The Floating Charge – An Elegy

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Abstract

This paper argues that the usual way of conflating floating with fixed charges as small variations on a single theme – as priority-based devices differing only in degree – fundamentally misunderstands its true nature. The floating charge plays a distinctive role as a residual management displacement device which can only be effective if coupled with an appropriate set of fixed security that enables its holder to gather information about the competence of the debtor's managers and to control their incentives to misbehave. The floating charge allows the debtor free use of its circulating assets while its management is doing well, and when the management fails, it crystallises to divest them of control even over these assets. At this time, it also contributes to controlling the motivation costs of other creditors by discouraging them from rushing to enforce their claims against circulating assets or threatening to do so, and by ensuring the unity of the debtor's estate under the receiver's control even after the onset of winding-up. This priority-independent view of the floating charge enables us to explain the peculiarities of its actual operation, to understand why it is generally taken in combination with fixed charges, and either over the debtor's entire undertaking or over those assets not amenable to the draconian control of the fixed charge, and also to bring out the non-anomalous status of the 'lightweight' floating charge. The analysis also helps throw light on the role of registration, and on the problems occurring at the boundary between the two types of charge. Despite all this, however, it will be argued that with the onset of changes introduced to the administration regime by the Enterprise Act 2002, the floating charge has outlived its utility, and that its continued retention is now difficult to justify.

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1. Introduction: The Mysterious Floating Charge

Whether they praise or (more frequently) condemn it, commentators do not generally realise how great a puzzle the floating charge is. Consider what we ordinarily expect of a security interest. Most obviously, the secured creditor would hope to enjoy *priority* in the proceeds of sale of the collateral over his debtor's other creditors. However, the floating charge does a very bad job, ranking behind not only a later fixed charge over the same assets, but also behind statutory preferential claims. Once the relevant provisions of the Enterprise Act 2002 come into force, the categories of preferential creditors will shrink.[1] However, a particular proportion of the value of the collateral subject to a floating charge will be 'ring-fenced' for general unsecured creditors,[2] leaving the floating charge holder's position no better off.[3] One might also wish a security interest to *encumber* the collateral, so that attempts by the debtor to pass on the assets subject to the charge would be unable to defeat the charge holder's rights. With a floating charge, however, the debtor "may deal with or dispose of such property without the approval of, or even consultation with, the charge holder",[4] and as long as this is done in the normal course of business, the transferee's title is unburdened by the charge holder's rights. At the very least, a secured creditor would wish to be able to tell how much collateral it had been offered in order to carry out a *risk assessment* on the loan. However, the creation of subsequent fixed charges and the accumulation of new preferential claims can dilute the floating charge holder's security, as can the debtor's ability to alienate the collateral free of the charge. So the floating charge holder cannot even know which assets it has security over, and how much they are worth! No wonder this has been described as a "key weakness" of this device.[5]

Security is also often said to bring efficiency benefits by allowing the secured creditor to monitor the assets subject to the charge, with the aim of deterring financial agency costs. The existence of security is said to facilitate this monitoring by creating 'focal points' for the monitoring effort: instead of having to keep an eye globally on the debtor's affairs, the creditor may focus simply on the presence, value, and use of the assets given as collateral.[6] This lowers monitoring costs, and on conventional reasoning, some part of these savings might be passed on to the debtor as lower interest rates. However, as Finch notes, floating charges are generally taken over the debtor's entire undertaking,[7] which means "monitoring in order to detect misbehaviour or calculate risks could involve scrutinising the whole business". In effect on this reasoning, much of the point of taking security as an aid in monitoring is thus negated. In the result, "the floating charge may offer a relatively expensive method of securing finance".[8]

[1] Enterprise Act, s. 251.
[2] See s. 176A of the Insolvency Act 1986, as inserted by s. 252 of the Enterprise Act.
[3] See also Insolvency Act 1986, s. 19(5), which grants the administrator the power to subordinate the claim secured by the floating charge to new monies advanced to finance the administration.
[4] V Finch, *Corporate Insolvency Law – Perspectives and Principles* (Cambridge, CUP, 2002) (hereafter, 'Finch') at 80. Finch's views will be taken as representative of the traditional understanding of the floating charge.
[5] Finch at 103.
[6] See e.g. S Levmore, 'Monitors and Freeriders in Corporate and Commercial Settings', (1982) 92 Yale LJ 49.
[7] Finch at 80.
[8] Finch at 92.

So if the floating charge is such a thoroughly inefficacious way of securing a loan from the lenders' perspective, why is it more or less ubiquitous in corporate debentures?[9] Critics offer a worrying explanation. Not only is the floating charge a terrible security device, it is also said to be exploitative. It is "a mechanism peculiarly conducive to the transfer of insolvency wealth from unsecured to secured creditors", and most likely "designed" for this very purpose.[10] It is "a charge upon all future property", sucking in after-acquired assets into its ambit "without the injection of fresh value by the original creditor". This creates a "windfall" for the charge holder and ensures that the rate on the secured loan is "increasingly advantageous" to it.[11] These interest rates are "excessively profitable" because the floating charge holder's ability to exploit its positions ensures "risks are loaded onto unsecured creditors".[12] What is more, unsecured creditors may have insufficient notice of the effects of the charge, since it might be "impossible to tell from the [company charges'] register how much the floating charges secure".[13] This deceptiveness adds to the exploitative value of this device, which is sufficiently great to make it universally popular for powerful lenders (i.e. banks) despite its many disadvantages.[14]

This is a damning indictment. In response, I want to suggest that the floating charge is not malignant, merely misunderstood. The floating charge is unlike other security interests, first and foremost, in that it provides a very poor priority to its holder in the debtor's insolvency. Focussing on this and yet keeping in mind its ubiquity encourages a search for its true function. It is suggested here that a theory claiming to reveal this function could be considered successful only if it could explain the development of the 'lightweight' floating charge, the reason why floating charges are usually taken over the debtor's entire estate[15] and why they are often coupled with fixed ones, the distinction between fixed and floating charges, and the desirability or otherwise of restricting the priority position of the holders of the latter.[16] Removing the misunderstanding as to the actual role of the floating charge would also allow us to quiet concerns that its main value has been in its ability to exploit. However, while it might not have been exploitative in the past, it will be argued that its existence will become wholly exploitative after the coming into force of the relevant portions of the Enterprise Act. It will therefore be suggested that it should now be abolished.

2. Priority and the Floating Charge

It would be useful to begin by pointing out that the indictment laid out above is self-contradictory. If criticism of the floating charge as to its efficacy in securing priority for its holder is correct, then criticism on the basis that it serves as a siphon for taking value away from unsecured creditors must be wrong.

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[9] See e.g. Finch at 82 nn. 100-1, *inter alia*, citing evidence that about 80% of all debtor companies in one sample had granted floating charges.
[10] Finch at 102.
[11] Finch at 455; see also at 462. It has to be said this last point is quite suspect even on this line of reasoning: surely the interest rate would have been set in the first place in full anticipation of the fact that more assets might well be drawn in as collateral? It is therefore difficult to see how it could become "*increasingly* advantageous" to the creditor.
[12] Finch at 263.
[13] Finch at 456. This is not such a problem with fixed charges; see Finch at 459.
[14] See Finch's rather ambivalent conclusions at, e.g., 102 and 104-5.
[15] Finch at 80 and 92.
[16] Such as that brought about by s. 176A of the Insolvency Act 1986, as inserted by s. 252 of the Enterprise Act.

It is submitted that not only is the floating charge generally ineffective in giving its holder priority over others, it is in fact not a priority-based device at all.[17] First of all, there is no doubt that the floating charge does not do much for its holder as far as priority is concerned. The well-known doctrinal facts about its ranking have already been rehearsed. What has not been done in the past is to view this ranking in the context of the empirical evidence available as to the recoveries of various classes of creditor in insolvency proceedings. Finch's recent discussion is a representative example. She faithfully reproduces the relevant statistics, which generally derive from the annual Surveys of its members by the Association of Business Recovery Professionals (ABRP),[18] and recently, from the study done by Julian Franks and Oren Sussman.[19] From the latter, Finch reports that "recovery rates for banks [who generally take security] are seventy-seven percent compared with 'close to zero' for trade creditors and twenty-seven percent for preferential creditors".[20] And according to the ABRP's most recent Survey, overall recoveries were thirty-five percent for preferential creditors, fifty-three percent for secured ones, and seven percent for unsecured ones.[21]

What Finch does not do, in common with most other commentators, is to draw out the implications of these figures for the debate about the nature of the floating charge. Important for our purposes is the recovery rate for preferential creditors, consistently revealed by these studies to hover around the thirty pence on the pound figure. We should recall that, under the 'absolute priority rule', creditors allocated a junior position in the statutory scheme for the distribution of insolvent estates are paid anything *only if* creditors senior to them have been fully paid off. Now it would be too quick to conclude from this that the average recovery on a floating charge, which ranks behind preferential debts, is zero. Unsecured creditors rank even further behind preferential creditors, yet their recovery is above zero at least in the ABRP study. (As noted, it is close to zero for firms in the Franks and Sussman data set.) However, a broader look at the pattern of distribution of recoveries overall in insolvency proceedings provides interesting insight. Preferential creditors get back everything they are owed in just over twenty-five percent of insolvency proceedings, receive nothing at all in just under twenty-five percent of cases, and recover less than five pence on the pound in the remainder.[22] So not only is there no recovery at all under a floating charge in almost twenty-five percent of insolvencies (because preferential creditors receive nothing), there is virtually nothing paid because of the floating charge in another fifty percent of cases (since preferential claimants get under five percent). And what about the twenty-five percent of insolvency proceedings in which preferential creditors receive their full amount, so that there would be a possibility of significant payments to floating charge holders as well? It is interesting to note that in these instances, the recovery rate for *un*secured creditors is high, at almost twenty-five pence on the pound. This compares not unfavourably with average recovery rates for both secured creditors – reported in this Survey to be about fifty-three percent[23] – and certainly those for preferential one. A likely explanation for this finding is that in such cases, a high return to preferential creditors indicates that the debtor's estate has sufficient value

