

NEWSLETTER

CMS RESTRUCTURING AND INSOLVENCY IN EUROPE

SUMMER 2011

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INTRODUCTION

We are pleased to present this Summer 2011 edition of the CMS Restructuring and Insolvency in Europe Newsletter. We aim to give information on topical issues in insolvency and restructuring law in countries in which CMS offices are located.

This edition looks at:

- the role of a provisional administrator in Belgium;
- insolvency law developments in the Czech Republic;
- the case of *Deko Marty Belgium* and its implications for German insolvency proceedings;
- the Hungarian Bankruptcy Act and its recognition of pending claims;
- a new exemption of bankruptcy crime in Italy and its effect on bank support for distressed companies seeking alternative procedures to bankruptcy;
- recent examples of the Dutch courts' application of the European Insolvency Regulation;
- amendments to the Polish Insolvency Law allowing for the close-out netting of collateral arrangements in a counterparty's insolvency;
- the potential liabilities facing members of a board of an insolvent Romanian company;
- changes to Ukrainian insolvency law preventing suspension of security enforcement on a moratorium; and
- recent case law regarding the application of the European Insolvency Regulation by the English courts.

CMS is the organisation of independent European law and tax firms of choice for organisations based in, or looking to move into, Europe. CMS provides a deep local understanding of legal, tax and business issues and delivers client-focused services through a joint strategy executed locally across 29 jurisdictions with 54 offices in Western and Central Europe and beyond. CMS was established in 1999 and today comprises nine CMS firms, employing over 2,800 lawyers and is headquartered in Frankfurt, Germany.

The CMS Practice Group for Restructuring and Insolvency represents all the restructuring and insolvency departments of the various CMS member firms. The restructuring and insolvency departments of each CMS firm have a long history of association and command strong positions, both in our respective homes and on the international market. Individually we bring a strong track record and extensive experience. Together we have created a formidable force within the world's market for professional services. The member firms operate under a common identity, CMS, and offer clients consistent and high quality services.

Members of the Practice Group advise on restructuring and insolvency issues affecting business across Europe. The group was created in order to meet the growing demand for integrated, multijurisdictional legal services. Restructuring and insolvency issues can be particularly complex and there is such a wide range of different laws and regulations affecting them. The integration of our firms across Europe can simplify these complexities, leaving us to concentrate on the legal issues without being hampered by additional barriers. In consequence we offer coordinated European advice through a single point of contact.

THE APPOINTMENT OF A PROVISIONAL ADMINISTRATOR AS A PRIOR STEP TO BANKRUPTCY

Under Belgian law, a provisional administrator (*administrateur provisoire/voorlopig bewindvoerder*) can be appointed in specific circumstances by the Court to carry out a specific mission or to replace the board of directors of a company that is no longer able, to guarantee the proper day-to-day management of the company. The provisional administrator will ensure, for a determinate period, the continuity of the company and will be able to take all appropriate decisions.

This article considers the scope, procedure and effects of an appointment of a provisional administrator under the Bankruptcy Act of 8 August 1997 (the “Bankruptcy Act”).

The appointment of a provisional administrator

Article 8 of the Bankruptcy Act foresees the possibility, in case of emergency and if there are *serious, precise* and *corroborating* signs that the conditions for a bankruptcy are met by a company, for the President of the Commercial Court to appoint a provisional administrator over such a company.

The procedure before the Court can be introduced by any person having an interest in the appointment of a provisional administrator. The Court is also competent to order the appointment of a provisional administrator *ex officio*.

The person appointed as provisional administrator needs to have experience in management and in accountancy, must meet the criteria of impartiality and independence in order to perform his functions in the sole interest of the company and the creditors, and is bound by a code of ethics.

The fees of the provisional administrator will be paid by the person requesting his appointment, or by the company if the judge appoints him *ex officio*. However, if the bankruptcy of the company is declared, the fees of the provisional administrator will fall in the passive of the company.

The functions of the provisional administrator

The President of the Commercial Court will have to specify the functions of the provisional administrator. He has a discretionary power to decide such functions, and can appoint more than one administrator if needed.

As a result of such an appointment, the board of directors will be discharged from the day-to-day management of the company in favour of the provisional administrator appointed. However, this removal will not be general or related to all the goods of the company; the Court will need to determine precisely the effects and the scope of the functions of the provisional administrator in its decision and will be able, at any time, to modify its decision at the request of the provisional administrator himself.

The provisional administrator will not be able to initiate bankruptcy proceedings on behalf of the company or to represent the company in bankruptcy proceedings. This rule has been introduced in the law to ensure the independence of the appointed administrator vis-à-vis the company and the creditors. However, pursuant to article 6 of the Bankruptcy Act, the provisional administrator will be able to issue a writ of summons against the company of which the day-to-day management is entrusted to him, so that the judge declares the bankruptcy of the company.

The Bankruptcy Act prioritises the effect of commercial acts that have been undertaken by the company without taking into account the provisional discharge of the Board and the appointment of a provisional administrator. They will be ineffective against the creditors of the company if such creditors had known of the existence of an administrator's appointment or if the acts fall within the scope of article 17 of the Bankruptcy Act, namely:

- all acts of disposal to movable or immovable properties, if the value of that given by the bankrupt company significantly exceeds the value of what it received in return;
- all payments either in cash or by transfer, sale, compensation or otherwise, for debts not due and overdue debts, and all payments other than cash or negotiable instruments; and

- all conventional mortgages and all pledges made on the debtor's assets for debts previously contracted.

The sanction of unenforceability of the acts will only be requested by the provisional administrator or the trustee of the bankruptcy if those acts have prejudiced the creditors of the company.

The end of the mission

The decision to appoint an administrator is a provisional measure. It is generally only decided if the President of the Commercial Court is convinced of the future bankruptcy of the company. It is interesting to note that, in Belgium, the Courts are reluctant to proceed to make such appointments because of the serious nature of the measure and the interference that it brings to the life of the company.

The provisional status of an administrator's appointment is reinforced by a double set of terms:

- a petition for bankruptcy must be introduced within fifteen days after the order nominating the provisional administrator has been made. If the procedure for the appointment of a provisional administrator has been started by unilateral petition from a person having an interest in such appointment, it is the same person who must introduce the proceedings aiming for the bankruptcy of the company. Otherwise, i.e. when the appointment has been decided by

the Court *ex officio*, the provisional administrator will need to initiate the bankruptcy proceedings against the company. He will then be considered as acting in the interests of the creditors of the company; and

- secondly, a judgment recognising the bankruptcy of the company must be handed down within four months of the petition for bankruptcy. This enables the judge to confirm that a bankruptcy has effectively occurred. This term can be extended by the Court.

