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(eds.)

Dealing with Economic Failure

Between Norm and Practice (15th to 21st Century)

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EDITION

Introduction

Writing in 1697 on bankrupts Daniel Defoe, the author of Robinson Crusoe, thought the English law on bankruptcy "has something in it of Barbarity". He continues:

> It gives a loose to the Malice and Revenge of the Creditor, as well as a Power to right himself, while it leaves the Debtor no way to show himself honest: It contrives all the ways possible to drive the Debtor to despair, and encourages no new Industry, for it makes him perfectly uncapable of any thing but *starving*.[1]

With these few words Defoe describes the hardships unfortunate traders faced in early modern England. Defoe suffered from the fate of a bankruptcy himself. After various unsuccessful ventures, among others in the wine trade with Portugal, and underwriting in insurance, he was declared bankrupt for more than £17,000 in 1692. Harassed by recalcitrant creditors he was committed to prison for several months, after a composition had failed, because four of his 140 creditors had refused to consent to an agreement. As the contemporary bankruptcy law contained no provisions for discharge Defoe remained liable with his future earnings. The harshness and cruelty of the law towards the debtor, he argues, "cast [him] out of Human Society, and expos'd [him] to Extremities worse than Death" Moreover, he thought that the bankruptcy laws were not only inhumane to the debtor but also of no advantage to the creditor.[2]

The bankruptcy laws of the early modern period treated the insolvent debtor as a criminal who had to be sanctioned severely. The perception of bankruptcy as a sort of theft or robbery of the creditor's property was not only a central element in the European bankruptcy laws but also in nineteenth-century America.[3] In Britain the insolvent debtor even had to face capital punishment until 1820.[4]

The shift from creditor-friendly towards more debtor-friendly legislation was a slow and uneven process lasting far into the twentieth century. The idea that

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1 Daniel Defoe: *An Essay upon Projects.* London 1697, p. 192.

2 Ibid. pp. 192–194, see also his articles on the fate of bankrupts in his Review: "*A Review of the State of the British Nation*" April 17, 1707, p. 115 "Miscellanea"; April 19. 1707, p. 119.

3 For the U.S.A. see among others Scott A. Sandage: *Born Losers. A History of Failure in America*. Cambridge Mass., 2005; Bruce H. Mann: *Republic of Debtors. Bankruptcy in the Age of American Independence.* Cambridge Mass. 2002.

4 1 Geo IV c. 115; see Emily Kadens: The Last Bankrupt Hanged: Balancing Incentives in the Development of Bankruptcy Law. *Duke Law Journal* 59 (2010), pp. 1229–1319.

prevails today, that bankruptcy law should be debtor-friendly, is a far cry from the creditor-friendly laws that dominated for centuries. Historically, according to Mike W. Peng, "entrepreneur-friendliness and bankruptcy laws are like an 'oxymoron', because bankruptcy laws used to be harsh and cruel".[5] Entrepreneur-friendly bankruptcy regimes are now advocated to make it easier to start afresh after a bankruptcy. Recent business literature highlights the role of entrepreneurs as agents of growth. As institutions decisively influence the level of entrepreneurial activity, business scholars pledge for entrepreneur-friendly institutional contexts that provide stimuli for innovation and risk-taking.[6] Although the New Institutional Economics have long emphasized that institutions matter, the relationship between entrepreneurship and bankruptcy regimes has hardly been looked into. Only within the last few years, induced by the growing concern of governments around the world to facilitate the re-entry of bankrupts, have scholars begun to inquire into indices for entrepreneur-friendly bankruptcy laws.[7] A strong interest in the question how bankruptcy laws impact on business activity resulted from various factors, the big financial crash in 2008, intensified global competition among business and states, the overall high number of failures even before 2008, and also from awareness that the percentage of firms that fail within the first five years is much higher than those that survive.[8]

The following papers are the outcome of an international conference that focused on the norms and practice of dealing with economic failure within and outside the courts from a long-term, international and interdisciplinary perspective. The papers cover the period from the early sixteenth century until today. Without

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5 Mike W. Peng et al.: Bankruptcy Laws and Entrepreneur-Friendliness. *Entrepreneurship. Theory and Practice* 34 (2010), pp. 517–730, here: p. 518.

6 Ibid; see also F. Wei and M.I. White: Personal bankruptcies and the level of entrepreneurial activity. *Journal of Law & Economics* 46 (2003), pp. 543–69; Paolo Di Martino: Legal institutions, social norms, and entrepreneurship in Britain (c. 1890–c. 1939). *The Economic History Review* 65 (2012), pp. 120–143, here: p. 122f.

7 For that discussion see Peng, Bankruptcy Laws, pp. 517–730; Seung-Hyun Lee et al.: How do bankruptcy laws affect entrepreneurship development around the world. *Journal of Business Venturing* 26 (2011), pp. 505–520 or John Armour and Douglas Cumming: Bankruptcy Law and Entrepreneurship. *American Law and Economics Review* 10 (2008), pp. 330–350; see also contributions in: Stijn Claessens et al. (eds): *Resolutions of Financial Distress. An International Perspective on the Design of Bankruptcy Laws*. Washington 2001 to name only a few.

