

**THE SUSPENSION OF PAYMENT INSTITUTION
UNDER THE DANISH BANKRUPTCY ACT, 1977**

BY

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1. INTRODUCTION¹

The object of the rules governing suspension of payment, which were introduced into Danish law in 1975, and which are now codified in ch. 2 of the Danish Bankruptcy Act, 1977, is to improve the possibilities of avoiding bankruptcy in favour of a voluntary agreement for the payment of the debts (the Danish term for bankruptcy is “konkurs”, and according to Danish law the terms “bankruptcy”, “bankrupt”, and “debtor” are applied both to individuals, partnerships, private companies and limited liability companies). Naturally, it would be ideal if suspension of payment could lead to a reconstruction of the debtor’s business, but the Suspension of Payment Institution is also intended to be a facility instrumental in the winding up of a business in connection with a settling and reduction of the debts of the debtor (the terms “winding up” and “liquidation” are used in this paper in the sense of “dissolution of debtor’s business”).

It has not of course been the intention that the suspension of payment should be used as a means of producing a calmer atmosphere for the winding up of a business without settling and reduction of the debts of the debtor. Even so, there is no doubt that a notice of suspension of payment is actually used to a certain extent to secure winding up without composition. The explanatory notes on a proposed amendment submitted by the Minister of Justice during the reading of the final Bankruptcy Act in the Folketing (Danish Parliament) contain the following passage:

During the period in which the rules governing suspension of payment have been in force, practice has shown that the rules are often applied to create a calm and peaceful atmosphere for the winding up of the debtor’s business.²

A normal jurisprudential examination may help to explain why the rules can be used contrary to their object, but it cannot show, of course, to what extent the rules are so used. In consequence of the economic crisis the Suspension of Payment Institution is used to quite a considerable extent in practice, and so the obvious path to take—as a supplement to the theoretical analysis of the contents and historical conditions of the rules— was to

¹ The present paper is based on my book, *Betalingsstandsning*, Copenhagen 1979.

² Cf. *Folketingstidende* 1976/77, 2nd session, supplement B, column 582.

undertake an empirical investigation. The investigation covered the Maritime and Commercial Court in Copenhagen, the City and District Court of Århus, the Town Courts of Holbæk and Høstebro, and the Town Court of Svendborg, and was limited to the cases of suspension of payment notified in the period from August 1, 1977, to July 31, 1978. The investigation comprised a total of 308 cases.

This cross-section is presumably representative of the whole country and of the whole of the period (from July 1, 1975) during which the suspension of payment rules have been in force. The object of the investigation was, however, solely to produce material that could serve as a mirror or touchstone of the theoretical analysis, and therefore the results have not been subjected to an independent statistical evaluation.

The main question was, what was the outcome of the suspension of payment. However, the investigation was not limited to this, but was also intended to clarify how the individual rules governing suspension of payment are used and administered.

If the suspension of payment is terminated by an adjudication order, or by negotiations for the purpose of a compulsory composition this is registered with the Bankruptcy Court. But the Bankruptcy Court has neither occasion to register nor any possibility of registering the result of a suspension of payment, and so the only possibility of providing a basis for an evaluation of the method of operation of the Suspension of Payment Institution was to make inquiries of those who had given assistance to the debtor in each individual case.

The investigation at the Bankruptcy Courts, which was carried out in the course of December 1978 and January 1979 and subsequently updated to March 1, 1979, embraces the standard elements forming parts of a suspension of payment.

From the outset the questionnaire inquiries were limited to the cases of suspension of payment which did not result in bankruptcy or had been followed by negotiations for the purpose of compulsory composition. Of these 204 cases, seven which had not been terminated as at March 1, 1979, were excluded as were eight other cases where the debtor had given no information about who had given him assistance and where no supervisor (see below at p. 258) had been appointed. Furthermore, one atypical suspension of payment where a legal-aid organization had been appointed supervisor was excluded. In a comparatively limited number of cases there was more than one advisor or more than one supervisor, and the result therefore was that a total of 208 questionnaires were sent out. This part of the investigation could have been limited to what the suspension of payment had resulted in. In order to further supplement the theoretical

analysis the questionnaires also contained a number of questions about other matters. The questionnaire inquiries therefore covered 188 cases and 131 answers were received—i.e. approx. 70 per cent. 135 questionnaires were in fact returned, but eight relate to four cases involving the same suspension of payment. Seen in relation to the number of questionnaires sent out (208) the percentage of answers received was 65.

2. THE HISTORICAL PREREQUISITES OF THE SUSPENSION OF PAYMENT INSTITUTION

The Bankruptcy Act, 1872 (Act no. 51 of March 25, 1872) was the first Act which gave an elaborate systematic regulation of the Danish law of bankruptcy, but it contained no rules for the support of attempts to avoid bankruptcy. The Act laid down rules for compulsory composition in bankruptcy, but no rules about preventive compositions or schemes of arrangement for the payment of the debts. The rules governing compulsory composition in bankruptcy have been of very little importance in practice.

By the Act of April 14, 1905, rules were introduced relating to compulsory composition out of bankruptcy. The background to the Act was a growing tendency to try to avoid bankruptcy in favour of voluntary schemes of arrangement. The main object of the Act was to redress misuse of private compositions of the payment of the debts and at the same time to assist attempts at securing loyal compositions. Although the Compulsory Composition Act has not been used much in practice, there is no doubt that it has played quite a considerable role serving as a model and lever for voluntary schemes of arrangement for the payment of debts.

In 1930 a commission was set up whose terms of reference were to consider a revision of the rules governing bankruptcy and composition. The commission submitted a recommendation called Draft Bill on Composition in 1941. The draft contained a rather complicated set of partially compulsory rules for suspension of payment and negotiations for composition or schemes. This complicated and troublesome arrangement was received with strong criticism. The commission's draft, which came under attack on other points as well, did not lead to the tabling of a Bill, and it has only to a very limited extent served as a model for the present rules governing suspension of payment.

On January 29, 1958, the Ministry of Justice appointed a committee which in consultation with corresponding committees in the other Nordic countries was to put forward proposals for a revision of the rules in force for bankruptcy and composition. In 1966 the Bankruptcy Act Committee

submitted a partial final recommendation on the order of priority of creditors in bankruptcy (Report I—no. 423 of 1966). The draft report gave rise to Act no. 332 of June 18, 1969, which in the main abolished the old preferential claims—with the exception of the preferential claim for wages—and Act no. 333 of the same date, which largely repealed the statutory liens for public claims in force up till then. In 1971 the Bankruptcy Act Committee submitted a final report (Report II, no. 606 of 1971), which contained a draft for a Bill on bankruptcy and composition. As a result of the economic situation the draft rules for suspension of payment became of special topicality, by Act no. 266 of June 26, 1975, and so these rules were incorporated in the Bankruptcy Act as ch. 5 a. By Act no. 298 of June 8, 1977, the draft of the Bankruptcy Act Committee was finally adopted. The Bankruptcy Act, 1977, which came into force on April 1, 1978, was accompanied by a consequential Act (Act no. 299 of June 8, 1977) dealing with amendments of various provisions relating to bankruptcy, etc. The most noteworthy feature is that the consequential Act to the Bankruptcy Act repealed the special rules relating to the winding up of insolvent joint-stock companies and private companies under the Companies Acts.

