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CASE REVIEW SECTION

Re Southern Pacific Personal Loans Ltd [2013] EWHC 2485 (Ch) (8 August 2013)

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Introduction

In the recent case of *Re Southern Pacific Personal Loans Ltd* [2013] EWHC 2485 the High Court was asked to determine the relationship between the Data Protection Act 1998 (the 'DPA'), the winding-up of insolvent companies and the duties of liquidators. In particular, the court was asked to determine whether liquidators would be treated as data controllers under the DPA and hence would be personally liable for compliance with the DPA in respect of data processed by the company of which they were liquidators.

Factual background

An application was made by the joint liquidators of Southern Pacific Personal Loans Limited (the 'Company') under s.112(1) of the Insolvency Act 1986 ('IA') for the determination of certain questions and consequential directions. The Company was a member of the Lehman Brothers group of companies but avoided an insolvency process at the time of the collapse of the Lehman group in the UK in September 2008. The Company entered creditors' voluntary liquidation on 4 September 2012.

The Company focused on the provision of personal loans to individuals resident in Great Britain, secured by way of second charge on their homes. Once such loans were made they were held, along with supporting security, by the Company on trust for various special purpose vehicles ('SPVs') for inclusion in securitisation transactions. The SPVs were entitled to call for a transfer of the legal title to the loans and supporting security.

As a result of the nature of the Company's business, the Company collected and retained data in relation to its borrowers. This data included names and addresses, the amount of loans etc. Such data comprised or included 'personal data' for the purposes of the DPA and as a result the Company was a 'data controller' as set out in s.1 DPA (see below). Data was held for the Company by another member of the Lehman group, a loan servicing company called Acenden Limited.

In 2010 the SPVs called for a transfer of the legal title to the loans and supporting security held by the Company. After the transfer, the only data retained by the Company related to redeemed loans and was not required to administer loans. Despite this, the Company has continued to receive data subject access requests ('DSARs') and other requests for information or copies of documents made under the DPA in relation to the data. Many of the DSARs and other requests were generated by claims handling companies to determine whether individuals have a claim to compensation over the mis-selling of payment protection insurance. The statutory fee for making a DSAR is GBP 10 and the cost of complying is approximately GBP 455, exclusive of VAT. The joint liquidators of the Company stated that the annual cost of responding to such requests would be GBP 589,000 and that a continuation of costs at this level would have a material impact on the distribution of funds to creditors.

The DPA

S.1 DPA defines 'data controller' as a person who (either alone or jointly or in common with other persons) determines the purposes for which and the manner in which any personal data are, or are to be, processed.

S.4(4) DPA provides that it is the duty of a data controller to comply with the data protection principles in relation to all personal data for which he is the data controller. The data protection principles are set out in part 1 of schedule 1 to the DPA. Of importance are paragraphs 5 and 6:

> 5. Personal data processed for any purpose or purposes shall not be kept for longer than is necessary for that purpose or those purposes.
>
> 6. Personal data shall be processed in accordance with the rights of data subjects under this Act.

S.7 DPA sets out the rights of access that individuals have in relation to personal data that is being processed by or on behalf of a data controller. S.7(1), so far as relevant, provides:

> Subject to the following provisions of this section and to sections 8, 9 and 9A, an individual is entitled –

(a) to be informed by any data controller whether personal data of which that individual is the data subject are being processed by or on behalf of that controller,

(b) if that is the case, to be given by the data controller a description of –

(i) the personal data of which that individual is the data subject,

(ii) the purposes for which they are being or are to be processed, and

(iii) the recipients or classes of recipients to whom they are or may be disclosed,

(c) to have communicated to him in an intelligible form –

(i) the information constituting any personal data of which that individual is the data subject, and

(ii) any information available to the data controller as to the source of those data, and …

The court may order a data controller to comply with a request from an individual pursuant to an application under s.7(9). Failure to comply with a DSAR would contravene paragraph 6 of the data protection principles and as a result the Information Commissioner may serve the data controller with an enforcement notice under s.40 DPA requiring the data controller to comply with the request.

Questions raised for determination

The joint liquidators of the Company sought the determination of four questions from the court:

(a) are the joint liquidators data controllers within the meaning of s.1(1) DPA?;

(b) if they are data controllers, may they refuse to comply with requests pursuant to s.7 DPA?;

(c) if they are data controllers, may they dispose of all personal data in their control in their capacity as liquidators of the Company?; and

(d) if they are data controllers, may they disclaim the personal data in their control, and thereby cease to be data controllers of the same?

Determination of question (a) – joint liquidators as data controllers

The key issue in relation to the first question was whether the commencement of liquidation and the appointment of a liquidator renders the liquidator, in place or in addition to the company in liquidation, a data controller in respect of data processed by the company in liquidation. Central to the determination of this issue was the fact that statute imposes duties on liquidators in either a personal capacity or as an agent of the company. The Commissioner put forward two arguments to suggest that the joint liquidators are in fact principals in control of data processed by the Company prior to liquidation and as a result they are data controllers.

Firstly, the Commissioner drew attention to the fact that the joint liquidators are under a duty to take into their custody or under their control all the property of the company. Based on this it was argued that where such power is exercised the office-holder would be acting as principal rather than agent. Richards J held that this was not the case and that 'the provisions of the insolvency legislation taken as a whole show that title to the assets of the company remains with the company notwithstanding its liquidation'. As a result the liquidator, in taking control of the company's property, is not acting as principal but as agent replacing the control formerly exercised by the board.

Secondly, the Commissioner focused on the purpose for which the joint liquidators exercised their powers. It was said that unlike directors, liquidators are not acting in the interests of the company as a separate entity or in the interests of members but instead act for the interests of creditors. Based on this liquidators ought to be treated differently from directors. Richards J held that although the commencement of a liquidation brings into effect a different scheme it does not follow that 'in exercising his powers and fulfilling his duties in respect of the property of the company, the liquidator is acting as principal'. Further, Richards J held that property rights and all rights to control the data remained vested in the company at and following its liquidation. Therefore, by exercising any rights in respect of the data, including those defined in the role of data controller, the liquidators would be acting as agents of the company. Richards J made a declaration that the joint liquidators of the Company are not data controllers in respect of the data processed by the Company prior to its liquidation. Further, he also made it clear that although the present matter related to voluntary liquidation he did not think the position would be different in a compulsory liquidation.

Determination of question (c) – disposal and/or disclaimer of data

Prior to addressing questions (b) and (d) Richards J made a determination in relation to whether or not the joint liquidators could dispose of the data held on behalf of the Company. In relation to this question he identified two issues: (1) the Company must retain sufficient data to enable it to respond to DSARs made to the Company before the disposal of the data; and (2) the Company must retain sufficient data to enable them to deal with any claims that may be made in liquidation.

The joint liquidators stated that they intended to advertise for claims against the company, inviting claimants to submit proofs and setting a date by which such proofs must be lodged. Richards J held that 'provided that adequate publicity is given to such notification and sufficient time allowed for the submission of proofs, the liquidators will be entitled to proceed with the distribution of assets without regard to any possible claims which have not been notified to them'. Further, he held that they will be 'entitled to dispose of all the data regarding redeemed loans, save for such data as is required to deal with such claims as may be lodged' so long as it is disposed of in accordance with the DPA.

Determination of questions (b) and (d) – refusal to comply with s.7 requests

As a result of his determination in relation to question (c), it was unnecessary for Richards J to make a determination in relation to questions (b) and (d). Despite this he gave preliminary observations in relation to question (b). The joint liquidators put forward two grounds for suggesting that the company would not be required to respond to requests even if the DSAR was framed appropriately.

The first was that the DSARs were being made for inappropriate purposes and accordingly the Company, as data controller, was entitled to refuse to comply with the request. In support of this contention the joint liquidators relied on the decision of Auld LJ in *Durant v Financial Services Authority* [2003] EWCA Civ 1746 at [24]. Richards J stated that the court could take into account the purpose for which the request was made but that the decision in *Durant v Financial Services Authority* is not authority one way or another for the proposition that a data controller can refuse to respond to a request under s.7. He also stated that this is an issue that may arise for decision in a future case.

The second ground taken by the joint liquidators was that s.8(2)(a) DPA provides that a data controller does not have to comply with a request under s.7(1)(c)(i) if it involves disproportionate effort. Richards J stated that this provision was of very limited use to the joint liquidators.

Conclusion

The decision of Richards J in *Re Southern Pacific Personal Loans Ltd* will be welcomed by office-holders as it removes their personal liability in relation to data processed by the companies they are engaged in winding-up. Although office-holders will not be held personally liable Richards J made it clear that office-holders must be aware of the various principles and provisions of the DPA. In particular, office-holders must ensure that any unnecessary data is disposed of in accordance with the DPA.

Concept Oil Services Ltd v En-Gen Group LLP & Ors [2013] EWHC 1897 (Comm)

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Introduction

Giving judgment on 5 July 2013 Mr Justice Flaux granted relief to the claimant, Concept Oil Services Limited ('Concept'), under sections 423 and 425 of the Insolvency Act 1986 (the '1986 Act') by way of declarations and orders the effect of which was to reverse certain complex international transactions.

Flaux J's decision is of importance in highlighting the utility of section 423 of the 1986 Act as a tool for creditors to challenge complex multi-jurisdictional transactions effected in order to defraud a company's creditors. This decision demonstrates that the Court is both able and willing to exercise its powers under this provision to reach beyond this jurisdiction to unwind relevant transactions, however complex and multi-jurisdictional, provided that there is a sufficient connection with England and Wales in the relevant sense.

Background and relief sought

Concept, a company incorporated in Hong Kong, trades crude and refined oil products and carries on related activities such as transportation. Between October 2008 and November 2010 Concept purchased refined oil from EG UK (the ninth defendant), an English registered company, pursuant to a framework agreement. EG owned EG Group (the third defendant), a Kazakh limited liability partnership, which in turn owned another Kazakh LLP which owned and operated a Kazakh oil refinery.

Concept's loss resulted from payments made to EG UK under the Framework Agreement for refined oil which was never delivered and for other related matters and loss under a tax loan agreement pursuant to which COS lent the group money to meet tax liabilities. Concept's case, which the Learned Judge accepted, was that it was induced to enter these various agreement by representations made by one of EG UK's directors ('K') which proved to be fraudulent.

When Concept attempted to recover these losses it transpired that EG UK had become an Anguillan company ('EG Anguilla') with no assets, EG UK having (i) re-registered itself in Anguilla, (ii) rearranging its corporate structure and (ii) divested itself of ownership of the subsidiary that owned the Kazakh oil refinery.

First, Concept obtained a freezing injunction against the first eight defendants on 6 March 2012. Thereafter proceedings were issued in which Concept claimed damages from EG UK, the other companies in the group and EG UK's directors, on the basis of the torts of deceit and conspiracy. Concept also argued that EG UK's transfer of assets amounted to transactions defrauding creditors for the purposes of section 423 of the Insolvency Act 1986 (the '1986 Act').

On the facts, Flaux J held that K had indeed made a fraudulent misrepresentation to Concept by continuing to hold EG UK out as an English-registered company with substantial assets in circumstances where (i) it had become an Anguilla-registered company with substantially no assets and (ii) Concept had made it clear that it would only trade on the basis that EG UK was an English-registered company.

Ineffective transfer

In fact, the claim for relief under section 423 of the 1986 Act arose only on facts that contradicted the Learned Judge's finding in relation to the effectiveness of EG UK's transfer of its assets. The section 423 claim only arose in circumstances where EG UK's transfer of assets to EG Anguilla had been effective, whereas Flaux J held that this transfer was a nullity. The transfer was null on the basis that, as a matter of English law, EG UK remained at all material times an English-registered company (notwithstanding the provisions of Anguillan statute). Accordingly, EG UK's purported transfer of assets and liabilities to another entity for no consideration was simply a nullity since such a transfer is not regarded as effective as a matter of English law. English law was the applicable law to determine the effectiveness of the transfer from EG UK since the law of incorporation of the transferring entity is the applicable one in these circumstances (following *Dicey, Morris and Collins on the Conflict of Laws*, 15th ed., at §30-011).