8 Peng, Bankruptcy Laws, p. 518 FN. 2: Germany experienced a considerable rise of insolvencies already before the 2008 crisis. They rose from a total of 15.302 in 1992 to 154.04 in 2006: failure among businesses rose from 10.900 to 30.357 (www.destatis.de).

claiming to give a comprehensive overview, the papers presented here – by addressing some central issues – should give an impression of the protracted process of modernization and adaptation. They focus on Europe's leading commercial centres, for it was here that the impact of economic change was first experienced. Here we find information on the earliest examples of alternative conflict regulations and efforts by the town councils to search for more viable ways of dealing with bankruptcies. The volume concludes with a paper on today's bankruptcy law in Germany to show where we are now.

The contributors to this volume are from various disciplines, social and economic as well as legal history and contemporary law. In Germany – perhaps more so than in Anglo-American countries – social and economic historians on the one side and legal historians on the other have for a long time approached the history of bankruptcies from diverging angles. Social and economic historians have used legal records like bankruptcy files predominantly for analyzing social and economic developments, or more recently turned their attention to cultural factors such as reputation, trust and the impact of social relations such as family, kin, or co-religionists on firms and companies.[9] Vice versa, legal historians have focussed on the law, paying only secondary attention to economic and social aspects.[10] Only within the last few years are some tendencies towards a broader approach visible in both disciplines. One of the aims of the conference was to intensify the dialogue between the disciplines.

A word needs to be said about the terms used: failure is a broader term that includes, but is not limited to, bankruptcy. A business may fail for lack of assets without undergoing a formal procedure before the courts. The term bankruptcy goes back to the Italian "banca rotta" meaning the break-up of a trader's business, when he was not able to pay his debts. "Bankrupt" or "banqueroute" or "Bankrotteur" frequently used to have a negative connotation applying to a fraudulent failure,[11] the term failure or the outdated continental version of "falliment", "fallissement"

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9 Given the vast literature on the cultural and social impact on economic relations the reader is only referred to the Douglass, C. North: *Institutionen, institutioneller Wandel und Wirtschaftsleistung*. Tübingen 1992; Oliver E. Williamson: *The economic institutions of capitalism: firms, markets, and relational contracting*. New York 1985; on trust, Niklas Luhmann: *Vertrauen*. Stuttgart 2000; Francis Fukuyama: *Trust. The Social Virtues and the Creation of Prosperity.* New York 1995.

10 Anke Meier: *Die Geschichte des deutschen Konkursrechts, insbesondere die Entstehung der Reichsordnung von 1877*. Frankfurt a. M. 2003.

11 Oxford English Dictionary online; Peter Hertner: Article: Bankrott. *Handwörterbuch zur deutschen Rechtsgeschichte*, vol. 1, 2. ed. 2008, column p. 428f.

for bankruptcy or "fallit" for the debtor did not carry the negative implication of bankruptcy. In the past "insolvency" was applied to small traders and non-trading groups in Britain, who had to undergo a different court procedure than a bankrupt.[12] Some of the papers in the volume are written by lawyers or legal historians. The character of the German legal language tradition may have connotations that are not to be found in the same English term. To open the German quotations in the articles to a non-German reading public, terms were adapted to the language used in the contemporary U.S. Bankruptcy Code.

Since the discovery of the Americas the world has changed fundamentally. The expansion of trade to distant non-European shores produced the financial revolution of the late seventeenth century followed by the industrial revolution.[13] The rise of the European commercial empires was not, however, a history of continuous growth but was also accompanied by birth pangs and setbacks. Trade with the non-European world offered surprising economic opportunities and profit prospects, but traders had also to cope with new and unpredictable risks. Although we do not have comprehensive and reliable figures on failures, those we do have suggest that the number began to rise with long-distance trade and first became an accompaniment to commercial life in the early modern commercial centres such as Antwerp, Augsburg or Nürnberg. For Augsburg, for example, Mark Häberlein counted 62 bankruptcies between 1529 and 1580 and a further 57 between 1580 and 1620. Even large firms such as Höchstetter in 1529 failed along with middling and small merchants.[14] A similar rise in bankruptcies can also be noticed in England during the sixteenth century.[15] Compared to the eighteenth

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12 Debtors were divided in three classes, merchants and traders owing at least £100, only this group came under the bankruptcy law, small tradesmen or mechanics owing less than £100 were dealt with at the Court of Common Pleas and later at insolvency courts. The third class consisted of persons with small debts of £20 and less. (Ian P.H. Duffy: *Bankruptcy and Insolvency in London during the Industrial Revolution.* New York / London 1985, see the first three chapters).

