

# THE BASIC BANKRUPTCY PROCESS IN ENGLAND

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## *The Initiation of the Bankruptcy Proceeding*

The bankruptcy process in England may be initiated by the debtor himself or by his creditors,<sup>1</sup> and as deceaseds' insolvent estates may be administered in bankruptcy, the personal representative of a deceased debtor may also petition for the administration of the estate in bankruptcy.<sup>2</sup> Limited companies or corporations are not subject to the bankruptcy process in England nor privileged to use it as a debtor.<sup>3</sup> A limited company, however, may be a petitioning creditor in involuntary proceedings against a bankrupt.<sup>4</sup> A debtor's petition (voluntary) need only allege that the debtor is unable to pay his debts and this forms the basis for starting the voluntary bankruptcy process in motion.<sup>5</sup> The prerequisite for a creditor's petition in bankruptcy (involuntary) are many, however. The debtor must have committed an act of bankruptcy within three months of the petition and the petitioning creditors must have aggregate claims to the amount of at least fifty pounds (\$140.) in excess of the value of any security held by them, and these must be for a liquidated sum.<sup>6</sup> There is no requirement that the debtor be insolvent or that any allegation of insolvency be made by the petitioning creditors. However, if the debtor satisfies the court that he is able to pay his debts, the court may dismiss the petition.<sup>7</sup> To facilitate the determination as to the amount of the unsecured balance of a claim held by a petitioning creditor holding security, such creditor is required to state in the petition either that he waives the security or gives an estimate of the value of the security. This estimated value will then be taken as a basis for determining the unsecured balance

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<sup>1</sup> Bankruptcy Act, 1914, Sec. 3.

<sup>2</sup> Bankruptcy Act, 1914, Sec. 130.

<sup>3</sup> Bankruptcy Act, 1914, Sec. 126.

<sup>4</sup> 2 Hal. Laws of England (3rd Ed.), Sec. 536, p. 287.

<sup>5</sup> Bankruptcy Act, 1914, Sec. 6.

<sup>6</sup> Bankruptcy Act, 1914, Sec. 4.

<sup>7</sup> Bankruptcy Act, 1914, Sec. 5(3).

of the claim for purposes of justifying his position as a petitioning creditor.<sup>8</sup> One creditor is sufficient to petition for involuntary bankruptcy if his unsecured claim equals or exceeds the fifty pound (\$140.) requirement.<sup>9</sup>

The legal personal representative or any creditor of a deceased debtor who would have been qualified to petition against the deceased had he lived, may petition for the administration of the deceased debtor's estate in bankruptcy. The probate court administering a deceased debtor's estate furthermore may, on its own motion, transfer the proceeding to the bankruptcy court if satisfied that the estate is insolvent.<sup>11</sup> The death of a debtor after a petition in bankruptcy has been filed does not discontinue the proceeding, but it may continue to its conclusion under the bankruptcy process.<sup>12</sup>

Where a petitioner does not proceed on his petition with due diligence, any other creditor having the requisite claim may be substituted as petitioner and the proceeding thus facilitated.<sup>13</sup> Once a petition has been presented either by the debtor or a creditor, it is recognized as in process and may not be withdrawn without the leave of the court.<sup>14</sup> The creditor's petition must be verified<sup>15</sup> and a deposit of seven pounds, ten shillings (\$21) made if the petition is presented by the creditor or five pounds (\$14) if by a debtor.<sup>16</sup> This is a strict requirement and no petition may be filed unless receipts for the deposit are submitted. In some provinces there is a growing tendency, however, for relief money to be made available to the totally destitute for this qualifying deposit, thus enabling him to get relief from the bankruptcy process. Moneylenders (Small Loan Co.) are particularly pointed out in the English bankruptcy process, and special detailed facts are required to be shown if the petitioning creditor is a Moneylender so that the claim may be assayed and divided into its components of principal and interest.<sup>17</sup>

The usual contacts base for bankruptcy jurisdiction over a debtor and his estate are presence, residence, or conducting business in Eng-

<sup>8</sup> Bankruptcy Act, 1914, Sec. 4(2).

<sup>9</sup> Bankruptcy Act, 1914, Sec. 4(a).

<sup>10</sup> Bankruptcy Act, 1914, Sec. 130(1) and 130(9).

<sup>11</sup> Bankruptcy Act, 1914, Sec. 130(3).

<sup>12</sup> Bankruptcy Act, 1914, Sec. 112.

<sup>13</sup> Bankruptcy Act, 1914, Sec. 111.

<sup>14</sup> Bankruptcy Act, 1914, Secs. 5(7) and 6(2).

<sup>15</sup> Bankruptcy Act, 1914, Sec. 5(1).

<sup>16</sup> Bankruptcy Rules, 1952, Rule 146.

<sup>17</sup> 2 Hal. Laws of England (3rd Ed.), Sec. 580, p. 305; Bankruptcy, Rules, 1952, Rule 165.

land.<sup>18</sup> This gives a very extensive base for the jurisdiction of the English bankruptcy process. The particular County Court to which a petition should be presented is that County Court for the district in which the debtor resided or carried on business for the longest period during the six months immediately preceding it.<sup>19</sup> The original jurisdiction of the High Court is much more extensive. This includes residence in or carrying on business within the London bankruptcy district for the greater portion of the six months immediately preceding the petition or for a longer period during the six months than in the district of any County Court, and also include jurisdiction over those not residing in England, and those whose residence the petitioning creditor is unable to ascertain.<sup>20</sup> However, incorrect venue is not a serious error, as proceedings taken in the improper court may be retained by it and such are not invalid.<sup>21</sup> This geographical suggestion for jurisdiction of the particular County Court or the High Court is further ameliorated by the ease with which proceedings may from time to time at any stage be transferred from one court to another.<sup>22</sup> Although the County Courts and the High Court have these geographical venue areas, the jurisdiction of each in bankruptcy extends throughout the whole of England.<sup>23</sup> With the groundwork laid by a proper petition, the court determines whether the matter will be dismissed or the second step in the bankruptcy proceeding taken. This second step is a far-reaching one with a major effect on the estate of the debtor. It is called the Receiving Order.<sup>24</sup>

The justification for a voluntary or involuntary petition in bankruptcy in England is a legal status denominated an Act of Bankruptcy, and every petition must be based upon at least one of these defined Acts.<sup>25</sup> However, the presentation of a debtor's petition for bankruptcy (voluntary petition) alleging inability to pay debts is in itself an act of bankruptcy, thus routinely and with no complications entitling him to the bankruptcy process.<sup>26</sup> The justification for a creditor's petition (involuntary bankruptcy), however, is hedged

<sup>18</sup> Bankruptcy Act, 1914, Secs. 1(2) and 4(1).

