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The European Insolvency Regulation - The First Years

Sweden's Perspective

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1. INTRODUCTORY REMARKS

On 31 May 2002 the European Council Regulation on Insolvency Proceedings ("the Regulation") came into force, at the same time becoming a binding instrument for all states of the European Union with the exception of Denmark. In addition to the Regulation, we also have the Directive on reorganisation and winding up of insurance undertakings and the Directive on the reorganisation and winding up of credit institutions ("the Directives")[1]. The Directives should have been implemented in each Member State by 20 April 2003 and by 5 May 2004 respectively, at the latest.

The Regulation and the Directives led the Swedish Ministry of Justice to appoint Swedish legal expert Mikael Mellqvist to analyse the necessary adjustments under Swedish law due to the Regulation and the Directives. Mr. Mellqvist submitted his report in a memorandum during 2002, proposing various adjustments to existing Swedish law and that supplementary provisions to the Regulation would be introduced.[2] The proposal has been reworked by the Swedish Ministry of justice and referred for consideration, remarks could be given until 24 March 2004. [3] At this time the Swedish Ministry of Justice is considering the remarks that have been given and their objective is that a new proposal will be finished shortly. This new proposal will then be referred to the Swedish Council of Legislation. According to the Swedish Constitution, the opinion of the Council on Legislation, comprising justices of the Supreme Court and of the Supreme Administrative Court, should be obtained before the Swedish Parliament takes a decision on a fundamental law concerning certain issues. Parliament will then vote on the bill that should provide for the amendments and the supplementary provisions to come into force at the earliest in the autumn of year 2005. Parts of the bill are summarised below in section 2.

In section 3 the Convention between Denmark, Finland, Norway, Sweden and Iceland on Bankruptcy, signed in Copenhagen on 7 November 1933, is discussed in a few words since the existence of two parallel legal instruments, both dealing with cross-boarder insolvency,

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[1] Directive 2001/17/EC of the European Parliament and of the Council of 19 March 2001 on the reorganisation and winding up of insurance undertakings and Directive 2001/24/EC of the European Parliament and the Council of 4 April 2001 on the reorganisation and winding up of credit institutions.
[2] See report Insolvens DS 2002:59
[3] See utkast till lagrådsremiss Europeisk insolvens (Ju2002/8967)

might lead to complications considering that Finland and Sweden are bound by the Regulation whilst Denmark, Island and Norway are not.

From a Swedish perspective the Regulation has been discussed in the legal literature as well as in the legal journals but has not, so far, resulted in any extensive legal problems being revealed. Further, the Regulation has to our knowledge only led to a few cases in higher courts. All cases dealt with jurisdictional matters or, more precisely, in which jurisdiction within the EU the centre of the debtor's main interest preferably was located. The cases are briefly described in section 4 below.

2. SWEDISH IMPLEMENTING MEASURES

As accounted for in the introductory part, the Regulation has caused the Swedish legislator to contemplate some amendments to existing Swedish legislation together with a supplementary Act relevant when applying the Regulation. A new act has also been proposed with a view to implement the Directives. A summary of these new features and an explanatory outline of existing Swedish bankruptcy law in the relevant areas are set out below.

The Swedish rules concerning international insolvency jurisdiction are based on analogies to the regulations on local jurisdiction of a court in the Swedish Code of Judicial Process. In short, this means that a Swedish bankruptcy can be initiated in Sweden if the debtor has its domicile/habitual residence or registered office in Sweden. A secondary bankruptcy can be initiated in a number of cases where the connection to Sweden is weaker than a requirement for domicile/habitual residence or registered office, for instance, the existence of assets in Sweden.