13 On the commercial revolutions see the still valuable publication of Peter G.M. Dickson: *The Financial Revolution in England. A Study in the Development of Public Credit 1688–1756.* London, New York 1967.

14 Mark Häberlein: Merchants's bankrupts, economic development and social relations in German cities during the long 16th century. In: Thomas Max Safley (ed.): *The History of Bankruptcy. Economic, Social and Cultural Implications in Early Modern Europe.* London, New York 2013, pp. 19–33, here: p. 21f.

15 W.J. Jones: The Foundations of English Bankruptcy: Statutes and Commissions in the Early Modern Period. *Transactions of the American Philosophical Society* 69 (1979), pp. 1–63, here: p. 5.

century the numbers were low. Two centuries later the numbers were several times higher in the leading commercial centres and jumped with the advent of industrialisation. In England they rose from an average of between 172 and 278 per year in the first half of the century to an average of 762 yearly in its last decade. A similar trend, although much lower in absolute numbers, can be perceived in Amsterdam and even in Stockholm.[16]

Given the economic change on the one side and the harshness of bankruptcy laws on the other, the question arises to what extent the laws were enforced and to what extent alternative solutions were sought. Researchers should not only study the provisions of the bankruptcy laws, but look at the practice of handling failures by the parties concerned.[17]

The penalizing treatment of the unfortunate trader had a more than thousand year old tradition dating back to the Roman times. As well as imprisonment, the bankrupt had to endure bondage and corporal punishment. The Romans already distinguished between the honest and the fraudulent debtor. While the fraudulent debtor faced bondage, incarceration and death, the honest debtor, whose misfortune was caused by external accidents, was granted a cessio bonorum and did not suffer the disgrace of losing his citizen's rights, if he surrendered his property voluntarily.[18] This distinction and the institution of cessio bonorum was lost with the decline of the Roman Empire and only slowly re-discovered in the early modern period. In some countries it took even longer before it was written down.[19]

Given the increase of risk and failure from the sixteenth century onwards, the question arises how debtors and creditors as well as the lawmakers and courts responded to the changing economic environment. Imprisonment for debt robbed the bankrupts of the opportunity to pay back their debts. For the creditor, imprisonment, death or flight of the debtor to some unknown place could mean that

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16 For London see Margrit Schulte Beerbühl: *The Forgotten Majority. German Merchants in London, Naturalization, and Global Trade 1660–1815.* New York / Oxford 2015, pp. 198f.; Julian Hoppit: *Risk and Failure in English Business 1700–1800.* Cambridge 1985, Appendix 1; for Amsterdam W.F.H. Oldeweit: Twee eeuwen Amsterdamse fallissementen en het verloop van de conjuncture (1636 tot 1838). *Tijdschrift voor Geschiedenis* 75 (1962) p. 421–435, here: pp. 432f.; for Stockholm see Klas Nyberg and Håkan Jakobsson's contribution in this volume.

17 Karl Gratzer, Introduction, in: Karl Gratzer, and Dieter Stiefel (eds): *History of Insolvency and Bankruptcy from an International Perspective.* Södertörn 2008, p. 18.

18 Gratzer, Introduction, p. 20f.

19 First examples of the re-introduction of the cessio bonorum are found at the end of the fifteenth and early sixteenth century (Gratzer, Introduction, p. 23).

he would have to write off losses and in the worst case be drawn into the failure, possibly facing bankruptcy himself. Given the laws, the questions will be: What opportunities did debtors, creditors and the court have for alternative instruments of conflict regulation and conflict reduction? What changes can be perceived in the level of imprisonment?

Law sources provide us with interpretations of what was considered right or wrong at a given time. These provisions vary in time and space as they are embedded in cultural values and responsive to social change. As Lawrence Friedman and, more recently, Jérôme Sgard have pointed out economic and social developments do not only have an impact on legal and judicial structures, but vice versa as well; the two spheres shape each other.[20] Reciprocal influences do not imply that changes correlate immediately. Legal norms may react much more slowly to changes, because lasting cultural perceptions, such as the criminal perception of economic failure for example, retarded change in the law. Furthermore, the early bankruptcy laws were often attempts to solve immediate problems and thus were vague and had defects.[21] By looking at judicial and non-judicial practices in dealing with bankrupts the impact of social relations on the outcome of a procedure should be taken into account.

The inability to repay debts opens up a Pandora's box of conflicts not only between debtor and creditor, but also between the creditors. It was conflict-prone on many issues, economic, social, cultural and legal, which had to be solved quickly and individually. Given the penalizing character of the pre-modern laws, bankruptcy was something to be avoided at nearly any price. Thus conflict reduction and prevention for the benefit of good governance have been the guiding principles throughout the centuries.