<sup>19</sup> Bankruptcy Act, 1914, Sec. 98(2).

<sup>20</sup> Bankruptcy Act, 1914, Sec. 98(1).

<sup>21</sup> Bankruptcy Act, 1914, Sec. 100(2).

<sup>22</sup> Bankruptcy Act, 1914, Sec. 100(2).

<sup>23</sup> Bankruptcy Act, 1914, Sec. 100(1).

<sup>24</sup> Bankruptcy Act, 1914, Sec. 5(2) and 6.

<sup>25</sup> Bankruptcy Act, 1914, Sec. 3.

<sup>26</sup> Bankruptcy Act, 1914, Sec. 6.

about with more detailed requirements and limitations on the Acts of Bankruptcy which will sustain the involuntary petition.<sup>27</sup>

The Acts of Bankruptcy in England are:

1. An assignment of property to a trustee for the benefit of creditors generally;
2. A fraudulent conveyance;
3. A fraudulent preference;
4. Concealing oneself with intent to defeat or delay creditors;
5. Execution and sale of goods or holding after execution for twenty-one days;
6. Notice by the debtor of intent to suspend payment of debts; and
7. The Bankruptcy Notice process.<sup>28</sup>

The Act of Bankruptcy upon which the petition is based must have occurred within three months of the petition.<sup>29</sup> Except as insolvency is involved in establishing an act of bankruptcy, such as an element in a fraudulent conveyance, it is not specifically emphasized as a requirement for bankruptcy. However, solvency may be used defensively in the hearing on the petition and the proceeding may be dismissed if the court finds that the debtor is solvent at that time.<sup>30</sup>

These acts of bankruptcy in general are similar to those in the United States, and are easily understood by those versed in the bankruptcy law of the States, with the exception of the Bankruptcy Notice grounds for bankruptcy which are entirely different. This enables a creditor who has obtained a judgment against a debtor to serve upon him a Bankruptcy Notice stating that the judgment debtor is required to pay the judgment within seven days or give security or compound for it to the satisfaction of the judgment creditor. The notice must recite the following, "...the Consequences of not complying with this notice are that you will have committed an act of bankruptcy, on which bankruptcy proceedings may be taken against you."<sup>31</sup> This may galvanize a slow debtor to action and will normally bring results unless the debtor is in true financial straits, in which case the bankruptcy process may well begin.

<sup>27</sup> Bankruptcy Act, 1914, Sec. 4.

<sup>28</sup> Bankruptcy Act, 1914, Sec. 1.

<sup>29</sup> Bankruptcy Act, 1914, Sec. 4(c).

<sup>30</sup> Bankruptcy Act, 1914, Sec. 5(3).

<sup>31</sup> Bankruptcy Act, 1914, Secs. 1(g) and 2.

### *The Receiving Order*

A Receiving Order is a technical second stage of the bankruptcy process. This comes upon a hearing on the petition for bankruptcy in which the court is satisfied that facts justifying bankruptcy have been shown.<sup>32</sup> The hearing is normally held in chambers and is conducted in an informal manner. The Receiving Order works a major change in the status of the debtor and his assets, for with it the estate is withdrawn from its normal free position into a sequestered status, and the Official Receiver of that court is automatically constituted a receiver of the property of the debtor, thus bringing it under the custody and control of the court. As the Receiving Order normally comes very shortly after the filing of the petition in bankruptcy, little time is lost in sequestering the estate for its supervision and protection. From the time of the Receiving Order unsecured creditors may not interfere with the property of the debtor except pursuant to the bankruptcy law and the debtor is denied any right to dispose of or in any way encumber his property.<sup>33</sup> These restrictions on the use or subjugation of assets of the debtor also run against property which may come to the debtor after the filing of the petition.<sup>34</sup> The Receiving Order, however, does not divest the debtor of title to property but restricts only his power and rights in the property which are subordinated to the rights given by law to the Official Receiver.<sup>35</sup> At the granting of the Receiving Order the first public announcement of the proceeding is required to be made by a notice giving the name, address and description of the debtor, the date of the order and of the petition. This must be published in the London Gazette and advertised in a local paper. Needless to say, a contention against bankruptcy will normally be fought with vigor in attempts to prevent the receiving order.<sup>36</sup>

The Receiving Order, then, marks the point in English bankruptcy at which the estate of the debtor is brought under the supervision of the court for the protection of creditors, pending further bankruptcy proceedings which may or may not go to the point of adjudication in bankruptcy. This is the point of complete immersion

<sup>32</sup> Bankruptcy Act, 1914, Sec. 5(2).

<sup>33</sup> Bankruptcy Act, 1914, Sec. 7.

<sup>34</sup> *Ibid.*

<sup>35</sup> Bankruptcy Act, 1914, see Sec. 18(1).