In the sense that it has no immediate counterpart in the rules previously in force, and that it was inspired only to a very limited extent by the draft of the commission from 1941, the Suspension of Payment Institution is an innovation. However, the Suspension of Payment Institution is built up on the basis of a system which gradually—and with very little authority in the Bankruptcy Act—had become established in legal writing on bankruptcy law. The purpose of this system was to make it possible for the hearing of a bankruptcy petition to be stayed for the purpose of obtaining a voluntary scheme for the payment of the debts, but for the consequences pertaining to the law of property—if the attempt in this respect should fail—to be related back to the date when the bankruptcy petition was presented to the Bankruptcy Court. In the main, the ideology behind the rules governing suspension of payment has been to extend and clarify the set of rules which had already evolved. It has thus never been the intention that the Suspension of Payment Institution was to be an innovation, but rather the legislators' acceptance of the procedure followed in practice for obtaining voluntary schemes for the payment of the debts.³ However, the system of staying a hearing on which the Suspension of Payment Institution is modelled has hardly operated in practice in quite the way it was described in the literature on bankruptcy law, nor is it likely that it has been generally

³ Cf. *Report II*, pp. 59 ff.

or even fairly frequently used as a basis for obtaining voluntary schemes of arrangement for the payment of the debts.⁴ The historical ties to a system which to all appearances has not operated according to assumptions have had the effect that the Suspension of Payment Institution has had so little to offer that there is a risk that it can only in rare instances be attractive in cases where a business still has a real chance of survival.

3. THE GENERAL FRAMEWORK FOR THE SUSPENSION OF PAYMENT INSTITUTION

The Bankruptcy Act does not contain any explicit definition of the concept of suspension of payment. However, a definition is indirectly incorporated in the rule dealing with revocation of acts committed during the suspension of payment (sec. 72 of the Bankruptcy Act).

With this rule as a starting point, suspension of payment as viewed in relation to ch. 2 of the Bankruptcy Act is to be understood as a general discontinuance of payment of debts, unless debts are paid in accordance with the order of priority of claims in bankruptcy, or payment is necessary in order to avoid losses, and as a general cessation of contracting and performance of contracts, with the exceptions of settlements which are necessary for the continuance of the debtor's business, the reasonable safeguarding of the common interests of the creditors, or for the procurement of daily necessities.

The far-reaching and rather inflexible contents of the concept of suspension of payment have presumably had the result that the Suspension of Payment Institution can function less advantageously for an insolvent business which has reasonable prospects of obtaining a scheme of arrangement for the payment of the debts.

According to the commission draft from 1941, a debtor with a liability to keep accounts was in certain circumstances committed to giving notice of suspension of payment, just as a creditor in certain circumstances could demand negotiations for a scheme for the payment of the debts of the debtor. Such compulsory elements are not found in the rules dealing with the suspension of payment. The debtor alone can give notice of suspension of payment, and it is the debtor himself who decides whether he wants to use the Suspension of Payments Institution. This clearly points to the fact that the system rests on the basic principle of voluntariness. The principle of voluntariness is further emphasized by the fact that the commencement

⁴ Cf. *Betalingsstandsning*, pp. 30 ff.

of suspension of payment is not based on the condition that the Bankruptcy Court finds that there is a reasonable prospect of avoiding bankruptcy by a voluntary scheme of arrangement for the payment of the debts.

A notice of suspension of payment must be based on the fact that the debtor “no longer finds himself in a position to fulfil his obligations”. It is the debtor himself who makes this judgment, which goes to show that the aim has been to make the suspension-of-payment system as informal as possible, and that the Bankruptcy Court as a starting point is only meant to function as a place of official registration.

In order to protect the debtor against bankruptcy proceedings on the part of a creditor, the Bankruptcy Court has authority to stay the hearing of the bankruptcy petition at the debtor’s request. Such stay may be granted even if the petitioning creditor does not agree to it, but it is a condition that the Bankruptcy Court holds the opinion that there are reasonable prospects of obtaining a scheme for the payment of the debts. Although bankruptcy proceedings instigated by a creditor may thus be barred by an attempt to obtain a voluntary scheme for the payment of the debts the rule for staying does, however—by virtue of the control element—contain safeguards against the use of suspension of payment as an unrealistic rescue operation.

If a debtor who has not given notice of suspension of payment beforehand is granted a stay of hearing of a bankruptcy petition, the effect is that the rules governing suspension of payment find full and complete application. This result does not appear explicitly from the rules of law, but is founded on a decision of the Supreme Court.⁵

The date of presentation to the Bankruptcy Court of the notice of suspension of payment fixes the “fristdag” (=the date of notice).⁶ Thus, in case of subsequent bankruptcy (or compulsory composition) the basis for the calculation of the time for avoidance of transactions has also been laid down. A number of other legal effects in connection with bankruptcy pivot on the date of notice.⁷

If the debtor revokes his notice of suspension of payment—which he can do any time he wants—or if the Bankruptcy Court decides that the effects of such notice shall cease, the date of notice automatically ceases to be of any effect. This is also the case if a bankruptcy petition is revoked or dismissed, or if a petition for the opening of negotiations for composition

⁵ Reported in 1979 UfR 1.

⁶ Cf. ch. 1, sec. 1 (1) (1) of the Danish Bankruptcy Act, 1977. In this Act “fristdagen” (=the date of notice) means: the day on which notice of suspension of payment, or petition for negotiations for a composition, or bankruptcy petition is presented to the Bankruptcy Court.

⁷ Cf. Mogens Munch, *Konkursloven af 1977*, Copenhagen 1978, p. 57, which contains a survey of the effects of the date of notice.

does not lead to affirmation of compulsory composition. In such cases it is, however, possible to maintain the original date of notice. The technique is that the date of notice can be maintained provided the Bankruptcy Court receives a basis for fixing a new date of notice within three weeks after the old one becomes ineffective. Notice of suspension of payment can, however, only be followed by a bankruptcy petition or negotiations for composition, and not by a new notice of suspension of payment, and a petition for the opening of composition negotiations can only be followed by a bankruptcy petition, whereas a bankruptcy petition can be followed by a petition for composition negotiations or a notice of suspension of payment as well as a new bankruptcy petition.⁸ By this loop system it is possible to maintain the date of notice, and there is nothing to prevent combination of further loops, so that the original date of notice, in principle, can be maintained indefinitely.

There are of course built-in time limits in the rules relating to the length of the period of suspension of payment and in the rules relating to staying the hearing of a bankruptcy petition.

The starting point is that the period of suspension of payment is three months. However, the Bankruptcy Court has power "in very special circumstances" to prolong the period by two months, if the debtor requests this before the time limit expires.

If the suspension of payment is based on a stayed bankruptcy petition, the system is approximately the same. The stay is for a specified time and can never exceed three months, in very special circumstances five months, from the day of presentation of the bankruptcy petition.

