House of Lords
House of Commons

Joint Committee on Statutory Instruments

Forty-second Report of Session 2017–19

Drawing special attention to:

Insolvency (Amendment) (EU Exit) Regulations 2018 **(Draft S.I.)**

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Joint Committee on Statutory Instruments

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The full constitution and powers of the Committee are set out in House of Commons Standing Order No. 151 and House of Lords Standing Order No. 73, available on the Internet via www.parliament.uk/jcsi.

Remit

The Joint Committee on Statutory Instruments (JCSI) is appointed to consider statutory instruments made in exercise of powers granted by Act of Parliament. Instruments not laid before Parliament are included within the Committee's remit; but local instruments and instruments made by devolved administrations are not considered by JCSI unless they are required to be laid before Parliament.

The role of the JCSI, whose membership is drawn from both Houses of Parliament, is to assess the technical qualities of each instrument that falls within its remit and to decide whether to draw the special attention of each House to any instrument on one or more of the following grounds:

i that it imposes, or sets the amount of, a charge on public revenue or that it requires payment for a licence, consent or service to be made to the Exchequer, a government department or a public or local authority, or sets the amount of the payment;

ii that its parent legislation says that it cannot be challenged in the courts;

iii that it appears to have retrospective effect without the express authority of the parent legislation;

iv that there appears to have been unjustifiable delay in publishing it or laying it before Parliament;

v that there appears to have been unjustifiable delay in sending a notification under the proviso to section 4(1) of the Statutory Instruments Act 1946, where the instrument has come into force before it has been laid;

vi that there appears to be doubt about whether there is power to make it or that it appears to make an unusual or unexpected use of the power to make;

vii that its form or meaning needs to be explained;

viii that its drafting appears to be defective;

ix any other ground which does not go to its merits or the policy behind it.

The Committee usually meets weekly when Parliament is sitting.

Publications

The reports of the Committee are published by Order of both Houses. All publications of the Committee are on the Internet at www.parliament.uk/jcsi.

Committee staff

The current staff of the Committee are Jeanne Delebarre (Commons Clerk), Jane White (Lords Clerk) and Liz Booth (Committee Assistant). Advisory Counsel: Daniel Greenberg, Klara Banaszak, Peter Brooksbank, Philip Davies and Vanessa MacNair (Commons); James Cooper, Nicholas Beach, John Crane and Ché Diamond (Lords).

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Instruments reported

At its meeting on 19 December 2018 the Committee scrutinised a number of Instruments in accordance with Standing Orders. It was agreed that the special attention of both Houses should be drawn to one of those considered. The Instrument and the ground for reporting it is given below. The relevant Departmental memorandum, is published as an appendix to this report.

1 Draft S.I.: Reported for requiring elucidation, for defective drafting and for unexpected use of powers

Insolvency (Amendment) (EU Exit) Regulations 2018

1.1 **The Committee draws the special attention of both Houses to these draft Regulations on the grounds that they require elucidation in one respect, that they are defectively drafted in one respect and that they make an unexpected use of the enabling power.**

1.2 These Regulations are made under the European Union (Withdrawal) Act 2018 ("the 2018 Act"). The purpose of the Regulations is to address deficiencies in legislation in the field of cross-border insolvency that would arise if the UK were to leave the EU without a deal. In particular, they amend Regulation (EU) 2015/848 on insolvency proceedings ("the EU Insolvency Regulation"). Under the 2018 Act, that Regulation will become part of UK domestic law on exit day.

1.3 The EU Insolvency Regulation currently deals with cross-border jurisdiction, co-operation, recognition and enforcement in insolvency proceedings in the EU. It imposes restrictions on the jurisdiction of the courts of an EU member State in respect of insolvency in cases where the debtor has assets and liabilities in more than one member State. It also provides for insolvency proceedings commenced in one member State to be automatically recognised in the other member States.