<sup>36</sup> Bankruptcy Act, 1914, Sec. 11.

into the full and final bankruptcy status. While the Receiving Order is in effect, the debtor is under a duty to give information as to his affairs, statements of his property, list of creditors and to cooperate with the Official Receiver and attend creditors' meetings, in preparation for further proceedings in the bankruptcy process.<sup>37</sup>

### *The Debtor's Opportunity for Composition*

After the bankruptcy process in England has progressed to the point where a Receiving Order has been made, the debtor is given an opportunity to clear himself and thus avert the consequences of adjudication in bankruptcy and the stigma that attends that status in England. Time is required to be given the debtor to permit him to exercise the opportunity to present a plan to the creditors setting forth in writing proposed terms of composition or some scheme of arrangement which he hopes the creditors will accept in substitution for the continuing bankruptcy proceeding. A plan thus proposed is submitted to the creditors in meeting and if approved by a majority in number and three fourths in value of all creditors who have proved, it becomes officially accepted by them. However, this is only the first step toward final effectuation of the plan, for it must also be approved by the court after the acceptance by the creditors.<sup>38</sup>

An application for approval by the court of the accepted composition or scheme must be made and a time set for hearing. At this hearing the Official Receiver is called to give a report on the plan and also to report on the conduct of the debtor. Creditors may also present objections to the plan at this stage, and the right to object by those who originally accepted the plan is preserved. The power in the court to refuse to approve a plan, if it is of the opinion that the terms are not reasonable or not calculated to benefit the creditors generally, is retained. If, however, facts are found which would require the court to refuse a discharge, then the court must refuse to approve the creditors' proposal for composition or arrangement and the regular bankruptcy process continues. If the facts are found justifying the approval of the plan, it will be so ordered and from that time its terms become binding on virtually all creditors.<sup>39</sup> The approval of the plan begins the reversing of the bankruptcy process. The Receiving Order is discharged, and the

<sup>37</sup> Bankruptcy Act, 1914, Sec. 14.

<sup>38</sup> Bankruptcy Act, 1914, Sec. 16.

<sup>39</sup> *Ibid.*

property of the debtor freed according to the terms of the plan.<sup>40</sup> It terminates the proceeding without an adjudication in bankruptcy and without a trustee taking title to the debtor's property. If, however, the terms of the plan are later in default, the creditors affected may make application to the court to enforce the provisions of the plan, or may take more drastic action and make application to annul the plan and to have the debtor reinstated in the bankruptcy process and adjudicated a bankrupt.<sup>41</sup>

If the plan for composition or scheme for arrangement is not accepted, an immediate adjudication of bankruptcy may be made.<sup>42</sup> Normally, however, a later hearing will be called and an adjudication decreed shortly after the refusal of the plan.

This time to work something out with the creditors after bankruptcy process has begun, but before its full impact is felt, seems an important pause built into the general bankruptcy process itself. However, the scope of its permissive use is to a great extent restricted by the requirement that the plan be refused if the debtor is not entitled to an absolute discharge in bankruptcy.<sup>43</sup>

#### *The Public Examination*

After the Receiving Order has been made, and the debtor has filed his statement of affairs and attended private examinations by the Official Receiver, a Public Examination of the debtor is required to be held.<sup>44</sup> This is a hearing open to the public and held before the Registrar. The debtor is required to "stand in the box" and be questioned on oath as to his financial history, his conduct, dealings and property. The Official Receiver in practice conducts the examination (much as a lawyer on cross examination), but creditors also are usually given wide latitude in questioning the debtor. A trustee, if one has been appointed, may also participate in the Public Examination. The Registrar may question the debtor and often rounds out relevant information by his own inquiries. The debtor may be represented by a solicitor in the County Courts, but the case for the debtor is presented by a barrister in the High Court. In most of the small asset cases, the debtor does not have the assistance of

<sup>40</sup> Bankruptcy Rules, 1952, Rule 208 and 209.

<sup>41</sup> Bankruptcy Act, 1914, Sec. 16(16); Bankruptcy Rules, 1952, Rule 213.

<sup>42</sup> Bankruptcy Rules, 1952, Rule 219.

<sup>43</sup> Bankruptcy Act, 1914, Sec. 16(9) and (10).

<sup>44</sup> Bankruptcy Act, 1914, Sec. 15; Bankruptcy Rules, 1952, Rule 188.

legal counsel, but is alone in his Public Examination. The testimony and inquiries presented in the Public Examination are recorded by a professional reporter, transcribed and later signed by the debtor. This may be used as evidence in later bankruptcy matters and is especially important as the bankruptcy process may continue for many years. This record is open to inspection by creditors and furnishes a broad and comprehensive base for further investigation into the finances of the debtor, and for use in the hearing on discharge if a discharge is later requested. An evaluation of the Public Examination will be made later.

### *Adjudication in Bankruptcy in England*

After the bankruptcy process has progressed through the hearing on the petition for bankruptcy, the issuance of the Receiving Order, the opportunity for the debtor to present a plan of arrangement, and the Public Examination, the time has come for a further major step in the bankruptcy process — the adjudication of bankruptcy.<sup>45</sup> The usual practice is an application for an order of adjudication which then will be set for hearing. This application may be made by the debtor, the creditors, the Official Receiver or the Court on its own motion may set a date for the hearing. The hearing on adjudication normally comes before the Registrar and is heard in chambers. As the Public Examination normally is held before the hearing on adjudication, the detailed report prepared as a result of it, is available on the adjudication hearing. The Order of Adjudication must be published in the London Gazette (gazetted), which is widely circulated throughout the United Kingdom.<sup>46</sup> This, then, is another stage of the bankruptcy process which must be publicly announced by gazetting, those first proceedings being the announcement of the Receiving Order and the time for the Public Examination.

With the adjudication, the bankruptcy process in England deserts its uncertain character and plunges into full administration. At this point the property of the debtor vests in the trustee when appointed and qualified and *as of the time of the commission of the act of bankruptcy upon which the petition in bankruptcy was based.*<sup>47</sup> Until this point, the Official Receiver had only the posses-

<sup>45</sup> Bankruptcy Act, 1914, Sec. 18; Bankruptcy Rules, 1952. Rules 217-220.

<sup>46</sup> Bankruptcy Act, 1914, Sec. 18(2) Bankruptcy Rules, 1952. Rule 221.

<sup>47</sup> Bankruptcy Act, 1914, Secs. 18(1), 37 and 53.

sory right of a receiver to protect the assets of the debtor, but with the adjudication order the property vests in the trustee and great powers are given him in respect to the property. Although the Official Receiver is prohibited from serving as the permanent trustee in bankruptcy except in small estates,<sup>48</sup> he does take a position similar to that of the trustee until a trustee is duly appointed and also in certain other interim situations.<sup>49</sup> Until the trustee is appointed, then, the property of the debtor, after the adjudication, will be under the control of the Official Receiver, thus preventing a lacuna in the interim.

