ANNEX

# GLOBAL RULES ON CONFLICT-OF-LAWS MATTERS IN INTERNATIONAL INSOLVENCY CASES

## STATEMENT OF THE REPORTERS

1. Introduction

In the main sections of our Report, we have examined the feasibility of transforming the ALI Principles of Cooperation Among the NAFTA Countries into a statement of principles suitable for global application. We believe it to be an integral requirement of such a mechanism for cooperation between courts of independent sovereign states that there should be a standard framework of commonly accepted rules to define the circumstances under which insolvency proceedings that are opened in one state are considered eligible to be accorded recognition and cooperation pursuant to the terms of the Global Principles. Also of vital importance is the promotion of internationally standardized definitions of the key terms that are employed in formulating the rules and principles on which the processes of international cooperation are to be based. The aspect of definition is addressed in the Appendix to this Report.

We are also convinced that the operation of these Global Principles would be greatly enhanced by a parallel process aimed at building a consensus regarding the principles to be applied to resolving conflict-of-laws issues in international insolvency. Even if it is possible to achieve general agreement as to the appropriate jurisdictional criteria to be employed for the purpose of opening insolvency proceedings, it is inevitably going to be the case that for the indefinite future, the domestic insolvency laws of the many sovereign states of the world will continue to differ from one another in numerous ways. It is therefore of considerable importance to try to reach consensus as to the choice-of-law approach to be applied in whichever forum insolvency proceedings happen to be opened. In this way, interested parties will be better able to anticipate the outcome that will result from the application of the provisions and processes of the relevant substantive law or laws to the circumstances of their particular claims or interests. The attainment of enhanced certainty and predictability of such outcomes is therefore a worthwhile goal to pursue. This objective can be facilitated by establishing agreed rules of choice of laws that will be applied by courts in relation to the issues that are encountered in an international insolvency case over which they are exercising jurisdiction. Such uniform rules, operated in conjunction with standardized rules for the exercise of jurisdiction, would introduce much-needed stability in the otherwise volatile and uncertain process of evaluating the possible consequences of insolvency for international commercial relationships.

The range of matters involving a potential choice of law is extremely wide. It would be unduly ambitious, as well as unrealistic, at this time to attempt to establish global rules for every conceivable choice-of-law issue that might arise in an international insolvency case. In the present state of the movement towards harmonization of the treatment of international insolvency matters, we believe it would be prudent to limit this exercise to exploring a selection of issues that are perceived to be of fundamental importance when considered in the context of the commercial relationship between a debtor and its creditors. In essence, this entails providing a general rule as to the law by which insolvency proceedings and their effects are to be governed, and a number of additional rules that are to operate by way of exceptions to that general rule in certain, defined situations. The Reporters' proposals for addressing that task, by means of uniform Rules, are set out in full in section 2 below. In section 3, the individual rules are analyzed and explained, and the Reporters' Notes provide additional information incorporating the comments of the Consultants who have participated in this project. It is envisaged that the proposed Global Rules could serve as the basis for international negotiation under the auspices of one or more appropriate organizations. To become formally applicable by national courts, it would be necessary for the Global Rules to become embodied in an international convention or model law to which a significant number of states might, in due course, become contracting or enacting parties.

The proposals regarding the principles to be applied to resolving conflict-of-laws issues in international insolvency are timely. In the latter part of the 20th century, rules regarding applicable law in international insolvency cases mainly were developed in the context of the application of general rules of private international law. The situation symbolized great uncertainty and unpredictability for parties concerned, while courts did not have a solid framework as a basis for their judgments. Until the beginning of the 21st century, the creation of a body of rules concerning conflict-of-laws (private-international-law) rules in international insolvency matters came from scholars, although their work may not have been understood or appreciated, see, e.g., D. Prosser, Interstate Publication, (1953) 51 Michigan Law Review 959, at 971: "The realm of the conflict of laws is a dismal swamp, filled with quaking quagmire, and inhabited by learned but eccentric professors who theorise about mysterious matter in a strange and incomprehensible jargon." See, with regard to conflict-of-laws rules in general in private international law, Horatia Muir Watt, Choice of Law in Integrated and Interconnected Markets: a Matter of Political Economy. Ius Commune Lectures on European Private Law No. 7, 2003 and Mathias Reimann and Reinhard Zimmermann (eds.), The Oxford Handbook of Comparative Law, Oxford University Press, 2006, and with regard to cross-border insolvency matters, Jay L. Westbrook, Choice of Avoidance Law in Global Insolvencies, in: 17 Brooklyn Journal of International Law 499, 517 (1991); Richard E. Coulson, Choice of Law in United States Cross-Border Insolvencies, 32 Denver Journal of International Law & Policy 275-314 (2004); Jay L. Westbrook, Universalism and Choice of Law, 23 Penn State International Law Review 625 (2005); Jay L. Westbrook, Avoidance of Pre-Bankruptcy Transactions in Multinational Bankruptcy cases, in: 42 Texas International Law.Journal 899 (2007); Ian F. Fletcher, Insolvency in Private International Law. National and International Approaches, Oxford Private International Law Series, Oxford University Press, 2nd ed. 2005, 1.01ff; Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, K. Pannen / S. Riedemann, in: Klaus Pannen, European Insolvency Regulation, Berlin: Walter de Gruyter, 2007, p. 7ff.

In recent years, however, national legislators have taken initiatives to draft legislation concerning conflict-of-laws rules applicable in international insolvency law matters. Although these initiatives are a relatively fresh departure, two approaches seem to emerge. In the first approach, general rules on conflict-of-laws matters are drafted in the form of a Code, which includes a special section of law applicable to international insolvency matters, see, e.g., the Belgian Code of Private International Law of 2004, which includes a Chapter XI on Collective proceedings concerning insolvency (Articles 116–121). The second approach, which seems to be favored by national (European) legislators, is based on an extension model, in which a modified and sometimes selected group of provisions have been drafted, inspired by the conflict-of-laws rules of the EU Insolvency Regulation (Articles 4–15). These latter rules are already binding in their entirety and directly applicable in 26 Member States as regards any matter that falls within the scope of the EU Insolvency Regulation. The extension relates to applicability of rules inspired by these Articles to matters that happen to fall outside the scope of the Regulation, and more generally to relationships with states that are not bound by the Regulation. See, for instance, Germany (Articles 336-341 and 351 Insolvency Code), Spain (Articles 201-209 *Ley Concursal* 22/2003) and the Netherlands (Articles 10.4.1-10.4.11 pre-draft 2007). For discussion, see Anna-Maja Schaefer, *Das autonome internationale Insolvenzrecht Spaniens im Vergleich zum deutschen Recht*, Schriften der Deutch-Spanischen Juristenvereinigung, Band 31, Peter Lang, Frankfurt, 2009; Jeroen van der Weide, Conflict of Law Rules: Section 10.4, in: Bob Wessels and Paul Omar (eds.), Crossing (Dutch) Borders in Insolvency, Nottingham, Paris: INSOL Europe 2009, pp. 87-95; Ian Fletcher, Commentary on Section 10.4, in: Bob Wessels and Paul Omar (eds.), Crossing (Dutch) Borders in Insolvency, Nottingham, Paris: INSOL Europe 2009, pp. 95-97; Nauta, M-L, and F. Bulten, Introduction to Spanish Cross-Border Insolvency Law—An Adequate Connection with Existing International Insolvency Legislation, 18 International Insolvency Review, Spring 2009, pp. 59-77.

In an aim to provide "certainty with respect to the effects of insolvency proceedings on the right and claims of parties affected by those proceedings," the UNCITRAL Legislative Guide on Insolvency Law (2005) (adopted in 2004), Part Two, section I.C. (paras. 80-91) has drafted, in close cooperation with the Hague Conference on Private International Law, five recommendations concerning the applicable law in insolvency proceedings. The recommendations, which are numbered as 30-34 inclusive, proclaim as their basic rule a proposition identical to that embodied in the EU Insolvency regulation, namely that the *lex fori concursus* shall govern the commencement, conduct, administration, and conclusion of insolvency proceedings. Where the UNCITRAL text parts company with the EU Regulation is in proposing a much more limited range of exceptions to the application of the *lex concursus*. Only two excepted cases are proposed (contained in recommendations 32 and 33), the first to accommodate the special arrangements that are operative among participants in a payment or settlement system or in a regulated financial market, and the second to enable the effects of insolvency proceedings on contracts of employment ("labour contracts") to remain subject to the law applicable to the contract. With respect, the Reporters consider that so limited a range of exceptions to the dominant role of the *lex concursus* is unlikely to prove commercially convenient or acceptable to the majority of parties engaged in international trade and business, given the present stage of uneven development of national laws governing such sensitive matters as security interests, set-off, and transaction avoidance. We therefore proclaim our allegiance to the alternative approach embodied in articles 4-15 of the EU Regulation (notably in articles 5, 6, and 13) whereby additional exceptions to the application of the *lex concursus* are permitted, under controlled circumstances, in respect of each of the three matters just mentioned.

It should be noted that the proposals set out in this Annex regarding conflict-of-laws rules do not aim to address "inter-state" conflict-of-law matters in the sense that is sometimes employed with reference to multijurisdictional entities such as federal states. For the purposes of the present Report, the term "state" (or: country) has been defined in the Glossary of Terms and Descriptions in the Appendix to this Report as "The political system of a body of people who are politically organized; the system of rules by which jurisdiction and authority are exercised over such a body of people." In this context, "inter-state" conflict of law may occur internally within states with a mixed jurisdiction; a state with separate regions (the People's Republic of China, with Special Administrative Regions Hong Kong and Macao, may form such an example); or a federation of states, for instance Germany (which has 16 "*Bundesländer*"), and the U.S.A. See James T. Markus and Don J. Quigley, Conflict of Laws-Which State Rules Govern?, ABI Journal, November 1999, p. 18ff.

2. Text of the Global Rules

## GLOBAL RULES ON CONFLICT-OF-LAWS MATTERS IN INTERNATIONAL INSOLVENCY CASES

### A. General Provisions

**Rule 1 Scope**

**These Global Rules shall apply to insolvency proceedings that are opened in a state which has jurisdiction for that purpose according to the provisions of Global Principle 13 of the Global Principles for Cooperation in International Insolvency Cases.**

**Rule 2 International Obligations of This State**

**These Global Rules shall not affect whatsoever the effects of binding international rules related to choice of law arising out of any treaty or other form of agreement to which [this state] is a party with one or more other states.**

**Rule 3** ***Ex Officio*** **Application**

**These Global Rules and the law thereby indicated are to be applied** ***ex officio.***

**Rule 4 Interpretation**

**In the interpretation of these Global Rules, regard is to be had to their international origin and to the need to promote uniformity in their application and the observance of good faith.**

**Rule 5 Exclusion of Renvoi**

**In applying these Global Rules, any reference to the law of a state means the internal ("domestic") rules of law in force in that state other than its rules of private international law.**

## B. Localization of Assets

### Rule 6 Immovable Property

**6.1. Immovables, and rights vested in or attached to them, are located at the place where the immovable, and the right vested in it or attached to it, is registered in a public register designated for the registration of rights.**
**6.2. If an immovable, and the right vested in it or attached to it, is not recorded in a public register designated for the registration of rights, then the immovable, and the right vested in it or attached to it, is located where the immovable is situated.**

### Rule 7 Nonregistered Movables

**7.1. Nonregistered movables, and rights vested in or attached to them, are located at the place where the nonregistered movable is situated.**
**7. 2. For the purposes of Global Rule 7.1, the following legal presumptions apply:**

> **a. Movables recorded in a vehicle license register, and rights vested in or attached to them, are presumed to be located at the place where the movable is recorded in the vehicle license register.**
>
> **b. Goods in transit, as well as rights vested in or attached to them, are presumed to be located in the state of destination.**

### Rule 8 Registered Movables

**8.1. Registered movables, and separately registered rights vested in or attached to them, are located at the place where the movable or the right in question is recorded in a public register designated for the registration of rights.**
**8.2. For the purposes of Global Rule 8.1, unless there is proof to the contrary, registered movables shall be presumed to be located at the place where the movable is recorded in a public register designated for the registration of rights.**

### Rule 9 Claims

**9.1. Claims payable to bearer or order, and rights vested in or attached to them, are located at the place where the bearer or order document is situated.**
**9.2. Claims of known creditors, and rights vested in or attached to them, are located at the place where the debtor has his seat or his domicile.**

### Rule 10 Shares in Joint-Stock Companies

**10.1. Bearer shares, and rights vested in or attached to them, are located at the place where the bearer share certificate is situated.**
**10.2. Registered shares, and rights vested in them, are located at the place where the registered share, or the right vested in it, is recorded in a register of shareholders kept by the company.**

**10.3. If a registered share, or a right vested in it, is not recorded in a register of shareholders, the registered share or the right vested in it is located at the place where the company has the center of its main interests. The center of the main interests of the company is presumed to be the place of its registered office.**
**10.4. Book-entry shares, and rights vested in them, are located at the place of the registered office of the intermediary with which the securities account is kept in which the book-entry shares are administered.**

### Rule 11 Intellectual Property Rights

**Patent rights, trademark rights, and copyrights, and rights vested in them, are located at the place where the patent holder, trademark proprietor, or copyright holder has his seat or his domicile.**

## C. General Rules of Law Applicable to Insolvency Proceedings

### Rule 12 Law of the State of the Opening of Proceedings

**12.1. Save as otherwise provided in [this Act/these Rules], the law applicable to insolvency proceedings and their effects shall be that of the state within the territory of which such proceedings are opened, hereafter referred to as "the state of the opening of proceedings."**
**12.2. The law of the state of the opening of proceedings shall determine the conditions for the opening of those proceedings, their conduct, administration, conversion, and their closure.**

### Rule 13 Law of the State of the Opening of Non-Main Proceedings

**If insolvency proceedings are opened in a jurisdiction other than that where the center of main interests of the debtor is situated ("non-main" proceedings), the effects of the application of the law of the state of the opening of such proceedings shall be restricted to those assets of the debtor situated in the territory of that state at the time of the opening of those proceedings.**

### Rule 14 Cross-Border Movement of Assets

**In relation to any asset of the debtor that is of a moveable character, Global Rules 12 and 13 shall apply, subject to the following modifications:**

> **(a) Any rule of insolvency law that is applicable by virtue of the localization of an asset in the territory of the state of the opening of insolvency proceedings, at the time of the opening of the proceedings, shall not apply if it is shown that the asset in question has been moved to that location from the territory of another state, to whose insolvency law it would otherwise have been properly subject, in circumstances that suggest that the transfer was effected wholly or primarily for the purpose of avoiding the effects of the law of the other state, including its insolvency law.**

(b) Conversely, where an asset has been moved from the territory of one state to that of another state under the circumstances stated in paragraph (a), the effects of any insolvency proceedings that are opened in the former state shall apply to the asset in question.

(c) In the absence of evidence to the contrary, it shall be presumed that any asset that has been removed from the territory of the state in which insolvency proceedings are opened, within 60 days prior to the opening of such proceedings, was made with intent to avoid the effects of the law of that state. It is for the party who seeks to maintain the validity of the act, whereby the property was removed from the territory of that state, to provide evidence that the transfer was made for a bona fide and legitimate purpose.

(d) Except in a case to which paragraph (c) is applicable, it is for the party who alleges that the provisions of paragraphs (a) and (b) of this Rule are applicable in relation to a particular asset to prove that this is the case.

## D. Exceptions to the General Rules of Law Applicable to Insolvency Proceedings

### Rule 15 Rights of Secured Creditors

**15.1. Insolvency proceedings shall not affect the rights in rem of creditors or third parties in respect of tangible or intangible, moveable or immoveable assets—both specific assets and collections of indefinite assets as a whole that change from time to time—belonging to the debtor, which are situated within the territory of another state at the time of the opening of proceedings.**

**15.2. The rights referred to in Global Rule 15.1 shall in particular mean:**

**(a) The right to dispose of assets or have them disposed of and to obtain satisfaction from the proceeds of or income from those assets, in particular by virtue of a lien or a mortgage;**

**(b) The exclusive right to have a claim met, in particular a right guaranteed by a lien in respect of the claim or by assignment of the claim by way of a guarantee;**

**(c) The right to demand the assets from, and/or to require restitution by, anyone having possession or use of them contrary to the wishes of the party so entitled;**

**(d) A right in rem to the beneficial use of assets.**

**15.3. The right, recorded in a public register and enforceable against third parties, under which a right in rem within the meaning of Global Rule 15.1 may be obtained, shall be considered a right in rem.**

### Rule 16 Exception

**16.1. By way of exception to Global Rule 15, a right in rem ("in rem security right") shall not be exempted from the effects of insolvency proceedings if proof is provided that the state where the assets are situated, at the time of the opening of insolvency proceedings, has no substantial relationship to the parties or the transaction in relation to which the security right was created, and there is no other reasonable basis for the fact that the assets are so situated.**

**16.2. It is for the party who claims that the conditions specified in Global Rule 16.1 are met, in relation to a particular security right, to prove that those conditions are in fact met in the relevant case.**

**Rule 17 Set-Off**

**Insolvency proceedings shall not affect the right of creditors to demand the set-off of their claims against the claims of the debtor, where such a set-off is permitted by the law applicable to the insolvent debtor's claim.**

**Rule 18 Exception**

**Where a right of set-off is demanded on the basis of Global Rule 17, if it is the case that, in the absence of express choice made by the parties, the law applicable to the insolvent debtor's claim would be that of the state of the opening of main insolvency proceedings, Global Rule 17 shall not apply if the law of the state chosen by the parties has no substantial relationship to the parties or the transaction, and there is no other reasonable basis for the parties' choice.**

**Rule 19 Reciprocal Contracts: General Rule**

**Save as otherwise provided by [this Act/these Rules], mutual obligations in respect of a reciprocal contract, which has been concluded prior to insolvency of one of the parties, shall be governed solely by the law of the state of the opening of proceedings.**

**Rule 20 Contracts of Employment (Labor Contracts)**

**The effects of insolvency proceedings on employment contracts and relationships shall be governed solely by the law of the state applicable to the contract of employment.**

**Rule 21 Restrictions to Exceptions**

**Global Rules 15, 17, and 20 shall not preclude actions for voidness, voidability, or unenforceability of legal acts detrimental to the general body of creditors, pursuant to the law applicable to the insolvency proceedings, as determined by Global Rule 12 or by Global Rule 13 (as the case may be).**

**Rule 22 Defenses to the Avoidance of Detrimental Acts**

**Global Rule 21 shall not apply where the person who benefited from an act detrimental to the general body of creditors provides evidence that:**

> **(i) The said act is subject to the law of a state other than that of the state of the opening of proceedings; and**
>
> **(ii) That law does not allow any means of challenging that act in the relevant case.**

**Rule 23 Exception**

**23.1. By way of exception to Global Rule 22, a transaction detrimental to the general body of creditors shall not be exempted from the effect of the avoidance rule of the law of the state of the opening of insolvency proceedings if proof is provided that the state to whose law the transaction is subject has no substantial relationship to the parties or the transaction, and there is no other reasonable basis for the selection of the law of that state as the law to govern the transaction in question.**
**23.2. It is for the party who claims that the conditions specified in Global Rule 23.1 are met, in relation to a particular transaction, to prove that those conditions are in fact met in the relevant case.**

## 3. Comments to the Global Rules

In this section, we set out explanatory Comments and Illustrations relating to the Global Rules on conflict-of-laws matters, as stated above. The Global Rules are treated in groups, or singly, as seems most appropriate. For descriptions of key terms, such as "law," "applicable," "insolvency proceeding," "state," "opening of proceedings," and "center of main interests," see the Appendix to this Report.

### A. General Provisions

**Rule 1 Scope**

**These Global Rules shall apply to insolvency proceedings that are opened in a state which has jurisdiction for that purpose according to the provisions of Global Principle 13 of the Global Principles for Cooperation in International Insolvency Cases.**

**Comment to Global Rule 1:**

The ultimate purpose of the proposed uniform rules of choice of law is to bring consistency and predictability into an area that has hitherto been notable—indeed notorious—for the variability of the possible outcomes to the resolution of a given matter. These outcomes are dependent on the approach traditionally favored by the conflict-of-laws rules of the state that happens to serve as the forum for proceedings. If the outcome of that process does not accord with the approach favored by other legal systems, before whose courts the matter may have to be further pursued, contradictory determinations may ensue, with consequent possibilities for the defeat of parties' expectations and considerable wastage of resources. However, before renouncing the rules and approaches that have formerly been followed under the auspices of their independent, sovereign authority, states can reasonably impose a stipulation that the insolvency proceedings to which they are in the future to apply choice-of-law rules of an internationally uniform nature, shall be shown to have taken place in a state whose exercise of jurisdiction has taken place in accordance with internationally agreed standards for so acting. Rule 1 is therefore intended to introduce such a controlling provision to determine the scope of application of the uniform rules that follow. By making reference to the criteria for according international jurisdiction that are specified in Global Principle 13, this Rule seeks to maintain consistency between the provisions dealing with international recognition and cooperation contained in Section II of this Report, and the complementary provisions concerning choice of law that are contained in this Annex.

**Rule 2 International Obligations of This State**

**These Global Rules shall not affect whatsoever the effects of binding international rules related to choice of law arising out of any treaty or other form of agreement to which [this state] is a party with one or more other states.**

**Comment to Global Rule 2:**

Codified and binding private international law has been laid down in many international and supranational treaties or conventions, or in other legally effective instruments, for example, conventions concluded within the Hague Conference on Private International Law or Regulations of the European Union. In many of these treaties and conventions, the supremacy of the rules they contain will follow from the text or will be produced by virtue of a state's constitution. In these circumstances, Global Rule 2 may seem superfluous, although in practice with a gradually growing body of legislation and regulation with international effects, a legal reminder may serve as a useful tool. It is noted that Article 3 of the UNCITRAL Model Law on Cross-Border Insolvency contains a similar principle.

**Rule 3 *Ex Officio* Application**

**These Global Rules and the law thereby indicated are to be applied *ex officio*.**

**Comment to Global Rule 3:**

This Global Rule addresses itself to a court, although application by a public body or authority is not excluded. An alternative approach would be to apply the Global Rules only in instances where a party has invoked them, with the general consequence that without the Global Rules being invoked in a given case, a court will apply either its own law (i.e., the *lex fori*) as an "automatic default," or alternatively (when dealing with a foreign proceeding) the law of the state where that insolvency proceeding is pending (*lex fori concursus*). In concordance with many codifications of conflict-of-laws provisions, Global Rule 3 has been preferred as it will provide the court, instead of an interested party, with the active role. Global Rule 3 also provides for the ex officio application of the law indicated by the Global Rules, which in certain circumstances could be the law of a state whose content may not be easy to access. Moreover, the rule implies that said law will be applied in the same way as in said state, therefore including the rules that follow from court cases, interpretation followed in legal theory, etc.

