Brexit's impact on cross-border insolvencies

Charles Draper brings us an update on Brexit and the impact it will have on the UK and the EU

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On 29 March 2017, the Government of the United Kingdom activated Article 50 of the Treaty on European Union, formally commencing the UK's exit from the EU.

The European Union (Withdrawal) Act 2018 fixed the exit date for 11pm on 29 March 2019. With only just over 6 months remaining until the UK officially divorces from the European Union, we summarise the current position and impact of withdrawal on EU-UK cross-border insolvency proceedings.

The current position of EU-UK cross-border insolvency proceedings

With the exception of Denmark, cross-border insolvency proceedings between the UK and EU Member States are governed by the *EC Regulation No 1346/2000 on Insolvency Proceedings* and the *Regulation (EU) 2015/848 on Insolvency Proceedings (Recast)* (the "EU Regulations").

The EU Regulations assist with the harmonisation of cross-border insolvency proceedings by:

- Establishing "main" and "secondary" insolvency proceedings and providing for a co-ordinated interaction between the two;
- Automatically recognising insolvency proceedings in foreign jurisdictions;
- Applying the local law of the country where "main" proceedings have been opened in other Member States; and
- Requiring co-operation and communication between foreign office-holders and courts to facilitate the co-ordination of cross-border insolvencies.

These benefits streamline proceedings; greatly reducing the time and cost involved, preserving foreign assets and assisting with recovery of those assets. These functions ensure parity between local and foreign creditors and help achieve the maximum return to creditors.

Update on Brexit

On 19 March 2018, the EU and the UK jointly published a draft agreement on the withdrawal of the United Kingdom from the European Union (the "Draft Withdrawal Agreement"). The

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Draft Withdrawal Agreement details the progress of negotiations of the terms on which the UK will depart from the EU, but does not deal with the legal framework that will govern the future relationship post-Brexit.

The Draft Withdrawal Agreement provides for an implementation period - lasting until 31 December 2020 - during which certain EU laws will continue to be applicable in the UK, giving the UK and the EU time to formulate a new framework to regulate cross-border matters. A joint statement from the negotiators of the EU and the UK published on 19 June 2018 confirmed that the EU Regulations will remain effective during the implementation period. However, this depends on the remaining terms of the Draft Withdrawal Treaty being agreed before 29 March 2019. If not, the UK will lose the benefit of the EU Regulations as of 30 March 2019; a so-called "hard" Brexit.

Hard Brexit

The UK Foreign Secretary announced last month that the chances of a "no-deal" Brexit are "*growing by the day*", although more recently it appears that a deal may be closer than thought. However, if a hard Brexit occurs, any UK insolvency proceedings with a cross-border element that commences after 29 March 2019 (and vice-versa) will no longer benefit from mutual recognition and the assistance provided by the EU Regulations. Instead, office-holders may need to incur the additional time, costs, disbursements and uncertainty of:

- Applying to the foreign court for recognition of their appointment and assistance in enforcing judgments and orders;
- Seeking assistance locally to apply the law of the relevant jurisdiction; and
- Dealing with foreign office-holders where there are competing insolvencies.

Additional complications may arise as a result of tension between foreign insolvency regimes or due to a lack of co-operation between foreign office-holders. This may cause foreign assets to be lost, harder to recover, or simply not cost effective to recover for creditors. In any event, an increased cost to creditors in any EU/UK cross-border insolvency is likely to be the outcome.

Prior to the EU Regulations, a small minority of EU Member States (Poland, Greece, Romania and Slovenia and the UK) adopted the UNCITRAL Model Law and those will continue to apply in the event of a "hard" Brexit. The Model Law also promotes recognition and assistance in cross-border insolvencies, but only between those countries which have adopted it, and not to the same extent as the EU Regulations therefore its value and assistance is, to a degree, limited. One of the main advantages to the EU Regulations is that they determine which Member State's law applies to the insolvency proceedings by reference to a company's COMI ("centre of main interests"). The Model Law does not provide a comprehensive alternative.

In the event of a hard Brexit, the Model Law (if adopted by the remaining EU Member States) would, at least in the short term, offer a more effective and harmonised insolvency regime with the UK than none at all, but if not, the UK will have to rely on domestic legislation and the laws of the remaining Member States in order to obtain recognition.

Soft Brexit

In the event the Draft Withdrawal Agreement is agreed upon, the EU and the UK will have further time during the implementation period to negotiate a future framework and mechanism to govern cross-border proceedings. Failing any agreement, the position will be the same as mentioned above if hard Brexit occurs next year, but with the EU Regulations ceasing to have effect in the UK from 1 January 2021.

It is still difficult to predict what the outcome will be.

Whilst it would be beneficial to both the UK and the EU to reach an agreement reflecting the EU Regulations and maintaining the status quo, the impact on free movement between the two economies as part of the wider Brexit-deal will likely cause difficulties in achieving that.

Alternatively, the UK is free to negotiate bespoke agreements with individual EU Member States but this would result in a complex web of insolvency regimes specific to each Member State, without the weight and status of EU law behind them.

Impact on the UK

It is hoped that the reputation of the UK's insolvency regime as an efficient, flexible and effective framework will not be undermined by Brexit. However, the differences between the UK's and the remaining Member States's insolvency regimes, combined with the effect of a weaker pound and the restrictions on free movement of goods and people, may cause the UK to be less attractive to foreign investors and multi-national corporates than previously was the case.

With a recent survey of UK office-holders indicating that 76% expect a hard Brexit will lead to more corporate insolvencies, the UK may also see companies seeking to re-establish themselves outside of the UK. ■

> "THE REPUTATION OF THE UK INSOLVENCY REGIME AS AN EFFICIENT, FLEXIBLE AND EFFECTIVE FRAMEWORK IS UNLIKELY TO BE UNDERMINED BY BREXIT"