Nonetheless, the Learned Judge considered the claim for relief under section 423 and was prepared to grant such relief as appropriate, notwithstanding his primary finding that the transfer was ineffective in any event.

Relief under section 423 of the 1986 Act

Section 423 of 1986 Act provides (so far as material):

> '(1) This section relates to transactions entered into at an undervalue; and a person enters into such a transaction with another person if –
>
> (a) he makes a gift to the other person or he otherwise enters into a transaction with the other on terms that provide for him to receive no consideration;
>
> …
>
> (c) he enters into a transaction with the other for a consideration the value of which, in money or money's worth, is significantly less than the value, in money or money's worth, of the consideration provided by himself.
>
> (2) Where a person has entered into such a transaction, the court may, if satisfied under the next subsection, make such order as it thinks fit for –
>
> (a) restoring the position to what it would have been if the transaction had not been entered into, and
>
> (b) protecting the interests of persons who are victims of the transaction.
>
> (3) In the case of a person entering into such a transaction, an order shall only be made if the court is satisfied that it was entered into by him for the purpose –
>
> (a) of putting assets beyond the reach of a person who is making, or may at some time make, a claim against him, or
>
> (b) of otherwise prejudicing the interests of such a person in relation to the claim which he is making or may make.
>
> (4) In this section "the court" means the High Court …
>
> (5) In relation to a transaction at an undervalue, references here and below to a victim of the transaction are to a person who is, or is capable of being, prejudiced by it; and in the following two sections the person entering into the transaction is referred to as "the debtor."'

Importantly, as the Learned Judge noted, the provision is quite a 'general' one, in that its scope extends to transactions which take place beyond this jurisdiction: see *Fortress Value Recovery Fund 1 LLC v Blue Skye Special Opportunities Fund LP* [2013] EWHC 14 (Comm), *per* Flaux J, at paragraphs [113] to [114]; and *Re Paramount Airways (No 2)* [1993] Ch. 223, *per* Sir David Nicholls V-C, at paragraphs [239] to [240].

Further, the question of the sufficiency of the connection with England required to justify relief under section 423 of the 1986 Act is not a threshold question of jurisdiction but rather a question of discretion. Accordingly, this provision is capable of serving as a powerful tool, with broad extra-territorial reach, in circumstances such as the instant case where complex multi-jurisdictional transactions have been effected in an effort to defraud a company's creditors.

Indeed, in the instant case Flaux J had little difficulty in finding that there was a sufficient connection with England to justify granting relief under section 423, on the basis that the starting point for the relevant transactions was the transfer of assets out of EG UK, an English-registered company, and that the other impugned transactions flowed directly out of this transfer.

In fact, the transfers which Concept impugned (and was obliged to impugn if it was to obtain an adequate remedy under the provision) were: (i) the transfer of the assets and liabilities of EG UK to EG Anguilla in September 2009; (ii) the transfer of the interest in EG Production (the Kazakh company which owned the oil refinery) to Akkert SA (a BVI entity) in June 2010 and (iii) the transfer of the interest in EG Group to Larson (an English-registered entity) at some point after 14 February 2011 when Larson was incorporated.

Accordingly, Flaux J was prepared to utilize the section 423 remedy to reach far beyond this jurisdiction in order to reverse the initial defrauding transaction and grant the Claimant its remedy.

Other issues which fell to be determined in relation to the section 423 claim included whether the threefold transfers referred to above fell within the meaning of 'transaction' for the purposes of section 423.

In brief, Flaux J was confident that the transfers did indeed qualify, relying in particular on Parker LJ's comment in relation to the meaning of 'transaction' for the purposes of section 426, namely that '[it] includes a gift, agreement or arrangement' (see *Feakins v DEFRA* [2005] EWCA Civ 1513, at paragraph [7]), and that 'arrangement is, on its natural meaning and in the context of section 423, apt to include an agreement or understanding between parties, whether formal or informal, oral or in writing. In my judgment the wide definition of 'transaction' in the context of section 423 is entirely consistent with the statutory objective of remedying the avoidance of debts …' (*ibid.*, paragraph [76]).

In light of Parker LJ's comments, and as a matter of principle, Flaux J was comfortable characterizing the threefold transfer set out above as a '*transaction*' in the relevant sense.

Conclusion

Flaux J's response to the defendants' fraudulent conduct in this case was an admirably commercial one, showing a readiness to use the Court's powers under section 423 of the 1986 Act to remedy a complex series of transfers designed to defraud the creditors of EG UK. The decision sends an important message to creditors that the English Court is able and willing to look behind complex multi-jurisdictional arrangements and to reverse them, provided it is established that these arrangements are intended to defraud creditors and that a sufficient connection exists with England and Wales in the relevant sense.

CASE REVIEW SECTION

LBI hf v Kepler Capital Markets SA [2013] EUECJ C-85/12

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Introduction

On 24 October 2013, the European Court of Justice ('ECJ') handed down its judgment in *LBI hf v Kepler Capital Markets SA and Frédéric Giraux* [2013] EUECJ C-85/12. This followed a request for a preliminary ruling from the French Cour de Cassation on the interpretation of Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding up of credit institutions ('the Directive'). Two questions were considered, firstly whether moratorium measures taken in respect to LBI hf ('Landsbanki') under Icelandic legislation constituted reorganisation measures or winding-up proceedings taken by administrative or judicial authorities under the Directive, and secondly whether the retrospective effect of Icelandic legislation was precluded from having effect under the Directive. As will be noted in due course, the ECJ's ruling conflicts with a decision of the English High Court.

Background and relevant legislation

On 10 November 2008, Mr Giraux served two provisional attachment orders in France on Kepler Capital Markets SA in order to guarantee payment of his claim against Landsbanki. Three days later, the Icelandic parliament enacted an amendment to article 98 of Icelandic Law[1] No 161/2002 to enable moratoria to be implemented to prohibit commencement of proceedings against financial institutions and to suspend any pending proceedings. On 5 December 2008, the Reykjavik District Court in Iceland granted Landsbanki such a moratorium (which was extended on a number of occasions until 5 December 2010).

Just 5 months later, due to apparent constitutional concerns, the moratoria provisions were repealed by Law No 44/2009 of 15 April 2009. This was accompanied by transitional provisions that continued existing moratoria and applied to such institutions the provisions of Law No 161/2002 on the liquidation of financial institutions 'as if the institution had been placed in winding-up proceedings by a judicial decision on the date on which [Law No 44/2009] entered into force'. The transitional provisions also provided that 'On the expiry of that authorisation [of the moratorium], the undertaking shall automatically be regarded as being the subject of winding-up proceedings in accordance with general rules, without any specific judicial decision …'.

Landsbanki applied to the Tribunal de Grande Instance in Paris to lift the two attachment orders on the basis that Law No 44/2009 made applicable article 138 of the Law No 21/1991 which annuls attachment orders against a company's assets within the 6 months preceding a court's declaration of insolvency. However, Landsbanki's application was dismissed in June 2009 on the basis that the provisions of Law No 44/2009 were not applicable in France because they did not constitute reorganisation measures or winding-up measures taken by 'administrative or judicial authorities' within the meaning of the Directive.

The Directive provides that the administrative and judicial authorities of a credit institution's home state shall alone be empowered to decide on the implementation of any reorganisation measure (article 3), or the opening of winding-up proceedings (article 9), including in respect to any branch established in a host state within the European Economic Area ('EEA'). Such decisions are effective throughout the EEA without further formality, and must be applied in accordance with the laws of the home state (unless provided otherwise in the Directive) even where the host state's laws do not provide for the reorganisation measures in question. Article 32 provides that the effects of reorganisation measures or winding-up proceedings on a pending lawsuit concerning an asset or a right of which the credit institution has been divested shall be governed solely by the law of the state in which the lawsuit is pending.

On 4 November 2010, the Cour d'Appel in Paris upheld the decision of the Tribunal de Grande Instance, its reasons including that the moratorium could not have the retrospective effect agued by Landsbanki. In apparent response to that judgment, on 16 November 2010 the Icelandic parliament amended the transitional

Notes

1 A reference within this article to a 'Law' is to a statute of the Icelandic parliament.

provisions in Law No 44/2009 so as to require that an application be made to the court for a winding-up order prior to the expiration of the moratorium. An application was accordingly made to the Reykjavik District Court which made a winding-up order in respect to Landsbanki on 22 November 2010.

Reference for a preliminary ruling

Landsbanki appealed from the Cour d'Appel on a point of law to the Cour de Cassation which opted in February 2012 to stay the proceedings in favour of referring the following two questions to the ECJ for a preliminary ruling:

> '1. Must Articles 3 and 9 of [the Directive] be interpreted as meaning that reorganisation or winding-up measures in regard to a financial institution, such as those under [Law No 44/2009], are to be regarded as measures adopted by an administrative or judicial authority for the purposes of those articles?
>
> 2. Must Article 32 of [the Directive] be interpreted as precluding a national provision, such as Article 98 of [Law No 161/2002], which prohibited or suspended any legal action against a financial establishment as from the entry into force of a moratorium, from having effect in regard to interim protective measures adopted in another Member State before the declaration of the moratorium?'

The first question

In its judgment, the ECJ noted that it was not disputed that the moratorium ordered by the Reykjavik court constituted a 'reorganisation measure' for the purposes of the Directive since it was designed to enable Landsbanki to reorganise its financial situation. It further noted that the transitional provisions introduced by Law No 44/2009 amended the effect of the moratorium by making the institution subject to a specific winding-up scheme, without the institution being wound-up before the expiry of the moratorium. However, as indicated by the first question, it was disputed whether the provisions of Law No 44/2009 should be regarded as measures adopted by an administrative or judicial authority where the provisions were effective only by means of a judicial decision to grant a moratorium.

The ECJ answered this question in the affirmative. At the outset the court emphasised that the Directive's preamble indicated its objective was to seek to establish mutual recognition of measures taken by member states to restore the viability of the credit institutions which the state had authorised. Together with the equal treatment of creditors, the court stated this required that reorganisation and winding-up measures taken by the authorities of the home state have the effects in other states which were conferred by the law of the home state.

However, the ECJ did not appear to be willing to hold that a measure enacted by the Icelandic parliament could directly have effect under the Directive, noting that articles 3 and 9 expressly stated that the administrative and judicial authorities of the home state are 'alone empowered' to decide on reorganisation and winding-up of credit institutions. That said, even though Law No 44/2009 had been enacted specifically for Landsbanki and two other Icelandic banks, the ECJ decided that the Icelandic parliament had not directly ordered the winding-up of such institutions, since the transitional provisions would apply only if a judicial decision had been taken to grant or extend a moratorium in respect to a specific institution.

In the circumstances, the ECJ held that the grant by the Reykjavik District Court of the moratorium in December 2008 was a reorganisation measure granted by a judicial authority. Secondly, that the opening of the winding-up proceedings announced by the Reykjavik District Court on 22 November 2010 amounted to winding-up proceedings for the purposes of the Directive. Accordingly, the court concluded those measures were capable of producing within the EEA in accordance with articles 3 and 9 of the Directive 'the effects which the Icelandic legislation confers on them'.

The ECJ reinforced its conclusion by various references to the Directive, including that the second subparagraphs of both articles 3(1) and 9(1) required that the effects in another state of the reorganisation or winding-up be determined by the law of the home state. The court therefore held the Directive 'does not prevent that Member State from amending, even with retroactive effect, the legal scheme applicable to such measures.' Furthermore, that the Directive, as shown by recital 6 in the preamble, established mutual recognition of national measures 'without seeking to harmonise national legislation on that subject', and such recognition was not to be subject to conditions imposed by the non-home state.

The second question

As will be anticipated from the dicta cited above, the ECJ proceeded to hold in respect to the second question that article 32 of the Directive must be interpreted as not precluding a national provision, such as the moratorium provisions of Law No 161/2002, from having effect in respect to interim protective measures adopted in another state before the declaration of the moratorium.

