EUROPEAN CORPORATE INSOLVENCY LAW

Development, Harmonisation and Reform

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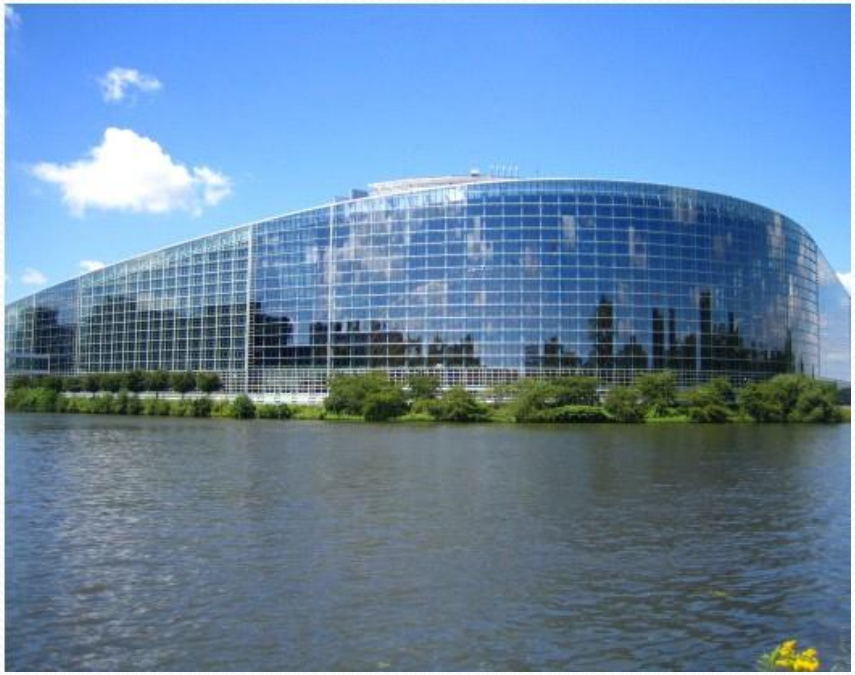

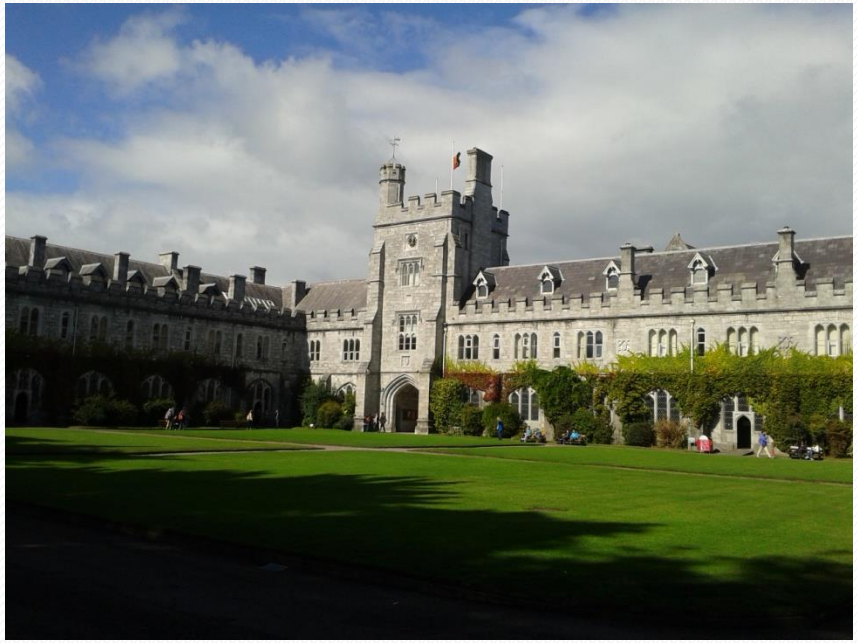

Prior Work

- LL.M Dissertation
- "The 'Rescue Culture' in England and Ireland: Key Differences and their Impact on the Promotion of a Uniform Insolvency Regime at European Level"
- Historical development of insolvency law in Ireland and England
- Backgrounds and various processes other than liquidation in those two jurisdictions
- Issue of harmonisation of the insolvency regime at European level

Description of the Research

- EU's efforts in providing a legal framework for dealing with cross-border insolvencies
- Council Regulation (EC) No 1346/2000 of 29 May 2000, OJ 2000 L160/1.
- Partial success
- Failure to harmonise the substantive insolvency laws of the Member States
- Analysis of the current revisions by the European Commission

Core Research Questions

- What are the main flaws of the European Insolvency Regulation 2000?
- What are the reasons for divergences in national insolvency laws?
- What level of harmonisation of insolvency law is required to further promote European economic integration and the smooth functioning of the Internal Market?

