

Perspectives on harmonisation of insolvency law in Europe

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7. Perspectives on harmonisation of insolvency law in Europe

7.1. Summary

135. In this Chapter we summarise our findings and present our conclusions.

136. “Harmonization is a euphemism for forcing commercially less important countries to adopt the remedies and priorities of the commercially more important countries”, asserts Lynn LoPucki in one of his challenging publications.¹ Although the author claims “global” application for his quote, he clearly misunderstands the situation in Europe, which for “insolvency” does not have (unlike the USA) a “federal” Bankruptcy Code, nor a federal system of bankruptcy courts.² The starting point in the European Union is that every Member State has its sovereign power to draft, amend and put into force binding legislation, by its very nature confined to the borders of its own territory and that the Treaty on the Functioning of the European Union (TFEU) does not contain an explicit legal basis authorising the Union to adopt measures which aim at the harmonisation or approximation of insolvency laws.

137. A second observation for the EU is that the governance structure of the Union, as well as the subjects to be regulated (bearing in mind such notions as the principles of subsidiarity and proportionality) stop short in where individual Member States are able to assert sovereignty rights, also in matters related to insolvency law. In fact, in the area of insolvency law until some twenty years ago, the overwhelming view of the Member States (at that time) was, as articulated in the Virgós / Schmit Report (1996), nr. 12 (in present day terms): “The idea of a single exclusive universal form of insolvency proceedings for the whole of the [Union] is difficult to implement without modifying, by the application of the law of the State of the opening of proceedings, pre-existing rights created before insolvency under the different national laws of other [Member] States. The reason for this lies in the absence of a uniform system of security rights in Europe, and in the great diversity of national insolvency laws as regards criteria for the priority to be given to the different classes of creditors.”³ Given this background, thinking about “harmonisation of insolvency laws in Europe” indeed is a challenging one.

138. In Chapter 1 we outline and demarcate the subject of this Report. Both the European legislature (European Parliament) as well as representatives of European insolvency practice (INSOL Europe) very recently have issued proposals for harmonisation of several topics of insolvency law in Europe. In Europe, after a decade of introducing and applying vast changes

¹ Lynn M. LoPucki, *Global and Out of Control?*, in: 79 *American Bankruptcy Law Journal* 2005, 79ff.

² In the USA, Article I, section 8, clause 4 of the U.S. Constitution explicitly vests the authority to regulate “bankruptcy” in the federal Congress, which – fully different compared to the European Union – established a network of federal bankruptcy courts to decide even on matters of state law, without having to defer to state courts, see Jason Kilborn, *National Report for the United States*, in: Dennis Faber, Niels Vermunt, Jason Kilborn and Thomas Richter (eds.), *Commencement of Insolvency Proceedings*, Oxford International and Comparative Insolvency Law Series, Oxford University Press, 2012, 753ff and 762.

³ A nearly similar view has been laid down in Recital 11 of the EU Insolvency Regulation, which therefore clearly underlines that it is concerned with cross-border issues and disputes in insolvency cases.

in cross-border and international insolvency law, both proposals may turn the page to a new chapter in the development of insolvency law.

139. We analysed the motion of the European Parliament of November 2011, expressed some doubts as to its basis and criticised several of the reasons for the EP's proposals, laid down in 31 recitals. The claim that "insolvency law should be a tool for the rescue of companies at Union level" is, in the absence of any substantiation, rather meaningless and woefully vague on the meaning of "tool" as well as "rescue". Considerations in relation to insolvency of (cross-border) groups of companies without giving evidence of taking into account (other) developments in the field of the further creation and the future of European Company Law is a misconception. "Insolvency" seems to be cast in the role of Cinderella in the ongoing drama of European commercial law, where we note with sorrow that the European Commission in its work plans for company law, despite calls in literature⁴, still is silent on this important theme of business life. From the European Parliament's proposals we decided to concentrate on certain matters related to harmonisation of national insolvency laws.

140. Furthermore, another theme for harmonisation of insolvency law in Europe was introduced for treatment in our Report. It has a strong component of private international law (conflict of laws), namely the June 2012 proposals of INSOL Europe for the incorporation of the UNCITRAL Model Law on Cross-border Insolvency into the Insolvency Regulation. It is the subject of review in Chapter 6.

141. We note that our Report focuses on harmonisation of specific aspects of insolvency law for businesses and their insolvency (commonly known as the theme of corporate insolvency) and that our observations make no claim to be of significance of the treatment of insolvency of natural persons, financial institutions or States (or: sovereign debtors).

142. In Chapter 2 we draw on general sources to clarify terms that variously have been used in aligning certain matters of law, including insolvency law, such as "convergence", "harmonization", "approximation" and "unification". These are used either in the TFEU or in literature.

143. In short, convergence is to be understood as a more generic term referring to the growing together of laws either through an institutionalised process or through voluntary or even spontaneous action - and therefore not necessarily on the basis of a legal obligation, but for reasons of consistency, pragmatic efficiency or natural justice. As such, convergence refers to a global phenomenon that transcends different legal orders within and without the legal or geographic borders of the EU (in the words of Van Gerven). Convergence serves as an umbrella term for all processes that contribute to a higher degree of similarity; terms such as unification, approximation, harmonization or coordination are its manifestations.

144. Unification is an expression used for a deliberate process to remove disparities between different legal systems, whereas harmonisation is a process in which diverse elements of legal systems are combined or adapted to each other in an aim to create a coherent body of rules or principles.

⁴ See e.g. Mads Andenas, *Insolvency Proceedings in Europe*, 20 *Company Lawyer* 1999, 253; Paul J. Omar, *The Convergence of Company and Insolvency Initiatives within the European Union*, in: *European Company Law*, June 2005, Issue 2, 59

145. Within the European Union these terms matter as for certain powers of the Union legal acts are allowed, but for instance these acts “shall not entail harmonisation of Member States’ laws or regulations” (Article 2(5) TFEU). We then observe that within a European context the terms “harmonisation” and “approximation” have been used to describe active (often legislative) means of convergence, although it has been submitted that approximation and harmonisation have a different emphasis: approximation accents a certain result; harmonisation implies purpose (Van Gerven). We note that harmonisation refers to a legislative activity that is intended to remove disparities, while approximation rather refers to the result of a process, which also can be the result of incremental convergence through case law, through soft law guidances and principles, which find their way to legislature, courts or insolvency practice. We suggest that in theory a distinction between harmonisation and approximation may flow from a different *animus harmonisandi*.

146. We also refer to a legislative method at EU level which acknowledges certain benchmarks of national sovereignty (such as the principles of subsidiarity and proportionality) and is open for initiatives from groups that ultimately are the destined addressees of certain legislative norms. As such, this method leaves Member States with more flexibility and discretion in shaping national legislation. It is termed Open Method of Coordination (OMC), which is a means of governance based on soft law mechanisms, including the establishment of an agenda for achieving certain goals in the short, medium and long terms, setting benchmarks against (international) best practices of creating European guidelines and converting these into national and regional policies by setting specific targets and adopting measures, taking into account national and regional differences and adding an evaluation process, the results of which should be used to improve these policies or the skills of the players that are working with them. OMC as a method was introduced not only to increase compliance of Member States with EU legislation, but also to achieve greater convergence towards the main EU goals, whilst overcoming the dilemma encountered by Member States which desire a closer cooperation in certain issues, but are not willing to resort to supranational decision-making (“joint decision trap”). This method has inspired us in using it for our suggestions for the further development of harmonisation of certain matters of insolvency law, which we will further explain below.

147. During the last three years especially the theme of harmonisation of insolvency laws in Europe is on the rise. Chapter 3 describes the Note of the Directorate-General for Internal Policies, Policy Department Citizens’ Rights and Constitutional Affairs (C) on “Harmonisation of Insolvency Law at EU level.” It sets out several reasons for harmonisation, but it most importantly lacks any reference to what the “EU” would have in mind as the goals for insolvency law, both as a perspective and as a result of any harmonisation. We offer as a common understanding of these goals, and therefore as a general basis for further discussion, the following.

148. The goal of any insolvency law in Europe is the maximisation of the assets of the estate of the debtor for the benefit of the body of creditors, in a transparent, predictable and efficient way. We have suggested in our ALI-III Report on Global Principles for Cooperation in International Insolvency Cases (“Global Principles”) that for insolvency in an international context the overriding objective is twofold: the maximisation of value of the insolvency estate and the furthering of the just administration of the proceedings.

149. The goal of maximizing the value of the debtor’s global assets includes the preservation where appropriate of the debtor’s business. This goal contains any form of the available

variations of administration or reorganisation of activities and assets of an insolvent debtor that can contribute to that primary goal. The aim of such maximization should be beneficial to the debtor's creditors, as well as other parties concerned, which includes other interests involved in a national or international case, such as the interests of maintaining employment or, exceptionally, the interest of shareholders.