1.4 According to the Explanatory Memorandum—

- "the primary purpose of [the draft Regulations] is to retain the EU Insolvency Regulation in a form that will operate effectively after exit day";[1]
- the EU Insolvency Regulation "cannot operate properly without the reciprocal application of its provisions between the UK and the states of the EU. Absent such reciprocation it would, for example, create an obligation for the UK to recognise incoming insolvency orders from EU member States, without any reciprocal recognition for UK insolvency proceedings in EU member States. Further, while the [EU Insolvency Regulation] would prevent insolvency proceedings being commenced in the UK that competed with proceedings in an EU state, proceedings in the UK would not benefit from the same protection in EU states";[2]

1 Paragraph 2.15 of the Explanatory Memorandum.
2 Paragraph 7.2 of the Explanatory Memorandum.

- "as the [EU Insolvency Regulation] relies heavily on reciprocation between EU member States in order to operate effectively, in a no-deal scenario it is not possible to continue the current system unilaterally".[3]

1.5 Most of the EU Insolvency Regulation is repealed by the draft Regulations with effect from exit day. Consequently, insolvency proceedings commenced in an EU member State will no longer be automatically recognised in the UK and current restrictions on the jurisdiction of UK courts in cross-border insolvency cases will be removed.

1.6 However, regulation 4 provides that these changes to the EU Insolvency Regulation only apply to insolvency proceedings opened on or after exit day. For insolvency proceedings "opened before exit day",[4] the pre-exit day law is to continue to apply, unless the court dealing with those proceedings considers that the conditions for operating the "safeguard mechanism"[5] in regulation 5 are met. That mechanism gives the courts power to disapply the pre-exit day law.

1.7 The Committee was unsure about the intended effect of regulations 4 and 5 and how they would operate in practice. It therefore asked the Department for Business, Energy and Industrial Strategy to explain this by reference to examples.

1.8 In parts 1 and 2 of its memorandum in response (printed as an Appendix), the Department gives the detailed explanation requested by the Committee, together with some helpful examples, for which the Committee is grateful. **It accordingly reports regulations 4 and 5 as requiring elucidation, provided by the Department's memorandum.**

1.9 The Committee was also uncertain about the circumstances in which the "safeguard mechanism" in regulation 5 would apply. It therefore asked the Department to explain the pre-conditions for its operation. These are set out in regulation 5(1), which provides—

> "(1) [The safeguard mechanism applies] where in any particular case [the EU Insolvency Regulation] applies in the UK by virtue of regulation 4 and the court considers that the effect is or would be different to what would be the effect had a member State treated the United Kingdom as a member State under the [EU Insolvency] Regulation, and either—
>
> a) the court considers that one or more of the following would be materially prejudiced—
>
> i. the interests of a creditor…,
>
> ii. the interests of the debtor,
>
> iii. where the debtor is a body corporate, the interests of a member… of the debtor; or
>
> b) the court considers it would be manifestly contrary to public policy to apply the [EU Insolvency] Regulation."

3 Paragraph 2.13 of the Explanatory Memorandum.

4 See regulation 4(2) of the draft Regulations.

5 This is the term used in paragraph 3.8 of the Explanatory Memorandum.

1.10 The Committee has struggled to understand this provision. It is not at all clear what is meant by *"the effect is or would be different to what would be the effect had a member State treated the United Kingdom as a member State under the [EU Insolvency] Regulation"* and the undefined terms *"materially prejudiced"* and *"manifestly contrary to public policy"*.[6]

1.11 The Department's explanation is given in part 3 of the memorandum, and the Annex to the memorandum sets out some helpful scenarios which illustrate how the application of the EU Insolvency Regulation in its pre-exit day form in the UK could produce effects that would materially prejudice the interests of creditors or others if courts in EU member States do not treat the UK in the same way as a member State.

1.12 Although the Committee considers that it is more likely than not that courts and other readers will interpret regulation 5(1) in accordance with the Department's policy intention, it would have been better to avoid ambiguity by spelling out in the draft instrument the intended meaning of the vague concepts italicised above. **The Committee accordingly reports regulation 5(1) for defective drafting.**

1.13 The "safeguard mechanism" itself is in regulation 5(2), which provides—

> "(2) The Court may—
>
> a) apply any other relevant law of the part of the United Kingdom in which the matter is being determined…;
>
> b) make any other order that it thinks fit."

1.14 This appears to give very wide powers to "the Court"[7] to decide the law that is to apply in any particular case. The Committee therefore asked the Department to explain what law a court is to apply instead of the pre-exit day law if it chooses to invoke the safeguard mechanism.

1.15 The Committee thanks the Department for the detailed explanation provided in the memorandum, and for the helpful examples in the Annex. However, the Committee remains concerned at the breadth of the discretion conferred on a court by regulation 5(2).