Powerful trading enterprises with trade links extending to the New World already existed in the first half of the sixteenth century. Well-known examples are the Fuggers and Höchstetters of Augsburg or the Imhoffs of Nuremberg. These firms had invested not only in long-distance trade but in mines and other early modern industrial enterprises. They were, moreover, money-lenders to the crowns and nobility of Europe. Although they were family firms, capital did not exclusively come from family members or dowries but also from non-related shareholders.

20 Lawrence M. Friedman: Legal Culture and Social Development. *Law & Society Review* 4 (1969), pp. 29–44; Jérôme Sgard: Do legal origins matter? The case of bankruptcy laws in Europe 1808–1914. *European Review of Economic History* 10 (2006), pp. 389–419, here: p. 389.

21 Jones, Foundations of English Bankruptcy, p. 7.

To prevent internal litigation and conflict among the active and silent partners that could end in bankruptcy, the Höchstetters, Imhoffs and other large family enterprises had concluded company agreements detailing the rights and duties of the governing members and providing instruments to deal with existing or threatened conflicts. Three measures proved particularly effective to prevent litigation, as Mechthild Isenmann explains in detail in her contribution; firstly they institutionalized regular and obligatory shareholder meetings that provided a platform for regulating internal conflicts. In case of unforeseen and imminent disputes the contract provided for extraordinary shareholder meetings. Secondly, if these could not be settled at the meetings the articles prescribed mediation either internally by a family member and kin, or if the matter could not be settled internally, they were to call in external mediators. Litigation was the last resort and only started when all other forms of conflict regulations had failed. Isenmann comes to the conclusion that mediation practices were generally preferred for several reasons. One was that information on internal business habits should not be laid open to the public, and a mutual agreement or mediation could be more advantageous to the parties concerned.

Another preventive measure to evade the threat of social death that accompanied bankruptcy in the early modern period is described by Wolfgang Forster. The commercial developments after the discovery of the New World began to shake the social and economic foundations of the traditional social elite in Spain by the new wealth of the mercantile middle classes. Traditionally, social status was based on landownership that needed to be displayed by a conspicuous and elaborate dress code and consumption rituals. The obligation to demonstrate noble status through a luxurious lifestyle and extravagant dowries for daughters was a financial strain. Unlike the mercantile classes they faced falling revenues from a declining population. Various instruments existed to prevent or delay bankruptcy of a noble family: creditors could grant a respite, a partial remission of debt was another option or the crown could intervene and hustle creditors and debtor into an agreement. When all of these possibilities failed only a "cession bonorum", i.e. relinquishing all assets to the creditors, remained in order to avoid imprisonment and disgrace. Surrendering all assets, however, implied losing noble status which was inalienably bound to the memoria of entailed estates in Spain. Faced with this problem the Spanish lawyer Salgado de Somoza developed a legal solution by separating administration from possession which allowed the over-indebted nobility to retain its social status.

Some factors allow the sixteenth century to be seen as a first turning point in the history of bankruptcy: around the turn to the sixteenth century a more systematic bankruptcy system began to emerge in Europe resulting from the expansion

of trade and credit relations, the frequent wars and rising number of bankruptcies. Suitable solutions for handling bankruptcy had to be found. In medieval cities creditors could take debtors to prison without the intervention of a court, and the old instruments for dealing with insolvent debtors led to tensions and discontent. The inadequacy of the old bankruptcy regulations was first felt in the commercial centre of Antwerp, whose mercantile community had grown considerably and become more international.

In response to rising litigation the Antwerp City council, as Dave De ruysscher elaborates, issued an ordinance in 1516 that for the first time introduced collective bankruptcy proceedings. Up to that time creditors who first made a claim to the assets of a bankrupt were prioritized over those who claimed compensation before the courts at a later stage. The new law imposed restraint on the individual creditor who sought full repayment at the expense of others. Besides the introduction of collective bankruptcy proceedings a second important measure was introduced in the 1520s and 1530s. During these decades de Ruyscher notices a certain shift from creditor-oriented to more debtor-oriented legislation that to some extent alleviated the debtor's fate, although its aim was primarily to encourage him to come forward and forfeit all his property. This development resulted from the economic and financial crises between the Frisian war of 1517 and the Italian wars of 1521 and went along with further changes, such as a distinction between unfortunate and fraudulent debtors, and the introduction of voluntary bankruptcy.

Furthermore, the council of Brabant and the urban government took an active role in hustling the parties into compromise, allowing the debtor to apply to the council of Brabant to commission the Antwerp aldermen to mediate a compromise, encouraging the creditors to consent to postponement of payments, and allowing a debtor to continue business at least during the negotiations. Although, as De ruysscher points out, the number of arrangements increased considerably in the 1530s. The new regulations were clearly adapted to the needs of a commercial hub, but the city authorities lacked effective instruments to force all creditors into a lasting compromise.

