Editorial

A Creditors' Charter?

There is no doubt that for many years the protection afforded by the limited company has been cynically exploited by unscrupulous company promoters and directors to the considerable cost of unsecured creditors. The long-awaited report of the Cork Committee on Insolvency Law and Practice (Cmnd 8558) contains many proposals which could materially improve the lot of unsecured creditors and render more onerous the position of those who seek to abuse the privilege of limited liability.

The Committee advocate the introduction of provisions against "wrongful trading" — any person who was party to such trading could be made personally liable for debts thereby incurred by the company. Directors would be the main target though bankers and auditors could also be affected. The new concept of wrongful trading would replace the civil aspects of s 332, Companies Act 1948 (fraudulent trading) in a more stringent form in that liability could be imposed even in the absence of fraud or dishonesty and without requiring a criminal standard of proof. The proposals contain the novel feature of provision for the court to be empowered to give advance clearance for proposed transactions — this could clearly be useful to banks wishing to make an advance to a company experiencing financial difficulties. Personal liability could also be imposed on a director of an insolvent company who started a new company within a short interval of the first failure should the second company also become insolvent. The provisions for the disqualification of directors of insolvent companies who have been guilty of misconduct would also be tightened up and in some cases automatic disqualification could apply. We welcome these measures which would deter the dishonest and bring home to directors in general the seriousness of the office they undertake.

Another concern of the report is the unenviable position of unsecured creditors as compared with secured or preferential creditors. One proposal is that part (say ten per cent) of a company's assets subject to a floating charge should be made available for distribution to the unsecured creditors. This proposal would be viewed with concern by the banks and could cause them to demand further secured personal guarantees from directors — this may be beneficial in concentrating their minds on the need for the company's continued financial viability. A drawback would be the costs of verification of the claims of unsecured creditors. The report also recommends further limiting preferential claims — this would be welcomed by creditors but as the principal preferred creditor is the Government, this feature of the proposals could cause their implementation to proceed even more slowly.

The Committee critically examined the growing use of "Romalpa" retention of title clauses by suppliers and they recommend that public registration of such stipulations should be a precondition to their validity and that the interest of the seller secured should not exceed the purchase price of the goods concerned. Enforcement of rights under retention of title clauses could become subject to a 12 month moratorium once a receiver (or a new styled "administrator" where a receiver could not be appointed) was appointed — in this event the supplier would have a prior claim to the proceeds of sale of any property covered by the clause. Clarification of the legal effect of such clauses is to be welcomed but the proposals could well make suppliers more restrictive with credit.

Action

This major review, produced under the chairmanship of the doyen of insolvency practitioners, must command the respect and serious interest of industry and the professions. However, no Government action to implement the report is likely in the lifetime of the present Parliament; it would be unfortunate if the report were to be left to gather dust merely because its proposals were not sufficiently vote-catching and were considered to be contrary to the Government's own financial interests.