

CROSS-BORDER DEVELOPMENTS IN AUSTRALIA – AN UPDATE

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1. Introduction

This paper considers the following issues in relation to corporate insolvencies:

- (a) What is cross border insolvency?
- (b) Australia's current legal framework for cross border insolvency; and
- (c) UNCITRAL's Model Law on Cross Border Insolvency and its adoption by other countries and its imminent adoption in Australia.

2. What is Cross Border Insolvency?

A cross border insolvency arises when an insolvent entity has assets or debts in more than one State. The term also encompasses the following scenarios:

- winding up foreign companies;
- recovery of foreign assets;
- examination of foreign residents;
- access to documents and information which is overseas;
- foreign creditors and priority conflicts;
- recognition of foreign insolvency proceedings;
- claims against local assets by a foreign insolvency administrator;
- coordination of insolvency proceedings in different jurisdictions; and
- concurrent insolvency administrations.

In the modern world, with ever increasing globalisation, international trade and electronic communications and asset transfers, the cross border complexities and complications of insolvencies are becoming more widespread and are certainly no longer the reserve of the largest companies of the world economy with global reach. Companies in greater numbers than ever before of all sizes increasingly have assets and creditors in more than one jurisdiction creating potential cross border insolvency

situations. This international element can be daunting to practitioners and creditors alike and protracted and is an added dimension to any purely domestic insolvency.

3. Universal Versus Territorial Approach

Over many years an international debate has occurred over whether an insolvency has universal application or whether its application is limited to the place of adjudication. Those competing theories are known as the *universal* and *territorial* theories of insolvency law. Out of that debate, the theory of *modified universality* has emerged.

The *universal* approach would dictate that one insolvency administration is to be universally recognised by all other jurisdictions in which the insolvent entity has dealings. Accordingly, one insolvency administrator, universally recognised, collects in all of the assets and has total administrative responsibility for the insolvency. Foreign creditors submit to the insolvency laws of that one insolvency administration and accept the result of that submission.

A modification to that universal approach applies where there are concurrent insolvency proceedings. The proceedings in the place of incorporation are normally acknowledged as the *principal* or *primary* proceedings and the other proceedings are treated as secondary or *ancillary* proceedings. The insolvency administrator in charge of the primary proceedings will be responsible for realising all of the assets of the company worldwide and the insolvency administrator of the ancillary proceedings will be obliged to concentrate on getting in and realising local assets and remitting the fund to the insolvency administrator of the primary proceedings.¹

On the other hand, the *territorial* approach involves each country employing its own insolvency laws to grab local assets and administer them locally according to the procedures and priorities of that country's laws. Under the strict territorial approach, there is no recognition of foreign proceedings and a separate insolvency administration is required in each country in which the insolvent entity operates.

The major disadvantages of a territorial approach include the following:

- Reorganisation of an enterprise is difficult or impossible because each unco-ordinated local proceeding focuses on maximising returns for local creditors rather than the total pool of creditors.
- Even in a liquidation, realisations of greater value can be achieved if national borders are ignored. For example, a division of a company may have manufacturing and distribution facilities in several countries with each division being saleable for a higher price as a unit than would be received for each bundle of assets in each State. Nevertheless, existing laws make it very difficult to sell assets in multinational packages.
- Although virtually all national insolvency laws endorse the principle of equality of distribution to creditors, territorialism produces highly unequal results. Aside from differing priority rules in each country, the distributions vary greatly depending on the assets sizeable in each country at the time of commencement of the external administration. Local creditors benefit where they are lucky enough to have more assets in their country at that moment and suffer where their jurisdiction is less fortunate. A very few sophisticated international creditors may collect in several proceedings and do very well, but most smaller creditors cannot play that game. The results are arbitrary and inconsistent with the principles of virtually every country's laws. Above all, they are unpredictable, creating substantially increased transaction costs in international financing.
- Shrewd debtors can exploit modern technology and the globalisation of commerce to move assets rapidly from one jurisdiction to another and to transfer assets to insiders or preferred creditors in other countries. Because recognition of foreign insolvency proceedings and co-operation with those proceedings is so cumbersome in most countries, it is very hard for administrators or liquidators to pursue and capture the assets.
- Although overt discrimination against foreign creditors is relatively rare, they often receive little or no real notice of insolvency proceedings and too often suffer de facto discrimination in those proceedings.

4. **Australia's Current Statutory Provisions and Common Law Principles relevant to Cross Border Insolvencies**

At the time of writing Australia is yet to follow through on its promise to adopt the UNCITRAL Model law.² Nonetheless, with a few exceptions³, its statutory provisions and common law principles position it toward the *internationalist* or *universal* end of the spectrum (as described more fully in Sections 5, 6 and 7 below), although there are occasional Australian cases which demonstrate a level of co-operation which is less than an internationalist might hope for.⁴

5. **Foreign Companies Carrying on Business in Australia**

Section 601CD(1) of the *Corporations Act 2001* (Cth) (the **Act**) prohibits a *foreign company* from *carrying on business* in Australia unless it is registered under Part 5B.2 Division 2 of the Act.

A *foreign company* is defined as a body corporate incorporated outside Australia.

The phrase *carrying on business* is defined in ss18 to 21 of the Act.

Section 21(1) provides that a body corporate that has a place of business in Australia carries on business in Australia. The establishment or use of a share registration office in Australia or a dealing with property situated in Australia as an agent, legal personal representative or trustee, whether by employees or agents or otherwise will also constitute the carrying on of business in Australia pursuant to s21(2).

A number of exceptions are contained in s21(3). A body corporate does not carry on business in Australia merely because it:

- (a) is a party to proceedings or settles proceedings or a claim or dispute;
- (b) holds meetings of its directors or shareholders;
- (c) maintains a bank account;
- (d) effects a sale through an independent contractor;
- (e) elicits or procures an order that becomes a binding contract only if the order is accepted outside Australia;
- (f) creates evidence of a debt or creates a charge on property;

- (g) secures or collects any of its debts or enforces securities relating to such debts;
- (h) conducts an isolated transaction that is completed within 31 days, not being one of a number of similar transactions repeated from time to time; or
- (i) invests any of its funds or holds any property.

A foreign company may apply for registration under s601CE of the Act. If it does so, the foreign company must appoint a natural person or a company resident in Australia as a local agent. A local agent of a registered foreign company is answerable for the doing of all acts that the foreign company is required to do under the Act and is personally liable for a penalty imposed on the foreign company for a contravention of the Act. Under s601CK(1) a registered foreign company is required, at least every calendar year, to lodge a copy of its latest balance sheet, cash flow statement and profit and loss statement.

In view of those obligations, an alternative for a foreign company seeking to carry on business in Australia is to incorporate an Australian company as a wholly owned subsidiary of the foreign company.

Where a foreign company carries on business in Australia but is not registered under Part 5B.2 Division 2, it commits a breach of s601CD(1) but that fact does not mean that Australian courts do not have jurisdiction in respect of that company for insolvency purposes. A foreign company owes its existence to its incorporation in a foreign state under a foreign law (not registration as a foreign company in Australia under s601CE of the Act). It therefore exists and proceedings can be commenced against it in the Australian courts notwithstanding that a foreign company is not a registered foreign company in Australia (see *Feng v GMS Fulfilment Services Limited* [2004] NSWSC 855 and *McIntyre v Eastern Prosperity Investments Pty Ltd (No. 6)* [2005] FCA 155) (also see [6.3] below).

6. Winding Up Foreign Companies

6.1 Part 5.4 does not apply

Part 5.4 of the Act contains the Court's power to order that an insolvent *company* be wound up in insolvency.

Section 9 defines a *company* as a company registered under the Act. There is no longer any reference in the definition of company to a company incorporated under the Act. Notwithstanding that, the reference in the definition of company to a Part 5.7 body being a company for the purposes of Part 5.7B (which deals with recovering property or compensation for the benefit of creditors of an insolvent company) together with the fact that the independent part (Part 5.7) that deals with winding up bodies other than companies is retained, strongly suggests that the legislature did not intend that foreign companies registered under Part 5B.2 Division 2 would fall within the definition of *company* and therefore be subject to winding up under Part 5.4 of the Act. Accordingly, the better view is that Part 5.4 does not apply to foreign companies.

6.2 Winding up a registered foreign company subject to a foreign insolvency administration

Section 601CL(14) provides that where a *registered foreign company* commences to be *wound up, or is dissolved or deregistered, in its place of origin*, the local agent of the foreign company must lodge notice of that fact and, when a liquidator is appointed, notice of the appointment with ASIC. The section also provides that the Australian Court must, on application by the liquidator for the foreign company's place of origin, or by ASIC, appoint an Australian liquidator of the foreign company.

The duties of the Australian liquidator of a registered foreign company who is appointed by the Australian Court are circumscribed by s601CL(15). The Australian liquidator must, before any distribution of the foreign company's property is made, advertise widely in each State where the foreign company carried on business at any time during the six years before the liquidation and invite all creditors to make their claims against the foreign company within a reasonable time before the distribution. The Australian liquidator must not, without obtaining an order of the Court, pay out a creditor of the foreign company to the exclusion of another creditor of the foreign company and must, unless the Court otherwise orders, recover and realise the property of the foreign company in Australia and shall pay the net amount so recovered and realised to the liquidator of the foreign company for its place of origin.

