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Private International Law Rules in Insolvency: The British Model

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Introduction

The rise of international commerce and the ease of setting up in more than one jurisdiction now means that many companies have little difficulty in gearing their economic expansion to a global scale. Just as expansion has brought considerations of conflicts of law and choice of law in international contracts and litigation, so too the periodic downturns in the world economy have brought considerations of private international law rules in relation to insolvencies. Insolvencies with an international dimension raise a number of important issues, including the diversity of laws which are potentially applicable to the transactions of a single company and which have important consequences at the time of insolvency.¹

This phenomenon has induced courts to begin to co-operate with each other, realising that insolvency can have far-reaching consequences on society and economies, both local and foreign. With the number of international insolvencies likely to increase, as a function of the decline in the world economy, this spirit of co-operation, though not universal in coverage, can only be applauded.

Common-Law Jurisdiction Principles

It is a general principle of law that the law of the state of incorporation of the company governs its status from creation to dissolution.² The recognition of the subjection of a foreign company to a foreign law does not necessarily mean the domestic courts will not assume some jurisdiction. The nature of these proceedings is described as ancillary to main proceedings being undertaken in the home jurisdiction of the company, the proposition being stated thus in Re: Matheson by Kay J.: "The mere existence of a winding-up order made by a foreign court does not take away the rights of a court of this country to make a winding-up order here, though it would no doubt exercise an influence upon this court..."³ and reiterated in Re: Commercial Bank of South Australia, where on the suspension of a bank incorporated in South Australia followed by a winding-up order, the creditors were held entitled to a winding-up order in England, the nature of which was described by North J. as "...ancillary to a winding-up in Australia...."⁴

¹Gardiner v Houghton (1862) 2 B & S 743; Antony Gibbs & Sons v Société Industrielle et Commerciale des Métaux (1890) 25 QBD 399.

²Cheshire & North, *Private international Law* (12th ed.) Butterworths at p 897.

³Re: Matheson Brothers Ltd. (1884) 27 Ch D. 225 at 230.

⁴Re: Commercial Bank of South Australia (1886) 33 Ch D. 174 at 178.

The extension of this jurisdiction often involves determining the precise application of provisions of domestic company legislation to foreign companies as in Re: Mercantile Bank of Australia,⁵ where the power to appoint a receiver and to require security to be given by a liquidator was held applicable to a company incorporated in Victoria but conducting business in London. The relationship of various classes of creditors standing to gain or lose by the winding-up process may influence the decision of a court as is seen in the case of Re: English, Scottish and Australian Chartered Bank,⁶ in which it was held that, as there was nothing unreasonable or unfair in the proposed scheme of reconstruction as between different classes of creditors, the expressed majority opinion should prevail. Nevertheless, a court may be keen to ensure that the priorities between proceedings in different jurisdictions are firmly set to ensure that any disparity in rights available to creditors acting in different jurisdictions do not affect the overall settlement of the liquidation.

A court may grant the enforcement of rights acquired in priority to insolvency proceedings beginning,⁷ though any disparity in the treatment of creditors may prompt the court to restrain one class of creditor from exercising rights available in another jurisdiction, as in the case of Re: Vocalion (Foreign) Ltd.,⁸ where it was held that a court may in the exercise of its equitable jurisdiction restrain a party from proceeding with an action on liability incurred abroad brought in a foreign court. A prime consideration is whether substantial justice is more likely to be attained by allowing the foreign proceedings to continue. Per Maugham J.: "It must be remembered that foreign creditors ... can not be restrained from taking such proceedings ... in their own country; ... the only result of such an injunction ... may be to benefit other foreign creditors without in any way increasing the amount of the assets ... distributable in the liquidation in this country."⁹

The costs of an ancillary liquidation may well amount to the equivalent of a full liquidation, particularly if decisions of liquidators are contested in several jurisdictions. The increase in costs is a factor that often motivates courts in deciding whether to permit further litigation as, from a practical standpoint, the result can only be to the detriment of creditors. The discretion to permit proceedings is also influenced by the just merits of the creditors' claims and the unfair result on their position especially where the company concerned, as in the case of Re: Suidair,¹⁰ had acted to the detriment of creditors in one jurisdiction. The ability of foreign liquidators to operate in the ancillary jurisdiction is of considerable advantage but not without some degree of difficulty. Apart from the question of recognition of the liquidator's qualification to act, there is the question of the degree of responsibility the liquidator may owe to the court in the main jurisdiction, which may lead to conflict between courts exercising jurisdiction in the same insolvency. This subject was treated

⁵Re: Mercantile Bank of Australia [1892] 2 Ch 204.

