CROSS-BORDER EUROPEAN INSOLVENCY IN THE BREXIT ERA

Date: 3 May 2017

Restructuring & Insolvency Alert

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The regime for dealing with insolvency proceedings within the European Union (EU) is about to become more coordinated. The timing is ironic given that the change will take place in the period leading up to the March 2019 exit of the United Kingdom from the EU. On 26 June 2017, the EU insolvency regime will be extended by the application of the Recast Insolvency Regulation[1] that reforms the first EU Insolvency Regulation which came into force on 31 May 2002.[2]

THE RECAST REGULATION

The main new and amended provisions are:

- the ability to coordinate insolvency proceedings of members of a group of companies established across several EU member states;
- refining the definition of "centre of main interests" (COMI) and trying to avoid forum shopping;
- widening the possibility of opening secondary procedures in several member states;
- improving publicity for creditors and debtors of insolvency proceedings by means of inter-connected insolvency registers throughout the EU;
- widening the scope of proceedings subject to the Recast Regulation to include various interim proceedings thereby restricting the ability of a debtor to manage its assets and affairs and/or proceedings involving a temporary stay of individual enforcement actions in order to allow for negotiations between a debtor and its creditors;
- giving the debtors and creditors the power to challenge a decision opening main insolvency proceedings on grounds of international jurisdiction; and
- the ability of the insolvency practitioner in the main proceedings to give a unilateral undertaking with a view to avoiding the commencement of secondary proceedings.

INTRODUCING RULES FOR GROUP INSOLVENCIES

Where insolvency proceedings relate to two or more members of a group of companies in different member states, an insolvency practitioner appointed in proceedings must cooperate with other appointed insolvency

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practitioners in the same group to the extent that such cooperation is appropriate to facilitate effective administration and is not incompatible with the rules applicable to each proceeding and does not entail any conflict of interest. The various insolvency practitioners and the courts involved should be under an obligation to cooperate and communicate with each other. Such cooperation is aimed at finding a solution that would give the best outcome across the group.

This obligation may also entail the opening of "group coordination proceedings" after the insolvency practitioner has obtained necessary authorisation. Each insolvency practitioner will have the choice as to whether or not to participate in such group coordination proceedings. However, if they initially object to inclusion then they can change their minds and subsequently participate. The aim of such coordination is to produce a generally positive impact for the creditors. The cost of the proceedings should not outweigh the advantages.

Where more than one insolvency practitioner wants to open and run group coordination proceedings, it is the court which is first in time to claim jurisdiction that will run the process. Any other court subsequently requested must decline jurisdiction. The court which is asked to open group coordination proceedings must give notice as soon as possible of the proceedings and of the proposed coordinator to the insolvency practitioners appointed in relation to other members of the group.

The role of the coordinator is mainly to identify recommendations for the coordinated conduct of the insolvency proceedings and propose a group coordination plan that identifies a set of measures to ensure an integrated approach to the resolution of the group members' insolvencies.

COMI AND FORUM SHOPPING

One of the criticisms of the original Regulation was that it encouraged individuals or companies within the EU to seek to move their business interests (or the appearance of their business interests) to a more debtor-friendly jurisdiction within the EU when they became financially distressed. The Recast Regulation seeks to address this by adding further tests to establish COMI. When determining whether the debtor's COMI is ascertainable by third parties, special consideration should be given to the creditors and to their perception as to where a debtor conducts the administration of its interests. The presumptions that the registered office, the principal place of business and the habitual residence are the centre of main interests should be rebuttable.

In the case of a company, it should be possible to rebut this presumption where the company's central administration is located in a member state other than that of its registered office. In the case of an individual who is not carrying on a business or professional activity, it should also be possible to rebut this presumption. An example would be where it can be established that the principal reason for moving was to file for insolvency proceedings in the new jurisdiction and where such filing would materially impair the interests of creditors whose dealings with the debtor took place prior to the relocation.

The presumption should also not apply where, in the case of a company, legal person or individual exercising a business or professional activity, the debtor has relocated its registered office or principal place of business to another member state within the three month period prior to the request for opening insolvency proceedings. Nor should the presumption apply in the case of an individual not conducting a business, where the debtor has relocated his or her habitual residence to another member state within the six month period prior to the request for opening insolvency proceedings.

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In all cases where there is doubt, the court should require the debtor to submit additional evidence to support its assertions and where the applicable law allows, give the debtor's creditors the opportunity to present their views on the question of jurisdiction.

SECONDARY INSOLVENCY PROCEEDINGS

As under the existing Regulation, there will be the ability to open secondary insolvency proceedings in another member state alongside one set of main insolvency proceedings. These new secondary insolvency proceedings will no longer be limited to liquidation-type procedures and can now include rescue-type proceedings, such as administration in England. Secondary insolvency proceedings can serve different purposes: protecting local interests; if the insolvency and estate of the debtor is too complex to administer as a unit; or the differences in the local systems concerned are so great that difficulties may arise from the extension of effects of the main insolvency proceedings.

In order to deal with these potential difficulties, the Recast Regulation confers on the insolvency practitioner in main insolvency proceedings the possibility of giving an undertaking to local creditors that they will be treated as if secondary insolvency proceedings had been opened. That undertaking has to meet a number of conditions, in particular that it be approved by a qualified majority of local creditors. For the purposes of giving the undertaking, the assets and rights located in the member state where the debtor has an establishment should form a sub-category of the insolvency estate.

