Corporate Insolvency and Employment Protection: A Theoretical Perspective

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Abstract

When a company faced with financial difficulties finally enters formal insolvency, several creditor interests are affected. However, the relationship between employees and their employer is more threatened as companies faced with insolvency usually consider cutting labour costs as a mode of restructuring. Other stakeholder interests and mutual expectations such as continuity of employment may be severely altered or cease to exist completely where the company is either liquidated or sold as a going concern. This may prompt various parties with interests in that company to pursue and recover their interests against the debtor company. However, secured creditors such as banks with privately agreed contractual arrangements may choose to pursue their interests by exercising those contractual rights, usually to the detriment of general unsecured creditors like employees. This raises questions as to whose interest should insolvency law seek to protect on corporate insolvency? In other words, what the legitimate aim or goal of insolvency is or ought to be on corporate insolvency. This article will analyse two insolvency specific theories namely; the Creditors' Bargain Theory (CBT) and the Team Production Theory of Corporate Reorganizations (TPT) and two general theories namely; Marxist Legal Theory and Dworkin's Interpretative Theory of Law, to examine their normative position on the treatment of employees on corporate insolvency and the impact they would impose on the drive to rescue insolvent but viable businesses. The two general theories (Marxist Legal Theory and Dworkin's Interpretative Theory) will be analysed in light of insolvencies to establish whether their normative perspectives may inform law and policy justifications on corporate insolvency in a non–specific insolvency perspective. The article will conclude by analysing what the legitimate goal of insolvency law ought to be if a balanced approach to stakeholder interest consideration is to be reached.

Introduction

For centuries, there have been various debates from insolvency scholars, academics and practitioners[1] on what the legitimate goal of insolvency law is or ought to be. One of the leading scholars of insolvency, Professor Baird is of the view that engaging debates on insolvency law's legitimate goal are mainly contested between two theoretical stands namely; the traditionalists and the proceduralists.[2]

The proceduralists look at insolvency law's main objective as a means of maximisation of value for creditors and therefore their approach can be viewed as creditor - biased. They contend that insolvency law should focus on addressing issues that only arise out of bankruptcy.[3] They believe that non-insolvency claims or entitlements should not be protected by insolvency law unless doing so would maximise value for creditors.[4] They prefer using economic models as a basis for analysing corporate insolvency and market solutions, as opposed to seeking judicial intervention based on vague standards of fairness for resolving issues arising on corporate insolvency.[5]

Traditionalists, however, take a stand that is opposite to that of the proceduralists in that they advocate a more inclusive approach to stakeholder interest consideration during corporate insolvency. They believe that all interests should be given equal weight of consideration on corporate insolvency.[6] They are against the notion that insolvency law exists to only serve the interests of creditors. In light of these varying views, there is a theoretical deadlock as to the legitimate aim of insolvency law. A consensus is yet to be reached. However, it should be noted that these normative views between the traditionalists and proceduralists have been transposed into various extant insolvency law theories. These theories may be used for solving disputes during corporate insolvency.

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[1] C. W. Mooney Jr, "A Normative Theory of Bankruptcy Law: Bankruptcy Law As (Is) Civil Procedure" Univ. of Penn. Law School, Institute for Law and Economics, Research Paper No. 03 -27 (2003); Elizabeth Warren, 'Bankruptcy Policy' (1987) 54 Uni. Chi. L. Rev. 775; E Warren, ' Bankruptcy Policymaking in an Imperfect World' (1993) 92 Mich. L. Rev. 336, 387; D. R. Korobkin, "Contractarianism and the normative foundations of bankruptcy law" (1993) 71 Tex. L. Rev. 554; D. Baird & T. H. Jackson, 'Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy' (1984) 51 U Chicago L. Rev. 97.

[2] D.G. Baird, "The Uneasy Case for Corporate Reorganizations" (1986) 15 Journal of Leg. Stud. 127, 133.

[3] Please note that the term bankruptcy is used differently in the US and the UK. In the UK, the term bankruptcy is used to refer to a situation where a person is unable to pay his debts and therefore faced with bankruptcy. The term insolvency is used to refer to a company that is unable to pay its debts. However, in the US bankruptcy is used to refer to both a person and a company being unable to pay their debts.

[4] C. W. Mooney Jr, "A Normative Theory of Bankruptcy Law: Bankruptcy Law As (Is) Civil Procedure" Univ. of Penn. Law School, Institute for Law and Economics, Research Paper No. 03 -27 (2003).

[5] See for instance, R. Posner, *The Economics of Justice* (Cambridge, MA: HUP, 1983) pp 60 – 87 on his account of wealth maximisation as an ethical principle, a typical law and economics perspective.

[6] D. R. Korobkin, "Contractarianism and the normative foundations of bankruptcy law" (1993) 71 Tex. L. Rev. 554.

Select Insolvency Theories

A theory is a factual concept or framework describing a given phenomenon, the way it is or it ought to be.[7] Where theories are used in insolvency disciplines, they are explored as normative phenomena as they prescribe methods of evaluation as to why insolvency is the way it is or ought to be in a given state or society.[8] Although it may be argued that theories on their own cannot solve underlying issues in a given state, they can however provide the basis upon which substantive insolvency laws and policies in different jurisdictions are prescribed or evaluated.

In attempts to explain the legitimate provinces and objectives of insolvency law to be pursued in any jurisdiction, several theories have been put forward by various academic theorists. These include for example; The Value Based Theory from the academic wisdom of Korobkin[9], Communitarianism[10] and the Multiple Value Approach,[11] among other theories. However, for the purpose of this article, two normative insolvency specific theories namely; The Creditors Bargain Theory (CBT) and the Team Production Theory of Corporate Reorganizations (TPT) and two general (non-insolvency) theories namely; Marxist Legal Theory and Dworkin's Interpretative Theory of Law will be discussed and analysed. The applicability of these theories to the treatment of employees on corporate insolvency will be analysed and it will be considered whether insolvency laws and policies modelled on their normative theoretical perspectives would be advantageous to employment protection over business rescue.

The main reason for these four selected theories is that, both the CBT and TPT are contractarian theories.[12] However, the CBT is premised on the creditors' primacy and wealth maximisation norms – a typical proceduralist approach to corporate insolvency. The TPT, although contractarian in nature, it is a social contractarian theory.[13] It is premised on the traditionalist view which recognises the interests of all parties to the company as a whole on corporate insolvency. The theory sees all interest holders as team members who join resources together to achieve the end product or service.

On the other hand, Dworkin's interpretative theory of law is chosen as it offers a normative approach to how laws, policies or practices should be interpreted in a more principled approach, drawing upon social ideals like moral obligation, value and purpose

[7] Brian H. Bix, *Jurisprudence: Theory and Context*, (6th edn., Sweet & Maxwell, London 2012) 4.
[8] D.R. Korobkin, 'Contractarianism and the Normative Foundations of Bankruptcy Law' (1993) 71 Texas L. Rev. 98.
[9] See Ronald R. Korobkin, 'Rehabilitating Values: A Jurisprudence of Bankruptcy' (1991) Colum. L. Rev. 717.
[10] See Karen Gross, 'Taking Community Interests Into Account in Bankruptcy An Essay' (1994) 72 Wash. U.L.Q 1031.
[11] Elizabeth Warren, 'Bankruptcy Policy' (1987) 54 Uni. Chi. L. Rev. 775; E. Warren, 'Bankruptcy Policymaking in an Imperfect World' (1993) 92 Mich. L. Rev. 336, 387.
[12] D. R. Korobkin, "Contractarianism and the Normative Foundations of Bankruptcy Law" (1993) 71 Texas L. Rev. 98.
[13] See, S. Freeman, *Justice and the Social Contract* (Oxford : OUP, 2007).

of the law rather than according to a static rule based approach. It is a social contract theory as it prescribes to protecting the interests of all parties to a dispute fairly drawing on extant legal rules and principles of law embedded in the legal system or precedents, and it can be applied to insolvencies.

