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Brexit: what might change
Insolvency & Restructuring

Introduction

On 23 June 2016 the UK population voted for the UK's exit from the European Union (EU). The applicable exit procedure and certain possible legal consequences of Brexit for Insolvency & Restructuring will be discussed below in the form of a Q&A.

In the short term, we do not identify material changes for the legal practice. The European law and regulations will remain in force until the negotiations between the EU and the UK have been completed and the withdrawal procedure has come to an end. To which extent European law and regulations will also apply following the UK's exit from the EU, will largely depend on the outcome of the negotiations. One of the fundamentals of the EU is the internal market, allowing for the free movement of goods, services, workers and capital (Internal Market). In this context we note that in January 2017, Prime Minister May announced that the UK will opt for a "hard Brexit", meaning that the UK will no longer maintain membership of the Internal Market, nor accede to any associated status. Instead, the UK will seek a free-trade deal with the EU outside the Internal Market.

Brexit – background

Since 2007 (Treaty of Lisbon), the EU Treaty offers a Member State an explicit legal basis to leave the EU (Article 50 TEU). Pursuant to Article 50(2) TEU, the UK can start the exit procedure by giving notice to the European Council. The exit agreement will be concluded on behalf of the EU by the Council[1], acting upon a qualified majority[2] and after having obtained the consent of the European Parliament. The agreement must set out the arrangements for the UK's exit and take account of the framework for the UK's future relationship with the EU. The UK cannot participate in the relevant discussions or decisions of the European Council or Council.

The EU Treaties cease to apply to the UK from the date of entry into force of the exit agreement or, if there is no such agreement, 2 years after the date of notice under Article 50 TEU, unless the European Council, in agreement with the UK, unanimously decides to extend this period. The exit procedure has never been called for and the way forward is full of uncertainties. Apart from Article 50 TEU, no further provisions or guidelines apply.

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1 The Council consists of a representative of each Member State at ministerial level, who may bind the government of the Member State in question and cast its vote (Article 16 TEU).

2 The qualified majority shall be defined as at least 72 % of the members of the Council representing the participating Member States, comprising at least 65 % of the population of these States (Article 238(3)(b) TFEU).

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Q&A - Insolvency& Restructuring

What is the current regulation regarding Insolvency & Restructuring in the EU?

While substantive insolvency law in the EU is largely unharmonised and remains subject to the domestic rules and regulations in each EU Member State (the Member State), the Insolvency Regulation[3], which applies in all EU Member States except Denmark, establishes common rules on the court competent to open insolvency proceedings, the applicable law and the recognition of insolvency proceedings and judgments. The Insolvency Regulation is directly applicable and does not per se require any implementing acts.

Under the Insolvency Regulation which comprises most insolvency and restructuring proceedings (although not the UK's scheme or arrangement) in the EU, a Member State in which a debtor's centre of main interests (COMI) is located (irrespective of the jurisdiction of incorporation or registration of such an entity) is entitled to open the main insolvency proceedings that would have a universal effect across the EU. Such proceedings are automatically recognised in all other Member States. Secondary proceedings can be opened in a Member State where the debtor has an "establishment"[4] with regard to the assets of the debtor located in this Member State.

On 20 May 2015, the recast Insolvency Regulation was adopted, which aims to expand the substantive scope of the Insolvency Regulation to include certain pre-insolvency rescue proceedings, to enhance communication and cooperation between the courts and insolvency practitioners in different Member States and to increase the transparency of the insolvency proceedings. New rules have also been introduced with regard to the insolvency of multinational enterprise groups. The recast Insolvency Regulations will largely apply as of 26 June 2017.

What will the effect of Brexit be on Insolvency & Restructuring proceedings in the UK?

As the Insolvency Regulation is directly applicable in the UK and its scope is limited to Member States only, it will cease to be effective in the UK following Brexit. As a non-participating state, the UK is unlikely to have any meaningful say in further developments of EU insolvency regulations.

The post-Brexit legal framework applicable to insolvency and restructuring proceedings will largely depend on the result of the negotiations with the EU and, in particular, on whether the UK and the Member States agreed to extend the EC Regulation to the UK or if another legal instrument with an equivalent effect were adopted. There is no certainty that this goal can be achieved due to the various political interests involved in the negotiations.

3 Regulation (EU) 1346/2000 of 29 May 2000 on insolvency proceedings.

4 "Establishment" means any place of operations where a debtor carries out a non-transitory economic activity with human means and assets.

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If no such agreement is reached, the UK will be applying its domestic rules to establish jurisdiction for opening the proceedings formerly, subject to the Insolvency Regulation. There is no guarantee that the domestic rules of different countries would provide for a similar outcome, thus resulting in inconsistencies and uncertainty for the parties involved.

The opening of insolvency proceedings in the UK would no longer be recognized automatically in the EU and vice versa, and any such recognition would operate solely on a comity basis. The insolvency practitioners may not have authority over the assets located across the Channel and the lack of harmonized rules is likely to lead to a longer and more complex, and hence more costly, process of recovering assets and distributions and the results across the jurisdictions may not be consistent.

Although the Insolvency Regulation is not the only international instrument regulating insolvency proceedings and the UK has also adopted the UNCITRAL Model Law on Insolvency & Restructuring, the latter can only be of limited use, as only a few EU Member States (i.e. the UK, Romania, Slovenia, Poland and Greece) have so far signed up to it.

What will the effect of Brexit be on the English scheme of arrangement?

English schemes of arrangement have been one of the most popular restructuring tools in recent times. The effectiveness of the scheme of arrangement in cross-border transactions will depend in part on its recognition in other Member States.

Since such schemes do not fall within the scope of the Insolvency Regulation, the Insolvency Regulation does not result in the scheme of arrangement being automatically recognised in other Member States. Although there is discussion on the matter in a number of jurisdictions, it has been argued under current practice that the Brussels Regulation[5] can be relied upon for the recognition of schemes of arrangements across the EU.

As with the Insolvency Regulation, the Brussels Regulation will no longer be applicable post-Brexit and the UK will need to negotiate a replacement. The UK may be able to accede to the Lugano Convention[6] in its own right or sign individual treaties with each Member State. In the absence of any such arrangements, any judgments passed in the UK (and this will probably also apply to schemes of arrangements) would be recognised only on a comity basis. At this moment, it is unclear what route will be taken.

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5 Recast Regulation (EU) 1215/2012 of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters.

6 The Lugano Convention of 30 October 2007 on jurisdiction and the recognition and the enforcement of judgments in civil and commercial matters regulates the relations between Member States on the one hand and Norway, Iceland and Switzerland on the other.

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What next?

Once the UK invokes Article 50 TEU, the UK and the EU will negotiate the terms of Brexit. It will be a highly political process and the outcome is as yet unclear. Therefore it is of the utmost importance to monitor the developments and the potential impact on your company's position closely. We will keep you informed about further developments.

Please contact your trusted adviser at Loyens & Loeff or send an e-mail to Brexit@loyensloeff.com if you have any queries.