## REPORTERS' NOTES

In general, a court may rely on certain treaties that provide for the exchange of legal information regarding foreign law (e.g., the European Convention on Information on Foreign Law of 1968, ETS No. 62, of the Council of Europe) or, where national procedural law so allows, to have interested parties to provide an expert opinion. If it should happen that the particular foreign law cannot be authoritatively ascertained, it is to be expected that a court in each individual case will find an appropriate answer, after having heard parties and applying general principles of conflicts of law and giving considerations to the international context of the case. Such a judgment will be carefully reasoned and should avoid overturning parties' reasonable expectations. An ex officio application will be limited by the applicable procedural rules of the state in cases where an appeal from the decision in the case can be heard only on limited grounds. On the English common-law approach to the pleading and proof of foreign law, see Dicey, Morris and Collins, The Conflict of Laws (14th Ed. 2006, London, Sweet & Maxwell), Chapter 9; R. Fentiman, Foreign Law in English Courts (1998, Oxford University Press); S. Geeroms, Foreign Law in Civil Litigation: A Comparative and Functional Analysis (2004, Oxford University Press).

### Rule 4 Interpretation

**In the interpretation of these Global Rules, regard is to be had to their international origin and to the need to promote uniformity in their application and the observance of good faith.**

### Comment to Global Rule 4:

Several private-law treaties contain a provision similar to Global Rule 4, while in its text it is nearly similar to Article 8 UNCITRAL Model Law on Cross-Border Insolvency. It should function as a reminder for courts and parties that application of the conflict-of-law rules will always carry the potential to engage foreign legal cultures where certain legal effects may create confusion or even aggravation, without interfering with a foreign court's exercise of jurisdiction, a foreign administrators' powers, or a foreign state's public policy. Global Rule 4 aims to ensure that these Rules are applied with sensitivity and in a uniform way, while in certain circumstances where the Rules allow, a court should apply analogous legal rules to produce effects that are akin to those achievable under the legal system to which they are addressed.

### Rule 5 Exclusion of Renvoi

**In applying these Global Rules, any reference to the law of a state means the internal ("domestic") rules of law in force in that state other than its rules of private international law.**

### Comment to Global Rule 5:

The doctrine of renvoi was developed by scholars of private international law (conflict of laws) during the 19th and early 20th centuries. It attempts to address the difficult issues encountered in the choice-of-law process when it transpires that there are significant differences of approach between the various systems whose laws are perceived to be in competition to supply the *lex causae*. A dilemma is presented to the court that is acting as the forum of the proceedings if it discovers that the result of applying its own choice-of-law process would indicate that the law of another state should serve as the *lex causae*: should the forum interpret the reference to be made exclusively to the internal (domestic) law of the other state, or to the totality of that system of law, including its own, separately evolved rules of conflict of laws? If the latter interpretation is adopted, how should the forum respond if it further transpires that the application of the choice-of-law rules of the *lex causae* to the facts of the instant case would result in the selection of the law of a different state (which could be that of the forum, or of some third state)? It is the potential for such an onward transmission (or renvoi) to occur that gives rise to intractable logical difficulties to which there is no agreed, single solution. Some states have responded to the dilemma by effectively declining to allow their courts to engage with it, and have opted to regard the initial reference made by their own choice-of-law rule as being addressed exclusively to the domestic law of the other state (e.g., Italy, Introductory Law to the *Codice Civile*, Art. 30). Others have opted for a "half-way" solution (also known as "partial renvoi") whereby the initial reference is treated as engaging the totality of the law of the other state, but any onward transmission that is made by application of the choice-of-law rules of that system is then deemed to be addressed exclusively to the domestic law of the state so indicated (e.g., France, L'Affaire Forgo, 1883, 10 Clunet 64).[349]

In the modern era, it has become widely accepted that one conspicuous benefit resulting from the conclusion of international agreements in the field of private international law is, or can be, the removal of the core problem giving rise to the insoluble dilemma that is renvoi, namely the divergent approaches to choice of law that have evolved under the laws of different sovereign states. If a set of uniform rules of choice of law regarding certain matters is adopted by the states ratifying an international treaty or convention, it can be assumed that the *lex causae* of any case falling within the scope of the convention would be identical, irrespective of which of the contracting states happened to serve as the forum for proceedings. Hence it has become a standard practice in the drafting of such conventions to include a provision whose effect is to exclude the application of renvoi by the courts of the states concerned, and to declare explicitly that any reference to the law of a state means the internal ("domestic") law of that state, excluding its rules of private international law.[350] Also, the EU Insolvency Regulation excludes renvoi, see recital (23), which states: "This Regulation should set out, for the matters covered by it, uniform rules on conflict of laws which replace, within

[349] Various alternative approaches have also been advocated or applied, of which perhaps the most conceptually taxing is that employed under English law whereby the English forum seeks to replicate the *outcome* that would be achieved by a court determining the case according to the full choice-of-law process that would be deployed under the law of the state chosen by the English choice-of-law rule (so-called "double" or "total" renvoi, explained in Dicey, Morris, and Collins, The Conflict of Laws (14th edition, 2006), chapter 4).

[350] As examples of such "Exclusion of renvoi" provisions, see: Convention of 19 June 1980 on the Law Applicable to Contractual Obligations (Rome Convention), Article 15; Regulation (EC) No.593/2008 of 17 June 2008 on the law applicable to contractual obligations (Rome I Regulation), Article 20; Hague Convention (No.XXVII) of 14 March 1978 on the Law Applicable to Agency, Articles 5, 6, 11; Hague Convention (No.XXXI) of 22 December 1986 on the Law Applicable to Contracts for the International Sale of Goods, Article 15 (not yet in force), Regulation (EC) No.864/2007 on the law applicable to noncontractual obligations (Rome II Regulation), Article 24; Article 16 of the Code on Private International Law of Belgium (2004) or Article 10:5 Dutch Civil Code.

their scope of application, national rules of private international law." It is self-evidently the case that the exclusion of renvoi from the choice-of-law process can give rise to new species of forum-shopping tactics, albeit of a different kind from those that may be deployed in proceedings where the court in question is known to apply the renvoi doctrine in some form. In response to such possible practices, it is essential both that the rules which determine the exercise of international jurisdiction in insolvency proceedings are clearly defined, and also that they are scrupulously respected by all courts before which insolvency proceedings are initiated. Hence, the provisions of Global Principle 13 have a vital bearing upon the operation of the Global Rules of Conflict of Laws, as well as forming an integral part of the processes of recognition and cooperation under the Global Principles themselves.

## REPORTERS' NOTES

Global Rule 5 is thus designed in accordance with the modern approach to the drafting of uniform rules of choice of law, so as to eliminate any uncertainty as to the outcome of the application of any of the choice-of-law rules embodied in the present Statement. Any court serving as the forum for insolvency proceedings within a state that has embraced the Global Rules would interpret the reference to the law so found as a reference to the internal (domestic) law of the system in question, disregarding any consequences that might hypothetically ensue from the application of the choice-of-law rules of the *lex causae* if it had been the case that the matter had arisen in the first instance before the courts of that other state. In Global Rule 5, the rule is laid down that in applying the Global Rules, any reference to the law of a state means the internal rules of law in force in that state other than its rules of private international law. These internal rules therefore do not contain (a reference to) that state's conflict-of-law rules. Global Rule 5 is intended to be a substantial norm (*Sachnorm*) and not a combined norm (*Gesamtnorm* or *Gesamtverweisung*). The application of conflict-of-laws rules in international insolvency matters is complex enough in itself, and the inherent requirements of the present subject matter—that insolvency issues should be resolved with speed and effectiveness—do not allow additional complications, for example, by using the method of "renvoi," see H.-C. Duursma-Kepplinger, in: Duursma-Kepplinger, H.-C, Duursma, D, Chalupsky, E., Europäische Insolvenzverordnung. Kommentar, Springer, Wien New York, 2002, Art. 4, nr. 10; Verena Lorenz, Annexverfahren bei Internationale Insolvenzen. Internationale Zuständigkeitsregelung der Europäischen Insolvenzverordnung. Max-Planck-Institute für ausländisches und internationales Privatrecht. Studien zum ausländischen und internationalen Privatrecht, nr. 140, Tübingen: Mohr Siebeck, 2005, 45; Ian F. Fletcher, Insolvency in Private International Law, National and International Approaches, Oxford Private International Law Series, Oxford University Press, 2nd ed. 2005, 7.79; Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, para. 10625. It is appreciated that in Germany the combined norm is found, see Jasnica Garašić, Recognition of Foreign Insolvency Proceedings: the Rules that a Modern Model of International Insolvency Law Should Contain, in: Yearbook of Private International Law, 2005, vol. 5, p. 358. For an overview of the discussion, see Peter Mankowski, Europäisches Internationales Insolvenzrecht (EuInsVO), Kapitel 47, Kölner Schrift zur Insolvenzordnung, 3. Auflage, Münster: ZAP Verlag 2009, nr. 97.

### B. Localization of assets

**Introductory Comment:**
In this section, so-called "localization rules" are suggested.[351] A localization rule is a rule that indicates where a debtor's assets must be deemed to be located so that it is possible to determine the scope of operation of (cross-border) insolvency proceedings. The main purpose of these rules is to clearly identify the location of assets that will be subject to, and therefore covered by, insolvency proceedings that have been opened in a certain state. Localization of assets can be relevant in different situations. In the Global Rules, the general principle of universalism is embraced: insolvency proceedings have universal effect and therefore cover all assets of the debtor regardless of their location. Although under these circumstances the problem of asset localization would seem to be less relevant, it is on the contrary relevant whenever the question arises whether the state(s) where assets of the debtor are located recognize the coverage of these assets by foreign insolvency proceedings. Also exceptions to the principle of universalism are suggested. As a consequence, different laws may apply, and it is therefore of utmost importance to determine which assets are subject to which law. Furthermore, in many legal systems the opening of non-main or secondary insolvency proceedings is allowed, often with the inherent consequence that the effects of these proceedings are limited to the state's territory. The legal consequences of these proceedings will only affect the assets located within this state. Laws of this state will only apply to assets that are located in this state, and therefore criteria have to be developed to determine the location of such an asset, as in such situations the question is: which assets are covered by the non-main or secondary proceedings and which are covered by the main insolvency proceedings?

When drawing up localization rules, the Reporters were convinced of the logic of including such rules in the body of rules of private international law, more specifically the conflict-of-laws rules. Conflict-of-laws rules characteristically state a connecting factor linking the legal relationship (reference category) to the applicable law. The connecting factor is often a matter of geographical fact. For this reason, the conflict-of-laws rule, and particularly the connecting factor forming part of the rule, will be a useful instrument to help formulate localization rules in case of cross-border insolvency proceedings.

The localization rules proposed are each focused on particular kinds of asset: tangible property (movables and immovables), as well as intangibles including claims, shares in joint-stock companies, and intellectual property rights (patent rights, trademark rights, and copyrights). The rules do not aim to cover localization issues relating to financial instruments, such as bonds, shares, and derivatives (options, futures, swaps, forwards).[352]

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[351] The Reporters acknowledge their gratitude to Dr. Jeroen A. van der Weide, Leiden Law School, for his thorough analysis of legislation and legal literature and for enabling them to incorporate several sections of his text in their Report.

[352] For the terms used, for example, assets, movables, immovable property, claim, share, intellectual property right, public register, vested right, and attached right, reference is made to the Glossary of Terms and Descriptions in the Appendix.

**Rule 6 Immovable Property**

**6.1. Immovables, and rights vested in or attached to them, are located at the place where the immovable, and the right vested in it or attached to it, is registered in a public register designated for the registration of rights.**
**6.2. If an immovable, and the right vested in it or attached to it, is not recorded in a public register designated for the registration of rights, then the immovable, and the right vested in it or attached to it, is located where the immovable is situated.**

**Comment to Global Rule 6:**

Property can be broadly divided into movables and immovables. Immovables are, from their nature, incapable of being moved. Movables, on the contrary, can be physically moved or, in the case of intangibles, their notional location may be capable of alteration. Rights vested in assets (ownership, pledge, mortgage) or rights attached to assets (reservation of title) are identified with the property in question. The distinction is generally made that all assets that are not movables are immovables. The term immovables includes land, unextracted minerals, plants growing on land, buildings, and works permanently united with the soil, either directly or by incorporation into other buildings or works. Further examples of immovables are houses, office buildings, and factory buildings, storage tanks for solid or liquid substances permanently attached to the soil, wires, cables, and pipes. Global Rule 6.1 lays down the general rule based on the premise that immovables, and rights vested in or attached to them, are, as a rule, recorded in a public register designated for the registration of rights. A logical choice when localizing immovables is to use the place of registration, which basic principle is here chosen. The term "rights vested in immovables" refers to absolute rights vested in an immovable, for example, the right of ownership and user and security rights such as usufruct, leasehold, and the right of mortgage. These rights are identified with the immovable in which they are vested. Some rights are not vested in the immovable, but are "attached" to it. Such quasi property-law rights occur inter alia in German law and in Dutch law. Examples are *Vormerkung* (§883 *Bürgerliches Gesetzbuch* (German Civil Code); Article 7:3 Dutch Civil Code) and *Auflassungsvormerkung*, which is linked to the *Anwartschaftsrecht*. Such a *Vormerkung* is an entry made in the German land registry (*Grundbuch*) or Dutch registry (*Kadaster*) of an intended transfer of an immovable or of its encumbrance with a right less than ownership. A *Vormerkung* gives the beneficiary a secured position (legally based expectation) with third-party effect. A public register designated for the registration of rights refers to the land register in which the legal status of immovables is recorded.

In the absence of registration in a land register or similar register, the immovable, the right vested in it, or the right attached to it is located at the place where the immovable is (physically) situated, see Global Rule 7. Its rationale is that immovables, by their nature, are incapable of being moved. This means that they are located at the place where they are (physically) situated. From the legal perspective, however, it is more natural in this context to link their location to the place of registration. This is, indeed, the general rule of the proposed localization rule.

## REPORTERS' NOTES

Global Rule 6 is similar to Article 2(g) EU Insolvency Regulation. In many occasions governed by such rule, the physical location (territory) and the place of registration will coincide. Under the general rules of private international law, the actual location is undisputed and universally accepted as a principle of determining which law is applicable to the proprietary regime of immovables. See, inter alia, G.C. Venturini, Property, in: Kurt Lipstein & R. David e.a. (eds.), International Encyclopedia of Comparative Law (Volume III, Private International Law, Chapter 21), Tübingen: J.C.B. Mohr (Paul Siebeck) 1976, p. 3; Hans Stoll, J. von Staudingers Kommentar zum Bürgerlichen Gesetzbuch mit Einführungsgesetz und Nebengesetzen. Internationales Sachenrecht, Berlin: Sellier de Gruyter 1996, no. 124; Christiane Wendehorst, Art. 43, p. 2531, marginal no. 2, in: Hans Jürgen Sonnenberger (ed.), Münchener Kommentar zum Bürgerlichen Gesetzbuch. Einführungsgesetz zum Bürgerlichen Gesetzbuche (Art. 1-46). Internationales Privatrecht (Band 10), München: Verlag C.H. Beck 2006; J.A. van der Weide, Mobiliteit van goederen in het IPR. Tussen situsregel en partijautonomie, PhD Vrije University Amsterdam 2006, p. 17. Explicitly section 99(1) of the Swiss IPRG and Article 87 of the Code on Private International Law of Belgium.

## Rule 7 Nonregistered Movables

**7.1. Nonregistered movables, and rights vested in or attached to them, are located at the place where the nonregistered movable is situated.**
**7. 2. For the purposes of Global Rule 7.1, the following legal presumptions apply:**

**a. Movables recorded in a vehicle license register, and rights vested in or attached to them, are presumed to be located at the place where the movable is recorded in the vehicle license register.**

**b. Goods in transit, as well as rights vested in or attached to them, are presumed to be located in the state of destination.**

### Comment to Global Rule 7:

All forms of property that are not immovables are movables. Movables can be distinguished into nonregistered movables and registered movables. Nonregistered movables are movables that are not recorded in a public register designated for the registration of rights. Examples of nonregistered movables are (company) equipment, fittings, and fixtures, stock in trade (inventory), machinery, motor vehicles, nonregistered airplanes, nonregistered vessels, and railroad coaches. Global Rule 7.1 determines that nonregistered movables and the rights vested in or attached to them are deemed to be located at the place where the nonregistered movable is situated. Regarding (nonregistered) movables, location means the place where the movable is usually situated. This does not include a chance holiday country or country of transit. There must be a longer-term connection between the movable and its location. In principle, nonregistered movables including the rights vested in or attached to them can only be localized in the state in which they are (physically) located. Global Rule 7.1 is consistent with Article 2(g) EU Insolvency Regulation. Under the general rules of private international law of several states, the actual location (situs) is undisputed and accepted as a principle of determining which law is applicable to the proprietary regime of movables. See, e.g., section 43(1) of the German EGBGB, Article 87 §1 of the Belgian WIPR, Recommendation no. 203 UNCITRAL Legislative Guide on Secured Transactions (2007): "The law should provide that (. . .) the law applicable to the creation, third-party effectiveness and priority of a security right in a tangible asset is the law of the State in which the asset is located."

There are two categories of movables with respect to which greater certainty is created as to their location by the introduction of a legal presumption. These are subjects of Global Rule 7.2.

These rebuttable legal presumptions pertain to movables recorded in a vehicle license register and to goods in transit (*res in transitu*). The rights vested in nonregistered movables are absolute rights vested in a nonregistered movable, for example, the right of ownership and user and security rights such as usufruct and lien. Some rights do not vest in the nonregistered movable, but are "attached" to it, for example, a stipulated retention of title, certain privileges and priority rights, and retention rights. These rights are not absolute, they are quasi property-law rights. In Global Rule 7.2, two categories of nonregistered movables are designated for which legal presumptions regarding the location of these assets have been formulated. These presumptions may be rebutted. Parties may demonstrate that, contrary to the legal presumption, the actual location is decisive.

## REPORTERS' NOTES

The list of Global Rule 7.2 is not exhaustive, as it is conceivable that the list of legal presumptions will be extended with legal presumptions with respect to other nonregistered movables to which special localization rules apply. Global Rule 7.2.a comprises movables that are recorded in a vehicle license register or similar registration system (e.g., railroad coaches) often maintained by (a public body of) the government of a state. Usually, these will be motor vehicles, such as cars, trucks, motorcycles, and mopeds. These movables recorded in a vehicle-licence register are presumed—subject to rebuttal evidence—to be located at the place where the movable is registered. The presumption is based on two arguments: (i) most often movables will usually be physically present in the state in which they are recorded in a vehicle license register; therefore brief removals of the movable to another state do not affect the result of the localization rule, (ii) the presumption serves as a means to fight against fraudulent acts in respect of creditors where a prospective insolvent debtor, for reasons of his own or other's benefit, transfers the movable to another State prior to the bankruptcy. By localizing the movable in the state in which it is registered, such transfers have no legal effect. The well-known phenomenon of "goods in transit" (*res in transitu*) refers to goods that are being transported pursuant to a contract of (international) carriage, performed by truck, train, ship, or aircraft. In practice, it is often difficult to localize *res in transitu*. Their location is an accidental state of transit or there is no location at all, for example because the goods are being transported by the open sea or by air or space. In this case, a fictitious location will have to be found for the purpose of localizing such goods. This may, for example, be the state of dispatch or the state of destination, which latter option has been followed in Global Rule 7.2.b, as in general goods in transit will, as a rule, be most closely connected with the country of destination, being their future location. A similar solution is found in various private-international-law regulations that have opted for the rule of *lex destinationis* to determine which proprietary regime is applicable to goods in transit, see, e.g., section 101 Swiss IPRG, Article 88 Belgium, and Article 10:133 Dutch Civil Code. The term "state of destination" means the state of destination designated by the parties and will refer to the state of final destination and not, for example, a transit port. Until the goods are dispatched, they must be treated as ordinary movables and must be localized at the place where they are located.

## Rule 8 Registered Movables

**8.1. Registered movables, and separately registered rights vested in or attached to them, are located at the place where the movable or the right in question is recorded in a public register designated for the registration of rights.**

**8.2. For the purposes of Global Rule 8.1, unless there is proof to the contrary, registered movables shall be presumed to be located at the place where the movable is recorded in a public register designated for the registration of rights.**

**Comment to Global Rule 8:**

Registered movables are movables that are recorded in a public register designated for the registration of rights. Examples are registered vessels and registered aircraft. Some absolute rights vested in movables are recorded separately in a public register designated for the registration of rights. The English floating charge is an example (see below). The term "separately registered rights" attached to the movable refers to rights that are not vested in the movable, but are "attached" to it. Examples of such rights are stipulated retention of title, privileges and priorities, and retention rights. These rights are not absolute, they are quasi property-law rights. Movables (including rights vested in or attached to them) are registered, if they are recorded in a public register designated for the registration of rights. As a rule, movables (including rights vested in or attached to them) recorded in public registers are localized at the place where they are registered. This rule established in Global Rule 8 follows Article 2(g) EU Insolvency Regulation and under the rules of private international law the "*lex registrationis*" is also the generally accepted basis for the localization of registered movables, see section 45(1) of the German EGBGB, Article 89 of the Belgian WIPR, and Article 10:127(2) and (3) Dutch Civil Code.

Global Rule 8.2 aims to provide a practical solution for registered movables that have been moved or are *in transitu*. Global Rule 8.1 for registered movables (including separately registered rights in movables) has been drafted in line with the prevailing view that, for legal purposes, registered movables are located at the place where they are recorded in a public register designated for the registration of rights. The movable is identified with the register, which represents the legal status of the movable in question. In private international law, the law of the place of registration, that is, the *lex registrationis*, is generally accepted as the reference point for the creation and transfer of rights in registered movables (vessels, aircraft). If, however, these movables are transferred from the state of registration to another state, one may wonder whether the *lex registrationis* still is the most obvious connecting factor. An example may clarify the problem. A vessel located in Finland is encumbered with a mortgage under Finnish law. Subsequently, the vessel is transferred to the Netherlands where the ship mortgage is foreclosed. The Finnish ship mortgage should, in principle, be assimilated with the Dutch equivalent. In that case, the *lex registrationis* (the law of Finland) is relevant only to the question whether the ship mortgage was established with legal validity. For the remaining issues, Dutch law will be applied. Another example relates to the question whether insolvency proceedings that have been opened can be enforced. For instance: a yacht building company, established in the Netherlands, is declared bankrupt by the Dutch courts pursuant to Article 3 EU Insolvency Regulation. At the moment that Dutch main insolvency proceedings have been opened, one of the Dutch company's ships is situated in the port of Seoul, Korea, and is arrested there by a Japanese creditor of the Dutch company. The ship sails under the Dutch flag and is registered in the Netherlands. The question is whether this asset is covered by the EU Insolvency Regulation and, therefore, whether the ship forms a part of the estate covered by the Dutch main insolvency proceedings. The answer to this question is affirmative, since the ship is registered in the Netherlands, and pursuant to Article 2(g) EU Insolvency Regulation it is therefore considered to be situated in the Netherlands. It depends, however, from Korean law, as the law of the actual location of the ship, whether the Dutch main insolvency proceedings opened pursuant to the EU Insolvency Regulation can be enforced in Korea. In such a case, the application of the EU Insolvency Regulation cannot interfere with and go against public policy in Korea. It may therefore be questioned whether, in cross-border insolvency proceedings, the decisive factor for the legal status of a registered movable is the place of registration or whether it should be its actual location. To allow such a solution, Global Rule 8.2 provides a rebuttable presumption.

