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## *Addressing the Reform of the European Insolvency Regulation: Wishlists or Fancies?*

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# **Addressing the Reform of the European Insolvency Regulation: Wishlists or Fancies?**

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## *Introduction*

The European Regulation on Insolvency Proceedings 2000<sup>1</sup> is the successor text to the European Insolvency Convention 1995. It is the result of a project nearly four decades long in the making and forms part of an overall jurisdiction, recognition and enforcement allocation initiative that also brought into being the Brussels Convention 1968.<sup>2</sup> The history of the project included a number of drafts whose remit moved gradually away from including elements of substantive harmonisation towards simple procedural harmonisation and choice of laws. There were a number of false starts, including the suspension of work after a failure to reach a consensus on a second draft in 1985, reversed following the initiation of a rival project by the Council of Europe which saw the conclusion of the Istanbul Convention 1990.<sup>3</sup> Although the Council of Ministers approved the text that became the European Insolvency Convention 1995, it did not enter into force because the United Kingdom failed to adhere within the time period open for signature.<sup>4</sup> Following a proposal co-authored by Germany and Finland in 1999, the Insolvency Regulation revived this project without major amendment to its provisions and the text entered directly into force on 31 May 2002 in all of the member states in the European Union subject to Title IV of the EC Treaty, then fourteen in number (Denmark being excluded as it had secured opt-out provisions during negotiations for the Treaty of Maastricht). As part of preparations for the European Union being joined by 10 new member states on 1 May 2004, the Insolvency Regulation was amended by the relevant Act of Accession, signed on 23 September 2003, with effect from the date of accession. There have also been some updating amendments to the lists of insolvency proceedings and officials in the annexes to the Insolvency Regulation.<sup>5</sup> It is likely there will be further amendments consequent on the Act of Accession, signed on 25 April 2005, providing for the accession of Romania and Bulgaria to the European Union on 1 January 2007.

## *Reform Challenges*

Since the enactment of the Insolvency Regulation, there have been calls for reforms to the text. Some of the relevant issues were raised in a 2005 conference paper authored by Gabriel Moss QC and Professor Christoph

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<sup>1</sup>Council Regulation (EC) No. 1346/2000 of 29 May 2000 ('Insolvency Regulation').

<sup>2</sup>Now superseded by Council Regulation (EC) No. 44/2001 of 22 December 2000.

<sup>3</sup>Owing to insufficient ratifications, this convention remains without force.

<sup>4</sup>See I. Fletcher, *The European Community Convention on Insolvency Proceedings: An Overview and Comment, with US Interest in Mind* (1997) 23 BJIL 25.

<sup>5</sup>Council Regulation (EC) No. 603/2005 of 12 April 2005 and Council Regulation (EC) No. 694/2006 of 27 April 2006.

Paulus and published in this journal in early 2006.<sup>6</sup> This paper dealt with concerns surrounding the definition of the 'centre of main interests', the phenomenon of forum shopping through debtors moving prior to the initiation of proceedings as well as the race to court highlighted by decisions such as *Eurofood*.<sup>7</sup> It also noted other related issues such as a possible framework for court-to-court communications, whether there should be a central register of insolvency judgments, perhaps together with publication through an official website, as well as difficulties attendant on the amendment process. The paper also questioned whether a special regime or default presumption for corporate groups should be created and the consequent impact on prospects for corporate rescue through the Insolvency Regulation by the maintenance of the limitation to winding up procedures in the case of secondary proceedings. A number of cogent points were made in the article, some of which have also been addressed by other authors,<sup>8</sup> explaining why reforms may be necessary. Many of these could usefully be taken on board during any amendments that may be made as the Insolvency Regulation is reviewed, a process to which the authors say consideration is already being given.<sup>9</sup>

### *More Reform Challenges*

Although it is not the purpose of this piece to respond directly to the Moss-Paulus paper, there are other issues that would merit consideration were reforms to be initiated that are germane to concerns raised in that paper. These include the issue of priorities and the possible interference of doctrines of public policy, the use of avoidance strategies aimed at preventing the proliferation of proceedings as well as the overall relationship of the Insolvency Regulation to other international instruments regulating cross-border insolvency, in particular the UNCITRAL Model Law on Cross-Border Insolvency 1997.<sup>10</sup>

#### (i) Priorities and Public Policy Issues<sup>11</sup>

The basic principle in the Insolvency Regulation is that the rules governing the admission and content of claims, the special position of debts arising after the institution of insolvency proceedings as well as proof and verification of all these claims are all matters for the substantive law of the jurisdiction where proceedings are opened (the *lex concursus* principle).<sup>12</sup> Similarly, the same substantive law also governs the distribution of proceeds when assets are

<sup>6</sup>G. Moss and C. Paulus, *The European Insolvency Regulation - The Case for Urgent Reform* (2006) 19 *Insolv Int* 1.