150. We just mention here that the other goal of the furthering of the just administration of the proceedings includes such desiderata as the application of the principle of equality of arms, so that there should be no substantial disadvantage to a party concerned, and the active management of an insolvency case, preferably in a way which accommodates the legitimate concerns of parties of interest, insolvency administrators and other courts involved.⁵

151. We then continue to discuss the reasons given to support harmonisation of certain matters of national insolvency laws. The European Parliament lists 4 of such reasons.

152. The argument that such harmonisation is beneficial for the "level playing field" is hard to assess, where it uses a legally vague concept of "stakeholders" and is puzzling where it argues that insolvency law should protect the value of the assets of the estate, thereby returning greater value to (creditors and) "shareholders". This latter group in many legal systems is not treated on the same footing as (unsecured) creditors. Although there may be little doubt that differences in national insolvency laws hinder efficient and effective restructuring of companies to the detriment of the internal market, the causal relationship in that "disparities in national laws" form "obstacles" to a successful restructuring of insolvent companies is unclear, whilst the claim that the internal market would benefit from a level playing field is idle, lacking any research of data and statistics that could support this assertion.

153. The argument of preventing forum shopping may gain more support, although it can not provide a solid anchor without a clear understanding of what "good" or "bad" forum shopping is, which is only possible if the interests to be taken into account when drafting or applying insolvency law are much more clarified than they are now.

154. We would be supportive to the argument that harmonisation of certain areas of insolvency law is "worthwhile and achievable", where the results of efforts of harmonisation may increase transparency and lead to a better understanding by the parties involved of the means and methods that are available to address the needs of companies confronted with financial difficulty and of the remedies available to e.g. the creditors of these companies. In our opinion it would also be worthwhile to promote harmonisation of areas that would ensure equitable treatment of similarly situated creditors, including transparent rules for gathering and dispensing information, predictable steps in administration processes and guaranteeing equitable distribution to these creditors. Moreover, if increased harmonisation were achieved in respect of timely, efficient and impartial resolution of any matter of insolvency, this would

⁵ See Global Principles 5 and 4 respectively, including our explanatory Notes. The case for applying the equality or arms principle in international insolvency cases convincingly has been made by Samuel Bufford, Center of Main Interests, International Insolvency Case Venue and Equality of Arms: The Eurofood Decision of the European Court of Justice, 27 *Northwestern Journal of International Law and Business*, at 351 ff. (2007). It has been applied further to the European situation by Alan J. Stomel, Answering the Call of the European Court of Justice in Eurofoods, Institute for European Studies Working Paper 3/2011, www.ies.be/files/WP%203:2011%20Alan%20J%20Stomel.pdf.

most assuredly enhance confidence in Member States' insolvency law and in those who have to apply it.

155. Progressive convergence in the national insolvency laws of the Member States, as the fourth and last argument, was not substantiated. The overview we provided of initiatives by academics, some common trends in developing prominent principles of insolvency law, a large spectrum of soft law documents to facilitate the realisation of the ongoing globalisation of commercial activity in the insolvency area, and the raised awareness internationally in nearly all circles (NGOs, global and regional associations, practitioners, judges, academics, and indeed central bodies of the EU), combined with several countries' national needs to actually change their existing legal framework to achieve economic results that are potentially better than those that might be achieved under liquidation, generally all point at convergence. However, whether that development is strong enough to support acts of harmonisation is another question, which is addressed in part of the remainder of our Report.

156. We then continue in Chapter 3 by posing the question: aren't there any disadvantages to harmonisation of national insolvency laws? In insolvency law related literature of the last five years this question has not been thoroughly addressed, but in the course of analysing and discussing other related matters authors have identified a quartet of disadvantages.

157. The first one is that harmonisation results in the loss of national peculiarities of insolvency law. This is – at least for company's insolvency – not a convincing argument. Law, also insolvency law, should facilitate business processes. Where in certain solutions public moneys (the taxpayers' contributions) are not at stake or can balance out with certain benefits that can be achieved, only certain well defined interests (such as a certain protection for employment or secured financing) should be protected by national insolvency laws.

158. Harmonisation – so runs the second argument – will also result in losing the dynamic possibilities associated with regular competition between countries to create better law systems, in which they can learn from each other. In the doctrinal literature it is debated whether states can in reality compete with each other to attract insolvency cases. We are not aware of a balanced study with empiric data to test this hypothesis. Conversely, the pessimists are of the opinion that such competition too readily degenerates into a "race to the bottom". "Delawarisation" may be beneficial for certain countries for matters of corporate law, but in the area of insolvency the consensus among experts tends to the contrary. Recent German legislation however seems an answer to such competition. There are no data yet whether this legislation brings the fruits it expects. In those countries on the other hand where calls for improving insolvency law fall foul to vested interests and passiveness of a country's government, the level playing field easily becomes an unfair battlefield in that companies in financial distress are caged inside undeveloped insolvency systems, established in a period prior to the invention of cars and planes, to say nothing of "credit swaps", "derivatives" and "synthetic collateralised debt obligations" or the true desire of creditors to be able to influence the appointment of an insolvency office holder, to receive adequate information and to be involved in the chosen course of action in the administration of the estate.

159. Related to the second argument is the other alleged disadvantage that individual countries will also be confronted with an extreme slowing down of the process of amending the law and the possibility of adapting it due to the need to maintain conformity with the harmonised "norm". This argument is not persuasive as it is based on the assumption that these and other processes themselves could otherwise be amended at greater speed. Both

arguments, moreover, seem to purely focus on (hard) law, overlooking the fact that the legal rules surrounding businesses in financial distress also could be drafted in a more flexible way, allowing judicial discretion, in a field where there is seldom one single solution. No one single solution indeed, but many times a solution reached in a process in which many parties with interest in the case participate, where only private money is involved and therefore based on voluntary agreement, rather outside of the scope of any “hard law” rules.

160. The fourth and final point made (harmonization between legal systems of Member States often leads to differences within the national systems themselves) clearly is a fair one. The answer most probably is to look for flexibility in legal norms to overcome these differences, whilst on the other hand ensuring as far as possible that situations in comparable circumstances receive an equal treatment.

161. In Chapter 4 we continue our research with an assessment of the legal basis in the EU Treaties for actions, including acts of harmonisation of insolvency laws. Our starting point is, as indicated earlier, that the TFEU does not contain an explicit legal basis authorising the Union to adopt measures which aim at the approximation of insolvency law. Two strong indirect candidates, also mentioned by the European Parliament, are Article 81(2) TFEU (concerning cross-border judicial cooperation) and Article 114 TFEU (measures “for the approximation of the provisions laid down by law, regulation or administrative action in Member States which have as their object the establishment and functioning of the internal market”).

162. After explaining the basis in the TFEU of the Directives 2001/17 and 2001/24 (winding-up and reorganisation of financial institutions) and the yin-yang position of the Insolvency Regulation with the Brussels I Regulation, we point to the former Regulation’s basis in Title V TFEU (“Area of Freedom, Security and Justice”), more specifically in Article 67 TFEU (ex Article 61 ECT) and Title V, Chapter 3 TFEU (“Judicial Cooperation in Civil Matters”) Article 81 TFEU (ex Article 65 ECT). On this legal foundation the Union “shall develop judicial cooperation in civil matters having cross-border implications, based on the principle of mutual recognition of judgments and of decisions in extrajudicial cases. Such cooperation may include the adoption of measures for the approximation of the laws and regulations of the Member States”, see Article 65(1).

163. We submit that on a plain reading of the text the provision is sufficiently broad to cover any topic in the area of judicial cooperation in civil, and therefore also insolvency matters. Article 81(2) TFEU then continues by providing that for the purposes of Article 81(2) measures are allowed to be taken “..... particularly when necessary for the proper functioning of the internal market, aimed at ensuring” the specific goals mentioned in Article 81(2) (a) – (h). It is our point of view that Article 81 discloses cross-border judicial cooperation’s basis (mutual trust between Member States), provides what it may include (approximation etc.) and where it should have its focus (goals of Article 81(2)), but the term “judicial cooperation” itself remains rather vague.

164. Article 81 TFEU (and its predecessor Article 65 EC Treaty) has been exclusively used for the adoption of rules on cross-border civil procedure and conflict of law matters in some fifteen Regulations and Directives. All these measures have an international element, so it seems that approximation of substantive laws in general, and more specific harmonisation of certain matters of national insolvency laws, is only covered by it in where the matters to be

harmonised contain this international element. Support for this view can be found in several recitals of the Insolvency Regulation.

165. Although arguments for the contrary can be made, we adhere to the view (expressed by Kuipers) that there is nothing in the wording of Article 81 that would exclude the adoption of measures envisaged at the approximation or unification of substantive law, and therefore substantive insolvency law, as long as the measure contributes to the general goal of judicial cooperation in civil proceedings. This means that the matters to be included are justified by the policy objectives listed in Article 81(2), such as (e) effective access to justice, (f) the elimination of obstacles to the proper functioning of civil proceedings, and (h) support for the training of the judiciary and judicial staff.