#### *The Trustee and Committee of Inspection*

The appointment of a trustee is made after the adjudication. In asset cases the appointment is made by resolution decided by a majority in value of the creditors present and voting at a creditors' meeting, or the creditors may leave his appointment to a Committee of Inspection. If, however, the creditors do not appoint a trustee, the Board of Trade may make the appointment.<sup>50</sup> In certain "no-asset cases" a trustee is not required, the Official Receiver taking over the functions of the trustee.<sup>51</sup> A bankruptcy trustee in England is entrusted with very broad powers. The title to all property of the debtor vests in him, all monies due the debtor may be received by him. He may sell any or all the debtor's property, carry on the business of the debtor, bring and defend actions, sell property on credit terms, compromise and allow claims, make allowances for the support of the bankrupt and his family, declare and distribute dividends to creditors and many other ministerial functions.<sup>52</sup> On all of these extensive powers of the trustee, the Board of Trade keeps a watchful eye.<sup>53</sup> A Committee of Inspection may also be used to guide him and he must also have regard for directions given him by creditors at a general meeting.<sup>54</sup> In general, however, a trustee may manage the estate and distribute it among the creditors in his own discretion.<sup>55</sup> The remuneration of the trustee is fixed by the creditors and is in the nature of a commission

<sup>48</sup> Bankruptcy Act, 1914, Secs. 19(5) and 129(i).

<sup>49</sup> Bankruptcy Act, 1914, Secs. 53(1) and 74(1) a and g.

<sup>50</sup> Bankruptcy Act, 1914, Secs. 19 and 167 "Ordinary Resolution."

<sup>51</sup> Bankruptcy Act, 1914, Sec. 129

<sup>52</sup> Bankruptcy Act, 1914, Secs. 48, 53, 54, 55, 62, 67 and 76.

<sup>53</sup> Bankruptcy Act, 1914, Secs. 19(2) and 81.

<sup>54</sup> Bankruptcy Act, 1914, Sec. 79.

<sup>55</sup> Bankruptcy Act, 1914, Sec. 79(4).

or percentage. This is reviewable by the Board of Trade and may be lowered by it.<sup>66</sup> Normally the remuneration is fixed as part of the agreement under which the trustee agrees to accept the position.

A Committee of Inspection may be a part of the bankruptcy machinery in England. It may be compared to the use of creditors' committees in the United States, but with clearer defined functions in the bankruptcy process itself.

A Committee of Inspection is not mandatory and normally will not be used unless the debtor's estate is sufficient to generate a special interest in the estate and the functions of the trustee. If no Committee of Inspection is used, its authorized or required functions may be exercised by the Board of Trade. This committee is appointed by the creditors by majority in value vote for the purpose of superintending the administration of the estate by the trustee. It must have at least three members, but not more than five, and each must be a creditor or representative of a creditor. The Committee has strict attendance requirements and is closely responsible to the general creditors. Members of the Committee may be removed at any time by a resolution at a meeting of creditors.<sup>67</sup> Some of the specific duties assigned the Committee of Inspection are: decide whether the trustee will be permitted to carry on the business of the bankrupt so far as necessary for the winding up of the estate; authorize the trustee to institute or defend actions, employ a solicitor, mortgage property, arbitrate and compromise claims, and authorize the trustee to allow the bankrupt himself to operate his trade.<sup>68</sup> The trustee must also get permission from the Committee of Inspection to make the family allowance out of the property of the debtor for the support of the bankrupt and his family.

With the appointment of the trustee and Committee of Inspection, the machinery of bankruptcy is ready for the realization of assets and distribution to creditors. If a trustee is used, he takes the major responsibility for administration with the Board of Trade and Committee of Inspection, if used, keeping strict watch over his activities. In practice, however, the burden of administering the small asset cases falls on the Official Receiver, as no creditors or

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<sup>66</sup> Bankruptcy Act, 1914, Sec. 82.

<sup>67</sup> Bankruptcy Act, 1914, Sec. 20.

<sup>68</sup> Bankruptcy Act, 1914, Secs. 56 and 57.

trustees will act when substantial funds are not available for payments.

### *Gathering the Bankrupt's Estate*

The title to the property of the debtor vests in the trustee and is deemed to relate back to the time of the commission of the act of bankruptcy on which the Receiving Order was made.<sup>60</sup> This period, however, is relatively short as an act of bankruptcy to be available as a basis for a petition in bankruptcy must have occurred within three months of the petition.<sup>61</sup> The seriousness of this relation back period is tempered as to transactions with third parties by validating provisions which recognize transactions with the debtor and his property made after the time of the commission of the act of bankruptcy, if made in good faith, for valuable considerations, and without notice of any available act of bankruptcy.<sup>62</sup>

Not only is property belonging to the debtor at the time of the commencement of the bankruptcy brought into the proceeding, but also all property which is acquired by or devolves upon the bankrupt debtor up until the time of his discharge.<sup>63</sup> Here is one of the basic differences between the English bankruptcy and that in the United States where only the property held by the debtor at the time of the petition is taken into the bankruptcy process.<sup>64</sup> This after acquired property feature of the English law has far-reaching effect as discharges are usually given, if at all, some years after the beginning of the bankruptcy process. In many cases no discharge is requested and theoretically all property of the bankrupt which in any manner comes to him by his own efforts or by gift, bequest, or devise is taken by the trustee in bankruptcy, and his estate upon death comes into the bankruptcy jurisdiction. This after acquired property feature also complicates the administration of the bankruptcy as there is a duty upon the trustee or Official Receiver

<sup>59</sup> Bankruptcy Act, 1914, Sec. 58.

<sup>60</sup> Bankruptcy Act, 1914, Secs. 37 and 38(a).

<sup>61</sup> Bankruptcy Act, 1914, Sec. 4(c).

<sup>62</sup> Bankruptcy Act, 1914, Sec. 45. See also Bankruptcy (Amendment) Act, 1926, Sec. 4.

<sup>63</sup> Bankruptcy Act, 1914, Sec. 38(a).