<sup>7</sup>*Eurofood IFSC Limited* (Case C341/04) (ECJ judgment of 2 May 2006).

<sup>8</sup>See R. Van Galen, *The Insolvency Regulation and Groups of Companies*, INSOL Europe 2003 Conference paper, copy available through the International Insolvency Institute website at: <[www.iiiglobal.org/country/european\\_union/Cork\\_paper.pdf](http://www.iiiglobal.org/country/european_union/Cork_paper.pdf)> (last viewed 11 August 2006).

<sup>9</sup>Moss and Paulus, *op. cit.* at 1.

<sup>10</sup>Model Law.

<sup>11</sup>An expanded version of this section appears in P. Omar, *Confronting the Challenge of Diverse Priority Rules through the Insolvency Regulation*, *International Case-Law Alert* No. 10 (June 2006) 7-9, to be made available through the EIR-Database website at: <[www.eir-database.com/caselaw\\_alerts.asp](http://www.eir-database.com/caselaw_alerts.asp)> (last viewed 11 August 2006).

<sup>12</sup>Article 4(2)(g)-(i), Insolvency Regulation.

realised, the ranking of claims as well as the rights of creditors who have obtained partial satisfaction after insolvency proceedings are opened (for example through the use of quasi-security). Because the Insolvency Regulation paradigm allows for the possibility of multiple proceedings subject to the threshold test of an 'establishment' existing in the case of secondary or territorial proceedings,<sup>13</sup> the possibility of multiple proceedings each governed by a separate priority rule is a natural consequence, especially as the text applies the law of the secondary jurisdiction to the same issues arising in those proceedings.<sup>14</sup> This position is complicated by the fact that the *pari passu* principle, providing for the equal treatment of creditors, is stressed as a pre-eminent principle governing the Insolvency Regulation. The text states clearly that all creditors, wherever domiciled in the European Union, have the right to assert their individual claims in any of the insolvency proceedings that may be pending in relation to their debtor.<sup>15</sup> This is reinforced by the provision permitting all creditors situated in member states the right to lodge their claims in writing in any proceedings taking place elsewhere.<sup>16</sup> The principle is further underlined by the requirement for the liquidator in any proceedings to inform known creditors resident elsewhere within the European Union, while the facility for publishing notice of the existence of proceedings serves to inform creditors of the need to exercise their rights.<sup>17</sup> There are issues here, however, as Moss and Paulus point out, given the absence of a central register of judgments or any means of official publication, by which notice could be given of the existence of proceedings in parallel.<sup>18</sup>

The possibility of multiple claims, however, does not mean that the diligent are rewarded any more than other creditors. In order to ensure the equal treatment of creditors, there is an attempt to co-ordinate the overall distribution of proceeds by requiring creditors to account for dividends received in other proceedings. The 'imputation' or 'hotchpotch' rule contained in the Insolvency Regulation states that creditors may only participate in the distribution of total assets in other proceedings if creditors with the same standing have obtained the same proportion of their claims.<sup>19</sup> Furthermore, the liquidator may also require a creditor to repay into a central fund any sum obtained as a result of enforcement measures in another country, subject to any *in rem* rights and quasi-security, such as reservation of title clauses.<sup>20</sup> The preservation of overall parity where multiple proceedings are opened is also effected by permitting liquidators to resubmit claims they have received in other proceedings, subject to the interests of other creditors being maintained.<sup>21</sup> Underlining this, creditors retain the right to object to the admission of claims, and the claimant itself is able to withdraw the application. The availability of funds from one set of proceedings for the satisfaction of creditors elsewhere is also a possibility given that the Insolvency Regulation

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<sup>13</sup>Ibid., Article 3(2).

<sup>14</sup>Ibid., Article 28.

<sup>15</sup>Ibid., Article 32(1).

<sup>16</sup>Ibid., Article 39.

<sup>17</sup>Ibid., Articles 40(1) and 21(1) respectively.