166. We then continue to explicit the necessity of developing mechanisms for judicial cooperation. It is at this juncture that EU legislature and developing (international) practice can amalgamate, where the latter has produced such examples as the use of protocols and cross-border insolvency agreements, and during the last a few years also in Europe there have emerged the 2007 European Communication and Cooperation Guidelines for Cross-Border Insolvency (CoCo Guidelines), and the authors' 2012 ALI-III Global Principles Global Principles for Cooperation in International Insolvency Cases. In the earlier part of our Report we did however observe that these non-binding principles and guidelines may have several disadvantages, relating to the ascertainability of the texts, their possible lack of legitimacy, quality and clarity or their effectiveness. A call for comparative research was made.

167. Within the described context we submitted that the central principle of cooperation in cross-border cases could lead to a set of Guidelines, as an addition to the Insolvency Regulation: (i) ensuring as far as possible that this Regulation works in practice, so that the debtor's estate is dealt with efficiently and effectively, (ii) fitting the current environment where efficient and effective solutions have been developed based on models reflecting cooperation and communication, and (iii) guaranteeing the organisation and conduct of a fair legal process and ensuring the fair representation of all parties concerned in insolvency processes. This then should be followed by training, which will aim to build capacity amongst the judges and practitioners, with the delivery of tools to be able to give full effect to the Insolvency Regulation, to develop autonomous and uniform interpretation of insolvency terms and concepts having regard to the objective of the Insolvency Regulation and to enable the development and familiarity with the developed Guidelines. An evaluation process of these Guidelines in a well-planned and structured way could in a term of say five years lead to additional rules and practices, which would reflect harmonisation of certain matters as these are felt or applied in European insolvency practice.

168. Article 114 TFEU may serve as a legal basis for harmonisation as it allows the adoption of measures for the approximation of the provisions laid down by law, regulation or administrative action in Member States which have as their object the establishment and functioning of the internal market. Our main conclusion, derived from literature, is that the meaning and scope of "internal market" is not fully clear and that its application may require further study regarding the question which measure of harmonisation of any matter of insolvency is genuinely aimed at improving market conditions and actually contributes to the elimination or prevention of existing or future obstacles to the right of free movement.

169. We finalised Chapter 4 by indicating that, in making insolvency law, Article 288 TFEU provides five mechanisms: regulations, directives, decisions, recommendations and opinions,

and we briefly explain these mechanisms. We maintain that in efforts to harmonise insolvency all these measures may be employed.

170. In Chapter 5 – after some introductory remarks on the stage of scholarly development of comparative insolvency law – we lay two rather contradictory topics under the magnifying glass, a rather substantive topic (the “insolvency” test) and a topic related to one of the crucial and active role-players in practically any insolvency proceeding, the insolvency office holder, especially the supervisory system which applies to its function.

171. We explain that presently the EU, in as far as the Insolvency Regulation will apply, has the possibility of the “opening” of some 100 different collective insolvency proceedings in 26 Member States. In any given Member State the number of available insolvency proceedings can range between one and seven. Both for the Netherlands as for the UK with short characteristics, in addition to the insolvency tests used, a broad spectrum of principal and detailed differences in requirements and legal consequences was displayed.

172. Recommendation 1.1 of the European Parliament suggests that a directive should harmonise aspects of the opening of proceedings. We submit that the preferred way is opposite: first the topic, then the preferred EU measure.

173. The European Parliament continues by listing ten groups of differences, largely relating to matters of a pre-opening nature, the opening itself, the opening test and post-opening matters. After explaining some considerations in terminology and approach, we submit that a sensible formulation of “opening” and its surrounding different treatment of requirements to adhere to, is only possible when a clear view has been developed of what the goals of insolvency law in general are and what the nature (or: goal) of a certain insolvency proceeding and the person who has the ability to invoke such proceedings, is. We will not delve into these matters now.

174. We then continue this treatment with an overview and explanation of “commencement”-criteria, as developed in soft law documents or literature, the most prominent being: (i) the “liquidity”, “cash flow” or “general cessation of payments” test, (ii) the “balance sheet” test, and (iii) the “imminent insolvency (prospective illiquidity)” test. Many of these tests, sometimes with different requirements, including the query of who has the right to initiate insolvency proceedings and whether a court is involved, are applied in the limited group of Member States that were subject of our research. Our provisional conclusion of this part of Chapter 5 is that the Note is fairly quick in its conclusion that overall, the liquidity test seems to be the most commonly used test in the EU Member States.

175. In the latter part of Chapter 5 the focus is on the professional position of an insolvency office holder. The European Parliament sets out six requirements which are recommended for harmonisation, four of which make sense in this category of aspects. We just look into only a part of the first requirement, wondering though why the European Parliament has not addressed a similar approach to the other important actor in insolvency cases, namely the court. Where the fundamental principle in cross-border insolvency matters within the EU is that recognition of judgments delivered by the courts of the Member States is automatic and is based on the principle of mutual trust, mutual trust serves as the cornerstone for confidence in the Member State’s judicial capacity. We recommend systematic examination in this specific field in an aim to obtain accurate and comparative data on aspects of the functioning of courts in insolvency matters.

176. Contrary to the opinion expressed in the Note we place the accent not so much on what an insolvency office holder does, but on her or his inherent professional and personal qualities, both in an international as well as in a national context. In cross-border cases in the EU an insolvency office holder may have either a dominant role in concurrent proceedings or he/she is – on the contrary – subject to the dominant position of his counterpart in the other interdependent proceeding. Not only in finding a fair balance in its complex role, which reflects the key of the model the Insolvency Regulation is built on, but also his or her other tasks and functions require certain specific qualities and skills.

177. In our proposals we are guided by a vision which was already expressed over thirty years ago: “The success of any insolvency system is very largely dependent upon those who administer it. If they do not have the confidence and respect, not only of the courts and of the creditors and debtors, but also of the general public, then complaints will multiply and, if remedial action is not taken, the system will fall into disrepute and disuse”.⁶ More broad than creditors’ confidence, the trust the market and the general public puts in the insolvency office holders’ functioning is crucial for any insolvency system. We submit that this position translates in her/his ability to be able to exercise a transparent process, e.g. for unsecured creditors to be informed in a clear way about any steps that influence their position and allows them to be able to influence any administration, to understand the way the profession is regulated, which would include a mechanism to maintain trust in any regulatory regime, such as a post-action review or a complaints procedure.

178. Although the available data and literature is not overwhelming, they provide an indication that the qualification, licensing, appointment, replacement and remuneration of insolvency office holders as well as their standards of work and conduct in several countries are arranged in quite a number of ways. As said, the available data could be more complete, but the vision expressed above brings us to suggest that the attempt be made to align and improve the professional standards and ethical guidelines applicable to insolvency office holders.

179. The third and last theme of harmonisation of insolvency laws has an international dimension and is a part of INSOL Europe’s Revision Report 2012, which includes the proposal that the UNCITRAL Model Law on Cross-border Insolvency will be incorporated into the Insolvency Regulation. We discuss this theme in Chapter 6. The main reason for the proposal is that the UNCITRAL Model Law (as such a soft law document) provides a system which is supported by the global community and contains a two staged system of recognition in an aim to ensure the interests of all parties concerned are adequately protected. INSOL Europe considers, with its suggestion of incorporation, that a unified approach to insolvency proceedings opened outside the European Union will enhance the proper functioning of the internal market and support a unified external trade policy.

180. For several reasons we criticise the proposal.

181. In a period of over ten years, some twenty countries throughout the world have enacted legislation that includes the adopting of the text of the UNCITRAL Model Law, either rather literally or in an amended version. Five of these countries are EU Member States, in

⁶ Cork-Report Insolvency Law and Practice – Report of the Review Committee, Chairman Sir Kenneth Cork, June 1982, [Cmnd. 8558], para. 732.

chronological order of enactment: Romania (2003), Poland (2003) (both prior to EU Membership), Great Britain (England, Wales and Scotland, 2006, Northern Ireland, 2007), Slovenia (2008) and Greece (2010). In our Report a brief survey of these Member States' enactments follows, as well as a short account of the characteristics of international insolvency legislation in Germany, Belgium and (the volatile pre-draft of) the Netherlands.