<sup>64</sup> There are a few exceptions in the United States as in situations: where property vests in the bankrupt within six months after bankruptcy by bequest, devise or inheritance; where certain non-assignable interests in real property become assignable within six months and; where estates by entireties become transferable within that time. See Bankruptcy Act (U.S.), Sec. 70(a) 7 and 1st and 2nd unlettered paragraphs.

to continue an observance of the bankrupt, his wages, his inheritances and any "good financial turn" which may befall him. With the fluidity of movement of bankrupts, this watchfulness is extremely difficult and it is estimated that there are many thousands of undischarged bankrupts in England who cannot be identified or located by the court having jurisdiction in a particular case. The severity of this after acquired property feature is in practice ameliorated by provisions in the law which permit wages and salaries paid bankrupts in their post bankruptcy endeavors to be retained by him and such are not sequestered by the trustee or Official Receiver unless clearly in excess of the legitimate amount required for the debtor and his family.<sup>65</sup> As to third persons, transactions with the bankrupt involving after acquired property are stabilized by providing that the bankrupt has the power to make valid transactions in respect to the after acquired property, real and personal, with bona fide purchasers for value if completed before any intervention by the trustee.<sup>66</sup>

A very small portion of the bankrupt's estate is not included in the assets taken by the trustee and thus not subject to creditors' claims in bankruptcy. These would be called exemptions in the United States, but not admitted to be such in England. These exclusions from the bankruptcy process are tools of trade, necessary wearing apparel and bedding for himself and wife and children. This exclusion is limited to a statutory value not exceeding twenty pounds "in the whole." (\$56)<sup>67</sup> In practice, however, this limitation may be overlooked or liberally treated by those responsible for the conversion of assets for the creditors. The trustee may also make allowances out of the estate for the support of the bankrupt and his family. This may be done only with the permission of the Committee of Inspection<sup>68</sup> and this being a creditors' committee would indicate a constrictive tendency in that allowance.

### *Processing Creditors' Claims*

Claims of creditors against the bankrupt may be proved summarily by delivering to the trustee or sending to them through

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<sup>65</sup> Bankruptcy Act, 1914, Sec. 51(2). 2 Hal. Laws of England (3rd Ed.), Sec. 855, p. 433.

<sup>66</sup> Bankruptcy Act, 1914, Sec. 47.

<sup>67</sup> Bankruptcy Act, 1914, Sec. 38(2).

<sup>68</sup> Bankruptcy Act, 1914, Sec. 58.

the mail, an affidavit verifying the debt. If a trustee has not been appointed, the affidavit may be delivered or sent to the Official Receiver who will later turn the affidavit over to the trustee if and when appointed.<sup>69</sup> Claims which are uncertain in value may be estimated as to value by the trustee. This estimated value set by the trustee may be appealed to the Court which may without a jury either fix the value of the claim or may declare it non-provable because the claim is incapable of being fairly estimated.<sup>70</sup> When a claim is presented to the trustee, he must either admit or reject it in writing and, if rejected, the writing must state the grounds for the rejection. This prepares the record for the appeal of the trustee's decision by the creditor to the court where the trustee's conclusions may be reversed or varied as the court justified.<sup>71</sup>

Certain claims or debts are not provable in bankruptcy such as unliquidated claims,<sup>72</sup> and those based upon liabilities arising after the time when an act of bankruptcy was available against the debtor and with full knowledge by the claimant of this situation.<sup>73</sup> Money Lenders (Small Loan Companies) are subjected to special proof of claim requirements. Their claims must be accompanied by a verified statement showing:

1. all sums lent with the dates,
2. all sums paid with the dates,
3. the proportion of the claim which is principal and the proportion which is interest, and
4. a statement of the amount of interest which would be due if calculated at five per cent (5%).<sup>74</sup>

Lessors of real estate or personal property, if the lease is disclaimed, may claim and be allowed for the full extent of the injury caused by the disclaimer.<sup>75</sup> Although many forms of gambling are legalized in England, gaming debts are frowned upon and may not be proved in bankruptcy.<sup>76</sup> This may be to the advantage of other creditors, but is a great disadvantage to the gambling debtor who may be

<sup>69</sup> Bankruptcy Act, 1914, Second Schedule, Rule 2.

<sup>70</sup> Bankruptcy Act, 1914, Sec. 30, subsections (3) — (7).

<sup>71</sup> Bankruptcy Act, 1914, Second Schedule, Rules 23-28.

<sup>72</sup> Bankruptcy Act, 1914, Sec. 30(4) and (6).

<sup>73</sup> Bankruptcy Act, 1914, Sec. 30(2).

<sup>74</sup> Bankruptcy Rules, 1952, Rule 251; 2 Hal. Laws of England (3rd Ed.), Sec. 580, p. 305.

<sup>75</sup> Bankruptcy Act, 1914, Sec. 54(8). Compare the year's rent restriction in the United States. Bankruptcy Act (U.S.), Sec. 63 (9).

<sup>76</sup> 2 Hal. Laws of England (3rd Ed.), Sec. 922, p. 468.

denied a right to discharge because of it,<sup>77</sup> or if a discharge is granted the gambling debt being not provable as it seems would survive the bankruptcy.<sup>78</sup>

Where a debt would have become due in the future, the claim will be decreased at the rate of five per cent per annum, computed from the date of the declaration of the dividend to the time it would otherwise have been payable.<sup>79</sup> Secured claims are processed expeditiously and firmly. The affidavit of the secured creditor must state whether or not he is a secured creditor,<sup>80</sup> and must state the value at which he assesses the security held. This evaluation is kept "honest" as the trustee then has the option to redeem the security on payment to the creditor of the value he has ascribed to it, or the trustee may require the security to be sold, thus ascertaining the value of the security.<sup>81</sup> If these steps are not taken, the secured debtor will be allowed to share in the distribution to the amount of the excess of his claim over the assessed value fixed by him. If a secured creditor files his claim without disclosing his security, he will be deemed to have waived his security, but may prove for the entire claim, the security asset reverting to the bankrupt's estate free from the creditor's security lien.<sup>82</sup>

Certain claims such as rates and taxes have priority in the distribution of the estate<sup>83</sup> and others are subordinated or postponed to other creditors. For example, in England, where a married man becomes bankrupt, any money or property of his wife lent or entrusted to him for the purpose of his trade or business is treated as assets of his estate in the bankruptcy and the wife will not be entitled to claim any dividend as a creditor in respect to it until all claims of the other creditors have been paid. A like subordination or postponement is applied to similar advances by a husband to his wife who later becomes bankrupt.<sup>84</sup>

#### *Distribution of the Estate*

One of the duties of the trustee in bankruptcy in England is to declare and pay dividends to creditors. Speed in distribution is

<sup>77</sup> Bankruptcy Act, 1914, Sec. 26(3) f.