The eighteenth century marks a step up in the history of bankruptcy. It saw the evolution of a commercial bankruptcy regime adapted to the needs of a commercial society. The bankruptcy system of Antwerp was a local regulation, but during the eighteenth century commercial opportunities and risk extended beyond the few city centres. After the fall of Antwerp in 1585 trade shifted to the north, to Amsterdam, later on to London. Besides the two leading financial hubs many larger and smaller trading and commercial centres had emerged by the eighteenth century. Non-European regions had become interconnected forming an early modern global trade by European trade companies, adventurers and individual

merchants, who had established far-reaching trade networks.[22] New financial institutions had been created during the course of the seventeenth century such as the Wisselbank in Amsterdam as early as 1609, the Hamburg Bank in 1619 or the Bank of England in 1694 along with insurance companies and other financial instruments to meet the rapidly growing credit demand of private businessmen and governments.

Although bankruptcy laws had been amended to some extent during the early seventeenth century they had become inadequate to meet the requirements of the commercialized economies at the end of the century. That did not only hold true for Britain. The laws had been suited, as Daniel Defoe remarked, for "the Circumstances and Time of the Evil they were made against", but were "now a Public Grievance to the Nation"[23] and their "severity served neither the creditor nor the debtor".[24] Suffering himself from the dreadful fate of a bankrupt, Defoe began to advocate a reform of the bankruptcy law that would allow a 'full and free discharge' of debts. His struggle for a reform resulted in the new bankruptcy law of 1706 (4 & 5 Anne c. 17). It can be seen as a turning point in the history of bankruptcy legislation as it introduced for the first time the possibility of a discharge from debt and a debt-free fresh start for the honest traders.[25] The law of 1706 alleviated the fate of at least some honest traders, but it neither abolished the traditional penalizing provisions (on the contrary, it even exacerbated punishment for fraudulent debtors by introducing the death penalty), nor did it introduce voluntary bankruptcy.[26]

Given the long period of wars between 1689 and 1714 (the Nine Years' War and the War of Succession) and a marked increase in failures, the perception that reforms were necessary induced many lawmakers across Europe to consider them. Besides Britain, Denmark passed a new bankruptcy law in 1706, Bremen followed a few years later in 1711. Further towns and countries followed during the next

22 Meanwhile a vast literature on the early modern globalisation has been published, among others see a short valuable summary of the literature in: Bernd Hausberg: *Die Verknüpfung der Welt. Geschichte der frühen Globalisierung vom 16. bis zum 18. Jahrhunderts.* Wien 2015.

23 Defoe, *Of Bankrupts*, pp. 196f.

24 Ibid., p. 192.

25 The law became a model for the American legislation after the independence. See Charles Jordan Tabb: The Historical Evolution of the Bankruptcy Discharge. *American Bankruptcy Journal* 65 (1991), pp. 325–371.

26 A discharge depended on the consent of four-fifths of the major creditors. It was certified by granting a certificate of conformity.

few decades. The new laws, however, only reflect a minor part of the reform efforts and changes in dealing with bankrupts. In the case of the free City of Hamburg, for example, discussions on a reform of the bankruptcy law already started before the end of the seventeenth century. Several attempts at new legislation followed, and discussions continued throughout the next fifty years, before the new law was finally passed in 1753. Even the new law did not stop further discussions.[27] Similarly in Britain discussions continued throughout the century, only a few amendments were passed, but all in all legislation became more lenient during the course of the century.[28]

The introduction of the distinction between unfortunate and fraudulent bankrupts was a first step by the lawmakers of the sixteenth century to take into consideration that failure did not automatically result from fraud. The novel dimension of speculation and financial crises causing huge bankruptcy waves changed perceptions as to the causes of failure. Especially from mid-eighteenth century onwards crises and bankruptcies grew in number and geographical reach. The financial crisis of 1763, which for example started in Amsterdam, sent out shock waves that were felt in places as far apart as Stockholm or Venice.[29]

In many countries, laws already granted security from imprisonment at least for a limited period during the bankruptcy procedure to encourage debtors to come forward and also to allow the unfortunate some subsistence. The growing risk of domino effects, that the failure of debtors could draw creditors themselves into bankruptcy, increased the willingness to come to an arrangement. By a composition, the creditor could at least get some of his money back, and it allowed a quicker return than a formal court procedure which could last decades. Furthermore, allowing a debtor to start again could raise the prospects of getting fully paid at some future time or being compensated by future business.[30] Willingness to come to a compromise, however, depended on the circumstances of the failure and the social embeddedness of the debtor. Creditors were more inclined to an

27 Staatsarchiv Hamburg: Senat 111-1-CI VIII; The political and commercial elite of Hamburg were more or less the same. In dealing with economic failures they had often responded flexibly to the changing commercial situation and felt little need to change the law.

28 E.g. amendments of 1718 or 1732, Jay Cohen: History of imprisonment for debt. *Journal of legal history* 3 (1982), pp. 153–171, here: 156f.; Duffy, pp. 10–14.