## REPORTERS' NOTES

The term "public register designated for the registration of rights" (see Global Rule 8.1) means a public register recording the legal status of the movable in question. Examples of such public registers within the meaning of Global Rule 8 are the public aircraft registers as referred to in Art. 1.1(ii) of the Convention on the International Recognition of Rights in Aircraft (Geneva, 19 June 1948) and the public registers in which seagoing or inland vessels are recorded. The register (nationality of aircraft) referred to in Article 17 of the Convention on international Civil Aviation (Chicago, 7 December 1944) may be equated with the public aircraft registers. Most often vehicle license registers or license registers of motor vehicles and vessels maintained by the authorities of a state will not be public registers within the meaning referred to here, as these registers will not be aimed at recording the legal status of the movables recorded in them. As a rule, a right of pledge on a car will be localized at the place where the car is physically located at that moment. This means that movables recorded in vehicle license registers are not considered registered movables and that they fall under the localization rule for nonregistered movables.

A "floating charge" is a much-used security instrument under English law. A floating charge hovers like a cloud over the business assets (the composition of which changes continuously) of the chargor (party providing security). When the chargor becomes insolvent, the floating charge is converted into a fixed charge. This conversion process is designated by the term "crystallization." Pursuant to section 860 of the English Companies Act 2009, a floating charge is entered into a public register designated for the registration of rights and maintained by the "Registrar of Companies." As a result, a floating charge or a fixed charge is located at the place where the floating charge is registered.

Some European countries have opened the possibility of registering security rights for specific movables. The French "*gage automobile*" is an example. To be effective on third parties, the gage automobile must be recorded in a register kept by the *préfecture* where the car is registered. As a rule, this is also the agency that issues the license (*carte grise*). In these cases, the obvious solution is to localize the security right in question at the place where it is registered. See further Philippe Simler & Philippe Delebecque, Droit civil. Les sûretés. La publicité foncière, Paris: Dalloz 2009, no. 584 et seq. Special rules have been created for "mobile equipment." On November 16, 2001, under the auspices of UNIDROIT, the "Convention on International Interests in Mobile Equipment" with the accompanying "Aircraft Equipment Protocol" was established in Cape Town, South Africa. As of early 2010, the UNIDROIT convention has been signed or ratified by over 30 countries, including China, France, Germany, India, Indonesia, the United Kingdom, and the United States. This UNIDROIT Convention creates a supranational security right, an international interest, in certain categories of mobile equipment, such as aircraft. The "Aircraft Equipment Protocol" that belongs to the UNIDROIT Convention relates to flying equipment, which pursuant to the Convention and the Protocol means airframes, aircraft engines, and helicopters. In 2007, a separate Protocol was established specifically for railway rolling stock (Luxembourg Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Railway Rolling Stock). At a later stage, another Protocol will be established for spacecraft. The international interest created by the UNIDROIT Convention is not an autonomous security right, but an umbrella term covering three forms of security frequently used in international financing practice. Pursuant to Article 2.2 of the Convention, these are (a) a security agreement, (b) a title reservation agreement, and (c) a leasing agreement. Article 1 of the Convention gives definitions of these three forms of security. Pursuant to

Article 2.4 of the Convention, the existence or otherwise of any of the three forms of security is governed by the conflict-of-laws rules of *lex fori*. The international interests created in accordance with the UNIDROIT Convention are recorded in a fully automated—and currently operative—global registration system accessible to the public via the Internet (www.internationalregistry.aero). This registration system is regulated in Chapters IV-VII (Articles 16-28) of the Convention. These provisions do not only concern the organization of the registration system, they also regulate the liability of the registrar. The "Registrar of the International Registry of Mobile Assets" has his seat in Dublin, Ireland (www.aviaretor.aero). International interests created under the UNIDROIT Convention are entirely virtual. Perhaps they can be localized at the place where the registrar has his seat.

## Rule 9 Claims

**9.1. Claims payable to bearer or order, and rights vested in or attached to them, are located at the place where the bearer or order document is situated.**
**9.2. Claims of known creditors, and rights vested in or attached to them, are located at the place where the debtor has his seat or his domicile.**

### Comment to Global Rule 9:

Another grouping of assets are claims. In the Glossary of Terms and Descriptions, for "claims" a description has been given as a right to payment from the estate of the debtor, whether arising from a debt, a contract, or other type of legal obligation, whether liquidated or unliquidated, matured or unmatured, disputed or undisputed, secured or unsecured, fixed or contingent, arisen on or before the commencement of the insolvency proceedings. Claims in the meaning of Global Rule 9.1 are claims as so described. Claims—rights entitling the creditor to performance by an insolvent debtor—can be distinguished into claims of a known creditor, claims payable to bearer, and claims payable to order.

A claim payable to bearer is a claim embodied in a negotiable document with a bearer clause ("payable to bearer"). A claim payable to order is a claim embodied in a negotiable document with an order clause ("payable to X or order"). Both types of claims are tangible. Bonds are an example of claims payable to bearer. Bills of lading are an example of a claim payable to order, although admittedly in practice a bill of lading often operates as a claim payable to bearer, because the order clause included in the bill of lading has often not been activated by the parties. Rights vested in claims payable to bearer or order are absolute rights vested in a claim payable to bearer or order, for example user and security rights (usufruct, pledge). Rights attached to a claim payable to bearer or order are rights not vested in the claim payable to bearer or order, but "attached" to it, for example, the right of retention. As a general rule, rights attached to a claim payable to bearer or order are not absolute; they are regarded as quasi property-law rights. Finally, unlike claims of a known creditor, claims payable to bearer or order are embodied in a negotiable instrument.

Both types of claims (payable to bearer and to order) are tangible and are therefore localized in the same way. Because claims payable to bearer or order are tangible, they are equated with nonregistered movables and deemed to be located at the place where the bearer or order document is (physically) located.[353] The same rule applies pursuant to the general rules of private international law, see, e.g., section 106(2) of the Swiss IPRG.

All claims that are not claims payable to bearer or order are claims of a known creditor. A claim of a known creditor is intangible. Claims of a known creditor are characterized by the fact that the creditor is known to the debtor. Examples of such claims are a current account of the insolvent debtor held with a bank or a claim for payment of a purchase price that a creditor has against the insolvent debtor on account of the sale of a movable or immovable. Rights vested in claims with a known creditor are absolute rights, for example user and security rights (usufruct, pledge), while rights attached to a claim with a known creditor are rights that are not vested in a claim with a known creditor, but are "attached" to it, for instance a priority right. As a general rule, rights attached to a claim with a known creditor are not absolute, but seen as quasi property-law rights.

Unlike claims payable to bearer or order, claims with a known creditor are not embodied in a negotiable instrument. They are intangible. This means that, strictly speaking, localizing claims with a known creditor based on their nature is illusory. In the context of insolvency proceedings, however, the location of claims with a known creditor can be a relevant issue, for example in connection with determining the scope of effect of insolvency proceedings that have been opened. In that case, there are several conceivable solutions, which in this Report are limited to three: (i) to localize a claim with a known creditor (fictitiously) at the place where either the creditor or the debtor has his seat or his domicile, (ii) to localize such a claim to the place where its counterpart (the obligation) has to be performed, or (iii) localizing the claim at the seat or domicile of the debtor, in spite of the fact that the claim, being an asset, is included in the creditor's assets. Global Rule 9.2 follows the latter alternative, because a claim with a known creditor must be asserted at the place where the debtor has his seat or his domicile. A comparable solution is found in Article 2(g) EU Insolvency Regulation. Pursuant to this provision, pecuniary claims are localized in the Member State within the territory of which the third party required to meet them has the center of his main interests. The alternative also is reflected in section 167(3) of the Swiss IPRG.[354]

Several claims against the debtor may arise from noncontractual sources, for instance from tort or delict, unjust enrichment, and management of another's business (*negotiorum gestio*). The passive side of such a claim is an obligation of the debtor that corresponds to a claim by a known creditor. For this reason, claims arising from tort or delict, unjust enrichment, undue payment, and management of another's business will have to be localized at the place where the debtor has his seat or his domicile.

## REPORTERS' NOTES

For the purposes of determining the domicile of the debtor, a distinction must be made between natural persons and legal entities. Natural persons are domiciled at the place where they have their habitual residence or practice an occupation, if applicable. Legal entities, on the other hand, will, as a rule, have their (registered) seat at the place where they have their registered office. Pursuant to Article 2(g) EU Insolvency Regulation, claims with a known creditor are localized at the place where

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[353] See, e.g., Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 313.

[354] Compare Swiss Federal Supreme Court 6 March 2008 (no. 4a-231/2007).

the debtor "has the centre of his main interests" as determined in Article 3(1) of the Regulation. For this purpose, the latter provision contains a presumption with respect to companies and legal persons in favor of the registered office. The preamble (recital 13) to the Regulation shows that "the centre of main interests" shall mean the place where the debtor conducts the administration of his interests on a regular basis and that is therefore ascertainable as such by third parties. It is acknowledged that there is legal uncertainty as to the details of this central criterion, which especially has been demonstrated in court cases in which international jurisdiction has to be determined. See, e.g., ECJ 2 May 2006, Case C-341/04 (*Eurofood*). In a case in which the debtor in state A holds a bank account in a branch of bank X, where the branch is in state B and bank X has its registered seat in state C and the center of its main interest in state D, the localization of the claim will be in state D, and not for instance in state B, in which the branch is situated. In this way, too, 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, p. 303ff, criticizing Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 312, who have defended the latter approach, which clearly deviates from the text of Article 2(g) of the EU Insolvency Regulation.

## Rule 10 Shares in Joint-Stock Companies

**10.1. Bearer shares, and rights vested in or attached to them, are located at the place where the bearer share certificate is situated.**
**10.2. Registered shares, and rights vested in them, are located at the place where the registered share, or the right vested in it, is recorded in a register of shareholders kept by the company.**
**10.3. If a registered share, or a right vested in it, is not recorded in a register of shareholders, the registered share or the right vested in it is located at the place where the company has the center of its main interests. The center of the main interests of the company is presumed to be the place of its registered office.**
**10.4. Book-entry shares, and rights vested in them, are located at the place of the registered office of the intermediary with which the securities account is kept in which the book-entry shares are administered.**

### Comment to Global Rule 10:

Following the Glossary of Terms and Descriptions, in general a share means the right to a proportional share in the capital of a company. Three groups of shares can be distinguished, namely bearer shares, registered shares, and book-entry shares. A bearer share is a share embodied in a bearer share certificate. A bearer share is tangible. Global Rule 10.1 provides a localization rule for bearer shares. A registered share is a share to which a specific person is entitled. As a rule, registered shares are intangible. Share certificates may be issued. This does not change the intangible nature of the registered share, however. Localization of registered shares is the subject of Global Rules 10.2 and 10.3. Thirdly, there is a book-entry share, which is a share that is kept and administered exclusively via a securities account. Book-entry shares are intangible. For its localization, see Global Rule 10.4.

Bearer shares are shares embodied in a bearer share certificate. Rights vested in bearer shares are absolute rights vested in a bearer share, for example usufruct or pledge. Rights attached to a bearer share mean rights that are not vested in the bearer share, but are "attached" to it. The right of retention is an example of such a right. As a rule, rights attached to a bearer share are not absolute; they are quasi property-law rights. In contrast with registered shares, bearer shares are embodied in a bearer share certificate. Although the practical relevance of bearer shares is increasingly diminishing as a result of the advancing dematerialization of security transactions, a localization rule has been drafted in Global Rule 10.1. Because bearer shares are tangible, they are equated with nonregistered movables, bearer documents, and order paper, and they are deemed to be located at the place where the bearer share certificate is (physically) situated. This principle is defended in literature[355] and is applied in codifications of general rules of private international law, for example, Article 91 §2 of the Belgian WIPR.

Registered shares are shares to which a specific person is entitled. Rights vested in registered shares are, for example, user and security rights (usufruct, pledge). In contrast to bearer shares, registered shares are as a rule not embodied in a security certificate. They are intangible. This means that strictly speaking localizing registered shares is a fictitious exercise. In the context of insolvency proceedings, however, the location of registered shares can be a relevant issue, for example in connection with determining the scope of effect of insolvency proceedings that have been opened. Registered shares and user and security rights vested in them must often be entered in a register of shareholders kept by the company. In that case, the obvious solution is to localize the registered shares there. A register of shareholders, in general, will be kept by the management of a company in which the names of all shareholders and, if applicable, of all holders of rights less than ownership (usufructuaries, pledgees) are recorded. Global Rule 10.3 deals with an absence of registration. In instances where there is no register of shareholders, the rule has been adopted that the registered share or the right vested in it is localized at the place where the company has the center of its main interests. See, for the term "center of the main interests," the Comment to Global Rule 9.2.

Book-entry shares are shares that are kept and administered exclusively via a securities account. Rights vested in book-entry shares are absolute rights vested in book-entry shares, for example user and security rights (usufruct, pledge). In contrast to bearer shares, book-entry shares are not embodied in a security certificate. They are intangible, which means that strictly speaking, as with registered shares, localizing of book-entry shares is a fictitious exercise. In the context of insolvency proceedings, however, the location of book-entry shares can be a relevant issue, for example in connection with determining the scope of effect of insolvency proceedings that have been opened. Book-entry shares are always administered in a securities account. It is therefore an obvious solution to localize book-entry shares at the place of the registered office of the intermediary with which the securities account is kept in which the book-entry shares are administered. See Global Rule 10.4. The proposed localization rule in Global Rule 10.4 has a wider scope of application than to book-entry shares alone. The rule can be applied to all securities (shares, bonds, options, and other derivatives) that are administered and traded via a book-entry system.

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[355] See, e.g., Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 313, and, with some reluctance, P.M. Veder, *Goederenrechtelijke zekerheidsrechten in de internationale handels- en financieringspraktijk*, in: R.W. Clumpkens et al., *Zekerhèdenrecht in ontwikkeling*. Preadvies voor de Koninklijke Notariële Broederschap 2009, p. 304ff.

## REPORTERS' NOTES

In Global Rule 10.4, the chosen localization rule follows the internationally accepted "PRIMA rule" ("Place of the Relevant Intermediary Approach"), according to which book-entry securities are localized at the place of the registered office of the intermediary with which the securities account in question is kept. As a rule, this will be the place agreed by the account holder and the intermediary (custodian) in the securities custody agreement. If the securities custody agreement does not give a definite answer on this point, the securities account is deemed to be located at the place where it is kept according to the custodian's books. Although there are practical objections to the PRIMA rule, there is at present no workable alternative, and the PRIMA rule also is the basis for the referral system of the Hague Convention on the Law Applicable to Certain Rights in Respect of Securities held with an Intermediary of 13 December 2002. Article 4 of the Hague Securities Convention allows for a restricted form of choice of law between the account holder and the relevant intermediary subject to the condition that the intermediary has, at the time of the agreement, an office in the state whose law has been chosen and that one of the other requirements mentioned in Article 4 is met. The Hague Securities Convention is thus based on the law of the relevant account-agreement approach. See, inter alia, Fabian Reuschle, *Haager Übereinkommen über die auf bestimmte Rechte in Bezug auf Intermediär-verwahrte Wertpapiere anzuwendende Rechtsordnung*, IPRax 2003, pp. 495-505; Fabian Reuschle, *Grenzüberschreitender Effektengiroverkehr. Die Entwicklung des europäischen und internationalen Wertpapierkollisionsrechts*, Rabels Zeitschrift für ausländisches und internationales Privatrecht 2004, pp. 687-769; Michel Germain & Catherine Kessedjian, *La loi applicable à certains droits sur des titres détenus auprès d'un intermédiaire. Le projet de convention de La Haye de décembre 2002*, Revue critique de droit international privé 2004, pp. 49-81; Roy Goode et al., Hague Securities Convention. Explanatory Report, The Hague: Martinus Nijhoff Publishers 2005; M. Haentjens, The Law Applicable to Indirectly Held Securities, The Hague: SDU Uitgevers 2006; Elke Vandendriessche, *Het Verdrag van Den Haag van 5 juli 2006 inzake het recht toepasselijk op rechten op effecten door een intermediair gehouden: toekomst in Europa*, Tijdschrift@ipr.be, pp. 47-80.

## Rule 11 Intellectual Property Rights

**Patent rights, trademark rights, and copyrights, and rights vested in them, are located at the place where the patent holder, trademark proprietor, or copyright holder has his seat or his domicile.**

### Comment to Global Rule 11:

After having proposed localization rules for tangible assets (immoveables, registered and nonregistered moveables), claims (payable to bearer or order or related to a known creditor), and shares (bearer shares, registered shares, and book-entry shares), the remaining category in a group of "other proprietary rights" formulates localization rules for intellectual property rights. An intellectual property right is a right in a product or intellectual creation of the human mind. Intellectual property right means any intellectual property right involving copyrights, neighboring rights, patents, trade secrets, trademarks, geographic indications, other intellectual property rights, and agreements related to any of these rights. The description follows § 101(4) juncto § 102(1) of ALI's Intellectual Property Principles (2008) (adopted in 2007). Global Rule 11 proposes a localization rule for only three types of intellectual property rights: patent rights, trademark rights, and copyrights. Intellectual property rights are intangible.

For the purposes of determining the seat or domicile of the proprietor of the intellectual property right in question, a distinction must be made between natural persons and legal entities. Reference is made to the Reporters' Notes to Global Rule 9.2.

## REPORTERS' NOTES

In general, a patent right is an exclusive right to exploit a new invention in all fields of technology, a trademark right is a person's right in a trademark, which are all signs capable of being represented graphically serving to distinguish the goods or services of an enterprise. This description is derived from Art. 2(1) of the Benelux Convention concerning Intellectual Property (Trademarks and Designs) of 25 February 2005. A copyright is the exclusive right vesting in the maker (author) of a literary, scientific, or artistic work or his successors in title to communicate that work to the public and to reproduce it.

Rights vested in patent rights, trademark rights, and copyrights are absolute rights vested in patent rights, trademark rights, and copyrights, such as user and security rights (usufruct, pledge). Where patent rights, trademark rights, and copyrights are intangible, they qualify as intellectual property rights in a general sense. This means that strictly speaking the localization of intellectual property rights is fictitious. In the context of insolvency proceedings, however, the location of intellectual property rights can be a relevant issue, for example in connection with determining the scope of effect of insolvency proceedings that have been opened. Some intellectual property rights are registered, but the registration of intellectual property rights is, however, a "hotchpotch" (see Th.C.J.A. van Engelen, Intellectuele Eigendomsrechten registergoederen?, Intellectuele Eigendom & Reclamerecht (IER) 2002, pp. 275-281), and for this reason, it cannot be used as a basis for localizing these proprietary rights. It may be this current confusing state of affairs that has led the Insolvency Regulation to adopt the rule that, for the purposes of the Insolvency Regulation, a Community patent, a Community trademark, or any other similar right established by Community law may be included only in the main insolvency proceedings (Article 12 of the EU Insolvency Regulation).

Various EC Regulations in the field of intellectual property rights provide that the law applicable to the intellectual property right in question shall be determined on the basis of the seat or domicile of the proprietor of the intellectual property right. See, for example, Article 16(1) of the Community trademark regulation (Council Regulation (EC) no. 40/94 of 20 December 1993 on the Community trademark (OJ EC 1994, L 11/1) pursuant to which the seat or domicile of the trademark proprietor determines which law is applicable to the Community trademark. Similarly, see Article 22 of the Council Regulation (EC) no. 2100/94 of 27 July 1994 on Community plant variety rights (OJ EC 1994, L 227/1), and Article 27 of Council Regulation (EC) no. 6/2002 of 12 December 2001 on Community designs (OC EC 2002, L 3/1).

For the purposes of determining the seat or domicile of the proprietor of the intellectual property right in question, a distinction must be made between natural persons and legal entities. Reference is made to the Reporters' Notes made to Global Rule 9.2.

## C. General Rules of Law Applicable to Insolvency Proceedings

### Rule 12 Law of the State of the Opening of Proceedings

**12.1. Save as otherwise provided in [this Act/these Rules], the law applicable to insolvency proceedings and their effects shall be that of the state within the territory of which such proceedings are opened, hereafter referred to as "the state of the opening of proceedings."**
**12.2. The law of the state of the opening of proceedings shall determine the conditions for the opening of those proceedings, their conduct, administration, conversion, and their closure.**

### Comment to Global Rule 12:

Since May 2002, in the larger part of Europe, a consensus has emerged for the application of the so-called *lex fori concursus* rule. According to that rule, the law of the jurisdiction ("state") in which insolvency proceedings are opened will govern the commencement, conduct, administration, and conclusion of those proceedings. This is perhaps most succinctly expressed by the terms of Article 4(1) of the EU Insolvency Regulation ("Save as otherwise provided in this Regulation, the law applicable to insolvency proceedings and their effects shall be that of the Member State within the territory of which such proceedings are opened, hereafter referred to as "the State of the opening of proceedings"). The UNCITRAL Legislative Guide on Insolvency Law contains a similar rule (recommendation 31).

A common feature found in these legislative provisions—and in Article 4(1) EU Insolvency Regulation—is the choice that has been made for the so-called *lex fori concursus* rule, which should be applied as the general choice-of-law rule for insolvency proceedings. In academic circles, the traditional dichotomy in discussions of international bankruptcy has been between territorialism and universalism. See the ALI-NAFTA report, Lynn M. LoPucki, Universalism Unravels, in: 79 American Bankruptcy Law Journal 2005, 143ff.; Ian F. Fletcher, Insolvency in Private International Law. National and International Approaches, Oxford Private International Law Series, Oxford University Press, 2nd ed. 2005, 1.01ff.; Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, para. 10009ff., also discussion of other concepts); John Pottow, The Myth (and Realities) of Forum Shopping in Transnational Insolvency, in: 32 Brooklyn Journal of International Law 785 (2007); Edward J. Janger, Universal Proceduralism, 32 Brooklyn Journal of International Law 819 (2007); Edward J. Janger, Virtual Territoriality, Brooklyn Law School, Legal Studies Research Paper No. 169, October 2009 (http://ssrn.com/abstract=1468615) (last visited Mar. 9, 2012); Christoph Paulus, *Deutsches Internationales Insolvenzrecht (§§ 335 ff. InsO und Art. 102 EGInsO)*, Kapitel 46, Kölner Schrift zur Insolvenzordnung, 3. Aulage, Münster: ZAP Verlag 2009, nr. 4. The aforementioned legislative developments in Europe and UNCITRAL's recommendation seem to confirm the almost universal agreement that the principle is that, unless otherwise stated, the law applicable to insolvency proceedings and their effects shall be that of the state within the territory of which such proceedings are opened. This proposition is expressed in Global Rule 12.1.

