

RESTRUCTURING AND INSOLVENCY

BRIEFING

CENTRE OF MAIN INTERESTS (“COMI”)

WHAT IS COMI?

COMI is a creation of European Union law designed to settle conflicts that can arise between jurisdictions in cross-border insolvencies, based on the principles of mutual recognition and co-operation. The EC Regulation on Insolvency Proceedings¹ (the “Regulation”) governs the opening of insolvency proceedings in Member States by laying down rules for deciding where main insolvency proceedings can be opened in circumstances where a company has a presence in more than one Member State. The Regulation is directly applicable to all EU Member States apart from Denmark, and applies to all forms of companies (but not to insurance undertakings, credit institutions or investment undertakings).

Under Article 3 of the Regulation, the courts of the Member State in which the company's COMI is situated have exclusive jurisdiction to open main insolvency proceedings – only secondary proceedings can then be opened in other Member States. The Regulations do not define the term “COMI” – the only guidance given is that:

- ◆ Article 3 states that the location of a company's registered office is presumed to be its COMI in the absence of proof to the contrary
- ◆ Recital 13 states that a company's COMI should correspond to the place where the company conducts the administration of its interests on a regular basis, and therefore can be ascertained by third parties

As a result of there being no statutory definition, COMI has been both manipulated by companies (giving rise to the concept of “COMI migration” or, the less flattering “forum shopping”) and more fully interpreted by the courts of Member States in a number of high-profile insolvencies and debt restructurings. Both creditors and debtors (in circumstances where the debtor is supportive of a proposed debt restructuring) who want to take advantage of a more favourable insolvency regime have sought to rebut the presumption that a company's COMI is the place of its registered office and have sought to migrate COMI to another chosen jurisdiction in order to open main proceedings in that jurisdiction, thereby using the insolvency laws and procedures of that jurisdiction.

FACTORS USED BY THE COURTS TO DETERMINE COMI

The decisions in both *Daisytek* and *Eurofood*² stated that any factors relied on to rebut the registered office presumption must be both objective and ascertainable to third parties. The court's judgment in *Daisytek* held that the most important third parties were the potential creditors of the company, because they must know where to contact the company and what legal risks they are incurring by lending to it.

Following a review of a number of decisions of the courts in England and the US and of the ECJ, the Court of Appeal held in *Re Stanford International Bank Ltd (in liquidation)*³ that the appropriate test of COMI depends on ascertainability by those who deal with the company, so that they should know where any insolvency proceedings of the company should be brought – and that only those factors which are in the public domain and which a typical third party would learn through their dealings with the company are relevant.

From the cases so far, factors to be considered when determining a company's COMI can include (but are not limited to) the location of the company's:

- ◆ internal accounting functions
- ◆ business relations with clients
- ◆ the law governing its main contracts
- ◆ creditors
- ◆ strategic control functions
- ◆ IT systems
- ◆ tax domicile and the domicile of its directors
- ◆ board meetings
- ◆ general supervision

WHY MIGRATE COMI?

COMI migration allows a debtor to work with its creditors to implement a restructuring of its debts, using the jurisdiction most attractive to the dominant stakeholder(s). The attraction to a particular jurisdiction may be that it:

- ◆ has a good track record and is considered to be more transparent, sophisticated, efficient and flexible in the way it handles proceedings. New insolvency legislation in certain jurisdictions such as Spain and Germany which is geared towards addressing the current financial crisis may make those jurisdictions more attractive; however, new legislation will often be untested and its benefits may be outweighed by the perceived uncertainty over its interpretation and implementation

¹ Council Regulation (EC) No. 1346/2000, of 29 May 2000, [2000] OJ L 160/1

² See the Appendix for more detail

³ See the Appendix for more detail

- ◆ is more familiar to stakeholders
- ◆ allows the debtor to impose a cram-down on dissenting secured or unsecured creditors
- ◆ allows more pre-planning (in the UK, for example, the use of the Administration procedure allows sufficient pre-planning to permit an immediate sale of businesses or assets on terms negotiated by the insolvency practitioner before his appointment as administrator - a “pre-pack Administration”)
- ◆ allows the stakeholder(s) to choose who is appointed as officeholder, rather than an appointed by the relevant Courts
- ◆ requires less court involvement
- ◆ provides an opportunity to take advantage of DIP funding available to insolvent entities (for example, debtor-in-possession financing in Sweden and the US or Insolvenzgeld in Germany and Austria)
- ◆ avoids the application of employees' rights on a transfer of an undertaking