By the Regulation coming into force, the existing Swedish rules concerning the local jurisdiction of Swedish courts are not fully legally valid. The Regulation only gives the courts of a Member State jurisdiction to open insolvency proceedings in two cases; if the centre of the debtor's main interests are situated in the Member State or if the debtor possesses an establishment within the territory of a Member State, restricted to the assets of the debtor in the latter case. Thus, the Member State cannot base its jurisdiction in respect of an insolvency proceeding on other circumstances. Since the Regulation is legally binding in Sweden, no further ruling would be required.

Considering that the Regulation makes a distinction between main proceedings and secondary proceedings it seems important that a court establishes under which of the two categories an insolvency proceeding shall classify. It is therefore proposed in the bill that Swedish courts shall be under an obligation to state which of the two categories of insolvency proceedings the jurisdiction is based upon in the Regulation. This obligation would also apply to the applicant of bankruptcy or reorganisation.

According to Art 21.1 of the Regulation the liquidator may request that notice of the judgment opening insolvency proceedings etc. is published in any other Member State in accordance with the publication procedures provided for in that State. In Art. 21.2 a Member State may require mandatory publication, provided that the debtor has an establishment in such Member State. It is proposed that the Swedish Bolagsverket publishes the opening of insolvency proceedings in accordance with the existing rules on publication of a Swedish bankruptcy, and that such publication becomes mandatory in a situation where the debtor has an establishment in Sweden and a main insolvency proceeding has been initiated in another Member State.

Further it is proposed that the supplementary Act also includes a provision on mandatory registration in Sweden in accordance with Art. 22.2 of the Regulation.

One part of the supplementary Act that has provoked some criticism from a practitioners view is the section dealing with which party should be responsible for informing known creditors in other Member States when opening insolvency proceedings with cross-border effects.[4] Swedish standard procedures provide that the court generally performs this task. However, according to the supplementary Act, it will be the liquidators' responsibility to inform known creditors who have their habitual residences, domiciles or registered offices in the other Member States.[5] This seems to conflict with well-established Swedish principle of equal treatment of the creditors and also lead to problems in cases where it is unclear whether the Regulation is applicable or not.

In respect of the two Directives on the reorganisation and winding up of insurance undertakings and on the reorganisation and winding up of credit institutions, the content of the Directives corresponds to the Regulation in many respects. A great difference however is that the Directives do not make an exception from the universal principle, i.e. it is not possible to open a territorial insolvency proceeding. Thus, the administrative or judicial authorities in the home Member State are alone empowered to decide on the reorganisation or winding up measures. It is from a Swedish law perspective proposed that the two Directives are incorporated into one Act. Even though the date for implementation for the Directives has expired, the Act implementing the Directives has still not entered into force.

[4] Cf. Art 40.1 of the Regulation.
[5] Article 5 of the Supplementary Act.

The European Commission has decided to refer Sweden and seven other countries to the European Court of Justice as they have not yet implemented the Dirctive regarding insurance undertakings. In a judgement dated 18 November 2004 the European Court of Justice declared that Sweden has failed to fulfil its obligations under this Directive.[6]

[6] Case C-116/04 EC Commission v Sweden [2004]

3. THE CONVENTION BETWEEN DENMARK, FINLAND, NORWAY, SWEDEN AND ICELAND ON BANKRUPTCY

On the 7 November 1933, the Convention between Denmark, Finland, Norway, Sweden and Iceland on Bankruptcy (the "Convention") was signed and was incorporated in Sweden in 1934 by the Act on bankruptcy which includes assets in Denmark, Finland, Iceland or Norway and by the Act on the consequences of a bankruptcy in Denmark, Finland, Iceland or Norway. The Convention text has been revised since then and in relation to Denmark, Finland and Norway, the "Act (1981:6) on bankruptcy which includes assets in another Nordic country" and also the "Act (1981:7) on the consequences/effect of a bankruptcy in another Nordic country"

Generally, the Convention is regarded as being a successful convention and has been considered to fulfil the need of handling bankruptcies covering more than one Nordic country.