Where the two above conditions are met, the mission of the provisional administrator will be terminated. If the bankruptcy of the company is announced, a trustee will be appointed to organise the bankruptcy and the distribution of the company's assets between the creditors of the company.

The publication of the appointment

Given the gravity of the measure, an order of the President of the Commercial Court appointing a provisional administrator will not be published in the Belgian Official Journal. This rule has been enacted to avoid any negative effect for the company.

Effectively, it might be possible that, following a deeper examination of the situation of the company, the bankruptcy of the company can be avoided. In these circumstances, the publication of a previous appointment of a provisional administrator would have severe effects

on the future of the company. In particular, the confidence of clients of the company would suffer, as they would have been erroneously led to believe that the situation of the company was critical.

/
Olivia de Patoul
 CMS DeBacker, Brussels
 E olivia.depatoul@cms-db.com

RECENT INSOLVENCY LAW DEVELOPMENTS IN THE CZECH REPUBLIC

Insolvency Act Amendment

Following a decision of the Czech Constitutional Court, the Insolvency Act has recently undergone further change since its introduction in 2008. A former regulation in the previous Bankruptcy Act which was valid until 2008, enabled creditors along with debtors and the insolvency administrator to deny the claims filed by other creditors. However, the new Insolvency Act reserves this valuable defensive tool in insolvency proceedings exclusively for the debtor and the insolvency administrator. The Constitutional Court stated that such provision restricted, or even nullified, the ability of creditors to seek protection of their rights before a court or other independent authority. As a result, an amendment to the Insolvency Act came into effect on 31 March 2011. It is again the creditors who file claims in the insolvency proceedings that have a right to question other creditors claims.

Czech case law development

Czech insolvency law is currently facing its biggest review for years. It is fortunate that the above amendment to the Insolvency Act became effective after the biggest insolvency case was initiated, and thus does not apply to those proceedings. Otherwise numerous creditors of the indebted company could have exercised this right and the rules might have caused an undesirable prolongation of the insolvency proceedings.

The debtor is a joint-stock company and is the biggest player in the betting industry in the Czech Republic, operating the most popular betting games. There is no comparable lottery or betting company of this size in the Czech Republic. Although the company was founded in 1992 as a joint-stock company, its lottery and betting business operated under the same business name by its legal predecessors from as early as 1956. In the communist period it was a monopoly, running a live and the most popular TV ballot. The company is, therefore, regarded as “national heritage” by some people, and its unique market position still exists today. Additionally, since the company’s profits are deemed to be used to foster sport and sports education, Czech sport is very much dependent on the company.

However, this long and well established company found itself in a deep crisis and has become the subject of insolvency proceedings. The insolvency proceedings against it were initiated in January 2011 by one of its biggest private creditors. The initiation of the insolvency proceedings was followed by the court’s announcement of the insolvency of the company in March this year. The number of creditors that have registered their claims with the relevant court so far exceeds 2,000, and the debt reaches an amount of over 41 billion Czech crowns (over EUR 1.6 billion). The company’s problems arose through the financing of a large construction project; the O₂ Arena in the Prague quarter called Vysočany that has

been hosting concerts of world famous stars and entertainment events, including the ice-hockey world championship in 2004. Despite its successful business performance over the last few decades, the company failed to pay off its debts in time.

Judging by the amount and value of receivables owed by the company, its largest creditors, and therefore the most significant ones when it comes to decision-making among creditors, are two financial groups. Both these entities have already expressed their interest in keeping the company going and even a readiness to eventually help the company by means of a *direct investment*.

The course of proceedings

In the last days of May, the first two day creditors meeting was held and it brought unusual results. Namely, the acknowledged creditors, as participants of the meeting, made a decision on how to deal with the company's insolvency. After having ruled out the possibility of restructuring, they voted for the bankruptcy option by the required majority. This scenario is considered rather unconventional and might be viewed as a clear sign of interest in resolving matters without undue delay, or even expediting the process. As each of the biggest creditors wanted to restructure the company in a different way, and a restructuring might have brought lengthy disputes, the creditors decided on solving the insolvency through bankruptcy.

The Czech Insolvency Act gives the insolvency court a deadline of three months following the decision of insolvency to decide on the manner of solving the insolvency. Usually, at the first session, the creditors' meeting confirms the position of the insolvency administrator and creates a creditors' committee representing the creditors. It is, therefore, regarded as very unusual that the company's creditors' meeting did not limit itself to the commonly performed actions. On the contrary, it went as far as deciding on bankruptcy. No wonder the creditors were in a rush; a well recognised large financial group is to enter the betting market in the Czech Republic in the very near future and seems to be a quality competitor for the company.

On Monday 30 May, the court confirmed the creditors' choice and officially announced the bankruptcy of the company. The court's resolution has already become effective, as this happens immediately upon its publication in the electronically maintained Insolvency Register. One of the most important consequences of this course of action is the fact that the existing statutory body of the company is no longer entitled to act on its behalf as there is an automatic transfer of powers to the insolvency administrator.

Uncertain future

As of today, the company still operates its business. However, it remains unclear whether the company's activities in the

betting market will cease to continue or not. The main goal of the bankruptcy is to satisfy the claims of the creditors by selling the assets of the debtor. The Czech finance ministry declared that pending insolvency proceedings as such do not constitute a legitimate reason for the company's hazard-games-provider licence to be withdrawn; the insolvency administrator may thus leave the company in the game and able to continue in the betting business. The planned entrance of a new competitor puts pressure on the company to keep improving its business activities in order to maintain its unique market position.

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Ivana Fára

CMS Cameron McKenna v.o.s., Prague

E ivana.fara@cms-cmck.com

/

Lucián Staněk

CMS Cameron McKenna v.o.s., Prague

E lucian.stanek@cms-cmck.com

ACTION TO SET ASIDE TRANSACTIONS AGAINST EU COMPANIES BEFORE THE GERMAN COURTS

There has been a steady increase in the number of cross-border insolvency proceedings owing to increasing economic ties. Decisions on European insolvency law so far have principally been concerned with the issue of applicable law and thus with determining the centre of main interest ("**COMI**"). However, recently there have been an increasing number of legal issues relating to annex disputes. It was clarified last year for German insolvency law that the insolvency administrator can file claims in Germany against companies which have their registered seat in other Member States. The key decision in this respect is the decision of the European Court of Justice (the "**ECJ**") in the matter *Deko Marty Belgium* (decision of 12.02.2009 Rs C-339/07), which turned the previous requirements of German civil procedure law upside down.

Background

The ECJ had to decide whether the insolvency administrator of the assets of a German GmbH was entitled to file a claim in Germany against a company with its registered seat abroad on the grounds of contesting insolvency proceedings.