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[17] In fact, it was in an effort to convert it into a priority-based device that lenders invented the 'negative pledge clause'. However, negative pledge clauses are not registrable, so their registration does not fix subsequent lenders or purchasers of the collateral with constructive notice. So subsequent lenders or purchasers are not bound by such clauses unless they have actual notice of their existence.
[18] See e.g. ABRP, *9th Survey of Business Recovery in the UK* (22 November 2001).
[19] *The Cycle of Corporate Distress, Rescue and Dissolution* (IFA Working Paper 306, 2000) (hereafter, '*Cycle*').
[20] Finch at 82 n. 102.
[21] *9th Survey* at 18.
[22] Ibid., Chart 16.
[23] Ibid. Needless to say, the difference between secured and unsecured claims should be expected to be reflected to *some* degree in the recoveries for these types of creditor.

to pay back all or almost all of the debt secured by the *fixed* charge. Now since the floating charge would generally secure the *same* debt as the fixed one, having enough left over to pay off preferential creditors in full should be correlated with having sufficient value in the insolvent estate to meet a significant proportion of the unsecured debt as well (the debt secured by the floating charge already having been paid, entirely or almost entirely, under the fixed charge).

One immediate conclusion, then, is that the widespread image of the floating charge – as a device "designed" to create "windfalls" for its holder by voraciously "transferring wealth from" and "loading the risks of insolvency onto" unsecured creditors – is grossly distorted. From the very evidence relied upon by its critics, it appears the floating charge directs, at best, tiny amounts of insolvency value to its holders in three-quarters of all insolvencies, and does not transfer *any* wealth at all in another quarter of the cases. This also means the argument that this charge loads insolvency risk onto unsecured creditors finds little support in the facts. And since the floating charge seems to take little out of the insolvent estate in an overwhelming majority of cases, and given the conventional view that a loan secured even by a floating charge is likely to be at least somewhat cheaper than an unsecured one, there remains little basis for suggesting that the rates charged on loans secured by floating charges are excessive (at least on the grounds listed above). Another conclusion is that the fact that registrations of this type of charge do not reveal the amount secured by, or the particular assets subject to it from time to time, is not objectionable, since the practical impact of the charge – its ability actually to 'bite' on the collateral, to 'corner' it for its holder, to apply it towards the discharge of the amount secured – is insignificant in most cases.[24]

So whatever else the role of the floating charge may be, it is not to exploit unsecured creditors by siphoning insolvency value away from them by virtue of the *priority* of this device. In fact, as this discussion shows, priority is not a great virtue at all of this charge. This leads to another conclusion. Let us focus on a peculiar feature of the 'lightweight' floating charge, viz., that it is taken by a lender whose exposure is fully or at least substantially secured by a fixed charge,[25] so that the floating charge is not required to provide it priority. In light of the quick discussion so far, it is suggested that lightweight charges are not some special category of floating charge. In fact, floating charges are *essentially* 'lightweight' in that they are not good at, and therefore not relied upon to, provide priority for their holders in the proceeds of sale of the collateral. It would require great faith in the *ir*rationality of lenders which are repeat players in the market, which lend to tens of thousands of companies a year, and which have accumulated expertise in dealing with the consequences of default,[26] to attribute to them the intention of taking floating charges in the hope of gaining priority. It is more credible to assume that they would have long learnt from experience they would get back next to nothing on this type of security in at least seventy-five percent of insolvencies, and would not need to get anything on it in most of the remaining.[27] In addition and crucially, they could not predict at the time of the loan agreement

[24] The role of registration is discussed further in the following Section.
[25] See e.g. C Rumbelow, 'Mortgages by companies: A problem', [1989] LSG 32, and F Oditah, 'Lightweight floating charges', [1991] JBL 49.
[26] See e.g. the discussion of 'central rescue units' in *Cycle*, examined below.
[27] This is not a 'psychological' claim about the state of mind (whatever that means) of institutional lenders. It might well be, e.g., that some bank managers etc. would state if asked that they included floating charges in security packages for the benefit of their employer because of the priority of this type of charge. That would be irrelevant to the present argument. The claim in the text here is the different one that the *practices* of institutional lenders (rather than *statements* on their behalf) reveal that they have taken on board the priority-independent nature of the floating charge. The practices relied on in support of this argument are precisely the ones discussed in the text, e.g. that floating charges are coupled with fixed ones, the sort of assets they are taken over, and that they are sometimes taken for purposes quite obviously unrelated to their

which of these groups a particular debtor would fall into, should it become insolvent. So it is not surprising that generally, floating charges are coupled with fixed ones.[28] The two perform different roles, and it is the *fixed* one which is relied upon to provide priority, encumbrance, and risk assessment. Note that on the priority-based view of the floating charge, it is difficult to provide a satisfactory explanation not only of the rationale for lightweight charges, but also of why floating charges are normally taken together with fixed ones.[29]

It is very important to be clear about precisely what is being argued here. The argument is *not* that having a floating charge *never* increases the holder's recoveries simply by virtue of the priority of this security. The evidence discussed above is by no means inconsistent with the proposition that in *some* insolvencies, the priority of the floating charge would cause a greater amount of value in the insolvent estate to be diverted to the holder of the charge than would be the case if the charge did not exist. What is in fact being argued is that this is both rare, and for that reason, also unpredictable. *At the time that the debenture was being issued*, it would be very difficult to determine whether this debtor – should it later have to go through a formal insolvency proceeding – would constitute one of those rare cases where the priority of the floating charge would inflate its holder's recoveries. Put differently, it would be difficult *ex ante* to predict whether the eventual insolvency of any particular debtor would constitute the case where the priority of the floating charge was both, not *illusory* (because all of the debtor's property had been distributed to fixed charge holders and preferential creditors) and not *unnecessary* (because the debt secured by the floating charge had already been paid under the fixed charge). Floating charges may *result* in some recoveries in some minute proportion of insolvencies, but the dominant *reason* for their inclusion in a vast proportion of debentures that create security interests is not to ensure these rare and trivial recoveries. As explained, it would not be a rational strategy for a lender seeking to gain priority over other creditors in a useful way to rely on the floating charge.

3. The Limited Role of the Floating Charge

So what *is* the floating charge for? It is suggested that it is a *residual management displacement device* which can work optimally *only* when it is part of a package of security interests covering the whole or substantially the whole of the debtor's property,[30] and generally, only when this package includes fixed security over assets strategically important to the debtor's business.[31] For reasons that will soon be apparent, someone holding such a security package will be referred to in this paper as the debtor's 'main creditor'. We can start building up our understanding of all this by taking into account suggestions about lightweight charges, and others about floating charges in general made quite recently in the literature. First, in explaining the causes for the emergence of

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priority. The claim is of course also that the analysis here coheres with the evidence available while the priority-based view of the charge does not, and also that it can – in a way that a priority-based view cannot – explain the structure of the relevant law both before and after the coming into force of the Enterprise Act 2002, e.g. about the provisions requiring registration and some of those governing administration; see below.

[28] See e.g. *Cycle* at 9 Table 4.

[29] Finch attempts to do so, e.g., at 81-2.

[30] Compare Insolvency Act 1986, s. 29(2). The argument here is that far from identifying some special category of floating charge, this provision describes the sort of security package that a floating charge must generally be part of, in order to be efficacious.

[31] A somewhat similar understanding seems to underpin comments by R Goode, *Principles of Corporate Insolvency Law* (London: Sweet & Maxwell, 1997) at 204.

lightweight charges, commentators have seized upon the obvious and important connection between having a floating charge over substantially the entire estate of the debtor, and being able to block the appointment of an administrator to manage it. Despite having protected its priority through a fixed charge, the lender nevertheless values these powers, since they are crucial to controlling the timing and manner of realisation of the security (i.e. that under the fixed charge).[32]

Second and not just in the context of lightweight charges, two sets of commentators have recently highlighted a possible *control*-based (as opposed to priority-based) explanation of the floating charge, noting that at least some of its value might lie in being able to take control of the debtor by appointing a receiver. Armour and Frisby, in their illuminating discussion of receivership, have noted that it "is conceptually possible to imagine a legal system in which a 'floating charge' offers its holder *only* control rights and no benefits in terms of priority".[33] And in their empirical study of the cycle of financial distress in the UK's SME sector, Franks and Sussman point out that "The crucial feature of the floating charge is that it grants the holder the right to take control of the firm in the event of default, through the appointment of an Administrative Receiver. Control of the firm allows discretion over whether to realize the assets by selling the firm as a going concern or liquidating it. These control rights can considerably influence the size of the proceeds accruing to the creditor".[34]

This brings out an element central to an accurate understanding of the floating charge. This is the ability to replace the existing management with an outsider. Franks and Sussman focus on the benefits to the floating charge holder of the ability to do so, but there are obvious advantages for other 'stakeholders' as well. Suppose we divide the causes of default on part of the debtor broadly into two categories:[35] management-related (to do with the incumbents' "irrationalities, lack of ability, failures of strategy and deficiencies of understanding", etc.),[36] and management-unrelated (external shocks, macroeconomic comparative disadvantages, inflation, over-regulation, delayed payments, government policies like those on taxation, etc.).[37] The former category is crucial. Surveys of insolvency professionals routinely identify management-related causes as being of the greatest importance in corporate failures.[38] So for example, one in two companies undergoing formal insolvency proceedings had suffered distress in the past,[39] "yet the company's directors still did not prevent insolvency".[40] It is a reasonable assumption that at least

