

EXPLANATORY MEMORANDUM TO
THE CROSS-BORDER INSOLVENCY REGULATIONS 2006

2006 No. 1030

1. This explanatory memorandum has been prepared by the Department of Trade and Industry and is laid before Parliament by Command of Her Majesty.

This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Description

- 2.1 Recognising that disparities in national laws governing international trade created obstacles to the free flow of trade, the UN General Assembly established the United Nations Commission on International Trade Law (“UNCITRAL”) and regarded the Commission as a vehicle by which the UN could play a more active role in reducing or removing these obstacles. A project to produce a Model Law on cross-border insolvency was initiated by UNCITRAL and in the early 1990s two international colloquiums were held to discuss whether that body should facilitate the development of a legal instrument providing a framework, which would encompass judicial cooperation, court access for foreign insolvency administrators and recognition of foreign insolvency proceedings. In 1995 a working group was established and in 1997, as a result of their work, UNCITRAL adopted the text of a model law designed to assist States to equip their insolvency laws with a modern, harmonised and fair framework to address more effectively instances of cross-border insolvency. The model law is intended to cover cases, for example, where the debtor has assets in more than one State or where some of the creditors of the debtor are not from the State where the insolvency proceeding is taking place.

- 2.2 This instrument gives effect to the model law in Great Britain.

3. Matters of special interest to the Joint Committee on Statutory Instruments

None

4. Legislative Background

- 4.1. The Regulations are made under section 14 of the Insolvency Act 2000 (c.39). Section 14 allows the Secretary of State by regulations to make any provision, which he considers necessary or expedient for the purpose of giving effect, with or without modifications, to the UNCITRAL model law on cross-border insolvency. This is the first use of the power in section 14 to give effect to the model law in Great Britain.
- 4.2. The Regulations are subject to the affirmative resolution procedure and making the Regulations requires the agreement of the Lord Chancellor insofar as they extend to England and Wales and of the Scottish Ministers insofar as they extend to Scotland.

5. Extent

This instrument applies to Great Britain. The instrument will not apply to Northern Ireland.

6. European Convention on Human Rights

Gerry Sutcliffe MP, Parliamentary Under Secretary of State for Employment Relations and Consumer Affairs, Department of Trade and Industry has made the following statement regarding Human Rights:

In my view the provisions of the Cross-border Insolvency Regulations 2006 are compatible with the Convention rights.

7. Policy background

Introduction

- 7.1. National insolvency laws are often not designed to cope with cross-border insolvencies and any problems that arise whether jurisdictional or practical. This makes it difficult to administer such insolvencies both quickly and effectively and any conflict in respective national laws can result in the dissipation of assets and the loss of a potential opportunity to rescue a viable business. Such uncertainties can be a barrier to trade and can have a negative impact on the flow of investment between countries. The UNCITRAL Model Law on cross-border insolvency is that body's attempt to promote modern and fair legislation for cases where the insolvent debtor has assets in more than one State. The Model Law is, however, designed to respect the differences amongst national procedural laws and does not attempt a substantive unification of insolvency laws.
- 7.2. The British Government has a commitment to the promotion of a rescue culture and supports the Model Law as an appropriate legislative tool to support this objective on the wider international stage. In addition, implementation of the Model Law will be beneficial in serving the cause of fairness towards creditors who may be located anywhere in the world. We hope that it may also provide an example to other countries of our readiness to engage in a genuine process of co-operation in international insolvency matters and that our actions will encourage other countries to implement the Model Law. In this way, insolvency officeholders in Great Britain should be able to enjoy, progressively, the same benefits abroad as their international counterparts, and be able to reduce administrative costs incurred in recovering assets from overseas. As a result funds available for distribution to creditors, wherever they are located, should increase.
- 7.3. Limitations on cooperation and coordination between different national jurisdictions can be the result of lack of a legislative framework or from uncertainty regarding the scope of the existing legislative authority, for pursuing cooperation with foreign courts. The passage of a specific legislative framework is useful for promoting international cooperation in cross border cases. The Model Law fills the gap found in many national laws by expressly empowering courts to extend cooperation in the areas covered by the Model Law.

