X-Part II-Memo06

Article 18. Effects of insolvency proceedings on pending lawsuit or arbitral proceedings

The effects of insolvency proceedings on a pending lawsuit or pending arbitral proceedings concerning an asset or a right of a debtor's insolvency estate shall be governed solely by the law of the Member State in which that lawsuit is pending or in which the arbitral tribunal has its seat.

[10711] Article 18 EIR 2015 differs in two aspects from the text in its near equivalent in Article 15 EIR 2000. Although it has been reported that in Member States '… no serious problems' have been raised in the context of Article 15 EIR 2000, and there would be no urgent need in this respect to amend Article 15 EIR 2000, it has been submitted that it would be rather easy and advisable to '… simply add the words 'or an arbitration proceedings' to the article', see Pfeiffer, in: Heidelberg-Luxembourg-Vienna Report (2013), nr. 856. It flows from the following commentary that the characterisation 'no serious problems' is a rather innocent view of some fifteen years of development. The suggestion made is reflected in Article 18. The present words '… a debtor's insolvency estate' replace wording which referred to a debtor that had been divested. These words reflect the wider scope of insolvency proceedings under the EIR 2015. The present Article 18 EIR 2015 has been introduced with firm, but not very substantiated words, see recital 73 to the EIR 2015: 'The law applicable to the effects of insolvency proceedings on any pending lawsuit or pending arbitral proceedings concerning an asset or right which forms part of the debtor's insolvency estate should be the law of the Member State where the lawsuit is pending or where the arbitration has its seat. However, this rule should not affect national rules on recognition and enforcement of arbitral awards.'
Distinguishing between individual enforcement proceedings and pending law suits. The Virgós/Schmit Report (1996), nr. 142, explains that the Regulation of 2000 distinguishes between the effects of the insolvency proceedings on individual enforcement proceedings and those on pending lawsuits. The effects on individual enforcement actions are governed by the *lex concursus* (see Article 7(2)(f) EIR 2015) and therefore the collective insolvency proceedings may stay or prevent any individual enforcement action brought by a creditor against the debtor's assets. Such individual enforcement actions may include attachment, sequestration and execution. However, the effects of the insolvency proceedings on other legal proceedings concerning an asset or a certain right of the estate are governed by the law of the Member State where such proceedings are pending, see Article 18. This *lex fori processus* is decisive in determining the 'effects of insolvency proceedings' on a lawsuit pending. These effects may result from the opening of insolvency proceedings, but also could be related to the continuation, conduct, conversion or termination of these proceedings. The procedural law of the latter State shall, according to the Report, decide whether or not the proceedings are to be suspended, how they are to be continued and whether any appropriate procedural modifications are needed in order to reflect the loss or the restriction of the power of disposal or the right to litigate (or continue litigation) by the debtor and the possible intervention of the insolvency practitioners, if appointed. Late 2016 the CJEU has clearly confirmed this division between individual enforcement and law suits pending, see CJEU 9 November 2016, C-212/15 *(ENEFI Energiahatékonysági Nyrt v Directia Generala Regionala a Finantelor Publice Brasov (DGRFP)* [2016] All ER (D) 110 (Nov), which observes (para. 34) that it would be contradictory to interpret Article 15 EIR 2000 as also covering enforcement

proceedings, with the consequence that the effects of the opening of insolvency proceedings would thus come within the scope of the law of the Member State in which such enforcement proceedings are pending, while, in parallel, Article 20(1) EIR 2000 (now Article 23 EIR 2015), by explicitly requiring to return to the liquidator of everything obtained 'through enforcement', would render Article 15 ineffective: '35 Consequently, it is necessary to find that enforcement proceedings do not come within the scope of application of Article 15' of the EIR 2000.

Article 18 EIR 2015 is irrelevant for the main proceedings. Order of the CJEU (Sixth Chamber) 7 November 2013, case C-371/13 (*SC Schuster & Co Ecologic SRL v Direcţia Generală a Finanţelor Publice a Judeţului Sibiu - Activitatea de Inspecţie Fiscală*) decides that Article 15 EIR 2000 is clearly not relevant for the decision in the main insolvency proceeding, as the article contains a rule for determining the law applicable in the event of a conflict between the laws of different Member States. The case at hand is only governed by Romanian law, the applicability of which is not disputed.

