HOUSE OF LORDS

OPINIONS OF THE LORDS OF APPEAL FOR JUDGMENT IN THE CAUSE

STEIN (A.P.)
(RESPONDENT)

v.

BLAKE
(APPELLANT)

ON 18 MAY 1995

Lord Keith of Kinkel
Lord Ackner
Lord Lloyd of Berwick
Lord Nicholls of Birkenhead
Lord Hoffmann

LORD KEITH OF KINKEL

My Lords,

For the reasons given in the speech to be delivered by my noble and learned friend Lord Hoffmann, which I have read in draft and with which I agree, I would dismiss this appeal.

LORD ACKNER

My Lords,

I have had the advantage of reading in draft the speech prepared by my noble and learned friend Lord Hoffmann. For the reasons he gives I too would dismiss this appeal.

LORD LLOYD OF BERWICK

My Lords,

I have had the advantage of reading in draft the speech prepared by my noble and learned friend Lord Hoffmann. For the reasons he gives I too would dismiss this appeal.

LORD NICHOLLS OF BIRKENHEAD

My Lords

I have had the advantage of reading in draft the speech prepared by my noble and learned friend Lord Hoffmann. For the reasons he gives, with which I agree, I too would dismiss this appeal.

LORD HOFFMANN

My Lords,

1. The issues

If A and B have mutual claims against each other and A becomes bankrupt, does A's claim against B continue to exist so that A's trustee can assign it to a third party? Or is the effect of section 323 of the Insolvency Act 1986 to extinguish the claims of A and B and to substitute a claim for the net balance owing after setting off the one against the other? And if the latter is the case, can the trustee assign the net balance (if any) before it has been ascertained by the taking of an account between himself and B? If yes, is that what the trustee in this case has done? These are the issues in this appeal.

2. The facts

The plaintiff Mr. Stein was adjudicated bankrupt on 16 July 1990. He was at the time a legally aided plaintiff engaged in suing the defendant Blake. It is unnecessary to go into the details save to say that Mr. Stein was claiming damages for breach of contract and a declaration that he was entitled to be indemnified against certain tax liabilities. Mr. Blake was counterclaiming for damages for misrepresentation and had in addition an indisputable cross-claim under various orders for costs in any event. Mr. Blake perhaps hoped that Mr. Stein's trustee, in whom the right of action (if any) had vested, would decide that it was not in the interests of creditors to spend money on pursuing the litigation. If so, he was right, but the trustee did not abandon the claim. Instead he executed a deed dated 4 April 1991 by which he assigned the benefit of the action back to Mr. Stein in return for 49% of the net proceeds. Mr. Stein again obtained legal aid. Mr. Blake applied to have the proceedings dismissed on the ground that a claim subject to a set-off under 323 of the Insolvency Act 1986 could not validly be assigned. The application succeeded before the judge but his decision was reversed by the Court of Appeal. Mr. Blake now appeals.

3. Bankruptcy set-off

Section 323 reads, so far as relevant, as follows:

"(1) This section applies where before the commencement of the bankruptcy there have been mutual credits, mutual debts or other mutual dealings between the bankrupt and any creditor of the bankrupt proving or claiming to prove for a bankruptcy debt. (2) An account shall be taken of what is due from each party to the other in respect of the mutual dealings and the sums due from one party shall be set off against the sums due from the other. (3) . . . (4) Only the balance (if any) of the account taken under subsection (2) is provable as a bankruptcy debt, or, as the case may be, to be paid to the trustee as part of the bankrupt's estate."

4. Bankruptcy set-off compared with statutory legal set-off.

Section 323 is the latest in a line of bankruptcy set-off provisions which go back to the time of Queen Anne. As it happens, legal set-off between solvent parties is also based upon statutes of Queen Anne. But the two forms of set-off are very different in their purpose and effect. Legal set-off does not affect the substantive rights of the parties against each other, at any rate until both causes of action have been merged in a judgment of the court. It addresses questions of procedure and cash-flow. As a matter of procedure, it enables a defendant to require his cross-claim (even if based upon a wholly different subject-matter) be tried together with the plaintiff's claim instead of having to be the subject of a separate action. In this way it ensures that judgment will be given simultaneously on claim and cross-claim and thereby relieves the defendant from having to find the cash to satisfy a judgment in favour of the plaintiff (or, in the 18th century, go to a debtor's prison) before his cross-claim has been determined.