29 See below the contributions of Klas Nyberg / Håkan Jacobsson and Magnus Ressel.

30 In the eighteenth century out-of-court arrangements could induce creditors to a moratorium or creditors would consent to a dividend in the hope of future business with the debtor that would compensate to some extent for his losses.

arrangement if the debtor was a reputable and trustworthy man embedded in an influential family and kinship network and whose misfortune was caused by external circumstances.

We have no means to evaluate the volume of private compositions, as only comparatively few cases left traces. What can be perceived is that the bankruptcy laws increasingly reacted to the spread of composition and entered clauses that provided for composition, since private and voluntary compositions suffered from a lack of any obligation. Taking the example of the bankruptcy law of Hamburg passed in 1753, it encouraged the courts to push the conflicting parties into composition. Similar to the Venetian law on bankruptcy the Hamburg Senate envisaged three categories of bankrupts. Besides the fraudulent and the unfortunate bankrupt it introduced a third type, the careless debtor, reflecting that speculation as well as careless bookkeeping could result in bankruptcy. For both cases, the unfortunate as well as the careless merchant, the courts were to advocate composition.

The perception that speculation, risk and failure were integral parts of any trade was no longer confined to the leading commercial centres, but had also spread to peripheral countries such as Sweden. Rising numbers of bankruptcies caused by crises abroad initiated, as Klas Nyberg and Håkan Jacobsson shows in their paper, a fundamental reform of the Swedish bankruptcy law. First vague provisions to regulate the bankruptcy procedure had already been introduced in 1734. Only in the aftermath of the bankruptcy wave in Stockholm, originating from Amsterdam, did the government include detailed provisions regulating the bankruptcy procedure in the bankruptcy laws of 1767 and 1773. They encouraged the debtor to come forward and deliver his assets by granting them free passage, protecting him from imprisonment, forbidding the creditors to seize the property individually, and fixing a strict time limit on the procedure in order to avoid unnecessary costs that wasted the bankrupt's assets. According to the findings of Nyberg and Jakobsson court officials induced parties, whenever suitable, to come to a composition. Before the opening of a formal and costly process a preparatory meeting of creditors, debtors and a justice was frequently used for an arrangement. Both authors also assume that the new business-friendly regulation contributed to the increase in bankruptcy declarations in the last quarter of the century. A similar well-regulated procedure as in Sweden was practiced in Venice in the second half of the century as Magnus Ressel illustrates in a case study on the German merchant and textile entrepreneur in Venice who failed in 1773. The Venetian bankruptcy law, although dating back to the early seventeenth century, was well adjusted to the needs of a commercial elite and diverged fundamentally from the laws in Italy as it did not distinguish between inhabitants and foreigners, and encouraged negotiations among creditors and debtors that were to be sanctioned by the Venetian court.

In all, settlements between creditors and debtors, either private or under the surveillance of a justice, in the period between the first official proclamation of insolvency and the formal opening of court proceedings became a widespread feature in eighteenth century Europe.[31] Formal time and asset consuming court procedures were used as a last resort when efforts for arrangements had failed.

Despite the growing leniency of law and the encouragement of private or court-surveyed compositions the Damocles Sword of imprisonment was still hanging over the debtor. Imprisonment for debt was not abolished until the 1860s and 1870s in European countries.

Until right into the nineteenth century bankruptcy laws applied only to the commercial classes. They excluded petty debtors such as labourers, craftsmen, tradesmen and non-commercial classes. A prevailing reason for excluding non-trading classes from the benefits of the bankruptcy laws was voiced by the famous lawyer W. Blackstone:

> "They [the laws] allow the benefit of the laws of bankruptcy to none but actual traders; since that set of men are … the only persons liable to accidental losses and to an inability of paying their debts, without any fault of their own. If persons in other situations of life run in debt without the power of payment, they must take the consequences of their own indiscretion"[32]

England was not the only country that excluded non-traders from the bankruptcy laws. Similar regulations are to be found in German towns such as Hamburg or in France.[33] As mentioned above petty debtors in England came under the insolvency laws which provided for imprisonment and unlike the big merchants they remained liable for their debts. The distinction between bankruptcy and insolvency was repealed in England only in 1861 and imprisonment for debt even later in 1869.

Like the commercial elite the middling and lower classes were embedded in a network of credit and reciprocal obligations. Financial crises and bankruptcy waves similarly plunged them into economic failures.[34] By the last quarter of the eighteenth century rising dissatisfaction and public critique against traditional

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31 For Britain see especially Sheila Marriner: English Bankruptcy Records and Statistics before 1850. *Economic History Review* 33 (1980), pp. 351–366.