The limitations of these provisions from the point of view of Australian creditors are obvious.

First, the provisions only apply to a *registered foreign company* and not deregistered or unregistered foreign companies (see *ASIC v Edwards* [2004] QSC 344 as followed by Barrett J in *Gebo Investments (Labuan) Ltd* [2005] NSWSC 544). A winding up of an unregistered foreign company in ancillary proceedings in Australia is not possible pursuant to s601CL but is possible under Part 5.7 (see *Re Application of Wayland (liquidator of ABC Containerline)* [2005] NSWSC 1).

Secondly, the provisions only apply to a foreign company which commenced to be wound up or is dissolved or deregistered in its place of origin. They do not apply upon the commencement of any other form of insolvency administration.

Thirdly, there is nothing in s601CL or anywhere else in the Act which provides that the general winding up provisions of the Act contained in Chapter 5 apply to the liquidation of a registered foreign company pursuant to s601CL(14). This contrasts with the position in relation to the winding up of Part 5.7 bodies and the specific provisions contained in ss582 and 583 of the Act which apply Chapter 5 to the winding up of a Part 5.7 body.

Fourthly, a creditor of the registered foreign company cannot itself initiate the appointment of an Australian liquidator. Only the foreign liquidator or ASIC can apply to the Court for the appointment of an Australian liquidator of the foreign company.

Fifthly, there is uncertainty as to whether the Australian liquidator can make payments to Australian creditors before paying the *net amount* to the foreign liquidator. Section 601CL(15)(c) seems to require the Australian liquidator to remit all amounts realised less the costs of realisation. However, ss601CL(15)(a) and (b) seem to contemplate the Australian liquidator paying Australian creditors of the foreign company.⁵

Section 601CL(14) appears to be the adoption by the legislature of a provision consistent with the universal approach to cross border insolvency. Under that section, the Court does not have the power to wind up the registered foreign company but only the power to appoint an Australian liquidator of the foreign company. The role of the Australian liquidator of the foreign company appears to be directed towards identifying Australian creditors and assisting the foreign liquidator in the orderly winding up of the foreign company.

In view of the limitations and uncertainty referred to above, Australian creditors are likely to favour the Part 5.7 approach referred to below.

6.3 Winding up a foreign company under Part 5.7

Part 5.7 of the Act contains the general sections which establish the regime for winding up foreign companies (and many other types of associations, some incorporated and some not). The application of Part 5.7 is limited to *Part 5.7 bodies*.

A *Part 5.7 body* is relevantly defined in s9(b) of the Act to mean a foreign company that:

- (i) is registered under Part 5B.2 Division 2 (referred to in Section [5] above); or
- (ii) not registered but carries on business in Australia.

Establishing whether a foreign company is registered or not is simple. Determining whether it is carrying on business in Australia may involve complex issues when it comes to applying the definitions contained in s21 of the Act (as referred to in Section 5 above).

As referred to above, there is an overlap between the application of Part 5.7 and s601CL of the Act. Section 582(1) provides that Part 5.7 has effect in addition to, and not in derogation of, s601CL and any provisions contained in the Act or any other law with respect to the winding up of bodies.

Importantly, s582(1) also provides that the liquidator or Court may exercise any powers or do any act in the case of Part 5.7 bodies that might be exercised or done by him, her or it in the winding up of companies.

A foreign company which meets the definition of a Part 5.7 body may be wound up under Part 5.7 notwithstanding that it is being wound up or has been dissolved, deregistered or has otherwise ceased to exist as a body corporate under the laws of the place under which it was incorporated (s582(3)).

The possibility of a foreign company being wound up in *both* Australia and its place of incorporation which is inherent in s582(3) of the Act, highlights the need for a framework for co-operation between Australian and foreign Courts and their respective liquidators in external administration matters.

Under s583 of the Act, a Part 5.7 body may be wound up under Chapter 5 and Chapter 5 applies accordingly to a Part 5.7 body with such adaptations

as are necessary. The circumstances in which a Part 5.7 body may be wound up are as follows:

- (a) if the Part 5.7 body is unable to pay its debts, has been dissolved or deregistered, has ceased to carry on business in Australia;
- (b) if the Court is of the opinion that it is just and equitable that the Part 5.7 body should be wound up;
- (c) if ASIC is of the opinion that the Part 5.7 body cannot pay its debts and should be wound up or that it is in the interests of the public, shareholders or creditors that the Part 5.7 body should be wound up.

Section 585 goes on to describe the circumstances in which a Part 5.7 body shall be deemed to be unable to pay its debts for the purposes of s583. In particular, s585(a) deals with a situation analogous to the failure to meet a statutory demand provisions contained in Part 5.4 of the Act.

Until relatively recently, there was some uncertainty as to whether a foreign company which was not registered in Australia and which had ceased to carry on business in Australia fell within the second limb of the s9 definition of a part 5.7 Body and consequently, whether it was capable of being wound up in Australia under Part 5.7. "*Carries on business in Australia*" is expressed in the present tense and as such the concern was that carrying on business in the past may not have been sufficient to fall within the s9 definition. That question was recently answered in the affirmative by Lander J in *ASIC v International Unity Insurance (General) Ltd* [2004] FCA 1060. As his Honour pointed out, one of the circumstances which would allow for a Part 5.7 body to be wound up is that it has ceased to carry on business in the jurisdiction: "*a company does not necessarily cease to be a Part 5.7 body in subs (b)(ii) of the definition if it ceases to carry on business in Australia. It remains a Part 5.7 Body for the purpose of the winding up order under s583 if the ground relied upon is that it carried on business in Australia but has ceased to carry on business.*"

In *ASIC v Edwards* [2004] QSC 344, McMurdo J went one step further and said that an unregistered foreign company was a Part 5.7 body even when the grounds for winding up were *just and equitable* grounds. His Honour commented that to allow a contrary interpretation, in either this issue or the issue raised in the *International Unity* case referred to above would "*enable a foreign company, which carried on business in Australia unlawfully by being unregistered, to avoid an order for winding up in Australia by ceasing*

its business just before the winding up application". His Honour further commented that this could never have been intended by Part 5.7. Barrett J endorsed this view in *Gebo Investments (Labaun) Ltd v Signatory Investments Pty Ltd* [2005] NSWSC 544 where he said as follows:

It cannot be accepted that a foreign company that has carried on business in Australia, with all the consequences that that entails (including, in most cases, incurring debts payable to Australian residents) is put beyond the reach of Australian winding up simply by retreating to its homeland. If, in reality, it has left no legacy requiring administration in Australia (assuming grounds for winding up are shown), any application for a winding up order is likely to be refused on discretionary grounds. But if matters cognisable in an Australian winding up have been left behind, the jurisdiction to wind up is, in my view, ongoing: cf *Banque des Marchands de Moscou (Koupetschesky) v Kindersley* [1950] 2 All ER 105. I respectfully adopt and endorse, in particular, the statements in para[41] of McMurdo J's judgment in *ASIC v Edwards*.

6.4 Part 5.4 vs Part 5.7

The difficulty for a creditor who is owed a debt by a Part 5.7 body is this: should it issue a demand for the payment of that debt pursuant to s585 or pursuant to the statutory demand procedures contained in Part 5.4?

This issue arises because of the way in which the legislature chose to deal with the interrelationship between the new Part 5.4 and the essentially unchanged Part 5.7. The Court at first instance in *The Peninsular Group Limited v Kintsu Co Limited (Kintsu)* described the drafting as "*indubitably lazy and imprecise*".

In *Kintsu*, the facts were as follows.

- (a) The defendant, The Peninsular Group Limited, was a Part 5.7 body as it was incorporated in the West Indies and registered as a foreign company pursuant to the Corporations Law (the **Law**) (the precursor to the Act).
- (b) The plaintiff issued a creditor's statutory demand pursuant to s459E of the Law and commenced proceedings seeking an order that the defendant be wound up in insolvency under the Law relying upon the failure of the defendant to comply with that statutory demand.

The defendant argued that the statutory demand served on it did not comply with s585(a) of the Law and therefore was not valid and effective to ground a winding up order against it. It argued that s585(a) mandated the form of demand and that the provisions of s583 that sought to apply Chapter 5 (together with the statutory demand procedures outlined in Part 5.4) only

applied to a Part 5.7 body those parts of Chapter 5 that were *necessary*. As s585(a) provided for a form of demand, the provisions of Part 5.4 dealing with statutory demands were not *necessary*.

At first instance, Santow J was of the opinion that the defendant's interpretation would offend "the substantial conformity that has existed for nearly sixty years between the provisions relating to the winding up of foreign companies for deemed inability to pay debts and the like winding up of local companies." He noted that there was nothing in the explanatory memorandum or in the first or second reading speeches or in any contemporaneous law reform report upon the introduction of the new Part 5.4 which evinced any intention to differentiate foreign companies. He stated that "there is no obvious logic or policy why the statutory demand regime should work radically different for the winding up of a foreign company". In concluding that the plaintiff could rely on the statutory demand it had issued, Santow J made the following comments:

The complete junction of the new Part 5.4 to the essentially unchanged Part 5.7 is neither smooth nor seamless, relying as it does on supplementation pursuant to s582 and the directive to make necessary adaptations. I am satisfied that this is the result, despite drafting which was indubitably lazy and imprecise.