182. From our short survey we conclude that quite a number of Member States since the coming into force of the EU Insolvency Regulation (2002) have included rules for international insolvency law to be applied beyond the scope of the Insolvency Regulation. A notable difference with the approach the Model Law takes is that Austria, Belgium, Germany, Spain, Romania and the Dutch pre-draft include an extension of the core of the conflict of law rules as laid down in the EU Insolvency Regulation, to be applicable to non-EU Member States. INSOL Europe's proposal does likewise, but it fails to take into account other notable differences, of which we list: (i) that in the UK, Germany and Greece cross-border cooperation in international cases is discretionary for a court (the court "may"), (ii) that Romania and Spain use reciprocity provisions (related to recognition), as Belgium does (more limited, related to cross-border cooperation), (iii) that in England and Wales, Scotland and Northern Ireland and also Slovenia a concentration of cases to specific courts has been included, taking the decisions in international cases away from the general national rules for jurisdiction of domestic courts, and (iv) that Slovenia as well as Greece integrate in their legislative framework as a form of judicial cooperation the possibility of formalisation by the court of cross-border protocols or insolvency agreements.

183. Already at this juncture it can be observed that the choice for incorporating the Model Law in a Regulation must be regarded as an error. Both the nature and the original effect of the Model Law, as well as the fact that certain matters already have been included in national legislation of Member States (be they followers of the Model Law or having drafted their own systems) in our opinion would only justify the use of a Directive as the medium for bringing about harmonisation of the laws of the Member States in relation to insolvency proceedings originating in non-EU states.

184. After having executed a brief test of selected general provisions in INSOL Europe's proposal the overall conclusion is that it should go back to the drawing board (leaving aside for now the question of who will follow up on this call). Although in the proposed Chapter VII of the Regulation the chosen numbering of articles makes comparison with the numbering of the Model Law burdensome, the text of Chapter VII INSOL Europe proposes is nearly verbatim the text of the Model Law. However, in its proposed relation to the Insolvency Regulation and in the light of over five years of experience in case law in several of the enacting States (we only took a short look at the USA, UK, Australia and New Zealand) the proposal falls short on several points.

185. Some of the drawbacks we observe relate to (i) inconsistency with the Insolvency Regulation (non-equal treatment of tax claims), (ii) an underdeveloped term "a law relating to insolvency" as part of the definition of "non-EU proceeding", (iii) an uncertain exclusion of certain proceedings relating to financial institutions from the scope of Chapter VII, (iv) the omission to give consideration to a partial exclusion from its scope (allowing foreign non-EU insolvency office holders and others in proceedings in relation to financial institutions to make use of the provision regarding access or the cooperation provisions), (v) an unbalanced provision regarding the relation between the Insolvency Regulation, the proposed Chapter VII and existing international treaties and agreements, (vi) a debatable choice for the competent

courts in non-EU matters, being the courts of the Member States with general jurisdiction, where centralising the court's competence in these international, mostly complex matters (such as in England (High Court), Scotland (the Court of Session in Edinburgh), Australia (Federal Court of Australia for individuals; the Supreme courts and the Federal Court as for other debtors), Mauritius (Supreme Court), the Netherlands (draft: Court of The Hague) and New Zealand (High Court), seems much more logical, and (vii) an interpretation provision which is not unproblematic in its application, given the purposive, sometimes autonomous interpretation which has to be given to EU-matters, as well as the fact that the originally intended "unity" of terms (such as the bothersome "COMI") only a few years after enactments have resulted in "diversity" in several jurisdictions all over the world.

7.2. *Conclusions*

186. Insolvency has human traits. In early American literature "bankruptcy" was depicted as a gloomy, depressing and discouraging topic.⁷ This may be true for insolvent debtors or in the eye of the general public. We however feel that the law, the legal profession and the legal system surrounding insolvency pulses the heartbeat of an economy, be it a national economy which will have a gamut of possibilities of being connected (influenced) by the outside world of trade and finance, resulting in variations of an open, interconnected economy. A transparent and solid national insolvency system has several advantages. It provides local lenders and foreign investors with confidence in the rules that govern economic development, which includes the possibility of failure. A good insolvency law is beneficial for such goals as the protection of certain groups of people against the penetrating consequences of over-indebtedness in today's credit society.⁸ As far as businesses are concerned we see insolvency law as a key component in any country's legal and financial infrastructure, in well-developed ones as well as in economies in transition.⁹ The themes covered in many insolvency laws cannot be missed for such aims as the support of modern economic processes which inherently include continuous change of the circumstances and market conditions in which businesses are operating and the challenge to adapt to these in timely fashion. Such processes should include rules for the facilitation of the rehabilitation of a business or for the orderly market exit of a business that is inefficient. When insolvency law includes rules which foster discipline and honesty in financial management it provides adequate protection to creditors. Not all these goals will be equally recognizable in a country's legislation, and some elements of these goals seem to contradict each other. Insolvency law, nevertheless, is a vivid and important part of the legal framework both for market economies and for economies in transition. Based on our experiences we believe that insolvency law ultimately is the litmus test for a well functioning civil and company law system, and even more broadly, for the entire economic structure of a country.

187. Insolvency law has a long history and it has changed its face during the last centuries from systems in which debtors were imprisoned and the debtor's failure was stigmatised to systems in which insolvency has gradually grown out of its criminalisation. After the introduction, in many European countries over a century and a half ago, of a separation

⁷ Charles Warren, *Bankruptcy in United States History*, 1935, reprinted by Beard Book, 1999, p. 3.

⁸ On this topic: Julia M. Davis, *Incorporating Social Justice Concerns into the New Law and Development Movement: The Importance of Insolvency Law* (August 25, 2011), <http://ssrn.com/abstract=2006105>.

⁹ See Manfred Balz and Henry N. Schiffman, *Insolvency Law Reform for Economies in Transition – A Comparative Law Perspective*, *Butterworth Journal of International Banking and Financial Law* 1996, 2ff.

between a person's assets and those of a company (with limited liability) in business life, insolvency has grown to become a calculable and acceptable risk.¹⁰ In most more developed legal systems insolvency law has grown in importance, although most countries continue to discuss and struggle with the desirable approach and therefore the goals of insolvency law.

188. Companies and businesses operate best in a challenging environment, which is beneficial for all parties concerned, such as suppliers, the companies' management, employees, creditors, customers and shareholders. This logically means that uninterrupted continuity of any business is a desideratum in itself, as it means: (i) the possibilities of continuing employment, (ii) job security for management, (iii) the (guided by good management) possibility of efficiently employing all the available means to run a good business (e.g. natural resources, technical equipment), (iv) a share in the profits (dividend) for shareholders and (v) the possibility to continue all other relations, with small suppliers of goods and services and buyers/customers of these products and services. In this respect, insolvency law is the vital core and provider of strength and resilience of an economic system. If the financial difficulties go from bad to worse, insolvency laws should have available rules to timely respond to these difficulties, to formulate a optimum approach to a solution, within which takes into account all rules of company law, contract law, the law on securities, employment law, and of course insolvency procedural law itself.¹¹

189. The creation of a European community and the further establishment of the European Union, including its four freedoms, strongly fostering and enhancing trade, business and investments across national boundaries can not be regarded as complete without such a transparent and solid insolvency system. We only can repeat the point made by one of the architects of what now is the EU Insolvency Regulation, in that a "functioning bankruptcy system is essential to any economy that aspires to achieve the freedoms of establishment of business and the free flow of goods, services and capital, and to integrate national markets into a unitary internal market."¹²

190. In addition to the acknowledgment of the necessity to include insolvency law within the achievements to develop such an internal market, another argument accounts for the relative decline of the autonomy of national legal systems to regulate matters of insolvency. The ongoing globalisation keeps on challenging national sovereignty. The problems confronting countries – from international terrorism, to such themes as financially distressed global businesses and collapsing banks, or libel tourism¹³, – increasingly transcend national

¹⁰ See Jay Lawrence Westbrook, Charles D. Booth, Christoph G. Paulus & Harry Rajak, *A Global View of Business Insolvency Systems*, The World Bank, Washington DC, 2010, 143, submitting that insolvency is an enterprise risk.

¹¹ See e.g. M. Didier, *Problématique du droit de la faillite internationale*, in: *Revue de droit des affaires internationales* 1989, 201 ("la législation de la faillite est une carrefour où se croisent et se rencontrent toutes les composantes du système juridique considéré"; insolvency law is an intersection where all components of any law meet and affect each other).

¹² Manfred Balz, *The European Convention on Insolvency Proceedings*, in: *70 American Bankruptcy Law Journal* 1996, 485ff, at 490.

¹³ See the 4 July 2012 Declaration of the Committee of Ministers of the Council of Europe on the Desirability of International Standards dealing with Forum Shopping in respect of Defamation, "Libel Tourism", to Ensure Freedom of Expression, <https://wcd.coe.int/ViewDoc.jsp?id=1958787&Site=CM&BackColorInternet=C3C3C3&BackColorIntranet=EDB021&BackColorLogged=F5D383>.

boundaries, either because the problems do not lend themselves to solely national regulation or because they involve the interests of the international community as a whole. In this new environment the traditional areas of national law (such as private law, criminal law, administrative law or insolvency law) acquire an increasingly internationalised character, in which its content is formed on different levels, with different legal measures (including soft law mechanisms), established either “top-down” the legislation-ladder or “bottom-up”, initiated by private actors or a mix of such modes of operating.¹⁴

191. Several developments point at what might be a solid basis for harmonization of certain aspects of insolvency law: the emergence of some common principles in the field of insolvency law shows that there is convergence of certain themes, not as a result of a deliberate process but a growing into a similar direction spontaneously, as for instance in several member States’ introduction of “rescue” procedures and provisions of international insolvency law.