⁶Re: English, Scottish and Australian Chartered Bank [1893] 3 Ch 385.

⁷Galbraith v Grimshaw [1910] AC 508.

⁸Re: Vocalion (Foreign) Ltd. [1932] 2 Ch 196.

⁹*Ibid.* at p205.

¹⁰Re: Suidair International Airways Ltd. [1951] 1 Ch 165.

in the case of Schemmer,¹¹ where it was held that before the English courts would recognise the title of a foreign receiver to assets in the jurisdiction or direct the establishment of ancillary receivership proceedings, the courts would have to be satisfied of the nexus between the defendant companies and the jurisdiction in which the receiver was appointed.¹²

A particular result of the development of case-law in this field is that the courts have not been slow to entertain the institution of ancillary proceedings where these are appropriate. The question of whether the ancillary jurisdiction may take a lead in the proceedings is one that has often been put, especially where the connexion of the foreign company is greater with the ancillary jurisdiction. A recent example is the case of Re: A Company (1987),¹³ in which it was held that, for a court to make a winding up order against a foreign corporation, it was not necessary to show that the company had assets within the jurisdiction but that there was a close link with the jurisdiction, which on the facts: company management, bank accounts and main business situated within the jurisdiction, made the courts in England the most appropriate to deal with the matter.

The precise role to be played by the ancillary jurisdiction in cases where proceedings were at an advance stage in the main jurisdiction is often a point of contention between the courts. It may be that the ancillary jurisdiction would prefer a winding-up to be instituted while the main jurisdiction has in mind preservation proceedings, enabling the company to continue its operations in a restricted form, with appropriate court supervision. These issues were the subject of the leading case of Felixstowe,¹⁴ where the proper approach of an English court was held to regard the courts of the country of incorporation as the appropriate legal forum for controlling the winding-up of that company. Where that company had assets in England, the normal procedure was to carry out an ancillary winding-up in harmony with the main court. However, a foreign (United States) restraining order which required assets to be moved outside the jurisdiction could have no effect in England on an English court. It was noted that, as the English practice was in harmony with certain provisions of the United States Bankruptcy Code,¹⁵ and, on the balance of convenience test, the defendants suffered no material prejudice as the assets remained preserved with no garnishee orders being permitted, the injunctions would be continued.

The case-law makes it clear that the courts retain a substantial discretion, particularly over whether to permit ancillary winding-up proceedings as in Re: Wallace Smith Group Ltd.,¹⁶ where a petition was dismissed as to allow it would have prejudiced concurrent proceedings on the same issue in the

¹¹Schemmer and Others v Property Resources Ltd. and Others [1975] 1 Ch 273.

¹²See Marks D., The Rights and Reliefs for Foreign Liquidators in England (1995-96) 1 RALQ 37.

¹³Re: A Company (No. 00359 of 1987) [1988] 1 Ch 210.

¹⁴Felixstowe Dock and Railway Co. v United States Lines [1988] 2 All ER 77.

¹⁵s304, United States Bankruptcy Code (11 USC s304) (For examples, see Re: Banco Ambrosiano Overseas Ltd. Bkrcty 25 BR 621 (1982), Interpool Ltd. v KKL and others 102 BR 373 (1988) and Lindner Fund Inc. v Polly Peck International PLC 143 BR 807 (1992)).

¹⁶Re: Wallace Smith Group Ltd. [1992] BCLC 989.

Ontario courts. It is not the case that once indebtedness is shown, together with a connexion with the jurisdiction and the possibility of benefit to creditors within the jurisdiction, that an ancillary winding-up order is automatic. The courts retained a discretion, one of the factors being whether there was a more appropriate jurisdiction for the claim.