Such a result accords with almost sixty years of legislative history – one which equates foreign and local liquidations in all essential aspects. It is entirely consistent with the broad non-discriminatory approach to local and foreign companies now evinced by the new Chapter 5. That in turn underpins the co-operation required for cross border insolvencies, which Part 5.7 expressly encourages.

There is no logic to differentiate between a demand against a locally incorporated company and a foreign company in such a manner. One has only to envisage a demand in relation to the same debt guaranteed by a group of companies, both local and foreign, to appreciate the inconvenience and improbable consequences from such an interpretation.

The Court of Appeal had a very different view. It held that the provisions of Part 5.4 of the Law dealing with statutory demands do not apply to the winding up of a foreign company on the grounds of insolvency. In coming to its conclusion, the Court of Appeal had regard to the following matters:

- Part 5.7 bodies are defined to include a variety of incorporated and unincorporated bodies in addition to foreign companies. A wide range of undertakings is involved in that expression yet the same provisions apply to all notwithstanding that there may be substantial differences in their character and the nature of their activities. Although there may be some uncertainty as to which parts of Chapter 5 apply to a Part 5.7 body, when it comes to the circumstances in which a Part 5.7 body may be wound up, the

provisions of s583(c) and s585 provide a comprehensive procedure. They provide, if not a code, then an exhaustive list of the grounds upon which a Part 5.7 body may be wound up. They include grounds not based on insolvency. There is thus a clear intention not to import into Part 5.7, for instance, the provisions of s461 dealing with the winding up of companies on grounds other than insolvency.

- The comprehensive form of s585, means that it is not “necessary” to adapt the application of other provisions of Chapter 5 so as to include within it the relevant provisions of Part 5.4.
- While the Court of Appeal accepted the force of the point made by Santow J about the undesirability of different treatment as between local and foreign companies, it was not persuaded that the clear words of s583 and s585 should be displaced by a consideration of that kind.

Interestingly, the Court noted that although the plaintiff’s statutory demand could not have been an effective statutory demand within the meaning of s459E of the Law, it may nevertheless have been an effective demand under s585(a).

In summary, two propositions emerge from the Court of Appeal decision in *Kintsu*. First, a creditor may be able to obtain an order for the winding up of a foreign company under s583 if its un-met statutory demand, although framed in terms of s459E, satisfies the requirements of s585(a). Secondly, a creditor who issues a s585(a) demand, without more, will then be able to seek a winding up order under s583 (although the scope of the defences to any such application is uncertain).

In general terms, the Part 5.7 regime is, in contrast to the s601CL approach, an approach at the territorial end of the universal versus territorial spectrum.

6.5 Voluntary Administration of a foreign company under Part 5.7?

Part 5.7 is limited in its application to the *winding up* of foreign companies. There does not appear to be any sound legal or policy reason why foreign companies should not be subject to the voluntary administration procedure contained in Part 5.3A of the Act particularly in circumstances where the foreign company is already involved in that procedure.

7. Co-operation Between Australian and Foreign Courts in External Administration Matters

Division 9 of Part 5.6 of the Act is as far as Australian law has gone down the *universal* path (although, as discussed below, the proposed enactment of the UNCITRAL Model Law on Cross-Border Insolvency would commit Australia more fully to a universal approach). Similar provisions exist in other countries, notably s426 of the UK Insolvency Act 1986. and Chapter 15 of the United States Bankruptcy Code..

Section 581(2) of the Act provides as follows:

- In all external administration matters, the Court:
- (a) must act in aid of, and be auxiliary to, the courts of
 - (i) external Territories; and
 - (ii) States that are not in this jurisdiction; and
 - (iii) prescribed countries;that have jurisdiction in external administration matters, and
 - (b) may act in aid of, and be auxiliary to, the courts of other countries that have jurisdiction in external administration matters.

Section 581(3) of the Act provides as follows:

Where a letter of request from a court... of a country other than Australia, requesting aid in an external administration matter is filed in the Court, the Court may exercise such powers with respect to the matter as it could exercise if the matter had arisen within its own jurisdiction.

Section 581(4) of the Act provides as follows:

The Court may request a court of... a country other than Australia, that has jurisdiction in external administration matters to act in aid of, and be auxiliary to, it in an external administration matter.

The phrase ***external administration matter*** means a matter relating to the winding up under Chapter 5 of a company or a Part 5.7 body, the winding up outside Australia of a body corporate or a Part 5.7 body or the insolvency of a body corporate or of a Part 5.7 body.

The ***prescribed countries*** are:

- (a) The Bailiwick of Jersey;
- (b) Canada;
- (c) The Independent State of Papua New Guinea;
- (d) Malaysia;
- (e) New Zealand;
- (f) The Republic of Singapore;
- (g) Switzerland;

- (h) The United Kingdom; and
- (i) The United States of America.

(Regulation 5.6.74 of the Corporations Regulations 2001 (Cth)) (the **Regulator**).

The authority given and the obligations imposed on the Court referred to above depend on whether there is an *external administration matter*. Whether there is a *winding up* outside Australia of a Part 5.7 body or the *insolvency* of a Part 5.7 body will depend on how those terms are construed by an Australian Court which, in turn, may involve the analysis and construction of foreign insolvency laws and procedures. The position would have been clearer had the legislature inserted a definition which sought to encompass foreign procedures which corresponded in general terms with the Australian procedures notwithstanding the foreign label applied to those procedures.

The distinction between subsections (a) and (b) of s581(2) should be noted. The Court *shall* act in aid of the Courts of prescribed countries however it *may* act in aid of the Courts of other countries.

The interrelationship (if any) between s581(2) and s581(3) is unclear. Section 581(2) obliges or authorises, as the case may be, the Court to act in aid of various Courts. Section 581(3) deals with the specific situation where a *letter of request* is received from a Court requesting aid in an external administration matter and that letter of request is filed in the Court. In that situation, the Court is given a discretion to exercise such powers with respect to the matter as it could exercise if the matter had arisen within its own jurisdiction. Apart from the general obligation of the Court to act in aid of a Court of a prescribed country, it appears as though an Australian Court has an unfettered discretion as to how it should exercise the powers it has pursuant to s581(3).

It is also not clear whether a Court of a foreign country or a representative or officer of that Court (such as a foreign liquidator of a foreign company) can seek the aid of an Australian Court directly pursuant to s581(2) without complying with the provisions of s581(3) and obtaining a formal letter of request from the relevant Court and arranging for that letter of request to be filed in the Australian Court. In *Re Independent Insurance Co Ltd* [2005] NSWSC 587 (*Independent*) (at [14]), Barrett J said that while s581(2) was not triggered by a letter of request, the absence of a letter of request was

likely to mean that the Australian Court does not know what action by it is "in aid of" or "auxiliary to" the other court. Accordingly, a letter of request is nevertheless desirable.

Section 581(4) contains a provision that authorises an Australian Court to request a Court of a country other than Australia that has jurisdiction in external administration matters to act in aid of and be auxiliary to the Australian Court in an external administration matter. Presumably, that will most commonly be done by way of a formal letter of request issued by the Australian Court.

7.2 Use in Australia of a Letter of Request issued by a Foreign Court – the *New Cap* decision

The provisional liquidator of New Cap Reinsurance Corporation (Bermuda) Limited (***Bermuda***) and its holding company, New Cap Reinsurance Corporation Holdings Limited (***Holdings***) obtained letters of request from the Supreme Court of Bermuda requesting that the Supreme Court of New South Wales assist the proceedings in relation to Bermuda and Holdings by appointing joint provisional liquidators to Bermuda and Holdings in Australia.

Holdings was registered in Australia as a foreign corporation. Bermuda was not so registered.

Young J⁶ noted the provisions of s581 of the Law and determined that that section did not require him to act in aid of the courts of Bermuda as Bermuda was not a *prescribed country* for the purposes of that section. However, as Holdings was registered under Part 5B.2 it was clearly a Part 5.7 body and that was sufficient to give the New South Wales Court jurisdiction to appoint the joint provisional liquidator to Holdings. On the other hand, Bermuda would only be a Part 5.7 body if it carried on business in Australia and Young J considered that there was a prima facie case that Bermuda was a Part 5.7 body.

Accordingly, he found that both Holdings and Bermuda were Part 5.7 bodies and may be wound up under s583 of the Law. Additionally, so far as Holdings was concerned, Young J also found that s601CL(14) of the Law authorised the New South Wales Supreme Court to wind up Holdings in New South Wales.

