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17th August 2017

For the attention of Dean Beale, Esq

Dear Sirs

CITY OF LONDON LAW SOCIETY INSOLVENCY LAW SUB COMMITTEE (THE "COMMITTEE"): THE IMPLICATIONS OF BREXIT FOR THE RESTRUCTURING AND INSOLVENCY PROFESSION

This letter follows up your various meetings with representatives of the City of London Law Society ("**CLLS**") Insolvency Sub-Committee (the "**Committee**"). These include the stakeholder meeting attended by the Committee chair, Jennifer Marshall and others, on 28 March 2017 and the meeting you and a number of your colleagues attended at the London offices of Hogan Lovells on 3 October 2016. As you are aware, the CLLS represents approximately 17,000 City lawyers through individual and corporate memberships. CLLS' corporate members include some of the world's largest international law firms. These law firms advise a variety of clients from multi-national corporations and financial institutions to government departments, often in relation to complex, multi-jurisdictional, legal issues.

The background to this letter is the Government's service on 29 March 2017 of the "Article 50" notice preparatory to Britain leaving the EU, the publication of the Government's White Paper

Legislating for the United Kingdom's withdrawal from the European Union (the "**Brexit White Paper**") and the recently introduced European Union (Withdrawal) Bill. The Article 50 notice marks the beginning of a two year Brexit negotiation process. The Committee recognizes that these negotiations will now be taking place in the new political landscape ensuing from the recent UK general election. The Committee considers, in consequence, that the need to ensure that the matters referred to in this letter are not inadvertently overlooked is more important than ever.

While the European Union (Withdrawal) Bill suggests that all existing EU regulations will be incorporated into English law unless there are any regulations to the contrary dealing with "deficiencies" arising from withdrawal, a "hard" Brexit would mean that we would lose the benefit across the European Union of the mutual recognition provisions in Council Regulation (EU) 2015/848 of 20 May 2015 on insolvency proceedings (the "**Recast Regulation**"). This could mean that insolvency practitioners appointed to UK companies could be unable to secure recognition as of right in other EU or EEA states. Their ability or otherwise to be recognized will depend upon European conflicts of law rules. The same consequences will result from laws implementing the Credit Institutions and Insurer Winding-Up and Reorganisation Directives elsewhere in the EU or EEA ceasing to apply to UK proceedings. Furthermore, while there are currently a number of bases pursuant to which an English scheme of arrangement will be recognised in Europe, the most frequently used basis for recognition is under the Judgments Regulation (EU 1215/2012). If we were to lose the benefit across Europe of recognition under the Judgments Regulation, this could have an impact on the recognition of English schemes.

The result would be to make English law governed restructurings and insolvencies less certain in outcome and more dependent upon the practices and discretions of the courts in individual EU and EEA member states. It may also lead to parallel proceedings needing to be commenced, in both the UK and the EU, adding to the costs of the proceedings for creditors and other stakeholders.

The Committee sees this as an outcome that should, if realistically possible, be avoided. The Committee believes that it would be contrary to the Government's own view (reiterated in the foreword to the *Review of the Corporate Insolvency Framework* consultation of May 2016) where it is stated that an efficient and effective insolvency regime is central to the promotion of enterprise and helps to create a business environment that supports growth and employment by ensuring that distressed yet viable businesses can be rescued quickly and efficiently. Where rescue is impossible, the Committee agrees that the UK insolvency regimes must provide consistent procedures for liquidating businesses and returning funds to creditors.

The Committee also recognizes the need identified in the Brexit White Paper for a smooth and orderly exit so that "wherever practicable and sensible" the laws governing business dealings on the day before Brexit occurs will continue to apply. To that end, the European Union

(Withdrawal) Bill proposes that all directly applicable EU laws (such as the Recast Regulation) and all EU-derived domestic legislation (such as the regulations implementing the Credit Institutions and Insurers Winding-Up and Reorganisation Directives) will become part of UK domestic law unless regulations to the contrary are made under section 7 dealing with deficiencies arising from withdrawal. Section 7 allows secondary legislation to be passed dealing with any reciprocal arrangements between the UK and the rest of the EU. The Committee's concern, however, is that such reciprocal arrangements are not an unilateral matter for the UK or the relevant minister: they will need to be agreed with the other EU member states.