Marxist Legal Theory is chosen as it offers normative arguments on the role and impact of capitalism on our society through an economic analysis of law. Marx's arguments on capitalism in modern society through the labour theory of value and the continuing and widening gap and struggle between the rich in our society (capitalists) and the poor[14] (working class – employees) will be explored. Marxist legal theory will serve as a big tool for analysing both the CBT and TPT theories in looking at the contractarian wealth maximisation model over the social contract model in creditor interest consideration during corporate insolvency.

Marxist Legal Theory

Karl Marx saw law as being part of a superstructure which was a reflection of the economic base of the society. Law, according to Marx, was used as a means of domination of the proletariat (working class or providers of labour) by the bourgeoisie (the rich who own and control the means and relations of production in society). To him, the history of all society was built on class struggle between the two classes – the owners of capital and the providers of labour.[15]

In several of his writings, which mainly centred on criticisms of capitalism, Marx gave us what can be termed as the theory of society.[16] Through this theory, Marx gives an account of how society works through social ideals, for example, law and morality, and social institutions such as education, which can be used to explain what is happening in our society today or perhaps why history, as prophesied by him, is unfolding. Marx gave various types of societies. These included among others, primitive, feudal, slave and capitalist societies through which society evolves. However, in this article, regard is to be given to the capitalist society.

Marx argued that the most important determinant of all aspects of our society is the economic situation. This determines or controls the productive system for goods or services as compared to other socio – political aspects like education, law and morality that are said to be elements that form the superstructure of our society. To Marx, whoever

[14] However, it should be noted that, some employees are highly paid than others. Cognisance has to be given to the fact that the economic situation at the time of Marx's writings, 'Professionals' were self – employed.

[15] D. McLellan, *Karl Marx: Selected Writings* (OUP, Oxford) 615; Z. Husami, 'Marx on Distributive Justice' in Cohen, Nagel, Scalon, *Marx, Justice and History* (Princeton University Press, Princeton 1980); J. Reiman, 'Moral Philosophy: The critique of capitalism and the problem of ideology' in T Carver, *The Cambridge Companion to Marx* (CUP, Cambridge 1991).

[16] Karl Marx, *Capital:* A Critique of Political Economy Volume 1: The Process of Capital Production (Samuel Moore and Edward Aveling trans.) Frederick Engels and Ernest Untermann ed. (Chicago: Charles. H Kerr and Co. 1909); A. Oakley, *Marx's Critique of Political Economy: 1884 to 1860* (London: Routledge, 1984).

controls the economic structure, which is the productive system of a society, is able to influence policies or laws that can change, reform or solve issues that are faced within that society.

Viewed in the context of our current economic society in the UK today, it would be unconscionable to deny Marx the praise for foreseeing what is happening today. The UK can be categorised as a capitalist society. This is because the current economic structure is mainly built on a relationship of two parties: the owners of capital and those that provide labour – who are the employees that are employed to offer either physical labour or a service based on their skills.

However, in a capitalist mode of production, capitalists take wealth maximisation as supreme above other social factors, such as the needs and welfare of employees who provide the labour that symbiotically[17] works alongside capital investment to achieve the end product. Moreover, capitalism is based upon the conventional economic theory and practice which is premised on the norm that production in society is driven by profit which creates and maximises wealth.[18]

Marxist Theory of Labour Value

According to Marx's "*The Labour Theory of Value*", capitalist wealth maximisation or giving supremacy to profit making over other social aspects in the production system of society constitutes exploitation of workers. Capitalists take as value, the price that will be paid for the product on the market against the value of labour that employees put into the production of that product.[19] It is a known and accepted practice in the world of business and investment that profit incentivises capitalists or shareholders to invest money in production that in return creates jobs and improves the economic welfare of society. It is also worth noting that production of a product or service requires capital as well as labour.[20]

Rewarding capitalists or shareholders (who simply put money into production) more than employees (who invest labour in the production process) creates social problems which adversely affect society at large. When a product that is produced by a combination of capital and labour is sold and a profit is made, a shareholder or a capital provider, is rewarded with a return on capital investment. Likewise, employees are paid

[17] This word derives from the term symbiosis which is used to explain the existence of a mutually beneficial relationship between two entities or people. In this chapter, the term is used to highlight the existence of two mutual entities: the employer and the employees who both mutually benefit from the existence and services of each other especially in the production or service industry.
[18] Karl Marx, *Capital:* A Critique of Political Economy Volume 1: The Process of Capital Production (Samuel Moore and Edward Aveling trans.) Frederick Engels and Ernest Untermann ed. (Chicago: Charles. H Kerr and Co. 1909).
[19] R. Miller, *Analyzing Marx* (Princeton University Press, Princeton 1980).
[20] A. Buchanan, *Marx and Justice* (Methuen, London 1982).

a wage for labour input. However, there is sense in the argument that employees are usually paid the lowest possible consideration for their input.[21]

Although shareholders or capital providers usually bear the risk that there would be no return on their capital and therefore assume such a risk, they usually do nothing more than contributing capital and often receive a proportionately greater return than employees. They actually benefit more from the value and wealth created by employees than employees themselves. This is because as said above, capitalists consider the profit generated by the product or service on the market as the main determinant factor in the production process.[22]

To Marx, the value of goods ought to be calculated in consideration of the amount of labour that is input, a notion that ought to be managed and controlled by the state's laws and policies. However, this is not possible because in a capitalist society, like the UK today, the state is a construct of a few but rich capitalists who control and own the forces and relations of production. They use the law to regulate issues such as property ownership and also limit attempts by the employees to claim or press for ownership rights.[23]

A vivid example is found in the practice in the working industry for employees to have employment contracts with terms and conditions stating what they can and cannot do or claim ownership for. Through the contractual approach, employees are more likely to have no ownership or say in the final product or service delivery as the final product is not their product. They are likened to robots or mercenaries who are hired to do specific duties to a certain level, which further highlights the level of inequality of bargaining power that exists in the relationship between the employee and the employer.

In these employment contracts, the business owners insert terms and clauses that entitle the employer to assume ownership of any property such as intellectual property that employees create while in the course of their employment.[24] This creates and widens the level of bargaining inequality between capitalist employers and the working class employees and may lead to social effects like alienation of the employees in their working places as their main interest is only their salaries and wages, irrespective of the level and value of input they invest in the business.[25]

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[21] J. Reiman, 'Moral Philosophy: The critique of capitalism and the problem of ideology' in T Carver, *The Cambridge Companion to Marx* (CUP, Cambridge 1991).

[22]Karl Marx, *Capital:* A Critique of Political Economy Volume 1: The Process of Capital Production (Samuel Moore and Edward Aveling trans.) Frederick Engels and Ernest Untermann ed. (Chicago: Charles. H Kerr and Co. 1909)

[23] S. Lukes, *Marxism and Morality* (Clarendon Press, Oxford 1985).

[24] See for example, Patent Act 1977, s.39(1).

[25] See, Z. Husami, 'Marx on Distributive Justice' in Cohen, Nagel, Scalon, *Marx, Justice and History* (Princeton University Press, Princeton 1980); J. Reiman, 'Moral Philosophy: The critique of capitalism and the problem of ideology' in T Carver, *The Cambridge Companion to Marx* (CUP, Cambridge 1991).

Moreover, this is further exacerbated by the fact that on corporate insolvency, employees are accorded a lower creditor status by the current UK insolvency laws in comparison to secured creditors such as fixed charge holders. The employees' main mode of protection during corporate insolvency is more concentrated on protecting benefits attached to their contract of employment like unpaid wages, accrued holiday, maternity and paternity holidays and pension contribution[26] by giving those rights priority status of consideration than expressly protecting the main employment from which such benefits are attached.