In the Netherlands, following the suggestion in the Report, Articles 32 *Fw* and 231a *Fw* were enacted as of 15 November 2003, providing, in general, that Articles 27–31 *Fw* (a set of rules concerning the influence of Dutch insolvency proceedings to pending lawsuits) apply equally to foreign main insolvency proceedings, if these are to be characterised as winding-up proceedings in the meaning of Article 2(c) EIR 2000, resulting in the liquidation of assets in the Netherlands. These provisions have been applied by Court of Appeal Amsterdam 25 August 2005, *NPIR* 2006/208, on a pending lawsuit ('*lopende rechtsvordering*') concerning an insolvent French company. The present text of Article 18 will necessitate a reconsideration of these provisions in the Dutch Bankruptcy Act.

No '*vis attractiva concursus*'. This principle generally provides that all pending litigation should fall under the exclusive authority of the insolvency court. One purpose of the provision of Article 18 is to avoid the application of the rule of *vis attractiva concursus* which sometimes applies under the law of Member States pursuant to which pending lawsuits may be removed from the civil or commercial court in which they are pursued into the exclusive control of the relevant court (commercial court dealing with insolvency cases or an insolvency court). The Regulation therefore does not adopt a general rule of *vis attractiva concursus*, see Virgós/Garcimartín (2004), nr. 82; Garašić (II, 2005), 132. Another purpose of Article 18 is to prevent that the court, for which the lawsuit is pending, has to assess and test foreign insolvency procedural law, with which this court usually will be unfamiliar. In stead of having to act like that, the court can apply its own procedural law, see e.g. Court (*Oberlandesgericht*) Cologne 17 October 2007, *ZIP* 48/2007, p. 2287ff. The rationale for Article 15 EIR 2000 is that '... domestic procedural law will not be disrupted (*überlagert*) by applying foreign procedural law', thus Wimmer (2006), p. 2317. Article 18's ultimate goal is to guarantee procedural clarity and certainty, see Dammann, in: Pannen (ed.) (2007, Art. 15, nr. 4; Müller, in: Mankowski/Müller/J.Schmidt (2016), Art. 18, nr. 3.

On the legal status of an English administrator in a German proceeding, see Schmitt (2009).

[10712] The scope of application of Article 18 EIR 2015 (leaving for the moment arbitration proceedings aside) is restricted as a consequence of the elements contained in its text. These are:

a. the 'effects of insolvency proceedings';
b. on a 'lawsuit pending';
c. 'concerning an asset or a right which forms part of a debtor's insolvency estate';

d. shall be 'governed solely';
e. by the law of the Member State in which that lawsuit is pending.
I will make some comments regarding these elements.

The provision is to be seen as a '… narrowly circumscribed exemption in favour of the *lex fori.* All remaining issues are left to the *lex concursus',* thus Torremans (2002), p. 187. It is generally accepted that the elements that form the text of (now) Article 18 should be interpreted or construed autonomously, without making a reference to a national legal system. See for instance Austria Supreme Court 17 March 2005 (8Ob131/04d); Duursma-Kepplinger (2002), Art. 15, nr. 15; Dammann, in: Pannen (ed.) (2007), Art. 15, nr. 8; Bork, in: Bork/Mangano (2016), 4.119. Only Paulus (Paulus (2006), p. 191) seems to defend the application of the *lex fori processus*. The *lex concursus* however is decisive with regard to the question of what qualifies as an 'asset' or a 'right', see Article 7(2)(b). In this way Austria Supreme Court 17 March 2005 (8Ob131/04d) and Austria Supreme Court 24 January 2006 (10Ob80/05w). See also Duursma-Kepplinger (2002), Art. 15, nr. 9: Virgós/Garcimartín (2004), nr. 258; Dammann (2007), Art. 15, nr. 7. I will now shortly analyse said elements.

[10712a] *(a) The effects of insolvency proceedings.* The *lex fori processus* is decisive in determining the 'effects of insolvency proceedings' on a lawsuit pending. These effects may result from the opening of insolvency proceedings, but could also be related to the continuation, conduct, conversion or termination of these proceedings. The form in which a lawsuit pending is to be continued, interrupted, postponed or stayed and any procedural changes to apply is solely determined by the *lex fori processus*, thus Austria Supreme Court 23 February 2005 (9 Ob 135/04z) and Austria Supreme Court 24 January 2006 (10Ob80/05w). District Court Munich 2 October 2012, *NZI* 24/2012, 1028, explains that French insolvency proceedings only will have effect when according to German law these proceedings are opened by a formal court decision or when in the decision opening these proceedings the power of the debtor to divest and to litigate has been transferred to a preliminary insolvency practitioner.