<sup>78</sup> Bankruptcy Act, 1914, Sec. 28(2).

<sup>79</sup> Bankruptcy Act, 1914, Second Schedule, Rule 22.

<sup>80</sup> Bankruptcy Acts, 1914 and 1926, Second Schedule, Rule 5.

<sup>81</sup> Bankruptcy Act, 1914, Second Schedule, Rule 12.

<sup>82</sup> Bankruptcy Act, 1914, and 1926, Second Schedule, Rules 5, 10-16.

<sup>83</sup> Bankruptcy Act, 1914, Sec. 33.

<sup>84</sup> Bankruptcy Act, 1914, Sec. 36.

emphasized with a requirement that the first dividend be distributed within four months of the first meeting of creditors. Notice of an intent to declare a dividend must be published in the London Gazette, and a notice of the declaration must be given creditors.<sup>85</sup> The highest priority against the sums held by the trustee are the costs of administration. Next come certain rates and taxes, wages and monies due under various Acts, all of which rank equally among themselves. An apprentice may be given preferential treatment as to the refunding of sums paid by him to the bankrupt under his indenture of apprenticeship.<sup>86</sup> A very important factor in distribution is the recognition by the law that certain transactions or claimed transactions are inherently subject to abuse in bankruptcy and being thus recognized these troublesome problems are categorically settled by it. Thus certain intra family claims are arbitrarily determined without being subjected to the troublesome problem of intent and bad faith. An example of this is the provision that money lent or property entrusted by one spouse to another who becomes bankrupt and if such was for the purpose of trade or business, it is treated as property of the bankrupt and the lending spouse may not claim any dividend as a creditor of the other until all other creditors have been paid in full.<sup>87</sup> Certain obligations resulting from contracts in consideration of marriage are also subordinated to claims of other creditors.<sup>88</sup> Interest, or any pecuniary consideration in lieu of interest, on loans in excess of five per cent are also subordinated to the claims of other creditors in bankruptcy.<sup>89</sup>

A late claimant who proves his claim after dividends have been paid will be entitled to his omitted share from later dividend payments before other creditors may participate in them. Previous dividend payments, however, may not be disturbed and the late claimant's only recourse is to later dividend payments.<sup>90</sup> If sufficient assets are or become available, claims of creditors will bear interest at the rate of four percent per annum.<sup>91</sup> This may be very important in the English bankruptcy system where discharges are few, or only after a considerable time has elapsed, and where after

<sup>85</sup> Bankruptcy Act, 1914, Sec. 62.

<sup>86</sup> Bankruptcy Act, 1914 and 1926, Sec. 33.

<sup>87</sup> Bankruptcy Act, 1914, Sec. 36.

<sup>88</sup> Bankruptcy Act, 1914, Sec. 42.

<sup>89</sup> Bankruptcy Act, 1914, Sec. 66.

<sup>90</sup> Bankruptcy Act, 1914, Sec. 65.

<sup>91</sup> Bankruptcy Act, 1914, Sec. 33(8).

acquired property of the bankrupt goes into the bankrupt estate. This is particularly disastrous to a bankrupt or beneficial to creditors, depending upon one's approach, when a bankrupt inherits property in his later years. Property taken under these circumstances, thirty years after the bankruptcy, was observed in 1964. In such a case, the interest may well far exceed the original claim.

### *Discharge*

No hearing or discharge will be held until the bankrupt applies to the court for an order of discharge.<sup>92</sup> In many cases no application is made and, as a result, the debtor continues fully liable to his creditors. This, coupled with the fact that all after acquired property of the debtor legally passes to the trustee and is administered in bankruptcy indicates the lasting effect of the bankruptcy status. Reasons for this neglect on the part of the bankrupt debtor to apply for discharge will be more evident as the discharge requirements are realized and the severity of the discharge process is understood. These reasons for not applying for discharge will be further speculated upon later.

The application for discharge may not be made until the debtor has been adjudicated in bankruptcy and the hearing on the application may not be held until after the Public Examination of the bankrupt is concluded.<sup>93</sup> In this way, a hearing on discharge may be prevented if the court is not satisfied with the Public Examination, by an adjournment of that examination rather than concluding it. The Official Receiver, trustee if any, and creditors must be given notice of the hearing on discharge and may take part in the hearing. It is not usual for a hearing on discharge to come on within one year of the petition in bankruptcy and in the relatively few cases where a discharge is requested, a period of four or five years has been common. There is some indication, however, that debtors lately are taking advantage of the opportunity to be discharged, especially in the London District. The hearing on discharge is conducted by the court and is a public hearing.<sup>94</sup> The bankrupt debtor is carefully questioned on oath and led through a report on his financial history by the Official Receiver much as an attorney cross

<sup>92</sup> Bankruptcy Act, 1914, Sec. 26(1).

<sup>93</sup> *Ibid.*

<sup>94</sup> *Ibid.*

examines in the United States. This part of the hearing is largely a repetition of the facts elicited at the Public Examination, which is part of the record in the case. However, the history of the conduct of the debtor in the bankruptcy process and financial changes since the Public Examination are carefully developed. The cooperativeness or lack of it on the part of the debtor with the Official Receiver and trustee during the bankruptcy process is noted. The Official Receiver is required to make a report at the hearing<sup>85</sup> and this is accepted as prima facie evidence of the facts stated in the report.<sup>86</sup> The statements of the debtor and others are taken by a court reporter and later transcribed and signed by the bankrupt. Uncontested application for discharges may be heard and determined by the Registrar. Contested discharges, however, must be heard by the County Judge except that Registrars in the High Court in London may hear and determine both the contested and uncontested discharges.<sup>87</sup>

There are several alternatives open to the court in determining an application for discharge:<sup>88</sup>

1. An absolute Order of Discharge. This may be either an absolute refusal or an absolute discharge.
2. A suspended discharge. This is the granting of a discharge to become effective after a designated time as fixed by the court.
3. A percentage dividend discharge. This suspends the discharge until a dividend of not less than ten shillings in the pound has been paid to creditors. (There are 20 shillings to the pound.)
4. Conditional discharge. A discharge subject to conditions as to any earnings, income or after acquired property. Under this feature a discharge may be granted except as to designated future earnings and property which would then come into the estate after the discharge is granted. This type of

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<sup>85</sup> Bankruptcy Act, 1914, Sec. 26(2). See also Secs. 72 and 73.