It is worth noting the comments made by Young J in the course of his judgment which bear on the likelihood of the court adopting a universal as opposed to a territorial approach to cross border insolvency. Young J said:

In recent years, the problem of corporations in trouble which have assets around the world has become an increasing problem. Winding up law is still basically a fairly local affair but when there are troubles with the company or group of companies which have assets throughout the world, then special action has to be taken to ensure as much as possible that the worldwide public is protected. To this end the courts throughout the world and particularly courts in Australia must obey the philosophy of s581 of the Corporations Law and facilitate as much as possible the control of assets throughout the world. Of course, proper considerations must be given at each step to the right of the corporators, the directors and others, but it is often necessary to act quickly to protect assets and if any error is to be made, to err on the side of protection rather than permitting assets to be in jeopardy.

Young J referred with approval to the approach taken in multinational liquidations by the UK court in *Re Dallhold Estates* referred to above. He said:

As far as I am aware, there are no Australian cases on this point, but in my view Australian courts should apply the same principle as is applied in England.

7.3 Sending a Letter of Request to an Australian Court – the *Independent* decision

In *Independent* a letter of request was directed by the English court to the NSWSC on the application by an English company and its provisional liquidators for orders in aid of the English court, invoking the NSWSC's auxiliary jurisdiction under s581 of the Act.

The NSWSC recognised, as a matter of comity, the English order appointing the provisional liquidators in England, discussed whether declaratory relief was appropriate where there was no dispute between the parties (*lis inter partes*) and considered whether such declaratory relief would be of any utility generally.

Barrett J also considered whether final injunctive relief should be granted in the absence of the other parties (*ex parte*) against persons generally, whether comity requires the making of orders in NSW of a kind made by the English court in generally reciprocal circumstances, and whether the auxiliary jurisdiction extends to the replication of orders made by courts in the United States and Ireland.

Letter of request

The English court requested the NSWSC to act in its aid by making orders including orders giving effect to provisions of the English Insolvency Act

1986.⁷ The request for these orders was based on evidence showing a tangible and substantial connection with Australia, in that *inter alia*, although Independent Insurance carried on insurance business in the United Kingdom, in the course of doing so, it wrote policies in favour of Australian residents.

Scope and effect of ss 581(2)(a) and 581(3) of the Act

Both s581(2)(a) and s581(3) of the Act arose for consideration because of the letter of request and the fact that the provisional liquidators were in office by virtue of an order made under a law of a 'prescribed country', which the United Kingdom is by reason of reg 5.6.74 of the Regulations. The threshold question as to the existence of an 'external administration matter' was satisfied as it was a matter relating to the insolvency of a body corporate⁸ since Independent Insurance was insolvent and unable to pay its debts.

Section 581(2)(a) says that the NSWSC 'must act in aid of, and be auxiliary to', among others the courts of the United Kingdom that have jurisdiction in external administration matters. The word 'must' means that it is an obligation. Section 581(2)(a) not only requires the court to act in aid but confers a specific jurisdiction to so act.

Section 581(3) applies where a letter of request is received from a court of a country other than Australia. It pays no attention to whether the other country is a 'prescribed country'. The effect of s581(3) is to confer a discretion upon the court rather than directing it to act. The court has a discretion to 'exercise such powers with respect to the matter as it could exercise if the matter had arisen in its own jurisdiction'.

Sections 581(2)(a) and 581(3) are thus different in purpose and effect. Section 581(3) allows the court to treat the foreign matter in practice as if it were a matter that had arisen within the court's own jurisdiction and to make any order relevant to such a domestic matter.

Section 581(2)(a) on the other hand imposes a requirement to act. In Barrett J's view, it is not triggered by a letter of request, in the sense that the court may act pursuant to it in the absence of such a request. However, the absence of a request is likely to mean that the Australian court does not know what action by it is or might be thought to be 'in aid of' or 'auxiliary to' the other court. A letter of request is thus a means of giving content to the s581(2)(a) requirement and in addition bringing s581(3) into play.

Justice Barrett noted that the effect of analogous United Kingdom provisions in s426 of the Insolvency Act 1986, from the perspective of a court receiving a letter of request, was considered by the English Court of Appeal in *England v Smith*⁹, where it was observed, following *Hughes v Hannover Ruckversicherungs AG*¹⁰, that the task of the receiving court is to apply either its own insolvency law or the insolvency law of the requesting country and, in either case, its own general jurisdiction and powers.

Section 581(3) enables an Australian court having jurisdiction which receives a letter of request issued by an English court to exercise, in respect of matters relating to the United Kingdom insolvency, powers that the Australian court could have exercised if the matters had arisen in Australia. Section 581(2)(a) requires the Australian court, by exercise of those powers or other aspects of its own jurisdiction, to act in aid of the English court. But Barrett J explained that the Australian court is not expressly permitted or required by the Australian legislation to exercise the statutory powers that the English court itself may exercise; nor can the United Kingdom legislation be the source of any direct power of the Australian court to do so.

Recognition of the English liquidation

Barrett J recognised the presentation of the English winding up petition, the pendency of the winding up application and the making and effect of the order by which the provisional liquidators were appointed in accordance with principles of private international law referred to by Gummow J in *Re Macks; ex parte Saint*.¹¹ The authority of the provisional liquidators and the position they occupied, as well as the status of their appointment under English law, were recognised as a matter of private international law and altogether apart from any order the Australian court might make under s581 or otherwise.

Claim for declaratory relief

The claims for declaratory relief were made beyond the confines of any demonstrated justiciable controversy. The claim for injunctive relief was also advanced apart from any *lis inter partes* and sought what Barrett J described in *Re AFG Insurances Ltd*¹² as 'an order expressed to be binding on the whole world in the manner of legislation'.

The question therefore arose as to whether the obligation cast upon the NSWSC by s581(2)(a) required, or the power conferred by a combination of

that provision and s581(3) permitted, the making of the particular orders sought. Was the court either bound or empowered to grant the declaratory relief sought on the *ex parte* application of Independent Insurance and its provisional liquidators?

The application was made in circumstances where no one was questioning the existence or status of the English proceedings or the making or effect of the order appointing the provisional liquidators. The only conceivably relevant jurisdiction of the NSWSC was therefore its inherent jurisdiction referred to in s75 of the *Supreme Court Act 1970*, the very wide discretionary power to make 'binding declarations of right': *Forster v Jododex Mines Pty Ltd*¹³ and *Ainsworth v Criminal Justice Commission*¹⁴.

Barrett J held that the declaration sought was one that would be of no utility. The only possible recipient of the message contained in the declarations sought would be the court itself. There was clearly no need for the court to make a declaration directed in effect to itself.

Claim for injunctive relief

The claim for injunctive relief was in effect a claim for a permanent injunction by way of final relief. The order, if made, would be an indiscriminate command to unidentified persons not to commence or continue any proceeding against Independent Insurance or its property in Australia while the provisional liquidators remain in office (or after a winding up order is made), except with leave granted by the English court under the English legislation.

Barrett J was satisfied that such an order would be an order made in aid of the English court in the matter of the provisional liquidation ordered by it in respect of Independent Insurance. This was because s130(2) of the *Insolvency Act 1986* (UK), a provision very similar to s471B of the Act, provides that, where a provisional liquidator has been appointed, no action or proceeding shall be proceeded with or commenced against the company or its property except with the leave of the English court and subject to such terms as it may impose, and a similar embargo applies after a winding up order has been made.

Section 581(2)(a) was the clear source of the jurisdiction. The order would be an order regulating the initiation or continuation of proceedings in a way that would have been open to the English court if the proceedings had been

prosecuted within its jurisdiction and this, following the second *AFG Insurances* case¹⁵, is an aspect of the 'acting in aid' jurisdiction.

Order directed to unidentified persons

The order in question however, if made, would be 'an order expressed to be binding on the whole world in the manner of legislation'. The entities to which it was directed were those with claims against Independent Insurance and they were presently unidentifiable.

Barrett J held that an injunction should not be made in terms which are indefinite as to the persons to be bound and nor should any relief be granted *ex parte* except in circumstances of urgency. No circumstances of urgency warranting *ex parte* relief were suggested in the case and there was no suggestion that any person was threatening to commence or continue relevant proceedings against Independent Insurance or in respect of its property.

The fact that the jurisdiction invoked was the particular auxiliary jurisdiction created by ss581(2)(a) and 581(3) did not displace the general principles applicable with respect to granting the particular form of relief sought. Barrett J stated that principles governing the making of orders in the exercise of general equitable jurisdiction must be observed even though that jurisdiction is resorted to in aid of a foreign court pursuant to statutory powers of the kind conferred by s581: *Fourie v Le Roux*¹⁶.

Reciprocity

It was submitted that comity warrants reciprocity in light of the willingness of the English court to make restraining orders of the kind in question where it is the NSWSC that makes a request and the English court that acts upon it.

The court held that Australia has not enacted laws adopting recognised international measures for the administration of cross-border insolvencies. Although moves towards incorporation of the UNCITRAL Model Law on Cross-Border Insolvency into Australian law are well advanced (see [9.4]-[9.5] below), in the meantime, in a case involving a corporate insolvency in the UK, the only special jurisdiction the NSWSC has is that conferred by s581, and, in so far as that section empowers the court to deploy its general equitable jurisdiction in aid of a UK court in a way that territorial limitations would otherwise not allow, the jurisdiction is to be exercised in accordance with general principles.