The insolvency debtor had transferred a sum of EUR 50,000.00 to Deko Marty Belgium N.V., a company with its registered seat in Belgium, only one day before filing for insolvency. Under German law, payments which are made shortly before an application for insolvency is filed and which have an adverse effect on the

creditors are frequently subject to an action to set the transaction aside. In such cases the insolvency administrator is entitled to demand return of the corresponding payments. As Deko Marty Belgium N.V. was unwilling to return the payments the insolvency administrator filed a claim with the Regional Court of Marburg, the district in which the insolvency proceedings had been commenced.

Decisions of the German courts

Both the Regional Court of Marburg and the Higher Regional Court of Frankfurt am Main dismissed the claim as not permissible owing to their lack of international competence. The reason behind these decisions is that in accordance with the provisions of Council Regulation (EC) No 44/2001 a claim may be filed in a Member State against a company with its registered seat in another Member State only in exceptional cases. As a rule, claims must be filed against the companies in their own country. However, neither Council Regulation (EC) No 44/2001 nor the national provisions governing German civil procedure law provided for such an exception. Therefore, a claim would have had to have been filed against Deko Marty Belgium N.V. at its registered seat in Belgium.

The Federal Court of Justice submitted the issues to the ECJ for a preliminary decision pursuant to Art. 267 TFEU (ex-Art. 234 EC Treaty).

ECJ – claim at the centre of main interest admissible

Instead of applying the Council Regulation (EC) No 44/2001, the ECJ decided to apply Council Regulation (EC) No 1346/2000 on insolvency proceedings. This Regulation regulates which Member State insolvency proceedings are to be opened in and subject to which provisions insolvency proceedings are to be carried out in the case of cross-border matters. Pursuant to Art. 3 (1) of Council Regulation (EC) No 1346/2000 on insolvency proceedings, the court which is responsible for the commencement of insolvency proceedings is the court where the insolvency debtor has its centre of main interest. In the *Deko Marty Belgium* case the ECJ held that Art. 3 (1) of the Council Regulation (EC) No 1346/2000 on insolvency proceedings must be interpreted as meaning that the courts of the Member State within the territory of which insolvency proceedings have been opened have jurisdiction to decide an action to set a transaction aside, by virtue of insolvency that is brought against a person whose registered office is in another Member State. It is the view of the ECJ that this interpretation follows from the practical effectiveness of Regulation 1346/2000/EG (*effet utile*), and the intention of the legislator to make the regulation cover all judgements which are delivered directly on the basis of insolvency proceedings and are closely connected with such proceedings.

Problem – no German jurisdiction

The consequence of this decision is that whenever the Council Regulation (EC) No 1346/2000 on insolvency proceedings is applicable, the insolvency administrator must have a national place of jurisdiction for claims against companies with their registered seat abroad if the claim is delivered directly on the basis of the insolvency proceedings and is closely connected with such proceedings.

However, in the *Deko Marty Belgium* case there was no such national place of jurisdiction provided for actions to set transactions aside under German law. German civil procedural law does not recognise a separate place of jurisdiction for claims of the insolvency administrator in connection with insolvency proceedings. Therefore, claims against former contractual partners are as a matter of principle to be filed at the registered seat of the defendant company abroad. The Federal Court of Justice was faced, therefore, with the problem that under case law of the ECJ, German courts were responsible internationally but the national provisions did not provide for any place of jurisdiction.

Decision of the Federal Court of Justice

The Federal Court of Justice solved the problem by granting the insolvency administrator its own place of jurisdiction at the place of the court responsible

for the commencement of insolvency proceedings. The Federal Court of Justice held that prior ranking European law may not be disregarded in a way that national law does simply not regulate the required local jurisdiction.

Conclusion

Companies with their registered seat in a Member State of the European Union which have a business relationship with German companies must in future expect, more frequently, that insolvency administrators will file claims against them in Germany in the event of an insolvency of the contractual partner. Practice shows that German insolvency administrators are increasingly making use of this option.

/
Dr Alexandra Schluck-Amend
CMS Hasche Sigle, Stuttgart
E alexandra.schluck-amend@cms-hs.com
/
Dr Steffen Liebendörfer
CMS Hasche Sigle, Stuttgart
E steffen.liebendoerfer@cms-hs.com

HOW PENDING CLAIMS ARE RECOGNISED IN HUNGARIAN INSOLVENCY PROCEEDINGS

Notwithstanding that beneficiaries of pending claims have been considered creditors since the amendment of the term “creditor” in September 2009, neither the jurisprudence nor practice could work out a clear interpretation of “pending claims”.

The term “creditor” is defined as follows: “[...] After the starting date of liquidation all persons having any claims, whether in money or in kind expressed in monetary terms, against a debtor (including pending claims arising from bank guarantees, insurance guarantees or from commitments issued by an insurance company containing surety facilities, if the timing of their payment and maturity is uncertain) that have been registered by the liquidator, shall be deemed creditors” (Act XLIX of 1991 on Bankruptcy Proceedings and Liquidation Proceedings (the “**Bankruptcy Act**”) 3 section (1) c).

This demonstrates that the Bankruptcy Act recognises pending claims as creditors’ claims only in liquidation proceedings (where the aim is to wind-up the debtor without legal successor and distribute its assets amongst creditors), as opposed to bankruptcy proceedings (where the aim is reorganisation of the debtor). However, in bankruptcy proceedings such claims could grant, for example, voting rights to their beneficiaries in the bankruptcy negotiations. The official interpretation of the Bankruptcy Act has not provided reasons as to why pending claims should be handled differently in the two types of insolvency proceedings.

Notwithstanding the above, a beneficiary of a pending claim may qualify as a creditor in bankruptcy proceedings if the debtor acknowledges, or at least does not dispute, these pending claims.

The scope of such ‘pending claims’ is not clear. On one hand, some of the above listed categories (for example, insurance guarantees and insurance suretyship obligations) are not yet known under Hungarian law. On the other hand, Hungarian restructuring and insolvency experts seem to be divided into two groups when discussing which claims are included in the definition of pending claims. One group takes the approach that the term pending claims under the Bankruptcy Act is complete, i.e. only bank guarantees, insurance guarantees and insurance suretyship obligations may be regarded as pending claims. The other group (as the majority) is of the view that the term is not complete, and argue that pending claims should also cover suretyships (regardless of whether they are banks or insurance companies).

On the basis of the recent non-final decisions of Hungarian courts, the above majority approach seems to be confirmed. If this view was or should be followed, it would raise the question as to whether or not third party security providers could be considered beneficiaries of pending claims (i.e. as a result of the exercise of their right of subrogation). In this respect insolvency experts are divided, however most of the judges (in their non-official

statements) seem to be reluctant to accept an approach which would consider third party security providers as creditors of pending claims.

Given the above uncertainty surrounding the regulation of pending claims, the Bankruptcy Act will need to be amended to provide necessary clarification.