<sup>86</sup> Bankruptcy Act, 1914, Sec. 26(6).

<sup>87</sup> Bankruptcy Act, 1914, Sec. 102(2) c and (3) and Sec. 103. Although the Registrar in County Courts may grant orders of discharge where the application is not opposed, it is the custom to reserve this function to the County Court (Judge). A specific Registrar of a County Court, however, may be given equal powers with those in the High Court. Sec. 102(5).

<sup>88</sup> Bankruptcy Act, 1914 and 1926, Sec. 26(2).

discharge prevents certain future property from being freed by the order of discharge.

5. A special conditional discharge. This is a technical discharge which requires the bankrupt as a condition of his discharge to consent to judgment for any balance not satisfied at the date of the discharge, which judgment shall be effective against future earnings and after acquired property, subject to supervision by the court. This consent judgment is given the Official Receiver or trustee and is enforceable by him; or
6. A combination order of discharge. The court may combine the suspended, the percentage and the conditional discharge as it deems appropriate in the particular circumstances.

Quite often the discharge order provides that it will become effective after six months, or after a certain percentage on the debts has been paid, or after the happening of a certain contingency. This means that all property coming to the bankrupt before that time comes into the bankrupt estate. The event contingency may be used where a bankrupt may imminently inherit property.

Two years after the initial order of discharge, the terms may be changed as the court may think fit upon a showing by the bankrupt that there is no reasonable probability of his being in a position to comply with the terms of the original order.

Under certain circumstances the court is bound either to refuse a discharge, or if a discharge be granted, to use the suspended or conditional discharge. The most important of these circumstances under which no absolute discharge may be given are:<sup>99</sup>

1. Where the bankrupt's assets are not a value to equal ten shillings (\$1.40) in the pound (\$2.80), *i.e.*, 50%. This, however, will not apply if the debtor satisfies the court that this asset to liability ratio has arisen from circumstances for which he cannot justly be held responsible;
2. Where the bankrupt has failed to keep proper books of account;
3. Continued to trade after knowing himself to be insolvent;
4. Contracted debts without reasonable grounds of expectation to pay;
5. Failure to account for assets;

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<sup>99</sup> Bankruptcy Act, 1914, Sec. 26(3):

6. Rash and hazardous speculation;
7. Extravagance in living;
8. Gambling;
9. Neglect of business;
10. Frivolous actions or defences to creditors' actions;
11. Made preferences;
12. Juggled liabilities to make assets equal to ten shillings (\$1.40) in the pound (\$2.80);
13. Has been previously bankrupt; or
14. Is guilty of any fraud.

Any one of the above situations bars a bankrupt from an absolute discharge and requires either an absolute refusal of discharge or some modified form as represented by the suspended and conditional discharges. It is self evident that very few bankrupts would be entitled to an absolute all inclusive discharge, not subject to any suspension or condition. In practice, the Official Receiver presents facts in the Public Examination which show at least one ground for refusal of an absolute discharge. This is then treated as an objection to discharge. As only uncontested discharges may be heard by the Registrar, and this objection to discharge makes it contested, the County Judge is called upon to hear the discharge matter and this is true in most bankruptcy proceedings in England. Only in the High Court are the Registrars empowered to hear and decide a contested discharge.<sup>100</sup>

A discharge releases the debtor from all debts provable in bankruptcy except those specifically excluded by the order of discharge and certain other claims. These non-dischargable claims include certain debts owed the Crown, debts incurred by fraud, liabilities for seduction and other matrimonial causes. The court, however, may permit the discharge to include these debts to such an extent and under such conditions as it may deem justified.<sup>101</sup> A discharge, however, does not automatically remove statutory disqualifications which accompany an adjudication in bankruptcy. In England, an adjudication in bankruptcy disqualifies one from holding certain offices and governmental positions. These disqualifications may be removed if the bankrupt obtains in addition to his discharge, a certificate to the effect that his bankruptcy was caused by misfortune

<sup>100</sup> Footnote 97 *supra*. See also Bankruptcy Rules 1952, Rule 227.

<sup>101</sup> Bankruptcy Act, 1914, Sec. 28.

without any misconduct on his part. This is called the Certificate of Misfortune and, if granted, reinstates the debtor to his civil rights lost by his adjudication in bankruptcy.<sup>102</sup>

The point of time at which the discharge takes effect is doubly important to the English debtor. First, he is relieved of his debts, and second, it is the point of time at which his income and after-acquired property are no longer taken into the bankruptcy estate. It is the discharge, then, which frees property and income from being subject to the debtor's estate in bankruptcy, as all property coming to the debtor before the discharge is taken by or subject to the bankruptcy process.<sup>103</sup> This absolute cut off, however, may be modified by the order of discharge itself, as is the case in contingent and suspended discharges discussed *supra*. Of course, the universal principle of exempting certain claims or debts from discharge is present here, as for example the non-dischargability of claims of the Crown, claims based on fraud, claims based on certain sexual offenses and claims resulting from certain family responsibilities.<sup>104</sup>

The court has an extremely wide discretionary power in regard to any discharge order given and in regard to the modification of an earlier discharge order. Although the court may be required by the Bankruptcy Act to give only a contingent or suspended order of discharge on certain facts, the qualification or contingency is within the discretion of the court and may range from a simple innocuous limitation on the discharge to a severe, long lasting restriction. This may be illustrated by the difference in effect of a discharge suspended for one month and one suspended for two years. The attitude of the various judges toward debtors generally and the particular debtor involved will be reflected in the severity or compassion evidenced by this discharge order. A generalization may be made that the provincial courts (County Judges) are more severe on debtors in this regard than the Registrars in the High Court in London.