1.16 The absence of legal certainty that this may give rise to seems obvious. Rather than dealing explicitly and in any detail with a range of scenarios that it can be anticipated could arise during the transition from the existing legal regime to the new legal regime, regulation 5(2) instead leaves it entirely to the courts to determine—on a case-by-case basis—what law they should apply in any particular case. The Committee is concerned that this provision could result in extensive and costly litigation to establish how regulation 5(2) should be interpreted and applied.

1.17 The Committee doubts whether Parliament contemplated that the regulation-making powers conferred by the 2018 Act would be exercised in the way provided for in regulation 5. **The Committee accordingly reports regulation 5(2) on the grounds that it appears to make an unexpected use of the enabling power.**

6 In regulation 5(1)(a) and (b).

7 "The Court" is undefined. The Department explains its intended meaning in part 4 of the memorandum.

Instruments not reported

At its meeting on 19 December 2018 the Committee considered the Instruments set out in the Annex to this Report, none of which were required to be reported to both Houses.

Annex

Instruments to which the Committee does not draw the special attention of both Houses

Draft S.I.	Merchant Shipping and Other Transport (Environmental Protection) (Amendment) (EU Exit) Regulations 2018
Draft S.I.	Occupational and Personal Pension Schemes (Amendment etc.) (Northern Ireland) (EU Exit) Regulations 2018
Draft S.I.	Occupational and Personal Pension Schemes (Amendment etc.) (EU Exit) Regulations 2018
Draft S.I.	Consumer Protection (Enforcement) (Amendment etc.) (EU Exit) Regulations 2018
Draft S.I.	Over the Counter Derivatives, Central Counterparties and Trade Repositories (Amendment, etc., and Transitional Provision) (EU Exit) Regulations 2018
Draft S.I.	Market Abuse (Amendment) (EU Exit) Regulations 2018
Draft S.I.	Jurisdiction and Judgments (Family) (Amendment etc.) (EU Exit) Regulations 2019

Instruments subject to annulment

S.I. 2018/1221	Merchant Shipping (Miscellaneous Provisions) (Amendments etc.) (EU Exit) Regulations 2018
S.I. 2018/1225	Higher Education and Research Act 2017 (Transitional and Saving Provisions) (University Title) Regulations 2018
S.I. 2018/1230	Building (Amendment) Regulations 2018
S.I. 2018/1236	Financial Penalty Deposit and Fixed Penalty Offences (Miscellaneous Provisions) Order 2018
S.I. 2018/1238	Livestock (Records, Identification and Movement) (England) (Amendment) (EU Exit) Regulations 2018
S.I. 2018/1241	Official Controls (Animals, Feed and Food) (England) (Amendment) (EU Exit) Regulations 2018
S.I. 2018/1244	Banks and Building Societies (Priorities on Insolvency) Order 2018
S.I. 2018/1251	Driving Licences (Amendment) (EU Exit) Regulations 2018

S.I. 2018/1252 Inquiries and Coroners (Amendment) (EU Exit) Regulations 2018

S.I. 2018/1257 Service of Documents and Taking of Evidence in Civil and Commercial Matters (Revocation and Saving Provisions) (EU Exit) Regulations 2018

S.I. 2018/1269 Sanctions Review Procedure (EU Exit) Regulations 2018

S.I. 2018/1276 Accreditation of Forensic Service Providers Regulations 2018

S.I. 2018/1277 Electronic Monitoring (Responsible Persons) (Amendment) Order 2018

S.I. 2018/1278 Ionising Radiation (Basic Safety Standards) (Miscellaneous Provisions) (Amendment) (EU Exit) Regulations 2018

Instruments not subject to Parliamentary proceedings not laid before Parliament

S.I. 2018/1261 Child Maintenance and Other Payments Act 2008 (Commencement No.16) Order 2018

Appendix

Draft S.I.

Insolvency (Amendment) (EU Exit) Regulations 2018

1. Explain the intended effect of regulations 4 and 5 and how the provisions in those regulations would achieve that effect.

