THE CENTENARY OF THE VOLUNTARY LIQUIDATION ACT 1891

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[*Recent trends in Australia have prompted some comparisons with the economic history of the 1890s. In Victoria, one of the key legislative responses to that earlier crisis was the Voluntary Liquidation Act 1891 (Vic.), purportedly enacted to keep companies afloat as, in the aftermath of the land boom of the 1880s, a wave of insolvencies and liquidations began threatening Melbourne land companies and financial institutions. To mark the Act's centenary, the author comments here on its origins and effects.*]

Reflecting on the crash of 1929 in the United States, J. K. Galbraith wrote '[a]s protection against financial illusion or insanity, memory is far better than law.'[1] History, he went on to say, sustains memory to this end. Whether or not he was right to depreciate legal regulation as a protection against financial disaster, Galbraith's remarks are an apt reminder of some of the uses of history. They gain particular point from some conspicuous, if partial, parallels between past crises and current economic difficulties in Australia.

Take, for example, this description of the origins of an economic crisis in Australia: high levels of borrowing not used in productive investment, multiplication of financial institutions, a 'gambling spirit' fuelling speculative dealings, and falls in the prices of basic exports. The similarities to some features of the Australian economy in the 1980s are obvious, yet the description applied to the depression of the 1890s, and was published in 1904.[2]

It would be wrong to overlook the differences between conditions in the 1890s and those in Australia today. One need only consider the modern regulatory structure, the functions of the Reserve Bank, and the role of government in economic management to see some of the points at which direct analogies will break down. Nor has Australia in the 1990s yet experienced anything like the scale of economic dislocation suffered in the 1890s. Nevertheless, the similarities are strong enough to be worth the attention of anyone looking at current developments. With this in mind, this comment notes the centenary of one legislative response to mounting economic difficulties in Victoria, where the boom of the 1880s was most intense, and the subsequent depression most severe.

A sudden rush of land company and building society failures began in Melbourne in December 1891, as the effects of the collapse of the land boom of the 1880s spread through the financial structure. The management of some of the organizations threatened with liquidation joined with parliamentarians to devise a scheme for legislative assistance to fend off compulsory winding-up. Among those involved, either initially or at later stages, were James Munro, the Premier

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1 Galbraith, J. K., *The Great Crash* (1975) 10.

2 Turner, H. G., *A History of the Colony of Victoria* (1904) vol. 2, 292-8.

at the time, and William Shiels, the Attorney-General. The scheme led to the enactment of the Voluntary Liquidation Act 1891.[3]

The consolidated Companies Act 1890 (Vic.) provided three options for the winding up of what were then generally known as 'trading' companies, that is, companies incorporated under the general provisions of the Act as distinguished from the special provisions for mining companies. The three methods were shareholders' voluntary winding-up, compulsory winding-up, and shareholders' voluntary winding-up under court supervision.[4] These methods were available both for companies registered under the Act and for some other associations, including building societies.[5] A company could be wound up voluntarily by its shareholders pursuant to a special resolution; there was no compulsory assessment of the company's solvency on voluntary winding-up, and no equivalent of the modern creditors' voluntary winding-up. In order for a creditor to obtain control over the appointment and actions of liquidators, it was necessary to make formal application to the court. This application could be for compulsory winding-up by the court on one of the specified grounds, which included inability to pay debts, or for court supervision of voluntary winding-up already in progress. This latter alternative was very flexible, and allowed the court a wide range of discretionary powers without going so far as to place the winding-up entirely in the court's hands. The Companies Act made it clear that an application for winding-up under supervision could be made by a creditor, and it eventually became settled that liquidators too could apply. Gaining the assistance of the court's flexible powers sometimes made it advantageous for the liquidator to make the application or agree to it when made by a creditor, although in other cases the liquidators were less eager for the scrutiny which this would entail.[6]

The Voluntary Liquidation Act had two main sections. Section 4 governed applications for the winding-up of a company by the court on the ground that it was unable to pay its debts, or that it would be just and equitable for it to be wound up. The section applied where the company was not already being wound up voluntarily. In these circumstances, the Act required the court to dismiss the petition or appoint a meeting of the creditors of the company. At that meeting, the consent of a majority of the creditors present, by number and value of debts, was required for winding-up to proceed. Section 3, on the other hand, applied where a company was already being wound up voluntarily. There, no order was to be made 'for the winding-up of such company' unless the petition was approved by specified majorities of creditors; no distinction was drawn here between different grounds for winding-up.