EXAMPLES OF CHANGING COMI TO THE UK

While the courts are keen to avoid COMI migration where it is crudely implemented, prejudices creditors and does not involve a legitimate transfer of interests, there is scope to undertake a COMI migration in order to take advantage of the insolvency laws and procedures of another Member State. The UK's appeal lies to a great extent in its ability to:

- ◆ cram-down minority creditors by the use of a Court sanctioned Scheme of Arrangement or a Creditors Voluntary Arrangement (a “CVA”). Broadly speaking, these procedures can cram-down up to 25% of each class of a company's creditors
- ◆ restructure debt and shareholding by the use of the Administration procedure

RECENT EXAMPLES OF COMI MIGRATION TO THE UK

Deutsche Nickel (2004) and Schefenacker (2007)

Schefenacker is an automotive supply group and Deutsche Nickel is an alloy supply group. In each case, their chosen option was a non-consensual restructuring of bondholder debt by way of a debt-to-equity swap implemented by a CVA (there is

some ability to cram-down in this way under German insolvency law, but it is more cumbersome and uncertain to implement and can give rise to equitable subordination issues).

In each case, COMI was migrated from Germany to the UK by transferring the assets and liabilities of a German holding company to an English holding company by way of an accrual (Anwachsung). Although this type of universal succession is not a valid method for passing title under English law, English law recognises a foreign law universal succession as long as it is properly structured.

Damovo (2007)

Damovo is a computer services business. Its chosen option was a non-consensual restructuring of its bondholder debt by way of a pre-packaged Administration. COMI was migrated to the UK by a number of corporate steps, including:

- ◆ the transfer of head office functions to the UK
- ◆ informing all suppliers, creditors and counterparties of its new address in the UK
- ◆ holding board meetings in the UK
- ◆ opening bank accounts in the UK

Wind Hellas (2009)

Wind Hellas is a major operator of fixed line and mobile technology services in Greece with (broadly speaking) two tiers of financing: those guaranteed by the principal trading company, Wind Hellas, (the senior debt comprising senior secured notes and senior notes) and those not guaranteed by Wind Hellas (including subordinated notes and PIK notes). Its chosen option was a non-consensual restructuring of its debts by way of a pre-packaged Administration that resulted in nearly €1.5 billion of subordinated debt being left in an insolvent company without recourse to any economically valuable assets.

COMI of a Luxembourg holding company, Hellas II, the immediate parent of Wind Hellas and the guarantor of all the senior debt and the issuer of the subordinated notes, was migrated to the UK by a number of corporate steps, including:

- ◆ making an English registered company the corporate general partner
- ◆ appointing UK resident individuals to be directors and members of the supervisory board of Hellas II

- ♦ opening a new head office in London, from where correspondence was sent and board meetings were held
- ♦ registering Hellas II at Companies House as a foreign company and as a UK establishment of an overseas company
- ♦ notifying all creditors of Hellas II of the change of its address
- ♦ conducting all negotiations with creditors in London

Although these examples show successful COMI shifts, it is important to remember that the key question on establishing a COMI is whether the information is already in the public domain which a typical third party would learn through their dealings with the company – the changes cannot only be “hidden” changes within the company’s organisation.