The essential and distinguishing characteristic of the Recast Regulation is that member states surrender jurisdiction over entities based elsewhere in the EU or EEA in return for recognition of the effect of proceedings over entities based in their own respective jurisdictions. This has two implications for the Government's intended approach in respect of UK entities. First, it is not possible for the UK to legislate to replicate the effects of these measures by providing for the post-Brexit recognition in the EU or the EEA of the UK's own domestic insolvency proceedings. Secondly, legislation which perpetuated EU constraints on UK jurisdiction whilst simultaneously obliging the UK courts to recognize and give effect to proceedings taking place in the EU or EEA would destroy any bargaining position which the UK might otherwise have to avert the undesirable outcome of the pan-European framework falling away as regards the UK. In short, the Government's intended approach could expose the UK to the risk of suffering all the detriment of the pan-European framework without retaining any of its reciprocal benefits.

It is of course possible that the approach set out in the Withdrawal Bill (i.e. the recognition by the UK of EU insolvency proceedings) is merely an opening position and that the powers under section 7 of the Withdrawal Bill could be used retrospectively so that, if one or more Member States do not agree, during the negotiations, to the recognition of UK insolvency and restructuring proceedings (including schemes of arrangements), the nuclear option could then be launched of using secondary legislation to "switch off" the UK's recognition of that Member State's insolvency laws (and this threat could be used in the negotiations with the Member States). In other words, section 7 could be used to ensure that reciprocity is maintained. It would be good to know, however, if this is the Government's intention. Such an approach does run counter to a modified universalist approach, though, and so careful thought would need to be given to this option by the Brexit negotiators.

The Committee recognizes that the current status quo under which UK restructuring and insolvency procedures enjoy recognition as of right throughout the EU and EEA is unlikely (and perhaps understandably) to lie at the top of politicians' in-trays. The Committee believes in consequence that the current proposals to reform English insolvency law and practice are more important than ever. The Committee further believes that everything possible needs to be done to ensure that UK restructuring and insolvency procedures are made and kept sufficiently

attractive to be seen as procedures of choice irrespective of the outcome of the Brexit negotiations.

The Committee believes that failure to achieve these objectives could risk the outcome of restructuring and recovery procedures becoming less predictable and thus more risky than is presently the case. There would also be the likelihood of more parallel proceedings with attendant, adverse, consequences in terms of increased cost and decreased efficiency.

[In an attempt to quantify the value of financing currently transacted through the UK financial markets, scheduled to this letter is data extracted from Dealogic showing a half yearly deal volume analysis (since the beginning of 2014) for:

(i) UK borrowers where a bank (or banks) from the EU27 nations were involved in the lending syndicate; and

(ii) EU27 borrowers where a bank (or banks) from the UK were involved in the syndicate.

Excluded from the search results are trade finance, project finance, export credit, structured commodity finance, trade flows and supply chain finance deals, in line with Dealogic standard reports. The volume figures include the amounts lent by other lenders who were in the syndicates, so these figures can best be described as representing syndicated loans where a UK lender was part of the syndicate lending to an EU27 borrower (a total amount of approximately €270 billion for 2016) or where a UK borrower was funded by EU27 lenders (a total amount of approximately €90 billion for 2016). If even a small proportion of these loans were to be impacted by Brexit, the economic consequences could be very significant.] [1]

Subject to your specific requirements and concerns, the Committee believes that your review of UK insolvency law and practice will need to address the following matters:-

1. CONSISTENCY WITH EU PROCESSES

1.1. If UK restructuring and insolvency procedures are to be seen as procedures of choice, they need at the very least to be consistent with and wherever possible improvements upon current and proposed European legislation. The proposed EU Directive 2016/0359 on harmonizing restructuring proceedings envisages the introduction of a new, four month, moratorium procedure. That procedure's objective is to provide debtors with a breathing space to facilitate the negotiation of a restructuring plan. It is also proposed that judicial or administrative authorities should be able to confirm a restructuring plan that is not supported by all classes of a company's creditors. The proposed directive also

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[1] This data was sourced by Dealogic and was generated on 29 March 2017. See the attached Schedule for the tables of results.

recommends the introduction of legislation allowing for the provision of new, priority, financing for the negotiation and subsequent implementation of a restructuring plan.

1.2. The Committee appreciates that versions of all three proposals were included in your *Review of the Corporate Insolvency Framework* consultation of May 2016 to which the Committee responded on 5 July 2016. In that response, the Committee indicated its support for a cram-down process for out of the money creditors or shareholders although the Committee was more skeptical about the case for a pre-insolvency moratorium. In relation to the proposals for rescue financing, the Committee commented that this was a complex area and encouraged you to investigate what factors were currently holding back potential participants in this market.