It is possible to further explain which topics are to be covered by the general rule of applicable law, being the law of the jurisdiction in which insolvency proceedings are opened that governs the commencement, conduct, administration, and conclusion of those proceedings. Article 4(2) of the EU Insolvency Regulation declares expressly as follows: "The law of the State of the opening of proceedings shall determine the conditions for the opening of those proceedings, their conduct and their closure." Article 4(2) also contains a long list of particular matters, contained in sub-paragraphs (a) to (m), which are specifically included within the general proposition expressed in Article 4 to the effect that the *lex fori concursus* has a dominant role at every stage of the insolvency process. The same principle as that found in Article 4 of the EU Regulation is expressed in nonlegislative terms in the UNCITRAL Legislative Guide on Insolvency Law, recommendation 31, which also includes a large group of examples ((a) to (s)), which fall within the remit of the general proposition to the effect that the *lex fori concursus* has controlling application save where an express exception is imposed. As the matters expressed in sub-paragraphs (a) to (m) of Article 4(2) of the EU Insolvency Regulation only have an illustrative character, they are not incorporated in Global Rule 12.2. This approach (mentioning the general rule; abstain from detailed examples) also has been chosen in Germany (Article 335) and the Netherlands (draft Article 10.4.1).

The law of the jurisdiction in which insolvency proceedings are opened that governs the commencement, conduct, administration, and conclusion of those proceedings will, in particular, also determine the rules relating to the voidness, voidability, or unenforceability of legal acts detrimental to the general body of creditors. Rules for the avoidance of prior transactions to which an insolvent debtor has been a party are of particular significance in international cases, because of the numerous ways in which the substantive provisions contained in national laws differ from one another, thereby causing uncertainty for parties in their dealings. The answer to the question whether a given transaction may be successfully impeached in the event of the insolvency of one of the parties to it can, in many instances, depend on the choice-of-law process employed by the court before which the matter is brought. Although, in the interests of reducing that element of uncertainty, it could be considered appropriate to include a clear and explicit affirmation of the basic principle that the *lex fori concursus* shall determine any matter of voidness, voidability, or unenforceability of legal acts on the ground that they are detrimental to the general body of creditors, we have not included this proposition in the express wording. It is noted that Article 4(2)(m) of the EU Insolvency Regulation contains the expression "acts detrimental to all the creditors" instead of "acts detrimental to the general body of creditors." The earlier expression (which appears in the official English version of the EU Regulation) is inappropriate because, literally, it would require proof that the act in question was detrimental to every single creditor including any creditor who happened to be a beneficiary of the very act that is impeached. It should be noted that, in other language versions of the EU Insolvency Regulation, the expression "general body of creditors" is used (French: "*l'ensemble des créanciers*"; German: "*die Gesamtheit der Gläubiger*"; Dutch: "*het geheel van schuldeisers*"). It should be noted too that the rule that the *lex concursus* determines the rules relating to the voidness, voidability, or unenforceability of legal acts detrimental to the general body of creditors, is subject to the further rules contained in Global Rule 21.

## REPORTERS' NOTES

In legal literature, the law of the "state of the opening of proceedings," is known as the "*lex concursus*," or the "*lex fori concursus*." The proposition that the law of the state of the opening should be accorded a dominant role in insolvency proceedings is expressed by the further Latin maxims: "*lex fori regit concursus*" or "*lex fori in foro proprio*." The choice in the EU Insolvency Regulation for the *lex concursus* is, in general, justified or at least remains uncriticized by the majority of legal commentators, see Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, no. 69; (German authors mentioned by) Verena Lorenz, *Annexverfahren bei Internationele Insolvenzen. Internationale Zuständigkeitsregelung der Europäischen Insolvenzverordnung.* Max-Planck-Institute für ausländisches und internationals Privatrecht. Studien zum ausländischen und internationalen Privatrecht, nr. 140, Tübingen: Mohr Siebeck, 2005, 44; Ian F. Fletcher, Insolvency in Private International Law. National and International Approaches, Oxford Private International Law Series, Oxford University Press, 2nd ed. 2005, 7.80; Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, para. 10624. Global Rule 12 formulates a point of departure as the applicability of the *lex concursus* must be seen in the light of certain exceptions ("Save as otherwise provided in [this Act/these Rules]"). In Global Rule 5 (Exclusion of Revoi), the rule is laid down that, in applying the Global Rules, any reference to the law of a state means the internal rules of law in force in that state other than its rules of private international law. For the descriptions of the key terms "applicable," "insolvency proceeding," "State," and "opening of proceedings," see the Glossary of Terms and Descriptions in the Appendix.

In the context of Global Rule 12, the term "law" deserves attention. Due to the universal effect of the *lex concursus*, the "law" of one state is, in principle, extended to other states. In the light of the Glossary and Global Rule 5 (Exclusion of Renvoi), "law" in principle means a certain state's substantive and procedural law, including its soft law, but excluding its rules of private international law. In respect of the insolvency proceedings and their effects, Article 4(1) of the EU Insolvency Regulation, the English, French, and Dutch texts use the wording "the law applicable" ("*la loi applicable*," "*het recht van de lidstaat*") respectively, whereas the German and the Austrian text refer to the applicability for the insolvency proceedings and their effects of "*das Insolvenzrecht des Mitgliedstaats*," meaning: the applicability of (only) the insolvency laws of the Member State (of the opening of proceedings). In recital 23, it is said: "This Regulation should set out, for the matters covered by it, uniform rules on conflict of laws which replace, within their scope of application, national rules of private international law," which seems to cover a broader scope than what follows from the German text of recital 23, in which "for the matters covered by it" is expressed as "*für den Insolvenzbereich*" (within the scope of insolvency). Consequently, Austrian and German authors are discussing whether certain topics belong to the domain of (German internal) insolvency law, for example, the issue of whether director's liability is an "insolvency" question. See also H.-C. Duursma-Kepplinger, in: Duursma-Kepplinger, H.-C, Duursma, D, Chalupsky, E., *Europäische Insolvenzverordnung. Kommentar*, Springer, Wien New York, 2002, Art. 4, nr.7; Ulrich Huber, *Inländische Insolvenzverfahren über Auslandgesellschaften nach der Europäischen Insolvenzverordnung*, in: Schilken, Eberhard et al., ed., Festschrift für Walter Gerhardt, RWS Verlag Kommunikationsforum 2004, p. 426. If so, these rules are exported to the other EU Member States when main proceedings are opened in Austria or Germany. The wording in the German and Austrian texts certainly indicates a narrower meaning of the *lex concursus* than the wording in other texts, as certain legal rules of "the law applicable to insolvency proceedings" may fall outside a Member State's domain of "insolvency law," falling instead under general civil law or general company law, but nevertheless applicable to insolvency proceedings. The width of the rule of the *lex concursus* is not only a European question, as in the Extract of UNCITRAL Legislative Guide the recommendation with regard to "Law applicable in insolvency proceedings" reads: "(31) The insolvency law of the state in which insolvency proceedings are commenced (*lex fori concursus*) should apply to all aspects of the commencement, conduct, administration and conclusion of those insolvency proceedings and their effects." In this Report, we submit the broader scope of the term "law"; thus the reference to the "law" of the state of the opening of proceedings is not limited to this state's insolvency law. In addition, some states will contain their "insolvency law" within an Act bearing a specific appellation referring to insolvency or bankruptcy and will not include general corporate, procedural, or civil-law rules related to insolvency under the description of "insolvency" law. To limit the reference only to such legislation as actually bears the terms "insolvency" or "bankruptcy" within its title would be to confuse form with substance, and would give rise to uneven and distorted results according to the variable practices followed by different states. In this way, too, (concerning the specific liability of a company director under Germany's Article 64(1) Gesetz betreffend die Gesellschaften met beschänkter Haftung) Udo Weiss, *Strafbare Insolvenzverschleppung durch den director einer LTD.* Schriftenreihe zum deutsche, europäischen under internationalen Wirtschaftsrecht, 9, Baden-Baden: Nomos Verlag 2009, p. 46ff. For this reason, the reference to the *lex concursus* encompasses the whole system of legal rules of the state in question (apart from its rules of private international law, see Global Rule 5), and not merely those rules that are formally classified as pertaining to the law of insolvency. As a result, the "law" applicable also contains the rules relating to director's liability, rules relating to land pollution or tax laws applicable for action done by a foreign insolvency holder in the respective state. This interpretation also means that "law" should not be understood as the rules of the law that serve as to guarantee that insolvency proceedings are administered to reach their goal of satisfying the general body of creditors (in this way, e.g., Virgós / Schmit Report, nr. 90, H.-C. Duursma-Kepplinger, in: Duursma-Kepplinger, H.-C, Duursma, D, Chalupsky, E., *Europäische Insolvenzverordnung. Kommentar*, Springer, Wien New York, 2002, Art. 4, nr. 7, and Horst Eidenmüller, *Gesellschaftsstatut und Insolvenzstatut*, in: 70 Rabels Zeitschrift für ausländisches und internationales Privatrecht 2006, p. 483).

In many cases, the choice-of-law analysis in insolvency is two-sided, see Jay L. Westbrook, The Present and Future of Multinational Insolvency, in: Bob Wessels and Paul Omar (eds.), The Intersection of Insolvency and Company Laws, Nottingham, Paris: INSOL Europe 2009, pp. 111-125, at p. 113, submitting that, in many instances, the case will involve "non-insolvency law" (e.g., the creation of a right or the existence and performance of a contract, prior to opening of insolvency proceedings and "insolvency law," which will govern the treatment of a right or a contract in the insolvency proceeding, such as the enforceability of the contract claim and the fixing of the amount actually to be paid. Westbrook uses the Lernout & Hauspie case (*Lernout & Hauspie Speech Products N.V. v. Stonington Partners, Inc.*, 268 B.R. 395 (D. Del. 2001), rev'd, 310 F.3d 118 (3d Cir. 2002), on remand In re *Lernout & Hauspie Speech Products N.V.*, 301 B.R. 651 (Bankr. D. Del. 2003)) in the United States and Belgium, in which case the court—thus Westbrook—failed to see that two different choice-of-law questions were presented under the differing priority rules in the two countries (one of "non-insolvency law" and one "insolvency law"). In a recent Dutch case, The Netherlands Supreme Court 19 December 2008, LJN: BG3573, such a distinction is made. The Russian *OAO Yukos Oil Company* is a company having its registered office in Moscow that has been established and is organized under the laws of the Russian Federation ("Yukos Oil"). The shares of Yukos Finance B.V. ("Yukos Finance"), a private company with limited liability, whose registered office is in Amsterdam, are held by Yukos Oil. Therefore, Yukos Oil holds the voting rights on all shares in Yukos Finance B.V, and—generally—should be able to control the assets of Yukos Finance, including (direct and indirect) holdings of shares in several other companies, including an indirect holding of 53.7% in AB Mazeikiu Nafta ("Mazeikiu"), the refinery company in Lithuania. Does the Russian insolvency holder have the power to vote on the shares? The Supreme Court agrees with the opinion of the plaintiffs (Yukos Finance) that, according to Dutch private international law, the question relating to the existence and meaning of the powers of a curator in bankruptcy liquidations proceedings is a question of insolvency law ("Answering this question will be determined by the law which is applicable to such bankruptcy proceedings, and therefore—contrary to what the court of appeal has decided concerning this point—it must be assessed whether the principle of territoriality of a bankruptcy liquidation, which is leading in Dutch private international law, limits the possibility that the defendant in his capacity of temporary administrator in the bankruptcy of Yukos Oil exercises the voting rights based on the shares in Yukos Finance"). In 2012, the Netherlands Supreme Court will decide on the merits of the case.

After these questions of qualification, the question then arises as to how the validity and the contents of foreign law should be proven to a court in another state if that court wishes to be informed of such matters. See the Reporters' Notes to Global Rule 3.

As mentioned above, Article 4(2) of the EU Insolvency Regulation contains an enunciative list of 13 subjects that are determined by the *lex concursus*. Below follows the text.
2. The law of the State of the opening of proceedings shall determine the conditions for the opening of those proceedings, their conduct and their closure. It shall determine in particular:
(a) against which debtors insolvency proceedings may be brought on account of their capacity;
(b) the assets which form part of the estate and the treatment of assets acquired by or devolving on the debtor after the opening of the insolvency proceedings;
(c) the respective powers of the debtor and the liquidator;
(d) the conditions under which set-offs may be invoked;
(e) the effects of insolvency proceedings on current contracts to which the debtor is party;
(f) the effects of the insolvency proceedings on proceedings brought by individual creditors, with the exception of lawsuits pending;
(g) the claims which are to be lodged against the debtor's estate and the treatment of claims arising after the opening of insolvency proceedings;
(h) the rules governing the lodging, verification and admission of claims;
(i) the rules governing the distribution of proceeds from the realisation of assets, the ranking of claims and the rights of creditors who have obtained partial satisfaction after the opening of insolvency proceedings by virtue of a right in rem or through a set-off;
(j) the conditions for and the effects of closure of insolvency proceedings, in particular by composition;
(k) creditors' rights after the closure of insolvency proceedings;
(l) who is to bear the costs and expenses incurred in the insolvency proceedings;
(m) the rules relating to the voidness, voidability or unenforceability of legal acts detrimental to all the creditors.
Recommendation 31 of the UNCITRAL Legislative Guide on Insolvency Law contains the same structure. Below follows the text.
Law applicable in insolvency proceedings
(31) The insolvency law of the State in which insolvency proceedings are commenced (*lex fori concursus*) should apply to all aspects of the commencement, conduct, administration and conclusion of those insolvency proceedings and their effects. These may include, for example:
(a) Identification of the debtors that may be subject to insolvency proceedings;
(b) Determination of when insolvency proceedings can be commenced and the type of proceeding that can be commenced, the party that can apply for commencement and whether the commencement criteria should differ depending upon the party applying for commencement;
(c) Constitution and scope of the insolvency estate;
(d) Protection and preservation of the insolvency estate;
(e) Use or disposal of assets;
(f) Proposal, approval, confirmation and implementation of a plan of reorganization;
(g) Avoidance of certain transactions that could be prejudicial to certain parties;
(h) Treatment of contracts;
(i) Set-off;
(j) Treatment of secured creditors;
(k) Rights and obligations of the debtor;

(l) Duties and functions of the insolvency representative;
(m) Functions of the creditors and creditor committee;
(n) Treatment of claims;
(o) Ranking of claims;
(p) Costs and expenses relating to the insolvency proceedings;
(q) Distribution of proceeds;
(r) Conclusion of the proceedings; and
(s) Discharge.

## Rule 13 Law of the State of the Opening of Non-Main Proceedings

**If insolvency proceedings are opened in a jurisdiction other than that where the center of main interests of the debtor is situated ("non-main" proceedings), the effects of the application of the law of the state of the opening of such proceedings shall be restricted to those assets of the debtor situated in the territory of that state at the time of the opening of those proceedings.**

### Comment to Global Rule 13:

Global Rule 13 lays down the rule that, when proceedings are opened in a jurisdiction other than that where the COMI is located (such as on the basis of an establishment of the debtor or merely the presence of assets of the debtor), the application of the full effects of the *lex fori concursus* is confined to those assets of the debtor that are situated within the territory of the state of the opening of the proceedings. The effect of Global Rule 13 is that its legal norm freezes the legal status quo, especially in relation to tangible assets.

### REPORTERS' NOTES

Global Rule 13 epitomizes the pragmatic accommodation of competing principles that lie at the heart of the theory of modified universalism. Global Rule 12 expresses a general rule for all insolvency proceedings that are opened at the debtor's center of main interests. Those proceedings are accorded the maximum degree of authority in relation to the debtor's global estate. In many legal systems in the world, it is contemplated that international insolvency matters, relating to one debtor, may be decided in two or more states where such proceedings are opened concurrently. Logically, only one set of proceedings can correctly claim the status of "main" proceeding by virtue of being opened at the debtor's center of main interests. Other proceedings may nevertheless be eligible for international recognition on the basis that they have been opened in a jurisdiction where the debtor has an establishment, while in other cases the debtor's connection with the place of opening may fall short of meeting that criterion. Global Rule 13, in principle, applies to all such proceedings, independently of their nature or name, (e.g., independent territorial, secondary, parallel, or ancillary) proceedings. The model of allowing two or more separate insolvency proceedings to be conducted parallel to each other has been accepted in all modern models for the regulation of international insolvency proceedings, see, e.g., Articles 28 and 29 of the UNCITRAL Model Law, including those countries that have enacted these provisions: Articles 3 and 27 of the EU Insolvency Regulation and the legislation of, e.g., Croatia (Article 302), Germany (Articles 354-358), Republic of Slovenia (Article 479 Slovenian Insolvency Act), Switzerland (Article 50), and the Netherlands (pre-draft Articles 10.2.1-10.2.6). The general aim of these "non-main" proceedings is: (i) to provide comfort to local creditors to file their claims in a court nearby, (ii) to prevent a race among creditors to initiate enforcement proceedings regarding the debtor's assets in jurisdictions that would allow them to do so, and (iii) to prevent the insolvent debtor from taking actions that would be detrimental to the creditors. See Jasnica Garašić, Recognition of Foreign Insolvency Proceedings: the Rules that a Modern Model of International Insolvency Law Should Contain, in: Yearbook of Private International Law, 2005, vol. 5, p. 349. The application of the *lex fori concursus* rule, therefore, is not limited to those cases where insolvency proceedings are opened at the place where the debtor's COMI is located.

## Rule 14 Cross-Border Movement of Assets

**In relation to any asset of the debtor that is of a moveable character, Global Rules 12 and 13 shall apply, subject to the following modifications:**

**(a) Any rule of insolvency law that is applicable by virtue of the localization of an asset in the territory of the state of the opening of insolvency proceedings, at the time of the opening of the proceedings, shall not apply if it is shown that the asset in question has been moved to that location from the territory of another state, to whose insolvency law it would otherwise have been properly subject, in circumstances that suggest that the transfer was effected wholly or primarily for the purpose of avoiding the effects of the law of the other state, including its insolvency law.**

**(b) Conversely, where an asset has been moved from the territory of one state to that of another state under the circumstances stated in paragraph (a), the effects of any insolvency proceedings that are opened in the former state shall apply to the asset in question.**

**(c) In the absence of evidence to the contrary, it shall be presumed that any asset that has been removed from the territory of the state in which insolvency proceedings are opened, within 60 days prior to the opening of such proceedings, was made with intent to avoid the effects of the law of that state. It is for the party who seeks to maintain the validity of the act, whereby the property was removed from the territory of that state, to provide evidence that the transfer was made for a bona fide and legitimate purpose.**

**(d) Except in a case to which paragraph (c) is applicable, it is for the party who alleges that the provisions of paragraphs (a) and (b) of this Rule are applicable in relation to a particular asset to prove that this is the case.**

### Comment to Global Rule 14:

Where both Global Rule 12 (for main insolvency proceedings) and 13 (for non-main proceedings) aim to prevent complications relating to the law applicable and to protect the interests of creditors relying on them, the application of the *lex fori concursus* to assets situated in the territory of the state of the opening of insolvency proceedings should not apply to assets or property that have been moved there from the territory of another state, to whose insolvency law they would otherwise have been properly subject, in circumstances that suggest that the transfer was effected wholly or primarily for the purpose of avoiding the effects of the law of the latter state, including its insolvency law. Conversely, the scope of insolvency proceedings, including territorial proceedings opened in the circumstances indicated in Global Rule 13, can be legitimately extended to include property that was transferred from the territory of the state of the opening of those proceedings in circumstances that support the conclusion that the transaction was motivated by the aim of avoiding the application of that state's law. Global Rule 14 aims to address these situations with the intention to modify the effects of the *lex concursus*, which flows from Global Rules 12 and 13.

It is appreciated that in matters where the operation of a rule of exception is dependent upon establishing the motive or intention that accompanied the acts in question, considerable difficulties concerning the matters of evidence and proof are likely to be experienced by any party—such as the liquidator or trustee in bankruptcy—seeking to invoke the rule. The solution embodied in paragraphs (c) and (d) of Global Rule 14 is to make it incumbent upon any party seeking to maintain the validity of any relocation of property that has taken place within a defined number of days prior to the opening of insolvency proceedings to adduce evidence to show that the transfer of the property was made for a bona fide purpose. The number of days could be 30, 60, 120, or any number of days. A period of 60 days has been found appropriately reflecting a fair balance between the protection of creditors' interest against the interest of the party seeking to prove the validity of his act. If a cross-border relocation of property has occurred at an earlier time than said 60 days, the effect of Global Rule 14, paragraph (d), is to make it incumbent on the party who contends that either paragraph (a) or (b) is applicable, to assume the onus of proving that the circumstances were such as to suggest, on the balance of probabilities, that the transfer was effected wholly or primarily for the purpose of avoiding the effects of the insolvency law of the state in which it was located immediately prior to relocation.

## D. Exceptions to the General Rules of Law Applicable to Insolvency Proceedings

### Introductory Comment:

In many states, where the general rule regarding law applicable is followed, modifications exist, either laid down in law or based on judgments of courts. Three groups of modification can be distinguished, one of which is of relevance for the present purposes. The effects of law applicable as a result of opening of main insolvency proceedings in state A can be limited by the opening of a non-main proceeding in state B (and state C). In such cases in principle, in state B, the *lex concursus* of state B, therefore the state's own law, will apply (and likewise for state C). A second method to limit the effects of the law of state A is—if no non-main proceedings have been opened—the right to invoke a public-policy exception. Also in the Global Principles, such an exception has been formulated, see Global Principle 3(iii) (public policy). Both these modifications are not further dealt with here. A third possibility is to create an exception to the general rule. In general, two categories of exceptions can be distinguished. One is an exception that takes the form of a substantial norm which expresses such exception. The other one introduces another point of departure in the meaning of a choice-of-law rule; therefore, instead of a choice for the law of the state in which a main insolvency proceeding has been opened (*lex concursus*), there is substituted a choice for another connecting factor, for instance for the law of the state in which an asset is situated (*lex rei sitae*) or the law of the state applicable to a contract of a certain nature (*lex causae*). These forms of exceptions are also to be found in the EU Insolvency Regulation.

The opening words of Article 4(1) of the EU Insolvency Regulation ("Save as otherwise provided in this Regulation . . .") indicate that the general rule of applicability of the *lex fori concursus* is subject to various exceptions. Its rationale is provided in recital 24: "To protect legitimate expectations and the certainty of transactions in Member States other than that in which proceedings are opened, provisions should be made for a number of exceptions to the general rule." These exceptions are provided by the further provisions of Articles 5 to 15 inclusive, which deal with a number of specific cases. The UNCITRAL Legislative Guide concedes the necessity of achieving a balance between the desirability of exceptions to the application of the *lex fori concursus*, which may produce advantages for certain individuals, and the goal of maximizing the value of the insolvency estate for the benefit of all creditors. The Guide mainly opted for the latter approach (instead of substituting for the *lex concursus* a choice of another law as connecting factor). The EU Insolvency Regulation contains three substantial exceptions to the general rule (for rights in rem, set-off, and reservation of title, Articles 5-7 InsReg) and seven choices of law (other than the *lex fori concursus*, Articles 8-15 InsReg). The UNCITRAL Legislative Guide advocates a position under which the exceptions are largely eliminated (see Recommendations (32) and (33)). Only two exceptions (other choices of law) are accorded any degree of support in the Legislative Guide, namely (a) carveouts that allow the effects of insolvency proceedings on the rights and obligations of participants in a payment or settlement system, or in a regulated financial market, to be governed solely by the law applicable to that system or market, and (b) carveouts that allow the effects of insolvency proceedings on rejection, continuation, and modification of labor (employment) contracts to be governed by the law applicable to the contract. These two categories of exception correspond to those embodied in Articles 9 and 10, respectively, of the EU Insolvency Regulation.