It should be argued that insolvency law is more concerned with debt collection and maximisation of value of returns for creditors. It does not take as paramount the protection of small or unsecured stakeholders, such as employees, as it thinks that this is the job of the state. That is why certain insolvency theories such as the CBT[27], which is pro–capitalist in the form of wealth maximisation, have continued to alienate employees from attaining equal treatment and participation in the affairs of their employer company during corporate insolvency even though employees play a big role in the economic structure of a business.[28]

Although it may be argued that capitalism contributes to economic development in our society, it however achieves this at the expense of other social factors like the welfare, equal treatment and consideration of other parties' rights to the production process such as those of employees and small trade creditors. Viewed from an analytical and economic point of view, it is worth highlighting that most normative insolvency law theories prescribe and carry with them, wealth maximisation ideals as a basis for the existence of businesses in society. These ideals are further transmitted into the corporate rescue processes such society prescribes as a means of solving corporate insolvency issues.[29]

The UK administration procedure, for example, is a 'practitioner in possession' model[30] with high levels of inclusivity of the insolvency practitioner and secured creditors who have more powers of influence in the procedure than other parties like employees. It does not give primacy to employment protection as the appointed administrator's main objective is to rescue the company as a going concern courtesy of paragraph 3(1) of Schedule B1 to the Insolvency Act 1986 (the "IA 1986"). Although a successfully executed administration procedure may lead to preservation of jobs for employees, it may be argued, job preservation is not expressly, part of the main three hierarchical rescue objectives prescribed in paragraph 3(1).

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[26] Insolvency Act 1986, Sch. 6
[27] Discussed below at 1.1.3.
[28] D. Milman, 'Priority Rights on Corporate Insolvency' in Alison Clark (ed.) *Current Issues in Insolvency Law* (Stevens, London, 1991) 57.
[29] Ibid.,
[30] See V. Finch, 'Control and Coordination in Corporate Rescue' (2005) 25(3) Legal Studies 474, 375; G. McCormack, 'Rescuing businesses: designing an "efficient" legal regime' [2009] JBL 299,330; V. Finch, 'Corporate rescue: who is interested?"[2012] JBL 190, 212.

The Marxist Normative Call for Value and Equality

To remedy this effect, according to a Marxist point of view, the state and its policy makers should abandon the capitalists' notion of taking wealth maximisation for creditors as the biggest determinant factor on corporate insolvency. They should take social analysis to aspects such as the contributory value of all parties involved in an establishment as the basis for passing laws or policies that would serve and protect equally the interests of all stakeholders.[31] Regard should be based on the questions: whose interest does the law, policy or proposal serve most? And how is a balanced approach achieved?

It should be remembered that not all parties to a contractual agreement possess the same bargaining power to press for terms that protect their interests. This highlights the need to have insolvency laws and policies that are premised on principles of fairness, equality and justice, otherwise such a regime would become the hub for powerful parties with better security to exploit the weaker ones; something which would echo the CBT's wealth maximisation ideal which is not good for employees during corporate insolvency as it would favour liquidation of the business where doing so maximises value for the creditors.[32] From the above argument, a balanced bargaining platform that values contribution, not wealth maximisation may be created. In return, a scheme of cooperation between parties based on moral equality of value input and fairness would be the solution. All stakeholder interests would be allocated equal consideration in insolvency proceedings on terms that are reasonable and fairly accepted by all interest holders.[33]

The Interpretative Theory of Law – Dworkin

There have existed many normative theories on various theoretical perspectives. However, in the field of legal theory and jurisprudence, there have existed mainly two dominant schools of thought. These are the natural law theorists and the legal positivists. The difference in these approaches is best illustrated by the famous debate between Fuller (on the natural law side) and Hart (on the positivist legal side).[34] It is worth noting that, since this debate, most legal theorists have continued to identify their theories as either being on the natural law side or the positivist legal side of this theoretical divide.

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[31] A. Buchanan, *Marx and Justice* (Methuen, London 1982).

[32] L. Ponoroff, 'Enlarging the Bargaining Table: Some Implications of the Corporate Stakeholder Model for Federal Bankruptcy Proceedings' (1994) 23 Capital University Law Review 441; Rizwaan J. Mokal, 'The authentic Consent Model: Contractarianism, Creditors' Bargain and Corporate Liquidation' (2001) 21 Legal Studies 400, 414.

[33] For a similar discourse on this point, see, Rizwaan J. Mokal, *Corporate Insolvency Law: Theory and Application* (OUP, Oxford 2005), Chapter 3.

[34] Regrettably, this debate is not discussed in this article, as it is outside its intended normative justification. However, see, H.L.A Hart, "Positivism and the Separation of Law and Morals" 71 Harv. L. Rev. 593 (1958); L. Fuller, "Positivism and the Fidelity of Law – A Response to Professor Hart" 71 Harv. L. Rev. 630, (1958).

There are mainly two particular versions of legal positivist ideals that natural law theorists argue against that have greatly contributed to this theoretical divide. Legal positivists see law as entirely comprising of rules. To them, law is the law as posited. Secondly, legal positivists, believe in the concept of judicial discretion. That is, during the course of their adjudication, if faced with legal questions (sometimes referred to as hard cases thesis) that cannot be decided on existing laws and precedents, judges must be able to draw on their discretion to fill the gap.

Among the most famous critics of these legal positivist ideals, is Professor Ronald Dworkin through his Interpretative Theory of Law.[35] Through this theory, Dworkin is seen as creating a sophisticated theory of law that can be termed as an alternative to legal positivism and natural law theories. However, it should be noted that occasionally, Dworkin has referred to his theory as a natural law theory. Moreover, viewed from the lens of the famous Fuller - Hart debate, Dworkin's theory seems to be on the natural law side of the theoretical divide.

Throughout this theory, Dworkin bases his arguments on three main ideals, which if analysed, support his interpretative approach to law as they offer normative justification for his critique of the legal positivists' ideals above on how law ought to be seen and interpreted in a given legal system or society. These ideals comprise of the "right answer" thesis (that centres upon his dissent to judicial discretion and his model Judge Hercules), law as integrity and Constructive interpretation (law as principles and rules).[36]

Through the constructive interpretative approach, Dworkin offers an approach to solving legal disputes in society through constructive interpretation. He opines that;

> "every time a judge is confronted with a legal problem, that judge should construct a theory of what the law is, that is, a theory that must adequately fit the past relevant governmental actions such as policy underlying the passing of that law to make the law the best it can be."[37]

According to Dworkin, law as practice and law as legal theory are best understood as processes of interpretation. Therefore, the judge must interpret the law in a manner that fits the legal context at hand because constructiveness in interpretation is the proper approach to artistic and literal interpretation as it coheres with the need to make the law the best it can be, carrying with it, the principles of moral value. Where constructiveness and integrity are applied in the interpretation of laws, policies and practices, it makes the laws of that society more like a product of a single moral vision. After all, a judge who accepts the interpretative ideal of integrity, decides cases

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[35] R. Dworkin, *Taking Rights Seriously* (Duckworth, London, 1977); R. Dworkin, *Laws Empire* (Cambridge, MA: HUP,1986).

[36] R . Dworkin, *Laws Empire* (Cambridge, MA: HUP, 1986), pp 46 – 48; R. Dworkin, "Pragmatism, Right Answers and True Benality" in *Pragmatism in Law and Society* (M. Brint and W. Weaver ed., Westview Press, Boulder, Colo., 1991) at 365.