Bankruptcy set-off, on the other hand, affects the substantive rights of the parties by enabling the bankrupt's creditor to use his indebtedness to the bankrupt as a form of security. Instead of having to prove with other creditors for the whole of his debt in the bankruptcy, he can set off pound for pound what he owes the bankrupt and prove for or pay only the balance. So in *Forster v. Wilson* (1843) 12 M. & W. 191, 204, Parke B. said that the purpose of insolvency set-off was ". . . to do substantial justice between the parties. . . ." Although it is often said that the justice of the rule is obvious, it is worth noticing that it is by no means universal. (*Wood, on English and International Set-Off* (1989), paras. 24-49 to 24-56. It has however been part of the English law of bankruptcy since at least the time of the first Queen Elizabeth. (op. cit., para. 7-26.)

Legal set-off is confined to debts which at the time when the defence of set-off is filed were due and payable and either liquidated or in sums capable of ascertainment without valuation or estimation. Bankruptcy set-off has a much wider scope. It applies to any claim arising out of mutual credits or other mutual dealings before the bankruptcy for which a creditor would be entitled to prove as a "bankruptcy debt." This is defined by section 382 of the Insolvency Act 1986 to mean:

"(1) . . . any of the following (a) any debt or liability to which he is subject at the commencement of the bankruptcy (b) any debt or liability to which he may become subject after the commencement of the bankruptcy (including after his discharge from bankruptcy) by reason of any obligation incurred before the commencement of the bankruptcy. . . (3) For the purposes of references in this Group of Parts to a debt or liability, it is immaterial whether the debt or liability is present or future, whether it is certain or contingent or whether its amount is fixed or liquidated, or is capable of being ascertained by fixed rules or as a matter of opinion: and references in this Group of Parts to owing a debt are to be read accordingly."

5. Taking the account under section 323

Bankruptcy set-off therefore requires an account to be taken of liabilities which, at the time of bankruptcy, may be due but not yet payable or may be unascertained in amount or subject to contingency. Nevertheless, the law says that the account shall be deemed to have been taken and the sums due from one party set off against the other as at the date of the bankruptcy. This is in accordance with the general principle of bankruptcy law, which governs payment of interest, conversion of foreign currencies etc., that the debts of the bankrupt are treated as having been ascertained and his assets simultaneously distributed among his creditors on the bankruptcy date: see *In re Dynamics Corporation of America* [1976] 1 W.L.R. 757, 762. It is clear, therefore, that when section 323(2) speaks of taking an account of what is "due" from each party, it does not mean that the sums in question must have been due and payable, whether at the bankruptcy date or even the date when the calculation falls to be made. The claims may have been contingent at the bankruptcy date and the creditor's claim against the bankrupt may remain contingent at the time of the calculation, but they are nevertheless included in the account. I consider next how this is done.

6. Quantifying the cross-claims

How does the law deal with the conundrum of having to set off, as of the bankruptcy date, "sums due" which may not yet be due or which may become owing upon contingencies which have not yet occurred? It employs two techniques. The first is to take into account everything which has actually happened between the bankruptcy date and the moment when it becomes necessary to ascertain what, on that date, was the state of account between the creditor and the bankrupt. If by that time the contingency has occurred and the claim has been quantified, then that is the amount which is treated as having been due at the bankruptcy date. An example is *Sovereign Life Assurance Co. v. Dodd* [1892] 2 Q.B. 573, in which the insurance company had lent Mr. Dodd £1,170 on the security of his policies. The company was wound up before the policies had matured but Mr. Dodd went on paying the premiums until they became payable. The Court of Appeal held that the account required by bankruptcy set-off should set off the full matured value

of the policies against the loan.