<sup>18</sup>Moss and Paulus, *op. cit.* at 4.

<sup>19</sup>Article 20(2), Insolvency Regulation.

<sup>20</sup>Ibid., Article 20(1).

<sup>21</sup>Ibid., Article 32(2).

authorises the transfer of surpluses from secondary proceedings for the benefit of creditors in main proceedings.<sup>22</sup>

The problem, however, arises, where the diligent or astute creditor, taking advantage of the disparity in priority rules, seizes the opportunity to which they are entitled to submit their claim in another jurisdiction, where their claim would be given a higher priority and stand a better chance of being the subject of a distribution. With the type of 'cross-priority' provided through the framework in the Insolvency Regulation, the creditor could 'promote' themselves because the priority rule in that jurisdiction would apply to their 'foreign' claim just as it would to a 'local' claim.<sup>23</sup> It is unlikely the converse would apply and a creditor choose to apply to a jurisdiction where their priority is 'demoted', unless substantial assets existed there that were likely to result in distributions further down the 'food chain'. Even allowing for the imputation rule, it would be cost-effective for any creditor in the position of being able to 'promote' itself to do so where the likelihood of a distribution in its home jurisdiction is low. The paradox is that this might confer an advantage on state creditors in those jurisdictions that have removed the preferential status accorded to these debts, but would inevitably benefit many other creditors, given the continuing diversity in domestic priority provisions. Under this system, the chances of the imputation rule applying to the distribution received in proceedings where the creditor is favoured is lessened, although not wholly avoided. The absence of a 'consolidated proportion survey', suggested in earlier proposals, which would have imposed a requirement for courts to record the tally of distributions in parallel proceedings, adds to the possibility that the shrewd creditor might avoid an account altogether unless the liquidators in multiple proceedings make use of the co-operation and communications provisions in the text to keep a tally of overall distributions. The issue of co-operation and communication is one that Moss and Paulus also raise and in particular the apparent lack of such a tradition in civil law countries.<sup>24</sup> Issues surrounding notice are also present here and whether the absence of a central judgments register or website will impede the awareness of liquidators of the need to communicate.

There is, however, a further problem. The possibility that disparate priority rules lead to the unequal treatment of creditors may well invite judicial intervention and the application of the Article 26 rule, which constitutes the public policy exception to the automatic recognition and enforcement provisions of the Insolvency Regulation. In fact, in *Re: MG Rover España SA*,<sup>25</sup> the possibility that recognition of main proceedings would fall foul of public policy in other member states was very much a concern. The fear was that if public policy were invoked to deny recognition of the British court order, this would lead inevitably to the opening of separate secondary proceedings

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<sup>22</sup>Ibid., Article 35.

<sup>23</sup>See Professor Jay Westbrook, 'Universal Priorities' (1998) 33 Texas International Law Journal 27.

<sup>24</sup>Moss and Paulus, op. cit. at 4.

<sup>25</sup>*Re: MG Rover España SA and others* (Norris J, 11 May 2005, Chancery Division, High Court: Birmingham District Registry), reported by E. Springford in (2005) 21 Insolvency Law and Practice 91.

and the probable loss of synergy for co-ordinated rescue to take place. The trial judge accepted this as good grounds to empower the administrators with the discretion to carry out a distribution that took account of the special position of employees in the other jurisdictions involved. The same provision has also been cited in the context of proceedings, albeit involving an Australian insurance company,<sup>26</sup> where the trial judge, Mr Justice Richards, held *obiter* that the Insolvency Regulation does not oblige the liquidator in secondary proceedings to comply with the requirement to transfer funds to main proceedings under Article 35, where the priority rules on distribution would be so different as to trigger a possible offence to a court's view of the *pari passu* principle. This would seem to militate for an assessment of whether a co-ordinated set of priority rules may be necessary as part of an overall review of the Insolvency Regulation. There will be difficulties here, of course, given that priority rules are part of the general *lex concursus* rule in Article 4, from which the specific carve-outs in Articles 5-15 are seen as important, but limited, exceptions. The harmonisation of priority rules would create another exception, this time in favour of a European rule, but might be unacceptable to those who do not see the remit of the Insolvency Regulation as extending into the area of substantive harmonisation.