Reinforcing its purposive approach, at the outset the ECJ stated that to answer the second question 'it must be noted that, as is apparent inter alia from recital 16, [the Directive] is based on the principles of unity and universality' and established a principle of mutual recognition of insolvency processes and their effects. Since article 32 provided that the effect of reorganisation measures or winding-up proceedings was governed by the law of the state in which the suit was pending, the court described this as an exception to the general rule that the effects are governed by the law of the home state. The ECJ therefore held that article 32 'must be interpreted strictly'.

The court stated that the scope of article 32 was clarified by recital 30 in the preamble, which made the distinction between 'lawsuits pending' versus individual enforcement actions arising from those lawsuits, the effect of the latter on reorganisation measures and winding-up proceedings being governed by the law of the home state. The ECJ accepted the European Commission's observation that '"lawsuits pending" cover only proceedings on the substance'.

The ECJ suggested that a contrary interpretation of the Directive would be capable of calling into question the effectiveness of the principle of universality. This was because the Directive had the 'very object of suspending individual enforcement actions in order to restore to viability the credit institutions concerned' and any enforcement action would reduce the availability of its assets thereby undermining the principle of universality.

The parties had not disputed that Mr Giraux's attachment orders were individual enforcement actions, and it followed that the measures did not fall within article 32 but were governed by Icelandic law as lex concursus. The ECJ therefore concluded:

> 'The fact that those measures were adopted before the moratorium at issue in the main proceedings had been granted to LBI cannot invalidate that conclusion. As follows from the very wording of the second and third subparagraphs of Article 3(2) and the second subparagraph of Article 9(1) of Directive 2001/24, the lex concursus also governs the temporal effects of reorganisation measures and of insolvency proceedings. Article 32 of that directive cannot prevent those measures and those proceedings from having retroactive effect.'

Comment

It is clear that a purposive interpretation of the Directive drove the ECJ's ruling in this case. However, it is unfortunate that given its potential significance, the judgment was not drafted to the highest quality. The judgment can be hard to comprehend, unaided by it not reproducing all the relevant Icelandic legislation, the full reasoning of the French courts, nor the parties' arguments, and although some assistance can be gained from the Advocate General's opinion this is not available in English.

Moreover, except where the ECJ considered a separate question of admissibility, the judgment makes no reference to any case law whether ECJ or domestic, save for referring to the French decisions in the case. Whilst the ECJ are not bound to consider domestic case law, it must be highlighted that their ruling on both questions is directly at odds with the conclusions reached by Mr Justice Burton in *Rawlinson and Hunter Trustees SA v Kaupthing Bank HF* [2011] EWHC 566 (Comm), followed by Mrs Justice Gloster in *Lornamead Acquisitions Ltd v Kaupthing Bank HF* in [2011] EWHC 2611 (Comm).[2]

Notes

2 Charlotte Cooke, '*Lornamead Acquisitions Limited v Kaupthing Bank HF* [2011] EWHC 2611 (Comm)', (2012) 1 *International Corporate Rescue* 60-62.

Comity, COMI and Anti-Suit Injunctions: *Kemsley* before the English and US Courts

Richard Fisher, Barrister, South Square, London, UK, and **Maja Zerjal**, Associate, Proskauer, New York, USA

I. *Kemsley*: background

The personal bankruptcy of a once prominent English businessman paved the way for two decisions showing the interplay of the English and US courts in considerations of comity, the UNCITRAL Model Law on Cross-Border Insolvency, and the centre of main interests ('COMI').

Paul Zeital Kemsley ('Kemsley') moved to the US with his family in 2009 after the collapse of his business. The family resided in Boca Raton, Beverly Hills, and New York, until Kemsley's wife moved back to the UK with their children in June 2012. Kemsley filed for bankruptcy in London (the 'English Proceeding') under the Insolvency Act 1986 ('IA 1986') on 13 January 2012. Kemsley's bankruptcy petition was based on his physical presence in England at that time, and on having had a place of residence in England within three years of presentation. The High Court of Justice (the 'English Court') declared Kemsley a bankrupt on 26 March 2012, and shortly thereafter, two trustees were appointed in the English Proceeding. Barclays Bank PLC ('Barclays'), a major creditor in the English Proceeding, sued Kemsley on 1 March 2012 in state court in New York and Florida, broadly seeking relief and remedies relating to a breach of a loan agreement to collect on a personal loan of GBP 5 million advanced to Kemsley. In response, Kemsley sought to stop Barclays on two fronts. First, on 21 August 2012, Kemsley's bankruptcy trustee (the 'Foreign Representative') filed a chapter 15 petition with the United States Bankruptcy Court for the Southern District of New York (the 'US Court'), seeking recognition of the English Proceeding as foreign main proceeding, and, in the alternative, as foreign non-main proceeding. The chapter 15 case was filed, in part, to stay Barclays' proceedings against Kemsley in the US. Second, after the filing of the chapter 15 petition but before recognition, Kemsley sought an anti-suit injunction against Barclays in the English Proceeding.

The decisions of the English Court and the US Court were issued on 8 and 11 March and 22 March 2013, respectively.

II. *Kemsley*: the English perspective

The decision of Mr Justice Roth in *Kemsley v Barclays Bank plc* [2013] EWHC 1274 (Ch) is useful from an English perspective in two principal regards: it confirms the general 'comity' or 'deference' principle which now appears to be the primary regulating factor relating to the grant of anti-suit injunctions (at least in relation to insolvency proceedings), and provides (for the first time) consideration of the role and relevance of COMI and the Model Law to the grant of anti-suit relief.

The comity principle

When should an English Court grant an anti-suit injunction so as to restrict a creditor from taking steps in a foreign forum which are inconsistent, or potentially inconsistent, with the English insolvency regime commenced by or against a debtor? The answer, according to Mr Justice Roth, and consistent with prior jurisprudence, is rarely if ever.

Mr Kemsley sought injunctive relief against Barclays on two bases. First, that Barclays, if it continued proceedings in the US, would obtain an advantage over other creditors as compared to the equitable *pari passu* distribution of assets contemplated by the English bankruptcy process. Second, that Barclays (if it obtained a US judgment which would remain enforceable for 20 years) would avoid and undermine the operation of the debtor's discharge from liability, which discharge was said to be a core element of the English bankruptcy regime.

Barclays conceded at the hearing that it would transfer any recoveries to the bankruptcy estate, subject to deduction of costs and expenses, such that the first basis for the application fell away. The second therefore became the principal focus for the application.

It was common ground between the parties that any stay imposed on proceedings commenced against a bankrupt when a bankruptcy petition was pending, or after the opening of bankruptcy proceedings, by virtue of Section 285 of the IA 1986 did not apply to foreign proceedings and enforcement measures. As such, relief could only be justified under the Court's general power to grant injunctions contained in Section 37 of the Supreme Courts Act 1981.

There is long-standing authority for the proposition that such a power could, in principle, be used to grant an injunction where an estate is being administered in England, or bankruptcy or winding-up proceedings have been commenced in England, and it was necessary to restrain a person from seeking, by foreign proceedings, to obtain the sole benefit of foreign assets falling in the estate. In such a case, the injunction is granted to protect the jurisdiction of the English court.[1] But it must be shown that the bringing or continuation of the foreign proceedings is vexatious or oppressive. The mere fact that England might be the natural forum for such proceedings, or that collective proceedings are underway in England, is not enough.

So what makes a case vexatious or oppressive? In this context, if and to the extent that inconsistency with English proceedings can and will be raised with the foreign court, something more than merely bringing the proceedings in breach of the collective process contemplated by the English process is required. Wrongful conduct will need to be established which requires the Court to intervene[2] and that, in practice, is likely to require some rather extreme or exceptional facts.[3]

The principal consideration in the insolvency context now appears to be the comity principle:[4] if there is a process for consideration in the foreign court of the objections being raised, comity and common sense suggest that it is the foreign judge who is best placed to decide whether the proceedings in his own court should continue.[5] 'Comity requires a policy of non-intervention': *Mitchell v Carter* [1997] 1 BCLC 673.

There is undoubtedly greater support for the grant of an injunction against a creditor who is resident in the English jurisdiction rather than abroad, or who has proved or otherwise participated in the English process (see the *Kemsley* judgment at [26] to [28]). But this may simply be a consequence of a need, in most cases, to establish personal jurisdiction over the creditor in order to satisfy the Court that relief granted will be effective.

What will need to be shown in every case is a good reason why the decision to stop the foreign process should be made in England rather than abroad (see the *Kemsley* judgment at [29]). What will amount to a good or sufficient reason cannot be definitely stated. But we can ascertain from cases where injunctions have been granted or refused what might be a good or sufficient reason. In this regard, the Court of Appeal decision in *Bloom v Harms Offshore GmbH & Co* [2010] Ch 187 is illustrative of the reluctance of the English court to intervene by way of anti-suit injunction to protect insolvency proceedings. In *Bloom*, *ex parte* maritime attachment proceedings were commenced by two German creditors in New York following the commencement of an administration, with the effect that monies paid by the administrators (who were unaware of the attachment) to a post-administration supplier of services were subject to attachment in New York. The Court of Appeal upheld the grant of an injunction, but for very limited reasons. By itself, the commencement of proceedings in New York did not appear to justify the grant of relief. What was objectionable, and moved the application into the realms of vexatious or oppressive behaviour, was the conduct of the creditors. In particular, the creditors commenced the US process without informing the US court that an administration order had been made and provided what was described as 'a very misleading picture' to the US court. The attachment was aimed at interfering with the process of the administration, and did not fasten on any pre-administration property. The creditors only informed the administrators of the attachment once it had succeeded in attaching sufficient funds and, in all the circumstances, were described as having set a trap for the administrators. As such, Stanley Burton LJ concluded at [29] that the case fell into the 'exceptional category' where considerations of comity would be outweighed notwithstanding the fact that the administrators could and had applied in New York to discharge the attachment. Sir John Chadwick agreed on the basis that it was the setting of a trap that obstructed the discharge of functions for which the English court had appointed the administrators that was key.

COMI and the UNCITRAL Model Law

Both England (as part of Great Britain) and the US have implemented the substance (with local variations) of the UNICTRAL Model Law on Cross-Border Insolvency via, respectively, the Cross-Border Insolvency Regulations 2006 and Chapter 15 of the US Bankruptcy Code. The existence of these provisions, and the reciprocal recognition of insolvency proceedings, was considered by Roth J to provide 'an important consideration for the

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1 *Society Nationale Industrielle Aerospatiale v Lee Kui Jak* [1987] AC 871 at 892E.
2 *Turner v Grovit* [20002] 1 WLR 107 at [24]; *British Airways Board v Laker Airways Ltd* [1985] AC 58 at 95.
3 *Midland Bank plc v Laker* [1986] QB 689 at 700.
4 There are echoes here of the stronger concept of comity advocated by the Supreme Court of Canada in its decision in *Amchem v Workers Compensation Board* (1993) 102 DLR (4th) 96, and perhaps now embodied in Rix LJ's description of the general relevance of comity to the grant of general anti-suit injunctions as set out in *Star Reefers Pool Inc v JFC Group Co Ltd* [2012] EWCA Civ 14. Comity increasingly regulates the court's discretion to grant anti-suit injunction relief for fear of acusations of unnecessary '*egoistic paternalism*'.
5 *Barclays Bank plc v Homan* [1993] BCLC 680 at 687.

present application' (see [39]) and is likely to do so in many future cases.

The English court approached matters on the basis that, in circumstances where Kemsley's COMI was either in England or the US (a question which would be considered by the US Court as part of the extant Chapter 15 recognition application), the need for an anti-suit injunction would only arise in circumstances where Kemsley's COMI was found to be in the US (see [40]). That was because, if his COMI was located in England, the bankruptcy proceedings would be regarded as main proceedings and lead to an automatic stay of proceedings in the US upon recognition.

If COMI was located in the US, and the English bankruptcy was recognised as foreign non-main proceedings, then it would be open for the Trustees to apply to the US Court for a stay in support of those proceedings. But if that application was refused, would there be any scope for an anti-suit injunction?

