

CROSS BORDER INSOLVENCY ISSUES: CASE UPDATE OCTOBER 2009

TEXT OF A CASE UPDATE PREPARED FOR INSOL EUROPE CONGRESS 2009

UNITED KINGDOM CASES

1 *Re: Nortel Networks SA and others* [2009] EWHC 206 (Ch)

The Nortel Group operated on a global basis. The European arm of the Group, which operated in Europe, the Middle East and Africa, had been placed into administration by the court on 14 January 2009, the same day as filings under the Companies Creditors Act 1985 in Canada and under Chapter 11 of the US Bankruptcy Code. The joint administrators concluded that in view of the complex trading relationships between the companies they controlled there should be a co-ordinated re-organisation of the entire group, in order to maximise value for creditors. That required each of the individual companies to continue trading in the meantime. The joint administrators had obtained '*Day One Orders*' to try and avoid secondary proceedings in overseas jurisdictions, but still sought greater protection. The *Day One Orders* would enable the administrators to make distributions to overseas employees and preferential creditors in accordance with the rules applicable to their own jurisdictions rather than under UK rules.

The joint administrators made an application for the court to send letters of request to the courts of certain other Member States asking that arrangements be put in place for the joint administrators to be given notice of any request or application to open secondary proceedings, and to permit the joint administrators to make submissions on any such request or application.

The court found that it had an inherent jurisdiction to make such a request of the courts of Member States. It referred to Article 31(2) of the Regulation which provides that “*liquidators in main and secondary proceedings are duty bound to co-operate with each other*”, and noted that the Article had been treated as referring to a wider duty extending to the courts who controlled insolvency procedures. The court cited previous examples of such co-operation.

The court also noted that it was desirable that a foreign court dealing with an application to open secondary proceedings should be provided with reasons by the joint administrators as to why those secondary proceedings might have an adverse impact on the main proceedings (as noted by the Court of Appeal of Versailles in *Rover France SAS*).

The court agreed that Article 33(1), which provides for a liquidator in main proceedings to apply for a stay of secondary proceedings, did not give sufficient protection of itself as the commencement and continuance of secondary proceedings, which could only be winding up proceedings, was likely to cause the relevant company to cease to trade. It would only be the realisation of assets in the secondary proceedings that was halted by the stay. The proceedings themselves would remain live.

In the circumstances Mr Justice Patten was willing to authorise the sending of appropriate letters of request to the courts of those certain Member States noted in the draft order.

This was a further good example of the court's willingness to co-operate with courts in other jurisdictions to promote the most beneficial outcome for creditors by enabling office holders to be heard .

2 Re: *Lennox Holdings Plc* [2009] BCC 155

This was a decision on COMI made by Mr Justice Lewison. The court was asked to make an administration order in relation to a UK parent company and three of its subsidiaries, two of which had their registered offices in Spain. There was no real doubt that administration was the appropriate insolvency procedure for all companies, but only if the court had jurisdiction in relation to the Spanish registered subsidiaries.

The court first of all considered Article 3 of the Regulation, that the place of the registered office is presumed to be the COMI. That is a rebuttable presumption. Mr Justice Lewison then went on to review the *Eurofood* decision and the 'head office function test', and concentrated on where the head office functions of the Spanish companies were carried out. COMI was not determined by where a company had its head office, or of itself by the COMI of the parent company. The important factor was the location of control of the subsidiaries by their boards, rather than control of their boards by the parent company. On the facts, the financing of the Spanish subsidiaries, their major decisions and the administration of the companies were all conducted in the UK through English suppliers, English directors and with English funding. The head office functions were carried out in the UK by the boards of the Spanish registered companies, and hence COMI was within the jurisdiction. The presumption as to the registered office was rebutted.

What is interesting this case is that Mr Justice Lewinson did not consider the ascertainability of COMI by third parties as a central concept to determine where COMI lay.

3 *Stanford International Bank Limited* [2009] EWHC 1441 (Ch)

Stanford was a further case that came before Mr Justice Lewinson. He handed down judgment in *Stanford* just over 12 months after his judgment in *Lennox*.

The Bank was incorporated and had its registered office in Antigua. Its largest group of investors were those based in the USA. On 16 February 2009 a receiver was appointed in the USA over the Bank's assets worldwide, and on 19 February 2009 the court in Antigua appointed a receiver-manager. The Antiguan court subsequently made a winding up order and appointed liquidators. Both the US receiver and the Antiguan liquidators applied for recognition under the Cross Border Insolvency Regulations 2006. The 2006 Regulations give effect in the UK to the UNCITRAL Model Law. Both office holders claimed to have been appointed in 'foreign main proceedings' i.e. under a collective judicial or administrative proceeding pursuant to a law relating to insolvency for the purpose of reorganisation or liquidation. In order to be a 'foreign main proceeding' the process must take place in the state where the debtor has its COMI. There is a presumption that COMI is in the state where the registered office exists.

The court was required to determine a number of matters in dispute, one of which was where the Bank had its COMI. Mr Justice Lewinson found it was reasonable to infer that COMI in the Model Law would bear the same meaning as in the Regulation, and counsel appearing before him agreed that the court should follow the decision of the ECJ in *Eurofood*. Having heard adversarial argument as to the nature of the 'head office function test', which he did not hear in *Lennox*, Mr Justice Lewinson found on this occasion that in order to rebut the presumption of registered office, not only did the party seeking to rebut the presumption have to demonstrate that head office functions were carried out in a different Member State on an objective basis, but also that the location of those functions was ascertainable by third parties. He had been wrong in *Lennox* to concentrate only on where the head office functions were carried out, and to find that 'ascertainability by third parties' was not a central concept to COMI.