#### (ii) Avoidance Strategies: Short-Circuiting the Insolvency Regulation

The decision in *Re: MG Rover España SA* also illustrates that synergy may be obtained, so as to enable the co-ordination of rescue across a group of companies, through the avoidance of secondary proceedings being opened. In part, this reflects concerns about the limitation of secondary proceedings to winding up ones, a position shared by Moss and Paulus.<sup>27</sup> Furthermore, present in the literature from an early date has been the concern that this provision may artificially limit the scope for rescue and result in rescue being dependent on the fortuitous location of proceedings,<sup>28</sup> leading to possible forum shopping measures and a race to the court seen as providing the most beneficial outcome, factors also highlighted by Moss and Paulus.<sup>29</sup> To this must be added the complication stemming from the absence of a special rule for groups of companies, leading to the (some say) inevitable competition for jurisdiction. The European Court of Justice has answered some of the arguments surrounding the competition between courts in its judgment in *Eurofood* by emphasising firstly, the strength of the presumption in Article 3(1) in favour of the registered office of corporate debtor, a presumption that may only be departed from in the presence of strong evidence,<sup>30</sup> and, secondly, the mutual trust aspect of the text, inherent in Article 16, by which courts must recognise judgments emanating from courts that have declared themselves competent to hear matters.<sup>31</sup> This serves to render a little more clearly the conditions in which the text is to apply and indirectly assists the determination

<sup>26</sup>*Re: HIH Casualty and General Insurance Limited and Others* [2005] EWHC 2125 (Ch) (7 October 2005).

<sup>27</sup>Moss and Paulus, *op. cit.* at 5.

<sup>28</sup>See G. Johnson, *The European Union Convention on Insolvency Proceedings: A Critique of the Convention's Corporate Rescue Paradigm* (1996) 5 IIR 80.

<sup>29</sup>Moss and Paulus, *op. cit.* at 3-4.

<sup>30</sup>At paragraph 37.

<sup>31</sup>At paragraphs 39-41.

of the 'centre of main interests' in the case of companies that are members of corporate groups. However, what the judgment means is that there cannot be jurisdiction on a group-wide basis unless and until the presumption is rebutted in the case of subsidiaries, usually in circumstances akin to how the doctrine of 'substantive consolidation' is employed in American law.<sup>32</sup> This would definitely have an effect on cross-border rescue initiatives and may well impede the organisation of rescue where viable units are constituted of elements present in a number of jurisdictions.

In this light, it is not surprising that cases such as *Re: MG Rover España SA* have shown the way towards achieving the effect of 'substantive consolidation' without necessarily displacing the presumption of jurisdiction. The recent decision of the High Court in *Re: Collins & Aikman Europe SA*<sup>33</sup> seems to permit consideration of the putative rights of foreign creditors according to the national law applicable to them in the context of distributions conducted as part of main proceedings, which incidentally have the effect of avoiding secondary proceedings from being opened. The decision is described as a 'valuable judgment which instils confidence' that the Insolvency Regulation is 'capable of operating in an efficient and pragmatic way and achieving advantageous outcomes in international insolvencies'.<sup>34</sup> As the judgment states, the group was a supplier of automotive components, whose European operations consisted of 24 companies located in 10 different countries.<sup>35</sup> When companies in the group filed for Chapter 11 protection in the United States, financial pressures soon became apparent, affecting the European members of the group. The European companies, including trading companies located in England and Wales, Spain, Sweden, Germany, Belgium, Italy and the Netherlands, lodged petitions for administration in England and Wales, which were granted on the High Court being satisfied on the evidence presented to it that main proceedings as defined in Article 3 of the Insolvency Regulation were possible and appropriate.<sup>36</sup> When the administrators that were appointed considered the affairs of the companies, the conclusion reached was that the companies formed an inter-connected group with operational functions being administered on a Europe-wide basis. For this pre-eminent reason, consideration was given to how the continuation of the business could be co-ordinated and the disposal of the business and assets could be organised to maximise the benefit to and possible return for creditors.<sup>37</sup>

It became apparent to the administrators that a Europe-wide strategy was at risk from creditors using Insolvency Regulation provisions to initiate secondary proceedings in various countries where group companies were located, provided, of course, that the threshold test for an establishment was met. Given that a number of the companies potentially met this criterion, the result could have been to put into jeopardy the continued trading of the businesses

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<sup>32</sup>Van Galen, op. cit. at 14.

<sup>33</sup>*Re: Collins & Aikman Europe SA and others* [2006] EWHC 1343 (Ch) (9 June 2006).

<sup>34</sup>Insolvency Lawyers Association Technical Bulletin (July 2006) at 1.