In the case of a company with no creditors outside Victoria, one third of the creditors of the company by number and value of debts were required to approve the petition under s. 3. In the case of a company having creditors outside

[3] See *Economist*, 6 February 1892, 177; *Argus*, 22 March 1892, 4; *Australian Dictionary of Biography*, vol. 5, 314; Coghlan, T. A., *Labour and Industry in Australia* (1st ed. 1918, 1969) vol. 3, 1721.

[4] See *Australasian Insurance and Banking Record*, 18 December 1891, 891.

[5] In re *Premier Permanent Building Society, ex parte Turner* (1890) 16 V.L.R. 424.

[6] Companies Act 1890 (Vic.) s. 131ff, *Argus*, 10 November 1892, 4; In re *Maitland Coal Mining Co. Ltd* (1892) 14 A.L.T. 107.

Victoria, the requirement was less stringent; the number required to approve the petition was then one quarter of the creditors resident in Victoria, holding one quarter of the company's Victorian debts, or one quarter of the whole of the company's creditors by number and value of debts. This was intended as a token comfort to British investors. As J. M. Davies said, somewhat optimistically:

> The desire was not to do anything that would cause any kind of uneasiness to the English creditor. They did not want the English creditor to feel that there were undue obstacles in the way of his obtaining a compulsory liquidation . . .[7]

Table Talk, on the other hand, said of satisfying the new requirements imposed by the Act

> with the books and documents under the control of persons averse to publicity, the task is beset with difficulties, and becomes almost impossible.[8]

The Act also applied to the winding-up of building societies.[9]

Sections 3 and 4 of the Act clearly restricted applications for winding-up by the court unless the specified majorities were obtained, and, in practice, it seems to have been taken for granted that orders for winding-up under the supervision of the court would be barred in the same way. Towards the end of the life of the Act, the *Argus* raised the possibility that it did not apply to such orders, but the requirements of the Act were in fact satisfied in at least one of the two cases which were cited as possible examples of this approach.[10]

The Bill for the Act was rushed through Parliament with extraordinary speed, passing through all stages in both houses in one day. One M.P. later said that anyone opposing it would almost have been jumped on by some members of the Assembly.[11] Royal assent could not be obtained to the Bill for a week owing to the absence of the Governor, but it was provided that the Act would commence retrospectively from the date of its passage.[12]

It was reported that those principally involved in the negotiations leading to the Act represented companies in difficulty rather than the financial community as a whole.[13] The main justification given for the Act at the time was the need to frustrate the activities of 'wreckers' (we might call them 'asset-strippers' today) who would force liquidation on a company for the sake of acquiring its assets, even though the company might be solvent in the long term. A story circulated about a solicitor, supposedly a prime example of a 'wrecker', who deposited ten pounds in each of ten companies in order to become a creditor of each and drive them into liquidation. The *Argus* pointed out that if the companies could not pay ten pounds to discharge the debt and forestall an application for liquidation, they had virtually no chance of survival anyway.[14]

7 Victoria, *Parliamentary Debates*, Legislative Council, 3 December 1891, 2834.
8 *Table Talk*, 11 November 1892.
9 Voluntary Liquidation Act 1891 (Vic.) ss 5-6.
10 *Australasian Insurance and Banking Record*, 18 December 1891, 891; *Argus*, 10 November 1892, 4; *cf. In re Maitland Coal Mining Co. Ltd* (1892) 14 A.L.T. 107, cited by the *Argus*, in which consents were filed from creditors owed more than three quarters of the debts of the company.
11 Victoria, *Parliamentary Debates*, Legislative Assembly, 24 November 1892-3, 3013 (W. T. Carter). See also *Economist*, 6 February 1892, 177.
12 Voluntary Liquidation Act 1891 (Vic.) s. 1.
13 *Argus*, 7 December 1891, 4; 24 May 1892, 4.
14 *Argus*, 18 July 1892, 4.

As the *Australasian Insurance and Banking Record* noted, it remained possible for a creditor to obtain a judgment for a debt and attempt to levy execution against a company, notwithstanding the obstacles placed by the Voluntary Liquidation Act in the way of compulsory winding-up. However, this course was no longer possible if voluntary liquidation commenced; creditors were then left to their rights to participate in the proceeds of the winding-up.[15]

In re Phillip Island Company Limited[16] provides an example of the working of the Act. The Union Bank presented a petition for the compulsory winding-up of the company, and a meeting of creditors was accordingly held, attended by the representative of the bank (which was owed £9,343 by the company) and twelve other creditors (who were owed a total of £628 by the company). All creditors other than the bank voted against compulsory winding-up, which was therefore prevented by the Act. On an application to the Supreme Court by the bank to have a time fixed for the hearing of a petition for the winding-up of the company, Hodge J. reserved his judgment 'for the purpose of seeing whether it was possible for the Bank to obtain any relief under the circumstances'. After looking carefully into the law, he decided the Voluntary Liquidation Act squarely covered the case, and the Bank was powerless to wind the company up.[17]