The term "very special circumstances" signifies that a suspension of payment cannot automatically be extended to five months. The intentions of the prolongation rules unequivocally show that the possibility of prolongation for a maximum of five months should be used only where there is genuine documentation demonstrating that the normal time limit of three months has been too short to establish a foundation for a reconstruction or settling and reduction of the debts of the debtor.⁹ If the business is a normal trading concern without extensive activities there will only in rare cases be a basis for prolongation to five months.

One of the questions asked as part of the Bankruptcy Court investigation was whether the suspension-of-payment period had been prolonged. The investigation shows that the period of suspension of payment was

⁸ Cf. Mogens Munch, *op. cit.*, pp. 53 ff., and Niels Ørgaard, *Konkursret*, 2nd ed. Copenhagen 1977, pp. 29 f., about the fixing of the date of notice.

⁹ Cf. *Report II*, p. 69 and p. 84, and *Folketingstidende* 1974/75, 2nd session, supplement B, columns 1185 f.

prolonged in a little more than half the number of cases (162 out of 308). This is not only the final total, but also the main trend for the individual Bankruptcy Courts.

This distribution is in itself an expression of the fact that the Bankruptcy Courts take a lenient view of the conditions for prolongation of the suspension-of-payment period from three to five months, as it must be assumed that necessary foundation for prolongation did not exist in more than one half of the notified cases of suspension of payment. In addition, the registered material contains no examples of dismissal of a request for prolongation. In actual fact, requests for prolongation have currently been granted so long as there is a fairly plausible foundation for the requests—e.g. that it had not yet been possible to procure the necessary accounting records for a proposal for composition. A justification of this nature may appear reasonable and sufficient from a liberal point of view, but is clearly incompatible with the conditions in the Act for granting prolongation.

One of the reasons why this practice, which is clearly at variance with the tenor and intentions of the prolongation rule, has been able to develop is probably that the Bankruptcy Court, where the possibility offers itself, will be inclined to avoid making a decision which may destroy the chance of avoiding bankruptcy. Another contributing factor may be that the Bankruptcy Court, especially in relation to suspension of payment, is to function in principle as a passively registering authority and that from a practical point of view it could be awkward if the Bankruptcy Court of its own accord were to prevent a prolongation which might not be met with objections on the part of the creditors.

The empirical investigation has not, of course, substantiated that the prolongation rules are no longer to be taken literally. A creditor who finds that the Bankruptcy Court has prolonged the period of suspension of payment without the requisite foundation for it has a right of appeal against the decision of the Bankruptcy Court. And there is definitely no basis whatever for assuming that the superior courts will adopt a correspondingly lenient interpretation.¹⁰ When—and this will happen sooner or later—it has been established that the prolongation rule is to be taken literally, the practice of the Bankruptcy Courts will of course be changed accordingly.

The loop system according to which the original date of notice can be maintained, even if its foundation subsequently ceases to exist, has given rise to the specific question of the possibility of combining several suspension-of-payment periods.

¹⁰ Cf. The Supreme Court decisions 1979 UfR 1, 94 and 99.

In the 1975 version of the Act the rules relating to both the suspension-of-payment period and the prolongation period were to be calculated from the date of notice. Consequently, the most expedient thing—and in accordance with the tenor of the Act this was necessary—was to adopt the view that a period of a total of five months could never be exceeded, irrespective of how a notice of suspension of payment and a bankruptcy petition were combined. This view was actually most in agreement not only with the unequivocal words in the prolongation rules but also with the tenor of the *travaux préparatoires* from which it appears, as is mentioned above, that prolongation in excess of three months should be granted only in quite extraordinary instances.

Nevertheless, it was assumed that in practice it was possible to combine two periods of five months each, which with the addition of three weeks between the periods led to the result that the date of notice could be fixed almost one year ahead of the date of the adjudication order.¹¹ One peculiar thing is that it was never mentioned that a combination of three or still more periods of five months each might be possible. In practice the Bankruptcy Courts have rather tended to combine two periods, but the issue has not been tried at the Supreme Court, nor at the High Court.¹² It may be mentioned that the combination is most often effected in the way that, after the expiry of the period of suspension of payment, the debtor himself presents a bankruptcy petition the hearing of which will then be stayed.

At the final adoption of the Bankruptcy Act the rules were adjusted to give a formal possibility, when a suspension of payment period expires and is succeeded by a bankruptcy petition, of authorizing the Bankruptcy Court to stay the hearing of the bankruptcy petition for a period of up to five months.¹³

When it has been laid down by the Supreme Court—and this will undoubtedly happen sooner or later—that the prolongation rules are to be taken in their literal sense and in accordance with the intentions of these rules, the question of a combination of more periods will in practice only arise in the most exceptional cases. For this very reason this empirical investigation does not include systematic registration of the extent to which combination of several periods have been practised. However, it can safely be stated that combinations have been used in at least 10–15 per cent of the registered cases of suspension of payment.

Furthermore, the idea suggests itself that the manœuvres which the

¹¹ Cf. Bernhard Gomard, *Juristen og Økonomen* 1975, p. 375.

¹² So it is believed—at any rate there are no printed reports to that effect.

¹³ Cf. *Folketingstidende* 1976/77, 2nd session, supplement B, column 583.

legislator has made in order to create the possibility of combining at least two periods have lent themselves to a blurring of the basic viewpoint, namely that it ought to be an exception that suspension of payment could be prolonged to five months.

A suspension of payment expires automatically after either three or five months, but it can also cease for other reasons. The debtor may terminate the suspension of payment by revoking his notice. The revocation can be made at any time and irrespective of whether the debtor has obtained a voluntary scheme for the payment of his debts or not. The debtor does not even have a duty to state the result of the suspension of payment. This goes to emphasize the basic principle of voluntariness and, on the whole, the informal character which is a distinguishing feature of the Suspension of Payment Institution. A suspension of payment also ceases if negotiations for a compulsory composition are initiated, or if the debtor is made a bankrupt. Finally, a suspension of payment becomes ineffective by a Bankruptcy Court decision to that effect. Such a decision may be a possibility in cases where it is discovered that the debtor is not endeavouring to obtain a voluntary scheme of arrangement for the payment of his debts.

The Bankruptcy Court investigation shows the following distribution on the various causes of termination.

Cause of termination	No.	%
1. Adjudication order ¹⁴	91	29.5
2. Petition for the opening of negotiations for compulsory composition	13	4.2
3. Revocation	14	4.5
4. Expiry (3 months)	57	18.5
5. Expiry (5 months)	92	29.9
6. Other	34	11.0
7. Not concluded as at March 1, 1979	7	2.3
	308	100.0

Group 6, headed "Other", comprises the slightly more diversified group of cases where combinations of notice of suspension of payment and staying of the hearing of the bankruptcy petition have been used. However, it is not possible solely on the basis of this group to ascertain the number of cases where combinations have been used. In any case it is necessary to add the seven cases registered in group 7 as not concluded as at March 1, 1979. The investigation is limited to cases of suspension of

¹⁴ This space includes cases where a limited liability company or a private company—before April 1, 1978—has been liquidated as insolvent.

payment notified before August 1, 1978, and it is obvious that these seven cases must have involved a combination of two periods. To this must further be added possible hidden cases of combination in groups 1 and 2.