<sup>35</sup>At paragraph 4.

<sup>36</sup>At paragraphs 5-6.

<sup>37</sup>At paragraph 8.

and the conduct of sales on a group-wide basis. To forestall the possibility of proceedings proliferating, the administrators provided assurances to individual creditors and creditors committees at meetings held across Europe that local priority rules would be respected as far as possible within the proceedings ongoing in England and Wales, provided that no secondary proceedings were opened. The measure of the success of the strategy taken can be seen in the fact that in only three minor instances were secondary proceedings initiated.<sup>38</sup> The general reliance creditors placed on the promises and support for the group-wide strategy was amply borne out by the result which achieved an increased USD 45 million worth over the estimates that had been received, ultimately providing a pot of about USD 125 million for distribution.<sup>39</sup> The instant case centred around the issue of confirming the jurisdiction for the assurances made by the administrator, strengthened by advice received on the point, particularly since the priority rules in the majority of cases would be substantially different from the usual under an application of the *lex concursus* rule.<sup>40</sup>

Following further consultation of the creditors and the absence of dissent, the court was persuaded to accept arguments that grounded jurisdiction on a number of bases, including the rule in *Ex Parte James*,<sup>41</sup> which permitted administrators to honour assurances given in the financial interests of the companies concerned, the inherent jurisdiction of the court to control the actions of its officers<sup>42</sup> as well as the specific authority of statutory provisions such as paragraphs 3(1)(a) and 3(1)(b) of Schedule B1 to the Insolvency Act 1986 setting rescue as a priority and paragraphs 65 and 66 authorising a distribution at variance with ordinary rules with either the permission of the court or if for the purpose of better achieving the purpose of the administration.<sup>43</sup> Jurisdiction having been asserted, the issue of whether the court should exercise discretion to permit the assurances to be honoured was raised. The administrators correctly pointed out that the fact the assurances had been given meant that secondary proceedings were largely avoided, a factor which avoided the significant disadvantage which would have arisen because of further expense and delay while these proceedings took place.<sup>44</sup> The court also accepted that injustice could be caused to creditors in other jurisdictions given they had not pursued claims on the basis of these assurances and, were these assurances to be repudiated, would suffer injustice by having to resort to litigation where assets had already been liquidated or sold on.<sup>45</sup> Despite there being some detriment to a small group of North American creditors who would receive less because of the use of priority rules other than English and Welsh ones,<sup>46</sup> the court concluded that the administrators' proposals would lead to the greatest advantage for the greatest number and sanctioned it on this basis. The interest of this judgment

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<sup>38</sup>At paragraph 11.

<sup>39</sup>At paragraph 9.

<sup>40</sup>At paragraph 10.

<sup>41</sup>At paragraphs 15-17, citing *Re Condon, ex parte James* (1874) LR 9 Ch App 609.

<sup>42</sup>At paragraphs 18-20, 37-40.

<sup>43</sup>At paragraphs 21-36.

<sup>44</sup>At paragraphs 42-48.

<sup>45</sup>At paragraph 9.

<sup>46</sup>At paragraph 49.

is that it illustrates clearly a very pragmatic method by which rescue can be coordinated, but which relies for its success on the avoidance of secondary proceedings taking place. The issue is, of course, whether, were the bar on rescue procedures in secondary proceedings to be lifted as Moss and Paulus suggest,<sup>47</sup> secondary proceedings would continue to be avoided on the grounds of costs and delay occasioned by the proliferation of proceedings.

