The Insolvency Exception in the Brussels Convention and the Definition of “Analogous Proceedings”

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Introduction

The European Insolvency Regulation1 is the result of a project nearly four decades long in the making. The beginnings of the project has its roots in the context of work supplementing the European Treaty framework as part of the intention behind the creation of a common legal system following the foundation of the European Community (now Union) in 1957. One of the fundamental principles enshrined in the EC Treaty provided that the purpose of the Community was the establishment of a common market.2 This was to be achieved by the creation of an internal market characterised by the abolition of obstacles to the free movement of goods, services, employees and capital.3 These freedoms brought in their wake the need for the settlement of disputes and for the availability of enforcement measures across the Member States of the Community so as to remove structural impediments to the free flow of commerce and the creation of an internal market between all Member States.

The extension of the framework of the EC Treaty to achieve the purposes of creating an internal market was in certain cases to be effected by further treaties or conventions between the Member States, in particular through developing instruments in the private international arena designed to secure the simplification of formalities governing the reciprocal recognition and enforcement of judgments.4 Most of the initiatives for instruments in this field resulted from the output of working parties set up by the Member States to consider the extension of the treaty, although only a limited number of multilateral conventions were entered into on the basis of this provision. Of these treaties, the most famous is that adopted in 1968 dealing with the recognition and enforcement of judgments in civil and commercial matters, known as the Brussels Convention.5 Other texts produced included some in the areas of patent law, contractual obligations and the recognition of legal entities.

The adoption of the European Insolvency Regulation is also a part of this history as it is the successor text to the European Insolvency Convention 1995, which was intended for adoption under the same private international law initiative. In fact, the 1995 text was only the last in a series 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. This position was only reversed following the initiation of a rival project by the Council of Europe which saw the conclusion of the Istanbul Convention 1990.6 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. Following a proposal co-authored by Germany and Finland in 1999, the European Insolvency Regulation revived the project without major amendment to its provisions and the text entered directly into force on May 31, 2002 in all of the Member States in the European Union subject to Title IV of the EC Treaty,7 then 14 in number.8 As new Member States have joined the European Union, the European Insolvency Regulation has been amended by the relevant Acts of Accession. There have also been a series of regulations updating the lists of insolvency proceedings and officials in the annexes to the European Insolvency Regulation to reflect changes in domestic insolvency law rules.9

The Brussels Convention exception

One of the most important texts of its time in the area of reciprocal recognition and enforcement, the Brussels Convention was expressed as having broad application

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1 Regulation 1346/2000 (European Insolvency Regulation).
2 EC Treaty art.2 (now repealed). The EC Treaty (itself the successor to the EEC Treaty, also called the Treaty of Rome 1957), has now been replaced after the conclusion of the Lisbon Treaty 2007 by the Treaty on the Functioning of the European Union (TFEU). The terminology of the “Common Market” was replaced by the term “Single Market” by the Single European Act 1986.
3 EC Treaty art.3 (now repealed).
4 EC Treaty art.293 (now repealed).
5 Convention on the Mutual Recognition and Enforcement of Judgments of September 27, 1968 (Brussels Convention), which was re-adopted as Regulation 44/2001 (Brussels I Regulation) under art.61 EC Treaty (now art.67(4) TFEU). The Brussels Convention continues to apply to the relations between Denmark and the other Member States as Denmark secured opt-out provisions of a permanent nature during negotiations for the Maastricht Treaty 1992, which meant that it was not bound by certain instruments adopted under Title IV, EC Treaty (in which art.61 was to be found). The UK and Ireland, which secured similar opt-out provisions, retained an opt-in facility and could choose by which instruments to be bound.
6 Owing to insufficient ratifications, this convention also remains without force.
7 On the basis of powers conferred by the Amsterdam Treaty 1997 Title IV introduced an “Area of Freedom, Security and Justice” where the justice element included the mutual recognition of judicial and extra-judicial decisions in civil matters.
8 Excluding Denmark, for the reason outlined in fn.5 above.
in civil and commercial matters, subject to a number of important exclusions, a position replicated in the Brussels I Regulation. These exclusions are in areas dealing with personal law, social security, arbitration and insolvency, the last of which includes in its definition bankruptcy, proceedings relating to the winding up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings. The reason that the Brussels Convention excludes insolvency stems from a decision made early on during preparatory work seeking to define the scope of that convention. As a result, the original working group was divided in 1963 with the formation of a second working group to examine the specific case for a convention in insolvency. This was due to the opinion of a committee of experts that a separate insolvency convention which dealt with the insolvency of both individuals and companies and other bodies seemed to be the only method of achieving harmony in this area of the law. This was fundamentally the reason that led to the hiving off of insolvency matters and ultimately to the proposal for the European Insolvency Convention 1995 that was later replaced by the European Insolvency Regulation.