[32] Oditah, e.g., provides an insightful discussion in 'Lightweight floating charges'.
[33] J Armour and S Frisby, 'Rethinking receivership', (2001) 21 OJLS 73 at 90. The thrust of the argument here is that such a legal system is not only conceptually possible, but in fact, given the generally poor and universally unreliable priority of the floating charge, is more or less our system.
[34] *Cycle* at 6 (footnote omitted).
[35] See generally Finch at 126-40.
[36] Finch at 259.
[37] *Ex hypothesi*, this latter category excludes 'external' factors which a reasonably competent management would have anticipated and taken steps effectively to deal with.
[38] Finch at 126 n. 34, provides a useful summary. Perhaps this is to be expected: insolvency practitioners clearly have an incentive to reinforce the suggestion of their relative superiority over humdrum non-'professional' managers. This might encourage their services to be resorted to more frequently and at an earlier stage of the corporate distress cycle (and so perhaps for longer). Even if that is the case (on which no position is taken here), it is probably true that, for the reasons to be explained in the text below, management failings are the primary cause of a significant proportion (perhaps the majority) of corporate insolvencies.
[39] *9th Survey* at 2. Franks and Sussman report this figure to be just over one in three; *Cycle* at 7 Table 2.
[40] This comes (inevitably, since that is the main available source of information) from the ABRP's *9th Survey* at 2; note, however, that this seems to assume that managerial action *could* have prevented insolvency.

some of these insolvencies could have been avoided by providing better leadership to the company. Indeed, insolvency practitioners claim that about one in four insolvencies could have been prevented if directors had sought timely advice, but since they did not, "in 4 out of 5 cases there was nothing [that] could be done to save the *company* by the time an insolvency practitioner had been appointed".[41] Subject to appropriate qualifications as to how much weight such findings should be given, we can postulate that *some* companies would be able to avoid insolvency through a change in management. In the case of such companies, other 'stakeholders' would generally be better off if such change could be brought about at the right time.

Now when a debtor appears to be on the verge of defaulting on its obligations, the preceding analysis provokes the question of how we might design a system which can distinguish between businesses that would benefit from a change of leadership (i.e. those beset by management-related problems) and those that would not, and once this information is at hand, how we might ensure that it could effectively be made the basis of a decision to act appropriately.[42] Gathering information is of course costly, and requires both accumulated expertise and influence over the debtor. Ideally, it would be based on (a) the debtor itself reporting potentially relevant information to an appropriate decision-maker, which in turn (b) has the competence to decide whether the information indicates management failings, and if so, (c) has the ability to remove the management without unnecessary expense and replace it with a better one. Let us examine each of these steps in turn.

First, then, consider the relevance of the fixed charge. Loans secured with a fixed charge are almost universally subject to covenants requiring that the value of the secured assets, or the income from them, or both, not fall below a certain multiple of the debt secured.[43] Especially when the charge is over strategically important assets, this creates the necessity for the debtor to explain to the charge holder the strategy pursued, business decisions made, and results obtained. Further, the fact that the charge encumbers the collateral means that attempts to dispose of these crucial assets would only succeed if the charge holder approves. This again necessitates the provision of information justifying the decision to sell. This minimises waste: remember that it is cheaper for the debtor to volunteer such information than for the creditor to have to extract it for itself. From the perspective of junior creditors, the benefit is that management's attempts to substitute assets (machinery for cash, say, or cash for employee-hours) so as to increase the riskiness of the debtor's activities – which would reduce the expected value of all their claims – become subject to external scrutiny. More relevant to this discussion is the fact that the flow of such information over a period of time would allow a picture to be built up of managerial competence, and this picture might be available for examination, should the debtor threaten to default on the secured loan. However, providing this information and obtaining the consent of the creditor to crucial decisions by persuading the latter of their wisdom, is costly for the debtor (not least in time and the marshalling of evidence and arguments). It follows that, especially for debtors in the SME sector, these costs would be justified only 'once over', i.e. for one 'main creditor' per debtor. Any duplication would generally be grossly wasteful.

This last point is reinforced by the fact that all this information provision and gathering is useful only if the chosen creditor has the ability to make use of it. Developing the competence to assimilate it and react appropriately would be costly, and economies of scale and the need for

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[41] Ibid. (emphasis added to emphasise that this should not be regarded as identical with the company's *business*, which might still be saved, as discussed below).
[42] This draws on Armour and Frisby, 'Rethinking receivership' at 82-6.
[43] D Citron, 'The Incidence of Accounting-Based Covenants in UK Public Debt Contracts: An Empirical Analysis', (1995) 25 Accounting and Business Research 139, especially at 144-5.

accumulated expertise ensure that only repeat players fit the bill. Even then, of course, the benefits of being able to tell badly managed businesses (whose value could therefore be increased by a change of management, to the advantage of all those with claims against it) from those troubled for other reasons, would have to be sufficiently large to justify this expenditure. A large number of dispersed creditors, each potentially entitled to a minute fraction of this 'surplus', simply would not have a sufficient incentive to invest in this type of monitoring. If this surplus is to be preserved, this point indicates the need for a repeat-playing creditor which provides a significant proportion of the debtor's credit needs and thus has a significant stake in any surplus from remedying the debtor's management deficiencies.[44] The most obvious such actors are banks, and as recent research highlights, there are indeed extensive monitoring arrangements within them. Monitoring takes place both at individual branches and at specialist 'central rescue units' operated by the banks. Firms sent to these units remain there for seven and a half months on average, and up to seventy-five percent of these are turned around. There is also strong evidence that banks often encourage firms to remove members of their management team, and further, that firms significantly improve their chances of being turned around if such changes are made.[45] There is little doubt, therefore, that there is an investment on part of main creditors both in information gathering at individual branches and central 'central rescue units', and in the development of expertise in distinguishing bad managers from good ones.

This leads to the third step in the problem mentioned above, that once information about management competence has been gathered and analysed, the party in possession of it should be able to take appropriate action on its basis. The potential problem here would arise if this creditor had to convince other creditors or a court of the desirability of replacing the existing management. This is a problem precisely for the reasons mentioned, that verifying the evidence in court might be expensive (at least in terms of time), and that other creditors might not have sufficient experience and expertise in being able to tell, say, a bad managerial team apart from a merely unfortunate one. Further, other creditors, who might only enjoy a tiny proportion of any surplus arising from the replacement of poor managers, would suffer incentives to hold out for side-payments from the main creditor.[46] Concentrating decision-making powers as to the future of the management in the very creditor which has built up and assimilated information concerning these factors would resolve these problem.

This gets us to the point where we must postulate the need for something like the institution of receivership.[47] But it does not explain the need for a floating charge. *Ex hypothesi*, the 'main' creditor would have *fixed* charges under which it would enjoy the right to appoint a receiver with respect to the property subject to those charges. However, this by itself might not be satisfactory. Recall from the discussion above that subjecting assets to fixed charges involves significant costs both for the debtor and the lender. The essence of the fixed charge is that its holder has *control* over the disposal or (through the operation of loan covenants) significant change of use of the collateral.[48] We have noted the benefits of this control, but it also

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[44] This draws on Armour and Frisby, 'Rethinking Receivership' at 84-6, and the sources they cite at nn. 84-9.

[45] This summarises some of the evidence in *Cycle*.

[46] Armour and Frisby, 'Rethinking Receivership' at 84 including n. 74.

[47] See e.g. Armour and Frisby, 'Rethinking Receivership' at 86-91. The appointment of a receiver suspends the managerial powers of the debtor's board of directors; *Moss Steamship Company Ltd. v Whinney* [1912] AC 254, 263 (though the case concerned a court appointed receiver); *Meigh v Wickenden* [1942] 2 KB 160, 166; and *Gomba Holdings UK Ltd v Homan* [1986] 1 WLR 1301.

[48] See e.g. *Agnew v Commissioners of Inland Revenue* [2001] UKPC 28, [2001] 3 WLR 454 at [32].

significantly constrains the debtor's ability to use those assets in the normal course of business.[49] For some 'circulating' assets, such as certain types of machinery, trading stock, and receivables,[50] the cost of crippling the debtor by rendering it unable to proceed without the creditor's consent, would far outweigh the benefits of the latter's monitoring. So creating fixed charges over such assets would often not be a rational strategy. This creates a problem *ex post*, once there is both a default and good reason to believe the management should be displaced. The benefits of removing the existing management would only accrue if this removal applied to the *entirety* of the debtor's undertaking. This might be because of the synergetic values of retaining under one management precisely those assets which could not rationally be subjected to the draconian discipline of the fixed charge. And in any case, what would have been badly managed would be the entire business, including those assets; so the incumbent managers' powers would best be curtailed with respect to the entire business. This would benefit all those interested in the undertaking of badly managed companies by improving their chances of survival, or otherwise by ensuring the value-preserving disposal of their business.

This, it is submitted, explains why floating charges are ubiquitous despite their poor priority position: they represent the residual element in the set of rights required properly to displace a poorly performing management. This also explains why they are generally coupled with fixed charges: the latter provide priority, encumbrance, and risk assessment, and also ensure a supply of the information that is vital to the effective deployment of the floating charge. Further, this analysis reveals why floating charges are generally taken over the debtor's entire undertaking, or else used – in combination with a fixed charge – with respect to assets not subject to the fixed charge. Their role is to 'mop up' and divert away control over (and *not* priority in) assets which, while the existing management is doing well, would best be left at their disposal.