1.3. The Committee would be happy to work with you to analyse the responses to this consultation in the light of the proposed Directive. The Committee believes that the objective of such a review should be to develop, ideally within the two year Brexit negotiation period, any changes to UK insolvency and restructuring law (including any "cram down" restructuring plan) to ensure that UK laws remain competitive with their equivalents in other European jurisdictions and the US.

1.4. The Committee also considers that the need for an ipso facto rule applicable to contracts in general, as opposed to only essential supplies, requires further deliberation.

2. Recognition and Reciprocity

2.1. The improvement of English rescue and composition procedures is only one half of the equation. The second matter to be addressed if English restructuring and insolvency procedures are to remain "processes of choice" in the post-Brexit world is the basis upon which such proceedings can be undertaken and recognized. Recognition is in turn a two way process. First, English restructuring and insolvency procedures must be capable of recognition in other jurisdictions and in particular the EU and EEA states. Secondly, the Government needs to ensure that there exists a robust and predictable basis for the recognition and implementation of EU and EEA restructuring and insolvency procedures in the UK.

2.2. The ideal solution would be for the United Kingdom to retain the reciprocal benefits of mutual recognition under the Recast Regulation, the Credit Institutions and Insurer Winding-Up and Reorganisation Directives and for judgments, the European Judgments Regulation (EU1215/2012) which would assist with the recognition of English schemes. The Committee recognizes, however, that such an outcome will depend on whether the other Member States are prepared to continue with this legislation in circumstances where the UK is not prepared to be part of the single market. However, for the reasons rehearsed earlier in this letter, reciprocity would be an essential part of continuing with this legislation.

2.3. An alternative approach could be to encourage EU member states, or better still the EU itself, to adopt the UNCITRAL Model Law on Cross-Border Insolvency Proceedings. Given the limitations regarding the recognition of insolvency judgments under the Model Law[2], this would fall a long way short of the ideal but may be preferable to the absence of any pan-European framework. As matters stand, all EU member states have the benefit of the UK's adoption of the Model Law through the Cross-Border Insolvency Regulations 2006 and will continue to do so post-Brexit. However, amongst other EU member states, only Greece, Poland, Romania and Slovenia have adopted the Model Law. It is therefore another example of a prospective imbalance which needs to be considered in the forthcoming negotiations.

2.4. Another option (which could be adopted in parallel with that explored in paragraph 2.3 above) could include expanding, or even abandoning, the list of "relevant countries or territories" for the purpose of recognition under section 426 of the Insolvency Act 1986. Currently, the list of "relevant countries or territories" includes dependencies such as the Channel Islands or the Isle of Man and various current or former Crown dependencies or colonies such as Bermuda, Canada, the Cayman Islands or Hong Kong. Ireland is the only EU member state which is a "relevant country". It will thus continue to benefit from section 426 post-Brexit without there being a comparable provision in favour of the UK in Irish legislation. While, prima facie, amendments to section 426 would only assist with the recognition of foreign insolvency proceedings in the UK (and not the recognition of UK proceedings abroad), one option would be to limit the relief available under section 426 to jurisdictions which did, in turn, recognize UK insolvency proceedings. Given that other jurisdictions already have the benefit of the UK's adoption of the Model Law, we wonder however whether there would be any negotiating leverage in such an approach[3].

2.5. An alternative way of dealing with recognition could be the conclusion by the UK of individual treaties with countries within or outside the EU to facilitate cross-border restructuring with the governments of countries willing to grant – and receive from the United Kingdom – mutual recognition and enforceability of restructuring and insolvency proceedings. The Committee recognizes that this could require the United Kingdom to give up the so-called rule in *Gibbs -v- Societe Industrielle* (1890) 25 QBB 399 *("Gibbs")*. Under the rule in *Gibbs*, the English courts will only recognize the discharge or release of an obligation governed by the proper law of a particular jurisdiction if that discharge or release is also governed by, or implemented in accordance with, the proper law of the same jurisdiction.

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[2] We understand that UNCITRAL is currently working on a project that would allow recognition of insolvency related judgments, either through a new Model Law or an adaption of the existing Model Law and so member states could be encouraged to sign up to this as well

[3] A rather radical option might be to amend the Cross Border Insolvency Regulations so that recognition is only afforded to foreign insolvency proceedings if the courts of the foreign jurisdiction were to recognise UK insolvency proceedings. This is not the intention behind the Model Law, however, which is intended to operate on a non-reciprocal basis.