But the winding up of the estate of a bankrupt or an insolvent company cannot always wait until all possible contingencies have happened and all the actual or potential liabilities which existed at the bankruptcy date have been quantified. Therefore the law adopts a second technique, which is to make an estimation of the value of the claim. Section 322(3) says:

> "The trustee shall estimate the value of any bankruptcy debt which, by reason of its being subject to any contingency or contingencies or for any other reason, does not bear a certain value."

This enables the trustee to quantify a creditor's contingent or unascertained claim, for the purposes of set-off or proof, in a way which will enable the trustee safely to distribute the estate, even if subsequent events show that the claim was worth more. There is no similar machinery for quantifying contingent or unascertained claims <u>against</u> the creditor, because it would be unfair upon him to have his liability to pay advanced merely because the trustee wants to wind up the bankrupt's estate.

7. The occasion for taking the account

In what circumstances must the account be taken? The language of section 323(2) suggests an image of the trustee and creditor sitting down together, perhaps before a judge, and debating how the balance between them should be calculated. But the taking of the account really means no more than the calculation of the balance due in accordance with the principles of insolvency law. An obvious occasion for making this calculation will be the lodging of a proof by a creditor against whom the bankrupt had a cross-claim. Indeed, it might have been thought from the words "any creditor of the bankrupt proving or claiming to prove from a bankruptcy debt" in section 323(1) that the operation of the section actually depended upon the lodging of a proof. But it has long been held that this is unnecessary and that the words should be construed to mean "any creditor of the bankrupt who (apart from section 323) would have been entitled to prove for a bankruptcy debt". Thus the account to which section 323(2) refers may also be taken in an action by the trustee against a creditor who, because his cross-claim does not exceed that of the trustee, has not lodged a proof: see *Mersey Steel and Iron Co. v. Naylor Benzon & Co.* (1882) 9 Q.B.D. 648 and *In re Daintrey* [1900] 1 Q.B. 546, 568.

Once one has eliminated any need for a proof in order to activate the operation of the section, it ceases to be linked to any step in the procedure of bankruptcy or litigation. This is a sharp contrast with legal set-off, which can be invoked only by the filing of a defence in an action. Section 323, on the other hand, operates at the time of bankruptcy without any step having to be taken by either of the parties. The "account" in accordance with section 323(2) must be taken whenever it is necessary for <u>any</u> purpose to ascertain the

effect which the section had. This is shown most clearly by the Australian case of *Gye v. McIntyre* (1991) 171 C.L.R. 609. In 1980 Gye, Perkes and three others bought a hotel in New South Wales from a company for $1.25m. For this purpose they borrowed $200,000 from Mrs McIntyre, who was the company's tenant. The business was a failure and in June 1982 Mrs McIntyre obtained judgment by default for $224,000 in respect of her loan, interest and costs. Execution was stayed while Gye and Perkes pursued an action for damages against Mrs McIntyre for having fraudulently induced them to buy the hotel from the company by overstating its profits. In 1985 both Gye and Perks entered into binding compositions with their creditors under which they assigned certain assets and promised certain payments to a trustee for the benefit of their creditors. The assigned assets did not include the benefit of the action against Mrs McIntyre and she did not prove as a creditor in either composition. In 1988 the action against Mrs McIntyre was successful and Gye and Perks obtained judgment in the sum of $214,600. They claimed a declaration that she was not entitled to set off the 1982 judgment, for which she could have proved in the compositions. The Australian Bankruptcy Act 1966 provides, if I may paraphrase in English terminology, that bankruptcy set-off shall apply in a composition as if a bankruptcy order had been made on the day on which the resolution accepting the composition was passed and the trustee of the composition was the trustee in bankruptcy.