Finally, we can also now understand why the oft-repeated criticism that the deceptiveness of the floating charge has never appropriately been remedied because the mechanism chosen for this purpose – registration – has never been efficacious, is also misplaced.[51] In fact, registration is not meant to counter the imaginary deceptiveness of the floating charge. Registration serves the different purpose of revealing the identity of the main creditor of a company. Under the pre-Enterprise Act law, it would be important to know for this purpose whether someone has fixed and floating security over all or almost all of the company's property (rather than to know exactly how much this person is owed). This would allow co-ordination of efforts by creditors to monitor the company's managers in order to control financial agency costs and also to build up a picture of their general competence. One way in which this might happen would be for potential creditors – notably, a second bank that might otherwise have set up its own monitoring arrangements – to refuse to lend upon discovering the existence of a prior floating charge (or else to enter into some arrangement with the first bank so as to avoid wasteful duplication of monitoring etc.).[52] Now because of its poor and unreliable priority, a floating charge is unlikely to be taken in isolation, and would generally be coupled with other, fixed, security over some or other of the company's property. This is bolstered by statutory provisions discouraging the taking of floating charges

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[49] This has long been recognised; see e.g. *In re Florence Land and Public Works Co* 10 Ch D 465, 541 *per* Sir George Jessel MR, and *Biggerstaff v Rowatt's Wharf Ltd* [1896] 2 Ch 93, 101 and 103, *per* Lindley and Lopes LJJ. Both cases are mentioned by Lord Millett in *Agnew* at [7].

[50] See, e.g., Finch at 81-2.

[51] See e.g. Lord Millett in *Agnew* at [10]. His Lordship describes the requirement that floating charges be registered as of providing merely "theoretical" rather than real benefit to trade creditors, the alleged victims of the floating charge's deceptiveness. For the reasons given in the text here, this is as it should be, since the perceived 'mischief' of the floating charge might also be merely "theoretical", not real.

[52] That one way of co-ordinating creditor actions is precisely to ensure only one creditor capable of monitoring the debtor lends to it is sometimes missed by commentators.

unless the creditor offers new value.[53] A creditor seeking security is not going to offer new value without gaining priority, and it cannot gain priority in a reliable and useful manner with a floating charge. This further increases the probability that a floating charge would be coupled with fixed security. It follows that the declaration of a floating charge on the register is a good signal of the existence and identity of a creditor playing the role of main creditor.

Finally in this Section, it would be helpful to consider the mechanisms whereby control is transferred away from the management of a troubled debtor.[54] The usual way of capitalising on the fruitful co-working of the fixed and floating charges in the past has been receivership.[55] The receiver may be appointed when there is a default on the secured loan. His appointment will accompany another significant event. Either the default itself, or his appointment, will crystallise the floating charge. Once in office, the receiver draws his powers from two sources.[56] His *in rem* powers "are held in right of the debenture holder and derive from the security created by the debenture. They include the power to collect in the assets comprising the security, to possess, control and use those assets and to deal with and dispose of them, whether by way of sale, lease, charge or otherwise".[57] His *personal* powers arise by virtue of the fact that he is regarded, by the terms of the debenture, as the debtor company's agent, and thus has the power on its behalf to carry on its business.[58] And in order to allow these personal powers to be exercised effectively, the law implies into the debenture a promise on part of the company that its board would not interfere with the receiver's running of the company.[59] Importantly for our purposes, note the three main uses of the *in rem* powers derived from the *floating* charge by the receiver. First and as already mentioned, it acts to divest the board of control over these circulating assets, since the crystallisation of the floating charge finally encumbers the collateral, and any subsequent unilateral attempts to pass those assets out of the ambit of the security would not succeed. Second, the crystallised charge takes priority over, say, charging orders. Were this not the case, unsecured creditors would have an incentive to rush to press their claims, thus causing the business to be dismantled and any going concern surplus to be lost. Because of the floating charge, however, the receiver is taken to be dealing with assets subject to the property rights of the charge holder, the party with the prior (because of its fixed security) and often primary

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53 Insolvency Act 1986, s. 245, decreases the net expected utility of taking a floating charge without offering new value.

54 This discussion draws on Goode, *Insolvency* at 215-7 and 237-9.

55 For the purposes of this argument, no distinction need be drawn between administrative receivership, and the receiver and manager of the pre-Insolvency Act 1986 law, except to note that where there is some reference here to powers *presumptively* granted to the administrative receiver by the Act, it will be assumed unless otherwise stated that the receiver and manager would have had equivalent powers *explicitly* under the debenture itself.

56 For a statement which comes close to eliminating the distinction between *in rem* and personal powers, see *Independent Pension Trustees Ltd v L.A.W. Construction Company Ltd* 1997 SLT 1105, 1110, *per* Lord Hamilton. His Lordship stated that an appropriately drafted floating charge could in principle encompass all commercially significant rights and powers of the company vested in its board. This should be read subject to the qualification that, at the very least, the right to challenge the validity of the debenture itself must as a matter of conceptual necessity remain with the board.

57 Goode, *Insolvency* at 237.

58 These powers include being able to raise or borrow money and grant security, appoint a solicitor, accountant or other professional, bring or defend actions, refer to arbitration any questions affecting it, effect and maintain insurance in respect of its business and property, use its seal, execute deeds or receipts on its behalf, appoint an agent, call up any uncalled capital, and change the situation of its registered offices, etc.; see Insolvency Act, Sch. 1.

59 See e.g. *Gomba Holdings UK Ltd v Homan* [1986] 3 All ER 94 at 98.

interest in the collateral.[60] Third, once the company goes into winding-up, the receiver's agency relationship with the company terminates. However, the receiver's *in rem* powers with respect to substantially the *whole* of the company's property persist (including over those assets which could not be subjected to a fixed charge), thus allowing him to continue deploying all of it in a value maximising manner. Having to hand some assets over to the liquidator might destroy synergies.

The *absence* of this feature would have several disadvantages in addition to those already noted. First, it would encourage other creditors to engage in rent-seeking behaviour by threatening to initiate a winding up, which would disrupt the receivership precisely by removing from the receiver's control assets not subject to the fixed charge. Second and following from that, if the expected cost of making these side payments was greater than the expected benefit to the charge-holding 'main' creditor of investing in information gathering and assimilation (as a prelude to initiating receivership if necessary), it would create a disincentive for it to do so. To the extent that this diminished its ability to detect and control financial agency costs, this would be harmful to all the claimants as a group. And third, it might encourage the 'main' creditor to substitute liquidation for receivership as the chosen method of management displacement. This would be undesirable because it might be more expensive to prove to a court's satisfaction that the company's liabilities exceeded its assets or that it was unable to pay its debts as they become due.[61] Much more importantly, the ability to remove the management by relying on a 'technical' default on a covenant in the debenture (e.g. requiring the income from some assets not to fall below a particular level) might be lost. An important benefit of the floating charge is its contribution to displacing the incumbent management *before* the company becomes insolvent in a way verifiable in court (and therefore perhaps more irredeemably).

4. An Old Problem

The discussion so far enables a bit of new light to be thrown on an old problem: the troublesome matter of distinguishing between fixed and floating charges.[62] Confusion as to the whereabouts of the boundary between these is a consequence of the confused view that, in however weak a manner, the floating charge is about gaining its holder priority. The key to this problem once again is to remember that the floating charge is not a priority-based device. This is important because encumbrance is a function (among other things) of priority, encumbrance and control (of the encumbered asset by the chargee) are necessarily related, and control is precisely what distinguishes fixed from floating charges.[63] Let us see what this means.

Consider the relationship between two of the features usually associated with a security interest, that with respect to the assets charged, it grants priority to its holder over the debtor's other creditors, and that it encumbers the assets so that they cannot be put beyond the ambit of the security without the security holder's consent. Now it is not possible to conceive of an asset being

[60] This point is sometimes missed. Note also that preferential creditors, who do hold claims enjoying priority to that of the floating charge holder, would generally have no incentive to act precipitously for the same reason, viz., that their claims have statutory protection over those of the charge holder. Given the unnecessarily perverse structure of receivership, however, this confidence is not always justified; see the discussion below of occasional opportunistic behaviour by receivers.

[61] Insolvency Act, s. 123. In many circumstances, this problem can be overcome by reliance on the effect of the s. 123(1)(a) statutory demand. See also *Taylor's Industrial Flooring v M&H Plant Hire* [1990] BCC 44.

[62] Uncertainty on this point is bemoaned by, e.g. Finch at 103 and 305; see also the sources cited at n. 154.

[63] As recently reconfirmed by the Privy Council in *Agnew*.

encumbered without relying on the notion of priority. To say that a charge encumbers an asset is simply to say that if the asset is transferred without the chargee's consent, the chargee would continue to enjoy priority in any proceeds of sale,[64] and that in appropriate circumstances, the transferee's title to the collateral is subject to the chargee's interests. To encumber an asset *is* to 'entrench' the priority of the chosen claim with respect to the asset and its proceeds by giving the claimant a veto over any attempt by the debtor unilaterally to disturb that priority. So understanding that the fixed charge is connected with priority – in a way that the floating charge is not – helps us distinguish between the two types of charge. A charge only encumbers collateral if it entrenches the priority of its holder's claim, and an asset can only be encumbered by the charge if the chargee is given control over the use and disposal of the asset.[65] Not to have control means not to have priority. The floating charge has neither one nor therefore the other.