The precise meaning of the term “analogous proceedings” has led to case law defining the relationship between the Brussels Convention and insolvency law. This has also been a useful exercise in that it also permitted a precise definition of the scope of work aimed at securing an insolvency text to run in parallel with the Brussels Convention. The Jénard Report, which accompanied the Brussels Convention, explained that the term “analogous proceedings” referred to proceedings based on the suspension of payments, the insolvency of the debtor or an inability to raise credit. Furthermore, these proceedings would normally involve the judicial authorities for the purpose of compulsory and collective liquidation of assets or a form of supervision of the debtor. However, what else was covered by the term was to be the subject of case law of the European Court of Justice, which had to consider the extent of the exception in art.1 of the Brussels Convention. The case of Gourdain involved a provision in French law requiring the German director of a holding company to contribute towards reconstituting the assets of an insolvent subsidiary of which he was regarded a de facto manager. This provision, although civil in nature, was regarded as arising out of insolvency proceedings and was thus not amenable to recognition under the Brussels Convention rules as the French court had originally intended and which the German director opposed.

The Opinion of the Advocate General in Gourdain on the definition contained in art.1 of the Brussels Convention is instructive. He regarded the phrase to be understood as having regard to the essential nature of the proceedings taking place with reference to the legal principles applicable in the Member State concerned. In this context, the purpose of the order was to get in assets for the purpose of satisfying the creditors in the insolvency. It thus arose directly from, and was intimately connected with, the insolvency. This line of reasoning has been followed in Germany with respect to the enforcement of a French judgment seeking to order the directors of an insolvent company to pay a certain sum into the assets of the company. However, a commentator on this judgment doubts whether the order is excluded from the Brussels Convention merely because it is ancillary to an insolvency, as the requirement in the Brussels Convention is that the insolvency itself be the subject of the judgment concerned. The analogy might be drawn with the recovery of debts by a liquidator from third Member States, which has also been held to fall outside the exception. Consideration of whether the definition is exhaustive has also occurred in a case where a company in insolvency had commenced claims against its directors for conspiracy and breach of duty and by way of constructive trust. It was held that the insolvency was a purely collateral measure that did not affect the substance of the claim and subsequently it could be enforced under the Brussels Convention. Professor Smart has argued that the cases that have been decided reveal that the nature of the claim, and not the person bringing the proceedings, is more appropriately the decisive factor.

The European Insolvency Regulation position

Reflecting the Brussels Convention and Brussels I Regulation positions, the European Insolvency Regulation also contains a provision in its art.25 dealing with judgments arising out of the insolvency process. Under this, judgments occurring or arising later in the insolvency process given by the same court or any other court concerning its course and closure shall also be recognised.
without further formality according to the provisions of arts 31 to 51 of the Brussels Convention. Various options were in fact canvassed for the recognition scheme for later judgments, the final choice being to use the simplified *exequatur* system under the Brussels Convention. If the judgment is not directly connected with the insolvency proceedings, enforcement will be a matter for the Brussels Convention as a whole, subject to any defences and exceptions contained in that convention. The question of whether a judgment is in fact related is a thorny one, given the art.1(2) of the Brussels Convention exception and the *Gourdain* case. The schematic of art.25 of the European Insolvency Regulation is directly related to the *Gourdain* case and the need to ensure that judgments, irrespective of the originating court, that are closely linked to insolvency proceedings are governed by the European Insolvency Regulation and not the Brussels Convention. For the former to apply, the actions must derive from insolvency law and be closely connected with insolvency proceedings being undertaken, examples being given of actions to set aside and director’s personal liability as in the *Gourdain* case. However, actions deriving from some other law, although affected by the opening of proceedings involving the insolvent debtor, should not be treated as connected with insolvency proceedings and thus should fall out of the scope of the European Insolvency Regulation.

The intention behind art.25 of the European Insolvency Regulation is to avoid cases falling in between the European Insolvency Regulation and the Brussels Convention. However, to draw a boundary is to invite review of that boundary and arguments as to where it is truly drawn. Such has been the experience with the interaction between art.25 of the European Insolvency Regulation and art.1 of the Brussels Convention.