/ **Erika Papp**
CMS Cameron McKenna LLP, Budapest
E erika.papp@cms-cmck.com

/ **Szabina Soptei**
CMS Cameron McKenna LLP, Budapest
E szabina.soptei@cms-cmck.com

/ **Kitti Tulner**
CMS Cameron McKenna LLP, Budapest
E kitti.tulner@cms-cmck.com

EXEMPTION OF BANKRUPTCY CRIME IN INSOLVENCY PROCEEDINGS

During the last few months, Italian banks have been more willing to grant facilities to companies in distress when the company has pursued alternative procedures to bankruptcy ("*fallimento*").

This trend has superseded the previous reluctance of the banks, which was justified by the risk of their officers being held jointly liable with entrepreneurs and companies for bankruptcy ("*bancarotta*") crimes in the case of a negative outcome of the alternative procedures.

Previously, in light of the risks mentioned above, banks were reluctant to lend funds to distressed companies, and consequently companies in distress were facing further difficulties in obtaining validation of recovery plans (which are alternative to bankruptcy ("*fallimento*")) from the competent courts which would allow the companies to keep their businesses running.

The recent change may have been motivated on the basis of Italian law no. 122 of 30 July 2010, which introduced into the Italian Insolvency Law (Royal Decree no. 267 of 1942), a specific exemption (namely Article 217 bis) from reckless and fraudulent bankruptcy ("*bancarotta semplice*" and "*bancarotta fraudolenta*") for companies and entrepreneurs (and any other third party involved) which made payments and acted in accordance with composition with creditors procedures ("*concordato preventivo*"), restructuring agreements ("*accordi di ristrutturazione*") or recovery plans ("*piani di risanamento*"), under, respectively, Articles 160, 182-bis and 67, paragraph 3, letter d), of the Italian Insolvency Law.

Article 216 of Italian Insolvency Law ("*bancarotta fraudolenta*") establishes that an entrepreneur who has been declared bankrupt ("*fallito*") may be sentenced

to up to five years' imprisonment if the entrepreneur made payments or concealed the privileged nature of his credit, to the detriment of his creditors, before or in the course of the bankruptcy procedure ("*procedura fallimentare*").

Article 217 provides for a softened case of *bancarotta*, namely reckless bankruptcy. According to this article, the entrepreneur who has been declared bankrupt may be sentenced to up to one year's imprisonment if the entrepreneur:

- faced expenses which appear exaggerated in relation to his economic status;
- dissipated a considerable fraction of his assets in unnecessary or risky transactions;
- carried out risky transactions aimed at postponing his bankruptcy;
- worsened his distress by abstaining from filing a bankruptcy petition; and/or
- failed to fulfil the obligations agreed upon in the course of previous agreements with creditors.

Reckless bankruptcy may also be declared where an entrepreneur did not properly keep the accounting books during the period not exceeding three years before his declaration of bankruptcy ("*fallimento*").

It is worth mentioning that banks and their directors can also be sentenced on the basis of the above mentioned provisions, if they contributed to the delay of the declaration of bankruptcy of the distressed company by providing further credit facilities to the distressed company.

Article 217-bis narrows the range of cases in which companies and entrepreneurs

can be sentenced for *bancarotta* crimes and, therefore, reduces the related risks for the banks which have granted loans to debtors in distress, provided that the loan is in line with the alternative restructuring procedures.

The above is confirmed by the fact that the introduction of Article 217-bis was carried out in the course of a wider amendment to Italian Insolvency law, aimed at financial stabilisation and economic competitiveness, by the fostering of the choice of procedures which are alternatives to bankruptcy ("*fallimento*") for companies and entrepreneurs in distress.

Through the choice of alternative procedures, entrepreneurs and companies are entitled to restructure their indebtedness and at the same time keep their businesses running, and in so doing can ensure the continuing employment of their workforce. Conversely, the declaration of bankruptcy ("*fallimento*"), which is a requirement in order for entrepreneurs and companies to be found to have committed reckless and fraudulent bankruptcy, hinders the possible continuation of the business.

As a result, banks (which typically are the main creditors of companies) are likely to be more interested in supporting companies which are facing distress in accessing alternative procedures to bankruptcy without facing the risk of being found jointly liable for any possible *bancarotta* crime.

/ **Paolo Bonolis**
CMS Adonnino Ascoli & Cavasola Scamoni, Roma
E paolo.bonolis@cms-aacs.com

/ **Gianfabio Florio**
CMS Adonnino Ascoli & Cavasola Scamoni, Roma
E gianfabio.florio@cms-aacs.com

THE APPLICATION OF THE EUROPEAN INSOLVENCY REGULATION BY THE DUTCH COURTS

The European Insolvency Regulation (Council (EC) Regulation 1346/2000) (the **"Regulation"**) has been in force since 31 May 2002. It regulates the jurisdiction of the courts, the applicable law and the recognition of insolvency procedures. The Regulation is binding in all its aspects and is directly applicable in each Member State. This article discusses a number of recent Dutch judgments in which the Dutch courts have applied the Regulation on their own initiative or on request.

The first judgment concerned the insolvency of a German franchisee of the Subway Restaurants chain. This franchisee had sold the inventory of the restaurant concerned. The purchaser did not pay the purchase price to the franchisee but instead paid it to Subway International BV, a Dutch company. Following that sale, the bankruptcy of the franchisee was ordered in Germany. The bankruptcy trustee in Germany claimed before the Dutch court, repayment of the purchase price received by Subway International BV (Amsterdam District Court, 17 February 2010, *JOR* 2011/155).

The question in this case was whether the Dutch court had jurisdiction to decide the case. The answer to this question was in the Regulation. The European Court of Justice found in a judgment that article 3(1) of the Regulation had to be construed in such a manner that the judicial authorities of the Member State in whose territory the insolvency proceedings had been opened, were competent to give judgment on the application to set aside a fraudulent

preference against a defendant who had its registered office in a different Member State (Court of Justice of the European Communities, 12 February 2009, C-229/07).

Accordingly, the German judicial authorities were held to be the competent authorities to hear the claim as the insolvency proceedings had been opened in Germany. The Dutch court applied the Regulation on its own initiative and found that it did not have the jurisdiction to rule on the substance of the case.

The Court referred in its judgment to a couple of provisions found in the preamble of the Regulation. It is stated in the preamble, among other things, that the objective of the coordination of all the pending concurring proceedings with regard to the insolvency of a company, is for the efficient and effective realisation of insolvency proceedings with cross-border effects. It is, furthermore, important that parties do not transfer their disputes from one Member State to the other in order to obtain a more favourable legal position. It should also be noted, however, that in the context of the principle of proportionality, the Regulation should only be confined to provisions governing jurisdiction for opening insolvency proceedings, and judgments which are delivered directly on the basis of the insolvency proceedings and are closely connected with such proceedings.