It will be observed that in this case the creditor was neither seeking to prove nor being sued by the trustee in bankruptcy. The issue was the effect which the deemed bankruptcy had had upon a claim which had never passed to the deemed trustee and which was later litigated between the bankrupt and the creditor. The High Court of Australia held that bankruptcy set-off applied. The judgment of the court said, at p. 622:

> "Section [323] is a statutory directive ('shall be set off') which operates as at the time the bankruptcy takes effect. It produces a balance upon the basis of which the bankruptcy administration can proceed. Only that balance can be claimed in the bankruptcy or recovered by the trustee. If its operation is to produce a nil balance, its effect will be that there is nothing at all which can be claimed in the bankruptcy or recoverec in proceedings by the trustee. The section is self-executing in the sense that its operation is automatic and not dependent upon 'the option of either party': see, per Lord Selborne L.C. in *In re Deveze; Ex parte Barnett* (1874) 9 Ch. App. 293, 295."

The court noted the majority decision of this House in *National Westminster Bank Ltd v. Halesowen Presswork & Assemblies Ltd* [1972] A.C. 785 that the application of section 323 is mandatory in the sense that it cannot be excluded by prior agreement of the parties. But it said that whether or not it could be excluded by agreement, its operation did not depend upon any procedural step. If, for example, the cross-claims produced a nil balance, one would hardly expect either the creditor to prove or the trustee to sue. But

there could be no doubt that if the question subsequently needed to be decided, the two claims would be treated as having extinguished each other. The court said:

> "Even if one were to accept the dissenting view of Lord Cross of Chelsea in the *National Westminster Case* [1972] A.C. 785, 813-818 to the effect that the otherwise automatic operation of a provision such as [section 323] may be excluded by an antecedent agreement, it would be wrong to attribute to the legislature the illogical intent that a directive which was intended to be otherwise automatic in its operation and to apply in circumstances where set-off produced a nil balance should not operate at all unless and until either the bankrupt's creditor saw fit to exercise the option of lodging a formal proof of debt or the trustee in bankruptcy instituted proceedings for recovery of a debt due to the bankrupt."

8. Do the causes of action survive?

The principles so far discussed should provide an answer to the first of the issues in this appeal, namely, whether if A, against whom B has a cross-claim, becomes bankrupt, A's claim against B continues to exist as a chose in action so that A's trustee can assign it to a third party. In my judgment the conclusion must be that the original chose in action ceases to exist and is replaced by a claim to a net balance. If the set-off is mandatory and self-executing and results, as of the bankruptcy date, in only a net balance being owing, I find it impossible to understand how the cross-claims can, as chooses in action, each continue to exist.

This was the conclusion of Neill J. in *Farley v. Housing & Commercial Developments Ltd* [1984] B.C.L.C. 442. Mr. Farley was the principal shareholder in W. Farley & Co. (Builders) Ltd, which in 1972 had entered into two agreements with the defendant company to build blocks of flats. Both led to disputes, with claims by the building company for money due under the contracts and cross-claims by the defendant for damages. In 1975 the building company went into insolvent liquidation. In 1979 the liquidator purported to assign to Mr. Farley the benefit of the agreements and all moneys payable thereunder. Mr. Farley then commenced arbitration proceedings under the agreements. The arbitrator stated a special consultative case (p. 447) asking:

> "(1) Whether by reason of the provisions of [the then equivalent of section 323 as applied to companies] upon the contractor becoming insolvent and being wound up . . . the debts due under the [two agreements] ceased to have a separate existence as chooses in action (and thus thereafter could not be assigned) being replaced by a balance of account under [section 323]."
>
> Neill J. answered in the affirmative. I think that he was right. The

cross-claims must obviously be considered separately for the purpose of ascertaining the balance. For that purpose they are treated as if they continued to exist. So, for example, the liquidator or trustee will commence an action in which he pleads a claim for money due under a contract and the defendant will counterclaim for damages under the same or a different contract. This may suggest that the respective claims actually do continue to exist until the court has decided the amounts to which each party is entitled and ascertained the balance due one way or the other in accordance with section 323. But the litigation is merely part of the process of retrospective calculation, from which it will appear that from the date of bankruptcy, the only chose in action which continued to exist as an assignable item of property was the claim to a net balance.