[10712b] *(b) A* '*lawsuit pending*'. The word 'pending' will in essence mean that the plaintiff has concluded all necessary actions he must take for the commencement to the institution of the proceedings prior to the date of the opening of insolvency proceedings, see Duursma-Kepplinger (2002), Art. 15, nr. 15; Virgós/Garcimartín (2004), nr. 259; Bork, in: Bork/Mangano (2016), 4.119. The (pending) lawsuit can involve proceedings to which the (now insolvent) debtor acts as a claimant or as a defendant (Duursma-Kepplinger (2002), Art. 15, nr. 20). It covers for instance declaratory actions and provisional remedies, as well as the enforcement of a tax claim, initiated by a foreign tax authority, see the German Federal Fiscal Court 9 February 2015, *NZI* 16-17/2015, 691. The word 'pending lawsuit' excludes lawsuits commenced after the opening of insolvency proceedings (which will by subject to a stay or any other measure resulting from applying the *lex concursus*) and individual enforcement actions, such as attachment and execution, a view adopted by CJEU 24 October 2013, Case C-85/12, ECLI:EU:C:2013:697 (*LBI hf v Kepler Capital markets SA*), interpreting Article 32 Directive 2001/24, which uses similar words as Article 15 EIR 2000, see Moss/Fletcher/Isaacs (2016), 8.273 et seq.

[10712c] *(c) Concerning* '*an asset or a right which forms part of a debtor's insolvency estate*'. The application of Article 18 is limited to an asset or a right which forms part of a debtor's insolvency estate. Article 15 EIR 2000 was limited to '... a lawsuit pending concerning an asset or a right of which the debtor has been divested'. As indicated, the

new version reflects that divestment of a debtor is not a requirement for the applicability of the Regulation. The limitation to an asset or a right forming a part of the debtor's estate makes it necessary, before applying the *lex fori processus*, to apply the *lex concursus* to answer that question. See also Bork, in: Bork/Mangano (2016), 4.117. See Article 7(2)(b) EIR 2015. If an asset is excepted from the effects of the insolvency proceedings Article 15 EIR 2000 is not applicable. See Fletcher (2005), 7.118; Dammann, in: Pannen (ed.) (2007), Art. 15, nr. 6; Mélin (2008), nr. 244. See too High Court of Ireland 27 july 2005, [2005] *IEHC* 274 (*Flightlease Ireland Ltd.*), considering that Article 15 EIR 2000 is not generally applicable to lawsuits pending, but only to those '… concerning an asset or a right of which the debtor has been divested', concluding: 'There is no suggestion, ... that in the case of other proceedings ... a similar principle applies'. In my opinion the phrase 'concerning an asset or a right of which the debtor has been divested' means that the lawsuit, in order to fall within the Article 15 EIR 2000 exception, has to concern some claim or proprietary right in or over an asset of the estate or at least a property of which it can be said that the debtor has been divested of or respectively of which he is restricted or will have lost the power of disposal and administration. See Mélin (2008), nr. 244. I agree with Bork, in: Bork/Mangano (2016), 4.122., that its meaning may even be more concentrated, ie that the lawsuit in some way affects the asset or the right. This opinion also is valid under Article 18 EIR 2015. This view, however, was rejected in Court of Appeal (Civil Division) 9 juli 2009 [2009] *EWCA* Civ 677 (*Josef Syska q.q. v. Vivendi Universal S.A. and others*), commented below (para. 10712h). Contrary to the clear text of recital 73 and the wording of Article 18 EIR 2015 Moss/Fletcher/Isaacs (2016), 8.611 et seq., submit that by removing in Article 18 the reference to divestment, and making an express reference to the debtor's insolvent estate, Article 18 does not continue the 'limitation' referred to above. A proceeding concerning the question whether indeed an asset is excluded could result in a circle: has the court in the main insolvency proceedings international jurisdiction (Article 7(2)(b) EIR 2015) or will it be decided by the court that decides on Article 18 EIR 2015. German and Austrian authors favour the latter solution, see Duursma-Kepplinger (2002), Art. 15, nr. 10; Dammann, in: Pannen (ed.) (2007), Art. 15, nr. 7; Müller, in: Mankowski/Müller/J.Schmidt (2016), Art. 18, nr. 16.

[10712d] *(d) Shall be* '*governed solely*'. All questions concerning possible effects of the main insolvency proceedings are governed solely, therefore exclusively, by the *lex processus*. The *lex processus* is decisive in respect of all procedural matters in pending lawsuits, irrespective of the *lex concursus* (of the main insolvency proceedings) provisions concerning the continuance of proceedings or the ability of the debtor to litigate with respect to the transfer of this power to the main liquidator, thus Austria Supreme Court 17 March 2005 (8Ob131/04d) and Austria Supreme Court 24 January 2006 (10Ob80/05w). In this way also Duursma-Kepplinger (2002), Art. 15, nr. 21.

