

An introduction to English
Insolvency Law

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The purpose of this note is to provide an introduction to English insolvency law by highlighting some of the formal procedures available on insolvency and the issues that can arise when a company is in financial difficulties. It also addresses some of the potential personal liabilities of the directors of the company.

1. FORMAL PROCEDURES

1.1. Overview

A company in financial difficulties may be made subject to any of five statutory procedures:

- i. administration;
- ii. company voluntary arrangement;
- iii. scheme of arrangement;
- iv. receivership (including administrative receivership); and
- v. liquidation (winding up).

With the exception of schemes of arrangement, which fall within the ambit of the Companies Act 2006, these are formal insolvency procedures governed by the Insolvency Act 1986.

An important distinction needs to be drawn between the first three procedures, which may restore a company to financial strength, and the remaining procedures, which deal with the disposal of a company's assets in cases where it cannot be rescued.

The administration procedure was introduced by the Insolvency Act 1986 and substantially revised by the Enterprise Act 2002 to include a streamlined procedure allowing the company or (more often) its directors to appoint an administrator without the involvement of the court. This "out-of-court"

procedure can also be used by certain secured creditors although their ability to appoint an administrative receiver has been severely restricted (see section 1.5 below). In addition to the changes in procedure, new objectives, including greater protection for unsecured creditors, were also introduced and the administrator has been given the power to make distributions to secured and preferential creditors (principally employees in respect of wages and certain pension fund contributions) and, in certain cases, unsecured creditors. The new regime also provides for mandatory set-off, similar to that arising in a liquidation, which will automatically apply when the administrator gives notice of a proposed distribution to creditors.

Voluntary arrangements and creditors' schemes of arrangement are procedures designed to assist a company to reach agreement with its creditors to reorganise or reschedule its debts.

Receivership and liquidation, in contrast, are likely to signal that the company itself has no future. The receiver's principal function is to sell the charged assets and pay all or part of the proceeds to his appointor. The liquidator, in contrast, will be seeking to sell the assets or business of the company before its dissolution. This may enable a purchaser to acquire at least part of the company's business as a going concern, thereby preserving the underlying business and work force.

A brief description of each of these procedures is provided below but note that, in some instances, the procedure will be modified by the Financial Collateral Arrangements (No.2) Regulations 2003, as amended.

These regulations implement the EU Directive on Financial Collateral Arrangements, which aims to simplify the process of taking financial collateral across the EU. They disapply a number of provisions of the Insolvency Act 1986, including the moratorium on enforcement of security in CVAs and administrations and the order of priority of claims in floating charge realisations. A discussion of the impact of these Regulations is beyond the scope of this note.

1.2. Administration

The administration procedure is intended for use as a rescue mechanism that aims to allow companies, wherever possible, to carry on running their businesses. The procedure is initiated either by applying to the court for an administration order or by filing papers with the court documenting an out-of-court appointment of an administrator. For practical purposes, it is common for more than one administrator to be appointed to the company, in which case they will usually agree to act jointly as well as independently of one another.

Separate procedures exist under the Banking Act 2009 for failing banks and building societies to deal with remaining assets, where there has been a partial transfer of their business, and for investment banks under the Investment Bank Special Administration Regulations 2011.

A court-based application will usually be made by the company's directors or creditors. An out-of-court application may be made by the company or its directors or by a secured creditor who is the holder of a "qualifying floating charge" ("QFC"). For a charge to be a QFC it must relate to the whole, or substantially the whole, of the company's property.

For applications other than by a QFC holder, it will be necessary to show that the company is or is likely to become unable to pay its debts. A QFC holder, in contrast, is able to appoint an administrator when an event has occurred that would allow him to enforce

his charge (usually where there has been a default under a loan agreement). Note that in a court-based application, even if the relevant criteria are satisfied, it is still within the court's discretion to decline to grant an administration order.

In all cases, the insolvency practitioner must provide an opinion stating that the statutory purpose of administration, which is set out as a hierarchy of objectives in the Insolvency Act 1986, is reasonably likely to be achieved. The primary objective is the rescue of the company as a going concern. Only if this objective is not reasonably practicable, or does not produce the best result for creditors, does the second objective apply. The second objective is to achieve a better result for the creditors as a whole than would be likely if the company were wound up without first being in administration. An example of when the second objective might apply is where the company is in a position to continue trading until the business (or parts of it) is sold as a going concern. Only if the second objective is not reasonably practicable, and it does not unnecessarily harm the interests of the creditors as a whole, does the third objective of realising the company's property for the benefit of one or more secured or preferential creditors apply.