The cases of suspension of payment resulting in bankruptcy may be said to have failed as seen in relation to the objectives of the Suspension of Payment Institution. In view of the fact that, in order to have a reasonable and rational motive for giving notice of suspension of payment, a debtor must have encountered such heavy economic difficulties that bankruptcy may be the result of his plight, a percentage of the cases of suspension of payment must, however, of necessity prove to have failed. Although the percentage ending in bankruptcy is quite large (about 30) it is not so high that it can be taken as proof that the Suspension of Payment Institution does not function in accordance with the intentions of the legislator.¹⁵

An evaluation of the way the suspension-of-payment rules function presupposes information of what the final outcome was in the combined percentage of approx. 65 of groups 3–6. This part of the investigation is accounted for in section 7 below.

The rules for suspension of payment build on the assumption that the debtor has engaged someone to provide assistance, an advisor. This point is not too clearly expressed in the law text, but in return it is self-evident in the *travaux préparatoires*.¹⁶ There are no stipulations requiring the advisor to possess any definite educational or occupational qualifications. Generally, a lawyer or an association for the protection of creditors is employed, but there is nothing to prevent a businessman without special legal training from functioning as an advisor. The Bankruptcy Court is not even to consider whether the advisor stated in the notice of suspension of payment can be expected to be able to discharge his duties in a reliable manner. This solution is in harmony with the intentions to make the suspension-of-payment system as liberal and informal as possible. In order to give a debtor the best possibility of obtaining expert assistance, priority in bankruptcies is given to the payment of reasonable costs in connection with abortive attempts to obtain a voluntary scheme. This priority in payment of costs does not only apply to rescue attempts instigated during a notified suspension of payment, but also to attempts which are not combined with a formal suspension of payment.

¹⁵ Notified suspension of payment has only to a very limited extent caused the debtor to file an application for the opening of negotiations for a compulsory composition, which on the face of it may seem strange. It is not necessary, however, to forestall an application for the opening of negotiations for a compulsory composition by a notice of suspension of payment, and therefore the investigation does not reveal the extent to which compulsory composition is used.

¹⁶ Cf. *Report II*, p. 64.

At the request of the debtor the Bankruptcy Court may appoint a supervisor to him. This means that it is the debtor's own decision whether he wants the appointment of a supervisor, but the Bankruptcy Court need not comply with the debtor's request to that effect. The fact that neither the Bankruptcy Court nor the creditors can force a supervisor on the debtor underlines the voluntariness and informality of the Suspension of Payment Institution. The creditors have a possibility, however, of indirectly forcing the appointment of a supervisor on the debtor. The Bankruptcy Court can, in actual fact, make it a condition for a staying of the hearing of the bankruptcy petition that the debtor comes under supervision. From the *travaux préparatoires* it appears that the Bankruptcy Act Committee was of the opinion that a supervisor would only be appointed in very few cases.¹⁷ The empirical investigation presents a different picture. Of the 308 cases comprised by the investigation a supervisor was appointed to the debtor in 241 cases, or almost 80 per cent.

It also appears from the *travaux préparatoires* that it had not been the intention of the Bankruptcy Act Committee that the professional advisor was to be appointed supervisor, but that a possible supervisor was to perform a checking function for the creditors.¹⁸ The suspension-of-payment system is based on a division of function—one function of assistance and one of supervision. The task of the advisor the debtor himself takes on, is to produce the foundation for a scheme of arrangement for the payment of the debts, whereas the task of an appointed supervisor is to supervise and control the debtor's and the advisor's work and to resolve whether the settlements submitted for his approval are proper and expedient. The formulation of the rules does not, however, exclude the possibility of the advisor being appointed supervisor, but the system does not perfectly fit cases where the two functions are fused.¹⁹

Even a preliminary investigation shows that the assumed division into one function of assistance and one of supervision has not become accepted practice. One general feature is that the debtor requests that his advisor be appointed supervisor, and that the Bankruptcy Court automatically complies with the request. In practice, the supervisor appointed by the Bankruptcy Court is thus in the vast majority of cases also the person who renders the debtor professional assistance.

The explanation of the fact that the debtor as a general rule requests to have his advisor appointed supervisor is undoubtedly that such procedure creates a possibility of setting up claims with priority in bankruptcy, and

¹⁷ Cf. *Report II*, p. 66.

¹⁸ Cf. *Report II*, *ibid.*

¹⁹ Cf. further in section 6 below.

that the extensive rules on avoidance in force for settlements made during the suspension of payment in this way are in reality eliminated. The fact that the valuable—and for the suspension of payment arrangement—vital dividing line between assistance and supervision has not been adopted in practice is partly the responsibility of the Bankruptcy Courts. Although a supervisor can only be appointed at the request of the debtor it is the Bankruptcy Court that decides who is going to be appointed.

The application by the Bankruptcy Courts of the rules relating to suspension of payment will gradually be harmonized through the decisions of the superior courts. However, this does not apply to the rule concerning supervision as the decisions of the Bankruptcy Courts under this rule are among the decisions against which no appeal lies to a higher court. With a view to the rather far-reaching effects of the appointment of a supervisor, this arrangement appears to be somewhat precarious.²⁰ Furthermore, on the basis of the empirical investigation it can be maintained with fairly great certainty that the system on precisely this central point is administered in contravention of the intentions of the Bankruptcy Act Committee.

4. PROTECTION AGAINST CREDITORS

Notice of suspension of payment does not debar levy of execution against the debtor's property. At the request of the debtor the Bankruptcy Court can decide that execution which was levied after the date of notice, or which could be avoided in bankruptcy, cannot be completed, e.g., by seizure and sale. Such a decision on protection against creditors does not imply that execution is out of the question, but only that completion is suspended. On the other hand, if the debtor obtains negotiation with a view to a compulsory composition, this will automatically exclude execution.

The failure of the Suspension of Payment Institution to give effective protection against execution is based on the following considerations:

The Bankruptcy Court does not supervise the work of obtaining an arrangement with the creditors or the debtor's settlements during the period of suspension of payment, and therefore it would hardly be justified to deny a creditor who holds a debt of record the right to obtain execution.²¹

From this quotation it appears that the reason why the Bankruptcy Act Committee refrained from proposing a rule debarring execution is that

²⁰ Cf. *Report II*, p. 65.

²¹ Cf. Mogens Munch, *op. cit.*, p. 599.

the Bankruptcy Court exercises no supervision of the work during the period of suspension of payment. The committee has endeavoured to build up the suspension-of-payment system to be as simple and informal as possible, which in return has deprived the committee of the setting up of an effective protection against execution.