32 Quoted after Cohen, History of Imprisonment, p. 160.

33 See the papers of Jasper Kunstreich, Erika Vause and Viera Rebolledo-Dhuin in this volume.

34 For the credit networks of the middling and lower classes see Margot C. Finn: *The Character of Credit. Personal Debt in English Culture, 1740–1914.* Cambridge 2003; Craig Muldrew: *The Economy of Obligation: the Culture of Credit and Social Relations in Early Modern England.* Basingstoke 1998; Gabriele, B. Clemens (ed.): *Schuldenlast*

imprisonment practices had already given rise to a more liberal interpretation of the term trader and other groups.[35]

The use of imprisonment seems to have deviated considerably from the provisions of the law. Napoleon's Code de Commerce constituted the first detailed description of the bankruptcy procedure. It stipulated strict surveillance and control of the bankruptcy proceedings and imprisonment at least until proceedings could be initiated.[36] In her paper on the credit problems and the development of bankruptcies among Parisian book traders in the 1820s and 1830s Viera Rebolledo-Dhuin raises the question to what extent the provisions of the code for imprisonment of the insolvent debtor and the loss of commercial rights was enforced. Based on a sample of 141 bankruptcy files of nineteenth-century Parisian book traders and publishers Rebolledo-Dhuin reveals that only four of the sample were imprisoned. Further reforms in the 1820s and 1830s limited imprisonment further and eased the fate of the debtor and his family by allowing the unfortunate trader to keep his tools, furniture and money. Thus bankruptcy among the book traders did not necessarily end their career but was frequently used as an opportunity for a restart.

Based on the internment records of the debtor's prison in Lyon between 1835 and 1840 Erika Vause researches the social composition of the imprisoned debtors and the reasons that induced creditors to jail them. Starting with the French law of 1832 that limited the time in prison for debts below 500 francs, and exempted certain persons such as women and minors from imprisonment unless they had incurred commercial debts, she analyzes the social composition of the imprisoned debtors and how that institution functioned for both debtor as well as creditor. Lyon used to be a centre of the silk industry for centuries, but none of the 318 imprisoned debtors belonged to that industry. A conspicuous number came from the hospitality industry such as tavern keepers and artisans. The sums they were indebted for were generally under 500 francs. The creditors who came from the

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und Schuldenwert: Kreditnetzwerke in der europäischen Geschichte 1300–1900. Trier 2008.

35 In 1772 a philanthropic society was founded for the release of imprisoned persons for small debts and after the turn of the century further reliefs were granted for petty debtors. Acts in 1785 and 1786 restricted the time of imprisonment for small debtors and in 1808 an act was passed to release petty debtors for sums below £20 from prison. A Court for Relief of Insolvent Debtors was established a few years later to decide on prisoners' petition for release (Cohen, Imprisonment for Debt, pp. 163f.; Duffy, *Bankruptcy*, pp. 56–106).

36 Sgard, Legal Origins, pp. 400, 403.

moneyed classes used imprisonment for three main reasons: to compel the debtor to mobilize alternative credit resources from family or friends, as a means of initiating legal proceedings for bankruptcy, or to initiate a composition.

Practices for dealing with insolvent debtors did not only vary considerably depending on time, respective laws and judicial institutions, social status of debtors and creditors and their relationship, but the gap between norms and practice also broadened. By the mid-nineteenth century the old bankruptcy laws and institutions had become obsolete. Neither imprisonment nor the distinction between merchants/traders and non-traders were any longer suited for industrialized and commercialized societies which were structured according to negotiable instruments and large-scale investments in industrial enterprises. Substantial reforms in Europe were not implemented until the 1860s.[37]

The next three papers present some information about the changes in law and practice in Germany from the mid-nineteenth century onwards. Until unification in 1871 the German states and free cities had their own bankruptcy laws. Jasper Kunstreich throws light on the practice of coping with financial crisis in the last decades of Hamburg's independence before unification. The local bankruptcy law of 1753, already mentioned, was well suited for a highly commercialized local society that was socially and economically closely interwoven. The mid-eighteenth-century bankruptcy law of Hamburg was to Kunstreich a particularly business-friendly piece of legislation designed to overcome liquidity problems and provide for a structured renegotiation procedure and a fresh start. The old law and long-established practice of dealing with bankrupts was still flexible enough to manage the global crisis of 1857 which was also felt in Hamburg. Faced with a wave of bankruptcies the Senate installed a crisis management. It resorted to temporary instruments already utilized in the eighteenth century to overcome transnational financial crises.[38] Among others it established an institution called "administration" that allowed businesses to continue under the control of officially nominated administrators. In all 118 firms applied for it. Besides this measure

37 For these reforms see Duffy, *Bankruptcy*, pp. 122 ff.; Paolo die Martino: The Historical Evolution of Bankruptcy Law in England, the US and Italy up to 1939: Determinants of Institutional Change and Structural Differences. In: Gratzer / Stiefel, *Insolvency*, pp. 263–279; Sgard, Legal Origins, op. cit.

38 For the institution of "administration" see also Margrit Schulte Beerbühl: Die Hamburger Krise von 1799 und ihre weltweite Dimension. *Hamburger Wirtschafts-Chronik, Neue Folge* 10 (2012), pp. 85–110, here: p. 104f.

some clauses of the bankruptcy laws were suspended and loan institutions were created to overcome the liquidity squeeze.