Once an application has been filed at court, or a notice of intention to make an out-of-court appointment has been given to any secured creditor who is entitled to appoint an administrator or administrative receiver, and other persons entitled to notice, an interim moratorium will automatically arise. The purpose of the interim moratorium is to protect the company and its assets from creditor action in the short period until an administrator is appointed. During this period, unless the leave of the court is obtained, the company may not be wound up except where the Secretary of State for Business, Innovation and Skills, or the appropriate regulator under the Financial Services and Markets Act 2000 ("FSMA 2000"), presents a petition on public interest grounds. There will also be a stay on enforcement of security and on all legal processes and proceedings against the company. Goods held under

leasing, hire purchase, conditional sale or retention of title agreements may not be repossessed and landlords may not exercise their rights of forfeiture in relation to premises let to the company. However, a QFC holder may appoint an administrator out of court or, in certain circumstances, an administrative receiver can be appointed and a petition to wind up the company may still be presented.

Where a QFC holder or the company (or its directors) is able to appoint an administrator out of court in circumstances where there is no one to whom notice must be given, there will be no interim moratorium. Instead, a full moratorium will come into effect upon the filing at court of the requisite documents. At that point, it will no longer be possible to appoint an administrative receiver and, depending on the appointment procedure used, any winding-up petitions are either dismissed or suspended.

The administrator will take over the management of the affairs, business and property of the company upon appointment. He will effectively be acting as its agent and will have a wide range of powers at his disposal. As he will be under a duty to act for the benefit of all creditors, he is likely to impose additional controls over the company's operations. The directors will continue to hold office but cannot exercise any management powers without his consent. This means that in some cases the directors' powers and duties, like those of the company secretary, are likely to be significantly diminished.

In a trading administration, or where the administrator is satisfied with the company's processes and controls, he may decide to leave some or all powers with the directors. Note that certain company law requirements for directors, such as submitting annual returns and accounts to the registrar of companies, will continue to apply but are unlikely to be enforced.

As soon as reasonably practicable after his appointment, the administrator will require one or more of the current or former directors or other

officers to provide him with a statement of the company's affairs. This statement gives details of the company's assets and liabilities, including any assets that are subject to fixed or floating charges, and enables the administrator to assess the company's financial position and formulate proposals to be implemented during the administration.

Within eight weeks of his appointment, the administrator must send a statement of his proposals to all known creditors and members of the company, and file a copy of the proposals with the registrar of companies. In complicated cases, he may apply to court to have this period extended. An invitation to an initial creditors' meeting, which must usually be held within ten weeks of his appointment, will be included with the copy of the proposals sent to each creditor.

In certain circumstances, the administrator has the power to sell the company's business or assets before the initial meeting and without the consent of the creditors. This will occur in a pre-packaged administration sale ("**pre-pack**") where the sale of the whole or part of the business, or its assets, is arranged before the administrator is appointed. The administrator then sells the business immediately or soon after taking the appointment. A person who deals with an administrator in good faith and provides valuable consideration need not enquire whether he is acting within his powers.

Another situation where the administrator is not required to hold an initial creditors' meeting is if he states either that the company has sufficient property to enable every creditor of the company to be paid in full or that the company has insufficient property to enable a distribution to be made to unsecured creditors other than from the statutory prescribed part (the prescribed part represents a proportion of the proceeds of the sale of assets subject to any floating charge, up to a maximum of £600,000, which is set aside for their benefit). A meeting must, however, be summoned if at least 10% in value of the creditors demand it.

Unlike a liquidator, an administrator does not currently have the power to seek a court order against directors for a contribution to the company's assets if his investigations reveal incidences of wrongful or fraudulent trading. However, he will be able to bring such claims when the relevant provisions of the Small Business, Enterprise and Employment Act 2015 ("SBEAA 2015"), which amend the Insolvency Act 1986, come into force. An administrator may, however, apply to court in the same way as a liquidator for an order to set aside transactions at an undervalue, preferences and transactions defrauding creditors (see section 3 below). He may also seek a declaration of invalidity in respect of any voidable floating charges and the repayment of any amounts recovered by the floating charge holder after the company entered administration. In addition, he may be required to submit information to the Secretary of State for Business, Innovation and Skills on the conduct of the directors and former directors of the company.