We also refer to a judgment of the European Court of Justice regarding

a request for a preliminary ruling submitted by a Polish court. A distinction is made in the Regulation between the main and secondary insolvency proceedings. The main proceedings will be opened before the court of the Member State in which the debtor has its centre of main interests. These proceedings have universal scope. This means that the proceedings will also extend to the assets situated in other Member States. Furthermore, it is also possible that a court of a Member State in which the debtor has an established office will open secondary insolvency proceedings. On the request for a preliminary ruling, the European Court of Justice found that the laws of the Member State in which these proceedings have been opened govern both the main proceedings and the secondary proceedings. This is called the 'lex concursus' (Court of Justice of the European Communities, 21 January 2010, *RvdW* 2010/371).

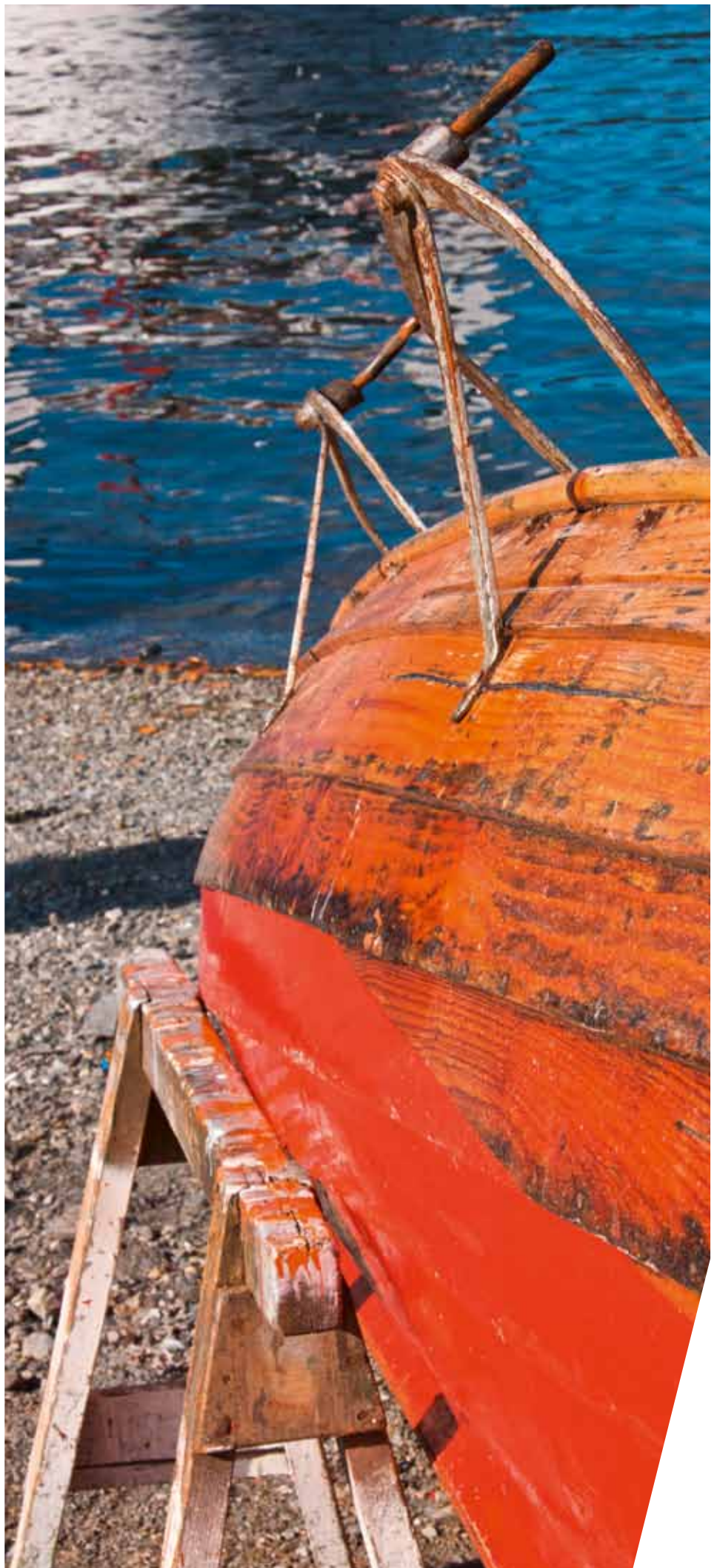
The European Court of Justice concluded that the competent authorities of a Member State in which no secondary insolvency proceedings had been opened had the obligation to recognise and execute all the decisions with regard to the main insolvency proceedings opened in a different Member State, save for the following grounds of refusal:

- (i) if the recognition results in a restriction of the personal freedom or the privacy of correspondence; or

- (ii) that the recognition violates public order (J.P.D. van de Klift, *Uitleg van bepalingen van de Insolventieverordening* (Explanation on the provisions of the Insolvency Regulation), BB 2011/24).

In a previous judgment, the Supreme Court of the Netherlands did indeed depart from the *lex concursus* as explained above. It was found in that judgment that the pending legal proceedings were excluded from the operation of the *lex concursus*. The consequences of insolvency proceedings subject to pending legal proceedings will be governed by the laws of the Member State in which the legal proceedings have been brought before the court; this is called the '*lex fori processus*' (The (Netherlands) Supreme Court 11 December 2009, *NJ* (Dutch Law Reports) 201/4). Therefore, it appears that there are exceptions to the main rule (J.P.D. van de Klift, *Uitleg van bepalingen van de Insolventieverordening* (Explanation on the provisions of the Insolvency Regulation), BB 2011/24). However, one has to be conscious of the fact that the Dutch court will apply the Regulation on its own initiative.

/
Jan Willem Bouman
CMS Derks Star Busmann, Utrecht
E janwillem.bouman@cms-dsb.com



CLOSE-OUT NETTING IN INSOLVENCY MADE SIMPLER IN POLAND

The Polish parliament has recently enacted amendments to the Polish Insolvency Law, providing long-awaited solutions to several issues that have impacted on the attractiveness of entering into master agreements for derivative transactions with Polish clients. In particular, the amended Insolvency Law will now allow for the close-out netting of collateral arrangements in the counterparty's insolvency. Following the President's signature and publication in the Journal of Laws, the amendments will come into force after a 14-day *vacatio legis*.

The current close-out netting regime in the Polish Insolvency Law has been in force since 2003. It prevents the receiver from "cherry picking" transactions entered into under a master agreement, introducing an exception to the general rules governing set-off in insolvency, and excluding the claims under derivative and repo transactions against an insolvent counterparty from the composition in the case of composition insolvency proceedings.