[37] See R. Dworkin, *Laws Empire* (Cambridge, MA: HUP, 1986), p.52.

by trying to find, in some coherent set of principles, about peoples' rights and duties drawing on the political and legal doctrines embedded in that community or field, to find a unique "right answer" to the legal question before him, rather than using his discretion to fill the gap – a legal positivist notion that Dworkin greatly dis-contends with.[38]

Through his right answer thesis,[39] Dworkin claims that all or almost all legal questions have a unique right answer, even the hardest of cases. To achieve that unique right answer, Dworkin devises the idea of a model judge in Hercules who is seen as super judge that can have an answer to every legal question brought to him.[40] However, the idea of Hercules has been seen as one of the most controversial propositions by Dworkin in his writings on legal theory and has therefore attracted criticism.[41] Among the criticisms is the question as to whether such a judge may ever exist in reality and execute the duties put before him diligently as Dworkin posits. Criticisms put aside, the idea of Judge Hercules may be useful in the quest for novel interpretation of laws and policies in our society especially where there are no existing legal precedents from which a judge and other legal practitioners may seek guidance and direction.

Application of Dworkin's Interpretative Theory to Insolvency

It should be remembered that theories provide evaluative and analytical tools for examining legal arguments and highlighting implications that arise from such arguments. Dworkin's approach to interpretation would play a big role in informing and highlighting the need for policy justification in dealing with contentious issues on corporate insolvency. For instance, it may be argued that the failure to reach a consensus on the legitimate goal of insolvency law creates a legal dilemma (which is interpretative in nature) that is an analogy to Dworkin's "hard case thesis".[42] The lack of consensus means that a judge faced with a task of interpreting insolvency law policies, statutes or provisions must find a right answer that does not cause absurdity to either party but commands the moral justification required of it.

It may be argued that in the UK, particularly, in the field of insolvency law, there have not been specific hard cases that are analogous to Dworkin's hard case thesis that would warrant the application of the Hercules theory. This is because in the UK, as opposed to other jurisdictions like the US where there is a level of skill set for bankruptcy judges to consider, judges in the UK insolvency proceedings, do not have to ask

[38] See, R. Dworkin, *Laws Empire* (Cambridge, MA: HUP, 1986), p.255.
[39] R. Dworkin, "Pragmatism, Right Answers and True Benality" in *Pragmatism in Law and Society* (M. Brint and W. Weaver ed., Westview Press, Boulder, Colo., 1991) at 365.
[40] R. Dworkin, *Taking Rights Seriously* (London: G. Duckworth, 1977) page 85.
[41] See for instance, H.L.A Hart, "PostCript", in *The Concept of Law* (2nd ed., Clarendon Press, Oxford, 1994) at 248, 249.
[42] R. Dworkin, *Taking Rights Seriously* (London: G. Duckworth, 1977) page 85.

themselves, whether, a company faced with financial difficulties, can or should be rescued. The UK judges do not consider economic and business decisions as part of their role in adjudication. They are willing to leave these matters to experts in these particular fields such as insolvency practitioners and business experts.[43]

Moreover, Dworkin's hard case theory is more judge focused and UK insolvency law is more insolvency practitioner focused and therefore, there is a high level of contrast. However, what can be drawn from Dworkin's Hercules and hard case theses, is the ability to analyse the administrator's role and capacity to discharge his duties in a manner that is analogous to that of a judge. This is supported by the fact that Schedule B1 to the IA 1986 which deals with administration proceedings, is about how the administrator thinks. The level of expectation from an administrator (especially in deciding which rescue objective would serves the interests of creditors as a whole) during insolvency proceedings, is analogous to that of Hercules presiding over a hard case as posited by Dworkin.

The administration procedure is largely controlled and driven by the administrator as he is afforded significant powers to exercise his discretion.[44] Upon appointment, the administrator is tasked to perform his duties in the interest of all creditors of the company as a whole.[45] Among the hierarchy of objectives to be pursued, the main objective is to rescue the company as a going concern.[46] However, it should be noted that, while rescuing the company as a going concern is the main objective to be pursued by the administrator, this objective may not be pursued by the administrator where he thinks that such an objective cannot be reasonably and practically achieved, or where he thinks that doing so would not serve or achieve the best interest for creditors as a whole.[47] It may be submitted that this amounts to a high level of decision making power afforded to the administrator, which analogously places him within the ambit of judge Hercules as posited by Dworkin.

Moreover, the administrator, being the person in charge of rescue proceeding, it may be argued, is well positioned to judge as to whether a particular objective, if pursued, would be successful and in the interest of all stakeholders. This may be partly, based on his level of expertise in that particular field and his professional judgement. What this implies is that, the threshold or test applicable in this situation is what the administrator *thinks* as opposed to what he *reasonably believes*.[48] With such decision making powers and high level of expectation, if an administrator decides for example, that disposing of business assets or laying off some employees

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[43] See the House of Lords debate to this effect; Hansard, HL Deb, vol. 638, col.768 (29 July 2002).
[44] See, particularly, IA 1986, Sch. B1.
[45] IA 1986, Sch. B1, Para.3(2).
[46] IA 1986, Sch. B1, Para. 3(1)(a).
[47] G. McCormack, "Control and Corporate Rescue – An Anglo –American Evaluation" (2007) Int'l & Comp. L. Quarterly 56(3), 515 – 551.
[48] R. Mokal and J. Armour, "The New UK Rescue Procedure – The Administrator's Duty to Act Rationally" (2004) 1 International Corporate Rescue 136.

would achieve a better outcome for company creditors as a whole, or preserve the going concern value of the business, such a decision will stand. Although some scope exists for aggrieved creditors to challenge an administrator's judgment[49] and sometimes such challenges are upheld by courts,[50] it should be noted that an administrator's judgment formed in good faith, may be very difficult to challenge, due to the level of regard accorded him by the law and judges.[51]

The need for constructiveness and integrity in interpretation of hard cases on the part of the administrator may be illustrated by the Court of Appeal decision in *Re Huddersfield Fine Worsteds Ltd and Re Ferrotech Ltd & Granville Technology Ltd*.[52] In that case, the Court of Appeal was asked to determine whether, liabilities for protective awards and payments in lieu of notice, to employees of a company in administration, whose contracts of employment have been adopted by the administrator, would be interpreted within the scope of "wages or salary" pursuant to paragraph 99(4)–(6) of Schedule B1 to the IA 1986.

Another practical importance of this case was that, the Court of Appeal had to hear this case at short notice as the following day (10th August 2005) the 14 day period since one of the companies involved in this litigation (Granville Technology Ltd) had entered into administration, was due to expire. This had the effect that the administrators of this company had to decide whether or not to adopt the contracts of employment of over 150 employees, depending on the outcome of the case.

Although this may not be categorised as a hard case *per se*, it may be argued, that the level of technicalities encountered in interpreting legal and policy provisions around paragraph 99 above, draws it closer to what Dworkin would term as a hard case upon which an administrator's and a judge's ability to adopt a novel interpretative approach to finding a fair and balanced answer may be drawn.

A protective award arises under s.189 of the Trade Union and Labour Relations (Consolidation) Act 1992 (the "1992 Act"), where by virtue of s.188 of the 1992 Act, an employer has failed on the obligation to hold consultations with employees in a case where more than 19 employees are to be dismissed by reason of redundancy unless there are special circumstances that render such consultations not reasonably practicable.[53] A payment in lieu of notice arises where, either with express or implied agreement, an employer either gives proper notice of termination of employment to the employee or the employer summarily dismisses the employee and tenders a payment in lieu of proper notice as such action would amount to a breach of contract of employment.[54]

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[49] IA 1986, Sch. B1, Paras.74 and 88.
[50] See for example, *Clydesdale Financial Services v Smailes* [2009] EWHC 1745 (Ch.)
[51] V. Finch, 'Re-Invigorating Corporate Rescue' [2003] J.B.L 527, 546.
[52] [2005] EWCA Civ. 1072.
[53] See the reasoning in *Re Hartlebury Printers Ltd* [1993]BCLC 902.
[54] See the four principal categories of payments in lieu of notice as set out by Lord Browne – Wilkinson in *Delaney v Staples* [1992] 1 AC 687, at 692D – H.