9. The reasoning of the Court of Appeal.

The Court of Appeal took the view that *Farley* was wrong and that the separate causes of action survived the bankruptcy and could be assigned, subject to the "equity" of the bankruptcy set-off. My Lords, the notion of an assignment subject to equities looks plausible when one is dealing with an assignment of the only claim which the bankrupt has against a creditor. In such a case it produces the same result as an assignment of the net balance. But the fallacy is exposed if the bankrupt has more than one claim. Take, for example, the two contracts in *Farley's* case and assume that the liquidator at first assigns only one to Mr. Farley. If each contract continues to exist as a chose in action, each can be the subject of a legal assignment. Mr. Farley sues on his contract and by way of defence the defendants plead counterclaims for damages under both contracts. The court decides that the damages exceed the sums due under the contract and dismisses the action. The liquidator then assigns the other contract to Mrs Farley. She is not bound by the decision in her husband's case and the defendant would have to plead and prove its counterclaims all over again. The account envisaged by section 323 would have to be taken twice (with possibly differing results) when the section plainly contemplates a single calculation.

The argument for the plaintiff, which was recorded and accepted by Balcombe L.J. in the Court of Appeal [1994] Ch. 16, 22, began with the proposition that "Nothing in the wording of section 323 changes the nature of set-off as it operates between solvent parties; it merely widens the categories of claim capable of being, and which must be, set off." I hope I have demonstrated that this submission is fundamentally wrong. It is true that bankruptcy set-off does cover a much wider range of claims than legal set-off. But for present purposes the important difference is that the latter must be pleaded and is given effect only in the judgment of the court, whereas the latter is self-executing and takes effect on the bankruptcy date.

Secondly it was submitted for the plaintiff (pp. 22-23) that "the language of the section draws a distinction between what is due - which is the word used in subsections (2) and (3) - and what is payable or recoverable - as

under subsection (4). The separate causes of action (claim and cross-claim) remain due, and do not cease to exist, until the set-off has been completed by payment one way or the other." This argument is derived, *via Derham on Set-Off* (1987), p. 74, from a dictum of Mason J. in *Day & Dent Constructions (Pty) Ltd v. North Australian Properties (Pty) Ltd* (1982) 150 C.L.R. 85. The learned judge said that "due" in the Australian equivalent of section 323(2) meant due at the date when the account had to be taken and he relied upon this construction to explain why a creditor should be entitled to set off a debt which was contingent at the bankruptcy date. I would respectfully disagree because I think that "due" merely means treated as having been owing at the bankruptcy date with the benefit of the hindsight and, if necessary, estimation prescribed by the bankruptcy law. The valuation provision in section 322(3) shows that the contingency need not have occurred even at the time when the account has to be taken. But the point was not necessary for the decision and was in any case addressing the question of what obligations should be taken into account in arriving at the net balance rather than whether those obligations survived as chooses in action.

Thirdly, Balcombe L.J. placed much weight upon a dictum of Brett J. in *New Quebrada Co. Ltd v. Carr* (1869) L.R. 4 C.P. 651, 653-654. This was an action by a company in liquidation for calls against three partners, joint owners of shares in a company. The plea was a set-off of a debt alleged to be owing by the company to the shareholders. It is important to bear in mind that this was pleaded as a legal set-off under the Statutes of Set-off, not a bankruptcy set-off arising on the liquidation of the company. Bankruptcy set-off did not apply to company liquidations until the Judicature Act 1875. It was therefore essential that the debt relied upon as set-off should have been legally actionable by the defendants. The replication was that after the action had been brought and before the plea, one of the partners had become bankrupt and his interest in the company's alleged debt had vested in his assignee. It had therefore ceased to be actionable by him. There was a demurrer to this replication. In support of the demurrer it was argued that the bankrupt's share in the debt had not vested in his trustee because under section 171 of the Bankruptcy Act 1849 (the then equivalent of section 323 of the Insolvency Act 1986) it was on his bankruptcy automatically set off against the calls due to the company. Bovill C.J., applying an earlier decision, disposed of the case on the ground that section 171 applied only to a sole trader and not to one partner in a firm. Byles J. and Montague Smith J. agreed. Brett J. also agreed, but went on to consider obiter what the effect of section 171 would have been if the bankrupt had been a sole trader. In his view, the debt owing to the bankrupt would have vested in his trustee and therefore ceased to be actionable by the bankrupt. Having so vested, it would then have been liable to be set off in the bankruptcy against the company's claim to prove for calls. He added:

