UK restructuring and insolvency regimes are widely regarded as being well-established, flexible and creditor-friendly. Taken in conjunction with the recognition afforded to certain of these processes in the EU and elsewhere, the UK is a popular jurisdiction for implementing complex cross-border restructurings and insolvencies. UK restructuring and insolvency legislation is not derived from EU legislation and so there would be no immediate effect on domestic legislation governing formal insolvency or duties of directors of insolvent companies (including for example the Insolvency Act 1986, Bankruptcy (Scotland) Act 1985 and Company Directors Disqualification Act 1986). Therefore, it is the possible impact on recognition in the event that the UK votes to leave the EU that is likely to have the greatest legal impact in this area.

The most notable international recognition regimes currently in place that are of relevance to the current topic are:

- EC Council Regulation on Insolvency Proceedings (the EC Insolvency Regulation).
- UNCITRAL Model Law on Cross-Border Insolvency (the Model Law).
- Brussels Regulation on Enforcements of Judgments (the Judgments Regulation).

What will happen if the UK votes to leave the EU is not clear. The effect would depend on the terms of the UK’s relationship with the EU post-Brexit. In this update, we consider the potential legal implications of a Brexit in the context of cross-border restructuring and insolvency.

**Cross-border cooperation: effect on jurisdiction and recognition**

**EC Insolvency Regulation**

The EC Insolvency Regulation aims to facilitate effective operation of cross-border insolvency proceedings. While the EC Insolvency Regulation does not seek to harmonise insolvency law of the EU member states, it is intended to facilitate single or co-ordinated EU-wide insolvencies.

The EC Insolvency Regulation provides rules to determine

- Jurisdiction.
- Applicable law.
- Mandatory recognition in other EU member states of a debtor’s insolvency proceedings.

It applies in the UK to compulsory liquidations, creditors’ voluntary liquidations, administrations, voluntary arrangements under insolvency legislation, bankruptcies and sequestrations. It does not apply to members’ voluntary liquidations, receiverships or schemes of arrangement.

At present, the EC Insolvency Regulation is binding on all EU member states except Denmark, which has opted out. As the EC Insolvency Regulation has direct effect in the UK, a Brexit would mean that the EC Insolvency Regulation would no longer automatically apply in the UK. If the UK leaves the EU, unless alternative equivalent arrangements were negotiated, the UK would lose the benefits of the recognition afforded under the EC Insolvency Regulation and would have to rely on
the cross-border rules of the remaining member states applicable to countries not covered by the EC Insolvency Regulation.

On a Brexit, the UK could seek to reach agreement with the EU that UK insolvency proceedings would continue to have automatic recognition under the EC Insolvency Regulations. However, that would be a novel solution which could require the agreement of all remaining member states. It could also leave the UK exposed to future amendments to the regime and would severely limit its ability to influence such changes.

The Recast Regulation on Insolvency Proceedings (the Recast Regulation) is due to come into force on 26 June 2017 i.e. after the referendum but, in the event of a vote to leave, before any Brexit is likely to have occurred. The Recast Regulation focuses more on restructurings by bringing certain pre-insolvency ‘rescue’ procedures within its remit (albeit not UK schemes of arrangement), and aims to improve the efficiency of cross-border insolvencies, particularly where there is a group of companies operating across a number of EU jurisdictions. The comments made in respect of the EU Insolvency Regulation would also apply to the Recast Regulation.

UNCITRAL Model Law
The Model Law has been adopted in UK law by the Cross-Border Insolvency Regulations (CBIR) to recognise certain insolvency proceedings between signatory jurisdictions. The Model Law has only been adopted by 41 jurisdictions of which the only other EU Member State signatories are Greece, Poland, Romania and Slovenia. The Model Law does not therefore operate as anything close to a comprehensive alternative to the EU Insolvency Regulation when seeking recognition of a UK insolvency proceeding in the EU.

Therefore, unless alternative arrangements were negotiated, recognition in remaining member states that have not adopted the Model Law would be dependent upon the recognition laws of each Member State applicable to non-EU entities leading to a far more piecemeal approach. This would lead to increased costs and uncertainty in UK insolvencies with cross-border aspects.