7.4. In May 2002, the European Union adopted its own Regulation on insolvency proceedings. There is a significant element of overlap between the UNCITRAL Model Law and the EC Insolvency Regulation and although the latter governs only the coordination of insolvency proceedings within the European Union, its underlying principles and approaches have been extremely influential in the international community. However the Regulation does not deal with cross-border insolvency matters extending beyond Member States of the European Union. Thus, the Model Law will provide a complementary regime of considerable practical value that will be capable of addressing instances of cross-border insolvency and cooperation outside the European Union. This will place Great Britain, by virtue of the operation of s426 of the Insolvency Act 1986, in the unique position of having a suite of statutory procedures available in cross-border insolvency cases, as well as the flexibility of common law.

Key provisions of the Model Law

- 7.5. Some of the key aims of the Model Law as set out in the Regulations and the way it will operate are summarised below.
- 7.6. An important objective of the Model Law is to provide direct access for the person administering a foreign insolvency proceeding (the foreign representative) to the courts of this country to seek a temporary respite and to allow the courts to determine what relief or coordination is needed for the optimal disposition of the insolvency.
- 7.7. The foreign representative is given the right to initiate an insolvency proceeding in this country in relation to the debtor who is the subject of the foreign proceeding and the right to participate in a British insolvency proceeding regarding that debtor.
- 7.8. The Model Law establishes criteria for determining whether a foreign proceeding is to be recognised and if so whether as a “main” or “non-main” (depending on whether the foreign proceeding is taking place in the country where the main operations of the business are located).
- 7.9. The Model Law sets out the effects of recognition and the relief available to a foreign representative. The relief accorded upon recognition of a foreign main proceeding includes a stay of actions by individual creditors and of enforcement proceedings against the debtor and a suspension of the debtor’s right to dispose of or encumber assets. This moratorium (which is automatically triggered by the recognition of a foreign main proceeding) provides a respite until appropriate measures can be put in place for the reorganisation or liquidation of the debtor’s assets. Exceptions and limitations to the moratorium will be the same as if the debtor had been wound up or made bankrupt under British insolvency law.
- 7.10. Following comments from respondents to our consultation, we have clarified that the stay and suspension does not affect specified security rights or the exercise of set-off rights which will be exercisable in the same way as they would in a British winding up or bankruptcy. This is intended to give protection to secured creditors and enable them to have greater predictability as to the likely outcome in a cross-border insolvency.
- 7.11. The Model Law also provides for the court to grant discretionary relief for the benefit of any recognised foreign proceeding, whether main or non-main. Such discretionary relief may consist of access to information concerning the assets of the debtor, appointing a person to administer all or part of those assets and any other relief that may be available

under British insolvency law (including the kind of moratorium imposed in a British administration). Urgently needed relief may be granted by the court on an interim basis pending a decision on formal recognition.

- 7.12. The Model Law contains provisions to protect the interests of local creditors (including secured creditors), the debtor and other affected persons. In particular, the court cannot grant discretionary relief without being satisfied that the interests of such persons are adequately protected. The court may subject the relief it grants to conditions and may modify or terminate the relief granted if so requested by a person affected by such a provision.
- 7.13. Recognition of foreign proceedings does not prevent local creditors from initiating or continuing with insolvency proceedings in this country in relation to the debtor.
- 7.14. The Model Law also aims to provide a transparent regime for the right of foreign creditors to commence and participate in an insolvency proceeding in this country.
- 7.15. A further key aim of the Model Law is to provide a legislative framework for cooperation and coordination between courts and insolvency officeholders in different States. Accordingly the Model Law expressly provides for the British courts to have the power to cooperate to the maximum extent possible with foreign courts or foreign representatives in the areas covered by the Model Law. In addition, a duty to cooperate is placed on British insolvency officeholders (to the extent it does not conflict with their duties under British insolvency law).
- 7.16. Furthermore, the Model Law provides for the coordination of a British insolvency proceeding and a foreign proceeding concerning the same debtor and facilitates coordination between two or more foreign proceedings concerning the same debtor. This is intended to foster coordinated decisions that would best achieve the objectives of both proceedings.
- 7.17. Finally, the Model Law expressly authorises British courts and insolvency officeholders to seek assistance from foreign courts and foreign representatives.