In *Re Huddersfield*[55], Peter Smith J had given judgment on 27 July 2005 that protective awards and payments in lieu of notice were paid in priority to administration expenses. However, on 9 August 2005, Etherton J, gave a judgment that both protective awards and payments in lieu of notice were not payable in priority to administration expenses in respect of two different companies in the *Re Ferrotech Ltd and Granville Technology* case.[56] These two conflicting first instance decisions led to this appeal.

By virtue of paragraphs 99(5) and 99(4), priority status applies to liabilities arising under a contract of employment which was adopted by the former administrator or predecessor. However, paragraph 99(5)(c) states that no account is taken of a liability to make a payment other than for wages and salaries. Under paragraph 99(6), wages and salaries include among other things, holiday pay and sick pay. However, the challenge in interpretation mainly centred on the interpretation of paragraph 99(6)(d) and paragraph 99(5)(c). Paragraph 99(6)(d) states:

> "in respect of a period, a sum which would be treated as earnings for that period for the purposes of an enactment about social security."

Interestingly, the Court of Appeal had to listen to four versions of interpreting this sub paragraph from each of the legal teams and the Attorney General during this case. However, more interesting, is the fact the Court of Appeal was not prepared to accept the submission of the Attorney General that the problem of interpretation before the court was as the result of a drafting error. Secondly, the test to ascertain whether protective awards or payments in lieu of notice are payable in priority to administration expenses, centred on two conditions being satisfied in paragraph 99(5):

- That the liability arose out of a contract of employment.
- That the liability fell within the category of 'wages and salaries.'

In the judgment (delivered by Lord Neuberger), the Court of Appeal allowed the appeal of the administrators against the decision of Peter Smith J in *Re Huddersfield*, holding that protective awards and payments in lieu of notice were not payable in priority to administration expenses and upholding the decision of Etherton J in the *Re Ferrotech Ltd and Granville Technology* case.

The judges opined that analysing both issues involved establishing a gateway and if the gateway was correct, protective awards would not enjoy super-priority because they could not be described as liabilities arising under a contract of employment, but were liabilities that no doubt arose because of the existence of a contract of employment.[57] Notably, the judges opined that:

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[55] [2005] EWCA Civ. 1682 (ch).
[56][2005] EWCA Civ. 1072.
[57] See paragraph 17 of the judgment.

> ".. ..the argument involved giving the words "arising under" in paragraph 99(5), their ordinary and natural meaning, the notion that such expression should not be given an artificially wide meaning…"[58]

Therefore, it may be argued that benefits and interests such as wages, salaries protective awards and so forth, are given recognition by the existence of a contract of employment. There is sense in the argument that policy considerations (especially, of the need to promote the rescue culture during corporate insolvencies) were pivotal in overruling Peter Smith J's judgment in *Re Huddersfield*. There is even more sense in the argument that, allowing protective awards and payments in lieu of notice to be paid in priority over administration expenses would make adoption of employment contracts by administrators substantially costly and burdensome to rescue attempts. However, the judgment in *Re Huddersfield* would be favourable to employees.

This case highlighted the extent to which the courts may be prepared to analyse what the legislature intended in passing this legislation. This is the interpretative approach, that carries with it the integrity and novelty in exploring extant legal rules and principles to derive at a unique right answer that Dworkin posits, in the manner of Hercules and which by extension, an administrator should arguably adopt. Similarly, the case of *DKKL Solicitors v H M Revenue & Customs*[59] further highlights the level of expertise and impartiality expected of administrators in their administration of insolvent but viable businesses. The decision further gives clear indication that judges still vest great reliance on the expertise and perhaps impartiality of administrators.[60]

In this case, an insolvent law firm of solicitors trading as a limited liability partnership made an application for an administration order for the financially struggling law firm, to be sold as a pre-packaged business to a newly incorporated limited liability partnership – Drummond Kirkwood LLP. The law firm was deeply in debt, totalling over £2 million pounds, and the largest creditor, HM Revenue and Customs was owed in excess of £1.7 million pounds. HM Revenue and Customs objected to the application for the administration order and instead, filed a petition for a winding up order against the law firm. As the majority creditor, H M Revenue and Customs were convinced that they would defeat the administrators' proposals if put before a creditors' meeting. However, the creditors' meeting was not convened due to the fact that the proposals in the application for the administration order were for the sale of the partnership business as a pre-pack.

Due to the nature of debt faced by the partnership business, the possibility of rescuing the partnership as a going concern would be practically impossible, therefore, the most viable objective was for the administrators to pursue the second objective of administration in paragraph 3(1)(b) of schedule B1 to the IA 1986. The court, in

[58] Ibid.,
[59] [2007] BCC 908 (Ch).
[60] Bo Xie, 'Protecting the Interest of General Unsecured Creditors in Pre-packs: The Implication and Implementation of SIP 16' (2010) 31(6) Company Lawyer, 189 -195.

considering whether or not this objective, as indicated in the statement of affairs presented by the proposed administrators, would be achievable, placed great reliance on the expertise and experience of the proposed administrators in granting the administration order.

Although it may be argued that the court, in considering its decision, was again influenced by policy considerations of saving the jobs of fifty employees, this is the decision that further highlights the over-reliance of judges on the professional expertise of administrators. Moreover, even if major creditors (H M Revenue & Customs) were to veto the administrators' proposals in creditors' meeting, the court may still ratify those proposals under paragraph 55(2) of Schedule B1 to the IA 1986.

Therefore, to Dworkin, through his right answer thesis, the administrator, due to the level of impartiality and expertise expected of him in exploring the available legal rules and principles embedded in the legal system, should be able to find the right answer, approach or objective to adopt in pursuing the rescue operations of the company. This may be done, especially, where such an administrator constructs a theory of what the law is, a theory that adequately fits the past relevant governmental action, such as a policy underlying the passing of the such laws, in this case, the IA 1986, without using his discretion to fill the gap, which may turn up to be detrimental to the interest of other stakeholders in the insolvent company.

To Dworkin, a theory that is built on the principles of fairness, equality and justice, can set moral standards or obligations that would be meaningfully tested in pursuing stakeholder interests during corporate insolvency. In return, the standard of morality or moral obligation expected of parties in dealing with each other in contractual arrangements would be justified. If, for instance, one stakeholder selfishly sets out to maximise his interest against the interests of other stakeholders, his intentions or reasons for doing so must be publicly tested and justified as being for fair and just intentions, not against the interests of others *per se*.

The Creditors' Bargain Theory

The CBT was developed by Jackson in the early 1980s[61] and partly in collaborative writings with Baird[62] and Scott.[63] The CBT is a contractarian theory in nature as it carries with it, some theoretical underpinnings of the Law and Economics movement.[64] It is

[61] Thomas H. Jackson, 'Bankruptcy, Non-Bankruptcy Entitlements and the Creditors' Bargain, (1982) 91 Yale Law Journal 857, 860; Thomas H Jackson, 'Avoiding Powers in Bankruptcy' (1984) 36 Stan. L. Rev. 725; Thomas H. Jackson, '*The Logic and Limits of Bankruptcy Law* (HUP, Cambridge, MA 1986).

[62] D. Baird & T. H. Jackson, 'Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy' (1984) 51 U Chicago L. Rev. 97.

[63] T. H. Jackson & R. Scott, 'On the Nature of Bankruptcy: An Essay on Bankruptcy Sharing and the Creditors' Bargain (1989) 75 Virginia L. Rev. 155.

[64] This is based on the "round table" discussions by leading scholars in the law and economics field including Richard A Posner, Ronald Coarse, Thomas Jackson, Douglas Baird among others. See, D G

premised on the notion of wealth maximisation, an ideology that insolvency law exists to maximise the collective interests or value for creditors on corporate insolvency. The theory is based on a hypothesis that creditors bargain with the debtor company during negotiations for credit and establish their position and remedies upon default by the company, such as on insolvency. Therefore, to the jurisprudence of the CBT, when a company goes into formal insolvency, several creditors with interests in it will try to recover their debt from the company. There will be a race against time for each creditor to recover their debt.