On the facts of the case before him,[6] and in light of the availability of Chapter 15 relief, Roth J concluded that there was not. At [45], he noted that, even if Kemsley's COMI was located in the USA, 'I do not see how it can be regarded as oppressive or unfair or in any way improper for the question whether Barclays should be allowed to maintain its action in the NY Court on an English debt or whether those proceedings should be stayed or dismissed on the basis that Mr Kemsley had become discharged from his debts under the British statute, or indeed whether there should be any restriction on enforcement on post-discharge assets, to be determined by the NY Court. It is not for the English Court to intervene by preventing Barclays from pursuing its case there.' The conduct of Barclays could not be described as 'underhand' as in the case of Bloom (see [47]).

Roth J noted that it was perfectly proper for different bankruptcy regimes to approach the question of release of bankruptcy debts differently, and that the Model Law was focused on procedure not substance ([48]). It could not be suggested, particularly if COMI was located in the US, that a refusal to apply the approach of the English statute would be contrary to English public policy or some international law principle

Roth J elected not to comment more widely on the relevance of the US having adopted the Model Law to the question of the availability of anti-suit injunctive relief generally to protect insolvency proceedings (for example, where COMI was located in a third jurisdiction: see [49]). It is, however, at least arguable that legislative intervention both in England and abroad aimed at implementing the Model Law renders reliance on the anti-suit jurisdiction even more inappropriate in the vast majority of cases. If the foreign jurisdiction has set out a process for recognition of foreign insolvency proceedings, which parallels that implemented in England, such a process should be the primary method of regulating litigation commenced before the foreign court. If the officeholder cannot obtain recognition and a stay before the foreign court under legislation which implements the Model Law, which is patently a question for the foreign court, it is increasingly difficult (absent extreme urgency) to envisage circumstances in which the comity principle ought ever to be outweighed by the wrongful conduct of a creditor in a particular case.

A US view on anti-suit injunctions

In contrast with the UK approach, the automatic stay imposed in plenary proceedings under the US Bankruptcy Code is expressed as having extraterritorial reach. The bankruptcy estate created under the US Bankruptcy Code includes all of the legal and equitable interests of the debtor, wherever located, held as of the filing date. The automatic stay protects the debtor's property by staying any action aimed at obtaining the property of the estate, and US bankruptcy courts have

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6 Roth J, in a postscript to his judgment, highlighted the following aspects of Judge Peck's subsequent decision in the US Court, which perhaps further explain his reluctance to grant relief:

'52 It is perhaps material to the position of Barclays in seeking to pursue the NY Proceedings that Judge Peck noted in his judgment:

"… Mr. Kemsley is a bankrupt who does not live like one. Since leaving his debts behind and coming to the United States, his financial difficulties have not diminished his high standard of living. He earns personal income from certain business activities (he has worked for Planet Hollywood and currently represents the iconic Brazilian soccer star Pele through a marketing business with offices in New York known as Legends 10) and rather conveniently also has ready access to abundant free cash (principally in the form of loans or gifts from generous friends) enabling him to live very well."

53 Further, although he made clear that there was no suggestion that Mr Fry was not acting in good faith, Judge Peck observed:

"…it should be noted that [Mr Kemsley], with the aid of surrogates, has been providing indirect financial support to Mr. Fry to cover the trustee's legal expenses in pursuing recognition under chapter 15.… This financial support may indicate that the trustee's petition for recognition is an aspect of a coordinated trans-Atlantic litigation strategy orchestrated by Mr. Kemsley and his advisers to shield [Mr Kemsley's] assets from enforcement actions by Barclays (notably his Florida real estate)…"

And noting that the granting of the Trustee's application for recognition would benefit Mr Kemsley by stopping the NY Proceedings brought by Barclays, he added:

"The working arrangement between the trustee and Mr Kemsley is an unlikely one. These are parties who would ordinarily be opposed to each other with respect to claims to recover [Mr Kemsley's] assets located in the United States for the benefit of UK based creditors. [Mr Kemsley] and the trustee have formed what amounts to a joint venture – with funding from sources loyal to [Mr Kemsley] – to achieve a result that is adverse to the interests of one of its major creditors."'

in rem jurisdiction extraterritorially – but only by way of *in personam* jurisdiction over entities violating the automatic stay.

Generally, US courts agree that they have ample authority and jurisdiction to issue an anti-suit injunction against parties pursuing litigation in a separate forum, but disagree on the circumstances under which such injunctions are appropriate. Under the 'conservative approach',[7] the court will issue an anti-suit injunction if it is demonstrated that '(1) an action in a foreign jurisdiction would prevent United States jurisdiction or threaten a vital United States policy, and (2) the domestic interests outweigh concerns of international comity'.[8] While comity appears to be at the centre of the conservative approach, the minority 'liberal approach'[9] seems to place a more modest emphasis on comity. Under the latter approach, an injunction is based on equitable factors, such as vexatiousness and oppressiveness of the foreign proceeding. None of the factors are mandatory, but the injunction should not threaten international relations.[10]

The US bankruptcy courts' power to issue an injunction with extraterritorial effect is based on the US Bankruptcy Code, which provides that a court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of the US Bankruptcy Code.[11] At least one court held that based on this independent authority, the anti-suit injunction threshold required under the conservative approach (as applicable in that matter) was irrelevant due to the exclusive jurisdiction of the US bankruptcy courts.[12]

Notably, chapter 15 is different than plenary cases under the US Bankruptcy Code in that the proceeding is ancillary in nature, the definition of 'debtor' is limited and specialised, and recognition does not create an estate under the Bankruptcy Code. Accordingly, and in view of international aspects of Chapter 15, the automatic stay does not afford broad anti-suit injunctive relief to a Chapter 15 debtor and applies outside the US only to the extent that such actions affect property of the debtor that is within the territorial jurisdiction of the US.[13]

III. *Kemsley*: the US proceedings

In *Kemsley*,[14] the United States Bankruptcy Court for the Southern District of New York ruled on its first contested petition for recognition of a foreign proceeding for an individual debtor. While recognising that the many personal moves of the individual in the past years made the decision a difficult one, the US Court concluded the English Proceeding could not be recognised as either main or non-main because the UK was neither the debtor's COMI nor a place of establishment, and, accordingly, the requirements for recognition were not met. Notably, as discussed below, the decision adopted an approach to the timing of determination of COMI that was rejected by a higher court shortly thereafter, but the decision is nevertheless relevant for its discussion of an individual's COMI.

In *Kemsley*, the Foreign Representative sought an order recognising the English Proceeding as foreign main or non-main proceeding,[15] based on the premise that Kemsley's COMI or at least establishment was in the UK because (i) he never intended to live indefinitely in the USA and, thus, his COMI did not move with him when he became a resident of the USA; and (ii) his COMI remained in the UK where the English Proceeding was administered, where his children were, and where he had ongoing personal and business interest. Among other things, the Foreign Representative claimed that the ability to use a spare office in London during business trips and his secondary employment with a UK company should prove an establishment, and, accordingly, allow recognition of the English Proceeding at least as foreign non-main proceeding. Barclays objected to the recognition, stating that Kemsley did not meet the statutory requirements for recognition because his residence was in the US, where he had continuously resided for three and a half years, and the UK was neither his COMI nor establishment.

The circumstances of the chapter 15 filing presented a rather unusual set of facts. In contrast with many other chapter 15 cases, in which the foreign debtors sought protection against creditors to prevent them from obtaining an unfair privilege and bypass the foreign insolvency proceeding and its creditors

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7 This approach is followed by the First, Second, Third, Sixth, Eighth, and D.C. Circuits.

8 *See Goss Int'l Corp. v Man Roland Druckmaschinen Aktiengesellschaft*, 491 F.3d 355, 359 (8th Cir. 2007); *see* also *Quaak v Klynveld Peat Marwick Goerdeler Bedrijfsrevisoren*, 361 F.3d 11, 17 (1st Cir. 2004); *Gen. Elec. Co. v Deutz AG*, 270 F.3d 144, 161 (3d Cir. 2001); *Gau Shan Co. v Bankers Trust Co.*, 956 F.2d 1349, 1355 (6th Cir. 1992); *China Trade & Dev. Corp. v M.V. Choong Yong*, 837 F.2d 33, 35-37 (2d Cir. 1987).

9 This approach is followed by the Fifth, Seventh, and Ninth Circuits.

10 *See Kaepa, Inc. v Achilles Corp.*, 76 F.3d 624 (5th Cir. 1996).

11 11 U.S.C. § 105(a).

12 *Sec. Investor Prot. Corp. v Bernard L. Madoff Inv. Sec., LLC*, 474 B.R. 76, 86 (S.D.N.Y. 2012) (internal citations omitted).

13 *In re JSC BTA Bank*, 434 B.R. 334, 337 (Bankr. S.D.N.Y. 2010).

14 *In re Kemsley*, 489 B.R. 346 (Bankr. S.D.N.Y. 2013).

15 The key difference among the two is that in a foreign main proceeding, certain relief (including the automatic stay) is granted automatically. Relief that is available automatically upon recognition of a main proceeding under Bankruptcy Code section 1520 may be granted at the discretion of the court in a nonmain proceeding if the requirements of Bankruptcy Code sections 1521 or 1507, as applicable, are satisfied.

by seizing the debtors' assets in the US, Barclays was willing to cooperate with the UK trustees for the benefit of all creditors with valid claims in the UK and to ratably share any net recoveries realised in Barclays' lawsuits against Kemsley in the US. The motivation for Barclays' actions can be seen from the passage of the judgment cited at footnote 5 above. Nevertheless, the Foreign Representative failed to reach an agreement with Barclays and, instead, formed an unusual coalition with the debtor – Kemsley, who was also providing indirect financial support to the Foreign Representative to cover his expenses related to the chapter 15 petition. The US Court noted that these facts may indicate that the chapter 15 petition was 'an aspect of a coordinated trans-Atlantic strategy orchestrated by Mr. Kemsley and his advisers to shield [his] assets from enforcement actions by Barclays'.[16] Even though such enforcement actions could have benefitted all creditors in the English Proceeding (based on Barclays' assurances) and the Foreign Representative's actions raised potential conflict issues, these facts were ultimately not directly related to whether the English Proceeding could be recognised under chapter 15 – or, in other words, where Kemsley's COMI or establishment was located.

In the case of an individual, the habitual residence is presumed to be the debtor's COMI in the absence of evidence to the contrary.[17] Habitual residence is not defined, but has been interpreted as the place where an individual resides with the intention of remaining for an indefinite period of time.[18] Judge Peck noted that 'habitual residence includes an element of permanence and stability and is comparable to domicile; it connotes a meaningful connection to a jurisdiction, a home base where an individual lives, raises a family, works and has ties to the community'.[19]

Kemsley's moves from the UK to the US and then within the US required an analysis of not only the place where an individual lives, but the ongoing personal intentions to stay in a certain location for the foreseeable future until a significant change occurs – including one involving the person's family members.[20] Struggling with Kemsley's 'unsettled'[21] life, the US Court found two possible conclusions: (i) Kemsley may have lived in the US without the intention of establishing a habitual residence; and (ii) any of Kemsley's residences in the US became habitual the moment he decided to stay there indefinitely. Any determination based on these premises would be highly subjective, but the US Court relied on a constant theme in Kemsley's testimony: the central role of Kemsley's children and his interest to reside with them. Accordingly, the US Court recognised Kemsley's COMI shifted when he sold his house in the UK and moved to the US with his family in 2009. Next, the US Court found Kemsley's children move to the UK to be a significant change that affected any commitment Kemsley may have had to remaining in the US indefinitely.

Having established two significant points in time, the US Court considered the relevant time to determine a foreign debtor's COMI and sided with a line of cases ruling that the date of commencement of a foreign proceeding is the proper date to determine the foreign debtor's COMI. Kemsley's English Proceeding commenced in 2012, when Kemsley had been residing in the US with his children for over two years. Therefore, the US Court found that Kemsley's COMI at the relevant time was in the US, and not in the UK, and the English Proceeding did not meet requirements for recognition as foreign main proceeding.