2. The policy purpose of regulation 4 is to avoid, so far as possible, any change in the insolvency law which applies to "existing insolvency proceedings"; i.e. ones that are already in progress on exit day. This is to avoid any change in the legal position of any person involved in those proceedings and to minimise any disruption or uncertainty in respect of those proceedings. Therefore regulation 4 saves the application of the EU Insolvency Regulation (Regulation (EU) 2015/848) (the "EUIR") and its predecessor, the EC Insolvency Regulation (Regulation (EC) 1346/2000) ("the ECIR") to existing insolvency proceedings to which those Regulations apply before exit day. Existing proceedings are defined by reference to the date the ECIR and its successor came into effect and by exit day. The ECIR came into force on 31 May 2002 and applied to pro ceedings opened after that date. The EUIR repealed the ECIR but saved its application to proceedings opened before 26 June 2017 (Articles 91 and 84(2)). The EUIR applies to insolvency proceedings opened from 26 June 2017 (Article 84(1)). Regulation 4 maintains the existing savings in respect of the ECIR and saves the application of the EUIR in respect of main proceedings opened before exit day. These savings are equivalent to the position under the draft EU Withdrawal Agreement. That provides in Article 67(3)(c) that the EUIR "shall apply to insolvency proceedings, and actions referred to in Article 6(1) of that Regulation, provided that the main proceedings were opened before the end of the transition period".

3. There is one important difference between the saving in the draft Withdrawal Agreement and in regulation 4. Regulation 4 can only save the application of the EUIR and the ECIR in the law of the United Kingdom. So under regulation 4 the United Kingdom will continue to apply the EUIR or the ECIR to existing proceedings within the UK or coming from EU states; but UK law cannot oblige member States to continue to apply those Regulations to proceedings in the EU as if the UK were a member State or within the EU to existing UK proceedings because the UK will not be a member State. The draft Withdrawal Agreement, does however, provide for the continued application of the EUIR (and the ECIR) in the United Kingdom and in the EU on a reciprocal basis. Under regulation 4 the UK courts will recognise an EU judgment opening insolvency proceedings but our law cannot make an EU state recognise a judgment opening proceedings in the UK. By contrast under the draft EU Withdrawal Agreement the UK will recognise EU judgments opening proceedings and EU states will recognise UK judgments opening proceedings.

4. It is the potential lack of reciprocity between the way that the UK will continue to apply the EUIR and the ECIR and the way that the member States may apply these Regulations that is being addressed by the safeguards in regulation 5. This regulation enables the court to depart from the EUIR (and the ECIR) in any particular case where either the lack of reciprocal application results in material prejudice, for example to the interests of a

creditor, or it would manifestly be contrary to public policy to apply the relevant EU or EC Regulation. In the Annex to this memorandum we have given examples of cases in which such material prejudice might occur. Regulation 5 enables the court to apply alternative law including the Cross-Border Insolvency Regulations 2006 (which apply to Great Britain) or the Cross-Border Insolvency Regulations (Northern Ireland) 2007. These Regulations, which implement the Uncitral Model Law on Cross-Border Insolvency, currently provide the legal basis for recognition and cooperation in respect of those cross-border insolvency proceedings to which the EU Insolvency Regulation does not apply.

2. Where regulation 4(1) or (2) applies, explain, by reference to examples, how the law would operate after the United Kingdom has left the European Union.

5. The continued application of the EUIR where main proceedings had been opened before exit day would first of all restrict the jurisdiction to open insolvency proceedings in the UK. For example where main proceedings had been opened in a member State before exit day it would not be possible to open proceedings in the UK unless the debtor had an establishment in the UK. If such a case secondary proceedings could be opened which would be limited to assets within the UK. The office holder in such proceedings would be obliged to send any surplus to the office holder in the main proceedings. The UK courts would continue to recognise judgments from member States opening insolvency proceedings automatically. Office holders in EU proceedings seeking to enforce debts in insolvency proceedings in the UK would be entitled to receive notices and to participate in those proceedings.

3. Explain the intended meaning of the following provisions in regulation 5—

a) *"the effect is or would be different to what would be the effect had a member State treated the United Kingdom as a member State under the relevant Regulation",*

b) *"material prejudice" [to the interests of a creditor, the debtor or a member of the debtor],*

c) "*it would be manifestly contrary to public policy to apply the relevant Regulation*",

d) "*The Court may—*

(a) apply any other relevant law…,

(b) make any other order that it thinks fit.",

and how it is anticipated that "the Court" will give effect to these provisions.

6. The Annex to this memorandum contains examples of circumstances in which the application of the ECIR or the EUIR in the UK to insolvency proceedings opened in a member State would produce different effects that would materially prejudice the interests of creditors or others because the UK was not treated in the same way as a member State. It also gives examples of how the court could remedy or avoid those adverse effects.