A decision on protection against creditors which—as mentioned above—does not debar execution, but only suspends the possibility of the creditor to follow up the execution by deprivation of the right of disposal or satisfaction, is conditional upon substantiation by the debtor to the Bankruptcy Court that proper steps are being taken to obtain a composition or scheme of arrangement. It has been established in a decision of the Supreme Court²² that the Bankruptcy Court must make demands to that effect.

In the case of notice of suspension of payment no information about the debtor's financial circumstances is demanded by the Bankruptcy Court. If, however, the debtor requests protection against creditors the Bankruptcy Court must nevertheless demand production by the debtor of such information. To the extent that requests are submitted for protection against creditors in connection with a notice of suspension of payment, it is therefore an illusion that the Bankruptcy Court merely can register the notice without paying heed to the circumstances of the debtor.

Decisions on protection against creditors were made in 145 cases out of the 308 cases of suspension of payment covered by the empirical investigation. In spite of the general assumption that the Bankruptcy Court is only to register the notice of suspension of payment without any investigation of the financial circumstances of the debtor, it was thus necessary in nearly one half of the cases covered by the investigation for the Bankruptcy Court to exercise its discretion as to a reasonable prospect of a successful composition or scheme of arrangement for the payment of the debts.

The numerous decisions on protection against creditors cannot in themselves be taken as a proof that the Bankruptcy Courts have currently complied with the request of the debtor. However, an indication hereof is that there are no recorded cases of refusal of requests for protection against creditors. In the case 1979 UfR 94 the Supreme Court laid down that it is a condition for a decision on protection against creditors that satisfactory steps are taken to secure an arrangement with the creditors, and that there are reasonable prospects of obtaining such an arrangement. Against this background there is every reason to believe that the practice of the Bankruptcy Courts has been altered in this respect.

²² Reported in 1979 UfR 94.

A grouping of the material in periods of four months each points to a growing tendency to request a decision on protection against creditors. The percentage rise is so pronounced (35.1 per cent—43.2 per cent—58.7 per cent) that it is hardly a coincidence, nor is it surprising that there was an increase in the tendency to use the possibility offered by the suspension-of-payment system. It will probably gradually become common practice to submit a request for protection against creditors in connection with a notice of suspension of payment. A materialization of this expectation would at the same time be a departure from the fundamental idea that the Bankruptcy Court shall not exercise control at the beginning of the suspension of payment.

5. SUSPENSION OF PAYMENT AND AVOIDANCE OF SETTLEMENT

The rules on avoidance of settlement laid down in ch. 8 of the Bankruptcy Act are applicable in cases where the debtor is adjudged bankrupt or obtains a compulsory composition. On the other hand, the carrying into effect of compulsory avoidance in connection with a voluntary scheme of arrangement for the payment of debts is not possible, irrespective of whether the debtor has given notice of suspension of payment or not. The approval of any third party is required for an avoidance to take effect. In order to obtain such approval threats may be made that a bankruptcy petition might be presented against the debtor, or—what would probably often be more effective—that a proposal for a voluntary scheme of arrangement for the payment of the debts would instead be implemented as a compulsory composition. The clearer the rules on avoidance the better the functioning of this principle of leverage.

Through the rules on avoidance bankruptcy (or compulsory composition) is given a certain retroactive effect. Even if the rules thus are immediately retroactive they play a considerable role at the preliminary stages of bankruptcy. The avoidance of an otherwise legal and fully valid settlement must invariably be of importance where a contracting party or a potential contracting party to an agreement is faced with financial difficulties that might result in bankruptcy.

The rules on avoidance may be regarded as a balanced compromise between, on the one hand, consideration for the creditors in general and, on the other, consideration for the fact that a business in financial difficulties may retain the freedom of action necessary to prevent such difficulties from resulting in bankruptcy.

All other things being equal it is conceivable that an extension of the rules on avoidance will reflect itself in a larger number of debtors being adjudged bankrupt, because in that case third parties will be more careful and reluctant to enter into or maintain commercial relations with a business in financial difficulties. However, there is no doubt that the rules on avoidance also have the effect of staving off bankruptcy. The possibility of avoidance in the case of subsequent bankruptcy must actually be considered to be one of the factors that might help the creditors to give a debtor an opportunity to surmount his financial difficulties. Thus it is far from certain that a limitation of the rules on avoidance—all other things being equal—will result in a smaller number of debtors being adjudged bankrupt.

The circumstances influenced in practice by the rules on avoidance are complicated and multifarious, and the individual cases may also differ widely from each other.

No doubt the pattern of reaction differs as against, on the one hand, a large business with extensive activities and, on the other, a small business that will not overthrow others when it falls. Therefore it is hardly possible to set up rules on avoidance giving optimum results in all instances.

As mentioned above the rules on avoidance in bankruptcy have a direct and retroactive effect, whereas at the preliminary stages of bankruptcy they are of indirect importance to the debtor's possibilities of disposal. However, during the suspension-of-payment period these effects interact to some extent.

Where, in an attempt to stave off bankruptcy in favour of a voluntary scheme, a debtor gives notice of suspension of payment, the retroactive effect of the rules on avoidance manifests itself in that the creditors who are to consent to the arrangement will put stress on the importance of the existence of any dispositions or legal steps taken prior to the notice of suspension of payment and which might be avoided in the case of a subsequent bankruptcy. If such dispositions or steps have been taken it is obvious that the creditors would qualify their consent by the establishment of voluntary—i.e. agreed—avoidance.

During the suspension-of-payment period the rules on avoidance also have the usual preliminary-stage effect. In principle, the debtor is free to dispose of his property at the suspension-of-payment stage, but in reality his power of disposal is limited by the rules on avoidance.

The rules on avoidance applicable on dispositions (and legal steps) taken before the date of notice are of such a nature that they can also be applied during the suspension-of-payment period. In addition, a rule on avoidance is laid down in sec. 72 of the Bankruptcy Act and is in effect limited to

settlements made after the date of notice, and thus refers in particular to the suspension-of-payment period. Therefore, this rule is the central element in the evaluation of the power of the debtor to make settlements during the suspension-of-payment period and thus also in an evaluation of whether the Suspension of Payment Institution is a suitable instrument in attempts to reconstruct a business or—the minor evil—to stave off bankruptcy through a voluntary scheme of arrangement for the payment of the debts.

6. SETTLEMENTS

As mentioned in section 3 above, the suspension-of-payment system is based on the assumption that, as part of his efforts to obtain a composition or arrangement, the debtor has in advance sought professional assistance, but, as also mentioned in section 3 above, it was not the intention that the advisor was also to be appointed supervisor. Therefore, the backbone of the system is the legislation laying down rules for the power of the debtor to make dispositions on his own or in consultation with the advisor.

In principle, a debtor who has given notice of suspension of payment to the Bankruptcy Court still has the right to dispose of his property, but in return settlements made by the debtor after the date of notice will generally have no better status in a bankruptcy situation than settlements made by the debtor at an earlier date. However, in reality the debtor's right of disposal is limited by the preliminary-stage effect of the rules on avoidance—*inter alia*, in particular the rules in sec. 72 of the Bankruptcy Act, which come into operation during the suspension-of-payment period.