Our approach to enactment

- 7.18. The Model Law is a legislative text that is recommended to countries for incorporation into their national law. In Great Britain, we have tried follow UNCITRAL's exhortation to stay as close as possible to the original drafting in order to ensure consistency, certainty and harmonisation with other countries enacting the Model Law.
- 7.19. The language of the Model Law is similar to that used in international treaties and conventions and will almost certainly be approached by the courts in that way, i.e. it will be interpreted purposively. Accordingly the UNCITRAL Guide to Enactment will be a useful tool in interpreting the text.
- 7.20. Following consultation with the Treasury and in view of the extensive EC legislation regarding the winding up and reorganisation of credit institutions and insurance companies, it was decided to exclude these bodies from the ambit of the Regulations. However, a number of respondents to the consultation have asked that they be included and after further consultation with the Treasury we have agreed that there could be benefits in doing so. However, the interaction between the Model Law and the relevant

EC legislation needs to be dealt with correctly. As the drafting of these provisions will take time, we have decided not to include them within the Model Law for the time being, but will consider their inclusion as soon as it is practicable and possible.

Scotland

7.21. The Regulations will apply to Scotland and accordingly they require the consent of the Scottish Ministers. In Scotland, the Regulations will be supplemented by Rules of Court both in the Court of Session and the sheriff court. These Rules are the responsibility of the Lord President of the Court of Session and are being developed separately, with a view to implementation to coincide with the commencement date for the Regulations.

Consultation

7.22. The Insolvency Service have engaged in discussion and exchange with other government departments, representative organisations and other interested parties, with regard to the implementation of the UNCITRAL Model Law on cross-border insolvency in Great Britain. This has included:-

22nd August 2005 – A public consultation on the Insolvency Service’s proposals to implement the UNCITRAL Model Law on Cross-Border Insolvency in Great Britain

October 2005 – Meeting with the Department for Constitutional Affairs and senior members of the Judiciary to hear their views about the implementation of the Model Law.

October/November 2005 – Meetings with the Insolvency Lawyers Association (ILA) - a representative of the Insolvency Service attended all the meetings held by the ILA in considering the consultation document.

January 2006 – Meeting with The Law Society to discuss their concerns about the implementation of the Model Law.

7.23. The consultation paper was sent to approximately 100 individuals, organisations and other government departments. We received 12 replies from a range of respondents, including many representative groups. Many of the responses were well thought out and of high quality and were overall in favour of implementing the Model Law. In the consultation response document, we have answered the issues raised by the respondents to the consultation, highlighting the main issues raised and detailing how we intend to proceed taking into account comments made and other pertinent information obtained since the commencement of the consultation.

7.24. Details of the consultation and response document can be found on The Insolvency Service website through the following link:-

http://www.insolvency.gov.uk/insolvencyprofessionandlegislation/con_doc_register/registerindex.htm

8. Impact

8.1 As the incidence of cases using the Model Law is predicted to be relatively low and any costs and/or regulatory impact is likely to be negligible, a Regulatory Impact Assessment has not been prepared for this instrument.

8.2 The framework should enable businesses and individuals to act with certainty by providing a predictable low cost regime for initiating and dealing with cross-border insolvency proceedings. The key benefits will be greater legal certainty and predictable procedures. There have been no specific compliance cost issues identified to date and there were no specific views raised from the consultation on this issue.

9. Contact

Any queries regarding this instrument can be addressed to Christine McCreath, Assistant Director, Policy Unit, The Insolvency Service, Room 510, 21 Bloomsbury Street, London, WC1B 3QW Tel: 020 7291 6858 or e-mail: [Christine.McCreath@insolvency.gsi.gov.uk]