7.3. *An Agenda for future work*

192. Although the reporters are not specialists in the area of “law-making”, we conclude our Report with the development of seven key indicators which may assist in identifying situations in which harmonisation may be beneficial, and the working method to achieve such harmonisation. These seven criteria – not necessarily in this order and overlaps could occur – may point at a direction to take in the process of developing a legislative skeleton for harmonisation of insolvency law in the near future.

193. These indicators are:

1. Consistency with international norms: strive for consistency with international norms, so any rules will be generally applied in the same way in any member State and/or across the EU;
2. Goals for the EU: agree on the basis allowing the European legislator to act and on the goals that the European legislator set himself to achieve;
3. Take stock: map the present level of harmonisation in all areas of law related to insolvency;
4. Overriding objectives: formulate overriding objectives to take into account, such as offering any involved party a sufficient degree of legal certainty;
5. Flexible legislation: draft a legal skeleton which is sustainable, including a process which is sufficiently flexible and capable of adapting to changing circumstances in which businesses operate;
6. Need for action: examine whether there is a specific need for a certain action or legislative intervention, and if so, what would be the most suitable course of action and ensure that its result be supported by a wider group that will have to work with it;
7. Balance: any rules of such a skeleton should reflect a fair balance between the (often competing) interests of creditors and other parties concerned.

¹⁴ See e.g. Petra Buck-Heeb / Andeas Dieckmann, *Selbstregulierung im Privatrecht*, Mohr Siebeck, 2010; Matthias Knauf, *Der Regelungsverbund: Recht und Soft Law im Mehrebenensystem*, Mohr Siebeck, 2010; Jan M. Smits, The Complexity of Transnational Law: Coherence and Fragmentation of Private Law, in: Netherlands Reports to the Eighteenth International Congress of Comparative Law (Washington 2010), Antwerpen-Oxford 2010, 113ff.; Jan M. Smits, Private Law 2.0. On the Role of Private Actors in a Post-National Society, Eleven International Publishing, The Hague, 2011; Sam Muller et al. (Eds), *The Law of the Future and the Future of Law*, Torkel Opsahl Academic Epublischer, Oslo, 2011.

Several of these indicators may demand empirical input, a point we now leave aside.

194. In para. 4.5. we explained the set of legal measures available to the Commission to exercise its powers. In addition to the well-known regulations and directives, the legislative toolbox contains the “decision”, which is binding in its entirety, but specifying those to whom it is addressed, and the “recommendation” and “opinion”, both of which have no binding force. As an example, it would be conceivable that a “decision” could be used towards the group of insolvency office holders, after they have drafted themselves a non-binding set of best practices with professional and ethical rules. The chances may increase if such best practices (i) (consistency with international norms) are based on studies regarding the professional and ethical rules for insolvency office holders, as provided for by regional and global institutions, such as UNCITRAL, American Law Institute, European Bank for Reconstruction and Development, International Bar Association, IFAC (International Federation of Accountants) or TMA (Turn Around Management Association), (ii) (goals for the EU) fit within the EU context (e.g. such best practices further detail the general duties of insolvency office holders to communicate and cooperate cross-border in parallel proceedings, see Article 31 InsReg), (iii) (take stock) take into account the results of study of the professional and ethical rules for insolvency office holders in a representative number of EU Member States), and (iv) involve insolvency practice (courts, agencies and especially practitioners) into its development.¹⁵

195. We now turn to the seven key indicators we presented above, explaining these. We will do this rather briefly, not only because of limitations of space, but also with the aim of presenting building blocks for a sufficiently open agenda, to allow for a further discussion with non-insolvency specialists, such as specialists in contract law, securities law or company law. With their input the key indicators should also be a matter of further debate.

196. *Consistency with international norms.* We are not hesitant to bring forward the UNCITRAL Legislative Guide as a non-binding guidance and standard setter for the organisation and furnishing of a national insolvency system. Under the heading “Provision of certainty in the market to promote economic stability and growth” the Guide observes that insolvency laws and its institutions (such as insolvency office holders, courts or supervising agencies) are critical to enabling a state to achieve “the benefits and avoid the pitfalls of integration of national financial systems with the international financial system. Those laws and institutions should promote restructuring of viable business and efficient closure and transfer of assets of failed businesses, facilitate the provision of finance for start-up and reorganization of businesses and enable assessment of credit risk, both domestically and internationally.”¹⁶ As the first of its (presently) over 250 recommendations the Guide then suggests that in a national effective insolvency law the following key objectives should be implemented “..... with a view to enhancing certainty in the market and promoting economic stability and growth”:

- “(a) Provide certainty in the market to promote economic stability and growth;
- (b) Maximize value of assets;
- (c) Strike a balance between liquidation and reorganization;
- (d) Ensure equitable treatment of similarly situated creditors;

¹⁵ On the collaborate effort of creating insolvency law and rules in practice by academics, judges, practitioners and the legislator, see Paul Omar, *The building blocks of insolvency reform: Is law enough?*, in: *eurofenix Summer 2012*, 32ff.

¹⁶ UNCITRAL Legislative Guide on Insolvency Law (2004), see part 1.I.A.1.4.

- (e) Provide for timely, efficient and impartial resolution of insolvency;
- (f) Preserve the insolvency estate to allow equitable distribution to creditors;
- (g) Ensure a transparent and predictable insolvency law that contains incentives for gathering and dispensing information; and
- (h) Recognize existing creditors' rights and establish clear rules for ranking of priority claims."

197. With as a starting point the assumption that an "internal market" within the EU is the equivalent of any national market (transposed "without borders" to a regional grouping of nations) we submit that Recommendation 1 could be a point of departure for a debate on the objectives and the position of "insolvency" within the internal market.

198. *Goals for the EU.* Rather recently within the EU supportive measures have been taken for the benefit of "delivering an area of freedom, security and justice for Europe's citizens" with the object of guaranteeing "... respect for the human person and human dignity, freedom, equality, and solidarity are our everlasting values at a time of unrelenting societal and technological change", see the so-called Stockholm Programme.¹⁷ After the entry into force of the Lisbon Treaty, in December 2009, an Action Plan Implementing the Stockholm Programme has been published aiming actively at strengthening confidence in the European judicial area.¹⁸ It is clear that it focuses on the area of freedom, security and justice, and therefore stays within the (perceived) restrictions of Article 81 TFEU.¹⁹

199. The European Council in the 2009 Stockholm Programme acknowledges the need to adopt measures in the field of justice which support economic activity²⁰ and, in the Action Plan, specifically provides for a proposal of amending the EU Insolvency Regulation. To this end, the Action Plan provides:

"Union law can make a concrete and powerful contribution to the implementation of the Europe 2020 strategy and mitigating the damage caused by the financial crisis. New EU legislation will be proposed whenever necessary and appropriate to strengthen our single market, helping businesses by removing administrative burdens and reducing transaction costs." The Plan then continues with a bucket full of ambitions: "Cutting red tape for business is a clear priority and the cumbersome and costly exequatur process that is required to recognise and enforce a judgment in another jurisdiction should systematically be consigned to history whilst maintaining the necessary safeguards. Ensuring that cross-border debt can be recovered as easily as domestically will help businesses trust our single market and *efficient insolvency proceedings can help recovery from the economic crisis* (italics by the authors). Cross-border transactions can be made easier by increasing the coherence of European contract law. Businesses are not taking sufficient advantage of the internet's potential to boost

¹⁷ European Council, The Stockholm Programme – An Open and Secure Europe Serving and Protecting Citizens (2010/C 115/01) (available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:115:0001:0038:en:PDF>).

¹⁸ Action Plan Implementing the Stockholm Programme, COM(2010) 171 final, 20.4.2010 (available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2010:0171:FIN:EN:PDF>).

¹⁹ "The European judicial area and the proper functioning of the single market are built on the cornerstone principle of mutual recognition. This can only function effectively on the basis of mutual trust among judges, legal professionals, businesses and citizens. Mutual trust requires minimum standards and a reinforced understanding of the different legal traditions and methods." (p. 4).