The rules in sec. 72 deal partly with “payment of debts” (sec. 72 (1)) and partly with “other settlements” (sec. 72 (2)).

According to sec. 72 (1) a claim for avoidance of payment of debts may be made, “unless the debt is covered under the rules of priority of claims in bankruptcy, or payment was necessary to avoid losses”. Thus, it is in no way remarkable that the debtor as a principal rule must refrain from paying his debts. It is not for the debtor to upset the position between the creditors. However, the exceptions are stated in such a restrictive and inflexible way that the rule is only fully applicable in cases where the financial circumstances of the debtor are (have become) extremely serious.

According to sec. 72 (2), a claim for avoidance of “other settlements”—i.e. settlements not falling under sec. 72 (1)—may be made “unless the settlement was necessary for the continuance of the debtor's business, the reasonable safeguarding of the common interests of the

creditors, or the purchase of daily necessities". In relation to the other rules on avoidance which expressly state what actually can be avoided, sec. 72 (2) is outstanding by being different in that it states what in exceptional cases cannot be avoided.

The starting point is that any settlement made by the debtor during the period of suspension of payment can be avoided. This holds good not only for impairing settlements, but also for "settlements for valuable consideration". In that case, however, avoidance will only be of limited value to the bankruptcy estate. It is true that the other party to the contract will have to pay damages according to the general rules of law, but in return the estate must pay a sum equivalent to the consideration received by the debtor. In a number of cases the estate may find it advantageous to avoid a contract though the value of the mutual considerations balance each other. If, for example, the debtor against cash has purchased goods still unsold, avoidance would be in the interest of the estate unless it is assumed as a matter of course that the goods can be sold at a higher price than the one paid by the debtor.

Taken literally the rules in secs. 72 (1) and 72 (2) put such a strong restraint on the freedom of action of the debtor that it is almost out of the question for him to carry on a fairly normal operation of his business. In addition to this, these rules—apart from cases where the debtor's financial collapse must be considered imminent—have more far-reaching effects than the ordinary rules on avoidance.²³ A debtor who has fair chances of overcoming his financial difficulties will therefore only rarely have a reasonable motive for giving notice of suspension of payment.

As mentioned in section 3 above, the Bankruptcy Court can appoint a supervisor to the debtor at the latter's request. Even though a supervisor has been appointed to the debtor the latter retains the right to make dispositions at his own discretion, but for more important settlements the approval of the supervisor is required. In this respect it makes no difference whether it is a question of a self-employed person or a company. For example, in the case of a limited liability company in suspension of payment the normal bodies—in this respect in particular the board of directors and the management—are still fully operative. The supervisor can either veto or approve a settlement, but it is not for the supervisor to take any initiative in trying to wind up the business. It is the function of the supervisor—as the creditors' representative—to supervise and control the course of events in obtaining a composition or scheme of arrangement.

The suspension-of-payment rules are based on the assumption that the

²³ Cf. *Betalingsstandsning*, pp. 235 ff.

debtor has sought professional assistance, but they do not imply the appointment of the advisor as supervisor as well. The Bankruptcy Act Committee assumed that the debtor only rarely—and then as a rule due to pressure from the creditors—would request appointment of a supervisor. However, the Bankruptcy Court investigation shows that a supervisor is appointed far more frequently than presumed, and that the assumed division into an advisory function and a supervisory function has not been established in practice. It is a common feature that the debtor's advisor is appointed supervisor, and that only one supervisor is appointed. The fact that the rules are not used as intended in this important respect points towards the assumption that the principal system of the Act does not provide a quite satisfactory basis for the aim of obtaining a composition or scheme. In any case the effect of the distortion in practice in relation to the starting point of the Bankruptcy Committee, is that the special rules applying in cases where a supervisor has been appointed to the debtor have been given a much more dominant position than was intended.

Appointment of a supervisor to the debtor does not mean a direct possibility of making settlements that the debtor cannot make on his own. The power of the supervisor to approve the settlements of the debtor is actually limited in exactly the same manner as the debtor's power of action (sec. 13 (3)). The possibility of appointment of a supervisor therefore does not make the Suspension of Payment Institution more attractive to a business that (still) has reasonable chances of survival.

During the final amendments to the Bankruptcy Act it was formally made possible for the supervisor to act *ultra vires* "with the approval of the creditors". However, it is uncertain whether consensus among the creditors is required or if a reasonable majority is sufficient. In view of the fact that the system must be operable in practice the latter solution is, of course, to be preferred.

Where the supervisor has approved the payment of a sum of money or other settlement, avoidance shall be possible only "where it is obvious that the supervisor has acted *ultra vires*" (sec. 72 (3)). In actual fact, the approval of a settlement by the supervisor negates the far-reaching rules on avoidance.

Whereas settlements made by the debtor alone during the suspension-of-payment period have no better status in bankruptcy than settlements made by him at an earlier date, debts incurred by the debtor with the approval of a supervisor appointed by the Bankruptcy Court have been given a right of priority over the usual bankruptcy claims (sec. 94 (1) (2)). There is no doubt that the effect of this rule in practice is that the debtor can buy on credit and raise new loans. If the debtor simply is the owner of

uncharged property of some magnitude it is obvious that the risk of granting credit with the approval of the supervisor is very limited, irrespective of whether the value of the debtor's liabilities may be several times greater than the value of his uncharged assets. As mentioned in section 3 above, the Bankruptcy Court need not comply with a request from the debtor for the appointment of a supervisor. However, the Bankruptcy Court investigation shows that the appointment of a supervisor is made currently. This practice is not quite unobjectionable. The opening up of the possibility of contracting priority debts in actual fact implies that the creditors in bankruptcy in reality may unwittingly take part in the financing of considerable items of debt incurred in unsuccessful attempts at staving off bankruptcy.

The very fact that many and perhaps heavy priority debts may in time have been contracted could very well play some part in leading the creditors to acquiesce in the fact that suspension of payment is used to create a calm atmosphere around an actual winding up of the debtor's business. The consequence of the creditors' intervention by having the debtor adjudicated bankrupt might well be that in reality they will be burdened with yet another round of new costs and new debts with status as preferential claims.

It is quite natural that the person who assists the debtor in an attempt at obtaining a composition or scheme, will often try to be appointed supervisor rather than function only as advisor. If the advisor is appointed supervisor it is substantially easier to carry on the debtor's business and carry through a voluntary liquidation, among other things, because of the possibility of contracting priority debts in bankruptcy.

A debtor who has given notice of suspension of payment and for whom no supervisor has been appointed, has only very limited possibilities of entering into new contracts of even tolerably appreciable dimensions. If a supervisor has been appointed the debtor will, on the other hand, have quite good opportunities of entering into new contracts with the approval of the supervisor. The approval of a contract by the supervisor has the effect of limiting the risk of avoidance, and of ensuring that claims arising out of the contract have a right of priority in case of bankruptcy.