The Recast Regulation also provides for the possibility that the court temporarily stays the opening of secondary insolvency proceedings in order to preserve the efficiency of the main insolvency proceedings. The court should grant the temporary stay if it is satisfied that suitable measures are in place to protect the general interests of local creditors. The insolvency practitioner in the main proceedings should not be able to realise or relocate, in an abusive manner, assets situated in the member state where an establishment is located.

ENSURING PUBLICITY FOR INSOLVENCY PROCEDURES

In order to improve the provision of information to relevant creditors and courts and to prevent the opening of parallel insolvency proceedings, member states will be required to publish relevant information in cross-border insolvency cases in a publicly accessible electronic register. Such registers should eventually become interconnected via the European e-Justice Portal (the "Portal").

By 26 June 2018, member states will be obliged to establish one or several registers concerning insolvency proceedings which should contain, amongst other information: the date of and name of the court opening insolvency proceedings; the type of procedure; information on the debtor and the insolvency practitioner; and any time limits.

From 26 June 2019, the European Commission must establish a decentralised system for the interconnection of insolvency registers via the Portal, which shall serve as a central public electronic access point to information in the system. Given the timing of Brexit, it remains to be seen whether the UK will take part in this scheme.

OTHER PROVISIONS TO NOTE IN THE RECAST REGULATION

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A debtor or any creditor may challenge before a court the decision opening main insolvency proceedings on grounds of international jurisdiction.

The court which opened main insolvency proceedings has jurisdiction to approve the termination or modification of contracts in relation to immovable property where: (a) the law of the member state applicable to those contracts requires that such contract may only be terminated or modified with the approval of a court opening insolvency proceedings; and (b) no insolvency proceedings have been opened in that state.

The closure of insolvency proceedings does not prevent the continuation of other insolvency proceedings concerning the same debtor which are still open at that time.

THE EFFECT OF BREXIT

The Recast Regulation will be applied in June 2017, being just three months after the triggering of the UK's two year period of Brexit negotiations. The Recast Regulation will come into force in the UK and will be applicable up to, at least, March 2019. Therefore, it remains as relevant to the UK as any other member state during that time and will continue to apply to any global business which has operations within the EU. The Recast Regulation does extend to companies registered outside of the EU, provided COMI falls within an EU member state (other than Denmark which has opted out of the Regulation regime).

WHAT OTHER LAWS WILL APPLY TO CROSS-BORDER INSOLVENCY AFTER BREXIT?

The UK is a party to the UNCITRAL Model Law (the "Model Law"), which in the UK has been implemented by way of the Cross Border Insolvency Regulations 2006 ("CBIR 2006"). The Model Law aims to encourage recognition of foreign proceedings and cooperation between jurisdictions. One of its key purposes is to provide for simplified procedures for recognition and for the appointment of a representative of foreign proceedings. According to the Model Law, domestic courts should cooperate "to the maximum extent possible" with foreign courts and representatives.

However, the Model Law has only been adopted by four EU member states other than the UK, namely Greece, Poland, Romania and Slovenia. Other major jurisdictions which are party to the Model Law are Australia, Canada, Japan, New Zealand, the Republic of Korea, Singapore and the United States. The Model Law will continue to apply to the UK after Brexit. However, given that few EU countries have adopted the Model Law, if more member states fail to join the UNCITRAL regime, it will be of limited use for pan-European insolvency coordination.

If the Recast Regulation and the Model Law do not apply in the majority of EU member states, then UK insolvency practitioners will need to rely on domestic law of the member state in which recognition is sought, whose outcome would be different according to the specific jurisdiction.

Alternatively the UK insolvency practitioner could open separate secondary proceedings in that other state. This would add time and costs to the process of realisations and distributions. The outcome for creditors would differ between jurisdictions.

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The existing Insolvency Regulation and the replacement Recast Regulation are each arguably a stronger and more advanced tool for the proper coordination of cross-border insolvencies than the Model Law. Certain countries, such as Poland, have backtracked on the scope of rights of non-EU foreign administrators and creditors by amending the international chapters of their insolvency laws into which the Model Law had been previously almost identically copied.

In relation to insolvency proceedings commenced in EU member states, these would need to rely on the UK's domestic rules of recognition, such as section 426 of the Insolvency Act 1986 (in the case of the Republic of Ireland) or the CBIR 2006.

SCHEMES OF ARRANGEMENT

English courts have been willing to sanction schemes affecting companies incorporated outside of England and Wales where it can be established that the company has a "sufficient connection" with England and Wales. The court needs to be satisfied that the scheme is capable of being in force in the jurisdiction in which the company's assets are situated. For example, that any relevant finance documentation was governed by English law and contained a clause granting jurisdiction in favour of the English courts.

OTHER REGIMES

On Brexit, absent any alternative arrangements, the EU Judgements Regulation, the EU Rome I Regulation (contractual obligations) and the EU Rome II Regulation (non-contractual obligations) will cease to be directly applicable in the UK. In relation to choice of law, the English courts are still likely to respect provisions in contracts and other cross-border obligations that confer jurisdiction by agreement on the English courts regardless of what replaces the EU Rome I and II Regulations. With regard to recognition of judgements, foreign legal opinions are likely to still be necessary.

CONCLUSION

The Recast Regulation has sought to deal with some of the issues exposed by seeing the original Regulation in action. It also represents a significant extension of cooperation between insolvency practitioners and courts across member states. The Recast Regulation provides for a review of the entire text no later than ten years after its coming into force and after five years on the application of the group coordination proceedings. By that time, the UK will have exited the EU.

NOTES:

[1] Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast)

[2] Council Regulation (EC) (No 1346/2000) of 29 May 2000 on insolvency proceedings

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