise until C is wound up.

When Section 75 was enacted, the right of proof in a bankruptcy did not generally extend to contingent liabilities. Section 75 was a deeming provision which widened the circumstances in which contingent liabilities could be proved, by allowing a proof in the estate of a bankrupt contributory for the estimated value of the bankrupt's liability to future calls (*Re McMahon* [1900] 1 Ch 173).

[19] *"The liability of a contributory creates a debt (in England and Wales in the nature of an ordinary contract debt) accruing due from him at the time when his liability commenced, but payable at the time when calls are made for enforcing the liability."*

[20] *Financial Corporation Ltd v Lawrence* (1869) LR 4 CP 731, 737-738 **[JA/1A/13]** (*"The clauses in part 4 of the Companies Act, 1862, speak only from the commencement of the winding up of a company. When they begin to speak, no doubt for some purposes they have a retro-active effect")*; *Re China Steamship Company, ex p Mackenzie* (1869) LR 7 Eq 240, 246 (*"when a call is made it has reference back"*) **[JA/1A/10]**; *Whittaker v Kershaw* (1890) 45 Ch D 320, 326 **[JA/1A/25]**.

[21] *"In a winding up by the court, any disposition of the company's property, made after the commencement of the winding up is, unless the court otherwise orders, void."*

Protections and qualifications available to contributories

39. The scheme which imposes the Statutory Liability provides protections and qualifications for the benefit of contributories. If the Judge is correct, a contributory of a company which is not in winding up will be subject to the burden of the Statutory Liability without these protections and qualifications.

Settling the list; making calls

40. The liquidator has the power to settle the list and to make calls (ss 148(1), 165(4)(a), (b) **[JA/3/20]**, r 4.202 **[JA/3/21]**). The directors and administrator do not. The provisions relating to settling the list and making calls provide protections for contributories, but only in a winding up (rr 4.196; 4.198, 4.199; 4.202, 4.203) **[JA/3/21]**.

41. If the power to prove in respect of a Statutory Liability were exercisable by a director or administrator of the company, these provisions would be bypassed (cf *Re Ayala Holdings (No 2) Ltd* [1996] 1 BCLC 467, 483) **[JA/1B/62]**.

Adjustment of the rights of contributories amongst themselves

42. The court and the liquidator have the power to adjust the rights of the contributories (ss 154; 165(5)) **[JA/3/20]**. The directors and administrator do not.

43. If the Judge is correct, a member of a company (which is not in winding up) which has paid a sum in respect of its Statutory Liability does not have the benefit of the Adjustment[22]. The Judge said that this could be reflected in the estimate of the member's contingent liability for the purposes of proof ([218], [223]); but there is no mechanism for doing so, nor is there any mechanism for ascertaining how much the company would be able to recover from other contributories if it entered winding up at some (indeterminate) future date and/or if other contributories entered winding up at some (indeterminate) future date(s).

[22] The Adjustment takes account of the different amounts which contributories have paid to the company (*Re Shields Marine Insurance Association, Lee and Moor's Case* (1868) LR 5 Eq 368, 372) **[JA/1A/9]**.

Qualification of the Statutory Liability in s 74(2)

44. The Statutory Liability is subject to the qualifications set out in s 74(2) **[JA/3/20]**. These qualifications do not apply unless the company is in winding up.

45. Section 74(2)(a) provides that a past member is not liable to contribute if he ceased to be a member for one year or more before the commencement of the winding up. Consider the following example of an unlimited company **C** and sometime member **M** of the company:

2011:	M enters winding up; C proves in M's winding up in respect of M's Statutory Liability
2012:	M ceases to be a member of C
1 Feb 2014:	Commencement of C's winding up

46. If the Judge is right, C is entitled to prove in M's winding up in respect of M's Statutory Liability. This is inconsistent with s 74(2)(a), the effect of which is that M has no liability to contribute because it ceased to be a member of C one year or more before the commencement of C's winding up.

47. Section 74(2)(c) provides that a past member is not liable to contribute unless it appears to the court that the existing members are unable to satisfy the contributions required to be made by them.

48. Section 74(2)(c) cannot operate unless the court is able to form a view as to whether existing members are unable to satisfy the contributions required to be made by them. If each member is subject to a proof in respect of its Statutory Liability in its own distributing administration or liquidation before the company is wound up, the proofs will be payable on a variety of indeterminate times (if at all), and the court will be unable to form such a view. In contrast, if every member is subject to a Statutory Liability when calls are made in the company's liquidation, the Statutory Liability will be payable by every member at that time, and the court will be able to form such a view.

Paragraph (ix): set-off in the administration of LBIE of the contingent liabilities of LBL and LBHI2 as contributories against the proof of these companies as creditors of LBIE

Paragraph (x): set-off in a distributing administration or liquidation of LBL or LBHI2 of the claims of those companies against LBIE's claims in respect of those companies' contingent liabilities as contributories

49. These issues proceeded on the basis of the Judge's finding that LBIE's administrators are entitled to prove in the administration or subsequent liquidation of LBL or LBHI2 in respect of those companies' contingent liabilities under s 74(1) ([227], [243]). If, as submitted above, LBIE's administrators are not so entitled, the Judge was wrong to find that those liabilities can be set off in the administration of LBIE or the distributing administration or liquidation of LBL or LBHI2.

~~9 June 2014~~

4 March 2015

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