HFW

INSOLVENCY

‘A complete mess’

Welcome to post-Brexit insolvency

Given the global pandemic, it’s somewhat unsurprising that the UK’s loss of access to the EU Regulation on Insolvency Proceedings (EUIR) has received relatively little press.

After all, what with the state support of furlough and loan schemes – along with the temporary suspension of winding up petitions and wrongful trading rules, as well as the ban on landlords evicting commercial tenants – formal insolvencies in the UK have “just dried up” says HFW fraud and insolvency co-head Rick Brown.

But a problem suspended is not a problem solved. Eventually, normal service will resume with the UK facing a backlog of insolvencies – much of it with a European dimension and, several months post-Brexit, still no formal mechanism for cross-border recognition. “We’ve got this really worrying position,” notes Brown. “This is potentially an open wound for the UK, but we’re not yet sure of the real impact because there are currently so few insolvency filings.” Quantuma restructuring veteran Andrew Hosking puts it more bluntly: “It’s a complete mess.”

Short of a UK/EU deal on a substitute for the EUIR being struck and implemented in short order (which seems unlikely), that leaves insolvency professionals with the unappealing prospect of either subsequently pursuing recognition in individual states, or running parallel proceedings – potentially in multiple countries. Aside from additional time and money wasted, many fear the situation risks a free-for-all, with creditors pursuing their interests in various national markets as an English law moratorium preventing civil proceedings against a debtor now loses automatic recognition. “This could lead to one, two, three or even six months of delay in enforcement or recognition steps,” says Brown. “If you’re trying to act quickly and stop creditors in other states acting before you, you’re at a real disadvantage.” Further uncertainty comes regarding the status of English schemes of arrangement – regularly used in restructurings – which also lose the automatic recognition they previously enjoyed under separate civil jurisdiction rules.

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Optimists note that the scenario looks considerably less uncertain for purely domestic insolvencies, and cases impacting assets outside the EU are obviously unaffected. Moreover, the English courts have established mechanisms for recognition of insolvency proceedings outside of the EU, mitigating much confusion on inward matters.

But there will obviously be many insolvencies that defy such neat categories. European states also have substantial incentives to bring more insolvency work to their jurisdictions, while the somewhat antagonistic relationship between the UK and the EU is hardly set to calm the situation. Brown warns that there will likely be major differences in how individual European states respond – especially in contentious insolvencies involving civil claims or allegations of fraud. "There won't be one single process to get recognition – some will be quick, some slow," he says. "Some states will require you to re-litigate your claim there. That's a really unwelcome development."

HFW fraud and insolvency partner Simon Jerrum says that uncertainty will stoke a renewed period of forum shopping in European insolvency as parties jostle for advantage. "There will certainly be a degree of COMI-shifting," he says. "You'll see stakeholders considering carefully the jurisdictional issues involved in order to take most advantage of the situation." As such, litigation around the COMI status of insolvent businesses with major operations in both the UK and EU states also seem likely.

The not so bad news

While UK insolvency professionals are clearly stuck with this problem for the foreseeable future, there are hopes that the situation may be clarified in the near future. For example, the UK has applied to join the Lugano Convention – the treaty governing cross-border recognition of judgments, with signatories including the EU, Switzerland, Norway, Iceland and Denmark. UK accession would be a substantial band-aid – especially as restructurings under a scheme of arrangement would likely be covered under the convention as well. However, Brown warns that "Lugano will not be a panacea but it will at least give a single defined process with clearer ground-rules". (At time of publication however, the EU Commission has recommended that the EU should not permit the UK to accede to Lugano.)

The UNCITRAL Model Law on Cross-Border Insolvency, a framework agreement that sets out when a nation's courts should recognise proceedings in another country, also offers help in some instances, as it has been adopted by four EU countries: Greece, Romania, Slovenia and Poland. Past that, a hotchpotch of the Hague Convention, the Rome Convention and certain bilateral treaties offer some options, especially for matters involving contracts with English jurisdiction clauses.

Jerrum notes that the English courts will start to build up case law to ease the path to recognition in cross-border European insolvencies. "We'll start to see some judgments that help on clarity, but it won't be for a number of years before you really get certainty. There's undoubtedly going to be more cost, more delay – more effort generally – but in the long-run the attractiveness of the UK will not be diminished."

Optimists also point to the English courts' commanding position in the European insolvency and restructuring market as providing considerable support for the UK's position. Further bolstering that standing is the popularity of English schemes of arrangement in restructurings – a propensity that has at times pushed the jurisdictional reach of the English courts to a substantial degree. Quantuma's Hosking argues that

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Grant Thornton partner Mark Byers

the UK will retain the lion's share of its insolvency work – despite the likelihood of more parallel proceedings – highlighting the lustre of English schemes and the UK's ability to get recognition with former Commonwealth States under Section 426 of the Insolvency Act. Section 426 countries include Australia, Canada, New Zealand, Hong Kong, South Africa and the Republic of Ireland. "We won't be disenfranchised," Hosking adds, "but I do think it will be horses-for-courses as to whether to use a European system or the UK if it's involving Hong Kong, Singapore, Australia, Canada, where the UK will be more quickly recognised."

There will also be hopes that the UK's well-received Corporate Insolvency and Governance Act 2020 – touted as a more debtor-friendly framework in the mould of the US – will assist

the UK in maintaining its appeal for cross-border insolvency matters. Others argue that, despite national jostling post-Brexit, the general direction of travel is moving towards unified approaches. Grant Thornton partner Mark Byers comments: "We are moving towards more universalism in our regime. The take-up of the UNCITRAL Model Law has been pretty poor in Europe, but universalism is here to stay. I was a Remainer, so feel it was a mad decision for the UK to come out of the EU, but we will find ways to be pragmatic and use other mechanisms to get the right solutions for restructuring."

The Takeaway

1. The loss of the UK's access to EU insolvency regime will result in delay, higher costs and parallel proceedings in multiple jurisdictions.
2. Creditors face the risk of a free-for-all with insolvent debtors with substantial pan-European operations.
3. Stakeholders should consider carefully the jurisdictional issues involved and take appropriate advice.

About HFW

HFW is a leading global law firm in the aerospace, commodities, construction, energy and resources, insurance, and shipping sectors. It has more than 600 lawyers, including 185 partners, based in offices across the Americas, Europe, the Middle East and Asia-Pacific.

The firm's fraud and insolvency group are experienced commercial litigators with a particular focus on dealing with high value, cross border matters where there is an overlap between fraud and insolvency. The team's expertise spans a wide range of sectors and industries, as well as knowledge of global jurisdictions and how to ensure the best possible result for clients.

HFW prides itself on its deep industry expertise and its entrepreneurial, creative and collaborative culture.

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