The Act also had the effect of preserving the secrecy of dealings which might otherwise have been revealed, under the scrutiny of the court, in compulsory winding-up or winding-up under supervision. Since it placed no restrictions on voluntary winding-up, companies were free to use the Act to defeat or avoid shareholders' or creditors' motions for winding-up under court control, only to go immediately into voluntary liquidation without court supervision, and with directors or their associates acting as liquidators. Then, as the *Argus* observed in May 1892:

> The very man who should be most mistrusted in the whole business, who, if there is false play, is at the bottom of it, is in a position to bury every scandal, and to turn affairs to his own advantage. There are no actions, no disclosures, no restitution — and all is supposed to be well.[18]

Details of business dealings preceding the winding-up were sometimes permanently concealed in this way. The Act, the *Argus* noted in retrospect

> contained a plain and palpable 'hush-up' clause. . . . [I]t was to obtain this particular provision that the bill was promoted.[19]

Much opinion was against the Act from the start, and the *Argus* criticized it repeatedly until its repeal.[20] The *Argus* pointed out, among other things, the likely effect of the Act on sentiment in Britain towards Victorian investments, damage which Victoria could ill afford given its dependence on British funds:

> The financial condition of the colony forbids the enactment of any legislation which will tend to frighten away a single penny of British capital.[21]

[15] *Gray v. Australian Deposit and Mortgage Bank Ltd* (1892) 13 A.L.T. 230.
[16] (1892) 13 A.L.T. 269.
[17] *Ibid.* 270.
[18] *Argus*, 24 May 1892, 4; 18 July, 1892, 4.
[19] *Argus*, 25 November 1892, 4. See also *Table Talk*, 30 December 1892, 6.
[20] *Argus*, 9 December 1891, 4; 10 December 1891, 4; 12 May 1892, 4; 16 May 1892, 4; 24 May 1892, 4; 10 June 1892, 4; 18 July 1892, 4; 25 November 1892, 4.
[21] *Argus*, 7 December 1891, 4.

Later comments suggest that the Act had exactly this effect.[22]

The Act was repealed in 1892 and replaced with provisions based on the Joint Stock Companies Arrangement Act 1870 (U.K.), permitting the court to order a meeting of creditors which could make a binding compromise with the company, subject to court approval.[23] The Act's restrictions on winding-up were removed. The collapse of the boom proceeded apace through 1892 and led in 1893 to a full-scale financial crisis which saw the closure, temporary or permanent, of most Australian banks.

At the time of its repeal, some M.P.s, including Isaac Isaacs and George Turner (the future Premier), still supported the policy of the Act, in limited circumstances.[24] Nor has more recent opinion been unanimous that it should be condemned.[25] The Act did give a measure of protection to companies temporarily unable to pay their debts, guarding them against forced liquidation on a heavily falling market. On the other hand, the form of this protection greatly reduced creditors' say in the outcome and gave them no assurance of any eventual return, unlike a court-ordered meeting with power to make a binding compromise. Perhaps most importantly, by protecting companies from being forced into winding-up under court control and allowing voluntary liquidation to proceed unrestricted, the Act facilitated concealment of mismanagement and outright fraud. As the *Australasian Insurance and Banking Record* concluded, '[t]he Act has defeated its own object, by adding to the prevailing uneasiness.'[26] To those today watching the evolution of a more recent cycle of boom and bust, this may be a small reminder of the ways in which confidence can be undermined when the financial system is under stress, and of the need for disclosure, and the public assurance of disclosure, in corporate affairs.

22 Victoria, *Parliamentary Debates*, Legislative Council, 12 July 1892, 407 (Zeal); Legislative Assembly, 24 November 1892, 3012-13 (H. J. Wrixon); Legislative Assembly, 1 November 1893, 2790 (Williams); *Bankers' Insurance Managers' and Agents' Magazine* (London) vol. 53 (1892) 732.

23 Companies Act Amendment Act 1892 (Vic.).

24 Victoria, *Parliamentary Debates*, Legislative Assembly, 24 November 1892, 3010, 3016-17; but *cf.* Isaacs' more critical comment on the Act in his maiden speech: Legislative Assembly, 12 May 1892, 18.

25 *E.g.* Hall writes that '[c]riticism, if any, should be directed towards the lengthy period it was allowed to stand — about a year — rather than to the fact that such legislation was introduced.' Hall, A. R., *The Stock Exchange of Melbourne and the Victorian Economy 1852-1900* (1968) 153.

26 *Australasian Insurance and Banking Record*, 18 December 1891, 887.