In connection to the Regulation entered into force, there is a risk that the inter-Nordic bankruptcies could be more difficult to handle. In respect of the issues dealt with in the Regulation, these apply between Finland and Sweden, replacing the Convention. In respect of Denmark, Norway and Iceland, Art 44.3a of the Regulation states that the Regulation does not apply in any Member Sate, to the extent that it is irreconcilable with the obligations arising in relation to bankruptcy from i.a the Convention. In respect of Denmark, it is not unlikely that Denmark in the end choose to join/enter into the Regulation, nor is it impossible that also Norway and Iceland, in the long run, would enter into the Regulation in its capacity as EEA-States.

4. CASE-LAW AND PRACTICE

As stated above, we only know about a few cases in higher courts in which the Regulation has been applied. All these cases deal with Art. 3.1 of the Regulation and have been relatively uncomplicated. Thus, the Court of Appeal has had no reason to go into detail and develop guidelines on how to apply Art. 3.1 or the Regulation as a whole.

In October 2002 the Svea Court of Appeal dealt with an application for bankruptcy in respect of an individual. The applicant creditor claimed that there were several circumstances, such as certain assets, that proved that the debtor had his habitual residence in Sweden despite the fact that the debtor had stated that his home address was in Spain and that he, according to the Swedish Registrar's Office, was registered as emigrated to Spain. The Court of Appeal initially pointed out that according to the Regulation the debtor's centre of main interest must be within the European Union. This was no problem since the individual in the case at hand had his centre of main interest in either Spain or Sweden. The Court further considered that in order for a Swedish court to have jurisdiction to open insolvency proceedings, the individual must, according to Art. 3 of the Regulation have its centre of main interest or an establishment in Sweden. Since it was not clear whether the individual had its centre of main interest or an establishment in Sweden, the application was dismissed.

Even though no references were made to the case, criticism has been levelled against a situation were individuals, vagabonding in Europe and who cannot be proved to have a centre of main interest or an establishment in a certain Member State, may not be declared in bankruptcy, thus escaping from inter alia tax debts.

An example of the latter situation is maybe illustrated by another case, again from the Svea Court of Appeal and again with the jurisdiction issue in focus.[7] The debtor was a natural person that had emigrated to Spain and was domiciled in that Member State pursuant to Swedish National Registration. He did neither have any assets nor any incomes in Sweden,

[7] Svea Court of Appeal, decision 2004-01-20, case no. Ö 9175-03

which involved the District Court to declare itself non-competent to try the case.[8] The Court of Appeal rejected the applicant's appeal on the same ground as the District Court had done.

The outcome of this last case must be considered fully consistent with the Regulation. Yet it might be questioned if the consequences of the court's decision serve the purpose of the Regulation. The argumentation the applicant (a Swedish insurance company) brought forward was not based upon the wording of the Regulation but rather upon pragmatic reasons. As the debtor had escaped Sweden, the insurance company saw no other possibilities to recover its debts than to appoint a liquidator with faculties to conduct a thorough investigation of the debtor's activities. From the company's point of view it may appear a nuisance having to go on with the case to courts across Europe (e.g. in this case, to Spain).

The Svea Court of Appeal has addressed a similar jurisdictional problem, i.e. the interpretation of Art. 3.1 of the Regulation, in a case regarding a Finnish limited liability company.[9] The issue the Court had to give an answer to, was whether a Swedish court had jurisdiction to open insolvency proceedings against the limited liability company in spite of the fact that the company had its registered office in Finland. The facts of the case indicated that the company neither did carry out business in Finland nor were there any assets situated in that jurisdiction even though one debt was related to Finland. The Swedish business was being wound up but still there were some contractual works in progress. The Court of Appeal ruled, by contrast with the District Court, that it had been demonstrated that the centre of the debtor's main interest was situated within the territory of Sweden (thus breaking the presumption of Art. 3.1), consequently remitting the case back to the District Court for retrial.