Public policy

7. The public policy ground for a court to depart from the application of the ECIR or the EUIR follows the existing ground in Article 33 of the EUIR (Article 46 of the ECIR) and in Article 6 of the Uncitral Model Law on Cross Border Insolvency (implemented in each of the Cross-Border Insolvency Regulations in Article 6 of Schedule 1). It would only be in an exceptional case that the Court would determine that an effect was "manifestly contrary to public policy" as a ground for disapplying the relevant Regulation. The CJEU has interpreted the test in the EUIR as imposing a high threshold where "recognition or enforcement of the judgment delivered in another Contracting State would be at variance to an unacceptable degree with the legal order of the State in which enforcement is sought inasmuch as it infringes a fundamental principle. The infringement would have to constitute a manifest breach of a rule of law regarded as essential in the legal order of the State in which enforcement is sought or of a right recognised as being fundamental within that legal order" (Eurofood IFSC Ltd C-341/04).

4. Explain where "the Court" is defined.

8. The court is not defined in the Regulations. The Regulations do not confer original jurisdiction to apply the EUIR or the ECIR. The "court" will therefore be any court in one of the three jurisdictions of the United Kingdom that has jurisdiction in proceedings in which the EUIR or the ECIR is in issue.

The Annex

Scenario 1: Prejudice to UK creditors

Summary

1. In this scenario creditors in the UK are prejudiced by not being given the same notice of insolvency proceedings to which creditors in a member State are entitled. As a result the UK creditors miss the deadline for submitting claims in those proceedings. The court is able to set aside the stay of proceedings in the UK under the applicable law of the insolvency proceedings so that the UK creditors can make a claim against assets in the UK. The court can enable the UK creditors to receive a return equivalent to what they would have received as "foreign creditors" in the insolvency proceedings.

2. If the main insolvency proceedings in this example were opened before 26th June 2017, they are governed by the ECIR. If they were opened on or after that date they will be governed by the EUIR. Regulation 4(1) preserves the application of the ECIR to proceedings opened before 26th June 2017 and regulation 4(2) preserves the application of the EUIR to proceedings opened on or after that date but before exit day.

Relevant Articles of the EUIR

3. Art 54 deals with the insolvency office holder's duty to inform creditors. Article 54(1) states that as soon as insolvency proceedings are opened in a member State, the court of that State or the insolvency practitioner appointed by that court shall immediately inform the known foreign creditors. Art 54(2) goes on to provide details of the notice itself, including the requirement to provide time limits for lodging claims, a copy of the form or where it can be found and details of to whom to send it.

Relevant Article under the ECIR

4. In relation to insolvency proceedings opened before 26th June 2017, Article 40 of the ECIR makes like provision to that made by Art 54 of the EUIR.

Scenario under the EUIR

5. Company B has its centre of main interests in member State Y (having its registered office and head office there) and sells antiques online across the EU. The business has many UK customers and holds a sterling account in London for buying and selling UK antiques, but it has no establishment in the UK. On 15th March 2019 company B enters formal rescue proceedings in Y. The insolvency law in Y requires that creditors must file their claims within 56 days of the opening of proceedings or be excluded from any distribution. The insolvency office holder writes to all "foreign creditors" on 1st April under Article 54 of the EUIR, informing them of the opening of proceedings and the deadline for making claims in the proceedings. At the time the insolvency proceedings are opened, Company B had 50 UK creditors who had paid for antiques which had not been delivered. Article 54(1) and (2) of the EUIR require the insolvency practitioner immediately to inform all known foreign creditors and give them specific information including the time limits for claiming. However the definition of "foreign creditor" in the EUIR is limited to creditors with their habitual residence, domicile or registered office in a member State other than the one in which the proceedings are brought. As the UK is no longer a member State, the insolvency office holder is not required to treat UK creditors as "foreign creditors". The office holder does not send them the notice to creditors when it is issued. Consequently the UK creditors do not find out about the existence of the insolvency proceedings until the end of May 2019 and their claims are rejected due to the cut-off date under the law of Y.

6. Being in possession of the bank details of Company B for payment purposes, a group of the UK creditors applies to court for an injunction to freeze B's London bank account. The insolvency office holder defends these proceedings on the grounds that the applicable insolvency law of Y prohibits the commencement of enforcement action after the opening of proceedings, and as the proceedings have been commenced before exit day, that law applies in the UK by virtue of regulation 4 and Article 7 of the EUIR. Furthermore, the office holder argues that there is no requirement under the domestic law of Y to contact creditors outside of the EU, and the requirement under Article 54 EUIR does not apply as the notices had been issued after the date of the UK's exit. The office holder argues that he has no obligation to recognise late claims, and the court cannot prevent the office holder from recovering the monies in the London bank account for the benefit of the insolvency estate.

