Seise the day--jurisdictional challenges

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Restructuring & Insolvency analysis: What effect will the recent Court of Appeal decision of Erste Group Bank AG v JSC 'VMZ Red October' have on jurisdictional issues in English law? Richard Morgan QC, one of the barristers who argued the case, says that although these types of issues may be litigated more frequently, the English courts are doing a good job acting as a gatekeeper in relation to the extent of their jurisdiction.

Original news

Erste Group Bank AG v JSC 'VMZ Red October' and others [2015] EWCA Civ 379, [2015] All ER (D) 135 (Apr)

What were the jurisdictional factors in this case and how did the issue arise?

The case concerned a loan to a steel factory in Volgograd called Red October. Erste Bank was one of a syndicate of lenders. The loan was governed by English law and allowed for the bank to serve on the borrower and the guarantor, its parent, as of right in England and elect to litigate in England. Erste, an Austrian bank, had participated by making the loan through the books of its English branch.

The third defendant, 'RT', for whom I acted, is a Russian entity holding state assets, one of which is an indirect minority interest in Red October.

Erste alleged that RT had conspired to cause Red October to go into insolvent liquidation by having it and its parent alienate their assets and then keep those assets from being realised in the insolvency process so that they could not be used to pay creditors. RT denied all the allegations.

Erste obtained permission to serve out on RT on the basis that:

- it was a necessary or proper party to the claims against Red October and its parent
- the claims were in respect of a contract governed by English law, and
- the claims were made in tort and damage was sustained in England, being the place from which Erste had made its loan and in which it expected repayment by the facility agent

Erste said England was the appropriate forum because:

- the claims were governed by English law
- the Russian courts had incorrectly set aside the guarantee on the basis that Russian law was applicable in the circumstances
- Erste would not get a fair trial in Russia because the Russian courts were biased and Erste had already experienced that bias in the course of its participation in the Russian insolvencies of Red October and its parent

At first instance, although setting aside service under the contract gateway, following *Alliance Bank JSC v Aquanta Corporation and others* [2012] EWCA Civ 1588, [2012] All ER (D) 230 (Dec), and holding that there

was no sufficient evidence that Erste would not get a fair trial in Russia, Flaux J refused RT's application under Part 11 challenging the jurisdiction of the court. He held, in outline, that:

- submitting proofs of debt in the Russian insolvencies was not submission of Erste's claims to the jurisdiction of the court
- it was strongly arguable that the applicable law of the torts was English, and Erste had the stronger argument that damage was sustained within the jurisdiction
- it was misconceived to suggest that there was insufficient connection with the jurisdiction to justify any relief under the Insolvency Act 1986, s 423 (IA 1986) so that the court should decline jurisdiction

He also held that the claim against RT should proceed in England as it was a proper party to the claims against Red October and the guarantor that would be going ahead in any event, and it would be verging on the perverse for Erste to have to litigate against RT in Russia. In addition, the judge held that the Russian courts had already applied the wrong law in setting aside the guarantee, and that English law, not Russian law, should arguably govern the disputes.

RT and a co-defendant appealed Flaux J's decision.

Had the bank submitted to the jurisdiction by proving the Russian insolvencies?

Following *Stichting Shell Pensioenfonds v Krys and another* [2014] UKPC 41, [2014] All ER (D) 280 (Nov), the Court of Appeal accepted RT's submissions that, by the mere fact of putting in proofs in the Russian insolvencies of Red October and its parent, Erste had submitted to the jurisdiction of the Russian courts all questions, of whatever kind, against those debtors--irrespective of the question of whether Russian insolvency processes and their doctrine of res judicata corresponded directly with English law. Further, that submission would be recognised by the English court, even though it was not the debtors themselves that were raising the issue. The consequence of submission of Erste's proofs (and admission as regards Red October) in the context of the insolvencies was that as between Erste and Red October and its parent there was no real issue that it was reasonable for the court to try.