The rise of big industrial enterprises employing a large workforce had already challenged the old bankruptcy system from the early nineteenth century onwards. Given the special situation of Hamburg, management of the 1857 crisis in that city may be seen as a late survival of the commercial bankruptcy regime. Due to the rise of big industrial enterprises with a large workforce and new corporate and managerial structures in the latter part of the century the old bankruptcy regime was replaced by industrial bankruptcy regimes in the European countries.

After the unification of Germany the local and regional bankruptcy laws were abolished and replaced by a new national law in 1879. It provided for two types of proceedings: the distribution procedure and compulsory composition. While the distribution procedure allowed the creditors to assert their claims even after the closing of a bankruptcy procedure, compulsory composition, described in detail by Ulrich Falk and Christoph Kling, provided several advantages for the debtor. Compulsory composition shortened the procedure considerably, and the creditors were compelled to accept the court's decision. From 1886 to World War I and the 1920s between 21% and 29% of bankruptcy cases ended with a compulsory composition. Only privileged creditors were exempted from compulsory composition, and an amendment of the law in 1898 refused to allow composition in those cases when the expected quota was below one fifth of the claims. The authors maintain that compulsory composition had been a rather effective and simple institution until the first half of the 20th century. They attribute the decline that followed to the growth of credit securing instruments which increased the number of assetless bankruptcies.

The final paper concludes the volume with an insight into today's German bankruptcy law. Peter von Wilmowsky analyses the role and principles that govern contemporary German insolvency law regarding stock companies and the various interests of both creditors and public in either keeping the firms going or closing them down. Among the aims of contemporary insolvency law are a ban on individual collection by creditors and a distribution of the assets according to hierarchy and order of claims. The law should also guarantee a neutral decision concerning the future of the firm.

Some issues addressed here are taken up again in the current debate on the impact of bankruptcy laws on entrepreneurship and the demands for entrepreneur-friendly bankruptcy regimes. Incentives to facilitate a fresh start for bankrupts are currently seen as imperatives for good governance. European societies were slow to accept failure as the Janus face of success and likewise that financial crises

and bankruptcies are integral features of the capitalist economy. According to the Schumpeterian view, bankruptcies are a sign of creative destruction. The level of speculation, risk-taking and failures are seen as indicators of growth which require a business-friendly legal framework.[39]

The path of change and relationships between creditors, debtors, laws and practice certainly diverged in the European countries over the past centuries depending on economic development and established cultural diversities. Despite variations some problems in dealing with bankruptcies reveals common features which all states had to cope with. In this volume the aim was to highlight some features of interaction between private and judicial conflict regulation.

Basic institutional and legal instruments to cope with the rise of risk and failure were missing at the beginning of the early modern age, and cultural perceptions of bankruptcy as a criminal act had to be overcome as well. Given the lack of a structured procedure, merchants and traders generally preferred to resort to private or extra-judicial conflict resolution, as this promised more advantageous and practical solutions. However, they needed laws as conflict-reducing devices against recalcitrant creditors and fraudulent debtors. In the early centuries lawmakers and judges generally possessed little expertise in commercial affairs.[40] The institution of commercial courts and commercial court judges was first introduced in France during the French Revolutionary and Napoleonic Period and spread after the turn of century to other European towns and countries.[41]

Compared to the pace of economic change norms and institutions responded only slowly, but they were receptive to the realities. The result of legislation reforms was often pragmatic measures to solve immediate problems, trying to

39 Werner Plumpe: *Wirtschaftskrisen. Geschichte und Gegenwart*. München 2012, p. 14; similarly Kim Christian Priemel: Was ist Spekulation, wer ist Spekulant? In: *Jahrbuch für Wirtschaftsgeschichte* 52, 2 (2013), pp. 99–26, here: p. 10, also Toni Pierenkemper: Von der Tulpenkrise zum Finanzkollaps. Das Allgemeine im Besonderen, in: ibid, pp. 139–159.

40 Concerning the influence of judges and their expertise on the bankruptcy procedure see Kenneth Ayotte: Matching Bankruptcy Laws to Legal Environments. *Journal of Law, Economic & Organization* 25 (2007), pp. 2–30.

41 On the French commercial courts and the predecessors see Rebolledo-Dhuin's contribution in this volume. In Hamburg the first commercial court was instituted in 1816 and Bremen 1845. (see August Schiebe, *Über einige Institutionen Frankreichs in Bezug auf Handel und Industrie*, [Leipzig] 1846; Willy Silberschmidt, *Die Entstehung des deutschen Handelsgerichts*, Berlin 1894.

generalize and legalize established practices, but the normative implementation could certainly also open up space for new practices and procedures. In all, the relationship between bankruptcy law, practice and economic change does not reveal straightforward interdependence but a complex and multifaceted configuration.

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