However, the current regulations have certain flaws, arguably the most significant of which is that they do not allow for the inclusion of claims under collateral arrangements in the close-out netting of transactions following the declaration of a Polish counterparty's insolvency. Such netting is currently only allowed in so-called reorganisation proceedings. Moreover, the effectiveness in insolvency of collateral in the form of a security transfer of ownership is dependent upon such transfer being effected on the basis of

an agreement signed with its date certified by a notary, which makes the giving of such collateral under agreements, such as the ISDA Credit Support Annex, often impractical.

The new regulations address those issues by explicitly stating that close-out netting of claims under collateral arrangements is possible in insolvency, and that the requirement for such collateral to be given each time on the basis of an agreement with the date certified by a notary shall not apply. These changes will bring Polish legislation in line with the provisions of Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements, which require that a financial collateral arrangement takes effect in accordance with its terms, notwithstanding the commencement or continuation of winding-up proceedings or reorganisation measures in respect of the collateral provider or collateral taker, and that the creation, validity, perfection, enforceability or admissibility in evidence of a financial collateral arrangement or the provision of financial collateral under a financial collateral arrangement should not be dependent on the performance of any formal act.

Another important change to the Polish Insolvency Law introduced by the recently enacted regulations is the extension of the scope of the insolvency close-out netting regime to repo transactions in all types of financial instruments, and to financial instruments lending transactions. The current regime only applies to so-called

"financial term operations" (i.e. generally, derivatives) and to repo transactions in securities only (securities being a much narrower category than financial instruments). Financial instruments lending does not seem to fall under either of those categories. The proposed changes to the regulations are aimed at increasing the attractiveness of entering into financial instruments lending and repo transactions with Polish counterparties, and are a reflection of a wider tendency in many European jurisdictions to extend the scope of application of close-out netting regimes to a growing number of types of financial instruments.

/

Konrad Werner

*CMS Cameron McKenna Dariusz Greszta
Spółka Komandytowa, Warsaw
E konrad.werner@cms-cmck.com*

LIABILITY OF THE BOARD OF AN INSOLVENT COMPANY

In the current economic climate, insolvency is an ever present concern for a company. The purpose of this article is to raise the awareness of the liability faced by the board of the insolvent company. Insolvency not only means that the debtor company must pay its creditors with its patrimony (the sum of its assets and liabilities) but also that, in some cases, the members of the board of the debtor company may be held personally liable.

Legal framework

Under article 138 of the Law no 85/2006 (the **"Romanian Insolvency Law"**), the members of the board of the insolvent company can be held personally liable for losses caused by his / her decisions, actions or omissions, and can be obliged, by a syndic-judge's decision, to account to the company for those losses.

Individuals who are members of the board of directors or the supervisory body of the insolvent company (including the associates, directors, etc), and any other person/persons may be held personally liable if they are found to have caused the company's insolvency by:

- using the assets or debts of the company for their own (or another person's) personal benefit;
- carrying out trading activities, for their personal benefit, under the company's cover;
- causing the company to carry on an activity from which they benefit where

such activity is, clearly, not in the interests of the company or causes the insolvency of the company;

- preparing and keeping fictitious accounts, concealing accounting documentation, or failing to prepare and maintain the company's accounts in accordance with the law;
- embezzling or hiding part of the active business of the company or fictitiously increasing its liabilities;
- obtaining finance to delay the insolvency of the company by using means that lead (or have led) to the ruin of the company; or
- during the month prior to the company's filing for insolvency, having the company make a payment to any of the company's creditors in preference to any of the others.

A claim can be brought against such person (or persons) within 3 years of a claimant finding out about such person's involvement in the insolvency of the company, but not more than 2 years from the date the company filed for insolvency. Such a claim can be brought against one or more members of the insolvent company's board by:

- the judicial administrator or liquidator, after drafting a report explaining the alleged link between the board members' actions (as listed above) and the company's insolvency; or

- the creditors' committee, if the judicial administrator or liquidator omitted to file a claim, and the claim is close to the statutory limitation period, or if the judicial administrator or liquidator didn't indicate in his report the person(s) culpable for the company's insolvency.

If more than one person or board member of the company is found responsible for the company's insolvency, their liability is joint, with the condition that the insolvency of the company happened after or contemporaneously with the period within which they exercised their authority within the company.

The best defence available to any board member is to show that he was not in favour of the company carrying out the action(s) which, eventually, caused the company's insolvency. Alternatively the individual can show that, if he was absent when the decision(s) causing the insolvency was taken, the individual later recorded his opposition to such a decision.

The judicial administrator, liquidator, or the creditors' committee is able to request that the syndic-judge place a restriction on the distribution of the patrimony of the individual(s) who are found personally liable.

Practical timing difficulties – case law

The Romanian Insolvency Law establishes a concrete timeframe for the insolvency procedure to run, including any claims filed by the judicial administrator/liquidator or

the creditors' committee. Despite this, in practice, due to the complexity of each claim, the time actually taken to complete the procedure often varies from that set by statute. This frequently results in procedural difficulties in applying the law since different statutes apply to insolvency proceedings and individual liability proceedings.

This was illustrated in a recent case where the insolvency procedure was closed before enforcing a court decision holding the company's director/executives personally liable, which caused confusion regarding the applicable law (Romanian Insolvency Law or Civil Procedure Code).

The confusion was caused by the apparent contradiction of the following legal provisions:

- article 133 of the Romanian Insolvency Law provides that the insolvency procedure (bankruptcy) can be closed only after the complete liquidation of the company's assets; after the distribution of all funds or assets in the debtor company's patrimony; and after depositing any remaining non-claimed funds into a bank account at the disposal of the company's shareholders or partners; and
- article 142 of the Romanian Insolvency Law provides that the forced enforcement over the patrimony of the persons held personally liable shall be performed by the enforcement officer, according to the procedure provided in the Civil Procedure Code.

It also provides that the sums recovered from the forced enforcement shall be allotted by the enforcement officer, according to the receivables definitive consolidated table provided by the judicial liquidator.

Thus, it seems that, the insolvency procedure cannot be closed before enforcement of a court decision holding the company's administrator personally liable, since the sums recovered from the enforcement should be distributed in their entirety to the creditors. Only after the distribution is complete can the procedure be closed.

In a related case (Court decision no. 3792/ December 8, 2009, rendered in file no. 4127/108/2007, before the Arad Tribunal), the syndic-judge also ruled on the closing of an insolvency procedure against the debtor company. The judge released the judicial liquidator from all duties and responsibilities regarding the procedure, the debtor company and its patrimony, the creditors, the shareholders and associates.

The creditors filed an appeal against this decision in the superior court. One claimant requested the modification of the court decision and the continuing of the insolvency procedure until the complete and effective covering of the debtor company's liabilities. The other claimant requested modification of the court decision, with the consequence of continuing the insolvency procedure until the recovery of all the receivables of the creditors against the insolvent company.