Because of the panic from these creditors, the assets of the company may be impounded or attached by creditors on a self–help "first come first served basis." However, this approach is usually dominated by selfish interests, especially from strong and secured creditors or those with preferential status that either arises out of statute, or is granted through pre-insolvency private contractual agreements.[65] However, not all creditors may be able to recover their debts on a self–help approach, as different creditors may have different enforcement rights against the debtor company, depending on their pre-insolvency contractual agreements.

Secured creditors, such as banks or qualifying floating charge holders, may have more enforcement rights against the debtor company than general unsecured creditors. The race by these creditors to pursue individual claims or interests against the debtor company creates other problems, such as costly litigation expenses. Moreover, other stakeholders may gain advantage unfairly, through having better information or stronger enforcement tactics, which may present more of a problem than the presence of secured creditors, who would be paid first anyway.

All of these shortcomings may cause depreciation in value to business assets which creates uncertainty of returns to all creditors and may turn out to be administratively inefficient.[66] To the CBT, the solution to these problems is to replace the individual enforcement approach with a collective regime which will enable all creditors to take part in a collective debt recovery scheme,[67] in accordance with pre-existing priorities. The debtor's business assets may be regarded as a pool of assets from which debts will be satisfied. The CBT claims that a collective and regulated formal scheme of asset distribution to creditors, rather than piecemeal liquidation of company assets, would

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Baird, "The Future of Law and Economics: Looking Forward" 64, *University of Chicago Law Review* 1129.

[65] Douglas G. Baird, 'A World Without Bankruptcy' (1987) 50 Law & Contemp. Probs. 173; B. E. Adler, 'A World Without Debt' (1994) 72 Wash. U. L. Q 811 – 827.

[66] D. Baird & T. H. Jackson, 'Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy' (1984) 51 U Chicago L. Rev. 97.

[67] M. Olsen, *The Logic of Collective Action: Public Goods and The Theory of Groups* (HUP, 1971) 2.

preserve the company's net asset value.[68] Viewed from the lens of business rescue and employment protection, formal asset disposal would be less costly and would enhance the going concern value of the business which, if successfully bought by a new owner, would save jobs for the employees.

However, it should be noted that collectivity in asset distribution may require the application of the insolvency law principle of redistribution, a move that the CBT is strongly opposed to. Redistribution involves the alteration of pre-insolvency entitlements, or the transfer of an interest from one creditor to another, to honour that creditor's interest on corporate insolvency.[69] The CBT and its proponents see this as a move that is unfair if the wealth of another creditor, who assumed the risk to invest in the debtor company, is altered or reduced to honour the claims of another creditor who would otherwise not be entitled to a redistributive interest. This is because the CBT and its proponents perceive insolvency as a foreseeable risk that can be assumed individually in a given business transaction.

Under the CBT, insolvency should be seen as any other financial risk that a creditor assumes by choosing to invest in the business. Therefore, the CBT does not support redistribution in insolvency. This theory supports the view that insolvency law should consider all the debtor company's pre-insolvency held interests as it finds them.[70] However, the counter argument to this point of view is that, although some pre-insolvency interests are negotiated and agreed in private contractual agreements, other interests arise out of statute for example; the claims of tort victims and government tax authorities who are unable to diversify risks or equity.[71] Where this is the case, courts of law or equity may be obliged to modify or make alterations to pre-insolvency contractual arrangements where it is just and equitable to do so.[72]

The CBT on Employment Protection

In any production or service industry, employees are closely involved with the operations of the company business. They play a big role in the means of production or service delivery compared to other interest holders like trade suppliers. Without employees, the production process may be severely disrupted as employees with equivalent skills or knowhow may not easily be sourced elsewhere and replaced at short

[68] Thomas H. Jackson, 'Bankruptcy, Non-Bankruptcy Entitlements and the Creditors' Bargain, (1982) 91 Yale Law Journal 857, 860; Thomas H. Jackson, 'Avoiding Powers in Bankruptcy' (1984) 36 Stan. L. Rev. 725; Thomas H. Jackson, '*The Logic and Limits of Bankruptcy Law* (HUP, Cambridge, MA 1986).
[69] J. Armour, 'Should We Redistribute in Insolvency?' (2006) Centre for Business Research, University of Cambridge Working Paper No. 319 (accessed online at http://www.cbr.cam.ac.uk/pdf/WP319.pdf) (last accessed October 2015).
[70] Y. Rotem, 'Pursuing Preservation of Pre-Bankruptcy Entitlements: Corporate Bankruptcy and Law's Self Executing Mechanisms' (2008) 5 (1) Berkley Business Law Journal, 79, 90.
[71] David G. Carlson, 'Rationality, Accident and Priority under Article 9 of the Uniform Commercial Code' (1986) 71 Minn. L. Rev.207.
[72] M. Bruckner, 'The Virtue in Bankruptcy' (2013) 45 Loyola University Chicago Law Journal 233, 234 – 35.

notice, where as other interest holders, such as trade suppliers may often be easily changed with minimal disruption to production or service delivery.[73] Their contribution to the business deserves fair recognition. Employees should not merely be classed as ordinary creditors on corporate insolvency since without their input in the production process or service delivery, the end product may not be achieved. This is one of the objectives that legislators and policy makers should seek to balance during stakeholder interest consideration during corporate insolvency.[74]

The CBT advocates a collective approach, rather than a self–help approach as the best mechanism in pursuing interests amongst creditors during the insolvency of the debtor company. Viewed from the context of the UK insolvency laws and corporate rescue processes such as administration, it may be submitted that the administration procedure is in line with this normative argument based on the CBT. It is the argument that during the insolvent state of the company, creditor primacy prevails against other interests. This is also evident in the legislative provisions of the IA 1986 setting out the hierarchy of objectives to be pursued by the administrator.[75] It is arguable that all three hierarchical objectives, carry with them the ultimate objective of recovering the interests of the aggrieved stakeholders.

However, collectivity in pursuing stakeholders' interests, as advocated for by the CBT, does not enhance employee protection during insolvency proceedings as employees are not given a special class in recognition of their special status. Moreover, current UK insolvency law and corporate rescue processes such as administration and company voluntary arrangements as well as administrative receivership still recognise employees as general unsecured creditors. It is the notion that for collectivity to be fully embraced, employees as the providers of labour, should arguably be viewed on the same platform as capital providers, after all, a combination of capital and labour are the two main factors of production or service delivery in any given market economy.[76]

In addition to the above, the CBT is premised on a hypothetical contract. Creditors are the parties to this hypothetical contract which is agreed under a veil of ignorance.[77] Although the bargain under the CBT is reached without regard to self-interest and therefore, objectively justifiable, there exists a lack of actual consent from parties to agree to contractual terms or conditions that would form a collective approach to pursuing collective over selfish interests. Therefore, the CBT's argument for a collective and mandatory regime may be seen as being coercive to the stakeholders with legal

[73] Karen Gross, *Failure and Forgiveness: Rebalancing the Bankruptcy Systems* (Yale Univ. Press, New Haven 1997) 19.
[74] L. Ponoroff, 'Enlarging the Bargaining Table: Some Implications of the Corporate Stakeholder Model for Federal Bankruptcy Proceedings' (1994) 23 Capital University Law Review 441.
[75] See, IA 1986, Sch. B1, Paragraph 3(1).
[76] See K. Marx, 'Capital: *A Critique of Political Economy Volume 1:The Process of Capitalist Production* (Samual Moore and Edward Avelling trans.) F. Engles and E. Untermann ed. (Chicago: C H Kerr & Co, 1990) Ch. 1; D. Milman, "Priority Rights on Corporate Insolvency" in Alison Clark (ed.), *Current Issues in Insolvency Law* (London: Stevens, 1991), P.57.
[77] J. Rawls, *Political Liberalism* (New York: Columbia University Press, 1996).

interests against the debtor company. For collectivity to be fully observed in this respect, there would be a need to give all stakeholders a voice or participation right in the decision-making process to enforce their interests.[78] For employees, it is envisaged that collectiveness would give them a chance to be involved in the actual rescue decisions or processes of their insolvent employer but in reality, CBT does not extend this to employees.