Winding-Up of Foreign Companies by Statute

Overseas companies,¹⁷ who establish a place of business in England and Wales or in Scotland, may register with the Registrar of Companies.¹⁸ The courts in these countries may, by virtue of this registration, entertain winding-up proceedings involving these companies.¹⁹ A jurisdiction conferred by statute has long existed for the winding-up of unregistered companies,²⁰ the definition of which may include foreign corporations.²¹ This was not considered as creating any particular legal problem where these companies continued to exist elsewhere, the winding-up applying only to their activities within the jurisdiction. Doubts arose because of the effect of the nationalisation decrees following the 1917 October Revolution in Russia, the effect of which subsequently became apparent as various suits against banks established in Moscow with operations in London were struck out as wanting, because of the prior dissolution of these companies in their place of incorporation.²²

Following a series of cases involving companies which had ceased to exist, the United Kingdom Companies Act 1929, which provided for the winding-up of an unregistered company, was extended to cover the situation where a company, which though operating within the jurisdiction through a branch or other office, had been dissolved in its place of incorporation.²³ It was held in the case of the Russian and English Bank that a foreign company, notwithstanding its dissolution in its place of origin, may be wound up as an unregistered company in England, when an action may be brought in its name to recover moneys due and unpaid at the time of its dissolution. Lord Atkin, one of the members of the panel, opined: "I think it is a necessary implication [of the provisions of the Companies Act] that the dissolved foreign company is to be wound up as though it had not been dissolved and therefore continued

¹⁷The definition of an "overseas company" in s744, Companies Act 1985 requires that a company incorporated outside the UK have a place of business within the UK for the purposes of Part XXIII of that Act.

¹⁸s691, Companies Act 1985.

¹⁹ss117, 120, Insolvency Act 1986.

²⁰s221, Insolvency Act 1986.

²¹See s32(3), Companies (Winding-Up) Act 1890 applying the Act to companies not having a registered office within the jurisdiction by the use of a deeming provision.

²²Lazard Brothers & Co. v Midland Bank Ltd. [1933] AC 289 (Garnishee proceedings on assets in London of a bank dissolved in Russia held void on grounds of it ceasing to exist).

²³s338(2), Companies Act 1929 reads:

"Where a company incorporated outside Great Britain which has been carrying on business in Great Britain ceases to carry on business in Great Britain, it may be wound up as an unregistered company under this part of this Act, notwithstanding that it has been dissolved or otherwise ceased to exist as a company under or by virtue of the laws of the country in which it was incorporated."

in existence.”²⁴ This extension of jurisdiction was confirmed in Re: Russian Bank for Foreign Trade,²⁵ which concluded that the impossibility of a branch continuing to function when its main office had ceased to exist according to its statutes of incorporation was ample reason to order a winding-up. In the case of Re: Banque des Marchands de Moscou (Koupetschetsky),²⁶ proceedings under the new United Kingdom Companies Act,²⁷ the claims of various creditors were held subject to Russian law and that the revival of the company for the purposes of winding-up could not revive claims which were barred by the nationalisation decree.

The situation of foreign confiscatory legislation could not, however, remove those obligations that the company had acquired within the jurisdiction where proceedings were being instituted, whether this company was the subject of liquidation proceedings or proceedings for the enforcement of debt as in the case of Metliss,²⁸ where it was held that, although Greek law had to be examined to ascertain the nature of the juridical body being created by the decree, the succession of this body to obligations acquired by its predecessor and expressed as being subject to English law must be examined by principles of English law. The nature of the obligations situated within the jurisdiction was the subject of Re: Compania Merabello²⁹ where it was stated that normally a case falling under the Companies Act envisaged no need to establish that the company had a place of business or that it had carried out business in the jurisdiction, but required a connexion with the jurisdiction and the presence of some assets of benefit to creditors. The nature of these assets might be intangible, such as a right of action, the success of which need not be proved to obtain a winding-up order, as was the case in Re: Allobrogia,³⁰ or might even consist of a potential claim against a statutory scheme, as in Re: Eloc.³¹