²⁰ Concerning e-Justice, the Stockholm Programme specifically provides for the gradual interconnection of insolvency registers (paragraph 3.4.1.).

sales: Union law can help by increasing businesses' need for legal certainty and at the same time guaranteeing the highest level of consumer protection. Consumers need to be aware of their rights and provided with access to redress in cross-border cases. Finally, the increased use of alternative dispute resolution can contribute to the efficient administration of justice.”²¹

200. What is interesting in this approach in this 2020 strategy is that it seems to contain an integrated approach, including many areas of law, such as civil procedural law, law of obligations, insolvency law, sales law, consumer law. Yet, most probably the suggestion that efficient insolvency proceedings can help recovery from the economic crisis is made within the context of cross-border judicial cooperation in insolvency cases (Article 81 TFEU). This also follows from EU Justice Commissioner Viviane Reding’s address of February 2012, setting out policies to provide the EU Insolvency Regulation with a face-lift.²²

201. We however submit that this would be much too narrow to satisfy the requirement of including “insolvency” as a true part of the legal skeleton for an internal market in the meaning of Article 114 TFEU. A design for an insolvency law that will meet the key objectives within the focus of EU policies on the longer term must in its substantial and procedural forms be brought into alignment with norms and principles which are predominant in non-insolvency law area and which may fundamentally differ from those within insolvency laws, such as in the area of securities law (rights in rem), contract law, including e.g. employment contracts, IP-contracts and contracts with consumers), company law (e.g. position of shareholders, position of management) or the rules applicable to avoidance of antecedent acts.²³

202. We recommend that a further study be undertaken to clarify the basis within the Treaties of the EU to assess the core of the provisions which could form the foundation of an “internal market insolvency law”. In our opinion this study should include further research into the present limits the Treaties may pose, such as the principles of subsidiarity and proportionality, as well as a provision like Article 345 TFEU (“The Treaties shall in no way prejudice the rules in Member States governing the system of property ownership”) and its consequences for the allocation of powers between the EU and the Member States as well as for its meaning for developing a European property law or the influence “insolvency” may have on “property”.²⁴ Such a study obviously will include research into the consequences for a suggested insolvency skeleton, which would flow from any provisions of the Charter of

²¹ Action Plan Implementing the Stockholm Programme, at p. 5.

²² Speech of Viviane Reding, Vice-President of the European Commission. EU Justice Commissioner, with the title “Taking Insolvency Law into the 21st Century to Ensure Justice for Growth”, 1st European Insolvency & Restructuring Congress, Brussels, 9 February 2012, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/12/108&format=HTML&aged=0&language=EN&guiLanguage=en>.

²³ For a start, see “The European Legal Order in Insolvency”, Chapter 11 in: Paul J. Omar, *European Insolvency Law*, Ashgate, Aldershot, England, 2004, 169ff, who includes employment law and company law.

²⁴ For an overview of an emerging European property law, see Sjeff van Erp & Bram Akkermans, *European Union property law*, in: Christian Twigg-Flesner (ed.), *The Cambridge Companion to European Union Private Law*, Cambridge University Press, 2010, 174ff.

Fundamental Rights of the European Union and the European Convention on Human Rights.²⁵

203. *Take stock.* In many areas in which the EU is competent, it has dealt with measures related to insolvency law, most prominently in excluding the winding-up of insolvent companies or other debtors, judicial arrangements, compositions and analogous proceedings in what is now the Brussels I Regulation containing the rules on jurisdiction and enforcement of judgments in civil and commercial matters. The EU Insolvency Regulation aims to fill up the gap, whilst for insolvency proceedings concerning insurance undertakings, credit institutions, investment undertakings holding funds or securities for third parties, and collective investment undertakings, which are excluded from the scope of the Insolvency Regulation, separate Directives have been produced (Directive 2001/17 for the reorganisation and winding-up of insurance undertaking and Directive 2001/24 for the same regarding banks (with measures concerning reorganisation and winding-up of (collective) investment undertakings still missing). Several years after their subsequent implementation into national legal systems it seems that time is ripe to study and analyse interpretation by courts, and any uncertainties that have been detected, to take these into account in future work. Regretfully, the number of cases is large, e.g. Icelandic banks, AA Mutual Insurance, Phoenix Kapitaldienst, Fortis, Anglo Irish Bank, Dexia, Lehman Brothers.

204. Leaving these financial institutions outside our scope, in other areas “insolvency” has been taken into account, although most likely as a topic of additional concern or not with an aim to align certain matters of “insolvency”, e.g. Directive 77/187/EC with regard to Safeguarding of Employees’ Rights in the event of Transfer of Undertakings, Directive 90/314/EC re the insolvency of a Tour Operator, Directive 97/9/EC re Investor Compensation Schemes, Directive 2000/35 with regard to Late Payments in Commercial Transactions, Directive 2000/74 on the Protection of Employees in the Event of Insolvency of their Employer (updating Directives 77/187 and 80/987), Regulation 2001/2157 with regard to the European Company Statute, in which Article 67 provides that an ECS will have the same treatment as public limited liability company set up in accordance with law of the Member State in which its registered office is situated. The aim of taking stock is to assess whether EU policies are aligned, that certain norm and terminology is consistent and whether in certain other areas similar provisions regarding insolvency could be included. Moreover, we estimate that a legal skeleton for future harmonisation of insolvency law could be inspired by the results of such a stock taking and suggest comparable provisions in certain matters in cases where the underlying ratio or approach a court has taken in its interpretation has led to satisfactory solutions.

205. *Overriding objectives.* We have provided an overriding objective for the goals of insolvency law and noted that in an international context the overriding objective is the maximisation of value and the furthering of the just administration of the proceedings, see para. 46 and 148. Most probably it will be necessary to make a distinction in the form of administering an insolvent estate, i.e. liquidation and reorganisation. Liquidation is the general name for proceedings to sell and dispose of assets for distribution to creditors in

²⁵ See the reports published in: J. Laffranque (ed.), *The Protection of Fundamental Rights Post-Lisbon: The Interaction between the Charter of Fundamental Rights of the European Union, the European Convention on Human Rights and National Constitutions*, Reports of the XXV FIDE Congress Tallinn, Vol. 1, Tallinn: Estonian Lawyers Association 2012. For a shortened version of the Dutch report, see J.H. Gerards en M. Claes, *Bescherming van fundamentele rechten post-Lissabon*, Sociaal-Economische Wetgeving (SEW), 2012, 270ff.

accordance with the applicable (national) insolvency law.²⁶ A “reorganization” is the process by which the financial well-being and viability of a debtor’s business can be restored and the business continue to operate, using various means possibly including debt forgiveness, debt rescheduling, debt-equity conversions and sale of the business (or parts of it) as a going concern. This is the term used in the UNCITRAL Legislative Guide²⁷, which formulates a “reorganization plan” (or: plan of reorganization) as thus a plan by which the financial well-being and viability of the debtor’s business can be restored.²⁸

206. In both methods of administration it is possible that a debtor in Member State A possesses assets in other Member States, such as real estate in Member State B, non-registered movables (machinery) in Member State B, non-registered means of transport or goods in transit in Member State C, registered movables listed in the Member State D, which holds the registry, shares in subsidiaries, incorporated in Member States E, F and G and so on. A challenging task is to devise a system in which creditors of similar categories receive an equal treatment. Would it be possible to create a European legal instrument providing a certain specific security, for fresh money that has been borrowed in certain well defined situations of financial distress?

207. In para. 9 we made some critical remarks about the European Parliament’s unsubstantiated statement that “insolvency law should be a tool for the rescue of companies at Union level”. We observed that indeed insolvency law can have as a goal the possibility to allow an insolvent debtor a fresh start or a business rehabilitation, to save for instance the value of the ongoing enterprise and/or as many of the workforce as possible. Where so many interests are at stake (contractual position of providers of goods and services, the interests of clients or customers in the uninterrupted provision of goods or services, continuity of jobs and carrying on of payments to the state of e.g. company taxes and VAT), further study would be able to clarify what “the rescue of companies at Union level” really implicates. The implications relate to two areas of assessment: (i) the influence of “opening of “rescue” on pre-existing rights, as well as (ii) the consequences of “rescue” ex post.

208. In the first area (i) the basis assumption of some 15 years ago – as laid down in Recital 11 of the EU Insolvency Regulation – has to be analysed whether it still holds that due to the fact “that as a result of widely differing substantive laws it is not practical to introduce insolvency proceedings with universal scope in the entire Community”, with as given examples “the widely differing laws on security interests” and “the preferential rights enjoyed by some creditors in the insolvency proceedings are, in some cases, completely different.”

209. In this second area (ii) it may very well be that the debate will concentrate on questions such as (a) the necessity of the requirement of an impending insolvency, (b) which interests to take into account for such a rescue, (c) the (possible) rights and duties the holders of these interests have during the process of negotiation of a reorganisation plan (which is, in its core, a multi-party agreement), and (d) the relative contexts between these interests. Such a debate will have to assess too the criteria to use to come to the result that maximisation of value indeed can be successfully achieved compared to the estimated result of a form of piece meal

²⁶ Compare UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”.

²⁷ UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”. UNCITRAL Practice Guide (2009), under B “Glossary”, in “2. Terms and explanations”.