### (iii) Extra-Territorial Application and Potential Conflicts<sup>48</sup>

The decision in *Re: Collins & Aikman Europe SA* also illustrates a phenomenon that has been apparent from an early stage following the implementation of the Insolvency Regulation, that of its potential extra-territorial application. The assumption behind the Insolvency Regulation is that it has uniquely an intra-Community effect and the text is to apply only where the centre of the debtor's main interests is within the European Union.<sup>49</sup> However, the general jurisdictional contest that occurred in the period following the implementation of the Insolvency Regulation included a number of cases involving the European activities of a group whose parent company was established elsewhere. *Re: Brac*<sup>50</sup> involved a company formed in Delaware and trading as an overseas company in the United Kingdom, where the operations were largely conducted and where the majority of employees were based. The company had been placed under the protection of Chapter 11 proceedings in the United States. In order to make an administration order, which was felt to be desirable, and in the absence of specific authority under the section 426 of the Insolvency Act 1986, which does not apply to the United States, Mr Justice Lloyd was obliged to consider whether the paradigm in the Insolvency Regulation dealing with the exercise of jurisdiction as between member states could be applied by analogy to the position of a debtor incorporated outside the European Union, where its centre of main interests was clearly within a member state. The argument to the contrary relied on the proposition that European legislation should not be presumed to apply to entities incorporated overseas without express mention. Although the potential for an extra-territorial effect was not dealt with expressly in the Virgos-Schmit Report, the judge held that the commentary and Insolvency Regulation were neutral on the point and accepted that they were not inconsistent with the argument put forward for jurisdiction. This argument relied on the fact that the only test in the Insolvency Regulation for jurisdiction referred to the centre of main interests and that the absence of a specific exclusion for debtors formed outside the European Union tended strongly towards a presumption allowing

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<sup>47</sup>Moss and Paulus, op. cit at 5.

<sup>48</sup>A considerably expanded version of this section and further argument on the relationship of both the Insolvency Regulation and the Model Law with section 426, Insolvency Act 1986 appears as P. Omar, Cross-Border Insolvency in the United Kingdom: An Embarrassment of Riches (2006) 22 IL&P (forthcoming).

<sup>49</sup>Recital 14 and Article 3(1), Insolvency Regulation. See also the Virgos-Schmit Report at paragraph 310. Although the report was issued to accompany the European Insolvency Convention text, it is often referred to as an interpretative guide for the terms of the Insolvency Regulation, its status as an extrinsic aid to construction being confirmed by Advocate-General Jacob's Opinion of 27 September 2005 in *Eurofood IFSC Limited* (Case C341/04) at paragraph 2.

<sup>50</sup>*Re: Brac Rent-A-Car International Inc.* [2003] EWHC 128 (Ch) (7 February 2003).

for jurisdiction to be exercised. A similar case, *Re: Daisytek-ISA*, involving a parent company located in the United States which had filed for Chapter 11 protection, featured an English court granting administration orders in respect of its English subsidiary, as well as other English and European companies, located in France and Germany, on grounds that the English company was not only the holding company for the European operations of the group but also provided management support and co-ordination of the group's activities.<sup>51</sup> In this light, cases such as *Re: Collins & Aikman Europe SA* are not so different, given that the financial difficulties of American members of the group impelled the opening of proceedings governing the European end of operations. What results from cases like these is the feeling that the fortuitous location of incorporation should not prevent the exercise of jurisdiction and the exercise of jurisdiction by (predominantly) English and Welsh courts has avoided the development of what could have been a serious lacuna in the Insolvency Regulation. However, the extra-territorial application by default of the Insolvency Regulation carries the risk that this text may come into conflict with other arrangements in existence governing cross-border insolvency and, in particular, the Model Law.<sup>52</sup>

The relationship between the Insolvency Regulation and other texts is expressed in its provisions and, normally, the Insolvency Regulation will not apply to the extent it would be incompatible with external obligations entered into by a member state with a country outside the European Union before it came into force.<sup>53</sup> A special mention is also given for the position of the United Kingdom insofar as arrangements with other Commonwealth countries are to remain similarly unaffected, a provision which refers implicitly to the paradigm in section 426 of the Insolvency Act 1986.<sup>54</sup> Although the wording of the text refers to existing obligations, a declaration by the European Council has provided that the Insolvency Regulation is not intended to prevent member states from concluding agreements with other countries on the same subject matter, provided the other agreement does not affect the operation of the Insolvency Regulation.<sup>55</sup> Professor Virgos, co-author of the Virgos-Schmit Report, suggests that the declaration was issued to 'prevent any misunderstanding' following the 'communitarisation' of insolvency law in this way, although he advises that member states should avoid entering into arrangements that could 'jeopardise the uniformity' of the Insolvency Regulation and that judges should expressly refrain from applying any existing text where it may be incompatible in any way.<sup>56</sup> In this light, the growing popularity of the Model Law, which has been adopted or stands to be adopted by a number of states with which European Union countries have major trading links,<sup>57</sup> may prompt European Union member states to consider its

<sup>51</sup> *Re: Daisytek-ISA Limited and others* [2003] BCC 562.

<sup>52</sup> See P. Omar, *The UNCITRAL Insolvency Initiative: A Five-Year Review* [2002] 6 *Insolv L* 228.