**Drawing boundaries: the case law thus far**

A limited number of cases have intervened to clarify the position of the boundary. This is very probably the effect of the rules on preliminary references to the European Court of Justice, which was limited, under Title IV of the EC Treaty, to issues raised in the context of proceedings occurring before national courts against whose decisions there was no judicial remedy under national law, normally understood to mean decisions not subject to appeal or judicial review. This wording, which also appeared in a similar form in the European Insolvency Convention 1995, limited preliminary references in practice to those from the highest courts in the civil structure in domestic law. This represented a considerable tightening of the bases on which preliminary references could be sought as compared with the Brussels Convention position, but was analogous to the position in the Brussels I Regulation, adopted under the same title. Although the position post-Lisbon appears to be different for all but a limited number of instruments, the number of references has not thus far appeared to increase dramatically as a result of this facility. Nonetheless, the cases, all decided in the course of 2009, invite some comment.

In the first of these, *Deko Marty*,

the facts arose from the insolvency of a German company, Frick Teppichboden Supermärkte GmbH. The German company had, the day prior to an application for the opening of proceedings on March 15, 2002 by the Marburg Local Court, transferred €50,000 to a bank account situated in Düsseldorf held by a Belgian company. The liquidator subsequently made an application to the Marburg Regional Court to set aside the transaction so as to restore the funds to the debtor company’s estate. On the application being dismissed on the basis that the court felt it did not have the international jurisdiction necessary under art.3 of the European Insolvency Regulation to determine the issue, the liquidator filed an appeal on a point of law to the Federal Court of Justice. The Federal Court of Justice stayed proceedings pending a reference to the European Court of Justice on two questions, the first being whether the courts of a Member State opening insolvency proceedings also have international jurisdiction under the terms of the European Insolvency Regulation in respect of an action to set aside a transaction brought against a company whose registered office is in another Member State and, secondly, if the answer to that question was in the negative, whether an action to set aside fell within the exception in art.1(2)(b) of the Brussels I Regulation.

The main consideration for the European Court of Justice was the jurisdictional issue under art.3(1) of the European Insolvency Regulation. For the court, an action to set aside a transaction was inherently an insolvency matter, given that its function was to increase the assets

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22 European Insolvency Regulation art.25(1), which adopts the convention regime apart from art.34(2) on grounds for non-recognition. The convention regime is replicated in arts 38–58 Brussels I Regulation (the equivalent exclusion being in art.45(1)).
24 European Insolvency Regulation art.25(2).
25 See M. Virgos and F. Garcimartin, *The European Insolvency Regulation: Law and Practice* (The Hague: Kluwer Law International, 2004), at para.388, where the authors are of the view the definition includes courts in the same Member State as the insolvency court as well as courts located elsewhere in other Member States.
29 EC Treaty art.234 (now art.267, TFEU).
30 EC Treaty art.68 (now repealed).
31 European Insolvency Convention 1995 art.44.
32 TFEU art.267 authorises all courts to seek preliminary references using permissive language in the case of subordinate courts and mandatory language in the case of courts from which no appeals lie. It seems that a broader (less abstract) approach for reference purposes has been applied to the notion of a court from which no judicial remedy lies.

available for distribution to creditors. Thus, on the precedent of *Gourdain*, the Brussels I Regulation could not apply in the instant case. In deciding this, the court referred to Recital 6 to the European Insolvency Regulation, setting out the principles governing the purpose of the instrument and which limits its use to matters closely connected with the opening of insolvency proceedings. Therefore, art.3(1) of the European Insolvency Regulation, which confers international jurisdiction on courts to determine matters closely connected with proceedings opened in that jurisdiction, must be interpreted consonant with this intention, particularly given the objectives of the text to improve efficiency and effectiveness. This required the concentration of all material matters before one court, so as to lessen the incentive for forum shopping and avoid the prospects of conflict between courts, which factor would undermine the objectives of the text. The court was also motivated by the fact that the recognition principle inherent in arts 16 and 25 of the European Insolvency Regulation requires that a court with international jurisdiction be competent to decide all matters connected with the opening, closure and conduct of proceedings. As a result, the European Court of Justice answered the first question in the reference in the affirmative and confirmed that the court which exercises international jurisdiction was equally competent to determine related matters such as applications to set aside, even if the subject of the application may well be, as in the instant case, a defendant located in another Member State.