The requirements for foreign non-main proceeding were also not met. The US Court found the evidence supporting Kemsley's establishment in the UK inconclusive and insufficient. Specifically, his secondary employment with a UK company, owned and operated by Kemsley's close friend, was based solely on an 'informal arrangement between friends',[22] and any money received was rather an advance than compensation for actual work. In addition, the office space Kemsley purportedly had available during his trips to London was not assigned to him based on a regular schedule, and the US Court found that insufficient to establish that he used it to carry out non-transitory economic activity.[23]

It is notable that *Kemsley* was decided before the ruling, on 16 April 2013, of the United States Court of Appeals for the Second Circuit (its decisions are binding for the US Court) in *Fairfield Sentry*. That ruling resolved a split among decisions and concluded that, for the purposes of recognition under chapter 15, the time of filing of the chapter 15 petition is the relevant time for COMI consideration.[24] Judge Peck had noted

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16 *In re Kemsley*, 489 B.R. at 351-352.
17 11 U.S.C. § 1516(c).
18 *In re Ran*, 607 F.3d 1017, 1022 (5th Cir. 2010).
19 *In re Kemsley*, 489 B.R. at 353.
20 *Id.* at 353.
21 *Id.* at 355.
22 *Id.* at 363.
23 A 'foreign nonmain proceeding' is a foreign proceeding, other than a foreign main proceeding, pending in the country where the debtor has an establishment, which is any place of operations where the debtor carries out a nontransitory economic activity. *See* 11 U.S.C. §§ 1502(2), 1502(5), 1517(b)(2).
24 *Morning Mist Holdings Ltd. v Krys (In re Fairfield Sentry Ltd.)*, 714 F.3d 127 (3d Cir. 2013).

in *Kemsley* that the approach adopted and result might have been different if COMI were tested as of the filing date of the Chapter 15 petition, when Kemsley was living in New York, separated from his children, and testified that he wanted to relocate to London to be closer to his children.

An English view on the recognition proceedings

Testing COMI (as Judge Peck did) as the time of the opening of the foreign proceedings is a familiar approach to English advisors: in England, both for the purpose of the provisions implementing the Model Law, and the EC Regulation on Insolvency Proceedings, the Courts have concluded (or proceeded on the basis) that COMI is tested at the time that the foreign proceedings are 'opened': see *Re Stamford* [2011] Ch 33 at [30]. This is the case, even though it has been noted that the purpose of the two sets of regulations differ (the former dealing with procedural rules of recognition, the latter substantive rules of jurisdiction) such that the approach to timing could differ.[25]

The decision in *Fairfield Sentry* has generally been welcomed in the common law world of off-shore insolvency as providing a sensible method for obtaining US recognition of insolvency proceedings commenced in the place of incorporation even if, prior to the liquidation, the place of incorporation could not be regarded as the location of the entities COMI. But the application of the *Fairfield Sentry* approach to timing (i.e. assessing COMI at the point when the chapter 15 application is made) is likely to give rise to further issues in the context of personal insolvency where the debtor will continue to run his post-bankruptcy affairs separate from (and potentially in a different location from) the administration of the bankruptcy estate. For example, if an English bankruptcy is opened when the debtor's COMI is clearly in England, it would be strange if the fact that the bankrupt has then moved to Australia to start a new life would impact on the ability of the trustee to obtain chapter 15 recognition. The simple answer may be that, as in *Fairfield Sentry*, the focus of the analysis will take into account all factors including the COMI of the estate and administration thereof, which may outweigh (in the context of personal insolvency) the post-bankruptcy conduct of the bankrupt.

Notes

25 See Moss, 'The Chapter 15 timing issue – the mist has cleared' (2013) *Insol. Int.* 122.

CASE REVIEW SECTION

Christian Van Buggenhout and Ilse Van de Mierop, acting as liquidators in the insolvency of Grontimmo SA, C-251/12, CJEU (19 September 2013)

Matthew Abraham, Barrister, South Square, London, UK

Introduction

In the recent decision of *Christian Van Buggenhout and Ilse Van de Mierop v Banque Internationale a Luxembourg SA*, the Court of Justice of the European Union (the 'CJEU') was asked to determine the scope of Article 24(1) of Regulation (EC) No 1346/2000 of May 2000 on insolvency proceedings (OJ 2000 L 160, p. 1) (the 'Regulation'). In particular, whether Article 24(1) must been interpreted as meaning that a payment made on the order of a debtor subject to insolvency proceedings, to one of its creditors, falls within the scope of that provision.

The relevant statutory provisions

Recitals 4, 23 and 30 in the preamble to the Regulation state:

> '(4) It is necessary for the proper functioning of the internal market to avoid incentives for the parties to transfer assets or judicial proceedings from one Member State to another, seeking to obtain a more favourable legal position (forum shopping).
>
> ...
>
> (23) This Regulation should set out, for the matters covered by it, uniform rules on conflict of laws which replace, within their scope of application, national rules of private international law. Unless otherwise stated, the law of the Member State of the opening of the proceedings should be applicable (lex concursus) ...
>
> ...
>
> (30) It may be the case that some of the persons concerned are not in fact aware that proceedings have been opened and act in good faith in a way that conflicts with the new situation. In order to protect such persons who make a payment to the debtor because they are unaware that foreign proceedings have been opened when they should in fact have made the payment to the foreign liquidator, it should be provided that such a payment is to have a debt-discharging effect.'

Article 24 of the Regulation provides:

> '1. Where an obligation has been honoured in a Member State for the benefit of a debtor who is subject to insolvency proceedings opened in another Member State, when it should have been honoured for the benefit of the liquidator in those proceedings, the person honouring the obligation shall be deemed to have discharged it if he was unaware of the opening of proceedings.
>
> 2. Where such an obligation is honoured before the publication provided for in Article 21 has been effected, the person honouring the obligation shall be presumed, in the absence of proof to the contrary, to have been unaware of the opening of insolvency proceedings; where the obligation is honoured after such publication has been effected, the person honouring the obligation shall be presumed, in the absence of proof to the contrary, to have been aware of the opening of proceedings.'

Factual background

The case revolves around the insolvency of Grontimmo SA ('Grontimmo'), a property development company, with its registered office in Antwerp (Belgium). Prior to the opening of insolvency proceedings in relation to Grontimmo, the company acquired a purchase option for EUR 1,400,000 issued by Kostner Development Inc. ('Kostner'). On 2 June 2006, Grontimmo's directors gave Dexia Banque International a Luxembourg ('BIL') a written order to issue a cheque for EUR 1,400,000 for the benefit of Kostner.

Grontimmo was declared insolvent on 4 July 2006 by a judgment of the Tribunal de commerce, Brussels, which had the effect of automatically divesting the company of all its assets. The judgment was published in *Le Moniteur belge* on 14 July 2006 but not in the *Journal official du Grand-Duche de Luxembourg*. On 5 July 2006, BIL, in compliance with the previous order from Grontimmo, issued and encashed a cheque for EUR 1,400,000, for the benefit of Kostner, for the payment of the purchase option (the 'Sums').

On 21 September 2006, Grontimmo's liquidators demanded that BIL repay the Sums forthwith on the basis that the payment was in contravention of the automatic divestment of Grontimmo's assets upon the opening of insolvency proceedings. BIL refused to repay the Sums on the ground that it had been unaware of the insolvency proceedings and that it could rely on Article 24 of the Regulation.

Question referred

The referring court in Belgium was uncertain on whether BIL could rely on Article 24 of the Regulation and so referred the following question:

> 'How should the words "obligation for the benefit of a debtor" in Article 24 of Regulation (EC) No 1346/2000 of 29 May 2000 be interpreted? Must those words be interpreted as including a payment made to a creditor of the insolvent debtor at the latter's request, in the case where the party which honoured that payment obligation on behalf and for the benefit of the insolvent debtor did so while unaware of the existence of insolvency proceedings which had been opened against the debtor in another Member State?'

Decision and reasoning of the CJEU

As a preliminary point the CJEU observed that although the Regulation contained various conflict of laws rules, Article 24 is not such a rule and is instead a provision of substantive law which applied in each Member State independently of the *lex concursus*.

The CJEU provided two lines of reasoning when coming to its decision in relation to the interpretation of Article 24.

First, the CJEU took a literal approach to interpretation holding that the ordinary meaning of the expression 'for the benefit of', does not, *prima facie*, cover the situation in which an obligation is honoured on the order of that person for the benefit of one of its creditors. In support of this the Court relied on the following:

(1) the various versions of the Regulation, in particular, the Spanish ('*a favor de*'), French ('*au profit du*'), Italian ('*a favore del*'), Dutch ('*ten voordelen van*') and Portuguese ('*a favor de*');

(2) the German and English version of Recital 30 which states that the situation covered by Article 24(1) relates to a 'payment' to the insolvent debtor; and

(3) the fact that Article 24(1) makes it clear that the Article concerns the debts of the insolvent debtor which have become debts of the general body of creditors after the opening of insolvency proceedings.

Second, the CJEU took a purposive interpretation with regard to the aim of Article 24(1) of the Regulation. The CJEU found that:

(1) Recital 30 made it clear that Article 24 enables situations which conflict with the new situation created by the opening of the insolvency proceedings to fall outside the liquidator's control;

(2) Article 24 permits the assets belonging to the general body of creditors to be reduced by the debts of the insolvent debtor paid to the latter by its debtors in good faith; and

(3) if the wide interpretation sought was allowed, the insolvent debtor could, via third parties who are unaware of the opening of insolvency proceedings, transfer the assets to that creditor and thereby undermine one of the principal objectives of the Regulation as set out in recital 4.

Conclusion

As a result of the CJEU's decision it is clear that the protection afforded under Article 24 of the Regulation, to third parties who make payments in good faith without knowledge of the opening of the insolvency proceedings, will not apply when payments are made on behalf of the debtor to one of its creditors. In order to fall within Article 24's protection a party will need to show that payment was made for the direct benefit of the insolvent debtor.

In situations where party A, honouring a debt obligation owed to party B, makes payment to party C who is party B's creditor, it will be essential for party A to check whether insolvency proceedings have been opened in relation to party B in any Member State. Until there is a unified search point to check for the opening of insolvency proceedings within the EU this may be a process that is difficult although necessary.

CASE REVIEW SECTION

Vivendi SA v Richards [2013] EWHC 3006 (Ch)

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Introduction

Vivendi SA v Richards [2013] EWHC 3006 (Ch) is an important decision of Mr Justice Newey as to the duties of shadow company directors. The claim was brought by Vivendi SA ('Vivendi') having been assigned the rights to the action by the liquidators of the second claimant Centenary Holdings III Limited ('CH3'). Vivendi brought proceedings against Stephen Bloch (who had been a de jure director of CH3) and Murray Richards (who it alleged was shadow director) for breach of duty in respect to over GBP 10 million in payments made by CH3 prior to its winding-up. As will be discussed below, Newey J considered that the hither-to leading authority *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 (Ch) understated the extent to which shadow directors owed fiduciary duties.

Factual background

CH3 became part of the Vivendi group in 2000 but by 2003 was no longer trading. In addition to some valuable assets, CH3 held a number of leases but which represented significant liabilities. The most significant of its leases was in respect to a property in Hammersmith called the Ark, for which a GBP 35.4 million provision had been made in its 2002 accounts. CH3 had no right to terminate its leases until the end of 2010 or early 2011 and the Ark's annual rent and related charges amounted to GBP 6.5 million. Vivendi wished to dispose of a number of the group's non-core assets including the Ark.

Mr Richards' brother, Mr Harrod, was the financial controller of CH3's parent company, and had been asked by Mr Richards to look out for projects for him. However, CH3 could not assign its leases in the Ark to one of Mr Richards' companies because the freehold owner required the leaseholder to have a triple-A rating. The solution chosen instead was for Vivendi to transfer CH3 itself, having first removed various assets, and for there to be a reverse premium of GBP 15 million to take account of CH3's lease obligations. A complicated series of steps was undertaken which resulted in CH3 becoming owned by a company indirectly beneficially owned by Mr Richards.