<sup>53</sup> Article 44(3)(a), Insolvency Regulation.

<sup>54</sup> *Ibid.*, Article 44(3)(b).

<sup>55</sup> Council Declaration 2000/C 183/02.

<sup>56</sup> See M. Virgos and F. Garcimartin, *The Insolvency Regulation: Law and Practice* (2004, Kluwer Law International, The Hague) at paragraph 41.

<sup>57</sup> Existing adherents include Japan, Mexico, the United States and South Africa. They are likely to be joined shortly by Canada, Australia and New Zealand.

use. However, at present, apart from the United Kingdom,<sup>58</sup> the only European Union member state to have adopted the Model Law is Poland, although it will be joined by Romania when the latter accedes on 1 January 2007.<sup>59</sup>

There will not necessarily be any conflict between the texts where the issue is the conduct of purely intra-Community insolvencies. Because the Model Law is designed to be adopted as part of the domestic legal order, Article 10 of the EC Treaty, which requires member states to take all possible measures to ensure fulfilment of the obligations they have entered into under the treaty, confirms the paramount status of European legal instruments over domestic ones. There is consequently no need to make an express stipulation in the adopting instrument to this end, although, in the United Kingdom, the primacy of the European text has been mentioned in the statutory instrument incorporating the Model Law.<sup>60</sup> It is possible, however, for a conflicting view to be taken. Although the Model Law is designed to be implemented as a domestic legal text, it nevertheless resorts from work carried out at the international level and the consensus achieved by UNCITRAL as to its contents. To that extent, the measure may be said to reflect international insolvency law and principles given effect through acceptance into the domestic legal hierarchy in the same way as the Insolvency Regulation represents a consensus at European level of principles that are then given direct and automatic effect through enactment in regulation form. In fact, a reminder of the roots of the Model Law comes in the British text incorporating it and the interpretation clause, which requires 'regard to its international origin and to the need to promote uniformity in its application' with, furthermore, good faith to be observed in its use.<sup>61</sup>

Even for intra-Community insolvencies, the issue may be whether the European text should continue to be paramount if it represents a different consensus to the international text. Professor Virgos agrees that the Model Law represents a 'genuine international standard' in insolvency matters.<sup>62</sup> He is of the view, however, that there is no risk of incompatibility or conflict between the texts given that it is not an international treaty in the strict sense, but a text given effect through domestic law. Furthermore, the observation may be made in comparing the texts that the Model Law bases its jurisdictional paradigm on that in the Insolvency Regulation and to that extent would not be incompatible. This is a view echoed by the Guide to Enactment accompanying the Model Law.<sup>63</sup> In fact, the Guide to Enactment states expressly that it offers European states considering its adoption a 'complementary regime of considerable practical value' of application to their cross-border relations.<sup>64</sup> However, there remain some observable differences between the texts, for example the conflict of laws provisions absent from the

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<sup>58</sup>Implemented on 4 April 2006 by The Cross-Border Insolvency Regulations 2006 ('SI 2006/1030').

<sup>59</sup>Non-member states in Europe also adopting the Model Law include Serbia and Montenegro.

<sup>60</sup>Article 3, Schedule 1, SI 2006/1030.

<sup>61</sup>Ibid., Article 8, Schedule 1.

<sup>62</sup>Virgos and Garcimartin (note 56 above) at paragraph 42.

<sup>63</sup>Guide to Enactment, paragraph 18.

<sup>64</sup>Ibid., paragraph 19.

Model Law and the different formulation of the co-operation paradigm in Article 31 of the Insolvency Regulation and Part IV of the Model Law. Nonetheless, it may be possible for both texts to be used in a complementary way and for both the Insolvency Regulation and Model Law to be used where both confer an advantage in different aspects of proceedings.