Co-operation between Courts

Many of the acts passed to regulate bankruptcy contained provisions dealing with the scope of assistance by one court to another within the Commonwealth. The history of the present provision in the United Kingdom goes far into the last century.³² However, for the purposes of this article, consideration to this history begins this century with the enactment of the Bankruptcy Act 1914.³³ This Act was originally designed as a measure to co-ordinate provisions and enabled the courts within the Commonwealth to request other courts to assist in the enforcement of bankruptcy proceedings within their own jurisdiction. This reciprocal assistance was embodied in the

²⁴Russian and English Bank v Baring Bros & Co. [1936] AC 405 at 427.

²⁵Re: Russian Bank for Foreign Trade [1933] 1 Ch 745.

²⁶Re: Banque des Marchands de Moscou (Koupetschetsky) (Royal Exchange Assurance v Liquidator) [1952] 1 All ER 1269; (Ouchkoff v Liquidator) [1954] 2 All ER 746.

²⁷s399, Companies Act 1948.

²⁸Metliss v National Bank of Greece and Athens SA [1958] AC 509.

²⁹Re: Compania Merabello San Nicholas SA [1973] 1 Ch 75.

³⁰Re: Allobrogia Steamship Corporation [1978] 3 All ER 425.

³¹Re: Eloc Electro-Optieck & Communicatie BV [1982] 1 Ch 43.

³²s220, Bankruptcy Act 1849.

³³s122, Bankruptcy Act 1914.

Act as a response to the growing numbers of insolvencies of persons and partnerships, to which the Act applied. The remit and purpose of the section were considered in Re: A Debtor,³⁴ in which it was held that the definition of “bankruptcy” referred to the judicial process dealing with insolvent persons and was to be construed in a wide sense as the section was designed to produce co-operation between courts acting under different systems of law. Once an English court was satisfied the request for aid fell within the ambit of the provision, there was no general duty to scrutinise anterior proceedings unless it could be shown that they were defective under the proper law of the court or that they offended against public policy.

The present provision in the United Kingdom relating to reciprocal assistance is contained in the Insolvency Act.³⁵ Owing to the consolidation of provisions relating to the bankruptcy of individuals and the insolvency procedures applicable to companies and other legal persons in the same Act, section 426 applies to both types of insolvencies. The number of Commonwealth countries to which the rules on assistance apply is at present limited.³⁶ This section has, however, been considered in a number of leading cases, not least in the growing number of international banking insolvencies. One of the most important statements of the purpose of this section came in Re: Dallhold,³⁷ where the liquidator applied to the Australian Federal Court for the issue of a letter of request to the English court for an administration order, following which directions were given in England for the presentation of a petition for an administration order by the provisional liquidator in England. The effect of the Act was held to confer on the English courts a jurisdiction to apply any domestic remedy. As the conditions were satisfied, an administration order would be made. The discretion in the Act extended solely to the granting of the request and not the application of the rules of insolvency law to a request which, once granted, was mandatory.

³⁴Re: A Debtor (ex parte the Viscount of the Royal Court of Jersey) [1980] 3 All ER 665.

³⁵s426, Insolvency Act 1986, the relevant parts of which read as follows:

“(4) The courts having jurisdiction in relation to insolvency law in any part of the United Kingdom shall assist the courts having the corresponding jurisdiction in any other part of the United Kingdom or any relevant country or territory.

(5) For the purposes of subsection (4), a request made to a court in any part of the United Kingdom by a court in any other part of the United Kingdom or in a relevant country or territory is authority for the court to which the request is made to apply, in relation to any matters specified in the request, the insolvency law which is applicable by either court in relation to comparable matters falling within its jurisdiction.

(11) In this section “relevant country or territory” means-

(a) any of the Channel Islands or the Isle of Man, or

(b) any country or territory designated for the purposes of this section by the Secretary of State by order made by statutory instrument.”