Although the court is given a very broad permissive power to alter, rescind or vary any order made by it under a general power,<sup>105</sup> this all inclusive authority to amend may be restricted in its appli-

<sup>102</sup> Bankruptcy Act, 1914, Sec. 26(4). See also 2 Hal. Laws of England (3rd Ed.), Sec. 1070, p. 538.

<sup>103</sup> Bankruptcy Act, 1914, Sec. 38(a).

<sup>104</sup> Bankruptcy Act, 1914, Sec. 28(1).

<sup>105</sup> Bankruptcy Act, 1914, Sec. 108.

cation to orders of discharge by the specific qualifying provision giving the court the power to modify a conditional or qualified discharge at any time after the expiration of two years and when satisfied that there is no reasonable probability of the bankrupt's being able to comply with the terms of the original discharge order.<sup>106</sup> The extent of the use of this modifying power again reflects the attitude of the court toward those who ask release from debts but more compassion may be evidenced in the modification than in the original discharge order because of the feeling that the debtor has doubly learned his lesson.

The order of discharge when made becomes available to the bankrupt debtor as a defense to any action on a debt released by the discharge.<sup>107</sup> Discharged debts, however, may be revived by a later promise but a new consideration is required. This revival may be effected without the new promise being in writing.<sup>108</sup>

### *Exemptions*

The bankruptcy law of England has no specific reference to debtor's exemptions as known in the United States. The provision that all property of the debtor vests in the trustee as of the date of the act of bankruptcy upon which the petition is based seems all inclusive. However, the tools of the debtor's trade, and the necessary wearing apparel and bedding for himself and his wife and children are not included in the property of the bankrupt which passes to the trustee and are excluded from the bankruptcy process. The scope of this exemption is severally restricted by a limit on the value which may not exceed twenty pounds (\$56).<sup>109</sup> This is the only specific exemption in the English bankruptcy system, but there are other indirect or oblique exemptions which in practical effect are quite substantial.<sup>110</sup> The court and trustee have a broad permissive power to permit a bankrupt to receive and retain his wages or salary or to be allowed sufficient out of his property for the support of himself and family.<sup>111</sup> This is not as definite and absolute as exemption allowing the tools of trade, etc., not to exceed twenty pounds (\$56) but in practice they are applied fairly generously to

<sup>106</sup> Bankruptcy Act, 1914, Sec. 26(2) unlettered paragraph.

<sup>107</sup> Bankruptcy Act, 1914, Sec. 28(3).

<sup>108</sup> 2 Hal. Laws of England (3rd Ed.), Sec. 1071, p. 538.

<sup>109</sup> Bankruptcy Act, 1914, Sec. 38(2).

<sup>110</sup> Bankruptcy Act, 1914, Secs. 51(1) and (2) and 52.

<sup>111</sup> Bankruptcy Act, 1914, Sec. 58.

the bankrupt. Keeping in mind that under the English system title to all property and income vests in the trustee until discharge, a wage earner would be completely cut off from any right to receive his wages during the bankruptcy process and until discharged, which normally would be years later, unless some ameliorating practical procedure was used. This has been done by permitting the wages and earnings of a bankrupt to be paid to him for his and his family's use until an order of the court directs that the whole or part of his wages be paid to the trustee.<sup>112</sup> In most cases where the debtor has only a moderate income, the debtor is permitted to continue to receive his wages and to use them for the support of himself and family. If the wages seem adequate, the court may order that a certain portion be paid by the debtor to the trustee each week or month as the case may be. Although there may be no interference with the debtor's current income, he may be questioned as to his use of it upon the hearing on his application for discharge and if the judge is convinced he could have contributed to his creditors, but did not, this irresponsibility may have an effect on the order for discharge. This freedom permitted the bankrupt debtor to continue to receive his wages to be used for the support of his family, is the real exemption process in England, although the Englishman says "there are no exemptions" there. It is flexible and completely within the discretion of the court. An affirmative action is necessary to bring any of the wages into the bankruptcy process and the question presented is how much the bankrupt can reasonably pay the trustee from his current wages in view of his necessary family expenses. The liberality of this exemption varies greatly in the multitudinous bankruptcy courts throughout England and reflects the attitude of the particular court as to what considered necessities are a more lenient treatment seems to be evidenced by the High Court in the London Bankruptcy District, than in the County Courts.

#### *Summary of the Basic Bankruptcy Process*

The bankruptcy process in England may be instituted either by creditors (involuntary) or by the debtor himself (voluntary). Certain Acts of Bankruptcy are required as a basis for the creditor's petition. Upon the approval of the petition a Receiving Order is made, which withdraws the debtor's estate from its free position into

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<sup>112</sup> 2 Hal. Laws of England (3rd Ed.), Sec. 855, p. 433.

the jurisdiction of the court. At this point in the process, the debtor is given the opportunity to suggest a Composition which, if accepted, ends the bankruptcy process. After the Receiving Order and if no Composition is effected, a Public Examination of the debtor is required. This is an intensive examination into the financial history of the debtor, conducted by the Official Receiver before the Registrar in open court. The next step is the Adjudication Bankruptcy and at this point the full process gets into high gear. The property of the debtor, including after acquired property, vests in the trustee and he, under the guidance of the Committee of Inspection and the Board of Trade, administers the estate. The trustee has considerable power in gathering the assets, processing creditors' claims and distributing the estate — much more so than a Trustee in a United States bankruptcy.

Discharges in England are carefully circumscribed and may be absolute, conditional or suspended in nature. There are very few Exemptions, but as a practical matter the debtor is allowed a reasonable amount of his future wages for the support of himself and family. There are special processes for the administration of small estates which are quite informal, less expensive in administration, and expeditious. The judicial attitude toward bankruptcy in England has operated many decades with little change and so has become somewhat vested. Whether there is a need for a modernization of this attitude will be considered later.

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