Importantly, it also follows that there is a price the chargee must pay for securing priority with respect to the proceeds of the assets in the debtor's insolvency. In order to do so, it must create and operate the mechanisms necessary for monitoring the use and disposal of the charged assets, and this it would do by exercising control over the collateral.[66] This is a substantive requirement, not merely a formal one, so that if no control were in fact exercised by the chargee, then the charge would be characterised as a floating one regardless of the parties' professed intentions.[67] Having such control does not, of course, ensure that all fixed charge holders would effectively monitor their debtors. As mentioned above, monitoring in this context is about gathering information about the debtor's use of its assets, and about holding a veto over their disposal or (because of loan covenants) changes in the use made of them. But monitoring is also about being willing and able to assimilate this information and having the expertise to judge good from bad management decisions. The discussion above ties the creditor's acquisition of priority to its possession and exercise of the power to sanction disposal of the collateral or changes in its use. How wisely the creditor exercises these powers is a different matter. Be that as it may, we can see that granting priority does at least create the opportunity for the priority-holding creditor to monitor the debtor with a view to controlling financial agency costs, and perhaps also, to build up a picture of managerial competence.

This also shows why it should not generally be possible to 'separate' a book debt from its proceeds, in order purportedly to create a fixed charge on the former and a floating one on the latter. We can understand these points through an examination of the notorious Court of Appeal decision in *Re New Bullas Trading Ltd*.[68] The debtor D had agreed to grant "fixed" charges over all its book debts to creditor C, and to pay all proceeds into a designated account. By the time this money reached the specified account, the agreement creating the charges envisaged that one of two things would have happened. There would either have been an event such as an order for the debtor's winding up or a petition to put it into administration, or the levying of distress against its property by another claimant followed by a demand by C, in which case the money in the account

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[64] See e.g. *Foskett v McKeown* [2000] 3 All ER 97 at 119.

[65] Consistently with this, see Millett LJ in *Re Cosslett (Contractors) Ltd* [1998] Ch 495 at 510.

[66] This suggests one reason why 'negative pledge clauses' are not usually effective; these often seek to ensure priority for a creditor without setting up real opportunities for the creditor to monitor. The same hostility displayed by English law to priority without monitoring could perhaps be seen in its attitude towards retention of title clauses, especially those concerning materials not in the form supplied (since the chances of the supplier being able to monitor these effectively are particularly slim).

[67] See e.g. Lord Millet in *Agnew* at [27]: "But the banks did not want to monitor the bank account and be required to give their consent whenever the company wished to make a withdrawal. They wanted the best of both worlds. They wanted to have a fixed charge on the book debts while allowing the company the same freedom to use the proceeds that it would have if the charge were a floating charge."

[68] [1994] 1 BCLC 485.

would be subject to a fixed charge and would not be dealt with except as directed by C. Alternatively, there might have been no such event, in which case the money deposited in the account would be "released from the fixed charge" and would become subject to a floating charge, allowing D to deal with it in the normal course of business. Speaking for the Court of Appeal, Nourse LJ held that

> "just as it is open to contracting parties to provide for a fixed charge on future book debts, so it is open to them to provide that they shall be subject to a fixed charge while they are uncollected and a floating charge on realisation."

The discussion above shows that this argument is a *non sequitur*. Taking the relevant issues in turn, three points should be noted. First, we should ask whether C was capable of effectively acting as the main creditor, able – in the way described above – to harness together fixed and floating charges in a mutually beneficial way. The answer must be in the negative. The charges granted to C were not the only ones at play. Prior fixed and floating charges had been granted to the very bank that operated the account into which the proceeds of book debts were to be deposited. The duplication inherent in granting C a similar package of security interests throws doubt on its usefulness. D was not a particularly large company, and so, as noted above, the investment required to derive utility from this sort of security package would only have been justified once over, i.e., by one creditor. Any duplication of information provision and assimilation would have been wasteful for the parties concerned. This should lead us to expect that no such duplication would be present. What is more, the bank would have an inherent advantage over C in monitoring the deposits in and especially the withdrawals from the account that D held with it.

So second and unsurprisingly, it is clear from the facts that C's security package was virtually devoid of monitoring potential. As discussed above, information about the use of assets *actually* subject to fixed security would be provided by the debtor when it sought the security holder's permission to dispose of those assets, or to exchange them for riskier ones. For book debts, this happens when they convert into money in the debtor's hands, most obviously and importantly, by being collected. At this point, the debtor comes in possession of cash that might be used in riskier or negative net present value ways. So it is here that outside monitoring would be most useful. The contested debenture in *Re New Bullas*, on the other hand, gave D the right to deal with the proceeds in the normal course of its business precisely at this point, thus obviating the need for it to provide any information to C. In fact, the agreement clearly envisaged that C would rely on monitoring done by the bank: it permitted the latter to furnish to C any financial statements and other information available to it about D's assets and liabilities. The fact that C had given no directions at all as to the book debts subject to the charge even when D became seriously distressed[69] supports the conclusion that (perhaps other than reliance on the bank's actions) C was not doing any monitoring of D. So third and finally, the Court's reasoning is fallacious. It is perfectly possible to create a fixed charge on future book debts by ensuring that, *inter alia*, the debtor accounts to the charge holder for their proceeds as and when they are collected. However, it is not possible for a charge to be 'fixed' if it does not ensure the provision of at least some information to its holder regarding use of the collateral.

[69] See e.g. the account of the facts in the first instance judgment at [1993] BCLC 1389.

5. The Changeover from Administrative Receivership to the 'New' Administration

It is important to note that the emphasis of the argument here is not on vesting control over the debtor in someone, like a receiver, who owes primary (in many respects, exclusive) allegiance to the holder of the floating charge. None of the analysis above depends on any arrangement featuring such single-minded devotion to the latter's interests.[70] The focus, instead, is on *di*vesting the incumbent management of control. In fact, it is almost certainly the case that receivership, especially under the wholly malign influence of decisions like *Downsview Nominees*,[71] has developed features that, apart from being unnecessary to the mutually beneficial operation of the floating charge discussed above, are both exploitative and value-destroying.[72] All of these undesirable incidents of receivership have the same roots. They are manifestations of the motivation costs created by the fact that the receiver expects to benefit from repeat appointments sent his way by a small group of institutions which act as main creditors with respect to an overwhelming majority of companies undergoing formal insolvency proceedings,[73] who has predominant responsibility for the appointing creditor's interests, but the costs of whose actions – including irredeemably wasteful acts or omissions – is mostly borne by a separate group of claimants.

Receivership is harmful in at least three respects. First, there are the costs of the procedure itself, which amount *on average* to a quarter of the value of the assets in the insolvent estate.[74] A process that consumes such a large proportion of the value it is meant to be distributing to a pre-determined group of claimants is intrinsically absurd.[75] The wastefulness of the process is strongly indicated by the fact that when receiverships have been tendered out (thus focussing the burden of any wasteful behaviour primarily on the insolvency practitioner concerned), their costs have fallen dramatically.[76] Arguably, Parliament saw the potential for just this type of motivation cost to be acute in the institution of receivership when it provided a power for the liquidator to approach the court to set the receiver's remuneration.[77] However, the courts (here as in so much else to do with receivership) destroyed the usefulness of this provision by insisting that they would only intervene if the level of remuneration set in the debenture was plainly excessive.[78] Given that standard terms in debentures provide that the receiver's remuneration would be fixed by reference to the charging practices of the receiver's firm,[79] and given also that the motivation costs mentioned above could be expected to be endemic within the

[70] Indeed, receivership may not necessarily have developed in a way which conflates the perfectly distinct functions of (a) managerial displacement, and (b) exclusive and unilateral pursuit of the charge holder's interests. So for example, the receiver is considered the agent of the company, and interference with his activities might cause the charge holder to become his principal and thus be liable for any default; see *In re Vimbos* [1900] 1 Ch 470.

[71] *Downsview Nominees Ltd v First City Corporation Ltd* [1993] AC 295.

[72] With respect and for reasons which follow, Armour and Frisby are at their least persuasive in what overall is a very persuasive paper when they argue against the point being made here; see the discussion in 'Rethinking Receivership' at 100.

[73] See e.g. D Milman and D Mond, *Security and Corporate Rescue* (Manchester, Hodgsons, 1999).

[74] Franks and Sussman, 'Resolving financial distress by way of a contract: An empirical study of small UK companies' (22 October, 2000), available at URL: <www.ifk-cfs.de/papers/franks.pdf> at 32-3.

[75] By contrast, formal insolvency proceedings cost on average 13% in Sweden and 14% in the US; see ibid.

[76] *Cycle* at 15.

[77] Insolvency Act, s. 36 (this provision makes no explicit reference to indemnity or reimbursement, though the argument in the text here applies to these as much as it does to the receiver's remuneration); see also Companies Act 1948, s. 371(1).

[78] *Re Potters Oils Ltd* [1986] 1 WLR 210.

[79] Lingard, *Bank Security Documents* (London, Butterworths, 1993 3rd ed.), para. 7-04.

institution of receivership regardless of the receiver's firm, the practical effect of this approach was to render the statutory provisions nugatory. The result is that, even by itself, this externality associated with receivership is probably sufficient to eat up most of the efficiencies generated by the otherwise beneficial joint operation of fixed and floating charges.