Viewing the UK administration rescue procedure under the lens of the CBT approach, the procedure may be regarded as a collective and inclusive recue process. It requires the administrator to serve the interests of all company creditors as a whole[79] but in reality secured creditors often benefit more from this provision than employees due to different levels of security held over the other. Interesting to note, is the fact that the CBT limits stakeholder participation in pursuing interests to only those with legal rights against the debtor company's assets. Stakeholders without express contractual entitlements but who mainly rely on implied rights or goodwill only have their rights or interest considered where they would add value and maximise the going concern value of overall returns to creditors. This makes the CBT a narrow theory in its approach to stakeholder interest consideration. Therefore, insolvency laws and policies modelled on the jurisprudence of the CBT would not recognise the special status of employees and so they would be less protective of employees.

The Team Production Theory of Bankruptcy Reorganizations (TPT)

TPT was developed by Professor Lynn LoPucki.[80] The theory owes its origin to the team production theory of corporate law which was developed from the economics literature on team production and corporate governance.[81] It was based on the ideology that the main purpose or economic goal of the firm is to maximise shareholder interests.[82] This is the ideology that LoPucki moves away from and develops into a theory to analyse bankruptcy reorganizations on the ideology that shareholders are not the only

[78] M. Frank, 'The Rights of Employees in the event of their Employer's Insolvency: A Comparative Approach to the Rights of Employees During Restructuring in the United States and Europe' (2005) 1 New Zealand Postgraduate Law E-Journal 7.
[79] IA 1986, Sch.B1, para.3(2).
[80] Lynn M. LoPucki, 'A Team Production Theory of Bankruptcy Reorganizations' (2003) UCLA Law School Research Paper No. 3 -12. (available at http://ssrn.com/abstract=397801). (Last accessed on 5 December 2015).
[81]A. A. Alchian and H Demsetz, 'Production, Information Costs and Economic Organizations (1972), Am Econ. Rev.777; M M Blair and Lyn A Stout, 'A Team Production Theory of Corporate Law'(1999) 85 Virginia L. Rev. 247.
[82] D. Millon, 'New Directions in Corporate Law: Communitarians, Contractarians and the Crisis in Corporate Law' (1993) 50 Washington & Lee L. Rev. 1373; L Fairfax, 'The Rhetoric of Corporate Law: The Impact of Stakeholder Rhetoric on Corporate Norms' (2006) 31 Journal of Corporation Law 675, 676; G Crespi, 'Maximizing the wealth of Fictional Shareholders: Which Fiction Should Directors Embrace' (2007) 32 Journal of Corporation Law, 383, 386.

party that contributes to the production process of a firm but other parties, such as trade suppliers and employees, all provide combined input to get the end product.[83]

TPT is built on the ideology that a production firm is a combination of team members who join resources together in a production process to achieve an end product. Under the TPT, without joining resources, a single party or unit cannot produce the end product on its own. Therefore, the end product belongs to all parties to the production process.[84] Because of this, the TPT supports the view that all parties to the production process should be able to embrace insolvency as a contractual term voluntarily, as it affects all as a team in a production unit. Their interests on corporate insolvency should be considered as part of a group, not as one stakeholder with priority status over the other.

Under the TPT, it is through mutual trust that all team members vest their legitimate interests in the board of directors of the company to decide how best to promote the fortunes of the company business. TPT is premised on actual contracts negotiated and entered into by all team members, a move away from the hypothetical contract model that the CBT is based on. Through this, reorganisations of the company business may be achieved through collective team agreements where this benefits team members as a group, in contrast to liquidation of company assets to the primary benefit of some secured creditors. Viewed from this context, collective restructurings, such as the closure of underperforming sections or units of the firm may be supported where it would benefit team members as a group and enhance the going concern value of the business.[85]

TPT is a theory that promotes inclusivity of all team members during insolvency proceedings. It supports the view that, apart from actual or physical contributions made by team members in a production unit, other non-physical contributions based on experience or job specific skills contribute to the enhancement of the going concern value of the company. Where liquidation of company assets is inevitable and accepted by all team members, TPT would support redistribution of some of the interest of one team member to another, as a means of fulfilling its obligation to its team members in contrast to the non-redistributive ideology that the CBT supports.

The TPT being an inclusive theory, advocates honouring all team members' interests on the insolvency of the company, whether in terms of financial gain or losses.[86] Therefore, as much as team members would benefit from the financial distributional gain in insolvency, losses should also be distributed amongst all team members, even if it

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[83] Lynn M. LoPucki, 'A Team Production Theory of Bankruptcy Reorganizations' (2003) UCLA Law School Research Paper No. 3 -12. (available at http://ssrn.com/abstract=397801). (Last accessed on 5 December 2015); M. Blair, *Ownership and Control: Rethinking Corporate Governance For The Twenty First Century* (The Brookings Institute, Washington DC, 1995).

[84] A. A. Alchian and H. Demsetz, 'Production, Information Costs and Economic Organizations' (1972), Am Econ. Rev.777.

[85] M. Blair and Lyn A. Stout, 'A Team Production Theory of Corporate Law'(1999) 85 Virginia L. Rev. 247

[86] J. Armour, 'Should We Redistribute in Insolvency?' (2006) Centre for Business Research, University of Cambridge Working Paper No. 319 (accessed online at http://www.cbr.cam.ac.uk/pdf/WP319.pdf) (last accessed October 2015).

would involve alterations to pre-insolvency entitlements from one member to another. Redistribution under the TPT, is a form of honouring the commitments made between the company and the team members, basing on pre-insolvency obligations.

Employees under TPT Employment Protection

The TPT is a theory that supports consideration of interests of all team members on the insolvency of the company. The theory supports the view that equal weight of consideration be given to all team members' interests without giving more weight to certain class team members, such as secured ones over others. Therefore, corporate insolvency policies built on this ideology would benefit employees more, as their interests on the insolvency of their employer company would be given equal weight of consideration, like those of other stakeholders.[87]

Moreover, their non-contractual rights, interests and expectations, such as the continuity of employment from the employees' point of view would be considered as relevant and deserving of protecting in an insolvency regime modelled on the normative principles of the TPT. This is supported by the argument that the TPT theory is built on the notion of maximising the welfare of all interest holders as a team, as each team member's input in the production or service delivery unit is considered relevant to achieving the end product or goal.

Due to the collective nature of the TPT, it is assumed that collective decision making on issues or policies that would enhance the going concern value of the company would be reached easily. Because there would be no panic among team members to race against time to extract selfish and readily realisable interests from the assets of the company, unnecessary liquidation of company assets on a piecemeal basis would be avoided. This would give the company a chance to continue trading out of its financial difficulties, rehabilitated and perhaps sold as a going concern. This would be beneficial to employees, as some jobs may be saved and the chain of continuity of employment may be preserved.

In addition to the above, corporate insolvency policies built on the principles of the TPT theory would support going concern sales of insolvent but viable businesses, such as those under the current UK employment law protective provision in the Transfer of Undertakings Protection of Employment Regulations 2006 ("TUPE"). A going concern business sale or transfer would preserve the continuity of employment through automatic transfer provisions under regulation 4 of TUPE and the prohibition on terminating employment contracts without just cause by employers, merely to make insolvent business sales attractive, in regulation 7 of TUPE. These provisions would be supported by a TPT generated insolvency law regime.

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[87] Bruce G. Carruthers & Terrence C. Halliday, *Rescuing Business: The Making of Bankruptcy Law in England and the United States* (OUP, Oxford 1998) 303.