On the day of completion on 22 January 2004, Mr Bloch (who had known Mr Richards since the mid-1990s) became CH3's sole director. In July 2005, Mr Harrod became a full-time employee of CH3. Mr Richards was appointed under a consultancy agreement dated March 2004 to provide consultancy services to CH3, with his express obligations including the requirement to 'well and faithfully serve CH3' and 'use his best endeavours to promote the interests of CH3'. Under the agreement, an up-front payment of GBP 600,000 was made by CH3 to one of the companies beneficially owned by Mr Richards.

Notwithstanding that the mechanics of CH3's transfer had assumed that rental income would be generated by letting the Ark, no rental income at all was produced by the time CH3 went into liquidation in 2005. A dividend of GBP 5.314 million had been declared and paid nonetheless. On 9 June 2005, Mr Bloch passed a resolution for a petition to be presented for CH3 to be wound up, which was duly presented and liquidators were appointed.

Vivendi's claim

The claim related to various payments made by CH3 between March 2004 and February 2005, namely (i) the consultancy agreement payment, (ii) the dividend, and (iii) 7 payments totalling GBP 4.157 million by way of loans and investments to various companies some of which were controlled by Mr Richards.

Vivendi's case was that Mr Bloch acted in breach of the duty of good faith (or loyalty) in procuring CH3 to make these payments, and that Mr Richards owed and breached similar obligations as a shadow director, and also dishonestly assisted Mr Bloch's breaches of duty. The proceedings were not issued until May 2011, more than 6 years after the last of the payments were made. As a result, Vivendi accepted that its claims would be statute barred unless it could rely on subsection 21(1) of the Limitation Act 1980 ('the 1980 Act'), of which paragraph (a) made it essential that Vivendi establish dishonesty on the part of the directors.

Mr Richards as a shadow director

Under section 741 of the Companies Act 1985 and now section 251 of the Companies Act 2006, a shadow director is 'a person in accordance with whose directions or instructions the directors of the company are accustomed to act', but a person will not be considered a shadow director 'by reason only that the directors act on advice given by him in a professional capacity'.

Mr Richards and Mr Bloch denied that the latter acted on instructions from the former. Newey J considered the evidence which included documents showing Mr Richards' involvement in the main business activities of CH3, namely the Ark and dealing with the money left in the company. For example, Mr Richards engaged with the professional advisors of CH3 but the same could not be said for Mr Bloch. By his own account Mr Richards found the projects in which CH3 invested. There was no compelling evidence showing that Mr Bloch sought to negotiate the consultancy agreement. In respect to some of the investments, the documentary evidence showed that Mr Bloch simply did what he was asked by Mr Richards.

Moreover, in cross-examination Mr Richards stated that 'Stephen [Bloch] usually sought ultimate shareholder support from me on just about – well, probably everything he did.' Equally, in his own evidence, Mr Bloch stated that because of Mr Richards' non-domicile status, if 'he was involved in any property or other development work involving UK companies he would need nominees or representatives on his behalf and he had in mind that I would be his "legman" for what I later learned was [CH3].'

Newey J concluded that Mr Bloch was accustomed to act in accordance with directions or instructions from Mr Richards and, hence, that Mr Richards was a shadow director of CH3. The Judge stated:

> 'In my view, the word "legman" accurately encapsulates Mr Bloch's role. He was not a mere cipher, paid for doing nothing of any substance. He will have spent significant amounts of time on matters relating to CH3 and other companies associated with Mr Richards and been privy to at least much of Mr Richards' thinking. But he was not his own man: he acted on instructions from Mr Richards. He gave effect to Mr Richards' decisions.' ([130])

Shadow director duties

Having traced the legislative history in respect to shadow directors back to the Companies (Particulars as to Directors) Act 1917, Newey J considered the case law which referred to fiduciary duties owed by shadow directors. In *Yukong Line Ltd of Korea v Rendsburg Investments Corp of Liberia* [1998] 1 W.L.R. 294 Toulson J held that a shadow director owed a fiduciary duty which he breached when funds were removed from the company's bank account. A similar approach was adopted by Ferris J in *John v Price Waterhouse*, unreported, 11 April 2001. Newey J referred to the Law Commission's endorsement of Toulson J's view in its 1998 consultation on company director duties, which suggested that the better view was that a shadow director was to be regarded as akin to a de facto director and could incur the liability of a de jure director where they effectively acted as a director through the people they influence.

However, these authorities needed to be contrasted to *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 (Ch); [2006] F.S.R. 17 at [1289] where Lewison J had concluded that:

> 'The indirect influence exerted by a paradigm shadow director who does not directly deal with or claim the right to deal directly with the company's assets will not usually, in my judgment, be enough to impose fiduciary duties upon him; although he will, of course be subject to those statutory duties and disabilities that the Companies Act creates. The case is the stronger where the shadow director has been acting throughout in furtherance of his own, rather than the company's, interests. However, on the facts of a particular case, the activities of a shadow director may go beyond the mere exertion of indirect influence.'

Newey J referred to the fact that the *Ultraframe* decision had received a mixed reception, and that at the heart of Lewison J's reasoning was the idea that the imposition of fiduciary duties depended on the person concerned having undertaken or assumed a responsibility. Having referred to a number of authorities supporting such a proposition, Newey J stated for it to be reconciled with the case law it must be by dint of two features. Firstly, the question of whether such an undertaking existed had to be determined on an objective basis because a trustee will not escape fiduciary duties because they did not want to assume them. Secondly, the taking on of the role must be capable of implying the undertaking of responsibility. Newey J cited *White v Jones* [1995] 2 AC 207 at 271 where Lord Browne-Wilkinson stated that the paradigm circumstances where equity imposed a fiduciary relationship was where a person assumed to act in relation to the affairs of another and therefore was taken to have assumed certain duties in relation to the conduct of those affairs, with the examples given including a company director who assumes responsibility for the affairs of the company.

Newey J stated that in his view *Ultraframe* understated the extent to which shadow directors owe fiduciary duties because:

> 'It seems to me that a shadow director will typically owe such duties in relation at least to the directions or instructions that he gives to the de jure directors. More particularly, I consider that a shadow director

will normally owe the duty of good faith (or loyalty) discussed below when giving such directions or instructions. A shadow director can, I think, reasonably be expected to act in the company's interests rather than his own separate interests when giving such directions and instructions.' ([143])

Applying the authorities including *White v Jones*, the Judge justified his conclusion that shadow directors would commonly owe fiduciary duties 'at least to some degree' with the following points:

'i) A shadow director will have assumed to act in relation to the company's affairs (to adapt Lord Browne-Wilkinson's words in *White v Jones*) and to ask the de jure directors to exercise powers that exist exclusively for the benefit of the company;

ii) A person who gives directions or instructions to a company's de jure directors in the belief that they will be acted on can fairly be described as assuming responsibility for the company's affairs, at least as regards the directions or instructions he gives;

iii) Although Parliament has not designated shadow directors as directors for all purposes in the Companies Acts, it has provided for important consequences to flow from the status.... Such provisions presumably reflect a perception that a shadow director can bear responsibility for a company's affairs;

iv) There is a compelling analogy with the position of promoters. Promoters owe fiduciary duties as a result of their acceptance and use of powers "which so greatly affect the interests of the corporation". A shadow director, too, can be said to choose to make use of powers which "greatly affect the interests of the corporation";

v) A shadow director's role in a company's affairs may be every bit as important as that of a de facto director, and de facto directors are considered to owe fiduciary duties;

vi) That a shadow director may not subjectively wish to assume fiduciary duties cannot matter as such;

vii) Public policy, so far as it may matter, points towards fiduciary duties being imposed on shadow directors.' ([142])

Here, the consultancy agreement provided an additional reason for concluding that Mr Richards had fiduciary duties given the express provisions requiring loyalty. Newey J accordingly concluded that Mr Richards was subject to the fiduciary duty of good faith in relation to the instructions he gave to Mr Bloch.

Duty of good faith

Applying *West Mercia Safetywear Ltd v Dodd* [1988] BCLC 250 and subsequent authorities, Newey J said he was under no doubt that in the present case the interests of creditors needed to be taken into consideration. On the evidence it was apparent that CH3 was insolvent from January 2004 and that those associated with CH3 were well aware of its fragility.

The Judge firstly considered the circumstances of the six payments that were made to the various companies between December 2004 and February 2005. He concluded that none of them were made in the interests of CH3 or its creditors, and that Mr Richards and Mr Bloch did not believe they were. In reality, the directors were seeking to extract CH3's remaining cash before it failed. The purpose of the transactions was to thwart the company's landlords rather than benefit them; to ensure that one of the companies beneficially owned by Mr Richards did not owe money to CH3 on its liquidation; and to benefit Mr Richards or companies associated with him.

Newey J considered separately the question of a particular loan made in January 2005, which he said was less clear-cut. However, the lending was known to be made in a distressed situation with the loan agreement providing for an unremarkable return; detailed due diligence had not been conducted; and it had been apparent that CH3 had no money to spare. On balance the payment was not in the interests of CH3 or its creditors.

As to the GBP 5.314 million dividend, the Judge stated this served to remove more than a third of the money that Vivendi had left in the company even though CH3's planned business activities had failed and no steps had been taken to generate rental income from the Ark. As such, CH3 was obviously going to find itself unable to meet its obligations to its landlords relatively soon, and this fact had been highlighted at the time by Mr Harrod to Mr Richards. Whilst the directors claimed the dividend was to be used to generate money which would be passed down to CH3, this was unsupported on the evidence. Newey J therefore concluded that the chances were that the dividend was paid with a view to extracting money in advance of CH3's failure, and that it was not made in the interests of CH3 or with any proper regard to the interests of the creditors.

In addition, the Judge rejected the directors' justification for the GBP 600,000 paid upfront under the consultancy agreement, and likewise considered that it was motivated by a desire to extract money from CH3 before its failure, and was not entered into because either Mr Bloch or Mr Richards considered it to be in the best interests of CH3 or its creditors.

Accordingly, Newey J held that Mr Bloch and Mr Richards acted in breach of duty in causing CH3 to make these various payments.

Dishonesty and limitation

The Judge reviewed the authorities in respect to section 21(1) of the 1980 Act and dishonest assistance. These included *Armitage v Nurse* [1998] Ch 241 at 251, 260 where the Court of Appeal held that section 21(1)(a) was 'limited to cases of fraud or fraudulent breach of trust properly so called, that is to say to cases involving dishonesty' and that a trustee will be acting dishonestly if he 'acts in a way which he does not believe is in … interests [of the beneficiaries]'. In addition, in *Starglade Properties Ltd v Nash* [2010] EWCA Civ 1314 at [39] Morritt C observed that 'The deliberate removal of the assets of an insolvent company so as entirely to defeat the just claim of a creditor is, in my view, not in accordance with the ordinary standards of honest commercial behaviour, however much it may occur.'

Newey J held that both individuals had been dishonest, acting in ways that they did not believe were in the interests of CH3 or its creditors, instead seeking to extract money before the company failed. Applying by analogy *Starglade Properties*, he found that their conduct was also contrary to the normal acceptable standard of honest behaviour. The claims for their breach of fiduciary duty were therefore not statute barred. In respect to the additional allegation of dishonest assistance, the Judge found that Mr Richards procured the breaches of duty that Mr Bloch committed, applying the Court of Appeal's decision in *Williams v Central Bank of Nigeria* [2012] EWCA Civ 415 (which it should be noted was subsequently overruled on appeal by the Supreme Court [2014] UKSC 10).

Dismissing the other defences proffered by Mr Richards and Mr Bloch, Newey J held that Vivendi's claim succeeded against them both.

Comment

Given the criticisms of the *Ultraframe* decision, Newey J's judgment is a welcome rebalancing of the law as to the duties of shadow directors. Moreover, in the particular context of an insolvent company, it shows that the obligation to consider the interests of creditors can apply not simply to formally appointed directors but to those who direct their decisions.