> "[Section 171] does not, I think, extinguish the mutual debts, but if it did, I should have thought it would have answered the plea of set-off. In either view I think it does not leave a right of action in the bankrupt

against the plaintiffs, and that he cannot, therefore, avail himself of his claim against the plaintiffs under an ordinary plea of set-off, and that, on the present pleadings and argument, it seems to me, is all we have to decide."

It should be noticed that section 171 of the Bankruptcy Law Consolidation Act 1849 (12 & 13 Vict. c. 106) said that "one debt or demand may be set against another", as opposed to the words "the sum due from the one party shall be set off against any sum due from the other party" which were used in the equivalent section [section 39] of the Bankruptcy Act 1869 (32 & 33 Vict. c. 71) and all its successors. It is therefore perhaps not surprising that the mandatory and self-executing nature of the set-off was not as fully apparent under the Act of 1849 as it is today. At any rate, I do not think that despite the eminence of its author, this somewhat throw-away dictum on the Bankruptcy Act 1849 can be regarded as authoritative on the construction of section 323 of the Insolvency Act 1986.

10. Can the net balance be assigned?

The next question is whether the trustee can assign the net balance. (I should mention that the question was not put to Neill J. in *Farley v. Housing & Commercial Developments Ltd.* [1987] B.C.L.C. 442.) The duty of the trustee under section 305(2) is to realise the bankrupt's estate and the right to the net balance is part of the property of the bankrupt vested in the trustee. One method of realisation is to transfer or assign the individual assets for value. In *Ramsey v. Hartley* [1977] 1 W.L.R. 686 the Court of Appeal, following authority which went back more than a century, held that even a bare right of action was property which the trustee was entitled to assign. His statutory duty to realise the estate excluded the doctrines of maintenance and champerty which would otherwise have struck down such an assignment. Likewise, there is no rule to prevent him from assigning such a right of action to the bankrupt himself. So why should a trustee not assign the right to the net balance?

Mr. Mark, for the appellant, says that the right cannot be assigned until the balance has been quantified by the account taken under section 323. The reason, he says, is that the trustee must be party to the taking of that account. Bankruptcy set-off is, as Lord Simon of Glaisdale said in *National Westminster Bank Ltd v. Halesowen Presswork & Assemblies Ltd* [1972] A.C. 785, 809, part of a "code of procedure whereby bankrupts' estates . . . are to be administered in a proper and orderly way." So, for example, section 322(3) (which I have already quoted) requires that the value of a contingent or otherwise unascertained debt to be estimated by the trustee.

I think that this submission of Mr. Mark is wrong for the same reasons that persuaded me that his submission on the first issue was right. If bankruptcy set-off is self-executing, it does not require the trustee or anyone else to execute it. The argument gives too literal a meaning to the notion of

taking an account. The case of *Gye v. McIntyre* (1991) 171 C.L.R. 609 shows the account being taken in proceedings to which the trustee was not a party. It is true that the situation arose because in a composition, the parties are able to decide which property should vest in the trustee and could exclude the claim against Mrs McIntyre. In the case of a bankruptcy, vesting is determined by the law. But for present purposes I can see no logical distinction between a case in which the trustee assigns the right to the net balance and one in which the bankrupt's claim, though subject to bankruptcy set-off, did not vest in him in the first place.