Conclusion

In conclusion, it is worth noting that the application of laws and policies modelled on the normative conception of pure insolvency–specific theories has so far failed to achieve a balanced platform for dealing with stakeholder interests on corporate insolvency. A consensus on the central question of insolvency law, that is, whose main interest should insolvency laws and policies give priority on corporate insolvency, is yet to be achieved. This may partly be borne in the argument that insolvency law is more focused on creditors getting their money back in a procedural way. It does not largely, carry with it social aspects such as protecting employees or the environment.

Drawing on the normative arguments discussed above, it may be argued that the application of Marxist legal theory that advocates for a balanced *labour–value* approach and Dworkin's interpretative approach to interpreting legal rules, policies and principles in a manner that carries with it ideals such as justice and fairness, may help balance the bargaining platform. It should be remembered that competing policy goals of rescuing insolvent but viable businesses and those of protecting and promoting employment are not totally incompatible. Where business rescue is pursued successfully, it saves jobs and promotes continuity of employment. However, the problem arises where the objective of rescuing businesses conflicts with the objective of protecting employment. This is because both objectives are difficult to achieve simultaneously; rather a compromise must be made. But this would be achievable through an interpretative approach to laws and policies that accords, to all stakeholders, a seat on the bargaining table.

Such a contentious issue as redistribution in insolvency would require a novel interpretative approach if equal regard to all stakeholder interests is to be achieved fairly. It would require the application of the principles of "moral value" and "fit" criteria as posited by Dworkin's interpretative approach to law, as it is a practice that the CBT and its proponents are so opposed to. CBT theorists view redistribution as an act of theft from one creditor to make the other happy in that, altering their entitlement to redistribute to another creditor would be seen as rendering their pre-insolvency entitlements ineffective.[88]

Although some claims and entitlements arise out of contractual arrangements, some arise out of statute.[89] For example, as mentioned above, involuntary creditors such as tort victims and tax authorities who never chose to be in the position they find themselves in, would require protection. Therefore, although some contractual arrangement may entitle certain class creditors, such as secured creditors or holders of qualifying floating

[88] Yaad Rotem, 'Pursuing Preservation of Pre- Bankruptcy Entitlements: Corporate Bankruptcy and Law's Self Executing Mechanisms' (2008) 5(1) Berkeley Business Law Journal 79, 90.

[89] R. J. Mann, 'Bankruptcy and the Entitlements of the Government: Whose Money is it anyway' (1995) 70 (5) New york University Law Review 1040; Y Rotem, Pursuing Preservation of Pre-Bankruptcy Entitlements: Corporate Bankruptcy and Law's Self Executing Mechanisms' (2008) 5 (1) Berkeley Business Law Journal 79, 84.

charges, to certain levels of protection and entitlement during insolvency, pursing these claims and entitlements may be unconscionable or unjust to the rights and entitlements of other class creditors, who also offer other forms of contribution to the company business that enhance its going concern value. Following Dworkin, the "moral value" and the "fit" criteria of interpretation would play a big role in evenly recognising the contribution of various parties to the company business,[90] a move that both Marxist legal theory and TPT would happily support.

In light of the current rescue processes such as administration and pre-pack business sales in the UK, both Dworkin and Marxist ideals would help to inform and influence the need for law and policy makers to address contentious issues being raised against these recue processes. For instance, although pre-packs have been credited for offering the best chance for more business rescue, maximising returns and value for creditors and saving jobs,[91] ethical and social issues such as disenfranchisement of minor trade and general unsecured creditors like employees, secrecy in the dealings that lead up to the sale of the business and phoenix practices, among others, still need addressing.[92]

Moreover, there are engaging debates on what the main aim of pre-pack business sales in the UK is and it is arguably, to maximise value or returns to creditors on corporate insolvency[93] against other objectives such as employment protection. Stakeholders with interests in the debtor company would not be arguing against pre- packs if they maximised every stakeholder's wealth or served every stakeholder's interest fairly where doing so was on a fair and equal level of involvement for all, especially in the operation and decision making process.

There is still huge concern that because pre-packs are generally agreed in consultations with secured creditors such as banks, company directors and sometimes the management, they take the interests of the directors or management and secured creditors ahead of general unsecured stakeholders like employees. Moreover, the nature of secrecy involved and the speedy sale of the business often leave employees not consulted or informed of the sale on time.

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[90] R. Dworkin, "Pragmatism, Right Answers and True Benality" in *Pragmatism in Law and Society* (M. Brint and W. Weaver ed., Westview Press, Boulder, Colo., 1991) at 365.

[91] Insolvency Service, "Enterprise Act 2002 – Corporate Insolvency Provisions: Evaluation Report" January 2008, 147,available at www.insolvency.gov.uk/insolvencyprofessionandlegislation/legislation/EA02CorporateInsolvencyReport.pdf (accessed on 10/01/2016).

[92]M. Herman, "Abuse of pre-pack deals 'Could turn Britain into an insolvency Brothel'" *Times* 18 January 2010 at 36.

[93] P. Walton, 'When is Pre-packaged Administration Appropriate? – A Theoretical Consideration' (2011) 20 Nott. L. J. 12; A. Kastrinou, "An analysis of the pre-pack technique and recent developments in the area" (2008) 29(9) *Company Lawyer* 259, 263; V. Finch, Corporate Rescue: a game of three halves, legal studies, (2012) 32(2) pp.302 – 324.

Although Statement of Insolvency Practice ("SIP 16") requires that general unsecured creditors are consulted and informed of the terms and the reasons as to why the pre-pack was chosen as the most effective rescue procedure, they usually receive this information after the business sale is completed. At this point, practices such as a phoenix sale of the business may have been exercised but not challenged. This raises questions as to whether the market was effectively explored to ascertain best offer for the business. Open marketing of the business may have been avoided due to the speedy and secretive nature of pre-packs yet ethical issues, especially on the transparency and open marketing of the business are heavily emphasised by SIP16.[94]

In order to balance the interests of all stakeholders during corporate insolvency, principles of fairness, equality and justice, have to be adopted by law and policy makers to achieve the level of moral obligation of those applying the law, either in adjudication or overall enforcement to achieve collectivity and inclusion.[95] This is the moral obligation borne with fairness, equality and justice that entices parties to enter into contractual agreements. The main goal of insolvency law would be to fairly and equally allocate resources or returns to all stakeholders based on these ideals.

An insolvency regime whose laws and policies are not built on the notions of fairness, equality and justice in consideration to value (contribution) would defeat the aims the laws set out to achieve in that jurisdiction. This would defeat the Cork Committee's vision that the basic objective of insolvency law is "to support the maintenance of commercial morality and encourage the fulfilment of financial obligations."[96] Therefore, in order to achieve collectivity, the interests of all parties including other constituents like employees must be consistently pursued collectively and reasonably in line with other secured creditors such as banks and insolvency practitioners.

Therefore, insolvency regimes built on the principles of fairness, equality and justice of inclusion and consideration of interests would inform and influence policy makers to treat all stakeholder interests fairly irrespective of whether those stakeholders have a direct or non- direct financial interest in the company business. Through the normative theories discussed above, legislative bodies and policy makers of a state are able to evaluate and analyse laws and policies and their impact on the economic and social welfare of the businesses and parties connected with them.

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[94] See, "The market for corporate insolvency practitioners: A market study" June 2010 (OFT1245) available at *http/www.oft.gov.uk/shared_oft/reports/insolvency/oft1245*. (last accessed October 2015); M. Ellis "The Thin Line in the Sand – Pre-Packs and the Phoenixes" Spring (2006) *Recovery* 3.

[95] J. Rawls *A Theory of Justice* (Revised edition) (Oxford University Press, 2009); R Mokal, *Corporate Insolvency Law: Theory and Application* (Oxford University Press 2005) at 61, 62.

[96] Insolvency Law and Practice: Report of the Review Committee (1982) cmnd 8558, para. 191.