Second, receivers are now known sometimes to engage in rent-seeking behaviour on behalf of their appointor by attributing some costs to the floating charge instead of the fixed one, with a view to inflating the recoveries under the latter.[80] This is a practice which does cause loss to be moved from the party best placed to deal with it *ex ante*, to those worse placed to do so. This is doubly the case since it is unpredictable *when* such rent-seeking behaviour might benefit the main creditor and when in turn a receiver might resort to it. So the fact that it might happen is unlikely to bring any (even theoretical) compensating benefits, in the form of lower interest rates from the main creditor, say. Third and most generally, there is the receiver's astonishing privilege to inflict harm on those, other than his appointor, who are interested in the debtor's estate, even when this would bring no benefits to his appointor.[81] This simply cannot be justified, for reasons of simple consistency in addition to everything else. Consider the receiver's duty, owed to junior charge-holders etc., to obtain the proper market price for the charged assets.[82] Keeping aside historical reasons, there is only one justification for this duty. This is what we might call the principle against gratuitous harm: not to require the receiver to obtain a proper market price would be to allow him to inflict gratuitous harm to the interests of junior claimants, which by definition is without reason and thus without justification. But if this principle applies to matters concerning the sale price of the charged assets, there is simply no reason for it not to apply to other functions performed by the receiver. In any case, receivership, as governed by *Downsview* and others of its ilk, is probably the only legal institution where property subject to the rights of a group of individuals is placed under the control of a person *not* bound to them by a general principle against gratuitous harm. It is for this reason that decisions like *Medforth v Blake*[83] are so welcome.[84]

Be that as it may, taking all these factors together makes it clear that few have reason to mourn the passing of this value-destroying, exploitative and anomalous institution.[85] Importantly, however, we should keep in mind the clear distinction between the floating charge, and receivership, the latter being only *one* possible way in which the advantages of this type of charge might be captured. Nothing in this discussion detracts from the analysis above, which points to the benefit of a properly informed creditor being able to remove the under-performing management of a defaulting firm without having to expend resources persuading other creditors or a court of the wisdom of this decision.

I suggest that the recent legislative changes to administration have moved precisely in this direction.[86] Under the changes introduced by the Enterprise Act 2002, an administrator might be appointed either by court order or out of court. The latter route is generally available only to the debtor company itself or its directors, and to the holder of a security package that includes at

[80] Franks and Sussman, 'Resolving' at 18.
[81] See e.g. Finch at 266-7.
[82] Confirmed even by *Downsview Nominees*.
[83] [1999] 3 All ER 97.
[84] Under the new legislation, the principle against gratuitous harm can now be found explicitly in Enterprise Act 2002, Sch. 16 (hereafter, 'Sch. 16'), para. 3(4)(b).
[85] Enterprise Act 2002, s. 250.
[86] So e.g., Finch at 270-2, recognises (though not for the reasons suggested here) that the new administration procedure might be regarded as an improved and more 'inclusive' version of receivership.

least one floating charge and which covers substantially the whole of the company's property, i.e. the main creditor. The court order route is open in addition to any of the company's creditors (and to the justices' chief executive for a magistrates' court). Consistently with the analysis above, three points are of interest here. First, the main creditor may continue to appoint an administrator on the basis of a 'technical' default under the debenture secured by the floating charge. It need not be demonstrated that the company is insolvent, whether the administrator is appointed out-of-court[87] or by court order.[88] As noted above, this would allow a poorly performing management to be displaced early enough for the debtor to have a better chance of survival. Contrast this with the fact that *anyone* else seeking to appoint an administrator through either route would have to rely upon the fact that the company is or is likely to become unable to pay its debts.[89]

Second, ordinary creditors would have to prove to the court's satisfaction that the administration order was reasonably likely to achieve the "purpose of administration".[90] Given the way the purpose of administration has been framed in the legislation,[91] this is likely to be a significant burden for most creditors. Note that before ordering an administration, the court would have to be satisfied of one of three things. First, the petitioning creditor would have to show that the administration was required to rescue the company as a going concern, which in turn would require the demonstration that despite its insolvency, the company was still more valuable as a going concern and hence worth preserving,[92] *and* (at least by implication) that the directors were unwilling to or incapable of complying with their duty to direct their best efforts to bringing about

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[87] Sch. 16, para. 16.

[88] Sch. 16, para. 35(2).

[89] Enterprise Act 2002, Sch. 16, paras. 11(a) (court order) and 27(2)(a) (out-of-court appointment by the company or its directors). In the case of directors, this requirement probably exists to counter the motivation costs arising in a situation where the advantages to the directors of having a moratorium in place outweighed the costs of administration *to them*, even though administration was not in the interests of all the relevant parties as a group. The declaration of insolvency (or near insolvency) required of them serves to bring home to them the fact that the company would thenceforth be operated (at least until it recovered), not in *their* interests (say) *qua* shareholders, but in the interests of its creditors as a group.

[90] Sch. 16, para. 11(b) and the definitional para. 111(1).

[91] The statutory objectives of administration have been defined and ranked in a very interesting way, and are worth producing here in their entirety. Sch. 16, para. 3 provides that:

> (1) The administrator of a company must perform his functions with the objective of-
> > (a) rescuing the company as a going concern, or
> > (b) achieving a better result for the company's creditors as a whole than would be likely if the company were wound up (without first being in administration), or
> > (c) realising property in order to make a distribution to one or more secured or preferential creditors.
>
> (2) Subject to sub-paragraph (4), the administrator of a company must perform his functions in the interests of the company's creditors as a whole.
>
> (3) The administrator must perform his functions with the objective specified in sub-paragraph (1)(a) unless he thinks either-
> > (a) that it is not reasonably practicable to achieve that objective, or
> > (b) that the objective specified in sub-paragraph (1)(b) would achieve a better result for the company's creditors as a whole.
>
> (4) The administrator may perform his functions with the objective specified in sub-paragraph (1)(c) only if-
> > (a) he thinks that it is not reasonably practicable to achieve either of the objectives specified in sub-paragraph (1)(a) and (b), and
> > (b) he does not unnecessarily harm the interests of the creditors of the company as a whole.

[92] Otherwise, Sch. 16, para. 3(3)(b) would apply.

a turnaround in its fortunes.[93] Merely showing that the company was unable to pay its debts probably would *not* do, since that would still leave open the possibility that its distress was due to management-unrelated factors which the current directors themselves could steer it out of.[94] Second and alternatively, the creditor would need to convince the court that interposing administration before liquidation would achieve a better result for the company's creditors as a group, probably by preserving the company's business, in whole or part, as a going concern. Once again, this would obviously depend on demonstrating that the company's existing management was not complying with its legal obligations.[95] Competent managers could be relied upon to perceive and respond to the need either for a formal insolvency proceeding (liquidation or administration) or at the least, the benefit to the company of the moratorium obtained through, say, administration, on the pursuit of claims against it. Finally and if neither of the above conditions was satisfied, the petitioning creditor would have to show that an administrator would be better able to realise the company's property in order to make a distribution to secured or preferential creditors as appropriate, than the incumbent management. For the reasons already given, this could only be done by showing that the managers were not taking every step they reasonably ought to be taking to minimise loss to the company's creditors (including, if appropriate, the initiation of a formal insolvency proceeding).[96]

For most creditors, being able to muster the evidence and arguments necessary to meet this burden would be very difficult indeed, requiring at the least something equivalent to the Rule 2.2 report that had virtually become a *sine qua non* for a successful application for administration under the old law.[97] The central aims of obtaining something like this report are of course to gather information about the debtor, and about whether it would benefit from the change of management that administration brings about. If the arguments made above are correct, the requirement to have such a report prepared should be waived for the main creditor, since the latter

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[93] The duty derives from, e.g., *Kinsela v Russell Kinsela Property Ltd (in liq)* (1986) 4 NSWLR 722, 730, *per* Street CJ; quoted with approval by Dillon LJ in *West Mercia Safetywear Ltd (in liq) v Dodd* [1988] BCLC 250, 252-3. In some circumstances, s. 214 of the Insolvency Act 1986 might also be relevant; see e,g, the discussion in Mokal, 'An agency cost analysis of the wrongful trading provisions', [2000] CLJ 335, at 365-6. The statutory duty would not *generally* be relevant under this head of the 'purpose of administration' because administration here is meant to rescue the company, while s. 214 applies only when there is no reasonable prospect of avoiding insolvent liquidation.

[94] This flows from the undeniable observation that replacing the directors with an administrator is costly, and that it would be unjustifiable to incur these costs if the incumbent management itself could steer the company out of crisis. The statutory context is provided by r. 2.4(2)(e) of the Insolvency (Amendment) Rules 2003.

[95] This is where s. 214 would certainly be relevant. We are now concerned with the situation where attempting a rescue no longer appears advisable (Sch. 16, para. 3(3)), or in other words, that there is no reasonable prospect of avoiding an insolvent liquidation. At this point, directors come under a duty to take every step they reasonably ought to, to minimise loss to their company's creditors. This here means, most obviously, attempting to preserve any going concern surplus when disposing of the company's business.

[96] Note that because of the reference to secured creditors here, there is only a partial overlap between satisfying this particular requirement, and showing a breach of s. 214: the latter imposes no duty on directors with respect to secured creditors. See the discussion in Mokal, 'Wrongful trading', especially at 357-60 and 364-5.

[97] Insolvency Rules 1986, r. 2.2. Note also Sch. 16, para. 36, which allows the main creditor to intervene in any application to appoint an administrator not made by it, and to ask for its nominee to be substituted in place of the one nominated in the application. Arguably, the former would be more likely to fulfil the purpose of administration than the latter, perhaps because of the superior information provided to him by the main creditor. There also seems to be some discouragement here for other creditors to invest (perhaps wastefully) in something like a Rule 2.2 report, since the person whose appointment this report would back might never assume office.

could be presumed to have acquired precisely that information through the normal operation of his security interests. A report would be superfluous and thus wasteful both of time and resources. The new law is quite consistent with this analysis. Under it, the company's directors, and more significantly, its main creditor, both are allowed to proceed without a court order simply on the strength of a statement by the intended administrator that "in his opinion the purpose of administration is reasonably likely to be achieved".[98] This treats the directors and the main creditor as on par in being in possession of information as to whether the company's business would benefit from a change of management. Either can be relied upon to arm the intended administrator with this information, enabling the latter to form the opinion that the purpose of administration is likely to be satisfied. This is bolstered by provisions which make it an offence knowingly to rely on a statement in making an out-of-court appointment that is false and that the appointor does not reasonably believe to be true.[99] Crucially, of course, neither the company's directors nor its main creditor have to persuade the court that the purpose of administration is likely to be fulfilled. Instead, the burden of showing the nominated administrator's statement to this effect to be false lies on the party wishing to challenge it.