Similar auxiliary relief in other countries

There were in force both in the United States and Republic of Ireland court orders generally similar in purpose and effect to the injunctive relief order sought. Barrett J described the mechanisms for ancillary administration in aid of foreign insolvency proceedings in s304 of the United States *Bankruptcy Code* and the provisions of Section 250 of the *Companies Act 1963* of Ireland. It was submitted that in a case of cross-border insolvency where Australia is one of several satellite jurisdictions, relief here should, to the extent possible, be framed so as to be compatible and consistent with relief already in place in comparable countries.

Barrett J's decision in this regard was that the statutory approaches and judicial attitudes to auxiliary jurisdiction in cross-border insolvency in the US and Ireland differ from those in Australia. Whilst in the US there is apparent acceptance of the notion that a prohibitory order against persons with no notice of it is unobjectionable because those persons may apply to be exempted from it, the clear emphasis in Australian courts is the other way: *BP Australia Ltd v Brown*¹⁷.

Conclusion

The *Independent* decision clearly explains how s581(2)(a) and s581(3) of the Act operate. The main findings were that the NSWSC will recognise, as a matter of private international law, an English order appointing provisional liquidators in the UK. However, declaratory relief will not be given in the absence of a *lis inter partes* (dispute between the parties) and in effect directed to the court, and injunctive relief will not be granted *ex parte* (in the absence of the other parties) as an indefinite order against unidentified persons.

Comity does not require that orders be made in NSW just because in generally reciprocal circumstances the English court would be prepared to make them. Similarly, the auxiliary jurisdiction does not extend to the replication of orders made by courts in the US and Ireland, since, irrespective of its being a satellite jurisdiction in the cross-border insolvency, the approach to *ex parte* injunctive relief in Australia is different.

7.4 Obtaining a letter of Request from an Australian Court

In *AFG Insurances*¹⁸, the administrators of AFG Insurances Limited (**AFG**) made an application under s581(4) seeking the issue of a letter of request

directed to the High Court of Justice in England to act in aid of the Australian Court in its external administration of AFG.

An earlier application by AFG¹⁹ had been denied on 2 grounds:

- (i) the Court was not satisfied that there was a situation of 'insolvency' as required by paragraph (c) of the definition of 'external administration matter' at s580; and
- (ii) the orders that the English court would have been asked by the letter of request to make were not orders in the making of which that court would 'act in aid of, and be auxiliary to' the Australian Court in relation to an 'external administration matter' as required by s581(4).

In granting the second application, the Court noted that the issue of insolvency was resolved by the presentation of more comprehensive evidence of the financial position of AFG. It further noted that the letter of request had been amended to an acceptable form. In considering the meaning of the phrase 'act in aid of, and be auxiliary to' in the context of s581(4), Barrett J stated:

The relevant concept of acting in aid of and being auxiliary to this court is not, I think, confined to recognising or giving effect to an order of this court, although the concept certainly has that aspect. An additional aspect, I am persuaded, involves the making by the foreign court, within and for the purposes of its jurisdiction, of orders that this court could have made in relation to the relevant subject matter had this court's jurisdiction, in the territorially limited sense, extended that far.

In *Dallhold Estates*²⁰ Dallhold was a wholly owned subsidiary of Dallhold Investments. Dallhold Investments was in liquidation and the liquidator served a demand upon Dallhold. Dallhold's main asset was a leasehold interest in a large estate in England. The landlord and its controller claimed they were creditors of Dallhold and were taking steps to terminate the lease the terms of which included a provision that on a final winding up order being made, the landlord would be entitled to terminate the lease. Under the relevant UK law, the lessee could not obtain relief against forfeiture.

The liquidators of Dallhold Investments sought the assistance of the Australian Court in making a request to the UK Court pursuant to s426 of the Insolvency Act 1986 that an administration order be made over Dallhold to prevent Dallhold being wound up and any security over its property being enforced without the consent of the administrator or the leave of the Court.

In deciding that it was appropriate to issue a letter of request, Gummow J stated that:

It is desirable that the best possible realisation of the assets of Dallhold Estates be achieved for the benefit of all its unsecured creditors. I will make a declaration that it is desirable to request the assistance of the English Courts. That assistance may be provided by the making of an administration order, if the English Court having charge of the matter thinks it fit so to order, or by the making of such further order or other order as it may consider appropriate.

7.5 Assistance from UK Courts

Shortly after judgment was delivered in *Dallhold Estates*, a letter of request was issued to the High Court of Justice in England. Initially, the UK court authorised the English provisional liquidator of Dallhold and Dallhold Investments to present a petition for an administration order in respect of Dallhold.

In granting the petition order made shortly thereafter, the UK Court²¹ applied the relevant provisions of s426 of the Insolvency Act 1986 which are 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.

In exercising its discretion under this subsection, a Court shall have regard in particular to the rules of private international law.

The Court reviewed the matter in this way. The matter specified in the letter of request was an application for an administration order. The relevant provisions in relation to the grant of an administration order were contained in s8 of the Insolvency Act 1986. Having satisfied itself that the conditions contained in that section for the grant of an administration order were present, the Court concluded that as s426 of the Insolvency Act 1986 obliged the requested Court to assist the foreign Court, the requested Court ought to make an administration order in that case *unless there is some compelling reason why that should not be done*. In other words, the UK Court held that the usual discretion as to whether it ought to make an administration order did not apply to the same extent where jurisdiction was

conferred on the Court by s426. A similar approach has been adopted in Australia which is dealt with below.

The UK court highlighted the significance of the matters specified in the letter of request from the Australian Court. It is the matters specified in that request which confer jurisdiction upon the UK court and the court was of the view that it was not open for it to engage in a far ranging inquiry which goes beyond the matters specified in the request. Accordingly, it is very important that the party seeking the issue of a letter of request by an Australian court drafts its request very carefully to ensure that the UK Court will be satisfied of its jurisdiction to provide the requested assistance.

Another example of a request made pursuant to s426 of the Insolvency Act 1986 was the request by the provisional liquidator of New Cap Reinsurance Corporation (Bermuda) Limited to the High Court of Justice in England for assistance to the Supreme Court of Bermuda by appointing joint provisional liquidators of that company and conferring powers and functions on the joint provisional liquidator as may be necessary or desirable with a view to ensuring that the company's affairs and business are fully investigated, the company's assets situated within the jurisdiction of the High Court of Justice in England are located, protected, secured and got in and the company's books and records situated within the jurisdiction of the High Court of Justice in England are located, protected and secured.

7.6 HIH Casualty & General Insurance cases and the limits of English assistance

An originating process to wind up HIH Casualty & General Insurance Ltd (**HIH**) and three associated companies was presented to the NSWSC in March 2001 and liquidators of HIH were appointed in August 2001. The NSWSC had already issued a letter of request to the English High Court for the appointment in England of provisional liquidators over HIH pursuant to s426 of the English Insolvency Act 1986 back in March 2001 and the English provisional liquidators were duly appointed to HIH, the liquidation of which in the UK was ancillary to the Australian liquidation.

It subsequently became clear that in order to assist the Australian liquidators in the performance of their duties, the sums collected by the English provisional liquidators would need to be remitted to Australia for the Australian liquidators to apply them in the due course of winding up HIH or in accordance with a scheme of arrangement. In June 2005 the Australian

liquidators demanded the remittance of the assets by the English provisional liquidators to Australia for distribution and the latter resisted, instead seeking directions from the English High Court as to the appropriate distribution of the assets collected in England. Accordingly, the Australian liquidators applied to the NSWSC for a letter of request to the English High Court to be issued to this effect.

Letter of request

On the application of the Australian liquidators, on 4 July 2005 Justice Barrett ordered the transmission of a letter of request to the English High Court. The letter of request stated that the Australian liquidators had shown to the satisfaction of the NSWSC that it was necessary that the English provisional liquidators remit the sums to be collected by them to the Australian liquidators for application in the due course of the winding up of HIH.

What is interesting, however, is that the letter of request did not directly request the English court to direct the English provisional liquidators to pay over to the Australian liquidators the sums collected in their official capacity. Instead, the letter of request asked the English court to assist, act in aid of and be auxiliary to the NSWSC '*by hearing and determining an application by the Australian liquidators for directions to the English provisional liquidators*' to pay over the relevant sums collected. It can be inferred that this attenuation of the request was made in the interests of comity between jurisdictions and reflecting Australian judicial respect for the equivalent court in England.

English proceedings

On the same date that Justice Barrett issued the letter of request in Australia, Justice Hart in the Companies Court in the Chancery Division of the English High Court ordered that the application for directions and the request application be expedited. Justice Richards accordingly heard the matter as English summer vacation business and handed down judgment on 7 October 2005.

Decision against transfer of assets to Australia

Justice Richards held that, if the companies in question were ordered to be wound up by the English courts, the English liquidators would be directed not to transfer assets to Australia, as those assets would not be distributed

in Australia according to rules for a *pari passu* distribution substantially the same as the English rules.