In the light of these developments, the question is whether, in principle, it is currently appropriate, or acceptable, to eradicate virtually all exceptions to the application of the *lex fori concursus*, or whether a number of specific exceptions should be introduced, and if so, which ones. These exceptions are related to certain policy goals that a state may seek to protect against the influence of another state's law that is applicable to the insolvency proceeding, and whose effects relate to legal relationships or assets originating in another state. The common basis of these policy goals, as reflected in the EU Insolvency Regulation, are: (i) the protection of certain creditors' interests, coupled with the complementary goal of ensuring certainty of commercial transactions and the importance for the granting of credit, or (ii) the preservation of the law that is applicable to certain legal relationships, which law applies either by virtue of an express choice-of-law provision or by application of the rules of conflict of laws applicable to the relationship in question. It can often be the case that the relationships to which such protective principles are applied have commenced long before insolvency of the debtor was at hand. In answering the question which exceptions should be drafted in the interests of producing more stable and predictable outcomes in the cases to which they apply, a final consideration should be decisive, namely: (iii) that insolvency proceedings should be organized in such a way as to prevent long deliberations or complexity, or other lengthy delays caused by legal uncertainty, which form an obstacle in the orderly, efficient, and timely administration of proceedings.[356] The third ground indirectly reflects the rationale to protect courts and insolvency office holders against the sometimes overwhelming complexities,

[356] See Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 135, referring to recital 11 to the EU Insolvency Regulation, which opens with the acknowledgment that as a result of widely differing substantive laws, it is not practical to introduce insolvency proceedings with universal scope in the entire Community, as "(T)he application without exception of the law of the State of opening of proceedings would, against this background, frequently lead to difficulties."

added costs, and time delays of solving, to every last detail, the more complex issues of conflicts of law. The overall justification for the above exceptions is that they operate to protect legitimate expectations founded upon provisions of law that are not replicated in those of the state in which insolvency proceedings are subsequently opened. In this way, they support commercial predictability and certainty and are intended to ensure a less complicated application of the rules of applicable law.

Based not on the form chosen, but on the interest an exception to the general rule aims to protect, the formulations chosen for drafting the exceptions to the applicability of the *lex concursus* in the EU Insolvency Regulation can be grouped into three categories. There are exceptions: (1) with regard to certain rights in respect of certain goods or property situated in another state than the state of the opening of proceedings, at the time of opening of those proceedings (Articles 5, 6, and 7); (2) with regard to certain legal relationships (Articles 8, 9, 10, 11, 14, and 15); and (3) with regard to certain rights concerning Community patents, trademarks, or any other similar right established by Community law (Article 12). In cases falling under the first two categories, the judicial decision will not be according to the *lex concursus*, but according to the law indicated in the specific conflict-of-laws rule. These categories generally correspond to the policy goals expressed in the paragraph next but one above, as points (i) and (ii) respectively. Rights that fall under the third category may, by virtue of the deliberate wording of Article 12 of the EU Insolvency Regulation, only be included in the main insolvency proceedings. The policy goal mentioned above as point (iii) seems to have been decisive here. The exceptions formulated in Recommendations (32) and (33) of the UNCITRAL Legislative Guide fall within category (2) of the groups of exceptions as listed above. Articles 4-15 of the EU Insolvency Regulation form, in the words of Fletcher (Ian F. Fletcher, Insolvency in Private International Law. National and International Approaches, Oxford Private International Law Series, Oxford University Press, 2nd ed. 2005, 7.78, ". . . . a miniature code of uniform conflict rules," which offer, in practice ". . . . the essential requirement of predictability for parties who need to calculate the legal consequences of their actions within an intra-Union context."

The exceptions, laid down in Articles 5-15 of the EU Insolvency Regulation, have a double function in their effect: (i) they exclude or limit in a specific case the applicability of the *lex concursus* (the law of the state in which main insolvency proceedings were opened); (ii) at the same time, they indicate that national rules of conflict of laws apply where the exceptions indicate the nonapplicability of the law of a Member State. This will, for instance, be the case when an asset is not located in a Member State, when a claim is not governed by the law of a Member State, or the proceeding is not pending in a Member State, see H.-C. Duursma-Kepplinger, in: Duursma-Kepplinger, H.-C, Duursma, D, Chalupsky, E., *Europäische Insolvenzverordnung. Kommentar*, Springer, Wien New York, 2002, 103; Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 24. It is appreciated that the dichotomy which is observed under the EU Regulation between assets located in Member States and those located in non-Member States is not suitable for use in the context of principles for the conduct of insolvency proceedings that are set in a global context. In formulating exceptions to the application of the *lex concursus*, it is therefore necessary to give some thought to the possibility that the location of assets at the time of opening of insolvency proceedings may be the consequence of some prior, planned activity designed to exploit the law of the situs in order to generate advantages for a particular party in interest. Similarly, where a concession is made to the effects of a law by which a particular transaction is governed, as opposed to any contrary effects that might otherwise result from the application of the *lex fori concursus*, it may be demonstrable that the law in question has no substantial relationship to the parties or the transaction, so that it is at least arguable that the sole purpose of the steps taken to cause the transaction to become subject to that law was to avoid the application of some other law that would otherwise have been applicable. One or more subsidiary rules may be needed to counteract any unfair advantages that may be otherwise gained at the expense of the general body of creditors by means of manipulative tactics of that kind. Such rules are herein formulated, see Global Rule 14.

For the purposes of these Global Rules, which are designed for application under the currently prevailing conditions of global diversity of national laws and policies, it is considered appropriate to maintain a certain number of specific exceptions to the general rule as laid down in Global Rule 12. The next question to be addressed is whether there is some international consensus as to which categories of exceptions should be recognized, and how those exceptions should best be formulated. Although, as mentioned above, several European states have followed the extension model and have drafted up to 10 exceptions to the general rule, of the categories of exceptions provided for in Articles 5 to 15 inclusive of the EU Insolvency Regulation only the following are selected for present consideration in the Global Rules: (a) rights of secured creditors ("third parties' rights in rem"), (b) rights of creditors to demand set-off, (c) contractual obligations, with special reference to rights under contracts of employment, and (d) defenses to the avoidance of detrimental acts. In drafting the selected exclusions, the protection of the rights mentioned under (a) and (b) have been drafted as substantial exclusions to the general rule (of *lex fori concursus*). Exceptions (c) and (d) express a choice of another law (than the *lex fori concursus*).

The Global Rules recognize the possibility of two or more insolvency proceedings concerning the same debtor, to which different substantive rules apply. This approach requires a degree of attuning and aligning, for which the Global Principles and Global Court-to-Court Guidelines for coordination and cooperation between office holders and courts have been designed.

## REPORTERS' NOTES

Arguably, other exceptions could have been selected too, including the ones we did not select from a larger group in the EU Insolvency Regulation, as well as others. Proposals for exceptions to the general rule, for instance, have been submitted for contracts with suppliers and tort claimants whose expectations of local-law application should be vindicated (see Jay L. Westbrook, The Present and Future of Multinational Insolvency, in: Bob Wessels and Paul Omar (eds.), The Intersection of Insolvency and Company Laws, Nottingham, Paris: INSOL Europe 2009, pp. 111-125, at p. 114). With this background, also consumer contracts or license contracts will be candidates for consideration. In these Global Rules, we have limited ourselves to those exceptions for which, both in the global domain of the relevant literature and also in the opinion of a large portion of the Advisers to the project, general consent is expressed. The UNCITRAL recommendations in the Legislative Guide suggest, in recommendation 32, an exception to the applicable general rule (*lex fori concursus*): "the effects of insolvency proceedings on the rights and obligations of the participants in a payment or settlement system or in a regulated financial market should be governed solely by the law applicable to that system or market." A similar deviation is provided in Article 9(1) of the EU Insolvency Regulation and, for instance, in § 340 German Insolvency Act (for relations with non-EU Member States). Such an exception has not been drafted in this Report because its necessity or advisability has not been tested by the project's Advisers. Furthermore, in the present overhaul of rules and frameworks in the banking sector, it seems logical to suppose that a rule that is reflected in recommendation 32 is under discussion. In the future, other national or international legislatures will respond to the need of drafting choice-of-law rules to guide the solutions of applicable law matters. It seems, therefore, wise to formulate Global Rules that address certain immediate needs while at the same time—with the ongoing development of international insolvency law—helping to stimulate longer-term efforts in articulating additional exceptions or, as the case may be, to limit their number, for instance in the light of certain steps to harmonization.

**Rule 15 Rights of Secured Creditors**

**15.1. Insolvency proceedings shall not affect the rights in rem of creditors or third parties in respect of tangible or intangible, moveable or immoveable assets—both specific assets and collections of indefinite assets as a whole that change from time to time—belonging to the debtor, which are situated within the territory of another state at the time of the opening of proceedings.**

**15.2. The rights referred to in Global Rule 15.1 shall in particular mean:**

**(a) The right to dispose of assets or have them disposed of and to obtain satisfaction from the proceeds of or income from those assets, in particular by virtue of a lien or a mortgage;**

**(b) The exclusive right to have a claim met, in particular a right guaranteed by a lien in respect of the claim or by assignment of the claim by way of a guarantee;**

**(c) The right to demand the assets from, and/or to require restitution by, anyone having possession or use of them contrary to the wishes of the party so entitled;**

**(d) A right in rem to the beneficial use of assets.**

**15.3. The right, recorded in a public register and enforceable against third parties, under which a right in rem within the meaning of Global Rule 15.1 may be obtained, shall be considered a right in rem.**

**Rule 16 Exception**

**16.1. By way of exception to Global Rule 15, a right in rem ("in rem security right") shall not be exempted from the effects of insolvency proceedings if proof is provided that the state where the assets are situated, at the time of the opening of insolvency proceedings, has no substantial relationship to the parties or the transaction in relation to which the security right was created, and there is no other reasonable basis for the fact that the assets are so situated.**

**16.2. It is for the party who claims that the conditions specified in Global Rule 16.1 are met, in relation to a particular security right, to prove that those conditions are in fact met in the relevant case.**

**Comment to Global Rules 15 and 16:**

The exceptions that relate to third parties' rights in rem and to set-off (see below, Rules 17 and 18) are structured similarly and use similar wording. For the description of the expressions "shall not affect" and "the time of the opening of proceedings," see the Appendix to this Report.

The main purpose of arrangements for granting some form of real security to a creditor is to provide the creditor with an alternative form of recourse in the event of the debtor's failure to perform his obligation. This includes the situation where nonperformance is due to the insolvency of the obligated party. Real security, therefore, offers a means of protecting a creditor against risks associated with the extending of credit. The extent to which the rights of a secured creditor are capable of being affected by the debtor's insolvency is an essential aspect of the creditor's assessment of the net risk to which he is exposed, and can have a significant bearing upon the decision whether to extend credit, and if so, on what terms. This rationale forms the basis of the exception created by Article 5 of the EU Insolvency Regulation, as is explained by its Recital (25), which adopts the principle that "the basis, validity and extent of such a right in rem should normally be determined according to the *lex situs* and not be affected by the opening of insolvency proceedings." That solution is embodied in Article 5, whose first paragraph states: "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."

For the reasons not to include the words "opening of," see the Appendix. The rights in rem in respect of the aforementioned assets belonging to the debtor, "which are situated within the territory of another State at the time of the opening of proceedings," are not affected by insolvency proceedings. Article 5 of the EU Insolvency Regulation provides that security rights in respect of assets belonging to the debtor, "which are situated within the territory of another Member State at the time of the opening of proceedings," are not affected by "the opening of" the main insolvency proceedings. In the Global Rules, any judgment (relating to the opening or separate judgments required during insolvency proceedings, e.g., the adoption of a rescue plan) or any specific legal rule (a rebate to all claims filed) is without prejudice to the right in rem. A discussion regarding the precise meaning of "the opening of" and the uncertainty and confusion such a discussion has provoked[357] is prevented under Global Rule 15 as here worded. The state in which assets are "situated" is to be determined by applying Global Rules 6-11.

Global Rule 15 adopts the same substantive approach as Article 5 of the EU Insolvency Regulation and serves, as indicated, as an exception to the enforcement of the *lex fori concursus*, which would be instrumental in governing which assets belong to the estate in the foreign insolvency proceedings. The general rule—founded upon the principle of universality—is that when assets of any kind (moveable or immovable; tangible or intangible, including real estate, a bank account, or other intangible property such as a debt) are situated in another state than the state of the opening of the main insolvency proceedings, they belong

[357] See H.-C. Duursma-Kepplinger, in: Duursma-Kepplinger, H.-C, Duursma, D, Chalupsky, E., *Europäische Insolvenzverordnung. Kommentar*, Springer, Wien New York, 2002, Art. 5, nr. 37; A.J. Berends, *Insolventie in het internationaal privaatrecht*, Ph.D. Vrije University Amsterdam, 2005, p. 149ff., and Alexander Plappert, *Dingliche Sicherungsrechte in der Insolvenz, Schriften zum Insolvenzrecht*, Band 21, Baden-Baden 2008, p. 268, defending a narrow interpretation of "opening" versus, e.g., Paul Michael Veder, Cross-Border Insolvency Proceedings and Security Rights. For a comparison of Dutch and German law, the EC Insolvency regulation, and the UNCITRAL Model Law on Cross-Border Insolvency, see Ph.D. Nijmegen 2004, p. 352 and Jasnica Garašić, *Anerkennung ausländischer Insolvenzverfahren*, Ph.D. Hamburg 2004, Frankfurt am Main: Peter Lang, 2005, 2 Volumes, Part II, p. 133, defending that "opening" in result means "the insolvency proceedings").

in principle to the estate of these latter proceedings. However, if the debtor happens to have an "establishment" (as specially defined) in the other state where the said assets are situated, these must be considered to belong to a potentially separate estate that may become the subject of a concurrent ("non-main") collective proceeding. Moreover, irrespective of the possibility that the debtor may have an establishment in the state where some assets are situated, some of these assets may be the subject of a creditor's or another third party's rights in rem. The EU Insolvency Regulation does not explicitly provide that these assets belong to the main proceedings, but it explicitly respects (at the moment these proceedings are opened) existing rights over certain assets belonging to the debtor that are located or situated within the territory of another Member State at the time of the opening of proceedings. The same approach respecting existing rights has been applied to Article 6 of the EU Insolvency Regulation (set-off). Global Rule 15 is only applicable to rights that are in existence at the time of the opening of insolvency proceedings. In the event that these rights have been created after the opening of proceedings, Global Rule 12 or 13 is fully applicable without attenuation or exception.

The use of the words "assets . . . belonging to the debtor" in Global Rule 15.1 expresses an intention to enable the rule to operate in a broad and flexible way. The term "belonging" not only covers legal ownership, but also forms of "economic ownership" and certain "proprietary rights" in assets, which according to the governing law are attributed to the estate. An example of such economic ownership is the financial lease.[358] This interpretation follows from the given policy consideration and is justified when, for instance, a certain asset or a right recorded in a public register, as set forth in Global Rule 15.3, is shielded from the applicability of the *lex fori concursus*.

Global Rule 15.1 refers to "rights in rem," but it does not define what these rights are. However, Global Rule 15.2 provides an enunciative, nonexhaustive list of such rights. In view of the variety of such rights, it seems wise to abstain from providing a closed definition of a right in rem, as this may differ from the definition given to "rights in rem" by the specific country in which the assets are located. Therefore, Global Rule 15.2 states that rights in rem "in particular" mean a concentrated group of four legal powers as described in paragraphs (a) to (d). The characterization of a right as a right in rem should be determined by the national law that, according to the general normal pre-insolvency conflict-of-law rules, governs these rights in rem, which in general will be the *lex rei sitae* at the relevant time.

Global Rule 15.1 provides that rights in rem that fall within its defined scope of application remain unaffected by the insolvency proceedings. The rule is broadly expressed so as to apply to third parties' rights in rem that exist ". . . in respect of tangible or intangible, moveable or immoveable assets—both specific assets and collections of indefinite assets as a whole that change from time to time—belonging to the debtor, which are situated within the territory of another state at the time of the opening of proceedings." The quotation carries a substantive component (in terms of which particular assets fall within the ambit of the exception) and a territorial component (in terms of where such assets are situated). Which specific assets are covered by it depends on the provisions and conditions contained in the internal law of the state (not being the state where the proceedings are opened), which dictates what species of

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[358] In this way, too, see, e.g., 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, p. 305.

assets are capable of being subject to certain rights in rem, for example—as the provision recognizes—tangible and intangible goods. Also, the effect of foreign insolvency proceedings upon the rights in question is determined by the aforementioned internal law. Under the laws of certain states, in addition to establishing rights in rem towards certain specific or existing goods, a security right may exist in respect of "collections of indefinite assets as a whole which change from time to time." For the purposes of ensuring that Global Rule 15.1 is applicable to certain types of security rights that exist in certain states (and often are known as "floating charges"), Global Rule 15.1 follows the approach of Article 5 of the EU Insolvency Regulation and expressly characterizes these as "rights in rem."

The criterion to be applied to qualify a right as a right in rem requires that the "assets" "belong" to the debtor and are "situated" within the territory of another state at the time of the opening of proceedings. Therefore, there must be an "asset" "situated" in a state. Certain "future" assets, for example, future installments of a lease, must exist at the time at which the proceedings are opened abroad.[359]

By virtue of Global Rule 15.3, the right, recorded in a public register and enforceable against third parties, under which a right in rem pursuant to Global Rule 15.1 may be obtained, shall be considered a right in rem. The provision deviates from the conflict-of-law rule of the *lex rei sitae* and determines that, for the application of Global Rule 15.1, the said right is a right in rem directly, without referring to a particular national law. Such a recorded right should also exist prior to the opening of the main proceedings.[360] See also the Comment to Global Rule 6.

Where assets are subject to rights in rem under the *lex rei sitae* in one state, but the insolvency proceedings are being carried out in another state, the liquidator of such proceedings should be able to request the opening of non-main proceedings in the jurisdiction where the rights in rem arise. This is asserted in Recital 25 to the EU Insolvency Regulation, which however provides this power only if the debtor has an establishment in the other state. These (non-main, within the EC "secondary") proceedings are conducted according to national law and will allow the liquidator to affect these rights under the same conditions as are provided for purely domestic proceedings.

Although Global Rule 15 results in the unaffectedness of certain rights in rem, Global Rule 21 ensures that the limitation of this principle does not lead to immunity from the provisions concerning detrimental acts contained in the *lex concursus*. See further below, in relation to Global Rules 21, 22, and 23.

The purpose of Global Rule 16.1 is to provide a counterbalance to the possibilities that a party may seek to take advantage of the "hospitable" laws that are to be found in various states in order to shelter assets from the effects of the insolvency laws to which either or both of the

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[359] This rule can only be the result of an interpretation of the national law of the state, not being the state of the opening of the proceedings, see Ian F. Fletcher, Insolvency in Private International Law. National and International Approaches, Oxford Private International Law Series, Oxford University Press, 2nd ed. 2005, 7.88.

[360] An example of such a right is the German *Vormerkung*, see Stephan Kolmann, *Kooperationsmodelle im Internationalen Insolvenzrecht.* Empfielt sich für das Deutsche internationale Insolvenzrecht eine Neu-orientierung?, Schriften zum Deutschen und Europäischen Zivil-, Handels- und Prozessrecht, Bielefeld: Verlag Ernst und Werner Gieseking, 2001, p. 303, and its Dutch equivalent in Article 7:3 of the Netherlands Civil Code, see Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, para. 10645.

parties are immediately or prospectively subject. While it is important to ensure that such "asset havens" are not exploited under circumstances that are unfairly prejudicial to the interests of the general body of creditors, it is also important to allow any party to conduct its legitimate dealings in a non-artificial manner and to avail themselves of such mechanisms for arranging protection against commercial risks as are offered under the laws of the states with which the party and its transaction are related. The basic protection provided by Global Rule 16.1 therefore admits of an exception where there is proof that the situs of the asset in respect of which a right in rem is claimed has been chosen purely for the purpose of claiming legal advantages, in the event of insolvency, that would not be available under the laws of any other state having a substantial relationship with the parties or their transaction, and provided that there is no other reasonable basis for the fact that the assets are situated in the location in which they are placed at the time of the opening of the insolvency proceedings. The additional provision in Global Rule 16.2, relating to the burden of proof for the purposes of Global Rule 16.1, ensures that it is for those who seek to question the legitimacy or efficacy of an in rem security right to prove that, in the relevant case, it does not enjoy the protection that would otherwise be conferred under Global Rule 15.

## REPORTERS' NOTES

For a more specific discussion of the aforementioned exceptions, specifically those included in the EU Insolvency Regulation, see J. Taupitz, *Das (zukünftige) Europäische Internationale Insolvenzrecht—insbesondere aus international-privatrechtlicher Sicht*, in: Zeitschrift für Zivilprozessrecht (ZZP) 1998, p. 315ff; Ian F. Fletcher, Insolvency in Private International Law. National and International Approaches, Oxford Private International Law Series, Oxford University Press, 2nd ed. 2005, 7.84ff; H.-C. Duursma-Kepplinger, in: Duursma-Kepplinger, H.-C, Duursma, D, Chalupsky, E., *Europäische Insolvenzverordnung. Kommentar*, Springer, Wien New York, 2002, Art. 5 et seq; Miguel Virgós and Fransisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr.; Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, para. 10629ff; Thomas Ingelmann, in: Pannen, Klaus (ed.), European Insolvency Regulation, Berlin: Walter de Gruyter, 2007, p. 245ff. Peter Mankowski, *Europäisches Internationales Insolvenzrecht (EuInsVO), Kapitel 47*, Kölner Schrift zur Insolvenzordnung, 3. Aulage, Münster: ZAP Verlag 2009, nr. 88ff.

Article 5(1) of the EU Insolvency Regulation merely states that the opening of (main) insolvency proceedings "shall not affect the rights in rem of creditors . . . ." The provision precludes the enforcement of the (universal effect of the) *lex concursus*, but it does not specifically provide when a "right" is a "right in rem." For further discussion on rights in rem, see Miguel Virgós and Fransisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 96. For comments relating to some 10 countries, see Nadine Watté, and Vanessa Marquette, *Faillite internationale—Compétence—Effets d'une faillite prononcée a l'étranger—sûretés réelles—droit de preference*, in: European Review of Private Law 1999, p. 287ff. For the Netherlands, see Paul Michael Veder, Cross-Border Insolvency Proceedings and Security Rights. For a comparison of Dutch and German law, the EC Insolvency regulation, and the UNCITRAL Model Law on Cross-Border Insolvency, see Ph.D. Nijmegen 2004, p. 330ff; A.J. Berends, *Insolventie in het internationaal privaatrecht*, Ph.D. Vrije University Amsterdam, 2005, p. 374ff. It should be noted that if there is no establishment in another Member State, the applicability in Europe of the *lex concursus* is halted by Article 5 in a situation in which secondary proceedings cannot be opened. The assets will be beyond the reach of the liquidator, and the secured creditor may exercise his right as if there were no insolvency. See Jona Israël, European Cross-Border Insolvency Regulation. A Study of Regulation 1346/2000 on Insolvency proceedings in the Light of a Paradigm of Cooperation and a Comitas Europaea, Ph. D. European University Institute, Florence, 2004, Intersentia, Antwerp-Oxford, 2005, p. 279.