[10712e] *(e) By the law of the Member State in which that lawsuit is pending.* The *lex fori processus*, in the meaning of Article 18, determines the law applicable to the pending lawsuit. The lex fori processus includes references to specific substantive law provisions (Duursma-Kepplinger (2002), Art. 15, nr. 6; Dammann, in: Pannen (ed.) (2007), Art. 15, nr. 11) and the relevant provisions could be these contained in procedural as well as in insolvency law (Dammann, in: Pannen (ed.) (2007), Art. 15, nr. 12); Mélin (2008), nr. 244.

[10712f] As submitted, when explaining the exclusions to the general conflict of laws rules of the applicability of the lex concursus (Article 7(1) EIR 2015), the Virgós/Schmit Report (1996), para. 92, account for their justification, namely 'To protect legitimate expectations and the certainty of transactions in Member States other than that in which proceedings are opened'. See also recital 67, second paragraph, to the EIR 2015. Where it is clear that another choice of law rule (other than the *lex concursus*) has been made (see Articles 11, 12, 13, 14, 17 and 18 EIR 2015) to following applies: 'In such cases, the effects to be given to the proceedings opened in other ... States are the same effects attributed to a domestic proceedings of equivalent nature (liquidation, composition, or reorganization proceedings) by the law of the State concerned ...'. 'The procedural law of the latter State shall decide ... whether any appropriate procedural modifications are needed in order to reflect the loss or the restriction of the power of disposal and administration of the debtor and the intervention of the liquidator in his place', see the Virgós/Schmit Report (1996), para. 142.

[10712g] *Arbitration.* From its heading and its clear words, Article 18 also applies to 'pending arbitral proceedings': the effects of insolvency proceedings on pending arbitral proceedings concerning an asset or a right of a debtor's insolvency estate shall be governed solely by the law of the Member State in which the arbitral tribunal has its seat.

[10712h] The inclusion of 'arbitral proceedings' has been welcomed in literature, see e.g. Bork, in: Bork/Mangano (2016), 4.117 et seq.; Müller, in: Mankowski/Müller/J.Schmidt (2016), Art. 18, nr. 11. Under Article 15 EIR 2000 the position of arbitration was unclear. See the previous edition of this work, para. 10712g, and for general discussion of this topic, see Sentner (2006); Lazić (2011); Pfeiffer (2011); Vorburger (2014), 397ff and 512ff; Bramford and Woods (2016). In a much discussed case indeed 'arbitration' was regarded to fit within the scope of Article 15 EIR 2000, see Court of Appeal (Civil Division) 9 juli 2009 [2009] EWCA Civ 677 (*Josef Syska q.q. v. Vivendi Universal S.A. and others*), commented by Fletcher, *Ins. Intel.* 2009, 155ff.; Sjostrand, *CR&I* December 2009, 249ff; Willson, *ICR* 2009, 388ff. See too Veder, *FIP* 2009, 54ff. The case itself demonstrates well the uncertainly that existed as well as the arguments used in the debate whether Article 15 EIR 2000 covered 'arbitration'.

In this case a liquidator (Joseph Syska) of a Polish insolvent company has to deal with a pending arbitration in London. In appeal he submits, in the words of Longmore L.J.: '… where an arbitration is proceeding in one Member State of the European Union and one of the parties to the reference becomes insolvent in another Member State, are the consequences of that insolvency, in so far as they affect the arbitration, to be determined by the law of the Member State where the insolvency proceedings have been instituted or the law of the Member State in which the reference is taking place?' Lord Justice Longmore considers: '… it is not difficult to see why pending lawsuits should be excluded from the general application of the lex concursus; a lawsuit (including a reference to arbitration) becomes necessary when there is a need to determine the existence or validity of a particular claim which (if valid) will then be permitted to participate in the insolvency proceedings. Until the validity of that particular claim is ascertained, it has no status in or relevance to the insolvency proceedings at all. If, moreover, a legal action has been begun or a reference to arbitration has been constituted in a Member State other than that in which the insolvency proceedings have been opened, it is natural and understandable that