The administration will end automatically after one year unless, as is often the position in large or complex cases, the administrator's term of office is extended by court order or with the consent of the creditors. Before that time, if the administrator was appointed by the company or its directors, or by a QFC holder, he may file a notice at court to end the administration if he considers that its purpose has been sufficiently achieved. If the secured creditors are likely to be paid and sufficient funds remain for a distribution to be made to any unsecured creditors, he may decide that the administration should terminate in a creditors' voluntary liquidation (see section 1.6 below). Alternatively, he may conclude the administration by way of a CVA, a scheme of arrangement or a compulsory liquidation or he may decide to dissolve the company if it has no property and there are therefore no funds available for distribution to creditors.

1.3. Company Voluntary Arrangement ("CVA")

A CVA is an informal but binding agreement between a company and its unsecured creditors in which the company's debts are compromised. It may be used to avoid or supplement other insolvency procedures, such as administration or liquidation.

A CVA can be proposed by the directors who will first appoint an insolvency specialist (normally an accountant) to act as a nominee. It can also be proposed by an administrator or liquidator where the company is in administration or liquidation. The nominee will report to the court whether, in his opinion, the proposed CVA has a reasonable prospect of being approved and implemented and whether it should be put to the creditors and members. If he believes that it should, meetings of creditors and members will be called to decide whether to approve it, with or without modifications. Any proposal or modification that affects the rights of a secured creditor to enforce his security, or those of a preferential debtor as regards the priority or amount payable, cannot be approved without their consent.

The proposal requires the approval of three quarters or more (in value) of the creditors present in person or by proxy and voting on the resolution. In calculating majorities at a creditors' meeting, certain votes are left out of account, including where notice of the claim has not been given and where the claim, or part of it, is secured. A separate meeting of members is also held to vote on the proposals. Members' approval requires a simple majority but if the result of their vote differs from that of the creditors, the creditors' vote will prevail.

If the proposal is approved, it will bind all creditors who were entitled to vote, whether or not they had notice of the creditors' meeting. Dissenting creditors and creditors whose votes are required to be left out of account are therefore bound by a resolution of the requisite majority. Secured and preferential creditors

will not be bound unless they have given their consent. The nominee becomes the supervisor of the CVA, once approved, and is responsible for its implementation. The CVA can be challenged in court by a creditor or member on the grounds of unfair prejudice or material irregularity (or both). This must be done within 28 days of the filing of the notice of approval with the court or, if the applicant did not receive notice, within 28 days of the day on which he became aware that the meeting had taken place.

Certain small companies contemplating a CVA are able to take advantage of an optional moratorium of between one and three months to protect them from creditor actions while the proposals are being put in place. A small company will be eligible for a moratorium if it satisfies two of three qualifying conditions laid down by the Companies Act 2006. These relate to the size of the company's turnover, balance sheet total and workforce. Some companies involved in specialised financing arrangements are excluded from eligibility so that certain secured creditors are not prevented from exercising their enforcement rights. Companies that do not meet the Companies Act 2006 criteria can otherwise continue to seek the benefit of a moratorium if the CVA is put in place after the company has entered administration.

1.4. Creditors' Scheme of Arrangement

A creditors' scheme of arrangement is a court-approved compromise or arrangement between a company and its creditors, or any class of them, to reorganise or reschedule the company's debts. It is not an insolvency procedure and does not include a moratorium on creditor action. However, it can be implemented in conjunction with formal insolvency proceedings (administration or liquidation), both of which include a formal moratorium. It can otherwise be implemented on a standalone basis by the company itself. In its simplest form, a scheme may be used to vary the rights of a class of creditors and can bind dissentient creditors if the requisite majority or

majorities vote in favour of the proposal. A scheme can also be used to compromise the debts of overseas companies, if they have a sufficient connection with this jurisdiction, and has been used in circumstances where such companies are unable to obtain the requisite level of consent to approve the compromise under local law.