The question of which law is decisive with regard to the basis, validity, and consequences of said right in rem will be determined by the applicable rules of private international law. The basis, validity, and extent of a right in rem, pursuant to Global Rule 15, will normally be determined according to the law of the state within the territory of which the property is situated (*lex rei sitae*). See recital 25 to the EU Insolvency Regulation: ". . . . The basis, validity and extent of such a right in rem should therefore normally be determined according to the lex situs and not be affected by the opening of insolvency proceedings. . . ." See Jasnica Garašić, Recognition of Foreign Insolvency Proceedings: the Rules that a Modern Model of International Insolvency Law Should Contain, in: Yearbook of Private International Law, 2005, vol. 5, p. 369. This right in rem shall not be affected by the opening of the insolvency proceedings. See further Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, para. 10651ff.

It is noted that the combination of Global Rule 15.1 (referring to "rights in rem," without fully defining these), and Global Rule 15.2 (an enunciative list of such rights), can be assessed as rather vague, and that Global Rule 15.3 (certain rights recorded in a public register are seen as rights in rem) may create unforeseen consequences. As indicated, in view of the variety of such rights it has been considered prudent to abstain from providing definitions, where the present formulations avoid doubts and may facilitate a flexible application.

In the Appendix to this Report, the words "shall not affect" have been explained as providing a "hard and fast" rule that appears to be clear-cut. However, it raises the question of precisely which elements of a right in rem will not be affected. Recital 25, second and third line, to the EU Insolvency Regulation provides: "The basis, validity and extent of such a right in rem should therefore normally be determined according to the lex situs and not be affected by the opening of insolvency proceedings. The proprietor of the right in rem should therefore be able to continue to assert his right to segregation or separate settlement of the collateral security." The question arises whether the hard and fast rule protects the right in rem itself or whether it also protects all the powers that are, according to the *lex situs*, attached to the said right. For instance, will the holder of the right be protected against all those rules that may not interfere with the right in rem itself, but that indeed do interfere with the exercising of this right? Examples are the following: the *lex concursus applicable* in the main insolvency proceedings opened in another state may contain certain forms of postponement or dissolution of rights, for example, (i) an overriding power enjoyed by the liquidator to redeem the right in rem, or (ii) a cooling-off period or temporary moratorium may be set in place, either by operation of law related to a certain event or based on a request for the opening of an insolvency proceeding. On different views of European authors, see Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, para. 10655ff. In the event that *the lex concursus* of this state contains a rule prescribing that secured creditors must also pay towards the costs of the insolvency administration (such as Articles 170-172 of the German Insolvency Act), it must be questioned whether this affects the secured creditor's right. According to A.J. Berends, *Insolventie in het internationaal privaatrecht*, Ph.D. Vrije University Amsterdam, 2005, p. 402ff, this rule results *ipso jure* from the opening of the insolvency proceedings and does not affect the creditor's rights. For an alternative view, see Kolja von Bismarck, and Kirsten Schümann-Kleber, *Insolvenz eines ausländischen Sicherungsgebers—Anwendung deutscher Vorschriften auf die Verwertung in Deutschland belegener Kreditsicherheiten*, Neue Zeitschrift für das Recht der Insolvenz und Sanierung (NZI) 2005, p. 149; 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, p. 307.

**Rule 17 Set-Off**

**Insolvency proceedings shall not affect the right of creditors to demand the set-off of their claims against the claims of the debtor, where such a set-off is permitted by the law applicable to the insolvent debtor's claim.**

**Rule 18 Exception**

**Where a right of set-off is demanded on the basis of Global Rule 17, if it is the case that, in the absence of express choice made by the parties, the law applicable to the insolvent debtor's claim would be that of the state of the opening of main insolvency proceedings, Global Rule 17 shall not apply if the law of the state chosen by the parties has no substantial relationship to the parties or the transaction, and there is no other reasonable basis for the parties' choice.**

**Comment to Global Rules 17 and 18:**

Research has demonstrated that the availability of set-off for a creditor in case its debtor is subject to insolvency proceedings is very different from state to state. Also the requirements to be fulfilled may differ, for example, concerning the "liquidity" of an obligation, the moment of creation of the obligation, the possibility of set-off for a debt owed to the insolvent debtor that has been transferred by a third party pre-insolvency, etc.[361] In addition, the underlying principles are diametrically opposed: the principle of protection of a position amounting to a de facto security in favor of the person authorized to set-off at the moment the power is created (concluding a contract prior to insolvency of the counterparty), versus the principle of equal treatment of all creditors as of the moment of insolvency. Both the smoothness of cross-border trade and the efficient administration of insolvency proceedings indicate the vital importance of a clear rule, which allows the applicable law to be known in advance, to enable the assessment of possible risks.

When searching for the most appropriate rule for global application, Article 6 of the EU Insolvency Regulation deserves further elaboration, given the richness of its drafting history and the fact that some national laws—for example, Germany (Section 338), Spain (Article 205 *Ley Concursal*), Republic of Slovenia (Article 483(1)), and the pre-draft in the Netherlands (Article 10.4.3)—follow a similar approach for international insolvency issues in relation to non-EU states. Article 6 generates a special rule applicable by way of exception to

[361] See Ian F. Fletcher, Insolvency in Private International Law. National and International Approaches, Oxford Private International Law Series, Oxford University Press, 2nd ed. 2005, 7.97; R. Derham, The Law of Set-Off, 4th Edn. (Oxford, Oxford University Press, 2010); P.R. Wood, English and International Set-Off (Sweet & Maxwell, 1989); Christoph Jeremias, *Internationale Insolvenzaufrechnung*, Max-Planck-Institut für ausländisches und internationales Privatrecht, Studien zum ausländischen und internationalen Privatrecht, nr. 150, Tübingen: Mohr Siebeck, 2005; Stefan Rosskopf, *Die Aufrechnung in deutschen und englishen Insolvenzrecht*, Schriften zum Verfahrensrecht, Band 26, Peter Lang Frankfurt, 2008 (comparing German and English insolvency rules regarding set-off).

the general rule laid down by Article 4(1) of the EU Insolvency Regulation, that "the law applicable to insolvency proceedings and their effects shall be that of the Member State within the territory of which they are opened." This anticipates that the availability of set-off will be dependent upon such a demand being allowed under the terms of the *lex concursus*. The same principle would be applicable under Global Rules 12 and 13 as set out above. Under the EU Regulation, the general rule of Article 4(1) is reinforced by a specific provision in Article 4(2)(d) to the effect that the *lex concursus* shall determine in particular "the conditions under which set-offs may be invoked." However, the opening words of Article 4(1) indicate that its provisions are subject to exception where there is contrary provision elsewhere in the Regulation itself. Such a contrary provision, in relation to set-off, is made by Article 6 (as indicated one of the substantial exceptions to the general rule of application). Article 6(1) states: "The opening of insolvency proceedings shall not affect the right of creditors to demand the set-off of their claims against the claims of the debtor, where such a set-off is permitted by the law applicable to the insolvent debtor's claim."

The exception created by Article 6 of the EU Insolvency Regulation is of a very precise character. As explained in the Virgós / Schmit Report (nr. 107), in the comment to Article 6 of the proposed EC Convention on Insolvency Proceedings (whose drafting was in every respect identical to that of Article 6 of the Regulation), the intention of this provision was that "When under the normally applicable rules of conflict of laws the right to demand the set-off stems from a national law other than the '*lex concursus*', Article 6 allows the creditor to retain this possibility as an acquired right against the insolvency proceedings: the right to set-off is not affected by the opening of proceedings." The reference to "the normally applicable rules of conflict of laws" is especially significant because, as is well understood, those rules are capable of giving rise to a situation where contractual or other liabilities are governed by the laws of (potentially) any state in the world. In relation to contractual obligations, among the Member States of the EU this possibility is accepted by the express provision in Article 2 of the Rome Convention, which entered into force on April 1, 1991. Article 2 declares that: "Any law specified by this Convention shall be applied whether or not it is the law of a Contracting State." The substance of this rule is replicated in Article 2 of the Rome I Regulation (Regulation (EC) No.593/2008), which has replaced the Rome Convention in all EU Member States with the exception of Denmark from December 17, 2009 onwards. As the Rome Convention was formerly applicable in all 27 of the current EU Member States, the literal and natural meaning of the expression "the law applicable to the insolvent debtor's claim" in Article 6(1) of the Insolvency Regulation is that it means any law capable of being identified as the applicable law of the obligation in question, according to the choice-of-law rules now standardized among EU Member States, initially by the Rome Convention and currently by the Rome I Regulation. Of additional interest is the provision of Article 17 of the Rome I Regulation, which bears the heading "Set-off." Article 17 paves the way for a more general application of set-off in matters of contract by providing "Where the right of set-off is not agreed by the parties, set-off shall be governed by the law applicable to the claim against which the right to set-off is asserted." Thus, among Member States of the EU, a consistent approach is adopted whereby the availability of set-off is determined by that law which (in the context of the insolvency of one of the parties to a contract) is the law applicable to the insolvent debtor's claim. Of course, non-EU states' rules of choice of law in contractual matters are not affected by the Rome Convention, nor by its successor the Rome I Regulation, and they are free to retain that diversity of approach for which the realm of private international law is notorious.

The above rationalization of the conclusions that follow upon an examination of the literal and natural meaning of Article 6 of the EU Insolvency Regulation is fully consistent with the interpretative guidance supplied by Recital (26) to the Regulation. Recital (26) (which is closely modeled upon statements contained in paragraph 109 of the Virgós / Schmit Report), states as follows: "If a set-off is not permitted under the law of the opening State, a creditor should nevertheless be entitled to the set-off if it is possible under the law applicable to the claim of the insolvent debtor. In this way, set-off will acquire a kind of guarantee function based on legal provisions on which the creditor concerned can rely at the time when the claim arises." It is noteworthy that Article 6 contains no words expressly restricting the scope of the exception to cases where the obligation through which the right to claim set-off is generated is governed by the law of one of the other EU Member States. The rule could therefore, based on its textual scope, be considered as a candidate for more universal acceptance as an exception to the dominant role of the *lex concursus* in main insolvency proceedings opened in any jurisdiction. In the course of developing the provision now embodied in Article 6, the members of the committee of experts established by the EC Council explored a number of alternative formulations that reflect a changing balance of opinion as to the correct principle to be applied. Examination of the textual history of this provision, by studying the successive drafts produced and discussed by the committee of experts between 1989 and 1995, shows that the rule in its current form, as quoted above, only appears in the draft versions of the convention produced after July 1993. Until that date, the proposed provision relating to set-off was expressed in the following terms: "The opening of insolvency proceedings shall not affect the right of creditors to the set-off of a claim forming part of the estate where *the law of a Contracting State other than the State of the opening of proceedings applies* to that claim" (emphasis added). In the subsequent versions of the provision produced between that date and the finalization of the text on September 25, 1995, the drafting was significantly altered with the omission of any reference to the law of a Contracting/Member State, and with the inclusion of wording to clarify the scope of the rule so as to confine its operation to those cases where the right of set-off is permitted by the law applicable to the insolvent debtor's claim (i.e., the claim under which the insolvent debtor stands as creditor towards the party seeking to invoke a right of set-off, also referred to as "the passive claim").[362]

It should be noted from the outset that the EU Insolvency Regulation's set-off rule has a limited scope. The final intentions of the EC committee of experts are summed up by a passage in paragraph 109 of the Virgós / Schmit Report (which supplied the basis for the statement contained in Recital (26) to the Regulation): "If the '*lex concursus*' allows for set-off, no problem will arise and Article 4 should be applied in order to claim the set-off as provided for by the law. On the other hand, if the '*lex concursus*' does not allow for set-off (e.g., since it requires both claims to be liquidated, matured and payable prior to a certain date), then Article 6 constitutes an exception to the general application of that law in this respect, by permitting the set-off according to the conditions established for insolvency set-off by the law applicable to the insolvent debtor's claim ('passive' claim)." Article 6(1) contains therefore a "carefully limited exception" to the *lex concursus*.[363]

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[362] See Ian F. Fletcher, Challenge and Opportunity: the ALI/III Global Principles Project, (2008) Vol. 1 Potchefstroom Electronic Law Journal 2/29-29/29, at pp.18/29-25/29.

[363] Thus, see Ian F. Fletcher, Insolvency in Private International Law. National and International Approaches, Oxford Private International Law Series, Oxford University Press, 2nd ed. 2005), 7.99. See also Christoph Jeremias, *Internationale Insolvenzaufrechnung*, Max-Planck-Institut für ausländisches und

When devising a rule for application in proceedings opened in any part of the world, consideration should be given to two key matters. The first question (or rather, series of questions) is whether the reference to the law applicable to the insolvent debtor's claim, rather than the law governing the obligation under which the insolvent debtor occupies the role of debtor towards the other party, is the appropriate rule in principle; or whether it should be possible to invoke set-off if such a right is available under the law applicable to either claim; or (more restrictively) only if such a right can be shown to be available under the law or laws applicable to both claims (assuming neither claim to be governed by the *lex concursus*).

The following Illustrations are based on the terms of Global Rule 17 as proposed above:

**Illustrations:**

1. Insolvent Debtor (ID), which is the subject of insolvency proceedings opened in state X, is indebted to Creditor C under a contract governed by the law of state Y. Creditor C is separately indebted to ID under a contract governed by the law of state Z. Under the law of state X, set-off is permissible in respect of the two debts under the circumstances in which they currently exist (i.e., in the actual case). Global Rule 12 accordingly applies without interruption, and the two claims are subject to set-off in accordance with the relevant provisions of the law of state X. The respective provisions of the laws of state Y and state Z, with regard to set-off, are of no relevance to the outcome in this instance.

2. The factual circumstances are as in Illustration 1, save that under the laws of both state X and state Y set-off is not permissible, whereas under the law of state Z ("the law applicable to the insolvent debtor's claim") set-off is permissible. Global Rule 17 applies with the consequence that set-off is permitted in accordance with the provisions of that law. In this instance, the law of state X is displaced and the law of state Y is of no relevance.

3. The factual circumstances are once again as in Illustration 1, save that, in this instance, under the laws of both state X and state Z, set-off is not permissible, whereas under the law of state Y (the law governing the claim of Creditor C) set-off is permissible. Here the circumstances do not bring the case within the scope of Global Rule 17. Accordingly, Global Rule 12 applies without interruption, and set-off is denied in accordance with the law of state X (the *lex fori concursus*).

A second matter for consideration is whether international set-off should be available merely on proof that such entitlement arises under one or other of the laws by which the mutual cross-obligations are governed, or whether there should be a further requirement that the party invoking set-off must show that such a right has formed part of its legitimate expectations arising in the context of the relationship between the creditor and the insolvent debtor, so as to have been part of the calculation of risk during the process of becoming a creditor on the terms agreed. Since it is a fundamental policy of insolvency law that all creditors are eligible to participate upon terms of global equality, any rule that introduces an exception to the *pari passu* principle needs to be justified with care, and should not be allowed to operate as a capricious or arbitrary device without regard to the context under which parties have had

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internationales Privatrecht, Studien zum ausländischen und internationalen Privatrecht, nr. 150, Tübingen: Mohr Siebeck, 2005, p. 261, who refers to Article 6 as a *Helfer in der Not* (A helper in need).

dealings with the debtor. Strictly speaking, however, this second matter of principle does not constitute a choice-of-law rule but, if it is found at all, it may be encountered as part of the domestic law of set-off of one of the states whose laws are potentially engaged, namely the *lex fori concursus*, or the state whose law is applicable to the insolvent debtor's claim. In such circumstances, the need to demonstrate that the creditor formed a legitimate expectation of a right to demand set-off may be interposed as a precondition to the availability of that right, whether it is invoked under the provisions of Global Rule 12 or under those of Global Rule 17. Indeed, it may be arguable that, as a matter of principle, such a precondition (tacitly, if not explicitly) ought to be incorporated in the substantive law of any state that allows the operation of set-off in cases of insolvency. It is noteworthy that the argument founded upon respect for the creditor's legitimate expectations serves as part of the rationale underlying the English common-law approach to such set-offs, since courts have at times appeared to justify its operation on the ground that it is intended "to do substantial justice between the parties" on the premise that the creditor, in giving credit, "must have" placed reliance on the ability to offset his own liability to the debtor.[364]

In adopting in Global Rule 17 the rule of Article 6 of the EU Insolvency Regulation, whereby the policy of the *lex concursus* is displaced by that of the law applicable to the passive claim (in situations where there is a true conflict between the two laws with regard to the availability of set-off *in casu*), the drafters of the Insolvency Regulation (and of the Convention that preceded it) were giving effect to the doctrine that scholars of the modern era seem to regard as the more satisfactory rule of decision for international cases. The "traditional" approach, as advocated by a number of writers in former times, required the cumulative application of both laws—that is, those governing the active and the passive claim respectively—and would deny set-off unless both laws were found to concur in allowing it to operate, thereby increasing the likelihood that the creditor would be denied the right of set-off. Modern analysis, on the other hand, has placed greater emphasis on the need to protect legitimate and reasonable expectations, and therefore on the need for a stable rule that enables the creditor to rely upon the provisions of a single system of law whose provisions are applicable in the context of his incurring an obligation towards the party who is subsequently the subject of main insolvency proceedings. There appears to be a growing consensus among modern scholars that such stability and predictability is best achieved through the application of the rule contained in the law applicable to the passive claim ("the insolvent debtor's claim"). Thus, if that law permits set-off, but the *lex concursus* denies it, the latter will be overridden. This is the approach that would be followed in the present day under English and Netherlands rules of private international law (i.e., quite apart from the rule now imposed under Regulation 1346/2000 for cases to which it applies). It can therefore be argued that the solution supplied by Global Rule 17, which is aligned with that of Article 6 of the EU Insolvency Regulation, is in harmony with modern views of the appropriate way in which to resolve issues of set-off in international cases, and reflects the practice that would be followed in many jurisdictions (including England) even where the Regulation itself is not applicable to the case in question.

[364] See Forster v. Wilson (1843) 12 M & W 191, 203-204; 152 E R 1165, 1171, per Parke B; Stein v. Blake [1996] AC 243, 251, per Lord Hoffmann. Notably, however, the English doctrine of set-off, as currently expressed in legislation, omits any mention of a need for the creditor to demonstrate an actual reliance on the availability of set-off as a condition to being able to have the benefit accruing from its automatic operation in the event of the debtor's insolvency (Insolvency Act 1986, s.323; Insolvency Rules 1986, rr.2.85, 4.90).

For the purposes of the Global Principles Project, the Reporters have endeavored to approach the issue of set-off with an open mind as to the international acceptability of any rule whereby it may be permissible to disapply the set-off law of the *lex fori concursus* in a way that enables a right of set-off to be claimable, where it can be shown that legitimate expectations of the availability of such a right, in the event of the counterparty's insolvency, have accompanied a creditor's approach to its relationship with the debtor. We are of the opinion that such disapplication should be permitted under defined circumstances, and that it would provide a useful support to trade and commerce if consensus could be achieved on a standard formulation of the basis on which set-off is to operate in international cases. For example, debtors who happen to be based in jurisdictions under whose laws set-off is not available may experience relatively greater difficulty in obtaining credit—including structured loans—from parties based in jurisdictions where set-off would ordinarily be operative in the event of the debtor's insolvency. By permitting such international relationships, if suitably structured, to benefit from the application of the rule and policy found in the legal system under which the creditor habitually operates, the proposed rule could enable such debtors to have access to credit that would otherwise not be so readily available to them.

Although Global Rule 17 results in the unaffectedness of certain rights (i.e., the right of a creditor to demand the set-off of its claims against the claims of the debtor, where such a set-off is permitted by the law applicable to the insolvent debtor's claim), Global Rule 21 ensures that the limitation of this principle does not lead to immunity from the provisions concerning detrimental acts contained in the *lex concursus*.

In proposing a Global Rule for global application, based on that of Article 6 of the EU Insolvency Regulation, the Reporters consider it to be essential to anticipate that some parties may seek to exploit the possibilities presented by the principle of party autonomy in selecting the law to govern an international contract. By so expressing their choice as to engage the law of an otherwise unconnected system of law that happens to be favorable to the doctrine of set-off, they may aspire to circumvent the law and policy of the system of law to which the insolvent debtor would otherwise be subject. Accordingly, Global Rule 18 operates to prevent the effect of Global Rule 17 from being invoked in a case where, in the absence of an express choice made by the parties, the law applicable to the insolvent debtor's claim would be that of the law of the state of the opening of insolvency proceedings, unless it is shown that there is a substantial relationship between the chosen law and the parties or the transaction, or that there is some other reasonable basis for the parties' choice. Moreover, Global Rule 21 ensures that the operation of Global Rule 17 itself does not give rise to immunity from the provisions concerning detrimental acts contained in the *lex fori concursus*. Consequently if, as a result of the application of the avoidance rule of the law of the state of the opening of main insolvency proceedings, the creditor's claim against the insolvent estate is either reduced in amount or is avoided completely, the creditor may be wholly or partly deprived of the benefit of set-off against the insolvent debtor's claim that might otherwise have been available. Finally, Global Rule 21 ensures application of the provisions concerning detrimental acts contained in the *lex concursus*. This principle could, for instance, apply in the event that A has a debt payable to the estate but also has a claim assigned to him by B against the estate and A demands set-off, a situation that, for example, is disallowed under the Netherlands Article 54(1) *Faillissementswet*.

## REPORTERS' NOTES

The exceptions that relate to third parties' rights in rem and to set-off are structured similarly and use similar wording. See the Appendix to this Report for the description of "shall not affect." The obligatory aspects concerning set-off are determined by private-international-law rules that form part of a state's law of obligations. Where set-off is concerned, two claims are mutually satisfied. In theory, the right to demand set-off is determined by either (a) the cumulative application of the laws applicable to each of the individual claims, or (b) solely by the law applicable to the debtor's claim ("passive" claim in the set-off; sometimes termed "primary" claim) against which the creditor intends to set-off his counter-claim ("active" claim in the set-off) against the debtor. The EU Insolvency Regulation comprises the latter method in that the right to set-off is derived from "the law applicable to the insolvent debtor's claim," see Article 6, that is, the law applicable to the claim under which the insolvent debtor is the creditor in relation to the other party, see Virgós / Schmit Report, nr. 108. The latter law is sometimes referred to as the *lex debitoris*. The assessment of the law that is applicable to the claim of the insolvent debtor is not the law at the time of the opening of the main proceedings, but at a prior point in time, that is, the moment that the right to set-off was created.