The next question was whether, notwithstanding that decision, the English court should direct the English provisional liquidators to make such a transfer in view of the fact that the directions for transfer were sought pursuant to a letter of request from the NSWSC.

Relevant UK insolvency legislation

The answer depended on the court's interpretation of the effect of s426 of the UK *Insolvency Act 1986* (England and Wales). Section 426 confers powers and duties on the English court to provide assistance to other courts in insolvency matters. The relevant provisions are in 7.5 above.

A restricted number of mainly Commonwealth countries, including Australia, were designated to be relevant countries or territories pursuant to the *Cooperation of Insolvency Courts (Designation of Relevant Countries and Territories) Order 1986* (England and Wales).²²

Section 426(10) defines 'insolvency law' in a manner which allows the English courts to apply either English insolvency law or the insolvency law of the requesting state to the extent that it corresponds to English insolvency law provisions.

First instance case law on section 426

The *prima facie* mandatory language of s426(4) was considered in three English first-instance cases in 1992, 1994 and 1997 respectively, and by the Court of Appeal in 1997. In *Re Dallhold Estates (UK) Pty Ltd*²³, Justice Chadwick referred to the court's discretionary power to make an administration order, and stated that if the statutory prerequisites for its exercise were fulfilled, the court should make the order '*unless there is some compelling reason why that should [not] be done.*'²⁴

In *Re BCCI (No. 9)*²⁵, Justice Rattee stated that the court has a discretion as to how it should provide assistance and that it ought to exercise its discretion in favour of providing the particular assistance requested by the foreign court '*unless there is some good reason for not doing so.*'²⁶

*Re Focus Insurance Co Ltd*²⁷ related to an application by the liquidators of a Bermudan company for an order requiring the giving of information by a person who had been bankrupt in England. Sir Richard Scott VC stated:

Section 426(4) ... appears to impose on the courts ... a mandatory obligation. The words used are 'shall assist'. But ... the subsection is silent as to the manner in which the courts ... 'shall assist' and it is easy to conclude that it could not be supposed that the courts ... would have a mandatory obligation to provide assistance in a manner that was contrary to the proper conduct of a bankruptcy in this country.

The objective underlying the originating application and the letter of request was contrary to the scheme for realisation of a debtor's assets and payment of the debtor's creditors prescribed by the bankruptcy legislation in force in the UK. Sir Richard Scott VC accepted²⁸ the guidance of Justice Chadwick and Justice Rattee. He stated that there was:

plainly some element of discretion vested in me as to whether I should or should not accede to the originating application pursuant to the letter of request, notwithstanding that sub-s(4) of s426 uses the words 'shall assist'²⁹.

The English Court of Appeal judgment in *Hughes v Hannover*

In the 1997 judgment of *Hughes v Hannover Rückversicherungs-AG*³⁰, Lord Justice Morritt broke down the sources of law which the English court may apply into three categories: (a) its own general jurisdiction and power, (b) English insolvency law, and (c) those provisions of the requesting state's law which correspond to English insolvency law. His Lordship outlined the English court's approach to the question of whether to provide assistance as follows:³¹

- It would require clear words to justify a conclusion that the English court was not intended by Parliament to perform its normal function of seeking to do justice in accordance with the law.
- The function of the court under s426 is to consider whether in accordance with the three sources of law identified as (a), (b) and (c) the assistance may properly be granted.
- If it may then it should be, thereby discharging the statutory duty under s426.
- If it may not be, then it should be withheld, as the duty is qualified by reference to what the English court may properly do as a court.
- If the English court cannot do exactly what is sought then it should consider whether it can properly assist in some other way in accordance with any of the available systems of law.
- The reasons for withholding assistance are not limited to reasons of public policy.

- Public policy may prevent assistance being given under (c) if the provision of the insolvency law of the country the court of which requested the assistance were contrary to the public policy recognised by the English court.
- The fact of the request for assistance is a weighty factor to be taken into account.
- The English court may be expected to accept without further investigation the views of the requesting court as to what was required for the proper conduct of the winding up.
- The request is not conclusive as to the manner in which the discretion of the court should be exercised.

In the HIH case under consideration in this paper, Justice Richards decided that the substantive rules of distribution under the English statutory insolvency scheme are mandatory and that the English court has no power to make an order which would have the effect of disapplying them. It therefore followed that the English court could not accede to the NSWSC's request for a transfer of funds to Australia. His Lordship held that the power to make such an order does not exist in English law and any power under Australian law could not be exercised by the English court in a way contrary to English law. In the words of Lord Justice Morritt, it would not be assistance that *'may properly be granted'*.

Ironically, were it not for section 562A and the statutory benefit it seeks to provide to insureds, the English court may well have been satisfied that the Australian insolvency regime was sufficiently similar to the English system providing for an appropriate *pari passu* distribution for it to have been appropriate to direct the English provisional liquidators to pass on the money they collect to the Australian liquidator for distribution in accordance with Australian law.

The decision of Justice Richards was a conservative view of the letters of request procedure in English insolvency law. It reflects a leaning towards the territorial side of the spectrum of ways to approach cross-border insolvency matters, as opposed to a more internationalist approach.

As so much reinsurance of Australian insurance risks is, and has historically been, written out of London, Justice Richards' decision effectively renders section 562A of the Act nugatory, at least when an Australian insurer went into liquidation and an ancillary liquidator is appointed in the UK prior to 20

April 2003 when the Insurers (Reorganisation and Winding Up) Regulations 2004 (SI 2004/353) were introduced. The regulations referred to above give a special priority to insurance claims such that they rank immediately after salary, social security, taxes and some entitlements over the assets of the insurance undertaking. This legislation does improve the priority position of insurance creditors in England but not to the same extent as section 562A. We will need to see whether a case relating to an Australian insurer going into liquidation in the UK after 20 April 2003 might produce a different result – applying the reasoning in HIH though we would think that the differences between the two regimes remain substantial enough so as to result in the same outcome ie the retention of assets in the UK so that English law is applied to any distribution. On the basis of this decision, reinsurance proceeds recovered in England in those circumstances will not be remitted to Australia for distribution in accordance with Australian law to the priority benefit of insurance creditors.

The English decision is therefore a very important one for Australian insurers, and more particularly their insureds and brokers, because the comfort they may have had that, if - in the worst of worlds - their insurer went into liquidation, they would still get first access to any reinsurance recoveries may be illusory. The decision of Justice Richards was appealed to the Court of Appeal.

Court of Appeal decision in HIH

The Court of Appeal held that Justice Richards had gone too far, and that in certain circumstances where a transfer of assets is for the benefit of creditors, the transfer should be made, even if this would involve the disapplication of English insolvency principles. The Court also found that the English court had jurisdiction to use section 426 to authorise a transfer of assets from the liquidators of an ancillary winding up to the liquidators of the principal winding up, where the companies are in liquidation in England, even if the result of such a transfer would interfere with the statutory scheme imposed on those assets by the Insolvency Act. However, the Court held that whether such a transfer should be authorised is discretionary, and in exercising its discretion, a Court must consider the prejudice to the interests of some creditors. Ultimately, the court refused to direct a transfer of the English assets, as this would have prejudiced the interests of many creditors. Accordingly, the appeal was dismissed.

The Court of Appeal decision stands for the principle that while a UK Court may apply foreign rather than English law, if asked by a letter of request to do so, it will not do so where creditors, or a class of creditors, would be disadvantaged. Leave has been given for the matter to be appealed to the House of Lords.

Consequences for HIH Schemes

Following the English judgment at first instance, the liquidators reformulated the scheme of arrangement and, at a hearing on 18 November 2005, Justice Barrett, taking the English decision into account, was satisfied that the new scheme satisfied his concerns and ordered that the proposed scheme could proceed. Following the subsequent creditors' meetings approving the amendments to the scheme, on 26 May 2006, Justice Barrett made orders approving the Australian scheme with one minor variation. The scheme of arrangement in the UK was approved by the Court on 12 June 2006.

Watch this space

We await with interest the judgment from the English House of Lords which should tell us the significance that it ascribed to the Australian letter of request in making its decision. The judgment will further develop this complex and fast-growing area of international insolvency case law.

The role and utility of letters of request – conclusion

One of the aims of letters of request in a cross border insolvency is to enhance co-operation between jurisdictions. That co-operation becomes all the more important as more and more Australian companies become involved in overseas business, whether insurance and reinsurance or otherwise. The decision of Justice Richards in HIH reflects a conservative view of the letters of request procedure in English insolvency law. While less restrictive than Justice Richards' approach, the Court of Appeal decision is similarly conservative, and perhaps indicates a lean towards a territorial approach to cross-border insolvency, as opposed to an internationalist approach. It will be interesting to see how the issue is dealt with by the House of Lords.

8. UNCITRAL Model Law on Cross Border Insolvency

8.1 Nature of Model Law

A broad framework for dealing with cross border insolvency issues has been established by the United Nations Commission on International Trade Law (**UNCITRAL**) in its model law on cross border insolvency (***the Model Law***), adopted by consensus on 30 May 1997 at the thirtieth session of UNCITRAL. In December of 1997, the General Assembly of the United Nations adopted resolution 52/159, in which it expressed its appreciation to UNCITRAL for completing and adopting the Model Law. One of UNCITRAL's functions is to seek to further the harmonisation and unification of World Trade Law.