Only a month after being handed down, the decision was followed by the President of Family Division in *R v R* [2013] EWHC 4244 (Fam) at [10] who expressly agreed with Newey J's reasoning. More recently, giving the Court of Appeal's decision in *Sukhoruchkin v Van Bekestein* [2014] EWCA Civ 399 at [40]-[41], the Chancellor cited without apparent criticism the conclusions reached at [142]-[143] of Newey J's judgment. However, he proceeded to refer to the differing approaches in *Ultraframe* and *Vivendi* and suggested that 'the law is not entirely settled as to the circumstances in which a shadow director owes fiduciary duties'. Clearly, the important issue of the duties held by shadow directors remains an area where further development is required.

CASE REVIEW SECTION

Crystal Palace FC Limited & another v Kavanagh & others [2013] EWCA Civ 1410: Administrator Wins on Points Difference

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Introduction

The administrator of any insolvent business who needs to make employees redundant will inevitably face the provisions of two, sometimes conflicting, regimes. The Transfer of Undertakings (Protection of Employment) Regulations 2006 (SI 2006/246) ('TUPE') protect employees on the transfer of their employer's business, but is frequently a source of tension with the regime implemented by insolvency legislation where such a transfer takes places in respect of a business in an administration. Whilst TUPE protects the interests of employees, one of the goals of the administration regime is to achieve the best result for the company's creditors as a whole, rather than its employees.

As explained below, Regulation 7 of TUPE addresses this inherent tension, at least to some extent, and it is with this Regulation that the *Crystal Palace* case is concerned. The Court of Appeal in this case, on appeal from a decision of the Employment Appeal Tribunal, provides some useful guidance as to how that provision operates, though it is recognised that their application is highly fact specific. Notwithstanding that the application of Regulation 7 of TUPE is so fact specific though, administrators can certainly take some comfort from the Court of Appeal's decision, which allowed the appeal restoring the decision of the Employment Tribunal.

The Court of Appeal recognised that, although an administrator will often have the ultimate goal of selling the company's business, it does not automatically follow that any dismissals are made with a view to making the business more attractive to a potential purchaser, thus avoiding what seemed to follow from the Employment Appeal Tribunal's decision, that liability for dismissals where a sale of the business is contemplated will almost always pass to the transferee. This matters from an insolvency point of view because, where the transferee assumes liability under TUPE, the purchase price will often be reduced to take that liability into account and that obviously means there is less money available to pay the insolvent company's creditors as a whole.

The Regulations

Regulation 7 of TUPE provides that where either before or after a relevant transfer an employee of the transferor or transferee is dismissed, the employee shall be treated as unfairly dismissed if the sole or principal reason for his dismissal is:

'(a) the transfer itself; or

(b) a reason connected with the transfer that is not an economic, technical or organisational reason entailing changes in the workforce.'

Under Regulation 4 of TUPE where the dismissal of a transferor's employee is treated as unfair pursuant to Regulation 7, liability in respect of the dismissal is transferred to the transferee. That being the case, whether or not the sole or principal reason for the transfer is the transfer itself or a reason connected with the transfer is of huge importance. Similarly, if the sole or principal reason for the transfer is a reason connected with the transfer, it is crucial to determine whether that reason is an economic, technical or organisational reason entailing changes in the workforce ('an ETO reason').

Prior to the *Crystal Palace* case, the question of what amounts to an ETO reason had been the subject of much discussion, and some case law.

The *Spaceright* decision

Spaceright Europe Limited v Baillavoine [2012] ICR 520 concerned the dismissal by administrators of the Chief Executive of a company in administration, on the day the company went into administration. A few weeks later the company's business was sold and, in the context of that sale it fell to be determined whether the reason for the Chief Executive's dismissal was an ETO reason. The Court of Appeal (as well as the Employment Tribunal and the Employment Appeal Tribunal) concluded that, the reason for the Chief Executive's dismissal was connected with the transfer, but it was not an ETO reason.

It is, in particular, worth noting what Mummery LJ (with whom Sir David Keene and Richards LJ agreed) at paragraph 47:

> 'For an ETO reason to be available there must be an intention to change the workforce and to continue to conduct the business, as distinct from the purpose of selling it. It is not available in the case of dismissing an employee to enable the administrators to make the business of the company a more attractive proposition to prospective transferees of a going concern.'

On the facts of that case, the Court of Appeal concluded that the Chief Executive was dismissed because a purchaser of the business would not require such an officer. As such the reason for the dismissal did not relate to the conduct of the business as a going concern and, therefore, it was not an ETO reason.

The facts

What does, or does not, amount to an ETO reason came before the Court of Appeal again in the *Crystal Palace* case, though in quite a different factual context.

The Claimants in the *Crystal Palace* case were employees of an insolvent football club, Crystal Palace Football Club (2000) Limited ('the Company'), which went into administration in January 2010. The administrator's aim was to sell the club as a going concern. Progressing a sale, however, proved difficult because a purchaser, who had been given preferred bidder status, wanted to purchase Selhurst Park stadium, as well as the club, the stadium being owned by another company which was also in administration, although with different administrators having been appointed.

In view of the stalling negotiations, together with the club's cashflow problems, the Company's administrator decided to '*mothball*' the club over a period when no games would be played. As part of that the Claimants were made redundant in May 2010.

Once there had been a sale, the Claimants argued that Regulation 7 of TUPE was engaged and, moreover, that liability for their dismissals passed to the transferee.

It was not in dispute that the principal reason for the transfers was not the transfer itself. Rather, the issue was whether it was a reason connected with the transfer that was not an ETO reason.

ET and EAT decisions

The Employment Tribunal concluded that the reason for the dismissals was connected with the transfer, but that it was an ETO reason and therefore that liability arising out of the dismissals remained with the Company rather than passing to the transferee. The Claimants appealed.

The Employment Appeal Tribunal, on the employees' appeal, held that they had *not* been dismissed for an ETO reason, so that liability in respect of their dismissals had indeed passed to the transferee.

The Employment Appeal Tribunal's reasoning drew on the decision in the *Spaceright* case. As touched on above, in the *Spaceright* case the Court of Appeal concluded that where the reason for a dismissal is to continue to conduct the business that is an ETO reason, but where the dismissal is part and parcel of a process with the purpose of selling the business it cannot be such a reason.

On the facts, the Employment Appeal Tribunal considered, the administrator did not intend to carry on the Company's business so much as to preserve it so that it could be sold. As such, it was held that the reason for the Claimants' dismissals was the sale of the business, rather than continuing to conduct that business. That being the case, the Employment Appeal Tribunal held, applying the guidance given in the *Spaceright* case, there was no ETO reason operating on the facts.

The Court of Appeal

The Court of Appeal allowed the appeal, restoring the Employment Tribunal's decision. Much of the Court of Appeal's reasoning was concerned with the *Spaceright* case and the ways in which the facts of that case differed from those presently before it, the Court of Appeal taking the view that that case could be distinguished.

The facts of this case were very different to the facts of *Spaceright*. Maurice Kay LJ, delivering the leading judgment, distinguished *Spaceright* on the basis that in that case it was always contemplated that the dismissed Chief Executive would be replaced (which indeed he was) and therefore there was no reduction in the workforce, merely a dismissal to make a sale more attractive to a prospective purchaser. Briggs LJ in his supporting judgment added that the application of *Spaceright* should be confined to its factual context.

The nature of the football business, where the main assets are often player contracts, is one in which the liquidation value is normally low. Since one of the objectives of administration is achieving a better result for creditors as a whole than would be likely if the company were wound up, a sale of the business is commonly required in order to achieve the purpose. However, continuation of that company's business is often a prerequisite to a beneficial sale and dismissing employees is a principal method by which an administrator can continue the business. The Court of Appeal found that the Employment Tribunal had correctly separated the administrator's objective in dismissal of the employees in order to continue the business from his ultimate objective of selling the club as a going concern.

Briggs LJ appropriately referred to Regulation 7 as 'the tie breaker' as to how to resolve the conflict between TUPE and the insolvency code. He observed that if the administrator's overall objective to sell the company is applied as the sole or principal reason for any dismissal, then the ETO exception to Regulation 7(1) will never or hardly ever apply.

Comment

The *Crystal Palace* case is interesting from the point of view of the interaction between the legislation dealing with the position of employees on the transfer of the undertaking of their employer and the regime dealing with companies in financial difficulties in administration. The scope of tension between those regimes is noted above, but it is emphasised that the purchase price, and therefore the return to creditors, is tied up with the question of whether liability passes under TUPE.

The Court of Appeal did rightly recognise that the application of Regulation 7 of TUPE is a fact sensitive issue and, of course, the facts of this case were somewhat unusual in that they related to the business of a football club, which is seasonal.

Nonetheless the case does provide some guidance as to how the Regulation works. The Court of Appeal recognised that an administrator will often have the ultimate aim of selling the business as a going concern, but this does not entail that all decisions will be taken to make the business more attractive to a purchaser. Had the Court of Appeal reached a different conclusion, it would seem to have entailed that nearly any dismissal by an administrator intending a going concern sale would result in liability being passed to the transferee, regardless of whether the dismissals in issue were necessary to keep the business going.

In the circumstances, administrators, and general creditors, can therefore take some comfort from the Court of Appeal's decision in this case, which certainly broadens (or rebroadens) the scope of relying on an ETO reason where an administrator's immediate aim is to continue trading the company's business.

Schmid v Hertel

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Introduction

The First Chamber of the Court of Justice of the EU (the 'Court of Justice') handed down, on 14 January 2014, its decision in the case of *Ralph Schmid (acting as liquidator of the assets of Aletta Zimmermann) v Lilly Hertel* (Case C-328/12).

The decision sheds critical light on the scope of the Council Regulation (EC) No. 1346/2000 (the 'Insolvency Regulation'), in particular by holding that Article 3(1) of the Insolvency Regulation[1] means that the Court of a Member State within whose territory insolvency proceedings have been opened has jurisdiction to hear and determine an action to set aside a transaction (or '*actio pauliana*') that has been brought against a person who does not reside within a Member State (in this case, in Switzerland).

Background

Mr Schmid was appointed in 2007 as the 'liquidator' of the assets of Aletta Zimmermann. Insolvency proceedings were opened in Germany against Ms Zimmerman on 4 May 2007: these were main proceedings for the purposes of Articles 3(1) and 27 of the Insolvency Regulation; there were no secondary proceedings opened in another Member State nor any element of the case involving any Member State other than Germany.[2]

Mr Schmid issued proceedings in the German Courts against Ms Hertel, the latter being resident in Switzerland, to set aside a transaction that had been entered into between Ms Zimmermann and Ms Hertel and, thereby, to recover EUR 8,015.08 (plus interest) for the insolvent estate from Ms Hertel.[3] Mr Schmid's action was dismissed as inadmissible by the lower German Courts, both at first instance and on appeal, on the ground that the German Courts did not have international jurisdiction.[4]

Mr Schmid appealed the decision of the lower Courts to the German Federal Court of Justice on a point of law. The German Federal Court stayed the proceedings, concluding that the outcome of the dispute depended on the interpretation of Article 3(1) of the Insolvency Regulation, and requested a preliminary ruling under Article 267 TFEU on the following question:

> 'Do the courts of the Member State within the territory of which insolvency proceedings regarding the debtor's assets have been opened have jurisdiction to decide an action to set a transaction aside by virtue of insolvency that is brought against a person whose place of residence or registered office is not within the territory of a Member State?'

Decision of the Court of Justice

It fell to the Court of Justice to determine the scope of Article 3(1) which provides as follows:

> 'The courts of the Member State within which 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.'

The Court of Justice, agreeing with the Opinion of Advocate General Sharpston (delivered on 10 September 2013), held that Article 3(1) must be construed as meaning that the Court of a Member State within whose territory insolvency proceedings have been opened has jurisdiction to hear and determine an action to set aside a transaction that has been brought against a person who does not reside within a Member State.

