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# Analysis

# Foreign Subsidiaries and UK Director Risks

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***Biography***

*Nick Hood is the Senior Business Adviser at the Opus Business Advisory Group (https://www.opusllp.com), the largest independent advisory, restructuring and insolvency firm in the UK.*

*Nick was a licensed Insolvency Practitioner, working in the business rescue market for 25 years. He is a committed internationalist, having created the largest global network of independent business rescue firms and having also worked overseas in Canada, Milan and Bahrain.*

*In his earlier career and after qualifying as a Chartered Accountant in 1970, Nick held senior executive positions in major companies in the construction, engineering and media sectors, as well as working for a boutique investment bank.*

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## Abstract

*UK businesses and their management are familiar with the need for risk management and regulatory compliance. If their UK companies get into financial difficulty, business rescue and insolvency procedures are transparent and there is a well-developed professional services sub-sector ready to guide owners and managers through resolving the issues and the potential personal risks they may face as a result. But as the author of this article explains, when it comes to troubled overseas subsidiaries, it can be a much more challenging environment with a minefield of unexpected hazards.*

## Introduction

The UK is a global trading nation, so there's no reason to be surprised that even quite small UK businesses might have a foreign subsidiary, or even several of them somewhere around the world. These may be little more than outposts, such as a sales operation or a retail outlet. Even when they are more substantial, the question is what happens when they get into financial difficulties and if the decision is taken not to continue to support them.

The failure of a UK company can expose dubious decision making, poor accounting records and a worse actual financial position than shown by current management


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information and even recent externally audited accounts. When the entity is in another jurisdiction, the problems often turn out to be far more serious than anticipated by the UK parent company and its Directors.

These issues may extend beyond financial shortcomings to encompass serious regulatory non-compliance. The causes may lie in a lack of corporate infrastructure such as sufficient management resource to maintain adequate internal controls and record keeping. They may stem from an over-reliance on external service providers, such as accountants or legal advisers who have not performed satisfactorily. The initial due diligence in setting up the overseas operation may have been deficient, or maybe the UK management have simply taken their eye off the international ball.

Quite apart from personal liability issues, there are likely to be unfamiliar aspects to actually getting a foreign subsidiary into the appropriate insolvency process and in any way controlling or influencing the proceedings, even if the UK parent company is the dominant creditor. Insolvency regimes around the world reflect local societal priorities and business practices, which in many cases are very different to those prevailing in the UK.

Some real-life recent examples of how some of these issues play out illustrate the potential difficulties faced by UK parent companies and their senior executives over struggling international subsidiaries.

## Issues in France

The implications of regulatory hazard for parent company executives are highlighted by the complications encountered recently in closing down the insolvent French subsidiary of a UK consumer-facing group, which is itself going through a restructuring.

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Having instructed a specialist insolvency law firm in Paris, some very unpleasant realities on the ground soon emerged. It seems that the French entity had never filed its annual accounts in Court as required by French law. It had been established in 2008, so this breach covered an extraordinary 17 years. Until this has been remedied, the company can't file for insolvency and in any case, is potentially liable for fines and penalties for the oversight. If it cannot pay these, its responsible officer is personally liable to do so and may possibly become liable for all of its other debts. In this instance, the responsible officer is the sole Director of the parent company.

From the UK Director's point of view, there was double jeopardy. If the breach wasn't rectified, the company couldn't file for insolvency, so they could face prosecution for that failure as well as the fines.

Additionally, the best solution for maximizing the realizations from the inventory in France was to move it to London. This was mooted to the French legal advisers, only to prompt rapidly raised eyebrows, a very Gallic shrug and a warning that moving assets physically out of the jurisdiction of an insolvent French company is a criminal offence, with imprisonment of the UK Director as a potential outcome.

## Problems in Germany

In another ongoing case, a consumer-facing UK business with a sales operation in Germany went into Administration at the beginning of Christmas week. The German company became insolvent as soon as the UK company went into Administration. The first local issue was a strict three-week deadline for an insolvency filing, which is always a challenge but became a major problem because of the long festive break and severe shortcomings in the local accounting records.


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Failure to file on time exposes the sole Director of the German entity, who is the UK parent company CEO, to personal penalties and potential responsibility for the German company's debts. There may also be issues for him with fines for non-compliance with payroll tax regulations for employees located in Austria and Switzerland.

The second issue in Germany is who gets appointed as the Insolvency Administrator. This a decision for the Courts there, who fiercely guard their independence on this and other aspects of their supervision of insolvency cases. Even where there is a preferred local insolvency practitioner (IP), there no certainty they will be appointed and unlike in the UK they are unable to provide any pre-appointment advice or do the initial insolvency filing, because that would be deemed to trigger a conflict of interest. This means instructing another firm of lawyers as initial advisers and to do the Court filing and then hoping an acceptable IP is appointed.

## In summary: the lessons to be learnt

In every instance, local insolvency regimes and executive risk factors are different to the UK and as between each other. As well as the laws themselves, their practical application can have unexpected consequences depending on the circumstances, both in terms of implementing an exit strategy and the implications for the UK Directors involved.

The outcome of this shouldn't be undue apprehension about overseas issues, but to approach solving them with an open mind and to use good quality local advisors, both when setting up international operations and if things go wrong. What is essential is staying on top of compliance by subsidiaries abroad.