RECENT EXAMPLES OF COMI MIGRATION TO OTHER JURISDICTIONS

In other cases, companies have shifted COMI:

- ♦ to France in order to take advantage of the Safeguard procedure (this was contemplated in the Monier and PAI restructurings, although not ultimately required in order to implement their respective restructurings)
- ♦ to Germany in order to bring all insolvency procedures under one jurisdiction (this was the case for the restructuring of PIN, a German mail delivery company that had a Luxembourg holding company)

CONTACT DETAILS

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APPENDIX

Re Daisytek ISA Limited (2003) (unreported)

ISA, an English registered company, was the holding company for a group including German and French subsidiaries. ISA performed the group's head office functions in the UK, negotiated supply contracts with major suppliers and guaranteed any outstanding balances due from the French and German subsidiaries.

The directors of ISA applied for administration orders over substantially all of the group, including the French and German subsidiaries. The court concluded that the requirement in Regulation 13 that the COMI must be ascertainable to third parties was of great importance. The most important third parties are potential creditors - if there are insolvency proceedings, creditors must know where to contact the debtor and what legal risks they are incurring in dealing with the debtor.

The administration orders were granted. The decision was based largely on where the finance was arranged and where the contracts with key suppliers were negotiated and administered, rather than where the services to customers were carried out.

As a secondary point, both the French and German courts of first instance decided they had jurisdiction over the French and German subsidiaries and did not recognise that the COMI of the subsidiaries could be anywhere other than the location of their registered offices. These decisions were overturned on appeal by the English administrators and the proceedings in these jurisdictions relegated to "secondary" proceedings.

Re Eurofood IFSC Limited [2005] BCC 1021

The Advocate General (AG) decided that in order to rebut the registered office presumption in Article 3, an entity must show that its head office functions are performed elsewhere. The focus should be on head office functions, not only the location of the head office. The AG commented "*in transnational business, the registered office is often chosen for tax or regulatory reasons, and has no real connection with the place where head office functions are actually carried out*".

In its judgement, the ECJ did not specifically mention the head office function test. It did, however, point out that in order to rebut the presumption in favour of the registered office, the factors relied on must be both objective and ascertainable to third parties, and held that the presumption would be rebuttable in the case of a letterbox company that carries on no business in the place of registration.

Stanford International Bank Limited and others [2009] EWHC 1441

The High Court followed Eurofood, holding that a company's COMI is presumed to be at the location of its registered office, unless there are objective factors that are ascertainable to third parties and that would lead them to conclude that the head office functions of the company were being carried out elsewhere. For these purposes, what is ascertainable to third parties is what is in the public domain and what a typical party would learn in the ordinary course of business with the company.

The Court of Appeal (*Re Stanford International Bank Ltd (in liquidation)* [2010] EWCA Civ 137) undertook an extensive review of the decisions of the courts in the UK and the US, and of the ECJ.

Having decided that the Antiguan liquidation (the "Liquidation") could be a foreign main proceeding under the UNCITRAL Model Law on Cross Border Insolvency (the "Model Law"), the issue then was whether the Liquidation was in fact a foreign main proceeding. This could only be the case if the Bank's COMI was in Antigua when the liquidation proceedings commenced.

The decision of the High Court was challenged on three grounds, the most important of which was that the wrong test had been applied as to the facts relevant to the rebuttal of the registered office presumption. On this issue, the Court of Appeal held that the High Court had been correct in applying the *Eurofood* test. The appropriate test depends on ascertainability by those who deal with the company so that they should know which law would govern the company's insolvency.

The Chancellor did not think that the Model Law and the Regulation required different meanings to be given to COMI and, further, that it was essential that they should be interpreted consistently. If there was any difference between the test set out by the ECJ in *Eurofood* and that applied by the US courts, the English courts should apply the *Eurofood* test.

The Court of Appeal held that *Eurofood* clearly established that:

- ◆ each company has its own COMI; and
- ◆ the head office presumption can be rebutted only by objective factors ascertainable by third parties.

The factors ascertainable by third parties should be confined to matters already in the public domain and what a typical third party would learn as a result of dealing with the company. Matters that could only be established on enquiry should be excluded.

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This note is intended to provide general information about some recent and anticipated developments which may be of interest. It is not intended to be comprehensive nor to provide any specific legal advice and should not be acted or relied upon as doing so. Professional advice appropriate to the specific situation should always be obtained.

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