It is true that the trustee will ordinarily not be party to the action between assignee and creditor. So if the creditor is asserting that there is actually a net balance in his favour for which he is entitled to prove, a successful outcome of the action will not, as a matter of res judicata, oblige the trustee to allow his proof. But there is no reason why a defendant should not, with leave, join the trustee as a defendant to his counterclaim. Even if the action had been brought by the trustee, the creditor would have needed the leave of the court to make a counterclaim. In these circumstances, there seems to me little additional inconvenience in having to add the trustee as a party. I would therefore hold that a trustee may assign the right to the net balance like any other chose in action.

11. Questions of construction.

Did the actual deed executed by the trustee have the effect of carrying the net balance? That is a question of construction. If a trustee purports to assign the bankrupt's rights in a cheque for £10,000, it would be absurd to hold that the deed has no effect because it turns out that the drawer of the cheque has some small counterclaim against the bankrupt. The intention of the parties is clear enough. If the assignment would have carried the original cause of action, it will also, as a matter of conveyance, carry the right to the balance after deduction of the cross-claim. Whether the assignee would have any claim against the trustee for having purported to assign a greater interest than he actually had need not here be considered.

There is greater difficulty if the trustee has assigned <u>less</u> than the net balance, i.e. to have kept back some credit item in the calculation. This would be an assignment of a part of a debt. On ordinarily principles it would not be enforceable in proceedings to which the trustee was not a party. Only if the trustee joined as a plaintiff could the single account envisaged by section 323 be taken.

In this case the deed of assignment of 4 April 1991 recited that the trustee had agreed with the bankrupt for the assignment to him of:

> "such claims and legal rights of action as are hereinafter mentioned which the trustee as trustee in bankruptcy of the assignee may have against [the defendant]"

The operative part said in clause 1 that the trustee assigned to the bankrupt:

> "such claim or claims against Mr. Blake as the Trustee may have as trustee in the bankruptcy of the assignee as presently formulated, or as amended by counsel with the Trustee's approval, based only on the facts pleaded in consolidated action number Ch. 1989 S-8148 and 1988 S-4555 ("the Claim") to the intent that the assignee shall be entitled (subject as hereinafter mentioned) to such monies as Mr. Blake may be to the Assignee in settlement of the Claim."

By clause 6 (ii) the parties agreed, for the avoidance of doubt, that:

> "nothing in this agreement shall affect the Trustee's right to take action against Mr. Blake if so advised in relation to matters not arising out of the facts other than those pleaded in the aforesaid consolidated action."

My Lords, the fact that the assignment makes no express reference to the defendant's cross-claim is, for the reasons I have given, no obstacle to holding the assignment effective to carry whatever balance is due after its deduction. But if the effect of this last clause was that the trustee retained a part of his claim to the net balance against Mr. Blake, then in my judgment the action would not have been properly constituted until the trustee had been added as a party. Mr. Blake could not be put in a position in which he had to raise the same cross-claim in two sets of proceedings. His remedy would have been to apply to have the action stayed until the trustee had been added. Before your Lordships' House, however, Mr. Bannister Q.C. for the plaintiff said that the trustee asserted no other causes of action against Mr. Blake. He is willing to make it clear that he is assigning the whole of the net balance due to the bankrupt's estate. In these circumstances it is unnecessary to discuss further the question of what might have happened if there had been an application for a stay on the grounds that the proceedings were not properly constituted. The application to which the judge actually acceded was to dismiss the action on the ground that Mr. Stein had no title to sue. For the reasons which I have given, which I think were the alternative reasons of Staughton L.J., the Court of Appeal was in my judgment right to hold that the judge's order could not be supported. I would therefore dismiss this appeal.

12. The wider issues.

I should add in conclusion that although the appeal may have turned on a somewhat technical question, it is a symptom of a wider problem. Although Mr. Mark argued that it was inconvenient and unjust for the account under section 323 should be taken between him and Mr. Stein, rather than between him and the trustee, he frankly admitted that his main grievance was that despite the bankruptcy, he was still being pursued by Mr. Stein with the benefit of legal aid. But he acknowledged that this complaint would have been the same if there had been no counterclaim and the case had not fallen

within section 323 at all.