Because the text is a Model Law rather than a treaty, it is meant to be adopted as part of the law of each enacting State. The Guide to Enactment as prepared by the UN Secretariat states that the Model Law is designed to assist the States to equip their insolvency laws with a modern, harmonised and fair framework to address more effectively instances of cross border insolvency. The Guide says that the Model Law reflects practices in cross border insolvency matters that are characteristic of modern, efficient insolvency systems. The Model Law is essentially procedural in other respects and the differences among national substantive insolvency laws are unaltered. The Model Law does not attempt a substantive unification of insolvency law. The solutions it offers include:

- providing access for the person administering a foreign insolvency proceeding (*“foreign representative”*) to the courts of the enacting State, thereby permitting the foreign representative to seek a temporary *“breathing space”*, and allowing the courts in the enacting State to determine what co-ordination among the jurisdictions or other relief is warranted for optimal disposition of the insolvency;
- determining when a foreign insolvency proceeding should be accorded *“recognition”*, and what the consequences of recognition may be;
- providing a transparent regime for the right of foreign creditors to commence, or participate in, an insolvency proceeding in the enacting State;

- permitting courts in the enacting State to co-operate more effectively with foreign courts and foreign representatives involved in an insolvency matter;
- authorising courts in the enacting State and persons administering insolvency proceedings in the enacting State to seek assistance abroad;
- providing for court jurisdiction and establishing rules for co-ordination where an insolvency proceeding in the enacting State is taking place concurrently with an insolvency proceeding in a foreign State;
- establishing rules for co-ordination of relief granted in the enacting State in favour of two or more insolvency proceedings that may take place in foreign States regarding the same debtor.
- Providing speedy access to foreign insolvency practitioners to the courts of enacting states to aid the prevention of the dissipation and transfer of assets out of the jurisdiction.

8.2 Scope

The model law applies in a number of cross border insolvency situations. Those situations include, where:

- (a) assistance is sought in Australia by a foreign court or a foreign representative in connection with a foreign proceeding;
- (b) assistance is sought in a foreign State in connection with a proceeding under Australian law;
- (c) a foreign proceeding and a proceeding under Australian law in respect of the same debtor are taking place concurrently;
- (d) creditors in a foreign State have an interest in requesting the commencement of, or participating in, a proceeding under Australian law (article 1).

8.3 Access

The model law gives a *foreign representative* the right to appear in local courts. A direct application for assistance can be made and proceedings can be commenced under the enacting State's laws. In addition, the foreign representative may participate in a proceeding regarding the debtor in the enacting State providing the foreign proceedings are first *recognised* (articles 9, 11 and 12). The Guide states that an important objective of the

Model Law is to provide expedited and direct access for foreign representatives to the courts of the enacting State. The law avoids the need to rely on cumbersome and time consuming letters rogatory or other forms of diplomatic or consular communications, which might otherwise have to be used.

8.4 Recognition of Foreign Proceedings

Articles 15-17 establish the criteria for determining whether a foreign proceeding is to be recognised. The decision includes a determination whether the jurisdictional basis on which the foreign proceeding was commenced was such that it should be recognised as the “*main*” or instead as the “*non-main*” foreign insolvency proceeding. A foreign proceeding is deemed to be the “*main*” proceeding if it has been commenced in the State where “*the debtor has the centre of its main interests*” (**COMI**). The determination that a foreign proceeding is a “*main*” proceeding may affect the nature of the relief accorded to the foreign representative.

Key elements of the relief accorded on recognition of the representative of a foreign “*main*” proceeding include a stay of actions of individual creditors against the debtor or a stay of enforcement proceedings concerning the assets of the debtor and a suspension of the debtor’s right to transfer or encumber its assets (article 20). Article 21 authorises the court to grant discretionary relief for the benefit of any foreign proceeding, whether “*main*” or not.

8.5 Treatment of Foreign Creditors

Article 13 of the Model Law gives foreign creditors the same rights regarding the commencement of, and participation in, a proceeding under the laws of the enacting State as creditors in that State. However, article 13 does permit the enacting State to grant or deny equivalent treatment for foreign creditors as to priorities, but provides a general floor of treatment as a general, unsecured creditor.

8.6 Cross Border Co-operation

As the Guide puts it, a widespread limitation on co-operation and co-ordination between judges from different jurisdictions in cases of cross border insolvency is derived from the lack of a legislative framework, or

from uncertainty regarding the scope of the existing legislative authority, for pursuing co-operation with foreign courts.

Articles 25 to 27 of the Model Law oblige and empower local courts to co-operate to the maximum extent possible with foreign courts or foreign representatives and examples of forms of co-operation are contained in article 27.

8.7 Co-ordination of Concurrent Proceedings

Recognising the reality of the politics of international co-operation, article 28 of the Model Law does not significantly limit the jurisdiction of the local courts to commence or continue insolvency proceedings. Under article 28, even after recognition of a foreign “*main*” proceeding, jurisdiction remains with the local courts to institute an insolvency proceeding if the debtor has assets in the enacting State and the effects of that proceeding are to be substantially restricted to the assets of the debtor that are located in that State.

The Model Law deals with co-ordination between a local proceeding and a foreign proceeding concerning the same debtor (article 29) and facilitates co-ordination between two or more foreign proceedings concerning the same debtor (article 30). The guide states that the objective of the provisions is to foster co-ordinated decisions that would best achieve the objectives of both proceedings (eg maximisation of the value of the debtor’s assets or the most advantageous restructuring of the enterprise).

When the court is faced with more than one foreign proceeding, article 30 calls for tailoring relief in such a way that will facilitate co-ordination of the foreign proceedings. If one of the foreign proceedings is a “*main*” proceeding, any relief must be consistent with that “*main*” proceeding.

Article 32 of the Model Law is designed to enhance co-ordination of concurrent proceedings by adjusting payments to creditors. It provides that a creditor, by claiming in more than one proceeding, does not receive more than the proportion of payment that is obtained by other creditors of the same class.

9. Adoption of the Model Law

9.1 International moves towards enacting the Model Law

Since its adoption by UNCITRAL in 1997, both the World Bank (in its April 2001 paper *Principles and Guidelines for Effective Insolvency and Creditor Rights Systems*) and the International Monetary Fund (in its 1999 report *Orderly & Effective Insolvency Procedures*) have expressed their support for the enactment of the Model Law. UNCITRAL's long standing program (begun in 1999 at Australia's instigation) to produce a Legislative Guide to Insolvency Law (adopted by UNCITRAL on 25 June 2004 and by the United Nations General Assembly on 2 December 2004) has added prominence to the Model Law, which is annexed to it. The Legislative Guide has been developed by UNCITRAL with consultation of insolvency professionals world wide and is designed to be a guide for national legislatures to use as a reference when reviewing or creating efficient and effective national corporate insolvency regimes. It is not intended to be prescriptive or obligatory in any way. By having the Model Law and the Guide to the Enactment of the Model Law annexed to the Legislative Guide, UNCITRAL hopes to facilitate greater awareness of cross border insolvency issues. It also puts the Model Law in the context of UNCITRAL's larger project to endeavour to modernise and standardise insolvency regimes worldwide for the benefit of all those participating in international trade and commerce.

To date the following countries have formally enacted the Model Law: Eritrea, Mexico, South Africa, Montenegro, Serbia, Poland, Romania, Japan, India, the British Virgin Islands, the United States of America and the United Kingdom. Others, including Australia, Canada, New Zealand and Malaysia, have made positive statements supporting incorporation of the Model Law into their respective legal systems but have not yet taken any positive steps towards enacting the necessary legislation. The relatively slow adoption of the Model Law is not so much an indication of a lack of support for its principles as a hesitation on the part of many governments to enact the Model Law before a critical mass of jurisdictions have done so.

The US legislation amending chapter 15 of the US Bankruptcy Code to incorporate, almost unaltered, the Model Law came into force in October 2005. The UK incorporated the Model Law into UK statutes at the end of 2005. By doing so, the USA and the UK took a perhaps belated leadership

role which may give greater impetus to the wider adoption of the Model Law in the global community.

9.2 Australian moves towards enacting the Model Law

The adoption and enactment of the Model Law in Australia was considered as a part of the Government's Corporate Law Economic Reform Program – CLERP 8. In October 2002, the government released a discussion paper on Cross-Border Insolvency in which the advantages and disadvantages of enacting the Model Law are considered.

In the forward to the Government's discussion paper, Senator the Hon Ian Campbell, Parliamentary Secretary to the Treasurer, states that effective cross-border insolvency arrangements “*have the potential to enhance the operation of the global financial system, providing long-term benefits to Australian business.*” To that end, the paper set out 14 proposals for the reform of Australia's cross-border insolvency regime and invited comments on the possible enactment of the Model Law by the Commonwealth Parliament.