Was there a sufficient connection with England for the IA 1986, s 423 claim?

Flaux J considered that the application of IA 1986, s 423 required a fact-sensitive enquiry that was not appropriate for determination on a summary basis at an interlocutory stage. The Court of Appeal preferred the approach of Lightman J in *Re Banco Nacional de Cuba* [2001] 3 All ER 923 that it was necessary for a claimant to demonstrate a serious issue to be tried in relation to the relief sought. In this case, the Court of Appeal considered that it was inconceivable that Erste would be able to show at trial that there was a sufficient connection with England to justify the grant of appropriate relief.

What did the court decide about the proper law doctrine? Which jurisdiction applies under Rome II, art 4?

There was no dispute between the parties that the choice of law for the alleged torts fell to be determined in accordance with Regulation (EC) 864/2007 (Rome II). The Court of Appeal decided that, whether or not Rome II would identify Russia as the location of the primary damage in accordance with *Dumez France and Tracoba v Hessische Landesbank:* 220/88 [1990] ECR I-49, in any event the unambiguous provisions of the loan agreement identified New York as the place for repayment of the loan, and Red October could obtain good discharge by making payment there, irrespective of whether the bank had instructed that any payment be transferred on to its account in London. On this basis, New York was the place where loss was directly suffered, but there was a manifestly closer connection between the alleged torts and Russia, and on that basis Russian law applied.

Do you think there is a growing trend for English courts to be more cautious in seising jurisdiction in cross-border cases?

No. I think the approach tends to be, give permission to serve out at the without notice stage and address technical concerns if a jurisdiction challenge is subsequently raised. It is only at that stage that the court really has to grapple with the nitty-gritty of the rules. I think the judiciary does a good job acting as a gatekeeper in relation to the extent of their jurisdiction.

The recent flurry of jurisdiction challenges is a result of the times. The global financial crisis generated a large number of claimants who wanted to try their luck here and the various changes to the European Jurisdiction and the Civil Procedure Rules 1998, SI 1998/3132 mean that the 'edges' of the English jurisdiction are perhaps less clear than they used to be. There will always be claimants who want to come here for a host of reasons (with the availability of freezing orders, disclosure and a truly impartial judiciary being significant drivers) and they will always argue for a more expansive approach--there will also always be defendants who are concerned about having their claims determined in a forum that they consider inappropriate or inconvenient. It is only those cases where the 'edges' come to be more defined that are reported, and those are the cases in which the court has given permission and then subsequently had to consider the position more closely when a challenge has been made.

In this case, the Court of Appeal was invited to grapple with the conflicting lines of authority in relation to PD 6B, para 3.1(9) on the extent of the tort jurisdiction. However, although they expressed serious concern about whether the first instance cases on the tort gateway were correctly decided, they did not need to decide the point as they had already effectively found that the bank's loss was sustained in New York, which meant the tort gateway was unavailable to Erste. However, the judgment sounds a warning bell to those who base their jurisdiction arguments on the *Booth v Phillips and others* [2004] EWHC 1437 (Admlty), [2004] All ER (D) 191 (Jun) and *Cooley v Ramsey* [2008] EWHC 129 (QB) line of authority on PD 6B, para 3.1(9) that their ability to serve out might not be completely secure. No doubt in due course the Court of Appeal will be presented with a case where this very issue has to be decided, but for the moment it remains one of those 'edges' that has yet to be clearly illuminated.

Richard Morgan QC is a barrister at Maitland Chambers and is principally involved in large scale Chancery/commercial litigation covering aspects of company law, commercial contracts, insolvency, civil fraud, asset tracing and recovery, and conflict of laws, along with the broader stream of Chancery work, including arbitrations and mediation. He has significant experience both applying for and opposing the grant of freezing orders and other interim relief. A number of his recent cases have involved jurisdiction challenges.

Interviewed by Janine Isenegger.