Options Available to the Court under the Regulations

7. Under regulation 5(1)(a) the court considers that the interests of UK creditors are materially prejudiced because they have not received the notice that they would have had if the UK had been treated as a member State. Under regulation 5(2) the court can freeze B's UK bank account until the office holder provides proper notice to the UK creditors. This would allow an extension of time for considering claims (for which the office holder has discretion under Y's law) and enable the office holder to agree to consider UK creditors' claims on the same basis as those of creditors from member States. If the office holder declines or is unable to do this the court could make orders for the UK creditors to have their claims paid out of the assets in the jurisdiction.

Scenario 2: Prejudice to the UK tax authority

Summary

8. This scenario is concerned with the position of HMRC as a creditor of a company with its COMI in a member State. Under the EUIR and the ECIR the tax and social security authorities of a member State are "foreign creditors" entitled to equal treatment in proceedings in another member State. In some member States this may be an EU exception to a general rule that such authorities are not recognised as creditors. In such a state HMRC might no longer be recognised as a "foreign creditor" after exit day. The court is able to disapply the stay of enforcement proceedings so that HMRC receives a return equivalent to that received by other creditors.

9. If the main insolvency proceedings in this example were opened before 26th June 2017, they would be governed by the ECIR. If they were opened on or after that date they will be governed by the EUIR. Regulation 4(1) preserves the application of the EUIR to proceedings opened before 26th June 2017 and regulation 4(2) preserves the application of the EUIR to proceedings opened on or after that date but before exit day.

Relevant Articles of the EUIR

10. Art 3(1) of the EUIR provides that the courts of the member State where the company's centre of main interests (COMI) is situated shall have jurisdiction to open insolvency proceedings ("main insolvency proceedings"). Art 3(2) states that where COMI is situated in a member State, the courts of another member State shall have jurisdiction to open insolvency proceedings against the company only if it possesses an establishment within that other member State. The effects of those proceedings are restricted to the assets situated in the territory of the latter member State.

11. Art 7 sets out requirements as to the applicable law and states the law applicable to insolvency proceedings and their effects shall be that of the member State within which such proceedings are opened.

Relevant Articles under the ECIR

12. In relation to insolvency proceedings opened before 26th June 2017, Article 3 of the ECIR makes the like provision to that made by Article 3 of the EUIR. Article 4 of the ECIR makes the like provision to that made by Art 7 of the EUIR.

Scenario under the EUIR

13. Company A is a company registered in member State Z, where its HQ is located. Company A previously had five establishments in the UK, but closed these in early 2018 after a difficult few years of trading. The company left a tax liability of £500k for unpaid PAYE for its former UK-based employees.

14. On 20th March 2019 Company A enters into a liquidation procedure in member State Z. As A's COMI is there the courts of Z have jurisdiction to open main insolvency proceedings under Article 3 of the EUIR. The applicable insolvency law under Article 7 of the EUIR is therefore that of Z. As these proceedings are commenced before Exit Day, regulation 4 means that the EUIR continues to apply to those proceedings in the UK.

15. HMRC had for some time sought to agree repayment with Company A without success. Company A still owns four freehold empty buildings in the UK with a combined value of £1m. In January 2019 HMRC obtains a default judgment for the £500k and on 1st April it commences enforcement proceedings by making an application for a charging order over the empty buildings. The liquidator appointed under the proceedings in Z writes to the UK court informing the court of those proceedings and the automatic stay which applies under the relevant law of Z. The UK court stays the charging order application recognising the applicable law of the EU proceedings under Article 7 of the EUIR.

16. The liquidator has great success in recovering monies from Company A's debtors and forecasts a 50% dividend. HMRC files its claim in the liquidation proceedings on 1st June 2019, but this is rejected by the liquidator. A similar tax claim from the US tax authority is rejected, but a claim from the tax authority of Y, another EU Member State, is allowed by the liquidator as that tax authority meets the definition of a "foreign creditor" under Article 2(12) of the EUIR. In Z, there are no domestic rules for the recognition of foreign state tax claims outside of the EU, and there are no tax treaties in place that might provide for such claims from non-EU countries to be recognised and enforced.