So third and following from both the points just made, there is a clear reliance on the main creditor to distinguish between a poor management, and a capable but unfortunate one. For the main creditor, the need to persuade the court that a particular debtor could benefit from a change of management is transformed into the need merely to demonstrate that the debtor is in default. The only hurdle that the main creditor must overcome in displacing its debtor's management by this route is exactly the one suggested here, viz., that there is a default on a secured loan, and that it considers itself able justifiably to back the statutory statement by the nominated administrator, viz., that to allow the management to remain in place would be to jeopardise either the company's survival or the interests of all, or if appropriate, some, of its creditors.

6. Why the Floating Charge Must Now be Abolished

The argument so far has been 'positive' in the sense that I have attempted to show the role actually played by the floating charge under the pre-Enterprise Act law, rather than 'normative' in the sense of advocating some change in the law.[100] Finally, however, I want to go further and explain why this paper claims to be an elegy for the floating charge, and not merely a eulogy. I will do so through a three-pronged argument. It will be suggested first that the beneficial role played by the floating charge under the pre-Enterprise Act law has now been rendered useless. This is the demise announced in the title of this paper. Second, the Enterprise Act retains certain functions for the floating charge, but it will be suggested that these do not depend on anything to do with its essential nature. They could equally be performed in other ways, and so do not justify the retention of this device. And finally, it will be claimed that the unnecessary retention of the floating charge will now cause it to operate, if only in a very small proportion of insolvencies, in a wholly exploitative manner.

Taking these points in order, then, recall that before the new administration procedure was introduced by the Enterprise Act, the floating charge was performing two main functions

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[98] Sch. 16, paras. 18(3)(b) (main creditor) and 29(3)(b) (directors).
[99] See Sch. 16, paras. 18(7) and 29(7).
[100] The 'scare quotes' in the text indicate my adherence to the view that invocations of the positive/normative distinction are often highly misleading. What we understand the law to be is inevitably influenced by our views of what it ought to be, though the two need not be identical.

with respect to distressed companies. When such a company defaulted on a secured loan and the main creditor formed the judgment that the default was due to management-related reasons, the (now crystallised) floating charge would be used to mop up control, proprietarily, over those assets which could not rationally be subjected to a fixed charge during the company's normal operation. Second and should liquidation start once receivership was underway, the floating charge would prevent the liquidator taking possession of these assets, thus preserving any synergetic value. The receiver's *in personam* powers to manage the business having ceased upon the initiation of winding-up, he would have to rely on the *in rem* powers gained under the floating charge. Note also that the main creditor would generally (though not always)[101] have preferred receivership, (a) because it could make an out-of-court (and thus non-wasteful) appointment of a receiver but not of an administrator, (b) because the receiver could apply the debtor's assets towards discharging the secured debt while the administrator could not, (c) because of the receiver's near-exclusive attention to the chargee's interests, and of the greater rent-seeking potential of receivership, and (d) perhaps because of the legal-commercial inertia which tends to favour familiar procedures over unfamiliar ones.

Contrast the present position. The new administration procedure creates a status which confers on its holder all the powers the floating charge would have conferred on the receiver, while removing the features that made the 'old' administration undesirable. The administrator acts as the company's agent,[102] his appointment divests the directors of control *globally* (and not, of course, simply over assets subject to fixed security),[103] and also prevents the appointment of a liquidator.[104] The administrator may now be appointed out of court without having to prove insolvency and even on the basis of a technical default, as noted, and he is now able to make distributions to creditors.[105] So all the mutually beneficial functions previously performed by the floating charge have now been rendered redundant.[106]

Second, however, the Enterprise Act retains two important roles for the floating charge. Most important is the way the Act continues to define the main creditor. For the purposes of the Act, this is someone with one or more debentures (a) at least one of which declares that its holder has the right to appoint an administrator, and (b) at least one of which contains at least one floating charge.[107] Now the first condition is unobjectionable, simply requiring a record of the creditor's claim to act as the main creditor for this company. However, the second condition

[101] See e.g. *Cycle* at 8-9 including nn. 3-4.
[102] Sch. 16, para. 69.
[103] Sch. 16, para. 67: "The administrator of a company shall on his appointment take custody or control of all the property to which he thinks the company is entitled."
[104] Sch. 16, para. 42.
[105] Sch. 16, para. 65; ordinary unsecured creditors may only be paid by court approval or if the administrator considers the payment is likely to assist in the achievement of the purpose of administration.
[106] What is absent from administration of course is most of the set of incentives for the office-holder to engage in rent-seeking on behalf of the main creditor, which, needless to say, is the very reason for the legislative rejection of receivership.
[107] Sch. 16, para. 14. Note that para. 14(3)(b) seems to treat as the main creditor (and thus one with the ability unilaterally to displace the management) someone who *only* has floating charges over substantially the whole of the debtor's property but no fixed security. This is inconsistent with the analysis in this paper: in every realistic situation that comes to mind, the floating charge could only properly work parasitically, as an appendage to some fixed security. However, this provision probably does little harm precisely for this reason: as explained above, creditors are highly unlikely to rely exclusively on floating charges for security. So if the analysis in this paper is correct, not too many administrators will be appointed under para. 14(3)(b). The Act also relies on the floating charge in identifying the main creditor for the purposes of the substitution or removal of the administrator in Sch. 16, paras. 92, 94, 97, and 103.

makes less sense. We know from the analysis above that, if the purpose is to enhance the value of the debtor's business to all those with claims against it, a creditor should only have the unilateral right to displace the debtor's management if it had both, the ability to gather and assimilate information about its competence, and the expertise to decide on its basis whether the removal of this management was warranted. There should also be some way of discouraging other creditors from engaging in opportunistic behaviour. Now the ability to gather information arises from the possession of *fixed* charges over assets strategically important to the debtor's business. The role of *floating* charges is very much a residual one, basically to ensure that the security package as a whole covers the debtor's entire estate and undertaking. This would enable the entire estate to be kept under one management, thus protecting any synergies. Recall also that as a rule, the purpose of a floating charge is *not* to secure priority for its holder, since its priority position is weak, generally unnecessary (because it most often secures the same debts as the fixed charges), and quite unreliable *ex ante*. It follows that since an alternative method has now been provided to divest the managers of control over essentially revolving assets, of preserving synergies, and of capturing the benefits previously associated only with an ensuing receivership, the floating charge no longer has any necessary role to play in our conception of the 'main creditor'.

The second role assigned to the floating charge by the Enterprise Act is of allocating priority as between those claiming to act as main creditors to a company. Priority of the floating charge for this purpose is by date of creation, but this may be altered by agreement among all those holding such charges.[108] Unless it agrees otherwise, the holder of any prior charge is given the right to a minimum of two business-days' notice if the holder of a junior charge intends to appoint an administrator,[109] and may if it so chooses ask the court for its own nominee to be substituted for the person appointed by the junior chargee.[110] Now it is entirely sensible for a mechanism to be provided which allows for the co-ordination of monitoring responsibilities, since, as noted, there should only be one creditor investing in the monitoring of most companies. A truly effective way of ensuring this would have been to grant unilateral management-displacement rights only to the prior-most chargee (identified chronologically as a default, and otherwise by agreement).[111] It could perhaps be argued that allocation of the right to determine the identity of the administrator (which is what the legislation is doing here) is an attempt to create a similar incentive structure. However, what matters is the chosen creditor's ability to gather information, and this is connected of course with the fixed charge, not the floating one. So the focus here in the legislation on the latter seems quite arbitrary, a hangover from the period when the floating charge was required to preserve the unity, upon management displacement, of the debtor's entire estate. The allocation of monitoring responsibilities and thus of the unilateral right to displace the incumbent management could just as easily be made by, say, attaching the declaration of the right to appoint an administrator[112] with the first fixed charge over some (or any of a specified list of) strategically important assets.[113] The floating charge simply is not required as a distinct entity, and the legislative focus on it is hard to justify.

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[108] Sch. 16, para. 15.
[109] Sch. 16, para. 15(1).
[110] Sch. 16, para. 96. Note that the prior chargee seems entitled to this substitution as of right, since para. 96 does not appear to be subject to any qualification. Contrast para. 95.
[111] Note the presumption in favour of the first-in-time chargee: it would have been operating monitoring arrangements for the longest period, and could be assumed to have relatively the most complete knowledge about managerial competence. The presumption would therefore be that it was best placed to decide whether any default was due to management-related factors.
[112] Sch. 16, para. 14(2).
[113] The list might include things like 'any of the debtor's bank accounts' or 'machinery involved in the debtor's day to day business'. These suggestions are very tentative, and a lot of thought would obviously have to go into formulating something like this list.

Moving now to the third prong of the argument, it is suggested that this focus on the floating charge in the new law is not only useless but also harmful. Here is why. It has repeatedly been argued that the priority of the floating charge is weak, unreliable, and often unnecessary. It was also noted, however, that in some (on the basis of the evidence considered, minute) proportion of insolvencies, its priority position *would* cause its holder to receive more from its insolvent debtor's estate than it otherwise would have. And this is what makes the continued existence of the floating charge objectionable.