Nevertheless, with respect to proceedings involving third countries, the observations made above with respect to the *de facto* extra-territorial operation of the Insolvency Regulation are relevant here. It is conceivable that the co-ordination of a group insolvency begins outside the European Union with the assumption by a court elsewhere of jurisdiction to open main proceedings. This is then accompanied by a request to a European court to initiate non-main<sup>65</sup> proceedings. Although these will be non-main as regards the proceedings outside Europe, they may well be regarded as main proceedings within Europe, particularly where the Insolvency Regulation model is used. As cases such as *Re: Brac and Re: Daisytek-ISA* illustrate, this may offer considerable advantages, especially where business activities of a group are conducted throughout Europe. In this scenario, other proceedings within Europe, where these exist, will be regarded as secondary or territorial proceedings *vis-à-vis* the first European set of proceedings. However, where the European court accepts non-main status, co-ordination between these proceedings and those initiated outside the European Union may be jeopardised by any purported exercise of jurisdiction by a second European court claiming authority to open main proceedings because it deems the centre of the debtor's interests in Europe to lie within its jurisdiction. There would be a straightforward clash here with the issue being to which court the obligation to conduct ancillary proceedings would be owed. Under the Insolvency Regulation, it is likely that the first court will be required to defer to main proceedings initiated elsewhere in Europe. Furthermore, despite the exclusion of Denmark from the territorial scope of the Insolvency Regulation, a similar argument has been made that Denmark would benefit from the '*comitas europaea*' principle (a form of mutual assistance and co-operation) requiring courts in other member states to give effect to Danish decisions (and vice versa) unless there were exceptional reasons for not doing so.<sup>66</sup> The potential here is that even with respect to a country not covered by the Insolvency Regulation, any conflict between a request for assistance by a third country and a decision of a Danish court might have to be adjudged with priority given to the Danish decision. The result could be that co-ordination on a world-wide basis could be frustrated by the opening of European proceedings claiming main jurisdiction.

## Summary

It may seem curious that with the Insolvency Regulation not quite five years in force that the calls for reforms have already started appearing. However, it must be appreciated that the text was a necessary compromise between very divergent views on the conduct of cross-border insolvency. For example, in

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<sup>65</sup>Equivalent to secondary proceedings under the Insolvency Regulation.

<sup>66</sup>See J. Israëï, *European Cross-Border Insolvency Regulation* (2005, Intersentia, Antwerp) at 328.

describing the jurisdictional paradigm in the European Insolvency Convention, Professor Ian Fletcher stated that the pursuit of a pragmatic course between territoriality and universality brought about an acceptable compromise in order to limit the multiplicity of proceedings.<sup>67</sup> Deficiencies in the text have naturally appeared, brought to light by the 150 or so cases decided since its implementation, and the effluxion of time has brought about an appreciation of lacunae in the text as a result of observations of its workings in practice. Quite how far any reforms should go is, however, debatable. Moss and Paulus steer a course between definitional changes and radical rewriting of the terms of the Insolvency Regulation. Clarification of some definitional points, such as what should constitute the 'centre of main interests', limiting forum-shopping by defining a time limit extending jurisdiction and removing the bar on rescue procedures in secondary proceedings all seem reasonable. A central register with perhaps a website where judgments are openly accessible are practical innovations that should assist co-ordination and co-operation. More contentious perhaps is whether there should be a presumption for corporate groups, while a framework for communications and co-operation, if adopted, may take time to enter into common usage.<sup>68</sup>

What is revealed by the issues debated in this article is the potential for reforms to go further, with many issues based upon the 'simple' ones outlined by Moss and Paulus seemingly good candidates for consideration in the context of any revision of the Insolvency Regulation. In relation to some issues, such as those surrounding priorities, further extension of the remit of the text into substantive harmonisation may be unacceptable to member states until such time as there is sufficient convergence between domestic legal regimes to make harmonisation a realistic prospect. In terms of the scope of the Insolvency Regulation and its potential extra-territorial effect, the capacity for resolution may lie in the way both it and the Model Law are used and interpreted by the courts. Thus a reform addressing any definition of the scope may be superfluous and raise further difficult issues of interpretation. What gives hope, however, that the Insolvency Regulation may yet prove a success, even in an unamended form, is the pragmatic course steered by insolvency practitioners and judges in the cases outlined above, where any lacunae or deficiencies are resolved by using the provisions creatively. If this continues to be the case, then reforms may not be entirely necessary and revisiting the text may be limited to the more immediate problems, thus avoiding an in-depth revision that could raise the spectre of dissension and disagreement. The nearly forty years it took for the Insolvency Regulation to be produced should, in this regard, serve as a warning of the perils of undertaking too ambitious a reform project.

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<sup>67</sup>See I. Fletcher, *The European Union Convention on Insolvency Proceedings: Choice-of-Law Provisions* [1998] 33 TILJ 119 at 123-124.

<sup>68</sup>The author is aware of an initiative seeking to create a framework using 'soft-law', part of a project sponsored by INSOL-Europe and headed by Professor Bob Wessels.