Apart from cases where the debtor has kept his notice of suspension of payment a secret it is likely that any potential contracting party will demand submission of the contract to the supervisor for approval in advance. The consequence of the very considerable difference between, on the one hand, the legal effects of a contract entered into by the debtor on his own and, on the other, the legal effects of a contract approved by the supervisor, is that the other contracting party willingly makes a detour via the

supervisor. In this way the system of unobtrusive supervision has actually sabotaged itself. Whether the supervisor from the outset intends only to control more important settlements or not, it must be considered safe to say that the supervisor will nevertheless be called upon to play a more active role by third parties.

7. THE QUESTIONNAIRE INQUIRIES

The Bankruptcy Court investigation shows that the direct outcome of about 30 per cent of the cases was bankruptcy, and that about 4 per cent of the cases of suspension of payment were followed by a petition for the opening of negotiations for compulsory composition. It was the object of the questionnaire inquiries to show what was the outcome of the other cases. It was necessary on this point to distinguish between, on the one hand, single-owner business and partnerships and, on the other hand, limited liability companies and private companies.

Some of the incoming answers showed that the suspension of payment resulted after all in bankruptcy. This "error" in the Bankruptcy Court investigation is due partly to the fact that in connection with suspension of payment there is no entirely automatic registration if the debtor is adjudged bankrupt, and partly to the fact that to a certain extent it is a question of cases where the original date of notice has not been adhered to. With the addition of this possibility the answers are grouped as follows:

Single-owner businesses and partnerships	Number of answers	Per-centage
Reconstruction of the business		
(a) in connection with composition	6	
(b) otherwise	6	13.5
Sale of the business		
(a) in connection with composition	4	4.5
(b) without composition for the debtor	13	15
Dissolution with subsequent distribution		
(a) in connection with composition	9	11
(b) without composition for the debtor	25	28
Actual dissolution abandoned	18	20
Bankruptcy	7	8
	88	100

Limited liability companies and private companies	Number of answers	Percentage
Reconstruction of the company		
(a) by new capital contribution	3	
(b) by conversion of debts into contribution	0	14
(c) otherwise	2	
Voluntary liquidation in connection with sale of the business	1	2.5
Voluntary liquidation with subsequent distribution	10	28
Actual settlement abandoned	2	5.5
Bankruptcy/insolvency liquidation	18	50
	36	100

Compared with the results of the Bankruptcy Court investigation these tables show that about 40 per cent of all cases resulted in bankruptcy. In reality this share probably constitutes half the number of cases.

Of the 88 single-owner businesses and partnerships 25 have been reconstructed or have obtained settling and reduction of their debts, and 5 of the 36 companies have been reconstructed. These figures should demonstrate that only a moderate share of the total number of cases of suspension of payment covered by the investigation—probably not much more than 10 to 15 per cent—has resulted in a reconstruction of the business or a settling and reduction of the debts of the debtor.

The investigation shows that a substantial number (38 out of 88) of the single-owner businesses or partnerships have been sold or wound up without a settling and reduction of their debts. A corresponding number of the companies (10 out of 36) have been voluntarily wound up during suspension of payment. In addition there are the somewhat similar cases (18 and 2), where actual winding up has been abandoned owing to insufficient assets.

Taken as a whole this—central—part of the investigation shows that the Suspension of Payment Institution is generally used only in the last resort and that it is used fairly often instead of bankruptcy and not so much as part of attempts at bringing about a true composition or arrangement for the debtor.

In order to throw (additional) light on the situation of the average debtor at the moment of suspension of payment, a question calling for a grading of the financial difficulties of the debtor had been included in the questionnaire. The answers were grouped as follows:

The financial difficulties of the debtor were	Number of answers	Percentage
Inconsiderable	0	0
Not very serious	4	3
Serious	25	21
Very serious	35	30
Insuperable	54	46
Total	118	100

These groups confirm the belief that notice of suspension of payment as a rule has been given so late that it was necessary to exclude the possibility of implementing a proper reconstruction of the debtor's business. Thus there is every reason to believe that, as a rule, notice of suspension of payment is given only as a last resort, not only perhaps because of the strict limitations on the right of disposal involved in cases with a notified suspension of payment, but rather because the answers support the belief that the suspension-of-payment system has no attraction for an insolvent debtor who (still) has reasonable chances of weathering the storm.

The financial difficulties of a business can arise out of many different circumstances. The questionnaire contained a question aiming at disclosing the main causes of notice of suspension of payment in order to produce a basis for a more general characterization of the debtors covered by the investigation. There is often more than one cause of the financial difficulties of a business, and therefore it was necessary to give several tick-off possibilities. Though this involves some lack of precision the answers have been added up for the sake of clearness without correction for the inclusion of some of the cases several times.

Causes of suspension of payment	Number of tick-offs
Insufficiency of own capital	61
Poor management	71
Special conditions in the trade	31
General market conditions	24
Other conditions	31

The distribution shows that the causes "insufficiency of own capital" and "poor management" have been rather dominant. The heading "other conditions" includes illness, personal difficulties of other kinds, and too

large a private consumption stated as causes in the individual remarks in the answers. The answers thus reflect the fact that, as a rule, the business examined suffered from fundamental—and consequently also often irreparable—weaknesses.

Seen as a whole the results of the investigation indicate that in practice the Suspension of Payment Institution is chiefly used by “unsound” businesses with serious or insuperable financial difficulties.

In order to form an impression of the practical functioning of the advisor/supervisor, the following question has been included in the questionnaire:

How would you roughly characterize your actual position during the suspension of payment period?

- (1) as a passively supervising authority
- (2) as an actively supervising authority
- (3) as temporary manager of the business
- (4) essentially as liquidator/trustee
- (5) as liquidator/trustee

Without correction for tick-offs of two items in some cases—typically item 2 and item 4—the total number of answers are grouped as follows:

The function of the advisor/supervisor: 119 answers	Number of tick-offs
As a passively supervising authority	14
As an actively supervising authority	42
As temporary manager of the business	10
Essentially a liquidator/trustee	44
As liquidator/trustee	33
Total	143

On the one hand, the answers cluster round items 1 and 2, and, on the other, round items 4 and 5, but with the greatest weight on items 4 and 5. Of the total of 119 questionnaires in which the question had been answered, tick-offs had been put on both sides of this dividing line in 24 questionnaires.

As between advisors and supervisors, respectively, the distribution is as follows:

Advisors – 16 answers	Number of tick-offs
As a passively supervising authority	5
As an actively supervising authority	6
As temporary manager of the business	2
Essentially as liquidator/trustee	2
As liquidator/trustee	4
Total	19

Supervisor – 103 answers	Number of tick-offs
As a passively supervising authority	9
As an actively supervising authority	36
As temporary manager of the business	8
Essentially as liquidator/trustee	42
As liquidator/trustee	29
Total	124

These tables show that advisors and supervisors on the whole have functioned in the same way. Paradoxically, a weak tendency is just noticeable showing that the advisors have played a less prominent role than the supervisors. The answers received clearly confirm that the function of the advisor and the function of the supervisor have become fused in practice. A supervisor functioning in accordance with the intentions of the suspension-of-payment system comes under either item 1 or item 2. The fact that the advisor/supervisor in 77 out of a total of 119 cases has conceived his position either as liquidator/trustee or essentially as liquidator/trustee, seems to show that suspension of payment very often has been used primarily as a basis for liquidation and not as part of an attempt at obtaining a voluntary composition.

