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EDITORIAL

Hard Choices: Restructuring and Insolvency Dealmakers Face Uncertainty Ahead of Possible 'Hard Brexit'

Kate Stephenson, Partner, Kirkland & Ellis International LLP, London, UK, and **Sacha Lürken**, Partner, Kirkland & Ellis International LLP, Munich, Germany

Summary

The UK Government has issued guidance on the prospect of a 'no deal' Brexit, including the possible future of the cross-border European restructuring and insolvency landscape. In this article, the authors consider the potential practical implications of this scenario.

Introduction

A 'no deal' Brexit would negatively impact the UK's restructuring and insolvency framework, the force of which depends, in part, on its pan-European reach. Losing the ability to deal with insolvencies via a single process, with automatic recognition across the EU, would make it more complex, lengthy and expensive to resolve cross-border mandates, with the prospect of parallel proceedings.

This would jeopardise the prospect of rescue and reduce returns for stakeholders – and undermine the UK's status as a leading global restructuring hub.

We – like the UK government – hope for a post-Brexit agreement that reflects the principles of mutual co-operation enshrined in the current EU framework.

Bracing for potential impact of 'no deal' Brexit

The UK and the EU are stepping up preparations for a possible 'no deal' Brexit. (The UK is scheduled to leave the EU on March 29, 2019; it is yet to be determined what kind of deal or transition arrangements – if any – will be reached.)

The UK Government has announced that, in a 'no deal' scenario:

- the majority of the EU Insolvency Regulation – which covers the jurisdictional rules, applicable law and recognition of cross-border insolvency proceedings – would be repealed in all parts of the UK;
- the UK would retain the EU rules that provide for the UK courts to have jurisdiction where a company or individual is based in the UK, and the law would ensure that insolvency proceedings could continue to be opened in those circumstances;
- post-Brexit, it would be possible to open insolvency proceedings under any of the tests set out in our domestic law, regardless of whether (or where) the debtor is based elsewhere in Europe (given that the EU Insolvency Regulation would no longer operate to restrict the opening of proceedings); and
- UK insolvency practitioners would need to make applications under an EU country's domestic law in order to have UK orders recognised there.

The announcement contains little that was not already known or obvious, but serves as a sharp reminder of the harsh reality of a 'no deal' Brexit for our market.

The scenarios below demonstrate the potential practical implications of the latest announcement. Of course, these are only brief, illustrative summaries regarding a highly complex and uncertain area of law; they are not a substitute for definitive advice.

Key takeaways for a 'no deal' Brexit
– There is a significant risk that UK insolvency proceedings and schemes of arrangement would not be recognised in other EU countries
– The EU Insolvency Regulation would be repealed in the UK
– UK courts may recognise EU insolvency procedures via the Cross-Border Insolvency Regulations, but such recognition would require a court application and – critically – would be unlikely to recognise the compromise of dissenting creditors' English law-governed claims (unless such creditors were present in the foreign jurisdiction or had submitted to the foreign proceedings)
– EU restrictions on opening UK proceedings in respect of EU companies would no longer apply
– US recognition of UK proceedings (and vice versa) would remain unchanged

'Inbound' recognition of European processes in the UK

In a nutshell: UK courts would continue to recognise European insolvency proceedings, though only upon application and with greater discretion as to the relief to be granted to the foreign insolvency officeholder.[1] As the law presently stands, the UK courts would not recognise a purported compromise or release of English law debt pursuant to foreign proceedings.[2]

SCENARIO 1

A distressed French company has its centre of main interests (CoMI) in France. Certain of its debt is governed by English law. The company opens French accelerated financial safeguard proceedings to amend and extend its existing financing arrangements.

Currently: The French insolvency proceedings would automatically be recognised in the UK under the EU Insolvency Regulation. This includes the amendment of the English law debt.[3]

In a 'hard Brexit' scenario: The French proceedings should be recognised via a court application under the UK Cross-Border Insolvency Regulations (CBIR), which implement the UNCITRAL Model Law on Cross-Border Insolvency.

In a potential application by an appointed foreign representative for recognition of the French proceedings under the CBIR:

– the French proceedings would benefit from a limited stay on proceedings against the debtor or its assets;[4] and
– the English court might grant additional appropriate (discretionary) relief.

However, creditors with debt governed by English law would not be bound by the purported compromise under the French proceedings, *unless* they were present in France at the time the French proceedings were initiated, were a claimant or counterclaimant in those proceedings, or voluntarily submitted to the French court's jurisdiction by appearing voluntarily or by agreement.

Compromise of French law-governed claims within the French proceedings would be likely to be recognised by an English court.[5]

'Outbound' recognition of UK processes in Europe

In a nutshell: There is a significant risk that UK insolvency proceedings and schemes of arrangement would not be recognised in other EU countries. Their ability to be recognised would depend upon European conflict of law rules. Only a small minority of EU countries have implemented the UNCITRAL Model Law on Cross-Border Insolvency.[6]

SCENARIO 2

An English company, with its CoMI in England, sells its business and assets to a creditor-owned Newco via (English) pre-pack administration. Certain of its direct subsidiaries and other assets are located in Germany.