²⁸ UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”. UNCITRAL Practice Guide (2009), under B “Glossary”, in “2. Terms and explanations”.

liquidation of assets, whilst the requirement of the furthering of the just administration of the proceedings should include measures to create and guard the right of unsecured creditors, mostly small businesses or consumers, to receive information timely and a level of involvement of these creditors in the furthering of such a rescue. These matters clearly need the input of non-insolvency specialists, such as corporate and contract lawyers (e.g. for creating rules for a Debt-Equity-Swap, a (partly) conversion of a contractual creditors-position into a shareholders-position), contract and trade lawyers (e.g. for such activities as the trade in poor claims, e.g. Non Performing Loans), corporate and financial lawyers (to discuss the desirability of rules applicable to the relation of the distressed debtor and certain reorganisations specialists, such as Private-Equity Funds) or employments and pension lawyers (for the rights and duties regarding termination or continuation of employment as well as the ramifications on pension rights or other retirement benefits).²⁹

210. *Flexible legislation.* Any regulation or rules of governance for these complex, multi-disciplinary and sometimes cross-border insolvency issues is to be dealt with in an efficient and predictable way. These last requirements many times flow from the very nature of a financial distressed position. Individual legal measures as well as the full legal skeleton of such measures should, on the other hand be sufficiently flexible and capable of adapting to changes in circumstances and market conditions in which businesses operate. The inherent tension between “predictability” and “flexibility” will result in including discretionary powers, both for insolvency office holders as well as for a court involved. The legal skeleton may not only lead to hard law measures, but certainly – as a result of the quite ordinary way of creating (international) insolvency law in the last two decades – include (European) insolvency soft law instruments. It should therefore be assessed which topics call for which legal measure as well as whether some results may be better achieved with soft law alternatives.³⁰

211. Here we provide the example of a “protocol”. During the last two decades in several cases the experience has been that existing legislation, or the lack of it or its conflicting rules have resulted in efforts of insolvency practitioners to negotiate and tailor-make specific, *ad hoc* solutions, many times including the approval of the courts involved. This development has led to the use of an instrument called “protocol” or cross-border insolvency agreement. In his inaugural lecture of 2008 Wessels has submitted that the stage of a non-binding recommended approach of working with protocols could be regarded as the *Lex Mercatoria* in international insolvency cases. He posed the question whether the experience that several parts of such protocols as these were applied in international practice seem to reflect a certain pattern, these could now be regarded as “customary international law” and therefore in terms of international public law could have the status of a source of law within the meaning of Article 38 of the Statute of the UN International Court of Justice.³¹ He concluded however

²⁹ For an overview of interests and how these should be taken into account, see Vanessa Finch, *Corporate rescue: Who is Interested?*, *Journal of Business Law* 2012, Issue 3, 190ff. For related topics, see Alan Kornberg and Sarah Paterson, *Out-of-Court vs Court-Supervised restructurings*, in: Rodrigo Olivares-Caminal et al., *Debt Restructuring*, Oxford University Press 2011, 35ff.; Reinhart Bork, *Rescuing Companies in England and Germany*, Oxford University Press, 2012.

³⁰ On such matters as fragmentation, coherency and integration of a interlocking, multifaceted legal order, see Roger Brownsword et al. (eds.), *The foundations of European private law*, Oxford: Hart, 2011.

³¹ Article 38:

1. The Court, whose function is to decide in accordance with international law such disputes as are submitted to it, shall apply:

that the merit of a protocol lies in the individuality of every case and the necessity to resolve practical matters. These observations more recently have found support in countries such as Brazil³² and Australia.³³

212. In a European context, especially in German literature, the debate is rather ongoing about the hybrid legal nature (contractual, procedural) of a protocol concluded between insolvency office holders in different jurisdictions (concluded in their “public” function, resulting in a “public law” contract?) and the way such a protocol can be arranged into German (insolvency) law.³⁴ In literature published in the Netherlands similar questions have been raised: can a cross-border insolvency agreement arrange for provisions which are contrary to the mandatory rules that apply to each of the insolvency office holders? Can it be enforced to the whole body of creditors? Which rules apply when such an agreement is countersigned by the court? Is the legal context of mutual duties so strong that it also establishes a claim from one insolvency office holder versus the other in main and secondary proceedings to indeed conclude such an agreement? Will an agreement in itself be binding also against third parties who are not a creditor?³⁵ We note that the Rome I Regulation on the law applicable to contractual obligations, in addition to allowing for a specific choice of law, “..... does not preclude parties from incorporating by reference into their contract a non-State body of law or an international convention.”³⁶ It could be debated whether such a reference could be made, for instance, to the “Principles of European Contract Law”. In general a “reference” has to be understood as a reference to substantial law and not the provisions of conflict-of-laws. So such a reference can not deviate from mandatory provisions determined by the law, which has been indicated by objective conflict-of-law rules.³⁷ Without doubt, a “protocol” or a cross-

a. international conventions, whether general or particular, establishing rules expressly recognized by the contesting states;

b. international custom, as evidence of a general practice accepted as law;

c. the general principles of law recognized by civilized nations;

d. subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law.

2. This provision shall not prejudice the power of the Court to decide a case *ex aequo et bono*, if the parties agree thereto.

³² See Francisco Satiro and Paulo Fernando Campana Filho, Transnational insolvency: Beyond state regulation and towards cooperation agreements, <http://ssrn.com/abstract=1858968>, signalling that developments in both pragmatic and academic fields “..... have been valuable in the construction of a contract-driven transnational law of international insolvencies which is much more resourceful and customizable than “hard law” mechanisms could ever envision – and, therefore, more suitable for facing the challenges imposed by the failure of companies scattered over an unpredictable, multifaceted, globalized world.”

³³ See Rosalind Mason, Cross-border Insolvency and Legal Transnationalisation, 21 *International Insolvency Review* 2012, 105ff, concluding that CBI (Cross-border Insolvency Agreements) may well prove to be one of the most useful strategies for resolving complex CBI issues.

³⁴ Most recently see Moritz Becker, *Kooperationspflichten in der konzerninsolvenz*, Beiträge zum Insolvenzrecht, RWS Verlag Kommunikationsforum, 2012, 109ff.

³⁵ See Bob Wessels, Cross-border insolvency agreements: what are they and are they here to stay?, in: N.E.D. Faber, J.J. van Hees, N.S.G.J. Vermunt (red.), *Overeenkomsten en insolventie*, Serie Onderneming en Recht, deel 72, Deventer: Kluwer 2012, 359ff.

³⁶ Recital 13.

³⁷ See P. Vlas, *Alle contracten leiden naar Rome I*, Weekblad voor Privaatrecht, Notariaat en Registratie (WPNR) (2009), 6824; S. van Dongen and A.P. Wenting, *Europa en internationale overeenkomst. EVO wordt*

border insolvency agreement now is at the forefront of creating a workable solution in many complex matters, some of which we have described above. If the use of protocols is the preferred way to go forward, this will arouse another set of legal problems and discussions as for instance to the law applicable. We recall that legislation in Slovenia and in Greece already makes reference to such an instrument. It is submitted that it should be discussed, within a European context, to start to think about “Principles for Insolvency Protocols”, to at least prevent some of the disputes and to create a certain level of predictability and certainty in an area which in itself is interesting, but not without problems. It goes without saying the participants to the debate certainly will include non-insolvency specialists.

213. *Need for action.* Any topic that is a candidate for a form of regulation must be based on the real necessity for such regulation. Efficiency as such is not a very convincing argument as a cause for harmonization. We strongly feel that any development towards greater convergence should be supported by solid study and open exchange of ideas and a genuinely transparent dialogue. This would include the rationale or the specific need for a certain action or legislative intervention, and if so, what is the most suitable course of action (“top down” or “bottom up” regulation) and in the “bottom up” approach the clear inclusion of a wider group that will have to work with the results of such action. As indicated in para. 99, the regulation of the profession of insolvency office holders is based on the desirability of maintaining the confidence of creditors and the general public in the key role players in insolvency matters. A “bottom up” approach will also open the doors to surprising sources for further consideration, such as the work of the European Bank for Reconstruction and Development (EBRD), which is working alongside the Serbian Bankruptcy Supervisory Authority (BSA) on a project to improve the regulation, supervision and discipline of insolvency administrators.³⁸ The result coming from said dialogue could well be a set of non-binding best practices for insolvency office holders (either appointed in purely national cases or in cases to which the EU Insolvency Regulation applies) and could include a “comply or explain” mechanism, either for individuals which are candidates for appointment or a countries’ association (or associations) for such professionals.³⁹

214. Finally: *Balance.* Any rule within the envisaged legal skeleton should be based on a fair balance between the (often competing) interests of creditors and other parties concerned. We provide one example, the position of secured creditors in situations of “rescue” or “insolvency”. Article 5(1) of the EU Insolvency Regulation, reads: “The opening of insolvency proceedings shall not affect the rights in rem of creditors or third parties in respect of tangible or intangible, moveable or immovable assets - both specific assets and collections of indefinite assets as a whole which change from time to time - belonging to the debtor which are situated within the territory of another Member State at the time of the opening of proceedings.” A majority in literature follows the so-called “hard and fast”-rule. The opening

Rome I, Nederlands Tijdschrift voor Burgerlijk Recht (NTBR) 2009/3, 82ff, both referring to non-Dutch literature.