The process is initiated by the company (or an administrator or liquidator if the company is in administration or liquidation) or any of its creditors. The first step is to apply to the court for an order giving permission for a meeting of creditors to be convened. At this point the company also identifies with whom it is proposing to make the compromise and the class or classes of creditors to whom the scheme proposal is to be put. Any creditors unaffected by the scheme (for example, because they are to be paid in full or because their debts are not required to be compromised) can be excluded from the scheme. If a simple majority in number of those voting in person or by proxy and a three-quarters majority in value is obtained at any meeting, a further application is made to the court for an order sanctioning the compromise or arrangement.

One of the main advantages of a scheme over a CVA is that it is binding on all members of the relevant class (or classes) of creditors, once it is approved by the appropriate majorities, sanctioned by the court and delivered to the registrar of companies. However, the procedure can be expensive and cumbersome and is less flexible than a consensual restructuring.

1.5. Receivership (including Administrative Receivership)

There are broadly three types of receiver. The first is a receiver appointed under statutory powers, in particular, pursuant to the Law of Property Act 1925 which confers the power to appoint on a mortgagee whose mortgage is created by deed. This type of receiver is known as a "Law of Property Act" (or "LPA") receiver. The powers of an LPA receiver are generally

limited to collecting in income and applying it to reduce outgoings and mortgage interest. The second type of receiver, known as a “fixed charge receiver”, is appointed pursuant to an express power in a security instrument creating a fixed charge or a security trust deed. His powers will typically be extended beyond those of an LPA receiver and will include taking charge of, and realising, the charged assets and using the proceeds of realisation to pay the monies due from the borrower to the appointing lender.

The third type of receiver is an “administrative receiver” who is appointed under the terms of a floating charge (or under such a charge and other forms of security) over the whole or substantially the whole of a company’s property. He will have wider powers than a fixed charge receiver and may continue to trade the business in the hope of selling it as a going concern, thereby maximising realisations for distribution to secured and preferential creditors. However, the circumstances in which this type of receiver can be appointed have been severely limited by the Enterprise Act 2002, which prohibits the holder of a floating charge created after on or after 15 September 2003 from appointing an administrative receiver, although he can appoint an administrator (see section 1.2 above). Exceptions apply where the floating charge is granted in relation to certain specialised financing arrangements. Holders of floating charges over the whole or substantially the whole of the company’s property created before 15 September 2003 can appoint either an administrative receiver or an administrator.

On appointment, an administrative receiver takes possession of the secured assets to realise their value and apply the proceeds to pay the amounts due to the secured creditor who appointed him. Creditors with fixed charges and preferential creditors must be paid before creditors with floating charges and, as in administrations and liquidations, a proportion of the proceeds of the sale of assets subject to any floating charge created on or after 15 September 2003 may be required to be set aside for the benefit of unsecured creditors.

1.6. Liquidation (Winding Up)

A company may go into voluntary or compulsory liquidation or, if it is a bank or building society, it may be made subject to a special insolvency regime under the Banking Act 2009 and related secondary legislation.

There are two types of voluntary liquidation: a “members’ voluntary liquidation” (“MVL”) and a “creditors’ voluntary liquidation” (“CVL”), both of which are initiated by the company itself passing a resolution at a meeting of members. A MVL is only possible where the directors are able to make a statutory declaration that all the liabilities of the company will be met within a period not exceeding 12 months. In this case, it is the members who appoint the liquidator. If the directors are not able to make the declaration (i.e. the company is insolvent), the company will be placed into CVL. In a CVL, the creditors will have a greater say and are also able to appoint a liquidation committee to supervise certain aspects of the winding up. In either case, the directors of the company must give prior notice to any QFC holder and to the appropriate regulator under the Financial Services and Markets Act 2000 if the company is an authorised deposit taker under the Banking Act 2009, of their intention to propose a resolution for voluntary liquidation.

A compulsory liquidation is initiated by the presentation of a winding-up petition to the court. The petition may be presented by the company, the directors, any creditor or (subject to certain exceptions) any person liable to contribute to the assets of the company in the event of a winding up. The grounds on which a court can make a winding-up order include where the company is unable to pay its debts and where the court believes it is just and equitable that the company be wound up. Any QFC holder who is entitled to appoint an administrator may apply to the court to have the winding-up order discharged and an administrator appointed.

In both a compulsory and a voluntary liquidation, the liquidator is under a duty to collect in and realise the assets of the company for distribution to the creditors. Once this process has been completed, the company will be dissolved. If, however, the liquidator believes that he could achieve a better result for the creditors if the company were placed into administration, then he may apply to the court for himself or another person to be appointed as administrator.