Why European Insolvency?

- Insolvency laws and regulations play an important role in the economy and in society
- Insolvency legislation closely interacts with other areas of law
- Impact of insolvency proceedings is no longer limited by geographic frontiers

European insolvency is a … branch of the study of insolvency that owes much to the phenomenon of cross-border incorporations and the conduct of business in more than one jurisdiction. It is, like insolvency, also a study of law and economic rules, to which is added the extra complication of EU law and the conflict of legal rules because of the involvement of more than one legal order…

Prof. Paul Omar (2008)

Outline

- A) Adequacy of the existing rules against the framework of EU law
- B) Issue of main and secondary proceedings
- C) European reforms

Setting the Scene:

Insolvency Law in the European Union

An Efficient European Insolvency Law Towards the Smooth Functioning of the Internal Market

- European Council Regulation on Insolvency Proceedings of 29 May 2000, entered into force on 31 May 2002

- Article 81 TFEU (ex Article 65 EC)

  Chosen as the legal basis for the harmonisation of insolvency law within the EU

Purposes of the European Insolvency Regulation

(a) To allow the proper functioning of the Internal Market which requires efficient and effective cross-border insolvency proceedings

(b) To coordinate the measures taken over the insolvent debtor's assets

(c) To avoid forum shopping

Jurisdictional Issues under the Regulation

- The Universalism vs Territorialism Paradigm
- Modified Universalism in the EIR and the concept of the “Centre of Main Interest”
- Secondary Proceedings: Impediments to the Rescue Culture?

Universalism VS Territorialism Paradigm

- Universality approach – reflects the unity of the debtor's assets
  - Law of the State where the debtor has his domicile (or registered office) and where the insolvency proceedings have been opened will be applied to administer the whole estate

- Territoriality approach
  - Proceedings only have effects within the jurisdiction of the State and within the territory of which they have been opened

Modified Universalism in the EIR and the Concept of the COMI

- Recital 11: acknowledges the different bankruptcy laws applied across the EU – difficulty to introduce pure universal proceedings
- Recital 13: COMI is situated in the country where a debtor "conducts the administration of his interest on a regular basis."
  - Needs to be ascertainable by third parties.
  - Presumption that the COMI is in the State of the registered office, unless the contrary is proven.

- Possibility to open secondary proceedings – departure from the universality model
  - Territorial effects of secondary proceedings
  - Can be opened in any Member State where the debtor has an “establishment”

- Secondary proceedings can be opened if:
  - Benefit local creditors
  - Main proceedings cannot be opened under the law of the Member State where the debtor’s COMI is located

Secondary Proceedings: Impediments to the Rescue Culture?

- "Corporate Rescue Culture"
  - Not a new concept – popular philosophy for some time
  - No precise definition
  - Generally refers to attempts to salvage a business
    - Out-of-court negotiated settlements/restructurings
    - Domestic insolvency procedures encouraging rehabilitation
- General policy is to preserve jobs and businesses perceived to have greater economic value as a going concern
  - After years of global recession, concept has received widespread renewed attention and focus

- Uneasiness as to the promotion of corporate rehabilitation under the EIR
  - Liquidation-oriented antecedents of insolvency legislation in several European Member States

- Secondary proceedings – impediments to corporate rescue
  - They cannot include rehabilitation provisions – only liquidation rules

Conclusion: Main Drawbacks of European Insolvency Law

- Title IV of the EC Treaty - not the most appropriate in terms of uniform application
- Use of the Regulation form - references to be made to the ECJ, but only from national courts in jurisdictions where there is no internal appeal
- COMI concept - EIR did not reach its initial goal of creating a well-ordered system granting legal certainty