Mr Justice Lewinson also found that following *Eurofood* the presumption of COMI coinciding with registered office was a true presumption and not simply a factor to be considered. The earlier case of *Re Ci4net.com Inc* should not be followed.

The court would therefore apply the following test:

- i. COMI is presumed to follow the registered office in the absence of proof to the contrary;
- ii. the burden of rebutting the presumption lies on the party seeking to rebut it (in this case the US receiver);
- iii. the presumption will only be rebutted by factors that are objective;
- iv. but objective factors will not count unless they are also ascertainable by third parties;
- v. what is ascertainable by third parties is what is in the public domain, and what they would learn in the ordinary course of business with the company.

Before deciding on the location of the Bank's COMI Mr Justice Lewinson looked at other matters to determine whether or not the 2006 Regulation applied. Was the US receivership a 'foreign proceeding' as defined in the UNCITRAL model law? The court heard argument as to whether or not it was a collective proceeding, whether or not the receiver was appointed pursuant to a law relating to insolvency and whether or not he was appointed for the purpose of reorganisation or liquidation. On considering the terms of the order under which the receiver was appointed the court found that the US receivership was not a 'foreign proceeding'. The receiver had been appointed to prevent dissipation and waste of assets, not to liquidate or reorganise the estate. Nor was the appointment made on the basis of an allegation of insolvency. There was no one specific factor that brought the court to its conclusion, but rather it was reached on looking at the overall terms of the order making the appointment. The receivership did not fall with the definition of a 'foreign proceeding'.

Was the Antiguan liquidation a ‘foreign proceeding’? It was common ground that it was a collective proceeding and that the liquidators were appointed to liquidate assets. But were they appointed pursuant to a law relating to insolvency? The petition was founded on section 300 of the International Business Corporations Act which does not require insolvency as a ground. The court considered the evidence that was put before the court in Antigua when the winding up order was made and noted that the winding up order was not based on section 300 alone, but also on consideration of the evidence which included evidence of insolvency. Mr Justice Lewinson found that the Antiguan winding up was a ‘foreign proceeding’.

Nor could the US receiver rely on the common law to gain recognition. The common law was there to supplement the 2006 Regulation, not to trump it. In so far as the 2006 Regulation applied the US receiver would not be recognised under common law principles.

The Justice Lewison then also applied the test for COMI referred to above to the facts of this case. Looking at all relevant factors including the ascertainability of the head office function by third parties, the court found that COMI was in Antigua and that the liquidators were entitled to recognition under the 2006 Regulation as foreign representatives of a ‘foreign main proceeding’.

This was the first reported case under the 2006 Regulation, although not now the only case.

4 Syska (Elektrim SA) v Vivendi Universal SA and others [2009] EWCA Civ 677

The final case is Elektrim, where the court had to consider the interaction between Article 4(2) of the EC Regulation and Article 15.

In 2003 Vivendi had commenced arbitration proceedings in London against Elektrim under the terms of an agreement made between the parties. In August 2007, shortly before the hearing on liability Elektrim was declared bankrupt by the court in Poland on its own petition. The Polish administrator argued that the arbitration proceedings were annulled under Article 142 of Polish bankruptcy law, which states:

Any arbitration clause concluded by the bankrupt shall lose its legal effect as at the date the bankruptcy is declared and any pending arbitration proceedings shall be discontinued.

Yet in October 2007 the English arbitrators had found that they retained jurisdiction and had gone on to make an award of substantial damages against Elektrim.

Article 4 of the EC Regulation reads:

1 Save as otherwise provided in this Regulation, the law applicable to insolvency proceedings and their effects shall be that of the Member State within the territory of which such proceedings are opened ...

2 The law of the State of the opening of proceedings shall determine the conditions for the opening of those proceedings, their conduct and their closure ...

There is then a non-exhaustive list of matters which fall under Article 4(2) including

(e) the effects of insolvency proceedings on current contracts ...

(f) the effects of insolvency proceedings on proceedings brought by individual creditors, with the exception of lawsuits pending.

Article 15 provides for the exception from Article 4 of lawsuits pending, and provides that the effect of insolvency proceedings on a lawsuit pending shall be governed solely by the law of the member state in which that lawsuit is pending.

The question to be determined by the court was whether Polish bankruptcy law should apply to the arbitration agreement under Article 4(2), with the unusual effect that the arbitration agreement, as a current contract, would be brought to an end. On annulment of the arbitration agreement the arbitrators in London would have no jurisdiction to continue. Or if English law should apply under the exception in Article 15, in which case under English law the arbitration could proceed. It was accepted in the Court of Appeal that the arbitration proceedings were a lawsuit pending.

The Court of Appeal reviewed the EC Regulation, the recitals to it and the Virgos-Schmit report. They also considered the leading text on the Regulation and held that, unlike the finding in the lower court, there was no conflict between Articles 4(2) and 15. There was a distinction between execution and proceedings to establish liability. The law of the contracting state would continue to apply in relation to lawsuits pending, and that law would determine whether the proceedings could continue, or be stayed or modified. If the proceedings could continue that might lead to a claim which would allow the creditor to participate in the insolvency proceedings. When it came to enforce any judgment or award the law of the Member State where the insolvency proceedings had been opened would apply. Accordingly the Polish 'torpedo' would not be effective. English law prevailed in relation to the ongoing arbitration proceedings and the award of damages against Elektrim stood so as to establish liability. The award would then be dealt with as a claim in the Polish bankruptcy.

This was a most useful clarification from the Court of Appeal as to the interaction of two provisions of the EC Regulation that appeared to the High Court to be in conflict with each other.

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