Remember that in the distribution of an insolvent estate, the priority of one creditor over a non-consenting other is a privilege. It must be *earned* in a way which brings benefits to *all* the relevant parties as a group. Let us call this the 'privilege view' of security interests. Traditionally minded English lawyers have attempted to provide other justifications that circumvent the privilege view, most notably those based on the freedom of contract of the chargor and chargee, and on the property rights of the former. For reasons well explored in the existing literature, neither holds water. Freedom of contract arguments "have force only with respect to arrangements that do not create direct externalities. [When] the contract directly impinges on the rights of third parties, there is no prima facie presumption of freedom of contract".[114] The truth of this proposition and of its close variants is attested by diverse parts of the legal system, competition law being perhaps the most important example. The privilege view of (priority-based) security interests is an acknowledgement of the fact that they seem to constitute a violation of this principle. At least *prima facie*, the contract whereby A grants a security interest to B transfers loss that would otherwise have fallen on B upon A's insolvency, to C (junior creditor), a stranger to this contract. The argument that the grant of a security interest is no more than an exercise of A's property rights fares no better, given that the extent of these rights is a matter of what the law allows, and whether the law should allow security interests to be created is precisely what is in need of justification.[115] It might be useful to restate this summary, and the privilege view of security interests, using concepts peculiar to insolvency law. An attempt to improve one's position compared to what it would otherwise be under the insolvency distribution scheme, but which does not bring compensating benefits to those relative to whom this improvement would be brought about, is nothing more than a preference, objectionable on exactly the same grounds as any other.[116]

Now as a rule, a *fixed* charge fulfils the requirements of the privilege view. Its holder deserves its priority position in its debtor's insolvency because the charge (a) helps control financial agency costs, or (b) encourages the chargee to provide new funding to troubled companies which, in the absence of the priority of fixed security, would not have been provided, or (c) both. This is mutually beneficial for all the parties interested in the debtor's undertaking since it lowers the risk of its ending up in insolvent liquidation and thus raises the expected value of the claims of all of its creditors, secured and unsecured.[117]

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[114] See e.g. L. Bebchuk and J. Fried, 'The Uneasy Case for the Priority of Secured Lending', (1996) 105 Yale LJ 857, 933.

[115] See generally A. Clarke, 'Re-locating security interests within the property framework", in Harris (ed.), *Property Problems from Genes to Pension Funds* (London, Kluwer, 1997).

[116] Even if it does not fall within s. 239 of the Insolvency Act 1986, perhaps because of the much-criticised shortcomings of its drafting (notably, the focus on the debtor's 'desire' to prefer).

[117] This argument and supporting empirical evidence can be found in detail in Mokal, 'The Search for Someone to Save: A Defensive Case for the Priority of Secured Lending', (2002) 22 OJLS 687.

The floating charge brings no such benefits, however. Because it does not entrench the priority of its holder's claim with respect to the collateral, it can make no contribution to the control by its holder of financial agency costs. And because its priority is highly unreliable *ex ante*, i.e. at the time at which the charge is created, an offer of a floating charge to a potential lender by a troubled company does not noticeably increase the chances of its receiving new funding.[118] The *distinctive* value-enhancing contributions of the floating charge have already been discussed, and while these contributions persisted, it was perhaps justifiable for its holder to be given the benefit of its priority in the small proportion of insolvencies where there would be such a benefit.[119] However, it has been argued that the floating charge no longer performs any distinctive socially useful role. All the social benefits previously derived from coupling it with fixed security and receivership can now be captured simply through the combined operation of fixed security and the new administration procedure.

Nevertheless, commercially powerful lenders (most obviously, banks) would continue to include floating charges in their debentures because (a) it is statutorily required in order to obtain the ability unilaterally to appoint an administrator (though nothing special about its nature makes this necessary), and (b) they would have nothing to lose and some advantage to gain from the prospect, however distant, of the usefulness of its priority. However, this priority, no matter how unlikely it is to be efficacious, would be merely exploitative when it *did* turn out to be useful, accomplishing nothing except the improvement of the position of its holder compared to what it would otherwise have been. In those rare cases, it would be draining insolvency value away from ordinary unsecured creditors, without (any longer) bringing them compensating benefits. Simply put, the retention of the floating charge now creates a mechanism for preferences to be obtained in some insolvencies which are every bit as objectionable, as a matter of principle, as any caught and avoided by section 239 of the Insolvency Act.[120]

7. Some Concluding Thoughts

This paper has argued that the usual way of conflating floating with fixed charges as small variations on a single theme – as priority-based devices differing only in degree – fundamentally misunderstands its true nature. The floating charge has played a distinctive role as a residual management displacement device which could only be effective if coupled with an appropriate set of fixed security that enabled its holder to gather information about the competence of the debtor's managers and to control their incentives to misbehave. The floating charge allowed the debtor free use of its circulating assets while its management was doing well, and when the management failed, it would crystallise to divest them of control even over these assets. At this

[118] The new legislation's linking of the right unilaterally to appoint an administrator increases the inducement for a creditor to include a floating charge in its debenture when otherwise it might not have. It does not create a significant inducement for the making of a loan on the security of a floating charge when the loan would not otherwise have been made, since – in the absence of the benefit of some priority-based security – the right to appoint an administrator bring little *private* advantage to the appointor.

[119] Put differently, it is being claimed that all the relevant parties bargaining in the choice position of the Authentic Consent Model would arguably have found the relatively small expected costs of allowing floating charge holders priority in a small proportion of insolvencies to be outweighed by the expected mutual benefits of the floating charge described above; see Mokal, 'The Authentic Consent Model', [2001] LS 400.

[120] Note a qualification: some preferences might be objectionable because they destroy synergies by removing an important asset from the debtor's estate for the benefit of the preferred creditor. This point is not implicated in the text here. What matters is that because of the priority of the floating charge, the preferred creditor would receive value that ought to have gone to other creditors.

time, it would also contribute to controlling the motivation costs of other creditors by discouraging them from rushing to enforce their claims against circulating assets or threatening to do so, and by ensuring the unity of the debtor's estate under the receiver's control even after the onset of winding-up. This priority-independent view of the floating charge enabled us to explain the peculiarities of its actual operation, to understand why it was generally taken in combination with fixed charges, and either over the debtor's entire undertaking or over those assets not amenable to the draconian control of the fixed charge, and also to bring out the non-anomalous status of the 'lightweight' floating charge. The analysis also helped throw light on the role of registration, and on the problems occurring at the boundary between the two types of charge. Despite all this, however, it was argued that with the onset of changes introduced to the administration regime by the Enterprise Act, the floating charge has outlived its utility, and that its continued retention is now difficult to justify.

It would be useful at this point to highlight three important issues that have not been examined in this paper. First and even if the arguments developed here do explain the nature of the floating charge as it exists at the present time, do they apply to its early history as well?[121] Has the floating charge *never* been a priority-based device? While I am content with the claim that the above analysis explains the floating charge as it operates at the present, there is at least some reason to think that it would never have been relied upon primarily for its priority, both because it would never have encumbered the collateral, and because it was always subject to preferential and (when there was a distinction between the two) Crown claims[122] which would be difficult to quantify *ex ante*. Second, it is important to note that the points made above have significant implications for the validity of 'automatic crystallisation clauses', which purport to crystallise a floating charge upon the occurrence of a specified event even when neither of the parties is aware of this. Once again, this is an effort to acquire priority for the holder of the floating charge without requiring it to exercise control over the collateral. For the reasons explained above,[123] the efficacy of this must be in serious doubt, normatively *and* by implication of the Privy Council's decision in *Agnew*. And finally, space does not allow consideration of whether and how the analysis here fits in with the Law Commission's recent proposals about the reform of security interests.[124] These questions, and others, require further thought.

I want to conclude by quickly suggesting two ways in which we might deal with the problem that, as I claimed above, has now arisen from the retention by the Enterprise Act of the floating charge. First and more obviously, the floating charge might be abolished outright, perhaps as part of the reforms which, it is hoped, would be brought about as a result of the Law Commission's ongoing investigation into reform of security interests. Alternatively, the Enterprise Act has laid down that a certain proportion of the value of property subject to a floating charge is to be distributed to unsecured creditors.[125] The appropriate proportion has yet to be specified. Now if the floating charge were a priority-based device, then this restriction on its priority might well have been objectionable, since, for example, it would dilute the ability of a

[121] That there might be such a distinction was suggested by Jacob Ziegel at the Commercial Law and Commercial Practice seminar at the LSE in November 2002 in response to my argument that the floating charge might not be a priority-based device, and has been reiterated since by Michael Bridge and Ian Fletcher.
[122] An excellent historical overview can be found in A. Keay and P. Walton, 'The Preferential Debts Regime in Liquidation Law: In the Public Interest?', [1999] CfiLR 84, 86-91.
[123] See Sections 4 and 6.
[124] See *Registration of Security Interests: Company Charges and Property other than Land* (Consultation Paper 164, London, TSO, June 2002).
[125] See s. 176A of the Insolvency Act 1986, as inserted by s. 252 of the Enterprise Act.

troubled firm to attract new funding, thus harming all those with claims against it.[126] However, in view of the arguments made above, it is submitted that there is a strong case for setting at the highest level politically feasible the proportion of property which should go to unsecured creditors, right up to one hundred percent. The floating charge is not relied upon for priority, except opportunistically (i.e. *ex post*), so this would result in some benefit to unsecured creditors and would cause no harm to creditors who take security.

[126] See e.g. Mokal, 'Search for Someone to Save', esp. at 721-7.