³⁶The Co-operation of Insolvency Courts (Designation of Relevant Countries and Territories) Order (SI1986/2123) specifies the following: Anguilla, Australia, The Bahamas, Bermuda, Botswana, Canada, Cayman Islands, Falkland Islands, Gibraltar, Hong Kong, Eire, Montserrat, New Zealand, St. Helena, Turks & Caicos Islands, Tuvalu and Virgin Islands. The Co-operation of Insolvency Courts (Designation of Relevant Countries) Order 1996 (SI 1996/253), which came into effect on 1st March 1996, also designates Malaysia and South Africa.

³⁷Re: Dallhold Estates (UK) Pty. Ltd. [1992] BCC 394.

Consideration of whether courts had a particular choice as to what rules to apply came in Re: BCCI,³⁸ where the liquidators in England and the Cayman Islands sought to commence proceedings against a former director of the bank and associated companies to recover the deficiency in the assets. Rattee J. noted that: "... the effect of s.426 is to give [the] court a discretion... as to whether it should apply English insolvency law whether 'procedural' or 'substantive' or the law of the requesting court...".³⁹ It is now clear that once a request for assistance is granted, it naturally follows that a court, where it chooses to apply domestic law, will apply all of the rules of insolvency law that would apply to a domestic insolvency subject to any exercise of discretion in the application of these rules that would feature in a domestic case.⁴⁰ There remains, however, the question of what foreign law rules the domestic court may choose to apply or disapply.⁴¹

The continuing evolution of co-operation is being seen in other proceedings in the context of insolvency, as the result indicates in Re: MCC,⁴² where an injunction, intended to prevent proceedings being brought in another jurisdiction to recover a preference, was denied on the grounds that an English court should not interfere with foreign proceedings where proceedings are legitimately brought and maintained in that jurisdiction. It was also held in that case that courts in this situation should not take the view that there is only one natural forum in which all proceedings must be brought. This must be seen as a remarkable step in the arena of co-operation between courts.

Summary

International insolvency has aroused a great deal of interest in recent years, owing to the spectacular rise in cases of the collapse of banks and multinational companies situated in a variety of jurisdictions. There is noticeable progress in the United Kingdom from the traditional common-law methods of asserting jurisdiction and their statutory equivalents, which lead inevitably to the winding-up of the company, towards procedures for reciprocal assistance, which allow domestic procedures to be extended to the foreign company, often allowing the company to attempt to consolidate its economic future, through the judicious use of rescue regimes.

In the United Kingdom, the rules relating to jurisdiction, recognition and enforcement rules are likely to undergo change, insofar as Britain's partners in the European Union are concerned, with the adoption of the European

³⁸Re: BCCI [1993] BCC 787.

³⁹Ibid. at 801-802.

⁴⁰Recent cases on the operation of this section are Re: Focus Insurance Co. Ltd. (1996) Times 6 May (Ch. Div.) and Re: Business City Express Ltd. (unreported) 20 January 1997 (Ch. Div.), Re: Electrical Mutual Liability Insurance Co. Ltd. (unreported) 28 January 1997 (CA), summaries of which are noted in Obank R., International Co-Operation and Foreign Insolvencies (1997) 6 JIBFL 269.

⁴¹See Re: Bell Lines Ltd. (unreported) 6 February 1997 (per Jacob J.), cited in Turing D., Set-Off and Netting: Developments in 1996 affecting Banks (1997) 4 JIBFL 155 at 158 (stay on set-off effective in Ireland given effect in England).

⁴²Re: Maxwell Communications Corporation [1992] BCC 757.

Insolvency Convention.⁴³ Nevertheless, this Convention will not affect existing arrangements with other, predominantly Commonwealth countries. Already, international insolvencies have become a regular feature of the insolvency practitioner's practice. Practitioners are already aware that much needs to be done to develop an international protocol for these types of insolvencies.⁴⁴ There are calls for courts to recognise the benefits of co-operation and to develop practice consonant with the needs of international business to implement rescues and termination procedures with speed and efficiency. This will have the added benefit of offering creditors, employees and other affected parties the best outcome possible in insolvency proceedings.

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⁴³See Omar P., An Introduction to the European Insolvency Convention (1995-6) 4 RALQ 245.

⁴⁴See Morris C., Lessons learnt from the Collapse of BCCI (1994) 1 RALQ 5.