In a second case, *SCT Industri*, the liquidator of the company concerned, over which proceedings had been opened before the Malmö District Court in 2003, had sold shares held by the company amounting to a 47 per cent ownership stake in an Austrian company, SCT Hotelbetrieb GmbH, to Alpenblume AB, which was registered in Austria as the owner of those shares. SCT Industri subsequently brought proceedings in Austria in which the Austrian court decided that the Swedish liquidator in fact had no power to effect that transfer and that, consequently, the shares revested in the company. The Austrian court decided this on the basis that the European Insolvency Regulation, which had not entered into force in Sweden at that time, did not apply and that the shares revested in the company. The Austrian court decided this on the basis that the European Insolvency Regulation, which had not entered into force in Sweden at that time, did not apply and that consequently the rules of Austrian private international law were to be used, leading to the determination that Austrian law did not recognise the title of the liquidator to effect a transfer of shares. Alpenblume AB brought proceedings before the Swedish courts for restitution of title to the shares with the District Court and Regional Court of Appeal holding that there was no impediment to the re-transfer occurring. On further appeal to the Supreme Court, a reference was made to the European Court of Justice asking whether the exclusion in art.1(2)(b) of the Brussels I Regulation covered a decision given by the courts in one Member State regarding the registration of ownership of shares in a company where the company is established in that Member State but a transfer has occurred pursuant to the act of a liquidator of a company located in another Member State which owned those shares, and where the basis of that decision was the non-recognition of the liquidator’s title to act.

In this case also, the European Court of Justice referred to *Gourdain* and the need to demonstrate the closeness of the link between the action at issue and insolvency proceedings. The court was of the view that, in the instant case, the link was particularly close. It stated that the dispute as to ownership arose because of the transfer in the context of liquidation proceedings by the liquidator exercising powers granted by the insolvency law concerned. These rules, which stipulated that the debtor lost the power of disposition over personal assets and that the liquidator administered these on behalf of the creditors’ interests, together with any necessary powers such as the ability to alienate the assets within insolvency proceedings, were acceptable derogations from the general private law position in property law. The court stated that the transfer and the action for restitution of title were a direct consequence of the insolvency proceedings and were indissociable from it. The same could be said of the action before the Austrian courts in which the transfer of shares was held invalid on the basis of non-recognition of the right of the liquidator to effect that transfer, which again was intimately linked to the insolvency proceedings. As a result, the court had no difficulty in holding that the art.1(2)(b) of the Brussels I Regulation exception applies to the issues at stake and that they are connected to and are issues arising out of the insolvency proceedings. Implicit in the court’s judgment is the view that it was merely incidental that the European Insolvency Regulation was not yet in force between the two Member States concerned and that recourse was therefore to the private international law position.

In a third case, *German Graphics*, a company established in Germany sold machinery to a Dutch company, Holland Binding BV, under a contract containing a reservation of title clause. The Dutch company subsequently entered into insolvency proceedings in 2006. The German company brought an action before the Brunswick Regional Court for protective measures to be ordered with respect to the machinery it had sold and that was located at the Dutch company’s premises. The order was granted and, on enforcement proceedings being undertaken in the Netherlands, was duly recognised by the supervisory judge appointed to oversee the proceedings in Utrecht. The liquidator appealed and the recognition order was quashed. On further appeal to the Dutch Supreme Court, proceedings were stayed pending a reference to the European Court of Justice. The reference asked three questions, the first of which was whether the proviso in art.25(2) looking to

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the application of the Brussels Convention (and by extension the Brussels I Regulation) rules first required a determination of whether the subject-matter of the action falls within the exclusion in art.1(2)(b) of the Brussels I Regulation and thus outside the scope of that regulation. The second question asked whether the reservation of title action brought in one Member State and sought to be enforced in another was an action that related to insolvency and thus fell within the art.1(2)(b) of the Brussels I Regulation exception, with the third question inquiring whether it was relevant for the purposes of defining the status of the reservation of title action that art.4(2)(b) of the European Insolvency Regulation requires the court where insolvency proceedings are opened to determine the assets that are to form part of the estate.