17. HMRC seeks direction from the UK court. Article 7 of the EUIR requires the court to recognise that the automatic stay on creditor actions under the law of Z prevents the making of the charging order in favour of HMRC. However HMRC has not received the corresponding benefit of sharing in the distribution to creditors. The court considers the interests of a UK creditor are materially prejudiced by the application of Article 2(12) of the EUIR in country Z which does not recognise the UK tax authority as a foreign creditor.

Options Available to the Court under the Regulations

18. The court can make such order as it thinks fit in order to put HMRC in the position that it would have been if it had been recognised as a foreign creditor in country Z. For example it can decline to apply the automatic stay under the law of Z and grant HMRC a charging order in the amount of the dividend that HMRC would have received as a foreign creditor. Either HMRC could enforce the charging order to meet its claim or the foreign liquidator could sell the property. In that case the liquidator would have to discharge the charging order by paying HMRC. In this way the prejudice to HMRC as a UK creditor would be overcome.

Scenario 3: Honouring an obligation to a debtor

Summary

19. Once proceedings are opened a person ("P") who owes money to the debtor ("D") subject to the proceedings should pay that money to the office holder who collects in all the money owed to D in order to distribute what is available amongst all the creditors. Article 31 of the EUIR provides an exception where P honours an obligation for the benefit of D by making a payment on its behalf in good faith without knowing of the insolvency proceedings opened in another state. In such a case P will be treated as having discharged the debt to D. Article 31 assumes that in a case where P knew of the proceedings the payment not being made to the office holder would not discharge the debt owed to D in the insolvency proceedings.

Relevant Articles of the EUIR

20. If P honours an obligation of D before notice of the opening of the insolvency proceedings is published in accordance with Article 28 (publication in another Member State where an establishment is located), P is presumed to have been unaware of the opening of the insolvency proceedings. If P honours the obligation after the notice is published, P is presumed to have been aware of the proceedings. In either case the presumption is subject to proof to the contrary.

21. If the main insolvency proceedings in this example were opened before 26th June 2017, they would be governed by the ECIR. If they were opened on or after that date they would be governed by the EUIR. If the proceedings are still ongoing on and after exit day, regulation 4(1) will preserve the application of the ECIR to proceedings opened before 26th June 2017 and regulation 4(2) will preserve the application of the EUIR to proceedings opened on or after that date but before exit day.

Relevant Article under the ECIR

22. In relation to insolvency proceedings opened before 26th June 2017, Article 24 of the ECIR makes the like provision to that made by Article 31 of the EUIR.

Scenario under the EUIR

23. Company D's COMI is in member State W, but it has establishments in some other member States, including the United Kingdom. Company E is a UK registered company trading in the UK. Under a contract between D and E, D regularly supplies E with machine parts. D becomes insolvent: as its COMI is in member State W, the main proceedings are opened there and the applicable law is that of member State W. E pays an invoice for £10,000 it has received from D after the opening of those proceedings into D's bank account in the UK but before notice of those proceedings being opened is published in the UK.

24. D's liquidator seeks to recover £10,000 from E for D's creditors. The liquidator's case is that E could reasonably have been expected to know of the opening of the main proceedings in W, when it paid the £10,000 invoice, that E should therefore have paid that sum to the liquidator's account for distribution to the creditors. E maintains that, as it paid the £10,000 invoice before notice of the opening of the main proceedings was published in the UK, it is not liable to pay this sum to the liquidator. E seeks a declaration, after exit day, from the court in W in support of its case. That court rules that, as the UK is no longer a member State, the court is not bound to apply Article 31 of the EUIR to the obligation honoured by E. The court in W finds that E ought to have known of the main proceedings having been opened in W at the time it paid the invoice and the court therefore declines to give the declaration sought. In accordance with the EUIR (as applied in the UK by regulation 4(2)), the liquidator seeks to enforce in the UK court the £10,000 debt it says E owes.

Options available to the Court under regulation 5

25. The UK court could consider under regulation 5 that E's interests have been materially prejudiced and that the effect in member State W of treating the UK as no longer a member State is that the presumption that E did not know about the proceedings was not applied

in its favour by the court of W. The UK Court can refuse to recognise the judgment of court W and declare that the liability of E to D has been satisfied.

Scenario 4: Giving an undertaking in order to avoid secondary proceedings

Summary

26. The EUIR enables secondary proceedings to be brought in a member State where a debtor has an establishment and for the effects of the secondary proceedings to be limited to the member State concerned. The EUIR enables an insolvency practitioner to give an undertaking in order to avoid secondary proceedings. This scenario is concerned with the position of creditors in the UK when the insolvent company has its COMI here, but also has an establishment in another member State, where the liquidator has given an undertaking prior to exit day to avoid secondary proceedings in that state, but the creditors in that state nonetheless seek to open secondary proceedings after exit day.