9.3 Benefits of Enacting the Model Law for Australia

In considering the benefits that would accrue to Australia should the Model Law be enacted, the discussion paper emphasises Australia's leadership role in the international insolvency community and the opportunity for Australia to encourage by example the adoption of the Model Law, particularly in the Asia-Pacific. Australia played a major role in the development of the Model Law. The Government considers that its adoption of the Model Law will have substantial persuasive value in the region. The position taken by New Zealand, which has proposed to enact the Model Law but not until it has been implemented in Australia, is set out as one example of the impact that Australia's enactment of the Model Law would have.

As the Model Law does not require reciprocity, the discussion paper recognises that the major benefits, in terms of equality of treatment for Australian creditors, ease of recovering assets from foreign jurisdictions and more efficient treatment of international insolvencies involving Australian businesses, will only accrue once other jurisdictions have also adopted the Model Law.

The discussion paper notes that Australia is not currently a party to a multilateral convention on cross-border insolvency and that there is no convention which it could appropriately enter into for this purpose. It concludes that, for Australia, 'the UNCITRAL Model Law is the leading initiative on this issue'.

9.4 Proposals by the Australian Government – CLERP 8 (as endorsed by the Parliamentary Joint Committee on Corporations and Financial Services "Corporate Insolvency Laws: a Stocktake" Report dated June 2004)

The main proposals made by the Government in its discussion paper are that:

- (a) Australia enact the Model Law by a separate Act of the Commonwealth Parliament, subject to specific proposals regarding the details of its implementation;
- (b) the Insolvency and Trustee Service Australia make recommendations to the Government about the application of the Model Law to individual debtors;
- (c) entities currently subject to special insolvency regimes in Australia (including financial institutions) be excluded from the scope of the Model Law;
- (d) the sections of the Act dealing with cross-border insolvency be retained with the following provisions:
 - (i) subsections 601CL (14)-(16), concerning the cessation of business of a foreign company, will only apply if the circumstances fall outside of the scope of the Model Law or if the Model Law is not invoked;
 - (ii) Part 5.7 *Winding Up Bodies other than Companies* be amended as necessary to ensure harmonious operation with the Model Law;
 - (iii) Division 9 of Part 5.6 be retained in relation to external administration matters arising under the Act;
- (e) Articles 1 – 14 of the Model Law be adopted essentially as written, together with the optional provision of Article 13(2) concerning the

exclusion from the Model Law provisions of revenue claims by a foreign state from insolvency proceedings under Australian law;

- (f) Articles 15 – 18 of the Model Law be adopted as written;
- (g) Articles 19 – 24 of the Model law be adopted as written with Article 20(2) specifying the exceptions as the right of a secured creditor to enforce a security over property of the debtor or specific relief from the effects of the stay granted by a court and Article 23(1) setting out the voidable transactions provisions in Division 2 of Part 5.7B of the Act;
- (h) Articles 25 – 27 be adopted as written;
- (i) Articles 28 – 32 be adopted essentially as written; and
- (j) in the enactment of the Model Law, a facility be set out by which the Model Law may be streamlined and tailored as it applies to particular types of proceedings or proceedings involving a specific State.

CLERP 8 essentially recommends the adoption of the Model Law in a separate Act of Parliament to the Act. In addition to recommending the retention of the cross border provisions currently contained in the Act (subject to minor amendment and standardisation with the Model Law), namely s601CL; Part 5.7 and s580 and s581, to cover issues not covered by the Model law (for example the winding up in Australia of a foreign company notwithstanding the fact that the foreign company was not being wound up in an overseas jurisdiction and recognition of those proceedings was not therefore being sought), CLERP 8 and the Joint Committee have endorsed the Model Law on the basis that it was well equipped to deal with all the complexities and consequences presented by cross border insolvency which the current Act regime does not fully cater for. CLERP 8 recommended that banks, insurance and life insurance companies, which have their own special insolvency regimes under the Banking Act 1959, the Insurance Act 1973 and the Life Insurance Act 1995 be excluded from the Model Law in a similar way in which the new chapter 15 of the US Bankruptcy Code excludes those industries (and essential services). CLERP 8 recommended that the State and Territory governments consider whether any other companies, for example providers of essential services, should also be excluded from the Model Law.

CLERP 8 foresees that winding ups arising from insolvencies; reconstruction and reorganisation under Part 5.1 and voluntary administrations will be covered by the scope of the Model Law. However private receiverships, members voluntary winding up and winding up on just and equitable grounds would be excluded from the Model Law.

9.5 Timing

In the light of Australia's close involvement in the Model Law project and the recent adoption of the Model Law developments in the USA and the UK, it is a question of when, not if, the Model Law is incorporated into the domestic cross border insolvency regime.

In November 2006, the government released draft legislation for consultation in relation to the Model Law within the next 6 months entitled *The Corporations Amendment (Insolvency) Bill 2007*. In the Explanatory Memorandum accompanying the draft legislation, the Australian government confirmed its commitment to adopting the UNCITRAL Model Law. This is now expected to occur in 2007 – probably in the Australian autumn.

10. Conclusions

There are many advantages to the UNCITRAL Model Law, including greater ease of access to courts for foreign practitioners, greater protection of assets and greater efficiency of gathering and realising assets.

Accordingly, adoption of the Model Law is likely to promote greater cooperation and coordination in cross-border insolvencies. The extent to which this will occur will of course depend on how uniformly the Model Law is adopted worldwide; however the likely imminence of Australian legislation, along with its acceptance by several countries including the US and UK suggests that a successful regime may emerge.

NOTE: This document is intended only to provide a general review on matters of concern or interest to readers. The text of this document should not be relied upon as legal advice. Matters differ according to their facts. The law changes. You should seek legal advice on specific fact situations as they arise.

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¹ Although even between Commonwealth countries with as common a background as Australia and England, the fact that one insolvency is said to be "ancillary" to the other does not necessarily result in the ancillary liquidator remitting assets to the primary liquidation – see eg *In the matter of HIH Casualty and General Insurance Limited & Ors* [2006] EWCA CIV732 (Ch) (discussed in more detail at 7.6 above).

² Although it is expected to do so in Australia's Autumn 2007 (see 9 above).

³ Certain provisions of the *Insurance Act* (Cth) and other legislation may in any event prohibit the remitting by an Australian liquidator of all funds simply less expenses overseas eg s116 of the Act which gives special protection to persons with 'liabilities in Australia', s562A of the Act which creates a quasi-charge over reinsurance recoveries received by an Australian liquidator (*HIH Casualty & General Insurance Limited & Ors* [2005] NSWSC 240), s562 of the Act which creates a quasi-charge over insurance recoveries in favour of certain third parties, s6 *Law Reform Miscellaneous Provisions Act* (NSW) (and its equivalent in the Australian Capital Territory) which creates a statutory charge over the right to insurance recoveries – see Rafal Zakrzewski, "The Nature of a Claim on an Indemnity" (2006) 22 JCL 54(?) and *Butterell v Douglas Group Pty Ltd* (2000) 35 ACSR 398] in favour of certain third parties.

⁴ For example, the New South Wales Supreme Court's (**NSWSC**) refusal to grant injunctive relief at the request of English provisional liquidators in *Independent Insurance Company Ltd* [2005] NSWSC 587 (22/6/05) (**Independent**) (discussed in more detail at 7.3 above).

⁶ *Re New Cap Reinsurance Corporation Holdings Limited* [1999] NSWSC 536 Young J 3 June 1999

⁷ sections 130(2) and 126

⁸ under s580(c)

⁹ [2001] 1 Ch 419

¹⁰ [1997] 1 BCLC 497

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- ¹¹ (2000) 204 CLR 158
- ¹² (2001) 20 ACLC 1588 (at [20])
- ¹³ (1972) 72 CLR 421 at p 435 per Gibbs J
- ¹⁴ (1992) 175 CLR 564 at pp581-2 per Mason CJ, Dawson, Toohey and Gaudron JJ.
- ¹⁵ (2002) 43 ACSR 60 at paragraph [8]
- ¹⁶ [2005] EWCA Civ 204, 7 March 2005.
- ¹⁷ (2003) 58 NSWLR 322 at p 348 per Spigelman CJ (with whom Mason P and Handley JA agreed)
- ¹⁸ *Re AFG Insurances Limited* [2002] NSWSC 844 Barrett J 11 September 2002
- ¹⁹ *Re AFG Insurances Limited* [2002] NSWSC 735
- ²⁰ *Re Dallhold Estates (UK) Ltd (Prov Liq Apptd)* [1991] 6 ACSR 378 Gummow J 27 November 1991
- ²¹ *Re Dallhold Estates (UK) Ltd (Prov Liq Apptd)* [1991] 6ACSR 378 Gummow J 27 November 1991
- ²² SI 1986/22123
- ²³ [1991] BCLC 621
- ²⁴ *ibid.*, at 627
- ²⁵ [1994] 3 All ER 764
- ²⁶ *ibid* at 785
- ²⁷ [1997] 1 BCLC 219 at 224
- ²⁸ *ibid.*, at p 227
- ²⁹ *ibid.*, at p 230
- ³⁰ [1997] 1 BCLC 497
- ³¹ *ibid.*, at pp 517-518