The basic rule concerning the priority of creditors in a winding up is that the claims are treated equally. This rule is subject to whatever security may exist over the company's assets. A secured creditor with a fixed charge has priority insofar as the proceeds of sale of the charged property are concerned. The claims of any floating charge holders are subordinated to those of any fixed charge holders. The floating charge holder is also obliged to account to certain preferential creditors and, as in administrations and receiverships, may be required to set aside a proportion of the proceeds of the sale of assets subject to any floating charges created on or after 15 September 2003 for the benefit of unsecured creditors. In addition, a floating charge holder's claims will be subordinated to the expenses of the winding up, to the extent that the assets of the company available for the payment of unsecured creditors are insufficient to meet them.

Any surplus is paid to the members in accordance with their entitlements, subject to any claims by subordinated creditors.

2. PERSONAL LIABILITY OF DIRECTORS

2.1. General Duties of Directors

The common law imposes duties of skill and care on directors of the company that apply at all times. These have broadly been placed on a statutory basis by the Companies Act 2006. One of the key duties is to promote the success of the company for the benefit of its members as a whole. However, if the company is approaching insolvency the directors are then also

required to consider or act in the interests of the company's creditors.

2.2. Wrongful Trading

Wrongful trading occurs where a director has failed to take every step to minimise potential loss to the company's creditors in a situation where he knew or ought to have concluded that there was no reasonable prospect of the company avoiding insolvent liquidation.

In such a case, a liquidator or administrator (or a bank liquidator or administrator appointed under the Banking Act 2009) can apply to the court for an order for the director to make such contribution to the company's assets as the court might consider proper. The standard required as to what a director ought to know, the conclusions he ought to reach and the steps he ought to take is that which would be known, reached or taken by a reasonably diligent person with the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as those of the director in relation to the company and with the general knowledge, skill and experience that the director has. Thus there is both an objective and a subjective test. Under the Banking Act 2009, it may assist a director of a bank in defending a wrongful trading claim if he ensures that the appropriate regulator under FSMA 2000 is notified of an application or proposal to place a bank into administration or of the presentation of a petition for the winding up of a bank, if done with a view to minimising the potential loss to a bank's creditors.

Not only do the wrongful trading provisions apply to directors or former directors (and there is no distinction in principle for these purposes between executive and non-executive directors), they also apply to shadow directors and de facto directors. A shadow director is a person (including a company) in accordance with whose instructions or directions the directors of a company are accustomed to act. A de facto director is a person occupying the position of director, regardless of the title he has been given, who has not been formally appointed as a director.

2.3. Fraudulent Trading

Fraudulent trading occurs where, during the course of the winding up of a company, any business of the company has been carried on with intent to defraud creditors. A liquidator (or a bank liquidator or administrator under the Banking Act 2009) can apply to court for an order that any person who was knowingly a party to carrying on the business in such a manner be made liable to contribute to the company's assets.

Note that fraudulent trading is also a criminal offence under the Companies Act 2006, carrying with it the threat of a fine, imprisonment or both. Such an offence may be committed whether or not the company has been, or is in the course of being, wound up.

2.4. Delinquent Directors

The Insolvency Act 1986 provides that if, in the course of a winding up, a person who has been involved with the promotion, formation or management of the company is found to have misapplied, retained or become accountable for any money or other property of the company, or been guilty of misfeasance or breach of a fiduciary or other duty in relation to the company, he may be compelled by the court to repay, restore or account for the money or property of the company with interest. He may otherwise be required to contribute such sum to the company's assets by way of compensation in respect of the misfeasance or breach of fiduciary or other duty as the court thinks just. The application to the court can be made by the official receiver or the liquidator or any creditor or contributory.

Breaches of duty that could be relevant here may include a director's involvement in the company granting a preference or entering into a transaction at an undervalue (discussed in section 3 below).

Case law suggests that these provisions (unlike those relating to wrongful trading) do not apply to shadow directors.

2.5. Disqualification

In addition to incurring personal liability, a director who has engaged in fraudulent or wrongful trading, or been found guilty of other misconduct in connection with a company, may be disqualified by court order for a period of between two and 15 years from acting as a director or from having any involvement in the promotion, formation or management of any company. This includes directors of banks that are placed into liquidation or administration under the Banking Act 2009.

