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# Enforcement of solvent schemes of arrangement and Part VII transfers in the United States and the European Union

Nobody likes to be ignored. Schemes of arrangement and Part VII transfers have become essential components of the London run-off market, but would that be the case if policyholders were able to ignore them? In the UK, the court order sanctioning a scheme or Part VII transfer is binding on all policyholders and cedants within the jurisdiction. However, it is common – due to the international nature of the London Market – for the majority of a proponent’s creditors to be located overseas. If they can ignore the English court’s order, there is likely to be little point in going ahead with the scheme or Part VII proposal.

Below we consider the enforcement of schemes and Part VII transfers in the two main geographical areas where London market reinsurers may be exposed: the United States and the European Union.

### The United States

Opponents of solvent schemes persist in expressing the intent to defeat them by preventing their enforcement in the United States. Despite this, such schemes consistently continue to be enforced by the US courts under Chapter 15 of the United States Bankruptcy Code, which replaced former Bankruptcy Code section 304 effective 17 October 2005.

As of this writing, the US bankruptcy courts have had before them thirteen Chapter 15 re/insurer related cases. In all of these cases, bar one where the decision was made not to pursue the scheme, the US bankruptcy courts ordered Chapter 15 recognition and relief in aid of the non-US proceedings.

To date, no formal reasoned objection has been filed asserting to a court that Chapter 15 relief is, or should be, unavailable in aid of solvent schemes

Even in the absence of formal objection to a Chapter 15 petition, the US bankruptcy court has an independent obligation to determine whether or not the court is jurisdictionally empowered to recognize and provide relief in aid of the non-US proceeding before it can enter an order doing so. Accordingly, each Chapter 15 order entered to date granting aid to a non-US solvent run-off scheme has the effect and precedential impact of a determination by the issuing court that the scheme proceeding has met each of the eligibility requirements solvent scheme opponents claim such schemes are incapable of fulfilling, and a determination that the scheme proponents are entitled to the relief solvent scheme opponents insist US courts must deny them.

No Chapter 15 petitions have been filed thus far respecting UK Part VII transfers. Two Part VII transfer cases were filed under former US Bankruptcy Code section 304. They were determined

differently by two different bankruptcy judges sitting in the same courthouse. The first court denied relief because, in that court’s view, the Part VII transfer process as presented to the court did not qualify as a ‘*foreign proceeding*’ entitled to assistance from US bankruptcy courts because it was not an ‘*insolvency-related*’ proceeding but rather in the nature of a merger and acquisition transaction (*In Re Rose*). The second court granted US aid to the Part VII transfer on the basis that the petition was uncontested, ignoring its colleague’s prior decision in an equally uncontested case.

Neither of these decisions bind any other US bankruptcy judge. They also do not control petitions filed under Chapter 15, whose definition of ‘*foreign proceeding*’ differs in significant ways from that applicable to former section 304. Even under section 304 the *Rose* decision is questionable. In fact, arguably that court’s own deliberations during the hearings in the case reveal bases upon which that court itself might rule differently respecting Part VII transfers.

Part VII transfers are not anathema to the United States or its bankruptcy system. They are in several ways analogous to proceedings in the United States, including proceedings filed under the US Bankruptcy Code by solvent entities for the sole purpose of disposing of burdensome or unwanted assets, which regularly are upheld. Even were they not comparable to US proceedings, the central purpose of Chapter 15 is to facilitate the enforcement of *non-US* orders and aid the effectiveness of *non-US* proceedings within the United States; not to impose US law or process. The success of any petition seeking US relief in aid of a Part VII transfer therefore will depend on the sensitivity of the pleadings submitted and arguments made in both the Part VII proceeding and the Chapter 15 case to the policy underpinnings of Chapter 15 which support such relief.

### Europe

As many readers know, the attractiveness of EU reinsurers transferring portfolios of business to the UK presented by the implementation of the EU Reinsurance directive, and witnessed

recently in the Deutsche Rück transfer, has focussed attention on the following questions:

- If, after a transfer of reinsurance business from an EU reinsurer to a UK entity, that book of business is schemed, can that solvent scheme be enforced against the reinsureds in their State?
- More generally, where a solvent scheme is being promoted by a UK company or a non-UK company with sufficient connection to the UK, will such a scheme be enforced against its non-UK EU reinsureds in the relevant EU States?
- Can a UK Part VII transfer of business in other EU States be enforced against the relevant reinsureds in those other States?

The answers will depend on the law and procedure of the EU State in question to a degree. However, as discussed below, such local laws and procedures must be interpreted in the context of EU harmonizing legislation which increasingly takes priority over local law. The position in Germany points up some of the hurdles which must be overcome in enforcing solvent schemes and UK Part VII in the EU.

## The Enforcement Regulation

The key tool to enforcing UK solvent schemes in EU States is the EU Enforcement Regulation (Council Regulation (EC) No 44/2001 of 22 December 2000) which replaced the Brussels and Lugano Conventions on jurisdiction and enforcement of judgments in civil and commercial matters. It came into force on 1 March 2002 and now regulates the recognition and enforcement of judgments for all EU Member States (except Denmark).

## Articles 32 to 37 of the Enforcement Regulation

The relevant parts of the Enforcement Regulation to be applied are Articles 32 to 37 which specify when judgment in an EU State must be recognised in another EU State. Article 32 defines a judgment as “any judgment given by a court or tribunal of a Member State, whatever the judgment may be called”. However, neither the European Court of Justice nor any Continental European court has yet considered whether the English court’s order sanctioning a

solvent scheme falls within this definition.

It has been argued that the only form of judgment which would be recognised must be preceded by adversarial proceedings and that a sanction order does not fall within such a description. Readers will know however that recent cases demonstrate very clearly that such proceedings have the potential for being adversarial. A second argument advanced is that the European Court of Justice has ruled that for a judgment to be enforceable under the Enforcement Regulation it must “emanate from a judicial body of a Contracting State deciding on its own authority on the issues between the parties” (*Solo Kleinmotoren GmbH v Boh ECR I-2237*). The argument goes that a solvent scheme is akin to a settlement approved by the court not a judgment. However, again, the BAIC case (*British Aviation Insurance Company Limited* [2005] EWHC 1621 (Ch)) disproves this. Lewinson J expressly clarified the law saying the judge’s role in sanctioning a scheme was to exercise an unfettered discretion despite creditors’ views expressed through their meeting resolutions.

Again, a third argument is that the genesis of a scheme is its filing with the registrar of companies and not the sanction given by the court. This does seem rather weak. The need for filing is an administrative notice requirement only.

The court proceedings applying to Part VII transfers are similar in many respects to that of solvent schemes, culminating in the court sanctioning the transfer. It would seem that the above points applying to solvent schemes apply equally to Part VII transfers.

The enforceability of these procedures beyond the UK is key to their effectiveness. But, as can be seen from above, there are still significant areas requiring further clarification. Resolving these outstanding issues will determine the true global reach of Part VII transfers and schemes of arrangement.

This article first appeared in *The Insurance and Reinsurance Review* (March 2008). It is for guidance only and is not intended to be a substitute for specific legal advice. If you would like any further information please contact:

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