Nevertheless, the superior court dismissed both appeals as groundless and maintained the first court's decision.

The court considered that there was no contradiction between the closing of the insolvency procedure and the distribution of the sums realised from the forced enforcement of the patrimony of the person responsible for the company's insolvency. The court's reasoning was as follows:

- under article 131 of the Romanian Insolvency Law, the syndic-judge can close the insolvency procedure at any stage, if it is found that the debtor has no assets, or if the assets it possesses are insufficient to cover the administrative costs of the insolvency and no creditor offers to advance these sums;
- the reports of the judicial liquidator show that the debtor company has no activity, no cash to pay the creditors, and has no further assets capable of being converted to cash;
- keeping the insolvency procedure open would only generate more costs, which the debtor company's patrimony will not be able to cover, and for which the administrator would then be liable, if ascertained that he is insolvent or owns no enforceable assets. Moreover, these costs would not be justified since continuing the procedure would no longer be necessary;
- the claim of the judicial liquidator for holding any director personally

liable was allowed by the court of first instance and the administrator was obliged to cover the company's liabilities in a sum equal to the total value of the creditors' receivables;

- enforcement against a director who would not wilfully execute the court's decision can be performed, according to article 138 of the Romanian Insolvency law, either within the insolvency procedure, at the request of the judicial liquidator, or after the closing of the insolvency procedure at the request of the interested creditors; and
- article 142 of the Romanian Insolvency Law states that if a director or other executive fails to comply with an order willingly, enforcement shall be performed by the enforcement officer in accordance with the procedure governed by the Civil Procedure Code. The aim of the forced enforcement is to cover the insolvent company's debts with the sums resulted from and transferring these to the enforcement officer, who should allot the sums accordingly to the receivables definitive consolidated table handed to him by the liquidator.

Based on these arguments, the superior court ruled that there was no legal impediment to commence enforcement and to allot the sums received from it after the closing of the insolvency procedure. As the enforcement procedure must be performed by the enforcement officer and as the allotting functions of the liquidator

are transferred, in this case, to the enforcement officer, he would act based on the definitive receivables table drawn up by the liquidator and acknowledged by the court.

Conclusions

The Romanian insolvency procedure is complex and comprises a multitude of inter-related legal procedures, each with its own conditions and timings. Its complexity sometimes generates situations which can create difficulties in determining which legal provisions apply to the case at hand. In such cases, precedents take a crucial role.

Even though the Romanian legal system does not recognise precedents as a source of law, they are considered to be useful practical guidelines, which is why both lawyers and magistrates consult them.

/ **Sergiu Mihailescu**
CMS Cameron McKenna SCA, Bucharest
E sergiu.mihailescu@cms-cmck.com

/ **Alexandra Weisman**
CMS Cameron McKenna SCA, Bucharest
E alexandra.weisman@cms-cmck.com

/ **Ahmad Khokher**
CMS Cameron McKenna SCA, Bucharest
E ahmad.khokher@cms-cmck.com



INTRODUCTION OF A MORATORIUM IN INSOLVENCY PROCEDURES NO LONGER SUSPENDS SECURITY ENFORCEMENT

On 09 March 2011, amendments to the Law of Ukraine “On Execution Service” came into effect and a new regulation concerning the suspension of enforcement proceedings was introduced. Pursuant to part 1 paragraph 8 article 37 of the amended legislation, the initiation of insolvency proceedings against a debtor by creditors, or by the debtor company itself, which involve a court-ordered moratorium on satisfaction of creditors’ claims, will no longer suspend the enforcement of pledges and/or mortgages granted by the debtor.

Under the previous law, banks and other creditors whose claims were secured by a pledge or mortgage were unable to enforce their security from the moment of imposition of a moratorium until the debtor company went into insolvent liquidation, and so, in many cases, had to wait between two and two and a half years before being able to enforce their security. Their alternative was to agree an amicable settlement or financial rehabilitation proceedings with respect to the debtor.

These recent amendments to the legislation mean that from now on, debtors will not be able to prevent security enforcement by delaying insolvency proceedings. Therefore, such amendments are likely to have a positive impact on the financial sector in the Ukraine.

/ **Taras Burhan**
CMS Cameron McKenna LLC, Kyiv
E taras.burhan@cms-cmck.com

CASE ROUND-UP

Each of the cases set out below deal with the application and interpretation of the EC Regulation on Insolvency Proceedings (Council Regulation (EC) No 1346/2000) (the “**EC Regulation**”) by the English courts. We have set out the facts and decision in each case, however, by way of summary we have identified the central principle of each case below:

- **Rodenstock GmbH:** neither the EC Regulation nor the Council Regulation (EC) No 44/2001 (the “**Judgments Regulation**”) have narrowed the scope of the meaning of “liable to be wound up” for the purposes of the Insolvency Act 1986 and, therefore, do not impact restrictively on the scope of the English court to sanction a scheme of arrangement in respect of a foreign registered company. A scheme of arrangement is a court-driven procedure which can be used for a number of purposes including the reorganisation of a company’s debts.
- **Eurodis Electron plc (in administration) and others:** notwithstanding that a Belgian winding up order over the company should not have been made, the judge stated that he did not have the power to determine that an order of a court of another country was invalid.

In the matter of Rodenstock GmbH [2011] EWHC 1104 (CH)

Summary

This case relates to the impact of the EC Regulation and the Judgments Regulation

(the “**Regulations**”) on the English courts’ jurisdiction to sanction schemes of arrangement over foreign companies.

Facts

The applicant company, Rodenstock GmbH (“**Rodenstock**”), was incorporated and had its COMI in Germany. Rodenstock had no establishment or assets in the UK, but the senior facilities agreement was governed by English law and contained an exclusive jurisdiction clause. In addition, the majority of senior lenders were based in the UK. A scheme of arrangement was proposed to bind the senior lenders to a variation of their rights under the senior facilities agreement. The aim of the scheme was to implement a restructuring in order to avoid having to place the company into an insolvency process. The scheme was passed by a large majority of the lenders, but dissenting creditors questioned the jurisdiction of the English court to sanction the scheme.

The Decision

Under English law, an English court has jurisdiction to sanction a scheme in relation to a company which is “liable to be wound up” under the Insolvency Act 1986. This would include a foreign registered company, provided that the foreign company met certain criteria (for example, that it had a sufficiently close connection with England).

The question to be answered by the Court in this case was whether either of the Regulations restricted the English courts’ jurisdiction to sanction a scheme

over a foreign registered company. The EC Regulation provides that the English courts only have jurisdiction to wind up an insolvent company with its COMI in an EU member state if that company has an establishment in the UK, and the Judgments Regulation provides that winding up proceedings must take place in relation to a solvent company in the jurisdiction of incorporation of that company.