8. SUMMARY AND EVALUATION

The rules on suspension of payment in ch. 2 of the Danish Bankruptcy Act, 1977, are based upon a system which with vague authority in law gradually came into existence in legal writing on bankruptcy law. In practice, however, this system hardly functioned in the way in which it was described in legal writing. The historical ties have been conducive to the fact that the Suspension of Payment Institution does not hold special

attraction as an instrument for obtaining voluntary schemes of arrangement for the payment of the debts.

The suspension-of-payment system is based on the main principle of voluntariness and has been designed to be as informal and simple as possible. It is for the debtor to decide whether he wants to use the Suspension of Payment Institution, and the debtor can at any time and without any special grounds revoke his notice of suspension of payment. In the opinion of the Bankruptcy Court the opening of suspension of payment is not conditioned by any reasonable prospect of a scheme of arrangement being obtainable. It is the task of the Bankruptcy Court solely to receive the debtor's notice of suspension of payment and ascertain that it complies with the formal conditions of the law. During the suspension-of-payment period the debtor is not subjected to public control, and neither the Bankruptcy Court nor the creditors can force a supervisor upon the debtor.

The suspension-of-payment system is built upon a division into an advisory function and a supervisory function. It is the task of the advisor, who is engaged by the debtor himself, to find a basis for a scheme of arrangement for the payment of the debts. It is the task of the appointed supervisor to supervise and control the attempts of the debtor and the advisor to stave off bankruptcy and estimate whether the settlements submitted for approval are justified and expedient. In view of the fact that the creditors normally would have confidence in the advisor the Bankruptcy Act Committee assumed that the debtor only in relatively rare cases—under pressure from the creditors—would request appointment of a supervisor. However, the empirical investigation shows that as a principal rule a supervisor is appointed, and that the advisory function and supervisory function become fused. The general practice is that the debtor's advisor is appointed supervisor, and that only one supervisor is appointed.

Notice of suspension of payment does not debar a creditor from levying execution against the debtor. At the request of the debtor the Bankruptcy Court may make a decision for protection against creditors, but the sole implication of such a decision is that an execution which is levied after the date of notice or which would be extinguished in the case of bankruptcy cannot be completed, e.g., by seizure and sale. Execution is, however, not possible after the opening of negotiations for a compulsory composition. The reason for the pronounced distinction between the suspension-of-payment rule and the compulsory composition rule is that the Bankruptcy Court does not supervise the work during suspension of payment, whereas during negotiations for a compulsory composition the Bankruptcy Court exercises some control over the proceedings, and even at the opening of

the negotiations the Court has found that there are reasonable prospects of carrying the composition into effect. Thus the price for this simple and informal distinctive mark is that the suspension-of-payment system offers much less protection against individual legal proceedings than the more formal and cumbersome compulsory composition system.

A scheme of arrangement for the payment of the debtor's debts was obtained in only a few of the cases of suspension of payment included in the empirical investigation. The outcome of close on one half of the cases was bankruptcy or insolvency liquidation. To a considerable extent suspension of payment has either been used as a basis for liquidation without settling and reduction of the debts of the debtor, or else has resulted in the abandonment of suspension of payment owing to insufficiency of assets. The reason why the suspension-of-payment rules have hardly been able fully to live up to the intentions of the Bankruptcy Act Committee, is probably largely the limitation on the powers to make settlements attached to suspension of payment.

The rules on avoidance of settlements made during suspension of payment are ostensibly based on the general principle that it is important to give a subsequent bankruptcy estate the best possible protection. In this way the freedom of action of the debtor during the suspension-of-payment period has been so heavily restricted that it may be extremely difficult to carry on the debtor's business. The effect of any imaginable avoidance of normal commercial settlements would invariably be a high degree of caution and reservation on the part of third parties in entering into or maintaining commercial relations with a business which has given notice of suspension of payment. The price for extensive safeguarding of the interests of a subsequent bankruptcy estate gives rise to a similar preliminary-stage effect. Therefore, the severe restrictions on the debtor's freedom of action imply that the possibilities of using the Suspension of Payment Institution as a basis for the reconstruction of an insolvent business must be regarded as modest.

The power of an appointed supervisor to approve the debtor's settlements is limited in the same way as the debtor's power to make settlements on his own. Thus the possibility of appointing a supervisor does not imply that the suspension-of-payment system will be more attractive to an insolvent debtor.

In the sense that the risk of avoidance is eliminated if a settlement is approved by a supervisor appointed by the Bankruptcy Court, the supervisor has a certain "authority". This authority is quite far-reaching in its effect. The authority of the supervisor is so narrowly confined that the suspension-of-payment system can hardly function unless the supervisor

makes use of the rule of authority. This assumption is to some degree confirmed by the questionnaire inquiries. However, it is not quite reasonable that the Suspension of Payment Institution is built up in such a way that it can function only if the supervisor acts *ultra vires*.

Debts incurred by the debtor with the approval of the supervisor during the suspension-of-payment period have been given a right of priority over the other claims in bankruptcy in the event of subsequent bankruptcy. This right of priority can be a contributory factor—through the use of suspension of payment—in the creation of a calm atmosphere for the liquidation without settling and reduction of the debts of the debtor. In step with the contraction of claims with right of priority during a suspension-of-payment period the creditors will often feel less inclined to have the debtor adjudged bankrupt, because this would, as a rule, mean additional costs for them.

The empirical investigation shows that the assumed division into an advisory function and a supervisory function has not become accepted in practice, and that a supervisor is appointed in many more cases than was assumed by the Bankruptcy Act Committee. The reason for the pronounced tendency to appoint the advisor of the debtor as supervisor is no doubt first and foremost the possibility of creating priority claims in this way, and that the extensive rules on avoidance thus are eliminated. The difference between the two lines in the suspension-of-payment system is simply so great that it must be considered impossible that the contracting parties of the debtor, and particularly his potential contracting parties, will accept if, together with an advisor who is not appointed as supervisor, he tries to bring about a scheme for the payment of his debts. This is at any rate the case if the debtor's business is (still) a going concern, but the Suspension of Payment Institution is certainly also designed for such cases.

The objects of the rules on suspension of payment in ch. 2 of the Danish Bankruptcy Act, 1977, are to strengthen the possibilities of staving off bankruptcy in favour of voluntary schemes of arrangement for the payment of the debts. The theoretical analysis shows, however, that the rules are not fully applicable to this purpose. This assumption has been corroborated by the empirical investigation which shows very clearly that the Suspension of Payment Institution is often used as a preliminary stage for bankruptcy or directly as a basis for liquidation without settling and reduction of the debts of the debtor ("bankruptcy without bankruptcy"). This use involves a cumulative effect. The more third parties consider a notified suspension of payment to be equal to bankruptcy the more difficult will it be to use suspension of payment as a basis for bringing about voluntary schemes of arrangement for the payment of the debtor's debts.