In this way, the Court of Justice built on its decision in *Seagon* (Case C-339/07), where the Court of Justice had held that the Court of a Member State within whose territory insolvency proceedings have been opened has jurisdiction to hear and determine a

Notes

1 References to Articles refer, unless stated otherwise, to the Insolvency Regulation.
2 See the Opinion of Advocate General Sharpston (delivered on 10 September 2013), at paragraph [15].
3 See *ibid.*, at paragraph [15].
4 See *ibid.*, at paragraph [16].

set aside application that has been brought against a person who does reside within another Member State.

However, in *Schmid v Hertel*, the Court of Justice effectively rejected the view, which has been espoused in particular by certain German academics, that the Insolvency Regulation will only apply where there are connecting factors between two or more Member States, with the result that it will not apply to an application brought within insolvency proceedings opened in a Member State against a person resident outside of the EU. The Court of Justice held that such a limited view of the scope of Article 3(1) was wrong inter alia because such a limited view does not follow from and is not suggested by Article 1 (which provides that the Insolvency Regulation shall apply to collective insolvency proceedings); Annex A (which sets out the different kinds of insolvency proceedings to which Article 2(1) refers); or Recital 14 in the preamble to the Insolvency Regulation (which suggests that the application of the Insolvency Regulation is only precluded where the debtor's COMI is not located in the EU).

More particularly the Court of Justice, referring to Recitals 2 to 4 and 8, noted as follows (at paragraph [25]) of the decision; emphasis added):

> 'Recital 8 refers to the objective of "improving the efficiency and effectiveness of insolvency proceedings having cross-border effects" and recital 12 states that insolvency proceedings falling within the Regulation's field of application "have universal scope and aim at encompassing all the debtor's assets". *The latter objectives may encompass not solely relations between Member States but, by their nature and in accordance with their wording, any cross-border situation*.'

As regards the effect of the decision in *Staubitz-Schreiber* (Case C-1/04), the Court of Justice concluded that application of Article 3(1) does not depend on there being some connecting cross-border feature involving another Member State.

Accordingly, the reasoning of the Court of Justice points up the very different jurisdictional spirit of the Insolvency Regulation compared, in particular, with the Brussels I Regulation (Council Regulation (EC) No. 44/2001) (the 'Judgments Regulation'):

(1) The Judgments Regulation, which relates to the main run of civil and commercial matters (save for well-defined exceptions such as insolvency proceedings), is geared towards favouring and protecting the defendant.

(2) The spirit of the Insolvency Regulation is quite distinct: its primary aim is to ensure that debtors cannot engage in forum-shopping at the expense of their creditors; that there are certain and predictable criteria to determine a debtor's COMI.

(3) Accordingly, the Court of Justice is not inhibited in the context of insolvency proceedings opened in a Member State to permit a person resident outside of the EU to become subject to the jurisdiction of the Court in which such insolvency proceedings have been opened.

(4) The Court's justification for taking this approach in the context of insolvency proceedings, and its defence to the criticism that a defendant to a set aside application becomes subject to a jurisdiction with which he or she may have no connection, lies in the issue of the COMI determination process, specifically that it 'is normally foreseeable for the defendant, who may take it into account at the time when he participates, with the debtor, in an act liable to be set aside in insolvency proceedings. Accordingly, the objectives of foreseeability of jurisdiction as regards bankruptcy and liquidation and of legal certainty, resulting from recital 8 in the preamble to the Regulation, and, as the case may be, the objective of avoiding incentives for the parties to transfer assets from one Member State to another, or to choose a particular forum, in order to obtain a more favourable legal position, referred to in recital 4, prevail over the concern to avoid the defendant being sued in a foreign court' (paragraph [35]).

A further criticism of the judgment might be that, even if the Court of Justice has not caused the Insolvency Regulation to overreach itself as a matter of jurisdiction, in any event the extension of the scope of Article 3(1) to include a set aside application that is brought against a resident of a non-Member State is futile since the Courts of the third country in question would not be obliged to recognise or enforce the judgment on the action. The Advocate-General's answer to this anticipated criticism, which the Court of Justice approved (see paragraphs [37] onwards), is threefold:

(1) The fact that the Insolvency Regulation cannot bind third countries does not in itself limit the scope of the application of Article 3(1) (i.e. questions of recognition and enforcement are for the Court of the third country rather than for the Court of the relevant Member State in which insolvency proceedings have been opened);

(2) If, in a given case, the Insolvency Regulation does itself not assist in comforting a third country Court that it should recognise and enforce a judgment on such a set aside application, there may be bilateral treaties or other mechanisms which would enable such recognition or enforcement; and

(3) Even if a third country's Courts were not to recognise or enforce such a judgment, this would be no bar to the Courts of other Member States recognising and enforcing such a judgment under Article 25.

It is the third answer of the answers set out above that offers the key to understanding the rationale Court of Justice's approach to the scope of Article 3(1). In essence, the Court of Justice has taken a practical approach to the question of recognition and enforcement. In principle, *Schmid v Hertel* will in some cases extend the scope of Article 3(1) beyond the point of being of any practical assistance to a liquidator or other office holder, for example where the third party Court refuse to recognise or enforce and the defendant has no assets in any Member State. However, in practical terms, *Schmid v Hertel* will assist the office holder wherever a defendant who is found liable on a relevant action holds assets within any Member State (see reason (3) above), since in such circumstances the office holder may enforce against those assets irrespective of whether or not the Courts of the third country in which the defendant resides are prepared to recognise and enforce the judgment.

CASE REVIEW SECTION

In the matter of APCOA Parking (UK) Ltd & Ors [2014] EWHC 997 (Ch)

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Introduction

Over the past few years the question of whether the English Courts have jurisdiction to sanction a scheme of arrangement, in relation to a foreign company, has been central to the European restructuring market.

The remit of the English Courts' jurisdiction to sanction a scheme of arrangement in relation to a non-domestic company has been expanded by the recent decision of Hildyard J in *APCOA Parking (UK) Ltd & Ors* [2014] EWHC 997 (Ch).

Hildyard J, as discussed below, was faced with the issue of whether the English Courts have jurisdiction to sanction a scheme in relation to a foreign company with its COMI outside the UK and where the sole basis for establishing jurisdiction was as a result of amendments to the governing law and jurisdiction clauses of the company's principal finance documents to English law (the 'Scheme').

Factual background

The Scheme related to nine companies (the 'Scheme Companies') that formed part of the German based APCOA Parking Group ('APCOA'). APCOA is the leading European car park operator that offers over 1.3 million parking spaces at some 7,413 locations, and has over 4,500 employees. APCOA is centrally managed from Germany by its holding company.

There are in total 39 subsidiaries in the group that are located in 12 countries. Out of the nine Scheme Companies, only two companies were incorporated in England. Of the remaining companies, two were incorporated in Germany, two in Norway and one each in Belgium, Austria and Denmark (the 'Foreign Scheme Companies').

Each of the Scheme Companies was a borrower under a facilities agreement dated 23 April 2007 that was, at inception, governed by German law and subject to the exclusive jurisdiction of the courts of Frankfurt/Main (the 'Facilities Agreement'). The Facilities Agreement was due to mature on 25 April 2014 (the 'Maturity Date') which was prior to the completion of the group's ongoing restructuring. In order for the Maturity Date to be extended under the terms of the Facilities Agreement unanimous consent of all of the creditors was required. As a result of this, the group sought to implement the Scheme as a way of extending the Maturity Date without having to obtain unanimous consent. The Scheme only required the majorities prescribed by Part 26 of the Companies Act 2006 ('CA 2006') for the Maturity Date to be extended.

Prior to proposing the Scheme the governing law and jurisdiction clauses of the Facilities Agreement were amended to English law and the English Courts respectively. The amendments to the governing law and jurisdiction were effected by the requisite majority of creditors as set out under specific provisions contained in the Facilities Agreement. The group obtained uncontested evidence of local law that stated that the amendments to the Facilities Agreement and an order sanctioning the Scheme would be recognised in each of the jurisdictions where the Foreign Scheme Companies were incorporated.

Jurisdictional issue

The English Courts' jurisdiction to sanction a scheme of arrangement is found in s.895 CA 2006 and relates to whether or not the English Courts have jurisdiction to wind up the company in question. 'Company' for the purposes of the CA 2006 is defined as 'any company liable to be wound up under the Insolvency Act 1986'. Sections 220 and 221(1) of the Insolvency Act 1986 ('IA 86') give the English Courts the power to wind up foreign companies.

The IA 86 does not itself set out any jurisdictional restrictions that refer to the company's place of incorporation, centre of main interest ('COMI') or establishment. The English Courts however have set out three conditions for the making of a winding up order in relation to a foreign company. Of particular importance to the issue arising out of the Scheme is the condition that the foreign company has a sufficiently close connection with England. For further analysis of the law relating to the conditions for the winding up of a foreign company and their application in the context of schemes of arrangements see the decision of Collins J in *Re Drax Holdings Ltd* [2004] 1 BCLC 10.

In many schemes of arrangement the question of whether there is a sufficient connection with England often requires looking at either: (i) the COMI of the company in question; or (ii) the finance documents of the company and in particular the combination of the lenders' choice of governing law and jurisdiction clauses that govern the relationship between the company and its lenders.

In *Re Rodenstock GmbH* [2011] EWHC 1104 (Ch) the English Court had to determine whether a foreign company had a sufficient connection with the UK based solely on the fact that the relationship between the company and its lenders was governed by English law and the English courts had exclusive jurisdiction. Briggs J held that such a relationship between the company and its lenders, governed by English law, was sufficient to warrant an intervention by the English Courts in the form of exercising its jurisdiction to sanction a scheme of arrangement. The English Courts have taken this approach in other cases including *Re Primacom Holdings (No.1)* [2011] EWHC 3746 (Ch) and *(No. 2)* [2012] EWHC 164 (Ch); *Re Nef Telecom BV* [2012] EWHC 2944 (Ch) and *Re Vietnam Shipbuilding Industry Groups* [2013] EWHC 2476 (Ch).

The issue that arose in relation to APCOA and the Foreign Scheme Companies was whether there was a sufficient connection with this jurisdiction despite the fact that the Facilities Agreement was, at inception, governed by German law with the German Courts having exclusive jurisdiction. To this extent the position of the Foreign Scheme Companies differed from the companies in *Re Rodenstock GmbH* and the other cases set out above which involved agreements that were, from inception, governed by English law and subject to the jurisdiction of the English Courts.

Decision of the Court

The Court held that as a result of the valid amendments to the governing law and jurisdiction clauses of the Facilities Agreement the Foreign Scheme Companies had a sufficient connection with this jurisdiction.

In addition to the sufficient connection test, Hildyard J stated that it was important that the English Courts were satisfied that its intervention pursuant to Part 26 CA 2006 would be recognised and enforced in the countries which matter. In this regard, Hildyard J accepted the expert evidence before him which confirmed that the original change of law and jurisdiction was in accordance with the laws then governing those instruments as well as being consistent with English law. The experts gave the view which expressly confirmed the propriety and effectiveness of the amendments made.

Of importance to the decision in the case was the fact that the creditors were fully informed about the amendments to the Facilities Agreement. To the extent the creditors were not aware of the purpose of the amendments the Court may not have exercised its jurisdiction. The evidence provided to the Court in relation to this was evidence of telephone calls purporting to fully inform the creditors.

Conclusion

The judgment in *Re APCOA Parking GmbH* is to be seen as a positive advancement in the law relating to schemes of arrangement and foreign companies.

The judgment is in line with the sequence of cases starting with *Re Drax Holdings Ltd* [2004] 1 WLR 1049 and develops on the jurisprudence set out in *Re Rodenstock GmbH* [2011] EWHC 1104 (Ch) on the extra-territorial effect of schemes of arrangements governed by English law and the choice of English jurisdiction.

The effect of the judgment is that restructuring lawyers now have a new avenue by which they can restructure the debts of foreign companies. Following the judgment it will be sufficient for foreign companies to scheme obligations arising under contracts which were not at inception governed by English law.

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