It is a matter of common occurrence for an individual to become insolvent while attempting to pursue a claim against someone else. In some cases, the bankruptcy will itself have been caused by the failure of the other party to meet his obligations. In many more cases, this will be the view of the bankrupt. It is not unusual in such circumstances for there to be a difference of opinion between the trustee and the bankrupt over whether a claim should be pursued. The trustee may have nothing in his hands with which to fund litigation. Even if he has, he must act in the interests of creditors generally and the creditors will often prefer to receive an immediate distribution rather than see the bankrupt's assets ventured on the costs of litigation which may or may not yield a larger distribution at some future date. The bankrupt, with nothing more to lose, tends to take a more sanguine view of the prospects of success. In such a case the trustee may decide, as in this case, that the practical course in the interests of all concerned (apart from the defendant) is to assign the claim to the bankrupt and let him pursue it for himself, on terms that he accounts to the trustee for some proportion of the proceeds.

It is understandable that a defendant who does not share the bankrupt's view of the merits of the claim may be disappointed to find that notwithstanding the bankruptcy, which he thought would result in a practical commercial decision by an independent trustee to discontinue the proceedings, the action is still being pursued by the bankrupt. His disappointment is increased if he finds that the bankrupt as plaintiff in his own name has the benefit of legal aid which would not have been available to the trustee. Similar considerations apply to an assignment of a right of action by the liquidator of an insolvent company to a shareholder or former director. In such a case there is the further point that the company as plaintiff can be required to give security for costs. The shareholder assignee as an individual cannot be required to give security even if (either because he does not qualify or the Legal Aid Board considers that the claim has no merits) he is not in receipt of legal aid.

I mention these questions because they were alluded to by Mr. Mark as a policy reason for why the courts should be restrictive of the right of bankruptcy trustees or liquidators to assign claims. But the problems can be said to arise not so much from the law of insolvency as from the insoluble difficulties of operating a system of legal aid and costs which is fair to both plaintiffs and defendants. Mr. Blake is in no worse position now that he was before the bankruptcy when Mr. Stein was suing him with legal aid (although this would not have been the case if the plaintiff had been a company.) Mr. Blake's complaint is that the bankruptcy has brought him no relief. But whether it should seems to me a matter for Parliament to decide.

Stein (A.P.) (Respondent) v. Blake (Appellant)

JUDGMENT

Die Jovis 18° Maii 1995

Upon Report from the Appellate Committee to whom was
:rred the Cause Stein against Blake, That the Committee had
l Counsel as well on Monday the 3rd as on Tuesday the 4th
of April last upon the Petition and Appeal of David Blake
Ordnance Hill, St. John's Wood, London NW8, praying that the
er of the Order set forth in the Schedule thereto, namely
rder of Her Majesty's Court of Appeal of the 5th day of May
, might be reviewed before Her Majesty the Queen in Her Court
arliament and that the said Order might be reversed, varied
ltered or that the Petitioner might have such other relief
he premises as to Her Majesty the Queen in Her Court of
iament might seem meet; as upon the case of Allan Stein
ed in answer to the said Appeal; and due consideration had
day of what was offered on either side in this Cause:

It is Ordered and Adjudged, by the Lords Spiritual and
oral in the Court of Parliament of Her Majesty the Queen
mbled, That the said Order of Her Majesty's Court of Appeal
he 5th day of May 1993 complained of in the said Appeal be,
the same is hereby, **Affirmed** and that the said Petition and
al be, and the same is hereby, dismissed this House: And it
urther Ordered, That the Appellant do pay or cause to be paid
he said Respondent the Costs incurred by him in respect of
said Appeal to this House, the amount thereof to be certified
the Clerk of the Parliaments if not agreed between the
ies: And it is also further Ordered, That the costs of the
ondent be taxed in accordance with the Legal Aid Act 1988.

Cler: Parliamentor: