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CASE REVIEW SECTION

Re Van Gansewinkel Groep BV [2015] Bus LR 1046

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Introduction

The scheme of arrangement has been a part of English company law since the nineteenth century. Since then it has been a powerful tool for restructuring the debts of both solvent and insolvent companies, and for a range of other purposes, such as effecting takeovers and mergers. The deceptively straightforward language of what is now Part 26 of the Companies Act 2006 provides a simple way to cram down dissenting creditors if a majority in number representing 75% in value vote in favour.

In recent years, the English scheme's flexibility has made it increasingly common for the court to sanction schemes of arrangement in respect of foreign companies with no assets or establishment in the UK. In this latest decision of the English Companies Court, Snowden J recognised the extent to which the international role of English scheme of arrangement has changed over time, and laid down new guidance as to how issues of jurisdiction should be dealt with.

Background

Van Gansewinkel Groep ('VGG') provided waste management services across The Netherlands, Belgium and Luxembourg. The applications before the court concerned six separate but inter-conditional schemes in respect of the scheme companies, all of which were members of VGG. One of the companies was a management holding company, the contractual party to several key contracts and performed the head office function for the group. Another was the principal operating subsidiary of VGG and had approximately 1,500 employees and numerous operating contracts. A third operated as a real estate holding company. Three other companies were investment holding companies. All of the scheme companies had their centre of main interests (COMI) within the EU but outside the UK. None of them had an establishment, or any substantial assets, in England or Wales.

The scheme companies had, among them, drawn down in the region of EUR 800 million under various facilities agreements. In addition, one of the companies was party to four hedging agreements with an aggregate notional amount of EUR 600 million in order to hedge the floating interest rate liabilities under the existing facilities agreements. The obligations of the scheme companies under the existing senior facilities agreement and the hedging agreements were guaranteed by each of the other scheme companies (and one additional group company, Van Gansewinkel NV) and were secured by a comprehensive security package over the assets of the group.

In recent years, VGG's revenue had fallen markedly due to a decline in waste volumes and severe price competition. The revenue for the group declined from EUR 1·034 billion in 2012 to EUR 962 million in 2014. Moreover, the group had negative net cash flow for 2014 of EUR 38 million. In spite of cutting costs, the group was unable to continue to meet its financial covenants and the scheme companies were unable to repay or refinance in full their obligations under the existing facilities agreements and hedging agreements. The group secured the forbearance of a significant majority of the scheme creditors pursuant to the terms of waiver requests so as to enable the formulation of the schemes. The scheme creditors also agreed to waive certain breaches, including breaches of financial covenants, under the existing senior facilities agreement. In the absence of the relevant waivers and forbearance, scheme creditors would have been entitled to accelerate the sums owing under the existing senior facilities agreement and enforce the security granted by the group.

Schemes of arrangement

Section 895 of the Companies Act 2006 provides that a scheme of arrangement may be entered into 'where a compromise or arrangement is proposed between a company and its creditors, or any class of them, or its members, or any class of them'. The application is often made by the company itself, but may be made by a creditor or a member (provided that the company itself consents) or by an insolvency officeholder (if the company is in liquidation or administration).

The first court hearing is a convening hearing, where the court will, if it considers appropriate, order that meetings be convened to vote on the scheme (s.896). The court will ensure at this stage that, where appropriate, creditors with different interests have

been separated into different classes for the purpose of voting: *Re Hawk Insurance Co Ltd* [2002] BCC 300. The company then sends an explanatory statement on the effect of the proposed scheme (s.897). The creditors then vote at the meeting, and if a majority in number representing three quarters in value of the creditors (or each class of creditors) vote in favour, then the matter will proceed to a sanction hearing, where the court will consider whether to sanction the scheme (s.899).

In the past fifteen years, the English courts have seen increasingly ambitious attempts to restructure the financial obligations of overseas companies that do not have their COMI, or even an establishment or any assets in England. In *Drax* [2004] 1 WLR 1049, for example, Lawrence Collins J sanctioned schemes in respect of companies incorporated in Jersey and Cayman because their debts were primarily governed by English law. In *DAP Holding* [2006] BCC 48, Lewison J reached a similar decision in a case concerning a Dutch (ie EU-based) company, confirming that the EC Insolvency Regulation did not apply. In *Sovereign Marine & General Insurance Co* [2006] BCC 774, Warren J sanctioned schemes in respect of companies based in France, Ireland, New York and Bermuda, holding that it did not matter that the French and Irish companies were solvent and so could not have been wound up in England, and in *Rodenstock* [2011] Bus LR 1245, a scheme was sanctioned in respect of a company with its COMI in Germany, Briggs J holding that there was nothing in the Judgments Regulation to preclude the scheme. *Primacom* [2013] BCC 201 was another notable case, where a scheme was sanctioned in respect of a German company which had no creditors in England and Wales.

The latest expansion of the English scheme came in *APCOA* [2015] Bus LR 374, where Hildyard J sanctioned schemes in respect of German companies whose debts had initially been governed by German law and subject to jurisdiction clauses in favour of the German courts. However, the creditors had voted to change the governing law to English law and the jurisdiction to England pursuant to Article 3(2) of the Rome I Regulation, which the English court considered created the sufficient connection with England to justify sanctioning the scheme.

Such 'forum shopping' has not been universally popular, and there were fears that the recast Insolvency Regulation might include schemes of arrangement within its ambit, which would have restricted the English court's ability to sanction schemes in respect of companies whose COMI is based elsewhere in the EU. Fortunately, this did not happen, and the English court retains its broad jurisdiction to sanction schemes in respect of foreign companies. The European Commission has recommended that EU member states introduce a rescue procedure equivalent to a scheme of arrangement in national legal systems, but this recommendation has not been widely implemented, leaving the English scheme of arrangement as one of the most popular restructuring tools for companies throughout the EU.

The VGG schemes

In outline, the operative provisions of the schemes in this case provided for the execution of a number of restructuring documents by an attorney appointed under the schemes to act on behalf of the scheme creditors. The essential elements of the compromise and arrangement between the scheme companies and their scheme creditors were to be found in those restructuring documents. The schemes in respect of each of the six companies were inter-conditional. In other words, each of the schemes had to be sanctioned in order for any of them to become effective. In accordance with usual practice, the terms of the restructuring and the schemes and the anticipated benefits and inherent risks were fully explained in a detailed explanatory statement circulated to scheme creditors prior to the scheme meetings.

Evidence indicated that if the schemes were not approved, then the group would probably collapse into a series of formal insolvency proceedings in The Netherlands and Belgium, and that such a scenario would lead to a materially worse return to scheme creditors than the schemes and would be likely to lead to the loss of the jobs of the group's employees.

Explanatory statement

The judge noted that no detailed material had been provided either to the creditors or to the court in support of the contention that a scheme was more advantageous than the alternatives. Snowden J did not consider this to be an impediment to the schemes in the present case, because the explanatory statement had asserted that the schemes would be more advantageous, and this was verified by a witness statement in support of the application. However, the judge noted:

> 'for the future that companies that seek the consent of their creditors and the sanction of the court to a scheme of arrangement that is put forward as a more advantageous outcome for creditors than formal insolvency proceedings may be well advised to ensure that greater detail is provided, both in the explanatory statement and in the evidence before the court, as to the possible alternatives to the scheme and the basis for the predicted outcomes. The provision of such information is likely to be essential if there is a challenge to the scheme.'

International jurisdiction

Snowden J identified what he considered to be a far more serious problem with the scheme documentation, not in the explanatory statement but in the letter notifying creditors of the convening hearing. In accordance with the guidance laid down by Chadwick LJ in *Re Hawk Insurance Co Ltd*, the court will try to deal with as many issues as possible at the convening hearing rather than the sanction hearing, the idea being to avoid the cost of convening meetings and listing a sanction hearing in respect of a scheme which was doomed to fail from the outset because of some technical defect. In accordance with Chadwick LJ's guidance, the Practice Statement (Companies: Schemes of Arrangement) [2002] 1 WLR 1345 obliges the company to draw to the court's attention, at the convening hearing, 'any issues which may arise as to the constitution of meetings of creditors or which otherwise affect the conduct of those meetings'.

Nothing in the Practice Statement (and accordingly nothing in the notice letters) said anything about the court's jurisdiction in the international sense. The judge rejected the company's submission that jurisdiction had been conclusively determined at the convening hearing, and went on to consider it afresh.

Snowden J noted that under s.895(2)(b) of the Companies Act 2006, the court has jurisdiction to sanction a scheme in respect of 'a company liable to be wound up under the Insolvency Act 1986'. The judge accepted the orthodox view that it did not matter whether the court would actually wind up the relevant company, merely that the company was the type of entity that the English court theoretically could wind up, which included foreign companies. Accordingly, even though all of the scheme companies had their COMI elsewhere in the EU, and could not actually have been wound up in England, Snowden J nonetheless held that they were the sort of entity in respect of which an English scheme could be sanctioned.

The judge then considered whether either the EC Insolvency Regulation or the recast Judgments Regulation affected the analysis. The judge noted that schemes of arrangement were not listed as a collective insolvency proceeding in the Insolvency Regulation, which therefore did not apply, and that there was nothing in the domestic legislation which indicated an intention to limit schemes to companies with their COMI in England. Again, this is orthodox reasoning.

Snowden J had more difficulty with the controversy in respect of the recast Judgments Regulation, noting that there are two possibilities: either the jurisdictional requirements in Chapter II of the Judgments Regulation are wholly inapplicable to schemes of arrangement, or schemes of arrangement do fall within Chapter II of the Judgments Regulation so that the English court has to be satisfied that it can assume jurisdiction under one of the articles in that Chapter.

The first possibility had found favour with Lewison J in *DAP Holding* [2006] BCC 48 (who thought that schemes fell within the bankruptcy exception) and with Hildyard J in *Primacom* [2013] BCC 201 (who considered that the Judgments Regulation only applied where somebody was being 'sued' and nobody is 'sued' when a scheme is proposed and sanctioned). The latter possibility was accepted by Briggs J in *Rodenstock* [2011] Bus LR 1245 in respect of a solvent company and by David Richards J in *Magyar Telecom* [2014] BCC 448 in respect of an insolvent company.

Noting that the point was not clearly settled, Snowden J proceeded to consider whether, if the Judgments Regulation did apply, jurisdiction could be founded on some provision within it. Three possible bases were identified.

The first was based on the argument that scheme creditors cannot insist on being sued in their member state of domicile under article 4(1) of the recast Judgments Regulation because they have contractually submitted to the jurisdiction of the English court for the determination of disputes concerning their relationship with the company, and that this extends to a scheme of arrangement to compromise such rights. On the facts of VGG, this basis was rejected. Although the scheme companies had contractually submitted to the English jurisdiction, the relevant clause expressly did not bind the creditors.

The second was based on the argument that article 8(1) of the recast Judgments Regulation allows a person domiciled in a member state to be sued, where he is one of a number of defendants, in the courts for the place where any one of them is domiciled, provided the claims are so closely connected that it is expedient to hear and determine them together to avoid the risk of irreconcilable judgments resulting from separate proceedings. Accordingly, provided one scheme creditor is based in England, and subject to the 'expediency' requirement, it is possible to 'sue' all of the scheme creditors in England through the process of a scheme. Snowden J noted that in the present case, out of a total of 106 scheme creditors, 15 creditors with claims totalling about EUR 135 million were domiciled in England. Although this was only a minority of creditors, the judge considered that the numbers and size of the scheme creditors domiciled in England were far from immaterial, and were sufficiently large that the test of expediency was satisfied.

The judge therefore did not need to consider the third basis: namely the possibility that the English court could simply apply its scheme jurisdiction rules by analogy with the provisions of article 6 of the recast Judgments Regulation, and the judge therefore expressed no view on it.

Snowden J concluded his remarks on international jurisdiction by saying that the practice statement letter to creditors notifying them of the convening hearing should, in future, give 'proper details of the argument'

concerning international jurisdiction, and that at the convening hearing the applicant should very clearly bring jurisdictional issues to the attention of the judge, so that a reasoned judgment can be given on the matter.

Conclusion

Despite the English courts' expansive approach to jurisdiction where schemes of arrangement in respect of foreign companies are concerned, the court will not act as a rubber stamp, and will always make an independent judgment as to whether it is appropriate to exercise its jurisdiction.

The judge's criticisms of the way that VGG approached the application may have been a little harsh. VGG complied with the 2002 Practice Statement, which simply does not deal with international jurisdiction. The English courts see schemes in respect of foreign companies far more frequently now than they did in 2002, and it may well be time for a new Practice Statement. The most important guidance from the judgment is that, where a foreign company is concerned, the practice statement letter should clearly indicate the arguments to be made in respect of international jurisdiction, and that the issue of jurisdiction must be clearly brought to the attention of the judge at the convening hearing.

Finally, the controversy regarding the application of the recast Judgments Regulation to schemes remains unresolved. In particular, there continues to be doubt as to whether it applies at all; and, if it does apply, the requirements of article 8(1) of the recast Judgments Regulation remain to be identified. The wording of article 8(1) suggests that the test will be satisfied if only one scheme creditor has its domicile in the UK; but the judge in VGG appeared to consider that the expediency requirement could be satisfied only if a sufficient percentage of scheme creditors were domiciled in the UK. This is doubtful. There is nothing in article 8(1) to suggest any such percentage threshold and it would seem that the test of expediency will always be satisfied where the claims of scheme creditors are governed by English law. In such a case, England is the only place where the debts can be effectively restructured: see *Magyar Telecom BV* [2015] 1 BCLC 418 at [15] per David Richards J. It may be that the expediency test is less about the relative number of UK-domiciled scheme creditors and more about the requirements for an effective restructuring. This point remains to be decided and will no doubt be addressed in future cases.

Richard James Philpott & Mark Jeremy Orton (as Joint Liquidators of WGL Realisations 2010 Limited) v Lycee Francais Charles De Gaulle School [2015] EWHC 1065 (Ch)

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Introduction

In this case HHJ Purle QC had to decide the appropriate method of resolution for a dispute between WGL Realisations 2010 Ltd ('the Company') and Lycee Francais Charles De Gaulle School ('the School'). While the School had submitted a proof of debt in relation to its claim against the Company, the joint liquidators of the Company ('the Liquidators') had not admitted or rejected this proof and maintained that they were unable to do so until an account had taken place under Rule 4.90 of the Insolvency Rules 1986 ('the Rules').

Since the construction contract to which the dispute pertained contained an arbitration clause, HHJ Purle QC held that any application to court by the Liquidators for directions for the taking of account required under Rule 4.90 could be stayed by the School under section 9 of the Arbitration Act 1996. Accordingly, the appropriate course was for the underlying dispute to be determined by arbitration, following which the taking of the account would be a simple matter of setting off the now-quantified claims and cross-claims.

Background

The Company and the School entered into a construction contract on 1 July 2008 ('the Contract'). The Contract contained an arbitration clause and also provided for adjudication. The Company later became insolvent and entered administration and, subsequently, voluntary liquidation.

The Liquidators' position was that the net balance owed to the Company under the Contract was GBP 615,000. The School maintained that, in fact, it was owed a sum of just over GBP 270,000 and submitted a proof for this amount in the liquidation.

Where a company in liquidation and another party have mutual claims against each other, Rule 4.90 applies and, in broad terms, provides for an account to be taken of the amounts due from each party to the other. These amounts are then set-off leaving a net balance owing one way. Insolvency set-off is mandatory and self-executing as at the date of liquidation (*MS Fashions Ltd International SA (No. 2)* [1993] Ch 425). A consequence of insolvency set-off is that after the date of liquidation the claims and cross-claims no longer exist, save as a mechanism for calculating the net amount due; all that remains is a net balance owed by one party to the other (*Stein v Blake* [1996] AC 243). However, in order to take the account envisaged by Rule 4.90, it obviously remains necessary for the various claims and cross-claims to be quantified.

The School argued that the arbitration clause in the Contract remained effective and that the claims and cross-claims should therefore be determined by arbitration. Since the Liquidation was a voluntary liquidation, legal proceedings were not automatically stayed. This meant that arbitral proceedings could be brought by the School against the Company, although it would have been open to the Liquidators to apply to stay any such proceedings under section 112 of the Insolvency Act 1986. The Liquidators' position appears to have been that the account should be taken in accordance with directions sought by them from the Court.

The decision

HHJ Purle QC considered that the real issue before him turned on the application of section 9 of the Arbitration Act 1996, which provides:

1) A party to an arbitration agreement against whom legal proceedings are brought (whether by way of claim or counterclaim) in respect of a matter which under the agreement is to be referred to arbitration may (upon notice to the other parties to the proceedings) apply to the court in which the proceedings have been brought to stay the proceedings so far as they concern that matter.
2) An application may be made notwithstanding that the matter is to be referred to arbitration only after the exhaustion of other dispute resolution procedures.
3) An application may not be made by a person before taking the appropriate procedural step (if any) to acknowledge the legal proceedings against him or

after he has taken any step in those proceedings to answer the substantive claim.

4) On an application under this section the court shall grant a stay unless satisfied that the arbitration agreement is null and void, inoperative, or incapable of being performed.

5) If the court refuses to stay the legal proceedings, any provision that an award is a condition precedent to the bringing of legal proceedings in respect of any matter is of no effect in relation to those proceedings.

The Judge noted that under sub-section 9(4) the grant of a stay was mandatory, subject to limited exceptions, which he held did not apply in the present case. In his view, the arbitration clause did not become inoperative as a result of the voluntary liquidation of the Company or the set-off provisions at Rule 4.90.

The Judge therefore accepted the School's submission that whatever form of court proceedings the Liquidators might choose to determine the balance of the account between the parties would be stayed if the School chose to invoke section 9. In the Judge's view, any application by the Liquidators to seek directions from the Court for the taking of the account under the Insolvency Act 1986 would constitute legal proceedings for the purposes of section 9 of the Arbitration Act 1996, and so would fall to be stayed under that provision. In his view, the Arbitration Act 1996 'trumped' the procedure in the Rules for the taking of an account under the Court's directions.

The Judge considered that this was consistent with previous decisions and he emphasised the importance of giving effect to the mandatory provisions of the Arbitration Act 1996 and Parliament's decision to strengthen the impact of arbitration clauses.

The Judge did not consider that the submission of a proof by the School constituted 'any step in those proceedings to answer the substantive claim' within sub-section 9(3) of the Arbitration Act 1996 and so would not preclude the School obtaining a stay of other legal proceedings to allow arbitration to proceed. Nor would any appeal by the School against a rejection of its proof by the Liquidators preclude a stay under sub-section 9(3); the submission of a proof and any appeal would be steps taken to advance the School's own claim, not to answer the Company's claim. In any event, if the School were to make an appeal, there would be no reason why the hearing of the appeal could not be stayed pending the outcome of any arbitration.

Accordingly, if the School wished to make use of the contractual arbitration clause to determine the amounts owing between the parties, there was nothing the Liquidators could do to prevent this.

Comment

While the view of the Judge that the Arbitration Act 1996 'trumped' the procedure for the taking of the account under the Insolvency Rules at first sight seems at odds with the principle that all matters relating to a company in liquidation should be dealt with in the winding up, in this case any determination of the arbitral panel would simply have been an alternative mechanism for the taking of the account necessary under Rule 4.90.

Some questions do remain though. HHJ Purle QC was sceptical that the procedure for appealing a rejection of proof would be any more economical than arbitration. However, it is by no means clear that this scepticism would have been justification for lifting any stay in place under the Insolvency Act 1986 to allow an arbitration to proceed and so the application of this decision to companies being wound up by the Court might prove to be limited.

The Judge was also of the view that any appeal against a rejection of proof by the School would not have resulted in a stay being precluded under sub-section 9(3) of the Arbitration Act 1996 on the basis that in appealing the School would have been advancing their own case not answering the Liquidators' substantive claim. While this might have been true on the facts of this case, it is possible to conceive of situations where a liquidator's reasons for rejecting a proof do in fact consist of an assertion of the company's claim and an appeal against those reasons could then consist of answering the substantive claim. In such cases, sub-section 9(3) would be engaged and thus it would be possible for the liquidator to seek to have the claims and cross-claims dealt with using the procedures set out in the Rules.

Overall though, this decision reinforces the importance of contractual arbitration clauses and emphasises that an agreement by parties to a contract to arbitrate will not necessarily be displaced by the insolvency of one or other of them.

Comité d'entreprise de Nortel Networks SA and others v Rogeau and others C-649/13, ECLI:EU:C:2015:384

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Introduction

The European Court of Justice handed down an important preliminary ruling on 11 June 2015 regarding the EU Insolvency Regulation, deciding that both the courts seised of the main proceedings and of the secondary proceedings have concurrent jurisdiction to determine which assets fall within the scope of the secondary proceedings.

Jurisdiction under the EC Regulation

The EC Regulation No 1346/2000 of 29 May 2000 determines which courts of the European Union have jurisdiction with respect to insolvency proceedings. The Regulation provides that the courts of the member state where the debtor's centre of main interests are located shall open the 'main proceedings', but that the courts of another member state may open 'secondary proceedings' but only with respect to assets within that jurisdiction. Accordingly, the relevant provisions of the Regulation are as follows. Firstly, Article 3 provides:

> '1. The courts of the Member State within the territory of which the centre of a debtor's main interests is situated shall have jurisdiction to open insolvency proceedings. In the case of a company or legal person, the place of the registered office shall be presumed to be the centre of its main interests in the absence of proof to the contrary.
>
> 2. Where the centre of a debtor's main interests is situated within the territory of a Member State, the courts of another Member State shall have jurisdiction to open insolvency proceedings against that debtor only if he possesses an establishment within the territory of that other Member State. The effects of those proceedings shall be restricted to the assets of the debtor situated in the territory of the latter Member State.'

Article 25 provides for the recognition and enforceability of judgments:

> '1. Judgments handed down by a court whose judgment concerning the opening of proceedings is recognised ... and which concern the course and closure of insolvency proceedings, and compositions approved by that court shall also be recognised with no further formalities. Such judgments shall be enforced in accordance with Articles 31 to 51, with the exception of Article 34(2), of the ... Convention [of 27 September 1968] on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters...
>
> The first subparagraph shall also apply to judgments deriving directly from the insolvency proceedings and which are closely linked with them, even if they were handed down by another court.
>
> ...
>
> 2. The recognition and enforcement of judgments other than those referred to in paragraph 1 shall be governed by the Convention referred to in paragraph 1, provided that that Convention is applicable ...'

Finally, Article 27 provides with respect to the opening of proceedings:

> 'The opening of the proceedings referred to in Article 3(1) by a court of a Member State and which is recognised in another Member State (main proceedings) shall permit the opening in that other Member State, a court of which has jurisdiction pursuant to Article 3(2), of secondary insolvency proceedings ... Their effects shall be restricted to the assets of the debtor situated within the territory of that other Member State.'

Nortel Group

The Nortel Group was a leading provider of telecommunications network solutions. Nortel Networks Limited ('NNL'), a Canadian incorporated company, was the majority owner of one of the Group's French subsidiaries, Comité d'entreprise de Nortel Networks SA ('NNSA'). Almost all of the Group's intellectual property was registered in the name of NNL, which granted the subsidiaries (including NNSA) free licenses for the intellectual property. Those subsidiaries were

also to retain beneficial ownership of that intellectual property in proportion to their respective contributions to the research and development actitivites. A Master R&D Agreement organised this relationship between NNL and the subsidiaries.

Following the Group's serious financial difficulties in 2008, Nortel decided to open insolvency proceedings in Canada, the US and the EU. In the EU these were commenced in England by order of the High Court on 14 January 2009 with respect to all Group companies established in the EU, including NNSA. Following an application by the administrators and NNSA, the French Court (Tribunal de Commerce de Versailles) opened secondary proceedings in France.

Industrial action occurred in France which was brought to an end in July 2009 by a Memorandum of Agreement, which provided for severance payments part of which were deferred, to be paid once operations ceased and out of funds from the sale of NNSA's assets, but after payment of the costs during the main and secondary proceedings. In order to secure a better price for the Group's assets, the various administrators and liquidators throughout the world agreed to sell those assets on a global basis, by branch of activity. Under a settlement agreement, the subsidiaries would waive their industrial and intellectual rights covered by the Master R&D Agreement, but conversely the subsidiaries' beneficial interests of the intellectual property would be preserved.

French proceedings

The liquidator of NNSA, Mr Rogeau, informed the works council of NNSA that despite there having been c. €39m in the bank accounts of NNSA, he was unable to give effect to the Memorandum of Agreement because the cash flow forecast showed a deficit of nearly €6m, in particular due to several requests for payment from the English joint administrators with respect to the costs of the continuance of the Group's activities during the proceedings and from the sale of certain assets.

This was contested by the works council and former employees of NNSA, who brought an action before the French Court. Firstly, they sought a declaration that the secondary proceedings gave them an exclusive and direct right to the overall proceeds from the sale of the Group's assets that fell to NNSA. Secondly, they sought an order that the liquidator of NNSA make immediate disbursement of the amounts due under the Memorandum of Agreement, including of the deferred amounts. The liquidator summoned the joint administrators before the French Court, who requested that the French Court decline jurisdiction in favour of the English High Court. Alternatively, they requested that the French Court decline jurisdiction to rule on rights and assets which were not situated in France when the secondary proceedings were commenced.

The French Court, staying the proceedings, referred the following question to the European Court:

> 'Do the courts of the State in which secondary proceedings have been opened have exclusive jurisdiction, or concurrent jurisdiction with the courts of the State in which the main proceedings have been opened, to rule on the determination of the debtor's assets falling within the scope of the effects of the secondary proceedings in accordance with Articles 2(g), 3(2) and 27 of ... Regulation ... No 1346/2000 ... and, in the event that there is exclusive or concurrent jurisdiction, is the applicable law that of the main proceedings or of the secondary proceedings?"

Rules on jurisdiction

In considering the first part of this question, the European Court referred to the settled position in case law that Article 3(1) must be interpreted as conferring international jurisdiction to hear and determine related actions on the member state within the the territory of which the insolvency proceedings have opened. Although the Court had previously only recognised this jurisdiction under Article 3(1), the Court stated that Article 3(2) must be interpreted analogously. In light of the scheme and practical effect of the Regulation, Article 3(2) must be regarded as conferring jurisdiction to hear and determine related actions on the court seised of the secondary proceedings, in so far as those actions relate to the debtor's assets that are situated within that territory.

This was firstly, as observed by the Advocate General, because the first subparagraph of Article 25(1) imposes an obligation on member states to recognise and enforce judgments concerning insolvency proceedings handed down by both the court having jurisdiction of the main proceedings under Article 3(1) and the court having jurisdiction of the secondary proceedings under Article 3(2). The second subparagraph of Article 25(1) provides that the first subparagraph applies also to judgments ruling on related actions. As a result, the European Court commented that the Regulation 'appears to confer at least implicitly on those courts jurisdiction to deliver such judgments'.

The second reason was that one of the fundamental objectives of secondary proceedings consists of the protection of local interests, notwithstanding that those proceedings may also pursue other objectives (regarding which the European Court referred to their decision in *Burgo Group*, C-327/13, EU:C2014:2158).

In the present case a declaration was being sought from the French Court that certain assets fall within the secondary proceedings, and secondary proceedings

are designed specifically to protect those interests. The European Court commented that this protection, and therefore the practical effect of Article 27, would be 'appreciably weakened' if the related action could not be brought before the court having charge of the secondary proceedings.

Exclusive or concurrent jurisdiction

Accordingly, the European Court held that the courts of the member state in which secondary proceedings have been opened have the jurisdiction to rule on the determination of what assets fall within the scope of those proceedings. This raises the question of whether such courts have exclusive jurisdiction, or share that jurisdiction concurrently with the court seised of the main proceedings.

In answering this question, the European Court first commented that their case-law with respect to jurisdiction under Article 3(1) to rule on related actions 'is founded principally on the practical effect of that regulation' (for example, see *Seagon*, C-339/07, EU:C:2009:93). The same principle applies to the analogous jurisdiction of the courts possessing jurisdiction under Article 3(2). Consequently, to determine the issue of exclusive versus concurrent jurisdiction, the Court referred to the need to ensure the practical effect of those provisions.

The Court observed that an action for a declaration that certain assets fall within the scope of secondary proceedings has a direct effect on the interests administered in the main proceedings, given that the declaration would mean those assets would not fall within those proceedings. However, as the Advocate General suggested, the courts with charge of the main proceedings also have jurisdiction to rule on related actions and therefore determine the scope of the effects of later proceedings. Accordingly, the European Court decided that the court seised of the secondary proceedings could not have exclusive jurisdiction to rule on the determination of the assets falling within those proceedings, since this would deprive Article 3(1) of its practical effect. It was also noted that the provisions of the Regulation did not show it conferred jurisdiction to rule on a related action on the court first seised.

Referring, again, to the Advocate General's opinion, the European Court suggested that the potential problem of concurrent judgments should be avoided since Article 25(1) requires that any court considering a related action must recognise an earlier judgment delivered by the court seised of the main proceedings, or as the case may be, the court seised of the secondary proceedings.

Applicable law

The second part of the question referred by the French Court was which law is applicable to determine which assets fall within the scope of the secondary proceedings. As set out above, by Articles 3(2) and 27 the Regulation provides that secondary proceedings are restricted to the assets which on the date of opening of the insolvency proceedings are situated within that member state.

In addressing this issue, the European Court first noted that the preamble (recitals 6 and 23) states that the Regulation sets out a uniform rule on conflicts of laws, which replace national rules of private international law, and that such replacement is limited to the field of application set down by the Regulation. As a result, the Regulation does not preclude, in principle, application in a related action of the legislation of the member state relating its private international law, in so far as the Regulation does not contain a uniform rule governing the situation in issue.

However, in relation to whether assets must be regarded as being situated within a member state on the date of opening the insolvency proceedings, the European Court held that the Regulation does lay down uniform rules, thereby excluding to that extent any recourse to national law. Namely, Article 2(g), which determines the meaning of 'the Member State in which assets are situated'. Although the Court acknowledged the complexity of the legal situation before the French Court, it stated that the rule in Article 2(g) must enable the French Court to determine the location of the property, rights or claims concerned, and consequently the scope of the secondary proceedings.

Comment

The recognition by the European Court of concurrent jurisdiction entails the risk of concurrent and potentially irreconcilable judgments. This was potential problem identified by several interested parties in their submissions and was a risk which the Court itself acknowledged. The Court suggested that this risk should be avoided by the requirement under the Regulation that courts recognise an earlier decision of the courts of another member state. It is hoped, however, that this does not lead to a race in certain proceedings to obtain the first judgment.

Re Codere Finance (UK) Ltd [2015] EWHC 3778 (Ch)

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Introduction

The decision of Mr Justice Newey on 17 December 2015 marks an important further development in the ability of the High Court of England & Wales to sanction cross-border schemes of arrangements under Part 26 of the Companies Act 2006, even in circumstances that can be described as 'forum shopping'.

Background

Codere SA is the ultimate parent of a group of companies which carry on business by way of gaming activities in Latin America, Italy and Spain. Financing for the group had principally been provided under a senior facilities agreement and more importantly for present purposes, a series of notes issued by a Luxembourg incorporated subsidiary, Codere Finance (Luxembourg) SA ('Codere Luxembourg'). The notes were guaranteed by the parent company Codere SA and other group companies, and were governed by New York law but subject to an intercreditor agreement governed by English law.

The Codere group had outstanding debts of approximately EUR 1,460 million, of which the notes accounted for EUR 1,214 million. The group was not in a position to meet all its debts. Negotiations occurred to achieve a restructuring and the available options were considered including through mechanisms available in the jurisdictions where the group operated. However, it was concluded that these options would involve some form of insolvency proceedings, and this could put at risk the gaming licenses on which the group depended to operate its business.

As a result, the view was taken that the best course was to use the scheme jurisdiction available in England & Wales under the Companies Act 2006. To that end, an English incorporated company, Codere Finance (UK) Ltd ('Codere UK'), was acquired by Codere SA. Codere SA caused Codere UK to accede to the notes as co-issuer and the English company thereby assumed a primary, joint and several obligation with respect to all of Codere Luxembourg's obligations under the notes.

The scheme

The scheme was intended to implement a complex restructuring, both as to the obligations under the notes and the structure of the group. In summary, the notes would be cancelled in exchange for shares and other notes, EUR 400 million of new money would be injected, and there would be a hive down of Codere SA's assets to a new company incorporated in Spain, with the interposition of two Luxembourg entities between the parent and the new Spanish subsidiary.

The scheme was expected to result in the noteholders receiving recoveries of at least 47% of the liabilities. In contrast, absent the scheme it was expected that the recovery rate could drop to 0%. Given that the notes were governed by New York law, even if the High Court approved the scheme, implementation was conditional on Codere UK subsequently obtaining recognition of the scheme in the US by an order under Chapter 15 of the US Bankruptcy Code.

At a hearing in the High Court on 26 October 2015, Mr Justice Nugee decided that a meeting of creditors be convened (*Re Codere Finance (UK) Ltd* [2015] EWHC 3206 (Ch)). At a creditors' meeting held on 14 December 2015 the scheme received strong endorsement from noteholders, with creditors representing 98.78% of the total indebtedness voting in favour of the scheme. Of the remaining 1.22% of creditors, it was not that they voted against the scheme, rather that the company had not succeeded in identifying them.

Scheme approval

The scheme came back before the High Court on 17 December 2015 where Newey J had to consider whether to approve the scheme. As many readers will be aware, the approach that the court should take in deciding whether to sanction a scheme is found in the decision of in *Re National Bank Ltd* [1966] 1 WLR 819, which approved the following guidance from Buckley on the Companies Acts:

> 'In exercising its power of sanction the court will see, first, that the provisions of the statute have been complied with; secondly, that the class was fairly represented by those who attended the meeting and

> that the statutory majority are acting bona fide and are not coercing the minority in order to promote interest adverse to those of the class whom they purport to represent, and thirdly, that the arrangement is such as an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve.
>
> The court does not sit merely to see that the majority are acting bona fide and thereupon to register the decision at the meeting; but at the same time the court will be slow to differ from the meeting, unless either the class has not been properly consulted, or the meeting has not considered the matter with a view to the interests of the class which it is empowered to bind, or some blot is found in the scheme'.

Given the overwhelming approval of noteholders to the scheme, the real question for the Court was whether it should exercise its discretion to sanction the scheme, against a backdrop of concerns that had been raised by Nugee J at the convening hearing in October 2015. Nugee J had described the proposed scheme as being 'at first blush, to be quite an extreme form of forum shopping, in which the restructuring is brought in the UK purely by incorporating a company to take on very large liabilities'. He had explained in more detail the novel situation which the Court was faced with:

> '... this is a group of companies with a Spanish holding company and operating companies trading in Europe and Latin America with no apparent connection with the UK before the restructuring took place, apart from a fact which I regard as of not great significance in this context, which is that an intercreditor agreement was governed by English law. The notes which are sought to be restructured are obligations of a Luxembourg company. They are obligations governed by New York law, and it is clear from the evidence that the connection with the UK has been brought about deliberately by the acquisition of the scheme company as a UK company, the UK company then accepting liability as a co-obligor under the New York governed notes, and then the UK company seeking a restructuring, which will have the effect, it is suggested, of not only restructuring the UK company's liabilities, but also the Luxembourg company's liabilities and the guarantee liabilities of other companies within the group.'

At the sanction hearing Newey J considered these observations but for a number of reasons was not deterred from sanctioning the scheme. The scheme related to an English company with its centre of main interests in England. Applying the line of authorities culminating in *Re Van Gansewinkel Groep BV* [2015] EWHC 2151 (Ch), the Judge held that the Insolvency Regulation No 1346/2000 of 29 May 2000 and the recast Judgments Regulation No 1215/2012 of 12 December 2012 would not present an obstacle, including because 22% in value of the scheme creditors were domiciled in England. Further, expert evidence presented to the Court indicated that the scheme was likely to be effective in the other relevant jurisdictions, either directly or indirectly following recognition under Chapter 15 of the US Bankruptcy Code.

Although Codere UK had only recently been acquired by the group, the Judge considered that there were other connections to the jurisdiction. Firstly, the intercreditor agreement dating back to 2005 was governed by English law. Secondly, as set out above, a significant percentage of the noteholders were domiciled in England. Thirdly, it was noteworthy that some 97% by value of the noteholders had now submitted to the jurisdiction of the English court. Fourthly, the note trustee and security trustee had since the outset performed their functions from offices in London. Fifthly, other relevant documents including the lock-up agreements were also governed by English law.

Newey J commented that the recent authorities have shown that the High Court had become comfortable with approving schemes with respect to companies which did not have long standing connections to the jurisdiction, for example where the company has shifted its centre of main interest to England or where the governing law of the relevant agreement had been amended. In addition, particularly analogous to the present case was the line of authorities including in *Re A I Scheme Ltd* [2015] EWHC 1233 (Ch); [2015] EWHC 2038 (Ch) where the company voluntarily assumed liabilities with a view to exercising the English scheme jurisdiction.

Forum shopping

The Judge acknowledged that 'In a sense, of course, what was done in the A I Scheme case, and what is sought to be achieved in the present case, is forum shopping'. This was because such debtors are seeking to give the High Court jurisdiction in order to take advantage of the scheme jurisdiction which is available in England but not widely available, if at all, in other countries. On the one hand the Judge commented that forum shopping can be 'undesirable ... for example, where a debtor seeks to move his COMI with a view to taking advantage of a more favourable bankruptcy regime and so escaping his debts'. On the other hand, in other circumstances 'if ... it is appropriate to speak of forum shopping at all ... there can sometimes be good forum shopping'. Newey J stated that the present case fell within the latter category because the intention was not to evade debts, but to achieve the best possible outcome for creditors.

The Judge did not consider that the fact that Codere UK had only been recently been acquired with a view to invoking the English scheme jurisdiction should

cause him to decline to sanction the scheme. He held that it was very much in the interests of the creditors and arose in the context of the scheme being devised in close consultation with creditors, and having their overwhelming support. Further, there was a lack of alternatives and according to the evidence, if the Court declined to sanction the scheme, it could cause the group and its creditors to lose the value of around EUR 600 million. Accordingly, the Court sanctioned the scheme of arrangement.

Comment

The decision is a further development in the ability of English law to provide cross-border restructuring solutions through schemes of arrangements which are approved by the High Court and then recognised directly or indirectly by foreign jurisdictions. One particular benefit of schemes of arrangement under the Companies Act is that they are not usually considered to constitute formal insolvency proceedings, and as explained above this was especially useful to the Codere group given the gaming licenses on which its business depended.

Mr Justice Newey's comments appropriately distinguish between 'bad' and 'good' forum shopping. The various decisions of the English bankruptcy court where debtors resident in other countries have purported to move their centre of interests to England demonstrate the potential for forum shopping to be abusive. In contrast, the decision in *Re Codere Finance (UK) Ltd* provides a clear example of where forum shopping can prove to be positive, in particular where the choice of jurisdiction for the restructuring was undertaken in consultation with the creditors, had their overwhelming support and was unquestionably in their interests.

Re Stemcor Trade Finance Limited [2015] EWHC 2662 (Ch); [2015] EWHC 2803 (Ch)

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Introduction

In contrast to many restructuring plans approved by the English Companies Court recently, the scheme of arrangement in respect of Stemcor Trade Finance Limited (the 'Company') did not raise difficult issues of international jurisdiction. However, there was an interesting point of practice in relation to classes of creditor.

Background

The Company was part of a steel trading group with a number of lines of business in various jurisdictions across the world. The Company was an English company which acted as the group's treasury company, and was therefore the borrower under a Senior European Term Loan facility.

Stemcor group had already restructured its debts in the recent past. In 2014 there was a scheme involving the Company and a related company, but the Stemcor group was unable to generate sufficient cash to reduce its existing debt burden. The group had also experienced difficult trading conditions as a result of which it had entered into fresh re-structuring discussions with a co-ordinating committee of its senior lenders under the Senior European Term Loan facility.

The envisaged re-structuring involved a de-merger of the Stemcor group's core business from its non-core assets and Indian operations, and a re-structuring to reduce the indebtedness of the core group of companies. The directors of the parent company of the group and of the Company considered that, if the scheme could not be implemented, a number of group companies would enter insolvency proceedings. External analysts had suggested that, in those circumstances, the return to senior lenders would be likely to be less than would be achieved pursuant to the scheme.

Schemes of arrangement

A scheme of arrangement may be entered into 'where a compromise or arrangement is proposed between a company and its creditors, or any class of them, or its members, or any class of them' (Companies Act 2006 s.895). The first court hearing is a convening hearing, where the court will, if it considers appropriate, order that meetings be convened to vote on the scheme (s.896). The court will ensure at this stage that, where appropriate, creditors with different interests have been separated into different classes for the purpose of voting: *Re Hawk Insurance Co Ltd* [2002] BCC 300. The creditors then vote at the meeting, and if a majority in number representing three quarters in value of the creditors (or each class of creditors) vote in favour, then the matter will proceed to a sanction hearing, where the court will consider whether to sanction the scheme (s.899).

Determining which classes creditors should be placed into can be fraught with difficulty. On the one hand, creditors should not be placed in the same class if their interests are so dissimilar that they cannot consult together with a view to a common interest. On the other hand, those whose rights are sufficiently similar to the rights of others that they can properly consult together should be required to do so; lest by ordering separate meetings the court gives a veto to a minority group: see *Re Hawk Insurance Company Limited*, at [33] *per* Chadwick LJ.

The court will take a broad approach to considering class issues: see *Re Cattles plc* [2010] EWHC 3611 (Ch), at [7]. Accordingly, creditors can have rights which are different, but which are not so different that they cannot consult together. For example, in *Re Telewest Communications plc (No 1)* [2005] 1 BCLC 752 [37], David Richards J noted that difference between creditors could be 'material, certainly more than de minimis, without leading to separate classes'.

The Stemcor scheme

The wider restructuring involved the demerger of the core group of companies from the remainder of the Stemcor group by way of sale of the core group to a new company owned by an intermediate holding company ('Midco') which was in turn to be owned by a new holding company ('Topco'). The Scheme envisaged the exchange of the existing rights of the senior lenders

under the Senior European Term Loan facility for the following consideration. All senior lenders would receive a pro-rata share of a new senior secured debt instrument to be issued by Midco with a face value of USD 100 million, which was more than senior creditors would have received in a hypothetical liquidation of the group. Lenders who elected to participate in the new banking facilities which would be made available to the core group would also receive a share of the equity in the new Topco in proportion to their participations. The senior lenders would also receive a share of the debt issued by the parent company of the remaining group equal to the value of the outstanding liabilities under the Senior European Term Loan less the equity value of the core group and the amount of the new Midco Loan.

Although the restructuring was complex, the terms of the Scheme were relatively simple. They provided for the calculation of the entitlements of the lenders, for the assignment of the scheme claims of the lenders under the Senior European Term Loan to Midco in return for the consideration outlined above; and for the scheme creditors to authorise the execution of the other documents necessary to implement the wider restructuring.

International jurisdiction

At the convening hearing, Snowden J considered whether the English court had jurisdiction to approve the scheme. The judge noted that under s.895(2)(b) of the Companies Act 2006, the court has jurisdiction to sanction a scheme in respect of 'a company liable to be wound up under the Insolvency Act 1986'. Since the Company was incorporated in England and Wales, the present case threw up none of the difficulties that had troubled the court in *Re VGG* [2015] EWHC 2151 (Ch).

Having found in *VGG* that the Insolvency Regulation did not apply to schemes of arrangement, the judge considered the effect of the recast Judgments Regulation, article 4 of which provided that 'persons domiciled in a Member State shall, whatever their nationality, be sued in the courts of that Member State'. This was potentially problematic, because the majority of creditors were not domiciled in the United Kingdom. The judge, however, found two reasons why, if the Judgments Regulation did apply, it was no bar to the English court considering the scheme.

First, the judge noted that article 8(1) of the recast Judgments Regulation allows a person domiciled in a member state to be sued, where he is one of a number of defendants, in the courts for the place where any one of them is domiciled, provided the claims are so closely connected that it is expedient to hear and determine them together to avoid the risk of irreconcilable judgments resulting from separate proceedings. Accordingly, provided one scheme creditor is based in England, and subject to the 'expediency' requirement, it is possible to 'sue' all of the scheme creditors in England through the process of a scheme. Snowden J noted that in the present case, out of a total of 39 scheme creditors, 8 creditors with claims making up 19% of the total value of the scheme debt were domiciled in the United Kingdom. Although this was only a minority of creditors, the judge considered that the numbers and size of the scheme creditors domiciled in England were far from immaterial, and were sufficiently large that the test of expediency was satisfied.

Secondly, the judge noted that the Senior European Term Loan agreement contained an exclusive jurisdiction clause in favour of the English courts. Under article 25 of the recast Judgments Regulation, this contractual submission to the jurisdiction entitled the English court to consider the scheme.

Class issues

Before the convening hearing, the Company had envisaged that the scheme creditors would all be placed in the same class. However, at the convening hearing, counsel for the Company drew the court's attention to three potential issues concerning class composition.

First, there was a requirement for senior lenders who elected to participate in the new facilities to provide cash collateral if they did not have a specified minimum credit rating. The judge did not consider that that difference was a material difference in rights conferred under the Scheme which would require creditors to be divided into different classes. Instead, it was to be regarded as simply a facet of the nature of the person holding the right to participate, rather than a difference in the underlying right itself. In any event, the judge thought that the requirement was reflective of both the terms of the existing facilities and market practice.

Secondly, under the scheme a creditor which became entitled to at least 15% of the ordinary shares in Topco, which had acceded to the lock up agreement, and which had elected to be a participating lender, was entitled to become 'Anchor Shareholder'. The Anchor Shareholder would gain a number of rights and benefits not available to other lenders. Those rights included the ability to select and appoint the top executive management of the core group, to provide strategic advice and support to the management, and to seek an exit for participating lenders from their equity holdings in the core group within a specified period. The judge was somewhat troubled by this. However, in circumstances where the Anchor Shareholder (who could be identified at that stage) was expected to vote in favour of the scheme anyway, the Company agreed that it was appropriate to convene a separate meeting of the Anchor Shareholder and its affiliates, and a second meeting of the other creditors. Accordingly, Snowden J did not have to rule on whether it was strictly necessary to convene separate meetings.

Thirdly, a very significant number of the scheme creditors, in excess of 94 per cent by value and 33 out of 39 in number, had entered into lock-up agreements by which they had undertaken to vote in favour of the scheme. Lock-up agreements are increasingly popular with companies which want to know that they have sufficient creditor support before embarking on the expensive process of applying to court. There were, however, no consent-fees or other similar fees payable under the terms of those agreements, and accordingly, that situation did not, in the court's view, give rise to a class question.

Conclusion

After the requisite majorities of both classes of creditor voted in favour of the scheme, Morgan J sanctioned the scheme at a hearing only 13 days after the convening hearing, noting that apart from one point 'nothing novel has arisen in the course of the hearing which needs mention'. That one point concerned the opposition to the scheme by certain subordinated creditors who were not scheme creditors. Morgan J restated the orthodox position that scheme creditors are not bound by the scheme. Accordingly, whatever concerns the subordinated creditors might have about the practical impact of the scheme should be dealt with at another time.

The Stemcor scheme adds little to the body of law which has grown up around schemes of arrangement. The court once again considered it unnecessary to decide whether the Judgments Regulation applies to schemes of arrangement since, if it did, the court would clearly have jurisdiction pursuant to the exclusive jurisdiction clause in the finance documentation. It remains to be seen how the courts will deal with this question if it ever arises for determination.

Similarly, the court found it unnecessary to decide whether the Anchor Shareholder and its affiliates had to be separated into a separate class, because on the facts it made no difference, and the Company was content for separate meetings to be convened. This pragmatic approach may prove useful in future cases where there is potential disagreement as to correct class composition. In circumstances where creditors have entered into lock-up agreements, the company will often be content for certain creditors to be placed in a separate class for voting purposes if it is clear that the classes will still each have the requisite majorities voting in favour. If the requisite majorities at both meetings vote in favour of the scheme, then there is no difficulty. If, however, the Anchor Shareholder's support cannot be counted upon, and it ultimately votes against the scheme, it will still be open to the Company to argue at the sanction hearing that the Anchor Shareholder should not be placed in a separate class with an effective veto. Either way, the judge at the convening hearing avoids having to determine a difficult issue which might ultimately not matter.

Lockston Group Inc v Nicholas Stewart Wood [2015] EWHC 2962 (Ch)

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A dispute arose between the creditors of Boris Berezovksy over the appointment of trustees of his insolvent estate. The dispute hinged upon the date on which the creditors' foreign currency debts should be converted into sterling and the date up to which creditors could prove for interest. At the first creditors' meeting the chairman, Nicholas Wood, had used the date of Mr Berezovsky's death for both purposes. Lockston Group Inc ('Lockston') contended that the correct date was instead that on which the insolvency administration order ('the IAO') was made. The effect of the different date on the value of the various creditors' claims was such that had it been used at the creditors' meeting, different trustees would have been appointed.

The resolution of the dispute turned on the construction of the Insolvency Act 1986 ('the Act') as amended by the Administration of Insolvent Estates of Deceased Persons Order 1986 ('the Order'). Following careful consideration of the relevant provisions, Mr Justice David Richards held that, consistent with a cardinal principle of insolvency law that there should be a single date for ascertainment of liabilities, the correct date was the date of Mr Berezovksy's death.

Background

Mr Berezovsky died on 23 March 2013. Following his death, it became apparent that there was a deficit of around £40 million between the assets in Mr Berezovksy's estate and the sums owed to creditors. On 10 April 2014, Nicholas Wood and Kevin Hellard were appointed as General Administrators of Mr Berezovksy's estate. By a petition dated 22 October 2014 Mr Wood and Mr Hellard applied for the IAO and an order that they, together with a Mr Leeds, be appointed as trustees of the insolvent estate. On 26 January 2015, Mr Justice Morgan made the IAO.

The first meeting of creditors took place on 26 January 2015. At this meeting a vote was held to determine whether or not Mr Wood, Mr Hellard and Mr Leeds (together, 'the GT nominees') would be appointed as trustees or whether instead two partners in KPMG ('the KPMG nominees') would be. Mr Wood, as chairman of the meeting, valued the creditors' provable claims as at the date of Mr Berezovksy's death. This meant that foreign currency claims were converted to sterling at the exchange rate prevailing on 23 March 2013 and interest on debts was provable only up to this date. A resolution was passed by £128,986,545 to £116,364,421 appointing the GT nominees as trustees of the insolvent estate.

Administration of insolvent estates

The three ways of administering the insolvent estate of a deceased person were set out at paragraph 10 of the judgment:

1. If a bankruptcy petition has been presented, or a bankruptcy order has been made, before the date of death then proceedings continue as if the debtor were alive, subject to the order of the court. The Act is modified in accordance with Schedule 2 to the Order.
2. If death occurs before a bankruptcy petition has been presented, an IAO may be made. In this situation there are significant modifications made to the Act, as set out at Article 3 of the Order.
3. The estate may be administered otherwise than in bankruptcy, in which case Article 4 of the Order applies.

Since the IAO had been made, the provisions in Article 3 of the Order applied. These are as follows:

(1) The provisions of the Act specified in Parts II and III of Schedule 1 to this Order shall apply to the administration in bankruptcy of the insolvent estates of deceased persons dying before presentation of a bankruptcy petition with the modifications specified in those Parts and with any further such modifications as may be necessary to render them applicable to the estate of a deceased person and in particular with the modifications specified in Part I of that Schedule, and the provisions of the Rules, the Insolvency Regulations 2006 and any order made under section 415 of the Act (fees and deposits) shall apply accordingly.

(2) In the case of any conflict between any provision of the Rules and any provision of this Order, the latter provision shall prevail.

Part I of Schedule 1 to the Order provides for the substitution of various phrases in the Act. Of most significance in this case were two substitutions:

1. where 'the commencement of the bankruptcy' appears in the Act it is to be replaced with 'the date of the insolvency administration order'; and
2. where 'a bankruptcy order' appears in the Act it is to be replaced with 'an insolvency administration order'.

Part II of the Order makes a number of detailed amendments to Part X of the Act, which is the part of the Act that deals with bankruptcy. The effect of the amendments in Part II of the Order is that in certain provisions of the Act, for example section 283 which defines the bankrupt's estate, the date of the insolvency administration order is deemed to be the date on which the deceased died. Thus the amendments have the effect that whereas under the Act the phrase 'commencement of the bankruptcy' refers to a single date, under the Order this phrase can refer to one of two dates; that of the IAO or that of the death of the insolvent debtor.

Lockston's argument

Lockston argued that the amendments made to the Act by the Order meant that the date of the debtor's death was the time at which debts were identified (section 382 of the Act as modified by the Order) but that debts were quantified at a later date, being that date on which the IAO was actually made. This was consistent with the modified section 278 of the Act, which provided that the bankruptcy of the deceased commenced on the date on which the IAO was made. In particular:

1. Section 322(2) provides that interest was provable insofar as it was payable up to the 'commencement of the bankruptcy' which, as modified by the Order, meant payable up to the date on which the IAO was made; and
2. Rule 6.111 of the Insolvency Rules 1986 ('the Rules') stipulates that for purposes of proving, debts denominated in foreign currency shall be converted to sterling as at the date of the bankruptcy order. Interpreting the Rules consistently with the Order, as required by Article 3(1) meant that conversion should take place as at the date of the IAO.

That the debts of the deceased were identified as at the date of death was an exceptional feature that distinguished proceedings under the Order from other insolvency processes but was necessary in order to exclude debts arising after the debtor had died.

Judgment

Mr Justice David Richards rejected Lockston's argument. He began by reviewing the provisions at Part X of the Act as they would apply to a living debtor, concluding:

> 'These provisions, and the common law rules on which they are based, produce a coherent and consistent structure for the rateable payment of bankruptcy debts. As has frequently been observed, the distribution of an insolvent estate among the general body of creditors on a pari passu basis is, as it always has been, a fundamental feature of our insolvency law. It applies to distributions across all the various forms of insolvency proceedings: the bankruptcy of individuals and the administration and liquidation of companies.'

As a matter of fact and of authority, a pari passu distribution required a common date and a common currency for the identification and quantification of debts. If the Order were intended to introduce separate dates for identification and quantification, 'express provision in clear terms' would need to be made; there was no such provision in the Order. Further, the scheme introduced by the Order was consistent with the usual approach. Addressing the specific submissions made by Lockston, Mr Justice David Richards held:

1. The modification to section 382 of the Act made by the Order defined a bankruptcy debt as, 'any debt or liability to which [the bankrupt] is subject at the date of death of the deceased debtor'. This provision applied as much to the amount of the debt as to its existence; if the debtor were subject to an accrued but unquantified debt, such as a contingent debt, it would be quantified as at the date of death of the deceased debtor. Further, statutory interest was payable under section 328 of the Act, as modified, from the date of the debtor's death. It would be 'contrary to the whole basis of statutory interest for it to be payable for periods before the date at which the underlying debt was quantified for the purposes of proof.' Consequently, the quantification of debts and liabilities was to be carried out at the date of death.
2. The modification to section 322(2) of the Act made by Part I of Schedule 1 to the Order, ie that 'commencement of the bankruptcy' should be replaced with 'the date of the insolvency administration order' was subject to the proviso 'except as the context otherwise requires'. This meant that in the case of section 322(2) the context required that interest was provable up to the date of the debtor's death, because 'It clearly cannot have been intended that a creditor could prove for interest for the period down to the date of the IAO and be paid statutory interest for the period between the date of death and the date of the IAO.'

3. Although Part I of the Order did not modify the Rules, by Article 3(1), the Rules were to be read in conformity with the Order. This led to the 'inescapable' conclusion that Rule 6.111 should be modified in the same way as section 382 such that conversion of the foreign currency debts took place at the date of death of the deceased debtor.

Accordingly, the correct date for the conversion of foreign currency debts into sterling was the date of Mr Berezovsky's death and interest on debts was provable up to this date. It followed that the resolution to appoint the GT nominees was validly passed.

In the matter of Indah Kiat International Finance Company B.V. [2016] EWHC 246 (Ch)

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Introduction

It is now common for distressed foreign companies to come to the UK for restructuring purposes and seek the assistance of the English Courts. This is particularly so through the use of the schemes of arrangement jurisdiction under Pt 26 of the Companies Act 2006. Case comments in this journal have dealt with a variety of issues faced by foreign companies that seek the assistance of the English Courts and illustrate the fact that the English Courts have been very generous to foreign companies that have sought their assistance: see for example the decision in *APCOA Parking (UK) Ltd & Ors* [2014] EWHC 997 (Ch).

A warning has however recently been sent out by Snowden J in *Indah Kiat International Finance Company B.V.* [2016] EWHC 246 (Ch) making it clear that the process of obtaining the English Court's approval for a scheme of arrangement should not be viewed as one of a rubber stamp. This case comment focuses on the key aspects of Snowden J's decision and the importance of the *Practice Statement: Schemes of Arrangements with Creditors* [2002] 1 W.L.R. 1345; [2002] B.C.C. 355. The judgment relates to the application by *Indah Kiat International Finance Company B.V.* ('Indah Kiat' and the 'Scheme Company') for an order convening a single meeting of its scheme creditors (the 'Scheme Creditors') to consider and, if thought fit, approve a scheme of arrangement (the 'Scheme').

Factual background

The Scheme Company is a special purpose vehicle incorporated in the Netherlands. The Scheme Company issued two series of notes which form the debts proposed to be compromised by the Scheme (the 'Notes'). The Notes are guaranteed by PT Indah Kiat Pulp & Paper Tbk (the 'Parent') which is the sole shareholder of the Scheme Company and which was the recipient of an immediate loan from the Scheme Company of all of the monies subscribed for the Notes. The Parent is a substantial enterprise incorporated in Indonesia and is a member of the Asia Pulp and Paper group which operates a global pulp and paper business.

The Indentures, the Notes and the obligations of the Parent in relation to them are all governed by New York law and the parties submitted to the non-exclusive jurisdiction of the New York courts in relation to such obligations. The only alleged connection of the Scheme Company with England is said to have been that its COMI was shifted to England from the Netherlands about three months prior to the scheme convening hearing for the purpose of the Scheme.

After the Notes fell due, judgments were entered into in the US in favour of the trustee of the Notes (the 'US Judgments'). In response to attempts to enforce the defaulted Notes in Indonesia the Scheme Company and Parent engaged in protracted litigation which resulted in a judgment that purported to invalidate the Notes and the obligations of both the Scheme Company and the Parent (the 'Indonesian Judgment').

Since entry into the Indonesian Judgment in 2011 the Parent was not troubled further in relation to attempts to enforce the Notes in Indonesia. The position changed however when APP Investment Opportunity LLC ('APPIO') took an assignment from the Note trustee of a portion of the rights under the US Judgments corresponding to Notes of which APPIO was the beneficial owner. Since taking its assignment APPIO sought to take steps towards enforcement in the US which appears to have prompted the Parent and the Scheme Company into action.

The Scheme is intended to release and discharge the Scheme Company and the Parent from all of their liabilities pursuant to the Notes and the US Judgments in return for the issue by the Parent to Scheme Creditors, of new notes (or equivalent loan participations), together with a cash payment by the Parent.

The Scheme Company's Part 8 application for an order convening a single meeting of the Scheme Creditors was strenuously contested by APPIO on the grounds that the Court does not have jurisdiction to entertain or sanction the Scheme. At the first hearing of the convening hearing APPIO sought an adjournment before Snowden J on the grounds that inadequate notice had been given to the Scheme Creditors and that there were other issues concerning the adequacy of the evidence and disclosure by the Scheme Company.

The Scheme Company had provided a notice regarding COMI (the 'COMI Notice') and a letter pursuant to the *Practice Statement: Schemes of Arrangements with Creditors* [2002] 1 W.L.R. 1345; [2002] B.C.C. 355 (the 'Practice Statement' and the 'Practice Statement letter') via an information agent to the relevant clearing systems through which the Notes were issued. The COMI Notice informed all account holders holding Notes that the Scheme Company had moved its COMI to England for the purpose of a scheme. The Practice Statement letter set out an account of the background to the Scheme and a summary of its terms, and gave notice that the hearing of the Scheme Company's application to convene a single meeting of Scheme Creditors would be heard on 21 January 2016. The evidence in support of the application was made by the sole director of the Scheme Company that was very recently appointed to replace the previous incumbents.

Decision

Snowden J accepted APPIO's submissions that an adjournment should be granted on the ground that inadequate notice had been given, and in providing his decision set out useful guidance in relation to the Practice Statement. In particular, at [28] his Lordship stated that '[t]he primary purpose of following the Practice Statement is to enable scheme creditors to have an effective opportunity to appear at the convening hearing at which the constitution of classes is determined.' In determining whether notice was adequate it was made clear that this will depend on the circumstances but factors to note would be whether the scheme was complex, novel and the amount of consultation that had taken place prior to the launch of the scheme. When there is great urgency in the scheme, for example when the company is in real financial distress, his Lordship indicated that the scheme company may well be able to persuade the Court that there is good reason to shorten the period of notice or depart from the Practice Statement. In the present case Snowden J found that there was not such justification for an urgent hearing.

In addition to an adjournment based on inadequate notice Snowden J also found that he would not have made an order convening a single meeting of Scheme Creditors or given the direction sought for in the draft Explanatory Statement on the basis that the evidence adduced by the Scheme Company as to the appropriate composition of the scheme meeting(s) and the draft Explanatory Statement were materially deficient.

In this regard his Lordship stated that the evidence provided by the sole director of the Scheme Company did not comply with CPR 32 PD 18.2 which requires that a witness statement must indicate the source of any matters of information and belief. In particular, it was held that the references to unidentified 'colleagues' and 'relevant people' as a source of information for the director of events prior to his appointment was too vague for the requirements of the CPR.

While reaching his conclusion Snowden J made it clear that, although the convening hearing was not the occasion upon which the court considers the merits or demerits of a scheme (see [39]), if the Court detects or its attention is drawn to manifest deficiencies in the draft explanatory statement, it is entitled to decline to convene the scheme meeting unless and until they are corrected (see [42]). It was made clear that at the convening hearing, the applicant company has the burden of adducing evidence of sufficient quality and credibility to persuade the court to act and that the company proposing a scheme has a duty to make full and frank disclosure to the court of all material facts and matters which may be relevant to any decision whether or not there is any opposition (see [40]).

As mentioned above, although noting the limited role of the court at the convening hearing, Snowden J indicated that in certain circumstances an opposing creditor might succeed in demonstrating at a convening hearing that the scheme company's evidence in relation to connection and recognition is manifestly deficient that it fails to show that there is a realistic prospect of the court ultimately sanction the scheme (see [89]). His Lordship did however reiterate the fact that if there are significant disputes of fact or expert evidence of foreign law then the convening hearing is unlikely to be appropriate to hear such disputes (see [89]).

Conclusion

The decision of Snowden J helpfully sets out the requirements that a scheme company must meet when making an application for the convening of a scheme meeting. The case itself provides a good working example of what the English Courts are likely to find as falling below the basic requirements. The case can also be seen as a signal by the Courts that, despite their broad view of the scheme jurisdiction, they will not be used as a rubber stamp and that those coming for Court approval must do so with the 'utmost candour' (see [40]).

Tchenguiz & Ors v Grant Thornton UK LLP & Ors [2015] EWHC 1864 (Comm)

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Abstract

In *Tchenguiz & Ors v Grant Thornton UK LLP & Ors* [2015] EWHC 1864 (Comm), Carr J considered the construction and effect of the Credit Institutions (Reorganisation and Winding-Up) Regulations 2004 (the 'Credit Institutions Regulations'), which implement Directive 2001/24/EC on the Reorganisation and Winding-Up of Credit Institutions (the 'Credit Institutions Directive'). Carr J held, *inter alia*, that the prosecution of a tort claim against an insolvent Icelandic bank was prohibited by Regulation 5 of the Credit Institutions Regulations.

Background

Kaupthing Bank hf ('Kaupthing') is an Icelandic bank, which fell into severe difficulties during the 2008 financial crisis. Following a series of interim protective measures, the District Court of Reykjavik made a winding-up order against Kaupthing in November 2010 (the 'Winding-Up Order'), pursuant to the Icelandic Financial Undertakings Act 2003 ('the FUA'). In January 2012, Kaupthing's affairs were brought under the control of a winding-up committee (the 'Winding-Up Committee'). Jóhannes Jóhannsson ('JJ') is a leading member of the Winding-Up Committee.

In November 2014, Vincent Tchenguiz and others (the 'Claimants') brought a claim in the Commercial Court (the 'VT Action') against five defendants: Grant Thornton UK LLP ('GT'), two partners of GT, Kaupthing and JJ. The Claimants sought damages for conspiracy, malicious prosecution and other forms of tortious misconduct. The claim form was served out of the jurisdiction on Kaupthing and JJ, both of whom were domiciled in Iceland. The Claimants contended that the claims against Kaupthing and JJ fell within the Convention on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters (the 'Lugano Convention'), so that permission to serve out of the jurisdiction was not required: see CPR 6.33(1)(b).

In January 2015, Kaupthing and JJ applied under CPR Part 11 for the VT Action to be stayed or dismissed (the 'Application'). The GT defendants did not participate in the Application, and accepted that the claims against them would continue notwithstanding the outcome of the Application.

Kaupthing argued that the VT Action should be stayed or dismissed on two independent grounds. First, Kaupthing argued that the VT Action was barred by the statutory stay under Icelandic insolvency law, which was to be recognised in England pursuant to Regulation 5(1) of the Credit Institutions Regulations (the 'Insolvency Ground'). Second, Kaupthing argued that the VT Action did not fall within the Lugano Convention, so that there was no basis for serving the claim form out of the jurisdiction without permission under CPR 6.33(1)(b) (the 'Jurisdiction Ground'). JJ also relied on the Jurisdiction Ground. However, since JJ was not a credit institution, he could not rely on the Insolvency Ground.

The Application was heard by Carr J in June 2015. Her judgment is reported at [2015] EWHC 1864 (Comm). Carr J held that the Insolvency Ground was successful (so that the VT Action could not be continued against Kaupthing), but that the Jurisdiction Ground was unsuccessful (so that the VT Action could be continued against JJ). Her reasoning is explained below.

The insolvency ground

The primary European instrument dealing with cross-border insolvency is Council Regulation No. 1346/2000 on insolvency proceedings ('the Insolvency Regulation'). However, by Article 1(2), the Insolvency Regulation expressly does not apply to insolvency proceedings in respect of certain financial institutions, including credit institutions.

The gap relating to insolvent credit institutions was filled by the Credit Institutions Directive, which applies in both the EU and the EEA (of which Iceland is a member). The Credit Institutions Directive is based on the concept of universalism. Thus, the 'home Member State' of a credit institution (in the present case, Iceland) has exclusive jurisdiction to implement reorganisation measures or to open insolvency proceedings

in respect of that credit institution; any such reorganisation measures or insolvency proceedings in the home Member State must automatically be recognised and given effect across the EEA; and 'secondary proceedings' in other Member States are prohibited. The latter point represents a departure from the normal rule under the Insolvency Regulation, which permits secondary proceedings in Member States where the relevant company has an establishment. By Article 10 of the Credit Institutions Directive, the effect of winding-up proceedings on a post-insolvency action brought by an individual creditor must be determined by the law of the home Member State.

The Credit Institutions Directive is implemented in England by the Credit Institutions Regulations. For present purposes, the critical provision is Regulation 5(1), which provides as follows:

> 'An EEA insolvency measure has effect in the United Kingdom in relation to –
>
> (a) any branch of an EEA credit institution,
>
> (b) any property or other assets of that credit institution,
>
> (c) any debt or liability of that credit institution
>
> as if it were part of the general law of insolvency of the United Kingdom.'

It was common ground that the Winding-Up Order against Kaupthing in Iceland was an 'EEA insolvency measure' within Regulation 5(1). Kaupthing argued that the VT Action was barred by Icelandic law, which was to be recognised and applied in England pursuant to Regulation 5(1). The Icelandic law on which Kaupthing relied was Article 116 of the FUA, which provides as follows:

> 'Legal action shall not be brought against a bankruptcy estate in the district court unless expressly permitted by law, except for criminal litigation in which a request is made for criminal sanctions applicable to bankruptcy estates. In such event, the action may be brought in the district where the bankruptcy proceedings take place.'

Carr J accepted Kaupthing's argument, and held that the VT Action could not be prosecuted against Kaupthing. Based on expert evidence of Icelandic law, she held that the purpose of Article 116 is to uphold the equal treatment of claimants and the *pari passu* principle. Under Article 116, all claims must be determined and controlled by a single insolvency process, and no creditor is allowed to take judicial proceedings outside that process. Any claims against Kaupthing must be submitted to the Winding-Up Committee under the normal Icelandic proof of debt process, rather than being adjudicated in England by way of a claim under CPR Part 7.

Carr J held, in the face of conflicting expert evidence, that Article 116 of the FUA has extra-territorial effect as a matter of Icelandic law. She held that, although Article 116 refers to 'the district court', its underlying purpose is to prevent civil proceedings from being commenced anywhere against a 'bankruptcy estate' (except by the normal proof of debt process under Icelandic law).

More importantly, however, Carr J held that it is *irrelevant* whether Article 116 has extra-territorial effect as a matter of Icelandic law. The effect of Regulation 5(1) is to treat Article 116, and other applicable provisions of Icelandic insolvency law, as if they applied extra-territorially in England. If Regulation 5 were not to be treated as giving effect to Article 116 in the UK, the fundamental purpose and effect of the Credit Institutions Directive and the Credit Institutions Regulations – namely, to give local insolvency laws of the home Member State extra-territorial effect and to provide a unified and universal regime – would be undermined. Proceedings against Kaupthing could be brought without any limitation or protection at all, resulting in a 'free-for-all' which the Credit Institutions Directive was expressly designed to prevent. (In this regard, Carr J rejected any suggestion that the Credit Institutions Regulations had failed properly to implement the Credit Institutions Directive.) Carr J noted that the existing authorities – such as *Lornamead Acquisitions Ltd v Kaupthing Bank hf* [2013] 1 BCLC 73, *Isis Investments Ltd v Oscatello Investments Ltd* [2013] EWHC 7 (Ch) and [2013] EWCA Civ 1493, *LBI hf v Kepler Capital Markets SA* [2013] EUECJ C-85/12 and *LBI hf v Stanford* [2014] EWHC 3921 (Ch) – supported Kaupthing's argument. Carr J also rejected VT's argument that the Credit Institutions Directive does not apply to actions falling within the Lugano Convention.

It is suggested Carr J's reasoning is correct. As she observed, the statutory stay under section 130(2) of the Insolvency Act 1986 provides a useful analogy. That section prevents creditors from bringing proceedings in England against companies in liquidation, but does not purport to prevent foreign courts from entertaining actions against such companies. Nevertheless, it is clear that the Credit Institutions Directive is intended to extend the statutory stay under section 130(2), such that it must be given effect across the EEA for English credit institutions in liquidation. Any other conclusion would mean that English credit institutions in liquidation would be unprotected by a stay anywhere else in the EEA, undermining an orderly and unified winding-up process. As Carr J noted, much the same analysis applies to Article 116 of the FUA.

The importance of Carr J's analysis for future cases is clear. Where an insolvent EEA credit institution has the benefit of a wide-ranging statutory stay under local law, the stay will be given effect in England under Regulation 5(1) of the Credit Institutions Regulations – regardless of whether the stay has extraterritorial

effect under local law. There is no material difference between the Credit Institutions Directive and the Insolvency Regulation on this point. Accordingly, the same analysis should apply under the Insolvency Regulation.

It should be noted that Carr J's analysis is arguably inconsistent with the analysis of Lawrence Collins J in *Mazur Media v Mazur Media GmbH* [2004] 1 WLR 2966, which is one of the earliest judgments on the Insolvency Regulation. In that case, Lawrence Collins J held that section 130 of the Insolvency Act 1986 could not be treated as having an extended extra-territorial effect in the context of the Insolvency Regulation. The decision in *Mazur Media* is widely considered to be incorrect by practitioners in the field of cross-border insolvency law. Nevertheless, it is perhaps regrettable that Carr J did not cite *Mazur Media* in her judgment.

The Jurisdiction ground

Although Carr J accepted Kaupthing's submissions on the Insolvency Ground, she rejected Kaupthing's submissions (adopted by JJ) on the Jurisdiction Ground. As noted above, the Claimants contended that the claims against Kaupthing and JJ fell within the Lugano Convention, so that permission to serve out of the jurisdiction was not required: see CPR 6.33(1)(b). Kaupthing argued that the VT Action did not fall within the Lugano Convention, so that there was no basis for serving the claim form out of the jurisdiction without permission.

Kaupthing relied on Article 1(2)(b) of the Lugano Convention, which is materially identical to Article 1(2)(b) of Regulation No. 1215/2012 on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters (the 'Brussels Regulation Recast').

Article 1 of the Lugano Convention provides as follows:

> '1. This Convention shall apply in civil and commercial matters whatever the nature of the court or tribunal. It shall not extend, in particular, to revenue, customs or administrative matters.
>
> 2. The Convention shall not apply to…
>
> (b) bankruptcy, proceedings relating to the winding-up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings … '

The scope of Article 1(2)(b) is narrow and specifically defined. For proceedings to fall within the exception in Article 1(2)(b), they must derive directly from the bankruptcy or winding-up and be closely connected with the insolvency proceedings: per Lord Collins in *Rubin & Anor v Eurofinance SA & Ors* [2013] 1 AC 236 at [100] and [101].

The application of this test has been considered in a number of recent cases before the CJEU. For example, in *German Graphics Graphische Maschinen GmbH v Alice van der Schee* [2008] EUECJ C-292/08, the German claimant company contracted to sell certain machines to the Dutch defendant company. The contract contained a reservation of title clause. After the contract was made (but before the purchase price had been paid), a Dutch court placed the purchaser into compulsory liquidation. The vendor brought an action in Germany to recover the machines. The Dutch liquidator contended that the German action fell outside the Regulation on Civil Jurisdiction and Judgments. However, the CJEU held that the exception in Article 1(2)(b) did not apply, because there was an insufficiently close link between the German action and the Dutch insolvency proceedings. The only issue before the German court related to the ownership of the machines. This issue can arise outside the context of insolvency, and does not depend on insolvency law (properly so-called). The mere fact that the Dutch liquidator was a party to the proceedings was insufficient. The ECJ held that the scope of the Insolvency Regulation should be construed narrowly, whereas the scope of the Regulation on Civil Jurisdiction and Judgments (and, in particular, the term 'civil and commercial matters') should be construed in a broad manner.

In the present case, Carr J rejected Kaupthing's argument, and held that the VT Action did not fall within the Article 1(2)(b) exception. It could not be said that the pleaded claims against Kaupthing and JJ derived directly from the proceedings relating to the winding-up of Kaupthing. The winding-up of Kaupthing was not the principal subject-matter of VT Action. The gravamen and root of those claims was an alleged tortious conspiracy between three individuals – two partners of FT, and JJ at Kaupthing – involving deliberate and malicious wrongdoing in connection with an investigation by the SFO. The winding-up of Kaupthing is was the *context*: but the claims did not derive directly from it. The Claimants placed no reliance on any insolvency aspect of the winding-up proceedings, nor are breaches of any duties or powers by JJ in his capacity as a member of the Winding-Up Committee relied upon. No reliance is placed on JJ's status under Icelandic insolvency law nor is any liability under the Bankruptcy Act suggested.

Lehman Brothers International (Europe) (in Administration): Parts A and B of the Waterfall II Application

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Introduction

On 31 July 2015, David Richards J (as he then was) handed down two judgments in respect of two trials that took place before him earlier in the year, each relating to one of the three parts of the Waterfall II application (Parts A and B) (the 'Part A Judgment'; the 'Part B Judgment'; together the 'Judgments'). The majority of the decisions set out in the Judgments are now in the process of being appealed to the Court of Appeal, with those appeals set to be heard in the early part of 2017.

The Waterfall II application was issued by the joint administrators of Lehman Brothers International (Europe) (in Administration) ('LBIE') (the 'JAs'), with a view to obtaining the Court's guidance in respect of a variety of issues relating, in broad terms, to the following categories of issues: (a) issues concerning the entitlement of creditors to interest on their debts for periods after the commencement of LBIE's administration (Part A); (b) the construction and effect of agreements made since the commencement of LBIE's administration between LBIE, acting by the JAs, and a significant number of its creditors (the 'Post-Administration Contracts') (Part B); and (c) generic issues arising out of the construction and effect of ISDA Master Agreements and other market standard agreements entered into by LBIE and certain of its counterparties, in particular in relation to the calculation of interest under those master agreements (Part C). The trial of Part C of the Waterfall II application was heard before Hildyard J in November 2015 and, as at the date of writing, judgment has yet to be handed down.

The unusual context in which the issues for determination in the Waterfall II application arose was that, after paying or providing for all the debts proved in LBIE's administration, there remained a substantial surplus in the LIBE estate which was estimated to reach or exceed some GBP 7.39 billion (the 'Surplus') (Part A Judgment, paragraph [3]). In the Waterfall I application, the High Court and Court of Appeal (see [2014] EWHC 704 (Ch), [2015] Ch 1; and [2015] EWCA Civ 485; currently being appealed to the Supreme Court) held, inter alia, that the Surplus was to be distributed in the following order: (a) statutory interest payable under rule 2.88 of the Insolvency Rules 1986 (as amended) (the 'Rules') ('Statutory Interest'); (b) non-provable claims of creditors, including claims arising in respect of currency conversion losses resulting from a depreciation of sterling against the currency in which creditors' contractual claims were payable between the commencement of the administration and the date on which dividends were paid on such claims ('Currency Conversion Claims', or 'CCCs'); and (c) the USD 2.27 billion subordinated debt owed by LBIE to Lehman Brothers Holdings Intermediate 2 Ltd ('LBHI2'). The Waterfall II application was brought on the basis that, notwithstanding the Waterfall I application, there remained various unresolved questions relating to creditors' entitlement to Statutory Interest and non-provable claims, as well as to the construction and effect of the Post-Administration Contracts and certain master agreements.

Since the majority the issues determined in the Judgments are now in the process of being appealed to the Court of Appeal, the present article limits itself to a neutral digest of David Richards J's decisions on the various issues raised in Part A and Part B of the Waterfall II application.

A. The Part A Judgment

The Part A Judgment concerns various aspects of the construction and effect of rule 2.88(7) of the Rules, as in force on 15 September 2008 (the date of LBIE's entry into administration), which provided for Statutory Interest to be payable on proved debts in the event of a surplus remaining after payments of the debts proved. Rule 2.88(7) provided: 'Any surplus remaining after payment of the debts proved shall, before being applied for any purpose be applied in paying interest on

Notes

1 Alex Riddiford acted for the Joint Administrators of LBIE in this case.

those debts in respect of the periods during which they have been outstanding since the company entered administration'. Rule 2.88(7) is to be read together with the other paragraphs of rule 2.88, in particular rule 2.88(9) which provided: 'The rate of interest payable under paragraph (7) is whichever is the greater of the rate specified under paragraph (6) [viz. the rate specified in section 17 of the Judgments Act 1838 on the date when the company entered administration] or the rate applicable to the debt apart from the administration'.

(i) Issue 1: Statutory Interest accrues on a simple basis and the calculation of the daily rate

In relation to Issue 1, the Court held as follows:

(1) On the true construction of rule 2.88(7) of the Rules, Statutory Interest payable pursuant to that rule at the rate provided for by section 17 of the Judgments Act 1838 (the 'Judgments Act Rate') accrues on a simple (and not a compound) basis; and

(2) For the purposes of calculating Statutory Interest at the Judgments Act Rate for any period that falls partly or wholly within a year (such year starting on 15 September) that includes 29 February, the daily rate to be used for calculating Statutory Interest for that part of the period falling within that year is the Judgments Act Rate divided by 366 days.

In the event, the issue giving rise to the decision referred to at (1) above was agreed among the parties, and the Judge ruled accordingly. The issue giving rise to the decision referred to at (2) above was contested and the Judge ruled in the JAs' favour. In particular, the Judge reasoned that '[i]f a creditor with a judgment of £1 million is entitled to £80,000 for a complete year, whether or not it is a leap year, he is not, in my judgment, entitled to an extra day's interest for part of a year which happens to include 29 February' (Part A Judgment, at [241]).

(ii) Issue 2: Bower v Marris *(1841) Cr&P 351, 41 ER 525*

Issue 2 raised the question whether, on the true construction of rule 2.88(7) of the Rules, Statutory Interest is calculated on the basis of allocating dividends: (i) first to the payment of accrued Statutory Interest at the date of the relevant dividends and then in reduction of the principal; (ii) first to the reduction of the principal and then to the payment of accrued Statutory Interest; or (iii) on the basis of some other sequencing.

As the Judge noted (Part A Judgment, paragraph [33]), the resolution of this issue stood to make a significant difference to the amount to be paid by way of interest out of the surplus in accordance with rule 2.88(7) of the Rules, perhaps in the region of some GBP 1.3 billion.

The parties agreed that this issue raised a question of statutory interpretation, as to the meaning and effect of rule 2.88(7) of the Rules. However the First to Third Respondents, together the Senior Creditor Group (the 'SCG'), and the Fifth Respondent ('York'), submitted that:

(1) There was a general equitable principle (as established by cases such as *Bower v Marris* (1841) Cr&P 351, 41 ER 525) applicable in the administration of insolvent estates that payments made by process of law in the payment of debts are, when it comes to calculating and paying post-insolvency interest, to be treated as appropriated first to any interest outstanding at the date of distribution and only then in reduction of the principal amount of the debt.

(2) Whilst there have been no cases in any form of insolvency since the enactment of the Insolvency Act 1986 (the '1986 Act') dealing with this issues, nonetheless this approach has been applied to bankruptcy and liquidations in other jurisdictions with regimes similar to the English regime before the 1986 Act and has been applied by the Canadian and Irish Courts in the context of legislative regimes similar but not identical to rule 2.88 of the Rules.

(3) It accorded with fairness, justice and fundamental principles of insolvency law that this equitable principle established by cases such as *Bower v Marris* should apply to rule 2.88 of the Rules and the similar provisions in bankruptcy and liquidation and there was no reason in principle why it should cease to apply or any acknowledgement in any authority or textbook that it has done so.

Notwithstanding these arguments, the Judge determined that the answer to this question was not (i) but (ii), namely that Statutory Interest is calculated on the basis of allocating dividends first to the reduction of the principal and then to the payment of accrued Statutory Interest, with the consequence that LBIE's non-subordinated creditors stand to receive some GBP 1.3 billion less by way of Statutory Interest than they would receive if the SCG and York had been correct.

In the event, the Judge accepted the submissions of the JAs and the Fourth Respondent ('Wentworth') that rule 2.88 of the Rules, and the equivalent provisions in the 1986 Act for liquidation and bankruptcy, are irreconcilable with the application of the equitable principle on which the SCG and York relied. The Court considered the parties' submissions and the authorities relied upon by them in great detail and it is beyond the scope of this article to review the Judge's reasoning in any detail. In brief, however, the Judge placed emphasis

on the importance of approaching the 1986 Act and the Rules as, in many respects, a new code and of not construing their provisions as if the previous law still applied. Since he found that the equitable principle established in cases such as *Bower v Marris* was incompatible with rule 2.88 of the Rules, it followed that this equitable principle did not apply in this context.

(iii) Issue 2A: non-provable claims for interest

This issue was, in essence, whether creditors who had rights to interest apart from the administration and who recovered less interest under rule 2.88(7) of the Rules than they might otherwise have done, for example by applying *Bower v Marris*, had a non-provable claim for the balance.

In short, the Judge held that:

(1) A creditor entitled to Statutory Interest is not entitled to any further interest or damages or any other form of compensation in respect of the time taken for Statutory Interest to be paid.

(2) If and to the extent that Statutory Interest paid to a creditor on a proved debt under rule 2.88(7) of the Rules is less than the amount of interest to which the creditor would otherwise have been entitled in respect of that debt, the creditor does not have a non-provable claim for the difference.

(3) If and to the extent that a creditor has a non-provable claim (including but not limited to a CCC) in respect of a sum on which interest is payable apart from the administration at any time during the period after the Date of Administration (15 September 2008), the creditor has a non-provable claim in respect of such interest (if any) as may have accrued on that non-provable claim in that period.

As to (1) and (2), the Judge concluded that rule 2.88 of the Rules represented a complete code for the payment of post-administration interest. In this context the Judge relied on the fact that rule 2.88(7) does not stipulate the time at which payment of Statutory Interest is to be made; and on the fact that the legislation does not make provision for the payment of interest on Statutory Interest. His Lordship held that, in the absence of a breach of an obligation to pay the Statutory Interest, no jurisdiction exists to award interest or damages in respect of the time taken to pay the Statutory Interest.

As to (3), the Judge held that the position of rule 2.88 of the Rules as a complete code relating to the payment of post-administration interest does not interfere with the enforcement of the contractual right to interest on a CCC as an integral part of that non-provable claim. In short, rule 2.88 of the Rules does not interfere with the enforcement of the creditor's contractual right to interest on a non-provable debt.

(iv) Issue 3: Compound interest

This issue was substantially agreed among the parties. The Judge held that:

(1) The words 'the rate applicable to the debt apart from the administration' in rule 2.88(9) of the Rules refer not only to the numerical percentage rate of interest but also to the mode of calculating the rate at which interest accrues on a debt, including the compounding of interest. Consequently, where a creditor has a right to be paid compound interest on a proved debt apart from the administration, the creditor is entitled to compound interest under rule 2.88 as part of the 'rate applicable to the debt apart from the administration' (if such compounding rate would give an effective rate of interest greater than the Judgments Act Rate).