Schemes of Arrangement
Schemes of arrangement do not fall within the EC Insolvency Regulation. Recent activity before the English courts demonstrates that schemes are an increasingly popular restructuring mechanism for European companies. The approach taken by the English courts has been to sanction a scheme of arrangement for a foreign company where a company has a ‘sufficient connection’ with England and Wales.

Before exercising its discretion to sanction a scheme for a foreign company, the court has been concerned with whether the scheme will be recognised by the foreign jurisdiction (where it might be challenged by creditors). Applicant companies usually argue that the English court order will be recognised under EU legislation, including the Judgments Regulation, and so will be effective. The Judgments Regulation will cease to have effect on a Brexit.

The Lugano Convention is materially similar to the Judgments Regulation and so may present a solution for recognition of UK court judgments abroad. The Lugano Convention currently applies to the EU, Switzerland, Norway and Iceland. On a Brexit, one option may be for the UK to sign up to the Lugano Convention which may minimise any impact on the choice of the UK courts to sanction a scheme.

If there is no mutual recognition, it may impact on the decision-making process in choosing the jurisdiction and form of restructuring process to be used in certain cases. It would also generally make enforcement of UK court judgments in the EU more complex and expensive.

Restructuring / insolvency: impact on employees
The potential impact of a Brexit on employment legislation as another matter of possible relevance in restructurings, for example, changes to the Transfer of Undertakings (Protection of Employment) Regulations 2006, could be of significance. Click here to view our Employment Brexit Analysis Bulletin.

Insolvency of banks and financial institutions
Financial institutions (insurance undertakings, credit institutions and certain investment undertakings) are excluded from the EC Insolvency Regulation. There are, instead, specific EU directives to recognise insolvency measures commenced in the member states of credit institutions and insurance undertakings which tie in with the home state regulator for the entity in question. These directives have been incorporated into UK law by statutory instruments.

These statutory instruments would remain in effect following a Brexit, although the UK Government might amend/repeal the provisions. However, the corresponding legislation under the relevant directives implemented by the remaining member states would not necessarily continue to afford recognition to UK proceedings that would otherwise have been recognised prior to a Brexit (although it is likely that mutual recognition would be negotiated as part of an overall financial sector.
deal on a Brexit). If the relevant legislation refers to EU membership as a criterion for recognition then, unless otherwise agreed as part of the exit negotiations, it will cease to cover UK institutions.

The EU Bank Recovery and Resolution Directive, which established a recovery framework for banks/investment companies in the EU, would also be affected. The UK Government extended the powers and responsibilities of the FCA, PRA and Bank of England, and introduced a bail-in option to stabilise firms in financial difficulties.

Again, this legislation would remain in effect following a Brexit, although the UK Government might amend/repeal the provisions if it was no longer required to comply with the EU Bank Recovery and Resolution Directive. The comment made above in relation to legislation implemented by other member states applies equally here.

Framework for relationship between UK and EU on a Brexit?

In discussing the options in the event of Brexit, the UK Government has produced a policy paper on four possible models which the UK could adopt: a Norwegian-style EEA Agreement, a Turkish-style customs union, the Swiss bilateral treaties model, or trading under World Trade Organisation (WTO) rules. We will be issuing a series of bulletins covering the various models.

At present, the UK Government has indicated that the Norwegian option is not the favoured model. If the UK did not reach a multilateral agreement with EU, it would be possible to negotiate bilateral agreements with member states for continued recognition. This ‘Swiss-model’ is likely to be very complex, and so may not be offered by the EU.

The Turkish and WTO-style models relate principally to trading, and so may not address cross-border complications relevant to restructuring and insolvency.

It is highly likely that the deal that the UK would negotiate following the Brexit would be UK-specific and not based on current models used by non-EU member countries.

Conclusion

Although a Brexit is likely to have minimal impact on domestic formal insolvency proceedings (subject to any potential future divergence on employment law), the uncertainty in terms of recognition of UK proceedings and judgments means a Brexit would have an impact on cross-border restructuring/insolvency, and may result in the UK being a less attractive forum for cross-border restructuring.

The effect on cross-border restructuring and insolvency will depend on the specific deal the UK negotiates with the EU (and interim measures while discussions are ongoing).