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PARTICIPATION IN A RUSSIAN INSOLVENCY DOES NOT BAR PROCEEDINGS AGAINST THE DEBTOR IN ENGLAND: Recent decision - *Erste Bank AG, London Branch v JSC "VMZ Red October"*

Following the Supreme Court decision in *New Cap Re*, creditors were concerned that by participating in a foreign insolvency of a borrower or other counterparty (usually in that party's home country), they might be giving up the right to bring proceedings against it elsewhere, conferred by negotiated jurisdiction clauses for example. The recent decision in *Erste Bank AG, London Branch v JSC "VMZ Red October" and Ors* [2013] EWHC 2926 (Comm) confirms that foreign insolvencies do not automatically defeat later proceedings brought in England, but creditors should remain cautious when participating in a foreign insolvency process.

Gide acted for the successful claimant in *Erste*. Mr Justice Flaux held that by simply proving in insolvency proceedings of its borrower and a guarantor in Russia, Erste had not submitted to the Russian court. It was still entitled to bring proceedings against the borrower and guarantor in England (under an exclusive jurisdiction clause) to determine claims against them following their default.

BACKGROUND

Erste Bank AG, London Branch ("**Erste**") is a member of a syndicate which provided a loan of USD 80m to JSC "VMZ Red October" (the "**Borrower**"). The loan was guaranteed by the Borrower's parent company, Red October Steel Works (the "**Guarantor**"). Both entities were incorporated in Russia and were part of a larger group of Russian companies, now headed by a State-owned entity, Rostech (the "**Group**"). Both the facility agreement and the guarantee were governed by English law with the option to bring proceedings in the courts of England.

Following significant asset transfers, the Borrower defaulted on the loan, and the Guarantor failed to pay under the guarantee. Both the Borrower and the Guarantor then entered insolvency proceedings in Russia.

The syndicate (including Erste) proved for unpaid amounts in the Russian insolvencies of the Borrower and the Guarantor. Erste then also brought a claim in England against the Borrower and the Guarantor for non-payment under the finance documents. Erste also brought a claim in England against those companies (as anchor defendants) and the wider Group in conspiracy, alleging a scheme of asset transfers and manipulation of the Russian insolvency process to avoid repayment of the loan altogether.

'Submitting a proof of debt means submission of all issues against that debtor to the foreign insolvency process?'

Two of the group companies, including Rostech, challenged the jurisdiction of the English court. One of the arguments raised was that Erste had submitted all its claims against the Borrower and the Guarantor to the Russian court by proving in their insolvencies. This was done by making an application to the Russian Court to be entered on to the debtor company creditors registers, and effected by court order. If claims against the Borrower and Guarantor could not be brought in England, then there was no basis to use them as "anchor defendants" i.e. use the claims against those companies to bring the other Russian defendants in to English proceedings.

PRINCIPLE

Under common law[1], a judgment issued in foreign proceedings, including insolvency or bankruptcy proceedings, will be capable of enforcement or recognition in England if the person against whom the judgment was given submitted to the jurisdiction of that court by voluntarily appearing in the proceedings (Rule 43 in *Dicey, Morris & Collins, The Conflict of Laws* 15th edition [14R-054]).

What amounts to a voluntary submission to the jurisdiction of a foreign bankruptcy is a question of fact.

In the *New Cap Re* appeal, the defendants had not defended proceedings brought in Australia to recover payments which the insolvent company had made to them, and had in fact objected to the jurisdiction of the Australian court in that respect, but they *had* filed proofs of debt in the liquidation in Australia and participated to a limited extent (e.g. attended creditors meetings). The liquidators obtained a judgment against the defendants and then sought to enforce that judgment in England.

Lord Collins said at [161]: "*The question whether there has been a submission is to be inferred from all the fac*ts". He accepted that having chosen to submit to New Cap's Australian insolvency proceeding, the syndicate should be taken to have submitted to the jurisdiction of the Australian court responsible for the supervision of that proceeding. He said, at [167]: *"[the syndicate] should not be allowed to benefit from the insolvency proceeding without the burden of complying with the orders made in that proceeding."*

'Whether there has been a submission is to be inferred from all the facts'

DECISION IN ERSTE

Mr Justice Flaux noted that, in *New Cap Re*, Lord Collins was not purporting to lay down some rule of law that putting in a claim for proof in a foreign bankruptcy or liquidation constitutes a submission of all issues to the jurisdiction of the foreign court.

[1] Foreign insolvencies might also attract recognition in England, automatically under the EU Insolvency Regulation (where the process is begun in another member state) or upon recognition granted under the Cross-Border Insolvency Regulations 2006.

The Judge highlighted three critical aspects of the facts which distinguished the case from *New Cap Re*, and which meant that Erste had not submitted to the jurisdiction of the Russian court, so as to preclude it from pursuing claims against the Borrower and Guarantor in England:

(1) There was no application being made by the Russian liquidation managers to recognise the Russian insolvencies in England.

(2) The insolvency procedure in Russia was different to that in common law jurisdictions (such as England and Australia). In Russia, admitting a claim to the list of creditors' claims is a formal process, of a provisional nature, and need not determine the underlying claims. Therefore, by putting forward its claim to be placed on the creditors' registers, Erste had not submitted the determination of the merits of its contractual claims against the Borrower and Guarantor (let alone the conspiracy claims) to the jurisdiction of the Russian courts.

(3) On the evidence of Russian law experts concerning the doctrine of *res judicata* in the Russian Arbitrazh court system, Russian court decisions are only binding as to the facts found and do not have extra-territorial effect. Accordingly, a Russian Court would not consider that its own judgments bound a foreign court in any way.

OTHER RECENT DECISIONS

'Later decisions distinguish New Cap Re to avoid an unsatisfactory result.'

Mr Justice Flaux's approach is consistent with other common law decisions made after *New Cap Re* on the question of submission by filing a proof of debt in insolvency proceedings.

In *Isis Investments Ltd v Oscatello Investments Limited and Ors* [2013] EWHC 75 (Ch), Mrs Justice Asplin refused to grant a stay of English proceedings in favour of insolvency proceedings in the Isle of Man, holding that proofs of debt submitted in the Manx proceedings were stated to be contingent to any entitlements to be determined in the English proceedings.

Likewise in Australia, in *Ackers v Saad Investments Company Ltd* [2013] FCA 738, the Federal Court decided that the Commissioner of Taxation had not submitted to the jurisdiction of the Grand Court of the Cayman Islands simply because he lodged a proof of debt in order to obtain information or to attend a meeting of creditors. Justice Rares considered that the Commissioner could not have made an election when, at the time of submitting the proof, he was unaware of what, if any, courses of action he had in Australia and where the object of the proof was to ascertain whether any assets were still left in Australia against which he could seek to recover. Critically, the judge determined that, in the period relied on by the foreign representatives, the Grand Court had never exercised any jurisdiction over the Commissioner and he did not make, and was not party to, any application to the Grand Court.

CONCLUSION

The decisions in *Erste* confirms that, by proving in foreign insolvency proceedings, a creditor will not necessarily be deemed to have submitted all issues against the debtor to the relevant foreign court and that any subsequent claim brought in England is not defeated automatically.

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