Currently: The administration would automatically be recognised in Germany (including the transfer of the company's German subsidiaries and other assets to Newco).

In a 'hard Brexit' scenario: The English administration would not automatically be recognised in Germany via the EU Insolvency Regulation. Encouragingly, however, the proceedings ought to be recognised automatically under German conflict of law rules,[7] based on the fact that the company's CoMI is in the UK.[8] (If the company's CoMI were outside the UK, the pre-pack would not be recognised in Germany.) There would remain a risk of parallel proceedings being opened in Germany, in respect of assets located in Germany; this contrasts with the current position under the EU Insolvency Regulation.[9]

Notes

1 The English court will generally grant the relief that would be available to an English insolvency practitioner.
2 This position may change, (a) if the UK implements the forthcoming UNCITRAL Model Law on recognition and enforcement of insolvency-related judgments, as expected and (b) depending on the outcome of a major case pending in the English courts.
3 Strictly, this point is not beyond doubt, but is considered the better interpretation.
4 As the company's CoMI is in France, the French proceedings would constitute 'main proceedings' under the CBIR and therefore be eligible for more extensive relief than that available for 'non-main' proceedings (for which relief is discretionary).
5 This is partly based on the Rome I Regulation (on the law applicable to contractual obligations), which applies to non-member states and which the UK government intends to retain even in a 'no deal' scenario.
6 Namely Greece, Poland, Romania and Slovenia, in addition to the UK.
7 Specifically, pursuant to section 343(1) of the *Insolvenzordnung*.
8 German courts would however have discretion to scrutinise whether the rules of the pre-pack administration comply with German public policy; this contrasts with the position under the EU Insolvency Regulation.
9 A creditor could ask the German court to commence territorial insolvency proceedings (*Partikularinsolvenzverfahren*) in respect of assets located in Germany if the creditor is able to demonstrate a legitimate interest, e.g. if the English proceedings provide for a significantly worse

The prospect of recognition of the pre-pack would be far less certain if recognition were sought in certain other EU jurisdictions. In certain circumstances, some EU countries may not recognise UK insolvency proceedings, for example if that would prevent creditors from taking action against the assets held in that country. Recognition would be more likely in those countries which have implemented the UNCITRAL Model Law on Cross-Border Insolvency and those countries with domestic provisions influenced by the Model Law, such as Germany.

This raises a prospective imbalance between UK 'inbound' recognition of EU proceedings and EU recognition of UK 'outbound' proceedings. The prospects of successfully obtaining recognition for a UK insolvency proceeding in an EU country would need to be carefully considered in each case.

SCENARIO 3

A Dutch company, with its CoMI in the Netherlands, pursues an English scheme of arrangement to amend and extend its English law-governed facility agreement.

Currently: The scheme would likely be recognised in the Netherlands, pursuant to the EU Judgments Regulation (a.k.a. the Brussels Ia Regulation),[10] Dutch domestic private international law or (possibly) the Rome I Regulation.

In a 'hard Brexit' scenario: It is likely – but far from certain – that the scheme would be recognised in the Netherlands, based on the Brussels Convention,[11] Dutch domestic private international law and/or (arguably) the Rome I Regulation. If the facility agreement provides for the exclusive jurisdiction of the English courts, then recognition might also be afforded under the Hague Convention on Choice of Court Agreements, which the UK government has announced it would seek to rejoin in the event of 'no deal'.[12]

Side note – jurisdiction to open UK proceedings

The EU Insolvency Regulation operates as a constraint on the ability to open UK proceedings in respect of a company with its CoMI in another EU member state. As this constraint on jurisdiction is set to be repealed, this opens the possibility of (non-main) UK insolvency proceedings being opened in respect of EU companies without the need for a CoMI shift. This potentially includes the UK's new restructuring plan procedure, to be introduced as soon as parliamentary time permits.

This means the full range of UK insolvency proceedings may be opened up to foreign companies, subject to some requirement for a 'sufficient connection' to the UK.[13]

However, this remains subject to the difficult question of whether such proceedings would receive the requisite recognition in other EU jurisdictions, as explored above.

SCENARIO 4

An English company pursues an English scheme of arrangement to effect a debt-for-equity swap in respect of its New York law-governed high-yield notes.

Currently: The scheme would likely be afforded recognition in the US pursuant to an application under Chapter 15 of the Bankruptcy Code. This includes recognition of the compromise of the New York law-governed notes.

In a 'hard Brexit' scenario: The scheme and its effects would be recognised in the same way as at present. Happily, even a hard Brexit looks unlikely to make a difference from the perspective of US cross-border insolvency.

Notes

outcome for that creditor than German proceedings. This applies even if the company does not have a branch in Germany.

10 The Brussels Ia Regulation would be repealed in a 'hard Brexit' scenario, according to the UK government's recent announcement.

11 The Brussels Convention on jurisdiction and enforcement of judgments in civil and commercial matters remains in place; both the UK and the Netherlands are contracting parties.

12 The UK currently participates in the Hague Convention based on its EU membership. The UK's independent accession to the Hague Convention is not guaranteed.

13 The requirement for a 'sufficient connection' already applies to schemes of arrangement and liquidation, but could be extended to administration and company voluntary arrangements.

International Corporate Rescue

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