Corporate Mobility & Regulatory Arbitrage

2 assumptions by the EIR drafters

- European firms did not substantially spread their activities outside their home State

- European firms could not reincorporate from one Member State to another, without first liquidating the business

No longer realistic

- Expansion of corporate activities across the EU situation needs to be regulated
- Increases uncertainties as to the location of corporations' COMI due to the fuzziness of this concept
- Case C-212/97 *Centros* [1999]
- Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies, OJ L 310/1

- optional regime as the premise of coincidence between COMI and registered office is no longer realistic

- inconvenient and impeding, particularly in promoting the recent “rescue culture”

The Reform of the Insolvency Regulation

Incentives for Reform

- 15 years
- achievement needs to be measured against its initial aims
- did not harmonise substantive insolvency laws within the EU
- multitude of individual rights and balancing interests at stake

International insolvency law has arrived at the threshold of an exciting period of development… There is now a necessity to build bridges between the individual national systems, and to create adaptable structures that will enable communication and cooperation to take place in response to the particular elements present within each case, - [this] requires a new vision, and new modes of thought, from all participants…

Ian Fletcher (1999)

Substance of the Reform

European Commission placed the amendment of the Regulation in its 2012 Work Programme

European Commission Recommendation of 12 March 2014 on a new approach to business failure and insolvency, C(2014) 1500 final

- "The objective is to shift the focus away from liquidation towards encouraging viable businesses to restructure at an early stage so as to prevent insolvency"
- Prevention of failures
- Second chance
  - "evidence suggests that failed entrepreneurs learn from their mistakes and are generally more successful the second time around. Up to 18% of all entrepreneurs who go on to be successful have failed in their first venture."

(European Commission Press Release, 12 March 2014)

INSOL Study on a new approach to business failure and insolvency – Comparative legal analysis of the Member States' relevant provisions and practices, 12 May 2014

- Large gaps between the laws of the Member States
- Liquidation is still the most common outcome in several countries
- Enterprises do not enjoy the same latitude or flexibility to handle and assess financial difficulties everywhere in the EU

CORPORATE RESCUE

EU's current main concern "to promote economic recovery and sustainable growth, a higher investment rate and the preservation of employment", as determined in the Europe 2020 strategy

Five General Areas

a) scope of the Regulation is expanded to include debtor in possession insolvency regimes, hybrid, pre-insolvency proceedings, and insolvency proceedings for natural persons
b) jurisdiction rules are clarified to improve the procedural framework for determining jurisdiction
c) legal regime for secondary proceedings is altered by authorising a court to refuse to open secondary proceedings
d) publically accessible national registers for insolvency cases will be established, which must be interconnected throughout the EU
e) measure of coordination for insolvency proceedings for the various members of a group of companies is provided

What's Next?

- Member States will have to enact further insolvency law procedures to facilitate the restructuring of businesses
- Inclusion of creditors during the adoption of restructuring plans
- More power to the court, to ensure that dissenting creditors do not face greater loss than they would have in the alternative scenario

- March 2015 - Member States are invited to implement the Recommendation

- September 2015 - Commission will review the implementation and the need for further measures

Evaluation of the Reform Proposals

- Not a complete overhaul of the Regulation
- Mention to European ideals and objectives:
  - Ensure the smooth functioning of the Internal
  - Market allow for more flexibility in time of economic crises, so as to promote business survivals
- Procedural, rather than *substantive* changes
  - Confined to the extension of the existing Europe-wide recognition to a larger category of restructuring proceedings

Conclusion

- Typically two opposing arguments are presented
  - full harmonisation of insolvency law, i.e. procedural AND substantive

OR

  - "choice model" for companies, i.e. chose their insolvency law

- Full harmonisation:
  - Subsidiarity principle
  - Foreseeability and certainty

- But:
  - European populations' preferences are heterogeneous
  - "Democratic deficit" of European institutions

Thus, a fully harmonised body of EU corporate insolvency law will most likely alter national balances and ranking of values and interests, hindering the process of total harmonisation, which, ultimately, is not only an issue of efficiency, but mainly of *politics* and *European integration*.

Thank you.