The Company Directors Disqualification Act 1986 ("CDDA 1986") introduced provisions for a director who is the subject of intended disqualification proceedings to give an undertaking to the Secretary of State for Business, Innovation and Skills not to act as a director for a given period. This procedure does not require court involvement and thus avoids the expense of disqualification proceedings.

Note that, under the SBEEA 2015, grounds for disqualification (or the giving of an undertaking) of persons who have been convicted of certain offences overseas, and for persons who are not directors but who have exerted the requisite influence over an unfit director of an insolvent company, will also be introduced.

In light of the above, it is clearly essential that directors receive legal and other professional advice when a company is in financial difficulties. In these circumstances, it is advisable to engage an insolvency practitioner at an early stage to provide an experienced and objective view of the company's problems. By following the advice of such a practitioner, directors will reduce the likelihood of being found personally liable in the circumstances described above.

3. VULNERABLE TRANSACTIONS

3.1. Background

If a company enters into certain types of transaction within specified periods leading up to its insolvency, an administrator or liquidator may apply to the court for an order to restore the parties to the position they would have been in if the transaction had not been entered into or to seek some other appropriate remedy. In some cases, entering into such a transaction could be treated as a breach of duty by the directors, in particular if the transaction is at an undervalue or is a preference.

3.2. Transactions at an Undervalue

A transaction is at an undervalue if a company makes a gift to a person or enters into a transaction on terms where the company receives no consideration or the value of the consideration is significantly less than the value of the consideration provided by the company. If the transaction is entered into in good faith to carry on the company's business and there are reasonable grounds for believing that it will benefit the company, then no liability will be incurred.

To be vulnerable to challenge, the transaction must have been entered into during the period of two years ending with the onset of insolvency (broadly, the commencement of the winding up or administration) and at that time the company was insolvent on a cash flow or balance sheet basis or became insolvent as a result of entering into it. There is a presumption of insolvency if the parties to the transaction are connected, for instance in an intra-group transaction or a transaction made between the company and one of its directors.

If a transaction is found to be at an undervalue, the court has very wide powers to restore the parties to the position they were in before the transaction was entered into, although there is protection for a third

party that has acquired some benefit or interest other than from the company itself, if they acted in good faith, for value and without notice.

3.3. Transactions defrauding Creditors

The same undervalue definition applies in respect of transactions defrauding creditors, although there is no defined period within which a challenge must be mounted and the company does not have to be subject to an insolvency process. The transaction must, however, have been entered into to put the assets beyond the reach of a creditor or to otherwise prejudice the interests of a creditor. Such claims are therefore rare where directors have acted in good faith.

3.4. Preferences

A company gives a preference if it does anything or suffers anything to be done that has the effect of putting a creditor or a guarantor of its debts in a position that, if it were to go into insolvent liquidation, would be better than the position that person would have been in if the thing had not been done. The repayment of a debt by a customer to its bank on the due date could fall within this wide definition. The company must have been influenced by a desire to produce the preferential effect in order for the transaction to be vulnerable. There is a presumption of such influence if the parties are connected.

Any such transaction will be set aside, in the case of an unconnected person, if it was entered into in the six-month period before the commencement of the winding up of the company or its entry into administration. This period extends to two years in the case of a connected person. For the transaction to be set aside, the company must have been insolvent at the time it was entered into or to have become so as a result of entering into it.

As with a transaction at an undervalue, if a transaction is found to be a preference, the court has very wide

powers to restore the parties to the position they were in before the transaction was entered into and, again, there is protection for a third party that has acquired some benefit or interest other than from the company itself, if they acted in good faith, for value and without notice.

3.5. Floating Charges

A floating charge may be invalid if it is created within two years of the onset of insolvency, if the parties are connected, or within one year if they are not. Such a charge will only be valid to the extent of the value of so much of the consideration for the charge as consists of money paid or goods or services supplied to the company at the same time as or after its creation, together with interest, if any, payable under the relevant agreement. There is a defence available for unconnected parties, which is that the charge will not be invalid if the company was solvent when it was created and did not become insolvent as a consequence of the transaction.