(2) Where Statutory Interest is payable at a 'rate applicable to the debt apart from the administration' and such rate is a compounding rate, accrued Statutory Interest does not continue to compound following the payment in full of the principal amount through dividends.

(3) A creditor does not have a non-provable claim in respect of interest that would have continued to compound on its proved debt apart from the administration following the payment in full of the principal amount of the proved debt.

(v) Issue 4: Rule 2.88(9) of the Rules and foreign judgment rates of interest

The Judge decided that the words 'the rate applicable to the debt apart from the administration' in rule 2.88(9) of the Rules include a foreign judgment rate of interest applicable to a foreign judgment obtained prior to the Date of Administration but do not include:

(1) A foreign judgment rate of interest applicable to a foreign judgment obtained after the Date of Administration; or

(2) A foreign judgment rate of interest which would have become applicable to the debt if the creditor had obtained a foreign judgment (when it did not in fact do so).

In reaching his conclusion on (2), the Judge determined that the words 'the rate applicable to the debt apart from the administration' cannot be read as including a hypothetical rate which would be applicable to a debt if the creditor took certain steps.

As regards his conclusion (1), the Judge agreed with the SCG that as a matter of language the words 'the rate applicable to the debt apart from the administration' were capable of including a rate applicable at or at any time after commencement of the administration,

but decided (in favour of Wentworth) that those words included only those rates applicable at the time of the commencement of the administration. The Judge's reasons for reaching this conclusion included that it was necessary for the operation of rule 2.88 of the Rules that there should be a single cut-off date for ascertaining the rights of creditors.

(vi) Issue 5:The comparison required by rule 2.88(9) of the Rules

This issue was agreed among the parties. In accordance with the parties' agreed position, the Judge held that:

(1) For the purposes of establishing 'whichever is the greater of the rate specified under paragraph (6) and the rate applicable to the debt apart from the administration' (as required by rule 2.88(9) of the Rules), the comparison required is of the total amounts of interest that would be payable under rule 2.88(7) of the Rules based on each method of calculation (including the compounding of interest), rather than only the numerical rates themselves.

(2) Where two or more separate provable debts are admitted as a single amount and the 'rate applicable to the debt apart from the administration' is different in respect of each of those provable debts (or nil in respect of at least one of them), the single admitted amount is to be disaggregated into its constituent provable debts for the purposes of establishing 'whichever is the greater of the rate specified under paragraph (6) and the rate applicable to the debt apart from the administration' (as required by rule 2.88(9) of the Rules and the relevant rates of interest are to be applied to each of those constituent provable debts individually).

(vii) Issues 6 to 8:The relevant date for the comparison required by rule 2.88(9) of the Rules

The Waterfall II application raised three interrelated issues the relevant date for the comparison required by rule 2.88(9) of the Rules. In particular, the Judge held as follows:

(1) *Issue 6*: For the purpose of establishing 'whichever is the greater of the rate specified under paragraph (6) and the rate applicable to the debt apart from the administration' (as required by rule 2.88(9) of the Rules), the amount of interest to be calculated based on the latter is to be calculated from the Date of Administration.

(2) *Issue 7*: Statutory Interest is payable in respect of an admitted provable debt which was a contingent debt as at the Date of Administration from the Date of Administration.

(3) *Issue 8*: Statutory Interest is payable in respect of an admitted provable debt which was a future debt as at the Date of Administration from the Date of Administration.

Again, this was a question of the correct construction of rule 2.88 of the Rules. The Judge noted that the purpose of rule 2.88(7) of the Rules is to provide for interest to be paid to all creditors, irrespective of whether they had any entitlement to interest apart from the administration; and that what they are being compensated for by the payment of interest under that provision is the delay since the commencement of the administration in the payment of their admitted 'debts', as ascertained or estimated in accordance with the legislation, rather than compensation for the non-payment of the underlying debts. Further, in the Judge's view, the reference in rule 2.88(7) of the Rules to 'any surplus remaining after payment of the *debts proved*' could only be a reference to the debts as admitted to proof (as opposed to the underlying debts). For these reasons (among others) the Judge considered that the correct date for the purposes of the comparison required by rule 2.88(9) was the Date of Administration.

(viii) Further miscellaneous issues

For completeness, it is noted that the Court also held as follows:

(1) *Issue 9*: The date from which Statutory Interest is payable in accordance with the decision in respect of Issues 7 and 8 above is not affected by a creditor's accession to the Claims Resolution Agreement entered into between LBIE and certain of its creditors (see the discussion of the Part B Judgment below).

(2) *Issue 10*: The calculation of a non-provable claim (excluding any non-provable claims to interest (as to which no declaration is made) but including, although not limited to, a CCC) should not take into account (nor, therefore, be reduced by) the Statutory Interest paid to a relevant creditor.

(3) *Issue 29*: Where a creditor with a claim originally denominated in a foreign currency receives Statutory Interest on a Sterling admitted claim at the Judgments Act Rate and such Statutory Interest is less than the amount of interest at the Judgments Act Rate which the creditor would have received on his claim in the original foreign currency, the creditor has no non-provable claim in respect of the difference (without prejudice to any non-provable claim to interest that such creditor may

have pursuant to the third head of the decision on Issue 2A[1]).

(4) *Issue 30*: Where a creditor with a claim originally denominated in a foreign currency receives Statutory Interest on a Sterling admitted claim at the 'rate applicable to the debt apart from the administration' and such Statutory Interest is less than the amount of contractual interest which the creditor would have received on his claim in the original foreign currency, the creditor has no non-provable claim for the difference (without prejudice to any non-provable claim to interest that such creditor may have pursuant to the third head of the decision on Issue 2A[2]).

B. The Part B Judgment

As noted above, Part B of the Waterfall II application concerned the construction and effect of various Post-Administration Contracts. The first, the Claims Resolution Agreement (the 'CRA'), was a multi-lateral agreement made in late 2009 to which over 90 per cent in value of eligible creditors with claims to trust assets became party. The others, Claims Determination Deeds (the 'CDDs'), were bilateral agreements in largely standard terms. The first were made in late 2010 and their terms evolved over time. By September 2014, some 1,600 deeds with about 1,290 different counterparties, agreeing claims totalling over GBP 9.9 billion, had been made. The principal purpose of these agreements was to simplify and accelerate the ascertainment of claims to trust assets and unsecured claims and to accelerate the return of trust assets and distributions among unsecured creditors.

The Judge considered various questions as to: (i) the correct construction of the CRA and the CDDs, in particular as to whether those agreements effected a release of creditors' CCCs and Statutory Interest claims; and (ii) whether, if those agreements did effect the release of such claims, the JAs would be directed not to enforce those releases. The questions of construction are of limited importance beyond the facts of LBIE's administration (and so the Judge's decisions on these issues are summarised briefly); whereas the Judge's reasoning as regards the applicability of the the principle in *ex parte James* (1874) LR 9 Ch App 609 and/or paragraph 74 of schedule B1 to the Insolvency Act 1986 is of some broader importance and therefore considered in greater detail.

(i) Release of CCCs and Statutory Interest

As regards the relevant questions of construction, the Judge noted that one key aspect of the admissible context was that the JAs were acting in accordance with their statutory duties as administrators of LBIE, rather than in their personal interests. There was no real dispute between the parties as to the applicable principles of construction, although the SCG (which argued against the purported releases) relied heavily on the context in which the Post-Administration Contracts were made, whilst Wentworth (which argued in favour of the purported releases) relied heavily on the terms of the agreements themselves. In short, the Judge held as follows:

(1) Neither the CRA entered into between LBIE and certain of its creditors nor any of the CDDs entered into between LBIE and its creditors has, as a matter of construction, the effect of releasing any CCCs.

(2) Neither the CRA nor any of the CDDs has, as a matter of construction, the effect of releasing in whole or in part claims to statutory interest under rule 2.88 of the Rules and, accordingly, creditors with provable debts agreed and/or admitted under such agreements are entitled to the payment of statutory interest on such debts at the higher of the rate provided for by section 17 of the Judgments Act 1838 or the rate applicable to the debt apart from the administration under rule 2.88(9) of the Rules.

(3) The CRA does not, as a matter of construction, create or give rise to any Currency Conversion Claims.

(ii) Whether the JAs would be directed not to enforce any releases

The Judge held that if (contrary to the decision set out at (1) above) the CRA or any of the CDDs had, as a matter of construction, the effect of releasing any CCCs, the JAs would be directed by the Court, under the principle in *Ex parte James* (1874) LR 9 Ch App 609 and under paragraph 74 of schedule B1 to the Insolvency Act 1986, not to enforce such releases.

The Judge emphasised that neither the SCG nor Wentworth had at any stage suggested that the conduct of the JAs should or could be the subject of any criticism. Rather, the question was whether the Court would restrain a particular course of action, namely the enforcement of the relevant releases (in the event that, on

Notes

1 Viz. If and to the extent that a creditor has a non-provable claim (including but not limited to a CCC) in respect of a sum on which interest is payable apart from the administration at any time during the period after the Date of Administration, the creditor has a non-provable claim in respect of such interest (if any) as may have accrued on that non-provable claim in that period.

2 See fn. 1 *supra*.

appeal, the CRA and/or the CDDs were held to provide for the release of CCCs, as contended by Wentworth), if such a course of action were ever to be proposed by the JAs.

The Judge cited the various statements of the principle in *Ex parte James* (1874) LR 9 Ch App 609 that have been given in the authorities, including (for example) Salter J's statement in *Re Wigzell* [1921] 2 KB 835, that the 'jurisdiction should be exercised wherever the enforcement of legal right would, in the opinion of the Court, be contrary to natural justice ... The effect of exercising the jurisdiction which these decisions have asserted and defined is to deprive the creditors of money which is divisible among them by law. I feel sure that such a power should not be used unless the result of enforcing the law is such that, in the opinion of the Court, it would be pronounced to be obviously unjust by all right-minded men.' The Judge also set out what he described as the latest and most authoritative word on the subject, specifically Lord Neuberger's statement in *Re Nortel GmbH* [2014] AC 209, at [122]:

> 'As to the common law, there are a number of cases, starting with *Ex p James; In re Condon* (1874) LR 9 Ch App 609, in which a principle has been developed and applied to the effect that "where it would be unfair" for a trustee in bankruptcy "to take full advantage of his legal rights as such, the court will order him not to do so", to quote Walton J in *In re Clark (a bankrupt), Ex p The Trustee v Texaco Ltd* [1975] 1 WLR 559, 563. The same point was made by Slade LJ in *In re TH Knitwear (Wholesale) Ltd* [1988] Ch 275, 287, quoting Salter J in *In re Wigzell, Ex p Hart* [1921] 2 KB 835, 845: "where a bankrupt's estate is being administered ... under the supervision of a court, that court has a discretionary jurisdiction to disregard legal right", which "should be exercised wherever the enforcement of legal right would ... be contrary to natural justice". The principle obviously applies to administrators and liquidators: see *In re Lune Metal Products Ltd* [2007] Bus LR 589, para 34.'

The Judge, proceeding on the basis that 'unfairness' was a sufficient ground for the application of the principle in *Ex parte James*, held that, in light of all the background facts that he had taken into account in construing the CRA and the CDDs, 'it would be grossly unfair to the creditors who have entered into the CRA or any CDD to enforce any waiver or release of their currency conversion claims that may, on the construction of any such agreement, exist' (Part B Judgment, paragraph [184]).

Turning to paragraph 74 of Schedule B1 of the 1986 Act, this provides that the Court may grant relief where:

> '(a) the administrator is acting or has acted so as unfairly to harm the interests of the applicant (whether alone or in common with some or all other members or creditors), or
>
> (b) the administrator proposes to act in a way which would unfairly harm the interests of the applicant (whether alone or in common with some or all other members or creditors).'

The Judge referred to the decision of Blackburne J in *Re Lehman Brothers International (Europe), Four Private Investment Funds v Lomas* [2008] EWHC 2869 (Ch), [2009] BCC 632, at [34], where Blackburne J stated that the requirement of harm is shown if the applicant establishes that the action of the administrator in question will be causative of harm to its interests. The Judge considered there to be no question but that the enforcement of releases of currency conversion claims will harm the interests of the creditors concerned.

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