It might appear considerations as to avoid an unnecessary complicated situation have conduced to the outcome of the latter case.[10]

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[8] The District Court had prior to its decision ordered the applicant to compliment his petition in respect of the Court's potential lack of jurisdiction. According to the supplementary provisions proposed, the applicant will have a general obligation to prove that (and on what basis) the Court has jurisdiction pursuant to the Regulation.

[9] Svea Court of Appeal, decision 2003-05-30, case no. Ö 4105-03.

[10] This approach seems to be characterized by a relatively generous interpretation of Art 3.1 to home state interests which is not entirely problem-free as it might provoke a "race" between the creditors in cases where the creditors are anxious for the insolvency proceedings to be opened in their home state, thus preventing courts in other Member States from opening the same form of proceedings.

In another case at Skåne and Blekinge Court of Appeal an English limited liability company was declared bankrupt in January 2005.[11] The court found that the company had its centre of main interest within the territory of Sweden due to the fact that its actual business was carried out in Sweden. The company was a limited partner to a Swedish limited partnership and it was the limited partnership which produced the income to the limited liability company. Furthermore the limited liability company was liable to tax in Sweden.

Also in January 2005 an English limited liability company was declared bankrupt by the District Court of Stockholm.[12] At same time proceedings had been opened in United Kingdom, a "Creditors voluntary winding up". The court which established that the company had its centre of main interest within the territory of Sweden did not mention these proceedings in its findings. It seems that the proceedings in United Kingdom not were seen as such which the Regulation refers to. The applicant had regarding this question pointed to the fact that the proceedings were voluntary, not registered at the courts and there was no change to the deputies of the company.

More recently a similar question was addressed by the District Court of Stockholm which declared a Swedish limited liability company bankrupt at the same time as a judgement from a district court in Estonia had been appealed against.[13] The Swedish court stated that district court in Estonia had passed a judgement according to which a bankruptcy proceeding in Estonia had ended and that the decision was put into effect directly. In the light of these facts the Swedish court decided that there was no ongoing insolvency proceeding in Estonia and that there had been no evidence that the centre of main interest of the company was outside of Sweden. The cased is now appealed and the Svea Court of Appeal is now (29 April 2005) evaluating the case.

An interesting bankruptcy, in which one of our colleagues at Setterwalls was appointed bankruptcy trustee in May 2002, is the bankruptcy of Insurance Company Folksam International (the largest Swedish bankruptcy ever). The company had its registered office as well as its centre of main interests situated in Sweden but also had a branch and a subsidiary in the UK and conducted a substantial part of its business in other European

[11] Skåne and Blekinge Court of Appeal, decision 2005-02-03, case no. Ö 21-05.
[12] District Court of Stockholm, decision 2005-01-21, case no. K 17664-04

states. At the time of the opening of the insolvency proceedings, the Regulation had still not come into force, which prevented the Regulation from being directly applicable.

Due to the lack of any common rules regarding cross boarder insolvency, it was claimed, at least to a certain degree, that the Swedish bankruptcy proceedings should not cover the assets within the UK territory. The Swedish bankruptcy trustee on the other hand was of the opinion that this would be the case and that the Swedish bankruptcy would cover all assets, despite their location and put forward the then forthcoming Regulation as an argument for his position. After negotiations, the UK creditors and the provisional liquidator in the UK (of the UK subsidiary in liquidation) entered into an agreement, agreeing with the Swedish bankruptcy trustee. The English court subsequently based its decision on this agreement.

An observation – perhaps without due nuances – from the Swedish bankruptcy trustee and his team after a couple of years is that, especially in the UK, national interests have been asserted which has rendered it difficult to get in control of the business. Also in France, funds have been blocked by French bank Credit Commercial Francaise. The bank has required that the bankruptcy is approved by a French court before payment can be effected, which has led to a court procedure, expected to take approximately one year.

[13] The District Court of Stockholm, decision 2005-03-24, case no. K 6276-05.