4. CROSS-BORDER INSOLVENCIES

4.1. The Legal Framework in the UK

There are three key statutory cross-border insolvency regimes in place in the UK: the EC Insolvency Regulation 2000, the Cross-Border Insolvency Regulations 2006 and the provisions relating to co-operation between courts in the Insolvency Act 1986. Common law principles may also apply and all form part of national law. The regimes share some common aims, including in relation to recognition of foreign proceedings, determination of which country's laws apply, access to courts and judicial co-operation.

4.2. EC Insolvency Regulation

The main purpose of the EC Insolvency Regulation, which applies in all EU member states except Denmark, is to establish a framework within which

the different insolvency regimes of individual member states can interact more effectively. It does this partly by providing for automatic EU-wide recognition of collective insolvency proceedings. These proceedings, known as "main proceedings", can only be opened in a member state where a debtor has its centre of main interests ("COMI") and will be governed by the insolvency laws of that member state. In the case of the UK, administrations, CVAs, compulsory liquidations and CVLs (the latter confirmed by court order) will automatically be recognised in other member states once main proceedings have been opened. Where a company has an establishment and assets in a member state other than the one in which it has its COMI, secondary proceedings may be commenced in that member state. For the time being, these must be winding-up proceedings, in respect of which local law will apply.

Case law has confirmed that the EC Insolvency Regulation has extended the insolvency law jurisdiction of the English courts to include non-EU registered companies that have their COMI in England.

Note that a revised version of the regulation is expected to come into effect in 2017. The amendments include changing the definition of insolvency proceedings to include hybrid and pre-insolvency proceedings, adding new language to assist the determination of COMI, extending the type of secondary proceedings to include any appropriate insolvency proceedings (not just winding-up proceedings) and introducing specific rules in relation to the insolvency of multi-national groups of companies.

Separate regulations exist to deal with the winding up and reorganisation of credit institutions and insurance undertakings.

4.3. Cross-Border Insolvency Regulations 2006

The Cross-Border Insolvency Regulations 2006 implement the UNCITRAL Model Law on Cross-Border Insolvency in the UK. They provide a basis for judicial co-operation where the EC Insolvency Regulation does not apply. In particular, they provide for recognition of foreign insolvency proceedings in Britain and access to British courts for foreign insolvency practitioners and creditors in cross-border insolvencies. They also provide for co-operation between courts of different jurisdictions and for co-ordination of cross-border insolvency proceedings. The Model Law has been enacted in 22 jurisdictions so far, including in the USA as Chapter 15 of the US Bankruptcy Code, and has proved to be a useful tool in cross-border insolvencies.

4.4. Cross-Border Co-operation under the Insolvency Act 1986

The Insolvency Act 1986 contains provisions for co-operation and assistance in relation to corporate insolvencies between the courts of UK jurisdictions (England and Wales, Scotland and Northern Ireland) and between those courts and the courts of certain designated countries. These are principally Commonwealth countries. Such countries have enacted equivalent reciprocal arrangements. The provisions are complementary to those found in the Cross-Border Insolvency Regulations 2006. The process is initiated by the foreign court or a Scottish or Northern Irish court making a request on behalf of the local insolvency office holder to the English court for assistance.

Slaughter and May

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This note provides an introduction to English insolvency law and is not intended to contain definitive legal advice, which should be sought, as appropriate, in relation to any particular transaction. If legal advice is required, please refer to Ian Johnson or Tom Vickers at Slaughter and May or your usual contact at the firm.

4.5. Common Law

Judicial assistance is also available under English common law. It relies on the debtor having a “presence of assets” or “sufficient connection” with England and may, for example, be used in cases where the debtor is excluded from the ambit of the EC Insolvency Regulation or the Cross-Border Insolvency Regulations 2006. Thus, a foreign representative may apply to the English courts for relief even in the absence of recognition under the Regulations.

5. RESTRUCTURING

Over recent years there has been a shift away from formal insolvency proceedings as creditors increasingly favour restructuring the debt of companies in financial difficulties by privately negotiated agreements. As a restructuring is a non-statutory remedy, there is no moratorium unless agreed between the creditors. Nor is there a statutory mechanism by which to compel a dissenting creditor to participate in the restructuring unless a formal procedure such as a CVA or a scheme of arrangement is included in the process, although the contractual arrangements may provide for this. In 2010, the Insolvency Service began a consultation on a number of proposals for a new court-based moratorium procedure for companies that are seeking to restructure their debts. However, responses were mixed and plans for a further consultation have been postponed.

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