³⁸ Together EBRD and BSA prepared a revised National Standards and Code of Ethics applicable to insolvency administrators in Serbia, adopted in early 2010. Both organisations have prepared a set of technical guidance notes designed to assist insolvency administrators, judges and the BSA in understanding and implementing the new National Standards and Code of Ethics, also published in 2010. See http://www.ebrd.com/pages/sector/legal/insolvency/legal_framework.shtml.

³⁹ We will not further deal with topics such as supervision of these professionals or installing a complaints proceedings, either nationally or e.g. for insolvency practitioners which work under the application of the EU Insolvency Regulation on a European level.

of insolvency proceedings in Member State A does not affect whatsoever the right in rem on a insolvent debtor's assets located in Member State B, although it is fully acknowledged that this treatment given to holders of rights in rem in Article 5(1), leads to "excessive" overprotection⁴⁰ or is – against the background of the strong rise in Europe of rescue of reorganisation methods and proceedings during the last decade – regarded as a "conceptual failure of the Regulation."⁴¹ which lead to a territorial split of the assets between these Member States, which is detrimental to its value⁴², and to the sheer impossibility for the insolvency office holder in the main insolvency proceedings, opened in Member State A, to administer the estate⁴³ or to implement a European wide rescue plan.⁴⁴ To find a right balance between the interests of the estate (including all unsecured creditors) and secured creditors abroad seems to be to include measures to prevent the creation of the unjustifiable bonus, only due to the internationality of the case for secured creditors in cross-border insolvencies. It does not do justice to the balance that in national insolvency laws is sought between the interests of the secured creditor on the one hand and the interests of the estate (and the unsecured creditors) on the other. Within the context of the Insolvency Regulation it seems appropriate to discuss as a solution to apply (in Member State B) the *lex rei sitae* (the insolvency law of the Member State in which the secured assets are located), therefore to confine the unlimited powers of a holder of a right in rem. But does such a solution in this (limited) cross-border context provide the right balance? Are secured creditors not overly protected on the whole, in legislations which have excluded or protected financial creditors from any consequences of insolvency? In 2007, Verougstraete (Chairman of the Belgian Court of Cassation) chastised the present state of such legal systems, characterising these as unreasonable and submitting that Europe deserves a new approach of collective insolvency proceedings. Here too securities law and insolvency law should walk hand in hand to find a fair balance.⁴⁵

215. After a wide-ranging survey of the background to what we present as key indicators for a future legal skeleton of insolvent law, it is time to shut down the computer. One fact is undeniable: harmonisation of insolvency law in Europe is on the political agenda.⁴⁶ What should now be the most preferable approach? We consider it as of use to take a step back. In

⁴⁰ Thus e.g. Philip Smart, Rights in Rem, Article 5 and the EC Insolvency Regulation, in: 15 International Insolvency Review, Spring 2006, Issue 1, 17ff; P.M. Veder, *Goederenrechtelijke zekerheidsrechten in de internationale handels- en financieringspraktijk*, in: R.W. Clumpkens et al., *Zekerhedenrecht in ontwikkeling*. Preadvies voor de Koninklijke Notariële Broederschap 2009, 307ff., at 309.

⁴¹ "...ein konzeptioneller Fehler der Verordnung" thus S. Reinhart, *EuInsVO*, in: Münchener Kommentar Insolvenzordnung, Band 3, 2. Auflage, München: Verlag C.H. Beck, 2008, Art. 5, nr. 14.

⁴² See Nina Scherber, *Europäische Grundpfandrechte in der nationalen und internationalen Insolvenz im Rechtsvergleich*, Europäische Hochschulschriften, Vol. 3865, Frankfurt am Main: Peter Lang, 2004, p. 147ff.

⁴³ Reinhart, o.c., Art. 5, 14; Sageart, review of Veder, o.c., in *Weekblad voor Privaatrecht, Notariaat en Registratie (WPNR)* 6812 (2009).

⁴⁴ Alexander Plappert, *Dingliche Sicherungsrechte in der Insolvenz*, Schriften zum Insolvenzrecht, Band 21, Baden-Baden 2008, 264.

⁴⁵ Ivan Verougstraete, *Insolvabiliteit en zekerheden. 200 jaar Wetboek van Koophandel*, in: A. Bruyneel et al., *Bicentenaire du Code de Commerce – Tweehonderd jaar Wetboek van Koophandel*, uitg. Larcier, Brussel, 2007, 233ff, and the response to Verougstraete's report by Bob Wessels, *Europe Deserves A New Approach To Insolvency Proceedings*, in: A. Bruyneel et al., *Bicentenaire du Code de Commerce – Tweehonderd jaar Wetboek van Koophandel*, uitg. Larcier, Brussel, 2007, 267 et seq.

⁴⁶ T.M. Bos, *Herziening van de Europese Insolventieverordening. Gedeeltelijke harmonisatie als wenkend perspectief?*, *Nederlands Tijdschrift voor Handelsrecht* 2012-3, 138ff.

the introduction it was signalled that “harmonisation” and “insolvency law” for many centuries have been an awkward couple. A first observation for a future agenda is that insolvency lawyers should learn from the legislative process of the “Europeanisation” of contract law.⁴⁷ This process is still ongoing, but the first resolutions of the European Parliament date from over 20 years back. Would it be feasible and desirable to work with a system of “options” in addition to existing norms within insolvency?⁴⁸ We feel that learning from successes and mistakes made in comparable processes may be beneficial for the drafting of any future agenda in this field.⁴⁹

216. Secondly, we feel that what is needed for this first step in this area of harmonisation of law is genuine European legal scholarship, based on historic and comparative study, therefore too the establishment of multi-jurisdiction groups of researchers and practitioners.⁵⁰ The technique to be followed would reflect what earlier in the Report has been described as the Open Method of Coordination (OMC) which in addition to the use of the more traditional hierarchic forms of legislation, allows the use of other instruments (soft law). The OMC method includes certain common goals and the means to learn from one another how these goals should be achieved, which also take into account the development and spreading of best practices in an aim to achieve greater convergence towards the main EU goals. Where “harmonisation” of “insolvency law” in its combination will deal with complex, politically sensitive policy areas which involve a great degree of uncertainty as to which solution will achieve the results desired, the OMC could become the method of choice.⁵¹

What the next step will be is to be awaited. Our recommendations seem modest, but in the light of history and the experience of any process of reviewing insolvency legislation they seem sensible to us, meaning by baby steps.⁵² Any grand achievement begins with a leap of faith and every 10 mile walk with a first step. *Dimidium facti, qui coepit, habet.*⁵³

⁴⁷ For a (repeated) call to include property law in the debates on the future shape of European private law, see Sjef van Erp, Arthur Salomons, Bram Akkermans (eds), *The Future of European Property Law*, Munich: Sellier european law publishers, 2012.

⁴⁸ For instance the possibility of introducing an “option” of a “European Rescue Plan”, for instance for the proposal of a plan covering a parent company and one or more subsidiaries incorporated in different Member States, as suggested in the INSOL Revision Report 2012, Chapter VI (The European Rescue Plan), 101ff.

⁴⁹ For a comparable view (“Can administrative lawyers learn form private lawyers?”), Jan H. Jans, *Towards a Draft Common Frame of Reference for Public Law*, <http://ssrn.com/abstract=1970307>.

⁵⁰ In this way for the process of “Europeanisation” of contract law Reinhard Zimmerman, *The Present State of European Private Law*, 57 *The American Journal of Comparative Law*, Spring 2009, 479ff.

⁵¹ See Jans, o.c., at 15. For an approach to draft “good” legislation, see Helen Xanthaki, *Technical Considerations in Harmonisation and Approximation: Legislative Drafting Techniques for Full Transposition*, in: Mads Andenas and Camilla Baasch Andersen (eds.), *Theory and Practice of Harmonisation*, Cheltenham: Edward Elgar, 2011, 536ff.

⁵² See for instance S. Block-Lieb and T. Halliday, *Incrementalism in Global Lawmaking*, Paper presented at the symposium ‘Bankruptcy in The Global Village – The Second Decade’, in: 32 *Brooklyn Journal of International Law* 2007, 851-903.

⁵³ Horace, *Epistles*, Book I, Ep. 2, l. 40 (Freely translatable as: “Well begun is half done”, or alternatively: “Once you’ve started, you’re halfway there”).