It was held that even though Rodenstock did not meet the requisite criteria to be wound up by the English courts pursuant to either of the Regulations (i.e. it did not have its registered office, an establishment or its COMI in the UK), the English court did have the authority to sanction the scheme. This was because neither of the Regulations restricted the meaning of “liable to be wound up” and the Court held that Rodenstock was liable to be wound up under the Insolvency Act 1986. The court further held that the Regulations did not attempt to restrict the English courts’ traditional jurisdiction over such schemes. As such, and on the basis that the choice of English jurisdiction in the senior facilities agreement amounted to a sufficient connection with the English jurisdiction, the scheme was sanctioned.

In the matter of Eurodis Electron plc (in administration) and Others [2011] EWHC 1025 (CH)

Summary

This case relates to the validity of a winding up order made by the Belgian courts in contradiction with the EC Regulation.

Facts

The applicants were the administrators of Eurodis Texim Electronics (**“Eurodis”**), a Belgian incorporated company that was put into administration in the UK. As Eurodis had its COMI in the UK, the administration formed the main insolvency proceeding for the purposes of the EC Regulation. The administration order should, therefore, have prevented the instigation of any other proceedings, or if any other proceedings were instigated they should have been secondary proceedings pursuant to Article 3 of the EC Regulation. Despite this, a winding up petition was lodged in Belgium, which was not expressed to be secondary proceedings. The Belgian court was not made aware of the UK proceedings and made an order to dissolve Eurodis. The administrators were not given notice of the Belgian winding up order and did not, therefore, take steps to challenge the order within the requisite time limit. As a result, the dissolution became irreversible.

The administrators claimed that the Belgian winding up order was invalid because the Belgian court had failed to give proper effect to the primacy of the English administration proceedings and applied for a declaration that they were entitled to continue to act as administrators in England notwithstanding the ostensible liquidation of Eurodis in Belgium. Alternatively, the administrators sought a winding up order in respect of Eurodis, their appointment as liquidators and authorisation to pay the expenses and remuneration of the administration.

The Decision

The court held that a winding up order made in the Belgian court could not be invalidated by the English court despite the fact that the order should not have been made because the main insolvency proceedings, pursuant to the EC Regulation, were in the UK. The administrators were therefore no longer entitled to act over the assets of a dissolved entity. However, the judge held that the administrators were entitled to a winding up order under section 221(5) of the Insolvency Act 1986. The judge, therefore, granted the winding up order and appointed the administrators as liquidators. In addition, as a matter of fairness, the outstanding expenses of the administration were ordered to be paid as an expense of the liquidation.

/ **Andrew Jackson**
CMS Cameron McKenna LLP, London
E andrew.jackson@cms-cmck.com

/ **Kairi James**
CMS Cameron McKenna LLP, London
E kairi.james@cms-cmck.com

CONTACT DETAILS

AUSTRIA

Vienna

CMS Reich-Rohrwig Hainz
Rechtsanwälte GmbH

Günther Hanslik

T +43 1 40443 3550

F +43 1 40443 93550

E guenther.hanslik@cms-rrh.com

BELGIUM

Brussels

CMS DeBacker

Jean-François Goffin

T +32 2 74369 24

F +32 2 74369 01

E jeanfrancois.goffin@cms-db.com

BULGARIA

Sofia

Petkova & Sirleshtov Law Office
in cooperation with
CMS Cameron McKenna

Teodora Ivanova

T +359 2 92199 10

F +359 2 92199 19

E teodora.ivanova@cms-cmck.com

CROATIA

Zagreb

CMS Zagreb

Gregor Famira

T +385 1 4825 600

F +385 1 4825 601

E gregor.famira@cms-rrh.com

CZECH REPUBLIC

Prague

CMS Cameron McKenna v.o.s.

Ian Parker

T +420 2 96798 815

F +420 2 96798 000

E ian.parker@cms-cmck.com

FRANCE

Paris

CMS Bureau Francis Lefebvre

Daniel Carton

T +33 1 4738 5651

F +33 1 4738 5555

E daniel.carton@cms-bfl.com

GERMANY

Cologne

CMS Hasche Sigle

Rolf Leithaus

T +49 221 7716 234

F +49 221 7716 335

E rolf.leithaus@cms-hs.com

HUNGARY

Budapest

Ormai és Társai

CMS Cameron McKenna LLP

Erika Papp

T +36 1 48348 00

F +36 1 48348 01

E erika.papp@cms-cmck.com

ITALY

Rome

CMS Adonnino Ascoli & Cavasola Scamoni

Paolo Bonolis

T +39 06 4781 51

F +39 06 4837 55

E paolo.bonolis@cms-aacs.com

THE NETHERLANDS

Utrecht

CMS Derks Star Busmann

Jan Willem Bouman

T +31 30 2121 285

F +31 30 2121 227

E janwillem.bouman@cms-dsb.com

POLAND

Warsaw

CMS Cameron McKenna

Dariusz Greszta Spółka Komandytowa

Małgorzata Chruściak

T +48 22 520 5555

F +48 22 520 5556

E malgorzata.chrusciak@cms-cmck.com

ROMANIA

Bucharest

CMS Cameron McKenna SCA

Alina Tihan

T +40 21 4073 875

F +40 21 4073 900

E alina.tihan@cms-cmck.com

RUSSIA

Moscow

CMS, Russia

Karen Young

T +7 495 786 3080

F +7 495 786 4001

E karen.young@cmslegal.ru

SLOVAKIA

Bratislava

Ružička Csekes s.r.o.

in association with members of CMS

Ian Parker

T +421 2 5443 3490

F +421 2 3233 3443

E ian.parker@cms-cmck.com

SPAIN

Madrid

CMS Albiñana & Suárez de Lezo, S.L.P.

Juan Ignacio Fernández Aguado

T +34 91 4519 300

F +34 91 4426 070

E juanignacio.fernandez@cms-asl.com

SWITZERLAND

Zurich

CMS von Erlach Henrici Ltd

Philipp Dickenmann

T +41 44 2851 111

F +41 44 2851 122

E philipp.dickenmann@cms-veh.com

UKRAINE

Kyiv

CMS Cameron McKenna LLC

Taras Burhan

T +380 44 39133 77

F +380 44 39133 88

E taras.burhan@cms-cmck.com

UNITED KINGDOM

London

CMS Cameron McKenna LLP

Martin Brown

T +44 20 7367 3000

F +44 20 7367 2000

E martin.brown@cms-cmck.com

○ CMS offices

◁ Rio de Janeiro

◁ Buenos Aires

◁ Montevideo

Beijing ▷

Shanghai ▷