it should be the law of that Member State where the legal action has begun or the reference to arbitration is taking place which should determine whether that action or that reference should be continued or discontinued. Of course, if no claim has been initiated before insolvency proceedings are opened, it is entirely appropriate that the lex concursus should determine how any subsequent litigation or arbitration should proceed. But if litigation or arbitration has begun before insolvency occurs the natural expectation of businesses would be that it should be that law that should determine whether the proceedings should continue or come to a shuddering halt.' Longmore L.J. finds support for his view in recital 23 and 24 of the EIR 2000: 'The phrase "to protect legitimate expectations and certainty of transactions" is, in my view, apt to include the expectation of businessmen that lawsuits (in which considerable sums of money may have been invested) should come to an appropriate conclusion'. Longmore L.J. refers to some passages from the Virgós/Schmit Report ('the authority of that Report which is generally regarded as an aid to the interpretation of the Regulation') and the book of Virgós and Garcimartin, referred to above. His conclusion is: 'Thus, when one is able to draw breath, it is apparent that both the Official Report and the leading text book on the Regulation support the view that, for good reason, the question whether pending lawsuits should be continued or discontinued in the light of insolvency is to be determined by the law of the State in which those proceedings are pending.' The specific issue in the Elektrim/Vivendi case, however, was that the *lex concursus* (Polish law) contained an Article 142 of the Polish Bankruptcy and Reorganisation Law, which provided: 'Any arbitration clause concluded by the bankrupt shall lose its legal effect as at the date bankruptcy is declared and any pending arbitration proceedings shall be discontinued.' Note, though, that this Article has lapsed (as per 1 January 2016, in Article 147 of the Polish Law on Bankruptcy, the bankruptcy of one of the parties will not discontinue the arbitration proceedings, see Zivković (2015, 14). The effect of said Article 142 is that it annuls the arbitration-clause itself. How to deal with Polish law, which (see Article 4(2)(e) EIR 2000 determines 'the effects of insolvency proceedings on current contracts to which the debtor is a party'. Another judge, Patten L.J., accepts that 'lawsuits pending' in Article 4(2)f EIR 2000 is an independent legal ground (as the Netherlands Supreme court does, see para. 10713a), with as a consequence: 'Once it is accepted that an existing reference to arbitration constitutes a pending lawsuit within the meaning of Article 15 EIR 2000 then the choice of national law to determine "the effects of insolvency proceedings on a lawsuit pending" would appear to comprehend any issues about the validity of the arbitration agreement which would affect the continuation of the arbitration itself. The only distinction made by Article 15 itself is between current and future proceedings. It seems to me unrealistic to assume that the Regulation was also intended to discriminate in its application of the choice of law rule between the types of lawsuit covered by Article 15 simply according to the jurisdictional basis (contractual as opposed to statutory) of the different types of possible proceeding. The present case is within the express terms of Article 15 and, in my judgment, one need look no further.' Another view however with regard to Article 142 of the Polish Bankruptcy and Reorganisation Law was taken by Arbitration Court, Economic and Agricultural Chambre of Czech Republic 15 January 2008, Case 135/2006, see Bělohlávek, Yearbook on Int'l Arbitration 2010, 145ff.

[10712i] *Pending arbitral proceedings.* Arbitration is regarded as a subform of lawsuits, see Article 7(2)(f). For the word 'pending', see para. 10712b. What an arbitral proceeding is must be interpreted autonomously. See Bělohlávek, Czech Yearbook of International Law 2015, 65ff; Müller, in: Mankowski/Müller/J.Schmidt (2016), Art. 18, nr. 15. The

term ‘arbitral proceedings’ has been translated in Dutch, rather curiously, as ‘*scheidsrechterlijk geding’*. The meaning should dovetail with the meaning of ‘arbitration’, as worded in Article 1(2)(d) Brussels I Regulation (recast). See Thole, MüKoEuInsVO 2015 (2006), Art. 18, nr. 2, who rightly excludes mediation from Article 18 EIR 2015, as mediation would not lead to a lawsuit.

Seat of the arbitral tribunal. The effects of insolvency proceedings on pending arbitral proceedings shall be governed solely by the law of the Member State in which the arbitral tribunal has its seat, see the final words of Article 18 EIR 2015. Party autonomy in arbitral proceedings may result in an actual location of this seat outside the EU, and although the dispute may be subject to a law of a Member State, the arbitral seat is located outside the EU. Article 18 will not apply, rather the PIL rules determinative for arbitral proceedings in that state. See Bork, in: Bork/Mangano (2016), 4.123. The other view is that Article 18 refers to the *lex fori concursus* of the tribunal. Would that be different then the tribunal has to clarify its position with relation to the effects of the insolvency proceedings of the *lex loci arbitri* for the other procedural questions. In this way Mankowski, *ZIP* 2010, 2482; Thole, MüKoEuInsVO 2015 (2006), Art. 18, nr. 3.

[10713] *Court cases.* Several courts have already struggled with Article 15 EIR 2000. These cases are also illustrative for the working of Article 18 EIR 2015. See for example: […..]