It is explained above that Article 6 of the EU Insolvency Regulation allows the creditor to retain its right to set-off as an acquired right against the insolvency proceedings (the right to set-off is not affected by the opening of proceedings) when "the normally applicable rules of conflict of laws" so provide, which could be the laws of (potentially) any state in the world. This is acknowledged in Article 2 of the Rome Convention. As new Member States have joined the EU since 1980, accession to the Rome Convention has been included among the terms of entry negotiated between the EU and its existing Members and the candidates for membership. For example, Spain (together with Portugal) acceded to the Rome Convention with effect from 1 September 1993 upon ratification of the Funchal Convention of 18 May 1992 (OJ 1992, C333/1). See Dicey, Morris, and Collins, The Conflict of Laws, 14th Ed. 2006, with cumulative supplements, para. 32-011, providing a list of accession conventions, etc., in fn.31.

It should be noted that in the German language, Article 4(2)(d) of the EU Insolvency Regulation reads that the *lex concursus* determines "*die Voraussetzungen für die Wirksamkeit einer Aufrechnung*" (according to our translation: "the presumptions for the effect of set-off"), where the English text reads "the conditions under which set-offs may be invoked"). The (alleged) difference in the text has led to the question being raised in German literature as to whether such presumptions also include material conditions, which according to this interpretation would be determined by the *lex causae*. For a summary of this debate, see Jens Haubold, *Europäische Insolvenzverordnung, Kapitel 32*, in: Gebauer M./ Wiedmann, T. (Eds.), *Zivilrecht unter europäischem Einfluss. Die richtlinienkonforme Auslegung des BGB und andere Gesetze—Erläuterung der wichtigsten EG-Verordnungen*, Richard Boorberg Verlag, 2. Auflage, 2010, nr. 125; Christoph Jeremias, *Internationale Insolvenzaufrechnung*, Max-Planck-Institut für ausländisches und internationales Privatrecht, Studien zum ausländischen und internationalen Privatrecht, nr. 150, Tübingen: Mohr Siebeck, 2005, p. 240ff. The latter author concludes (op. cit., p. 255) that Article 4(2)(d)'s *lex concursus* is decisive with regard to both the substantive legal effects of set-off as well as the permissibility of set-off during insolvency. In this way, too, see Miguel Virgós and Fransisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 181ff.

Article 6 of the EU Insolvency Regulation only concerns a right to set-off arising in respect of mutual claims incurred prior to the opening of the insolvency proceedings. After this moment in time, Article 4 will be applied, without exception, to decide whether or not the set-off is admissible (see the Virgós /

Schmit Report, nr. 110). An obvious question concerns the maturing of claims. According to Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 188, Article 6 applies "when the claims arose out of contracts or other dealings entered into prior to the opening of the insolvency proceedings, even if they were, at that moment, mature or unmature, contingent or not." We concur with this statement.

For the earlier statement made above, that presently under English and Netherlands rules of private international law (outside of the scope of the EU Insolvency Regulation) the rule of Article 6 is followed, see the current edition of Dicey, Morris, and Collins, The Conflict of Laws, 14th edition 2006, para. 7-032, where the learned editors, having drawn a distinction between procedural and substantive set-off (the former being concerned with the possibility that certain kinds of claim may be triable together according to the procedural rules of the *lex fori*), then state: "A set-off may, on the other hand, amount to an equity directly attaching to the claim and operate in partial or total extinction thereof; an example is the compensation *de plein droit* of French law. The question whether a set-off of this kind exists is one of substance for the *lex causae*, that is, the law governing the claim that the defendant asserts has been discharged in whole or in part." (footnotes omitted). In the passage quoted above, "the claim which the defendant asserts has been discharged in whole or in part" corresponds to the "passive" claim, as between the creditor and the insolvent debtor, because that is the claim that would be enforced against the creditor (as defendant) by the insolvent debtor (as claimant). For the Netherlands, it has been suggested that in the light of the judgment of the Netherlands Supreme Court 24 October 1997, JOR 1997/146; NJ 1999, 316, the rule laid down in Article 6 may provide the inspiration for solutions in cases that fall outside the scope of the Regulation, see Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, para. 10664. The principle indeed has been applied by District Court Amsterdam 17 December 2009, LJN: BI2613 (Australian parent company with subsidiary in the Netherlands).

Global Rule 17 aims to provide a rule for set-off in general. In as far as set-off covers a phenomenon such as "netting," the Reporters have not drafted a global principle. It is noted that the UNCITRAL Legislative Guide offers the following recommendation nr. 32: "Notwithstanding recommendation (31), the effects of insolvency proceedings on the rights and obligations of the participants in a payment or settlement system or in a regulated financial market should be governed solely by the law applicable to that system or market." Specific rights concerning set-off belonging to the participants of a payment or settlement system or to a financial market, as pursuant to Article 9 of the EU Insolvency Regulation, shall be governed solely by the law of the Member State applicable to that system or market.

There is considerable debate as to the meaning of the reference to "law" as used in various contexts under the EU Insolvency Regulation. With regard to Article 6, the issue is whether the word "law" in the wording of that Article ("the law applicable to the insolvent debtor's claim") refers only to a state's general civil law governing the debtor's claim, or whether "law" also includes the insolvency-law provisions of such law? The wording of Article 6(1) is broad and the Virgós/Schmit Report (1996), para. 109, does not offer further elaboration, merely stating that Article 6 permits ". . . the set-off according to the conditions established for insolvency set-off by the law applicable to the insolvent debtor's claim ('passive' claim)." In literature, generally the approach is followed that in cases in which general civil law and insolvency law of a certain state provide for different requirements, any choice of the law of such a state also encompasses "insolvency law." In this way, several German, Austrian, and Dutch authors: Peter von Wilmowsky, *Aufrechnung in internationalen Insolvenzfällen*, in: Konkurs- Treuhand- und Schiedsgerichtswesen, Zeitschrift für Insolvenzrecht (KTS) 1998, p. 360; Stephan Kolmann, *Kooperationsmodelle im Internationalen Insolvenzrecht. Empfielt sich für das Deutsche internationale Insolvenzrecht eine Neuorientierung?*, Schriften zum

Deutschen und Europäischen Zivil-, Handels- und Prozessrecht, Bielefeld: Verlag Ernst und Werner Gieseking, 2001, p. 312 ("In its result the provision of Article 6 also leads to a most favoured treatment; only very minor limitations of insolvency law will be enforced, so the guarantee function [of set-off] can be realized to the optimal effect"); Christoph Jeremias, *Internationale Insolvenzaufrechnung*, Max-Planck-Institut für ausländisches und internationales Privatrecht, Studien zum ausländischen und internationalen Privatrecht, nr. 150, Tübingen: Mohr Siebeck, 2005, p. 259; H.-C. Duursma-Kepplinger, in: Duursma-Kepplinger, H.-C, Duursma, D, Chalupsky, E., *Europäische Insolvenzverordnung. Kommentar*, Springer, Wien New York, 2002, Art. 6, nr. 18; A.J. Berends, *Insolventie in het internationaal privaatrecht*, Ph.D. Vrije University, Amsterdam, 2005, p. 430 et seq.; Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, 10666.

## Rule 19 Reciprocal Contracts: General Rule

**Save as otherwise provided by [this Act/these Rules], mutual obligations in respect of a reciprocal contract, which has been concluded prior to insolvency of one of the parties, shall be governed solely by the law of the state of the opening of proceedings.**

## Rule 20 Contracts of Employment (Labor Contracts)

**The effects of insolvency proceedings on employment contracts and relationships shall be governed solely by the law of the state applicable to the contract of employment.**

## Rule 21 Restrictions to Exceptions

**Global Rules 15, 17, and 20 shall not preclude actions for voidness, voidability, or unenforceability of legal acts detrimental to the general body of creditors, pursuant to the law applicable to the insolvency proceedings, as determined by Global Rule 12 or by Global Rule 13 (as the case may be).**

## Comment to Global Rules 19-21:

Any insolvency of a party will have effect on the existence or the performance of reciprocal (synallagmatic) contracts, which have been concluded prior to insolvency of one of the parties. If, at the time of the opening of main proceedings, mutual obligations are still to be (fully) performed by both parties in respect of a current contract, applicable national insolvency law may contain a provision that the contract is deemed to be dissolved by operation of law. Alternatively, under the relevant national insolvency law, where both parties have failed to perform their obligations (fully or partially) under a reciprocal contract, the liquidator may have the authority, by operation of law, to choose whether he will continue performance or not. When he chooses not to do so, the relevant national insolvency law may contain a specific rule or sanction, in general protecting the interests of the counterparty. In the Netherlands, if a liquidator has not declared himself willing to be bound by the contract within a reasonable term set by the counterparty in writing, the liquidator will forfeit the right to demand performance of the contract (see Article 37(1) Dutch *Faillissementswet*). A similar rule exists in Germany (§ 103 *Insolvenz Ordnung*). Such rules generally aim to protect the insolvent estate against mandatory performance of the contract that could be detrimental to the estate, due to the changed circumstances, see Virgós / Schmit Report (1996), nr. 116, to which is added (op. cit., nr. 117), that, in the Insolvency Regulation, the general rule on conflict of laws is that the regulation of the effects of proceedings on current contracts to which the debtor is party falls to the law of the Member State of the opening of the main proceedings, see Article 4(2)(e). Therefore, the *lex concursus* and not the *lex contractus* determines these effects.[365] The applicable national insolvency law interferes with and displaces the rules applicable to contracts, which derive from the law applicable under the Rome Convention. This is generally considered to be to the advantage of creditors, see Virgós / Schmit Report, nr. 117.[366]

Both the EU Insolvency Regulation (Article 4(2)(e)), and the UNCITRAL Legislative Guide (Recommendation 31) assert that the *lex fori concursus* should apply to all aspects of the commencement, conduct, administration, and conclusion of insolvency proceedings and their effects (emphasis added). In neither of these sources does one find an elucidation of the terminology "effects." If and insofar as the opening, the conduct, or the closure of main proceedings has "effects" on a current contract, such effects will be governed by the *lex fori concursus.* According to Global Rule 19, those effects will be extended all over the globe. In literature on the European continent, the question has been raised as to whether an "effect" will include the provision in the *lex fori concursus* that the counterparty has an obligation to continue supplying (or more generally, continue performing), for example, the supply of energy, finance, or bank credit (hypothesising that the *lex concursus* contains such provisions) or that the counterparty may first ask to be paid the overdue payments or lodge a claim against the estate as an unsecured creditor for the total amount. A logical consequence of the proposed Global Rule 19 is that, for instance, the mandatory obligation, for example, to continue performance of certain obligations (e.g., the supply of energy or water) and therefore the injunction to prevent suspension, represents an "effect" of proceedings to which the *lex concursus*, containing such a provision, applies. It appears that, in material terms, the difference will be not so great as the question of which claims may be lodged in the estate, which consequences arise from claims created after the opening of proceedings, and which rules govern the lodging, verification, and admission of claims, all of which will be decided according to the *lex concursus* (Article 4(2)(g) and (h) EU Insolvency Regulation).

Based on perceived impressions of the importance of certain social policies and on several high-profile court cases,[367] the Reporters believe that a rule of global application should be

[365] See, e.g., Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 197; Jasnica Garašić, Recognition of Foreign Insolvency Proceedings: the Rules that a Modern Model of International Insolvency Law Should Contain, in: Yearbook of Private International Law, 2005, vol. 5, p. 349.

[366] This rule must be regarded as current Netherlands' private international insolvency law, which will also therefore govern the consequences of current contracts when the counterparty to a contract is located in another state. On the other hand, under English law, according to settled (albeit controversial) authority, an insolvency proceeding taking place in a foreign jurisdiction that is the debtor's domiciliary forum is not considered to be effective to discharge a contractual obligation of the debtor that is governed by English law (Gibbs v. La Société Industrielle et Commerciale des Métaux (1890) 25 Q.B.D. 399 (CA). See Ian F. Fletcher, Insolvency in Private International Law. National and International Approaches, Oxford Private International Law Series, Oxford University Press, 2nd ed. 2005, 2.124-2.129.

[367] E.g., the *Daisytek* case, Re Daisytek-ISA Ltd [2003] BCC 562 (High Court, UK); JOR 2003/287; NZI 2004, 219.

proposed with regard to current contracts of employment in case of the insolvency of the employer. A clear rule to apply to such contracts will contribute to the certainty that employees should have with regard to the question: what law is to govern the performance of the obligations of the employer versus the employee? This includes such issues as deciding which law is to be applied to a certain term, or what period is to be observed when terminating such a contract, including the legal consequences of such termination. The challenge in drafting an appropriate choice-of-law rule for such cases is therefore to respect the need to prevent possible conflicts between the legislative policies of the various states concerned, which reflect the varying approaches to the protection of different social or general interests with regard to employment.[368] A rule that reflects the balance of current opinion on the best response to this challenge is contained in Article 10 of the EU Insolvency Regulation (stipulating that the applicable law is the law applicable to the contract of employment), see further below. A similar approach has been followed for relations with non-EU states in, for example, Germany (Article 337), Spain (Article 207), Croatia (Article 305), and the Netherlands (Pre-draft Article 10.4.7).[369]

Both the EU Insolvency Regulation and the UNCITRAL Legislative Guide follow an aligned path in their approach to the matter of contracts of employment. Article 10 of the EU Insolvency Regulation declares: "The effects of insolvency proceedings on employment contracts and relationships shall be governed solely by the law of the Member State applicable to the contract of employment." Its rationale is explained in Recital (28): "In order to protect employees and jobs, the effects of insolvency proceedings on the continuation or termination of employment and on the rights and obligations of all parties to such employment must be determined by the law applicable to the agreement in accordance with the general rules on conflict of law. Any other insolvency-law questions, such as whether the employees' claims are protected by preferential rights and what status such preferential rights may have, should be determined by the law of the opening State." The UNCITRAL Legislative Guide determines in recommendation 33: "Notwithstanding recommendation 31, the effects of insolvency proceedings on rejection, continuation and modification of labour contracts may be governed by the law applicable to the contract." The key basis for recommendation 33 is that, in several states, special (often mandatory) protections may be afforded in terms of a financial safety net for employees, or restrictions on the rejection or modification of those contracts in insolvency. The rationale of (mandatory) provisions, according to the Guide, ". . . lies in protecting the reasonable expectations of employees with respect to their contract of employment, recognizing that workers may have a relatively weaker bargaining position than their employer, and in ensuring non-discrimination amongst workers working in the same state, whether they are employed by a local or by a foreign employer." [para. 87]. Both sources mentioned, therefore, result in the application of the law of the (Member) state applicable to the employment/labor contract, sometimes referred to as "*lex laboris*." It is also notable that special rules of choice of law, whose purpose is to protect the employee against loss of protection resulting from the manipulation of the applicable law of the contract of employment, are included in the Rome Convention of 1980 (Article 6) and in Article 8 of the

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[368] See Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 201.

[369] As to choice of labor law, for example, see J.L. Westbrook, Multinational Financial Distress: The Last Hurrah of Territorialism, 41 Texas International Law Journal 321 (2006) (reviewing L.M. LoPucki, Courting Failure: How Competition for Big Cases is Corrupting the Bankruptcy Courts (2005)).

Rome I Regulation that has superseded the Rome Convention in respect of all EU Member States, except Denmark, with effect from December 17, 2009 (see further below).

It is noted that both the rules embodied in Article 10 of the EU Insolvency Regulation and in Recommendation 33 of the Legislative Guide represent a limited exception to the application of the *lex concursus*. They both constitute exceptions only with regard to their effects on current employment contracts, but do not cover other aspects regulated by the *lex concursus*, for instance, in the case of the EU Insolvency Regulation, the ranking of the resulting claim (Article 4(2)(i)); the rights of the employee after the proceedings are closed (Article 4(2)(k)); and the voidness, voidability, or unenforceability of acts that are detrimental to the creditors as a whole (Article 4(2)(m) and Article 13). These issues have to be resolved by the *lex concursus*. The *lex concursus* governs the "effects" of the main insolvency proceedings on current employment contracts to which the debtor is party, see Article 4(2)(e). The rights and obligations based on, or derived from, the contract itself remain to be determined by the *lex causae* of the contract of employment. The question who is an "employee" in the meaning of Global Rule 20 is to be determined by the internal law of the state applicable to the contract of employment. In many states, the frontiers of meaning of the term "employee" are tested, for example, quasi self-employed persons, artists or persons who are to deliver a certain result of service, without continuous supervision or control by a third party. It is the law applicable that is decisive.[370]

The proposal for Global Rule 21 can be explained using a European background. In the European context, a rule similar to Global Rule 21 is explicitly drafted for rights in rem and reservation of title (Articles 5 and 7 EU Insolvency Regulation). Under the application of the EU Insolvency Regulation, it has, however, been questioned whether Article 13 is applicable to (detrimental) acts relating to contracts that fall under the scope of Article 10 (employment). The *lex laboris* applies "solely" to such contracts. In agreement with H.-C. Duursma-Kepplinger, in: Duursma-Kepplinger, H.-C, Duursma, D, Chalupsky, E., Europäische Insolvenzverordnung. Kommentar, Springer, Wien New York, 2002, Art. 13, nr. 22, we are of the opinion that the law relating to detrimental acts serves its own purposes, whereas the purpose of Article 10 is to protect certain, defined interests that are unrelated to acts which are detrimental to the general body of creditors. Article 13 of the EU Insolvency Regulation is applicable. No second paragraph with wording similar to, for example, that in Article 6 of the EU Insolvency regulation with regard to set-off ("2. Paragraph 1 shall not preclude actions for voidness, voidability or unenforceability as referred to in Article 4(2)(m)"), appears in the final text of Article 10. Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 232, argue that the omission of any reference in Article 10 to the possible application of Article 4(2)(m) is because Article 10 serves as an exception to 4(2)(e) and not as a general exception to Article 4, for which reason allegedly an explicit exception to Article 4(2)(m) was not considered necessary in Article 10. With respect, this reasoning is not readily obvious or apparent to someone reading Articles 4 and 10 as printed. As Global Rule 12 does not contain a list of items that are covered by the general principle of applicability of the *lex concursus*,

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[370] See Peter Mankowski, Contracts Relating to Intellectual or Industrial Property Rights under the Rome I Regulation, in: Stefan Leible and Ansgar Ohly (eds.), Intellectual Property and Private International Law, Tübingen: Mohr Siebeck 2009, 31ff, who submits that for the application of Article 8 Rome I Regulation, the persons mentioned should not be regarded as "employees."

and also for the sake of clarity, Global Rule 21 is proposed in order to ensure that the avoidance rules of the *lex fori concursus* as referred to in Global Rule 12 remain applicable.

## REPORTERS' NOTES

Based on Global Rules 12 and 13, in principle the law applicable to the effects of insolvency proceedings on current contracts to which the debtor is party is the *lex concursus*. Article 10 of the EU Insolvency Regulation provides for an exception, taking the form of the choice for another law to be applied. We have explained this form of exception in the commentary to Global Rule 12. The words "employment contract and relationships" in Article 10 of the EU Insolvency Regulation include, according to Christoph G. Paulus, *Die europäische Insolvenzverordnung und der deutsche Insolvenzverwalter*, in: Neue Zeitschrift für das Recht der Insolvenz und Sanierung (NZI) 2001, p. 513, collective (bargaining) employment contracts. For another view (limited to: individual employment contracts), see Peter Mankowski, *Europäisches Internationales Insolvenzrecht (EuInsVO), Kapitel 47*, Kölner Schrift zur Insolvenzordnung, 3. Aulage, Münster: ZAP Verlag 2009, nr. 118. On a European level, the broad interpretation is defensible, on a global scale it should indeed be limited to individual employment contracts. It should be noted that the quoted words, under the application of the EU Insolvency Regulation, must be interpreted autonomously and not according to the *lex laboris*, see Jens Haubold, *Europäische Insolvenzverordnung, Kapitel 32*, in: Gebauer M./ Wiedmann, T. (Eds.), *Zivilrecht unter europäischem Einfluss. Die richtlinienkonforme Auslegung des BGB und andere Gesetze—Erläuterung der wichtigsten EG-Verordnungen*, Richard Boorberg Verlag, 2. Auflage, 2010, nr. 135. In addition, when applying Article 10 of the EU Insolvency Regulation, the preliminary question of whether there is indeed an employment contract and what law applies to that contract (according to the *lex contractus*) has to be resolved, see Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 209; Jona Israël, European Cross-Border Insolvency Regulation: A Study of Regulation 1346/2000 on Insolvency proceedings in the Light of a Paradigm of Cooperation and a Comitas Europaea, Ph. D. European University Institute, Florence, 2004, Intersentia, Antwerp-Oxford, 2005, p. 284. This meaning also is reflected in Global Rule 19.

The power to terminate an employment contract is imposed according to the law governing the contract of employment. Where the exclusion should be narrowly construed, it follows that any time limits that must be observed must be calculated according to the *lex laboris*. Questions regarding the amount of the employees' claim, for example, whether or not compensation for holidays not taken should be included, is determined by the *lex laboris*. The actual lodging of the claim and the ranking of the claim are determined by the *lex concursus*, which follows from Article 4(2)(h) of the EU Insolvency Regulation (see the Virgós / Schmit Report, nr. 128; A.J. Berends, *Insolventie in het internationaal privaatrecht*, Ph.D. Vrije University Amsterdam, 2005, p. 316) and likewise from the general principle laid down in Global Rules 12 and 13.

Articles 6 and 7 of the Rome Convention (and correspondingly Articles 8 and 9 of the Rome I Regulation) determine which law applies to an individual employment contract, the general principle being that the parties are free to choose to which law the employment contract is subject, see Article 3 Rome Convention (and also Article 3 of the Rome I Regulation). By taking advantage of this free choice, the employee may not be deprived of the protection afforded to him by the mandatory rules of the law that would be applicable under Article 6(2) Rome Convention (see the corresponding provisions within Article 8(2), (3), and (4) of the Rome I Regulation) in the absence of this free choice. Article 6(2) of the Convention (and, to the same effect, Article 8(2) and (3) of the Rome I Regulation) sets out that an employment contract shall be governed (in the absence of a choice in accordance with Article 3): (i) by the law of the country in which the employee habitually carries out his work in performance of the contract, even if he is temporarily employed in another country, or (ii) if the employee does not habitually carry out his work in one country, by the law of the country in which the place of business through which he was engaged is situated. Both conflict rules are excluded if "it appears from the circumstances as a whole that the contract is more closely connected with another country," in which case the contract shall be governed by the law of that country.