In its response, the European Court of Justice first indicated that in deciding whether the art.25(2) of the European Insolvency Regulation exclusion, referring to the use of the Brussels I Regulation enforcement framework in the case of judgments falling outside the purview of the European Insolvency Regulation, applied required the court to first determine whether the judgment concerned was within the scope of the Brussels I Regulation. This may seem clear as, consonant with the case law thus far, the critical issue is whether the judgment falls to be enforced within the insolvency or general civil and commercial frameworks, albeit the court concedes the possibility, without giving any concrete examples, of judgments falling outside the scope of both regulations. In response to the two remaining questions, the court again referred to the Gourdain case and reiterated the test established in that case. Although the court was of the view that the Brussels Convention (and Brussels I Regulation) rules were to be given as wide a reading as possible and that the European Insolvency Regulation framework governing one of the exceptions to that framework should be closely interpreted, it nonetheless accepted the Gourdain formula requiring a sufficiently close and direct link should apply. In the instant case, it held that the question of asset recovery and whether the reservation of title applies was a question independent of the opening of insolvency proceedings and, although the liquidator was a party to proceedings, the recovery action was not based on the law of insolvency proceedings and arose irrespective of the existence of proceedings or appointment of a liquidator. As regards art.4(2)(b) of the European Insolvency Regulation, the court was of the view that the rule merely serves to avoid a conflict of laws by introducing a rule for the determination of the procedural law applicable, with no consequent effect on whether the Brussels Convention (and Brussels I Regulation) rules apply, while art.7(1) of the European Insolvency Regulation, which creates a carve-out for reservation of title from the procedural law of the forum does not influence the classification of whether actions under its provisions are connected with insolvency proceedings.

**Conclusion**

As the European Insolvency Regulation reaches the end of its ninth year since it came into force, the number of reported cases on its provisions continues to increase. Many of these are on the jurisdictional paradigm contained in art.3 of the European Insolvency Regulation and the repartition of competence between courts as far as opening insolvency proceedings is concerned. The cases above mark the beginnings of a new line of jurisprudence that seeks to settle a problem that goes back to the beginnings of the project that eventually led to the European Insolvency Regulation when an attempt was made to carefully delineate the fields of competence between that text and the Brussels Convention (and Brussels I Regulation) framework on judgments in civil and commercial matters. These cases will undoubtedly settle an issue of interest to many insolvency practitioners, given the possibility of such claims continuing to arise as the European Insolvency Regulation framework develops. It will not resolve all issues related to the conduct of proceedings, many of which have yet to be determined. Part of the problem lies in the fact that many issues important to insolvency law and practice only rarely receive the attention of the European Court of Justice, largely owing to the desire of practitioners to avoid expensive and protracted litigation on issues that may only be of marginal relevance to the outcome.

Ultimately, whether the litigation is settled under the general civil framework or within the context of insolvency goes to the issue of costs and thus some need exists for the delineation of the boundaries between the two frameworks. The accumulated case law thus far before the European Court of Justice, variously involving transactions to set aside, registration of share transfers and reservation of title, indicates that the court is careful to draw the boundaries in a way that conforms to a logical and substantive appreciation of the connection between the actions and insolvency law, using the decision in Gourdain as the benchmark for that determination. Implicitly, the decisions also indicate that the court is conscious of the underlying need to consider issues of efficiency and effectiveness. The same pattern has been seen in the emerging case law on similar issues before the courts of various Member States. Although the view has been put forward in the German Graphics case that the European Insolvency Regulation as a régime d’exception should be interpreted restrictively, it nonetheless appears, at all levels, that the courts have been keen to give purposive interpretations consonant with the fundamental principles of efficiency and effectiveness and to ensure that, wherever possible, issues arising from insolvency are treated within the one or limited set of proceedings. However, the connection between the issues and insolvency law has to be established and arguments cannot be sustained where to do so would stretch the definition of or put an artificial construction on the meaning of insolvency in the domestic
law concerned. As cases continue to be brought on the boundaries between the insolvency and general civil law enforcement frameworks, the continuing evolution of the line of jurisprudence noted here and whether the scope of the definition of insolvency and “analogous proceedings” will change will certainly be of interest.

36 See Byers v Yacht Bull Corp [2010] EWHC 133 (Ch); [2010] B.C.C. 368, where the issue was a claim made by joint liquidators of a company asserting beneficial ownership to a yacht, which was registered in the Cayman Islands in the name of a different company under the ownership of the wife of the first company’s owner. The trial judge, Sir Andrew Morritt C., said that the link between the claim as to ownership and the winding up was, in the language of the Gourdain case, neither “direct nor close” (at [26]) so as to attract the application of the European Insolvency Regulation’s provisions. See also Gibraltar Residential Properties Ltd v Gibraltar 2004 SA [2010] EWHC 2595 (TCC).

37 The pending review of the Brussels I Regulation (which occurred in December 2010) does not seem to have addressed this. There remains the anticipated review of the European Insolvency Regulation in the course of 2011-2012, which may well offer the opportunity for a revisiting of the relevant definition.