2.6. The advantage to the United Kingdom of granting and accepting full, mutual, recognition from and by other jurisdictions would be ensuring certainty of outcome between those countries that signed up to mutual recognition arrangements with the UK. Such arrangements, while limited to the particular countries and treaties involved, could nevertheless be more broadly cast and thus more certain in their application than would be recognition tied to, for example, the more narrow grounds set out in section 426 Insolvency 1986.

2.7. Although not linked to the question of recognition, and very much as a fall-back if we are not able to maintain the status quo under the existing European legislation, the UK may want to consider replacing the "centre of main interests" or "establishment" tests for primary or secondary proceedings with the "liable to be wound up" basis upon which an English court will assume jurisdiction to sanction a scheme of arrangement under Part 26 of the Companies Act 2006. (Indeed, the application of administration and company voluntary arrangements to foreign companies is currently governed by EU law and incorporation within an EEA state so that it will require reconsideration in any event in the context of Brexit.)

2.8. For the reasons given above, the Committee considers that the best option remains that of negotiating legislation to replicate the effects of the Recast Regulation. Although there are other options available, these will all result in the recognition process being more complex than it is today. Without any measures being taken, the post-Brexit recognition of UK restructuring and insolvency proceedings in the EU would (as stated above) be a matter for the discretion of the courts in the jurisdiction concerned. The result (as also stated above) would be to introduce an unacceptable degree of further cost and uncertainty into the recognition process.

2.9. The Committee's principal focus has been on major transnational corporate or financial restructurings or insolvencies. That focus is consistent with individual Committee members' firms' own client lists, largely comprising major corporate and financial institutions. Nevertheless, the loss of the Recast Regulation and the broad measures of recognition available on account of the United Kingdom's EU membership could also have particularly severe consequences for United Kingdom individuals doing business in Europe, were those individuals forced into English bankruptcy or individual voluntary arrangement proceedings.

2.10. Were Brexit to lead to the "discharge" in the UK processes ceasing to be recognized in Europe, individuals denied recognition could find it difficult to continue to carry out business in Europe. This is because they would face the risk of any assets located in Europe being seized to satisfy pre-bankruptcy debts.

2.11. The loss of reciprocity could also assist rogue directors who had moved their assets out of one EU jurisdiction before insolvency to obtain negotiating leverage to the detriment of other stakeholders. That would result from the inability of an insolvency practitioner appointed to the individual of being recognized, as a right, throughout the European Union.

The Committee recognizes that the only certain aspect of the Brexit process is that the Government has a two year period within which to negotiate the best possible post-Brexit trading environment for all affected stakeholders (plus potentially any transitional phase if the status quo remains during that phase). The Committee also recognizes that the ultimate shape of any revised restructuring process and its recognition will depend upon the way in which the political situation develops during such negotiations. Accordingly, the purpose of this letter and the points it makes is to set a preliminary non-prescriptive framework around which further discussions can take place.

The Committee and its members will support you in whatever way you believe will assist the Government in achieving the overall objective of ensuring that United Kingdom restructuring and insolvency procedures are seen as procedures of choice irrespective of the outcome of the Brexit negotiations. Please contact either Jennifer Marshall or Joe Bannister as and when you have the opportunity of digesting the points made above and you are ready to discuss further.

Kind regards

Yours faithfully

Jennifer Marshall,
Chair, Insolvency Law Committee
City of London Law Society

17th August 2017

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Schedule

Source: Dealogic
Volume of syndicated loans where a lender from EU27 was involved in the syndicate lending to UK borrower

EU 27 lenders to uk borrowers

Credit Date by Half Year	Deal Value Euro (m)	No.
2014 First Half	74,916.67	117
2014 Second Half	89,198.23	127
2015 First Half	86,089.18	127
2015 Second Half	68,221.12	100
2016 First Half	61,957.64	84
2016 Second Half	30,761.20	66
2017 First Half (to 28 March)	62,253.95	23
Subtotal	**473,397.98**	**644**
Total	**473,397.98**	**644**

Source: Dealogic
Volume of syndicated loans where a UK lender was involved in the syndicate lending to an EU27 borrower

UK lenders to EU27 borrowers

Credit Date by Half Year	Deal Value Euro (m)	No.
2014 First Half	216,382.99	192
2014 Second Half	188,180.62	219
2015 First Half	196,669.05	186
2015 Second Half	250,222.94	186
2016 First Half	91,029.69	133
2016 Second Half	180,393.09	149
2017 First Half (to 28 March)	53,445.31	48
Subtotal	**1,176,323.70**	**1,113**
Total	**1,176,323.70**	**1,113**