27. If the main insolvency proceedings in this example were opened before 26th June 2017, they are governed by the ECIR. If they were opened on or after that date they will be governed by the EUIR. If the proceedings are still ongoing on and after exit day, regulation 4(1) preserves the application of the ECIR to proceedings opened before 26th June 2017 and regulation 4(2) preserves the application of the EUIR to proceedings opened on or after that date but before exit day.

Relevant Articles of the EUIR

28. Art 3 (2) and (3) state that where main insolvency proceedings have been opened by a court of one member State and recognised in another member State, the courts of that other member State may open secondary insolvency proceedings.

29. Secondary proceedings can occur when the debtor, despite having their COMI in the member State where main proceedings have been opened, also has an "establishment" (defined in Art 2(10) as any place of operations in the 3 months leading up to proceedings where the debtor has carried out a non-transitory economic activity with human means and assets) in another member State. The effects of secondary proceedings are restricted to assets located in the member State where those secondary proceedings have been opened.

30. Article 36 provides for a right to give an undertaking in order to avoid secondary proceedings. The undertaking is given by the insolvency practitioner in the main insolvency proceedings in respect of assets located in a member State where secondary proceedings could be opened (i.e. a member State in which the debtor has an establishment) and the insolvency practitioner undertakes to comply with the distribution and priority rights that the creditors in that member State would have under national law if secondary proceedings were opened there. If such an undertaking is given, the member State's law applies to determine preferential creditors and the ranking of creditors' claims against the assets located in that member State. An undertaking has effect if approved by known local creditors in accordance with the rules on majority and voting in the member State concerned. The existence of such an undertaking does not prevent creditors from applying to a court for the opening of secondary proceedings in that member State, but if such an application is made, the insolvency practitioner can under Article 38(2) ask the court not to open secondary proceedings and, if the court is satisfied the undertaking adequately protects local creditors' interests, the court must refuse the creditors' application.

Relevant Article under the ECIR

In relation to insolvency proceedings opened before 26th June 2017, Article 3 of the ECIR makes identical provision to that made by Article 3 of the EUIR, as does Art 2(h) in relation to the definition of establishment in Art 2(10) of the EUIR. There is no corresponding provisions for Art 36 and Art 38 under the ECIR for insolvency proceedings opened before 26th June 2017.

Scenario under the EUIR

Company F is a UK registered company, whose COMI is in the UK, but it has an office with some employees and operations in member State V. F goes into liquidation in January 2019. As its COMI is in the UK, the UK liquidation proceedings are the main insolvency proceedings for the purpose of the EUIR. Those proceedings are still ongoing after exit day and, by virtue of regulation 4(2), the pre-exit version of the EUIR applies to those proceedings and to any secondary proceedings in respect of F. Following discussions with F's creditors in V, the liquidator in the UK insolvency proceedings gives an undertaking which is approved by the known local creditors under Article 36 in February 2019. This means that the law of V applies to the ranking of creditors' claims and to preferential creditors' rights in relation to those assets. Because of regulation 4(2), this will also be the case after exit day.

In April 2019 (i.e. after exit day) the creditors in V make an application for the opening of proceedings there. The liquidator, in accordance with Article 38(2) of the EUIR, asks the court in V to dismiss the creditors' application. However, the law of V applying the EUIR no longer treats the UK as a member State and under that law, the UK liquidator no longer has the status of the liquidator in the main proceedings. The court in V allows the creditors' application and proceedings are opened. The proceedings result in a distribution of assets in V which produces less favourable outcomes for some creditors in the U.K. than would have been the case had the original undertaking been adhered to. Those creditors apply to the courts in the UK under regulation 5.

Options Available to the Court under the Regulations

This is a case where the EUIR applies in the UK by virtue of regulation 4 and in these circumstances it would be open to the court, under regulation 5 to consider that the effect of this is different to what it would have been if the authorities in V continued to treat the UK as a member State for the purposes of the EUIR and that, as the outcome of this is less favourable for some creditors, that (depending on how much less favourable) some creditors' interests would be materially prejudiced. The court uses its power under regulation 5 to make an order for the distribution of UK-based assets which remedies the otherwise less favourable outcome for the creditors affected.

Department for Business, Energy and Industrial Strategy

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