Under the application of the above system, Article 7(1) of the Rome Convention allows effect to be accorded to the mandatory rules of the law of another country with which "the situation has a close connection, if and in so far as, under the law of the latter country, those rules must be applied whatever the law applicable to the contract." However, by Article 22(1)(a) of the Convention, a Contracting State is permitted to lodge a reservation whereby Article 7(1) shall not apply in proceedings that take place before the courts of the State in question. Several Contracting States, including Germany, Luxembourg, and the United Kingdom, have exercised the right of reservation in relation to Article 7(1). Also, by Article 16, the applicability of a rule of the law of any country specified by the Convention (i.e., by initial application of the Convention's choice-of-law rules) may be refused under the public policy (ordre public) of the State whose court is hearing the case, but only if such application is manifestly incompatible with the public policy of the forum. Among authors there has been considerable debate as to whether Article 7 of the Rome Convention allows a court to apply said rules, as this matter is specifically dealt with in Article 10 of the EU Insolvency Regulation (see Jona Israël, European Cross-Border Insolvency regulation. A Study of Regulation 1346/2000 on Insolvency proceedings in the Light of a Paradigm of Cooperation and a Comitas Europaea, Ph. D. European University Institute, Florence, 2004, Intersentia, Antwerp-Oxford, 2005, p. 285; Jasnica Garašić, *Anerkennung ausländischer Insolvenzverfahren*, Ph.D. Hamburg 2004, Frankfurt am Main: Peter Lang, 2005, 2 Volumes, Part II, p. 310). Under the redesigned provisions of the Rome I Regulation, now applicable to all Member States other than Denmark, Article 9(2) provides that "Nothing in this Regulation shall restrict the application of the overriding mandatory provisions of the law of the forum," and Article 21 ("Public policy of the forum") replicates the substance of Article 16 of the Rome Convention. However, Article 9(3) of the Rome I Regulation contains a provision that differs in a significant way from Article 7(1) of the Rome Convention. The new Article 9(3) states: "Effect may be given to the overriding mandatory provisions of the law of the country where the obligations arising out of the contract have to be or have been performed, in so far as those overriding mandatory provisions render the performance of the contract unlawful. In considering whether to give effect to those provisions, regard shall be had to their nature and purpose and to the consequences of their application or non-application." It should be noted that, unlike the Rome Convention, the Rome I Regulation contains no provision allowing a Member State any option whether to apply or disapply any provision of the Regulation, which is binding in its entirety and has the direct force of law within all the EU Member States, with the exception of Denmark, since December 17, 2009. The expression "overriding mandatory provisions" is defined in Article 9(3), and means: ". . . provisions the respect for which is regarded as crucial by a country for safeguarding its public interests, such as its political, social or economic organisation, to such an extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable to the contract under this Regulation."

## Rule 22 Defenses to the Avoidance of Detrimental Acts

**Global Rule 21 shall not apply where the person who benefited from an act detrimental to the general body of creditors provides evidence that:**

**(i) The said act is subject to the law of a state other than that of the state of the opening of proceedings; and**
**(ii) That law does not allow any means of challenging that act in the relevant case.**

**Rule 23 Exception**

**23.1. By way of exception to Global Rule 22, a transaction detrimental to the general body of creditors shall not be exempted from the effect of the avoidance rule of the law of the state of the opening of insolvency proceedings if proof is provided that the state to whose law the transaction is subject has no substantial relationship to the parties or the transaction, and there is no other reasonable basis for the selection of the law of that state as the law to govern the transaction in question.**
**23.2. It is for the party who claims that the conditions specified in Global Rule 23.1 are met, in relation to a particular transaction, to prove that those conditions are in fact met in the relevant case.**

**Comment to Global Rules 22 and 23:**

"Fraud by insolvent debtors, in particular by concealing assets or transferring them to foreign jurisdictions, is an increasing problem, in terms of both its frequency and its magnitude. The modern, interconnected world makes such fraud easier to conceive and carry out," thus the Guide to Enactment to the UNCITRAL Model Law, para. 14. To prevent and to attack fraudulent acts, which are to the detriment of creditors, it is of utmost importance to have a clear and robust rule, while at the same time ensuring that parties who have dealt with the debtor should be afforded measures of protection when they have acted in good faith. In the absence of such a safeguard, confidence in commercial transactions would be considerably weakened, and legitimate expectations of parties who have dealt in good faith, for value, and in the ordinary course of business, could be undermined through the application to the counterparty of a *lex concursus* that applies different rules and criteria for the challenge of transactions. It should also be borne in mind that a party may undergo an alteration of circumstances between the time of entering a transaction and the time of becoming insolvent, such that it becomes amenable to undergo insolvency proceedings in a different state to that whose law would have been reasonably anticipated by the counterparty at the time of the original transaction.

As has been repeatedly stated above, Article 4(2)(m) of the EU Insolvency Regulation supplies a basic choice-of-law rule to the effect that the *lex fori concursus* "shall determine the rules relating to the voidness, voidability or unenforceability of legal acts detrimental to all the creditors." However, the application of this rule is moderated by reason of the opening words of Article 4(1), "Save as otherwise provided in this Regulation . . . ." Article 13 of the Regulation provides for such an exception to the rule of general applicability of the avoidance rules of the *lex fori concursus*. Its text reads:
"Article 4(2)(m) shall not apply where the person who benefited from an act detrimental to all the creditors provides proof that:
- the said act is subject to the law of a Member State other than that of the State of the opening of proceedings, and
- that law does not allow any means of challenging that act in the relevant case."

The antithesis between the provisions of Article 4(2)(m) and Article 13 is explained as follows. While in the first instance, and as a basic rule, the *lex concursus* of the state of the opening of the insolvency proceedings determines the rules relating to the voidness, voidability, or unenforceability of legal acts detrimental to the general body of creditors, it is the aim of Article 13 ". . . . to uphold legitimate expectations (of creditors or third parties) of the validity of the act in accordance with the normally applicable national law, against interference from a different '*lex concursus*,'" see Virgós / Schmit Report (1996), para. 138. The same paragraph of the Report proceeds to express the opinion that the application of Article 13 is justified with regard to acts carried out prior to the opening of the insolvency proceedings, and ". . . . threatened by either the retroactive nature of the insolvency proceedings opened in another country or actions to set aside previous acts of the debtor brought by the liquidator in those proceedings." A similar rule in relationships to non-EU states has been introduced in Germany (Section 339), in Spain (Article 208),[371] and the pre-draft of November 2007 in the Netherlands (Article 10.4.9).[372]

The attainment of enhanced certainty and predictability and the principle of protection of legitimate expectations results in a rule that only applies to acts carried out prior to the opening of the insolvency proceedings. After opening of such proceedings in another state, the creditor's reliance on the validity of the transaction under the national law applicable in noninsolvency situations is no longer justified. From that moment on, all unauthorized disposals by the debtor are, in principle, ineffective by virtue of the divestment of his powers to dispose of the assets. National law may supply answers for situations in which a creditor was not aware of insolvency, including those cases in which this creditor acted in the normal course of business transactions.[373] The provision is based on the premise that all such dispositions are void unless validated by the court. If applied inflexibly and insensitively, such a rule could have devastating consequences for any debtor experiencing a period of financial difficulty during which some unpaid creditor happens to take the first formal step to initiate an insolvency proceeding. Even if the debtor may have genuine grounds for resisting that process, any legal uncertainty as to the integrity of transactions entered into during the interim period, while resolution of the matter is pending, may precipitate the very collapse that the debtor is striving to avert, as business may be stultified in the meantime. The risk of such an unwanted outcome may be mitigated by a prudent judicial approach to the exercise of the power to validate transactions entered into during such a "twilight" period between a third party and the debtor, provided that the dealings are conducted for value, in good faith, and in the ordinary course of business. The confidence thereby engendered in the ultimate confirmation of legitimate transactions may enable the debtor to continue to trade while awaiting the outcome of a pending application to open insolvency proceedings, especially where there is a valid case for resisting the application, or where the completion of transactions will result in a preservation of value for the benefit of creditors generally.

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[371] For a comparison between the German and Spanish rules, see Anna-Maja Schaefer, *Das autonome international Insolvenzrecht Spaniens im Vergleich zum deutschen Recht*, Schriten der Deutch-Spanischen Juristenvereinigung, Band 31, Peter Lang Frankfurt, 2009, p. 188.

[372] In this way, too, see Virgós / Schmit Report, nr. 93, alleging that the need to protect legitimate expectations and the certainty of transactions is equally valid in relations with non-EU states.

[373] For instance, Insolvency Act 1986, s.127 (UK) confers a discretion on the court to validate a post-insolvency disposition of property of the debtor.

Global Rule 22 aspires to complement such rules and practices of domestic law as may be designed to sustain commercial confidence in the integrity of bona fide transactions that take place during a period of uncertainty regarding the debtor's solvency. It is self-evidently based upon the terms of Article 13 of the EU Insolvency Regulation, and in a similar way Global Rule 22 is designed to bring about the displacement of the avoidance rules of the *lex fori concursus* where the person who benefited from the transaction is able to show that it is subject to the law of a state other than that in which insolvency proceedings are opened, and that the *lex causae* does not allow any means of challenging the act in question in the actual circumstances under which it has taken place. Two particular points of divergence should be noticed between the wording of Global Rule 22 and Article 13 of the EU Insolvency Regulation. First, for reasons already explained above, the expression "an act detrimental to the general body of creditors" has been employed in preference to "an act detrimental to all the creditors," as is used in Article 13. Secondly, as befits a rule intended for global application, no qualifying adjective is attached to the word "state" where it is used in paragraph (i) to refer to the act being "subject to the law of a state other than that of the state of the opening of proceedings," whereas in Article 13 the more limited reference is made to "the law of a Member State . . . ." The absence of such a restriction in Global Rule 22 is necessitated by the global context in which the rule is destined to operate, but it is also necessary to create a balancing provision in view of the obvious potential for exploitation of the liberal terms in which the Rule is drafted. Global Rule 23 is designed to answer that need (see below).

The structure of Global Rule 22 is such that the *lex fori concursus* will not apply if the person who benefited from the act whose validity is challenged provides the proof as required in paragraphs (i) and (ii). This entails a two-phase process. It must be presupposed that, in the first instance, a challenge to the validity of the act in question is made in accordance with the provisions of the *lex fori concursus* by a party eligible to do so—typically the insolvency office holder. Two elements that are logically required to be proven are "benefit" to one or more individual persons and "detriment" to creditors generally. Such benefit and detriment are governed in this initial phase of the process by the *lex fori concursus* and have to be stated and proved by the party invoking the avoidance rule of that system of law. This rule of proof is followed under the application of the EU Insolvency Regulation.[374] In the next phase, the burden of proof falls upon the person who seeks to enforce the exception to the avoidance rule of the *lex fori concursus*. To do so, the defendant must show that the *lex causae* does not allow any means of challenging the act in question in the relevant case. The expression "in the relevant case," used both in Global Rule 22 and in Global Rule 23, means that the act should not be capable of being challenged in fact, that is, after taking into account all the concrete circumstances of the given case: "It is not sufficient to determine whether it can be challenged in the abstract" (see Virgós / Schmit Report, nr. 137). Moreover, the process of proving that the *lex causae* does not allow any means of "challenging" that act requires the defendant to demonstrate that neither the insolvency law of that state nor the general (civil) law, if applied to said act, contain any ground on which a successful challenge

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[374] See, e.g., Miguel Virgós and Fransisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 240; Jona Israël, European Cross-Border Insolvency regulation. A Study of Regulation 1346/2000 on Insolvency proceedings in the Light of a Paradigm of Cooperation and a Comitas Europaea, Ph. D. European University Institute, Florence, 2004, Intersentia, Antwerp-Oxford, 2005, p. 288; Jasnica Garašić, *Anerkennung ausländischer Insolvenzverfahren*, Ph.D. Hamburg 2004, Frankfurt am Main: Peter Lang, 2005, 2 Volumes, Part II, p. 360.

could be maintained on the basis of the evidence concerning the actual circumstances in which the act took place (see again Virgós / Schmit Report (1996), nr. 137). It should be noted that there is no requirement that any actual proceeding—such as an insolvency proceeding—should actually take place in the state whose law happens to be the *lex causae* of the act that is subject to challenge. The task of ascertaining the contents of that law, and of assessing the consequences of its application to the circumstances of the act in question, involves a special exercise in what is termed the proof of foreign law, which will be conducted according to the practice and tradition of the *forum concursus* regarding such matters, during the course of litigation before the courts of that state.

The two-phase process of challenge, and the complex burden of proof imposed upon the defendant who is required, in effect, to "prove a negative" with respect to every possible ground on which the act could be challenged under the *lex causae*, results in several questions of private international law that are not related to insolvency law itself. For instance, the question how the *lex causae* should be determined remains a matter to be resolved in accordance with the system of private international law of the state before whose court the challenge to the act is taking place. Illustrative of the problems to be encountered in this context is the question of which law is decisive of the (detrimental) act as far as concerns the transfer of assets. The *lex causae* of the act (e.g., the contract) will be relevant to the application of Global Rule 22, also for acts concerning transfer of property of assets. In such a case, the system may be that the *lex rei sitae* of the assets must be assessed (i) in the event of transfer or encumbrance of assets, and (ii) with regard to the voidness etc. of the underlying contract, irrespective of the law that is applicable to the act itself. Conversely, with regard to the law of property, certain aspects of assignment and pledging of claims, the possibility of a choice of law may exist.[375] If the alleged detrimental act is a payment, then a national private-international-law system may contain a rule providing that the *lex causae* of the payment should be the law that governs the obligation to pay and therefore not the *lex contractus* that governs the method of payment.[376] On the other hand, the application of Global Rule 22 assumes that no provision exists ("That law does not allow any means," see Global Rule 22(ii)) which provides grounds to challenge the debtor's act, either under the *lex causae*'s general (civil) law or under its insolvency law. The rationale is, after all, the attainment of enhanced certainty and predictability and the principle of protection of legitimate expectations of a creditor or third party concerning the legal validity and the effectiveness of an act that has been performed, against interferences of the *lex fori concursus* of another state.

Article 13 of the EU Insolvency Regulation is intended to offer only a limited scope for displacement of the avoidance rule of the *lex fori concursus* by some alternative applicable law by which the act is governed. By expressly restricting the scope of the exception to cases where the lex causae is that of an EU Member State, Article 13 gives rise in practice to somewhat limited possibilities of escape from the avoidance rule of the *lex fori concursus*. Even so, the inclusion of this exception in the Insolvency Regulation was not uncontroversial.

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375 See, e.g., Dutch private international law, see Netherlands Supreme Court 16 May 1997, NJ 1998, 585 (*Hansa Chemie*).

376 See H.L.E. Verhagen and P.M. Veder, *Faillissementspauliana*, in: Tijdschrift voor Insolventierecht (TvI) 2002/Special—Insolventieverordening, p. 137ff; Miguel Virgós and Francisco Garcimartín, The EC Regulation on Insolvency Proceedings: A Practical Commentary, Kluwer Law International, 2004, nr. 231, and Bob Wessels, International Insolvency Law, Deventer: Kluwer, 3rd ed., 2012, para. 10720.

Ultimately, the possible disadvantage of international forum-shopping was considered to be less important than providing the possibility of protection for a third party against a sudden confrontation with foreign law, that is, the *lex fori concursus*. In transposing this principle to a global level of application, it must be borne in mind that, in some circumstances, a state's law might be selected as the *lex causae* of a transaction purely on account of its unusually favorable provisions from the standpoint of a party who may subsequently wish to resist any challenge to the validity of the transaction, particularly (though not exclusively) in the event of the insolvency of the other party. Global Rule 23 is intended to provide a safeguard against attempts to exploit such advantageous attributes embodied in the law of a state that has otherwise no substantial connection with the transaction or the parties to it, and where there is no other reasonable basis on which the law of that state could be applicable to the transaction.

## REPORTERS' NOTES

In literature, the combination of the applicability of the general rule (*lex fori concursus*) together with the defense mechanism, which is contained in Article 13 of the EU Insolvency Regulation (a defense against the application of the *lex concursus*, to be invoked by any interested party), has been greeted with acceptance. At the same time, criticism has been expressed, both on the chosen combination and—accepting the combination—the uncertainties it contains. See, e.g., Jan Peter Klumb, *Kollisionsrecht der Insolvenzanfechtung*, KTS Schriften zum Insolvenzrecht, Band 25, Carl Heymans Verlag, 2005, and Christoph Thole, *Die tatbestandlichen Wertungen der Glaubigeranfechtung*, Zeitschrift für Zivilprocess (ZZP) 2008, Heft 1, pp. 67-92. Both authors point at the difficulty that the legislation in certain states may contain different rules regarding avoidance in insolvency matters and outside insolvency. See also Jay L. Westbrook, Avoidance of Pre-Bankruptcy Transactions in Multinational Bankruptcy Cases, 42 Texas International Law Journal 899 (2007), at 914. As a general rule, we would suggest that there is no free choice for a certain law, but that insolvency avoidance rules should be applied, as these in general will be created for the benefit of the body of creditors, where the noninsolvency rules more probably only benefit one creditor.

The defense operates against a plea for the voidness, etc., of the act, which would follow from the application of the *lex fori concursus* or as a "veto," based on the *lex causae*, against the dominance of the *lex fori concursus*, see Virgós / Schmit Report, nr. 136; H.-C. Duursma-Kepplinger, in: Duursma-Kepplinger, H.-C, Duursma, D, Chalupsky, E., *Europäische Insolvenzverordnung. Kommentar,* Springer, Wien New York, 2002, Art. 13, nr. 5; Sebastian Zeeck, *Das Internationale Anfechtungsrecht in der Insolvenz*. Max-Planck-Institut für ausländisches und internationales Privatrecht, Studien zum ausländischen und internationalen Privatrecht, nr. 108, Tübingen, Mohr Siebeck, 2003, p. 76; Georg E. Kodek, *Die Geltendmachung von Anfechtungsansprüchen nach der EuInsVo*, in: Andreas Knonecny (ed.), *Insolvenz-Forum 2004*. Vorträge anlässlich des 11. Insolvenz-Forums Grundslee im November 2004, Wien Graz: Neuer Wissenschaftlicher Verlag, 2005, p. 119ff. The in-built limitation, referred to above, results in a "veto by the *lex causae*" ("That law does not allow any means of challenging that act in the relevant case," see Global Rule 22(ii)), which could be seen as too broad in a worldwide context, open for manipulation and in its result contradictory to the predictable rule of the application of *lex concursus*, as observed in literature. Critical opinions towards the approach as chosen in Article 13 are expressed by, e.g., Sebastian Zeeck, *Das Internationale Anfechtungsrecht in der Insolvenz*. Max-Planck-Institut für ausländisches und internationales Privatrecht, Studien zum ausländischen und internationalen Privatrecht, nr. 108, Tübingen, Mohr Siebeck, 2003, p. 127ff; Jasnica Garašić, *Anerkennung ausländischer Insolvenzverfahren*, Ph.D. Hamburg 2004, Frankfurt am Main: Peter Lang, 2005, 2 Volumes, Part II, p. 324, and Westbrook, in: 42 Texas International Law Journal (2007). Zeeck has submitted an alternative solution ("The proposed connection alternatively invokes the *lex fori concursus* or the *lex causae* of the legal act to be avoided—subject to which law, in each individual case, is most favourable to avoidance, thus allowing avoidance wherever possible"). This alternative drifts away from the central principle of the applicability of the *lex fori concursus*, as laid down in Global Rule 12. Jasnica Garašić, *Anerkennung ausländischer Insolvenzverfahren*, Ph.D. Hamburg 2004, Frankfurt am Main: Peter Lang, 2005, 2 Volumes, Part II, p. 324, and Jasnica Garašić, Recognition of Foreign Insolvency Proceedings: the Rules that a Modern Model of International Insolvency Law Should Contain, in: Yearbook of Private International Law, 2005, vol. 5, p. 371, on the other hand favors, as a rule, that the *lex fori concursus* is the applicable law for insolvency-law avoidance as, in her opinion, it represents the law of the closest connection. Applying such a rule would, in our view, diminish a party's justified protection of legitimate expectations arising from the transaction. Westbrook has suggested that, given countries' differences in rules regarding avoidance and distribution, the choice of applicable avoidance law should depend "on which proceeding will be distributing the proceeds of an avoidance recovery," which in general will be the main proceeding, see Jay L. Westbrook, The Present and Future of Multinational Insolvency, in: Bob Wessels and Paul Omar (eds.), The Intersection of Insolvency and Company Laws, Nottingham, Paris: INSOL Europe 2009, 111ff (p. 114). Westbrook disagrees with the defense mechanism, similarly as reflected in Article 13 of the EU Insolvency Regulation, as it results in the principle that a specific transaction is not avoidable unless it would be avoidable under both relevant laws. See Jay L. Westbrook, Avoidance of Pre-Bankruptcy Transactions in Multinational Bankruptcy Cases, 42 Texas International Law Journal 899 (2007), at 913.

Where, in any transaction, parties would be able to maneuver their transaction and bring it under a system with any avoidance rules at all, Global Rule 23.1 aims to avoid the effect of Rule 22 "if proof is provided that the state to whose law the transaction is subject has no substantial relationship to the parties or the transaction, and there is no other reasonable basis for the selection of the law of that state as the law to govern the transaction in question." The rationale of Global Rule 23 is that in the situation in which the Rule applies, the expectations of the person who benefited from an act detrimental to the general body of creditors cannot be said to be legitimate. It is formulated as an exception to the applicability of the *lex causae* at the expense of the avoidance law of the *lex fori concursus*, to stress the importance of the protection of the interests of the body of creditors as a whole.

We conclude these Notes with three examples:
(a) Debtor D, whose COMI is in state X, enters into a transaction with counterparty CP, based in state Y. The parties expressly choose the law of Y to govern the transaction. D undergoes insolvency proceedings in state X, by the law of which the transaction would be voidable at the instance of the insolvency office holder (e.g., a liquidator, L), as detrimental to the general body of creditors. CP can demonstrate that under the law of Y (both under the general law as well as the insolvency law of that state) no action could be successfully brought by L to impeach the transaction under the actual circumstances in which it took place. The court of X should conclude that in view of the connection between CP and state Y, there is a substantial relationship between the parties or the transaction and the law of Y, and additionally that the choice of the law of Y has a reasonable basis. Accordingly the court should uphold the defense invoked by CP based on the law of Y. See Global Rule 22.

(b) With the parties' roles and affiliations as in (a) above, but with the additional feature that the transaction would also be voidable by the law of state Y, the transaction is expressed to be governed by the law of state Z, which has no functional connection with either of the parties or their transaction. However, under the law of Z it is very difficult to bring about the avoidance of consensual transactions, and CP can demonstrate that it would be able to defend L's action. The court in X could properly conclude that the transaction is unconnected with Z and that there is no reasonable basis for the choice of the law of Z (since the only apparent motive for doing so is to avoid the application of the law of X or Y). Accordingly, L's action, based on the avoidance rule of state X, should succeed. See Global Rule 23.1.

(c) With the parties' roles and affiliations once again as in (a) above, the transaction is expressed to be governed by the law of state M. Although there is no functional connection between the parties or the transaction and state M itself, it can be shown that there is a very common practice, among parties entering into transactions of the kind in question, to specify the law of M as the governing law. This is on account of the fact that M is a major center for international dealings of this type, and its law is widely understood and accepted as providing the standard basis for such business. The court in state X should acknowledge that in view of the established international practice of choosing the law of M, there is a reasonable basis for its choice by CP and D as the governing law of their transaction. If CP can demonstrate that it would be able to defend L's action according to the law of M, that defense should succeed in proceedings brought by L in the court of state X. See Global Rule 23.1.