

**SUCCESS AND FAILURE
IN CROSS-BORDER INSOLVENCY PROCEEDINGS
OF MULTINATIONAL CORPORATIONS
– PARMALAT –
A EUROPEAN AND AMERICAN PERSPECTIVE**

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ABBREVIATION

ABIJ	The American Bankruptcy Institute Journal
ABLJ	American Bankruptcy Law Journal
AJICL	Arizona Journal of International and Comparative Law
B.C.	Bankruptcy Code
BLJ	Business Law Journal
CLT	Corporate Legal Times
CJIL	Connecticut Journal of International Law
COMI	Centre of Main interests
DIP	Debtor-in-Possession Financing
DZWiR	Deutsche Zeitschrift für Wirtschafts- und Insolvenzrecht
ECJ	European Court of Justice
EIR	European Insolvency Regulation (Council Regulation No. 1346/2000 on Insolvency Proceedings)
EuZW	Europäische Zeitschrift für Wirtschaftsrecht
Fn.	Footnote
EBRD	European Bank of Reconstruction and Development
EHC	High Court Dublin
EJL	European Law Journal
FJC	Federal Judicial Center
FTD	Financial Times Deutschland
IFSC	International Financial Service Centre
IFLR	International Financial Law Review
IESC	Irish Supreme Court
III	International Insolvency Institute
I.L.Pr.	International Law Press
IPRax	Praxis des Internationalen Privat- und Verfahrensrechts
IRLE	International Review of Law and Economics
JIBFL	Journal of International Banking and Financial Law
JIBLR	Journal of International Banking, Law and Regulation
JuS	Juristische Schulung
L.D.	Legislative Decree
Ltd.	Limited (limited liability company under English Law)
MLR	Michigan Law Review
MPA	Milk Products of Alabama LLC
NASBL	Norton Annual Survey of Bankruptcy Law
NJW	Neue Juristische Wochenzeitschrift
NJILB	Northwestern Journal of International Business
NZG	Neue Zeitschrift für Gesellschaftsrecht
NZI	Neue Zeitschrift für Insolvenz und Sanierung
PPL	Private Placement Letter
RDAI	Revue de droit des affaires internationales
RWI	Recht der internationalen Wirtschaft
S&P	Standard & Poor
S.D.N.Y.	U.S. District Court for the Southern District of New York
SpA	Società per Azioni (public stock company under Italian Law)

Srl	Società a responsabilità limitata (limited liability company under Italian law)
TIL	The International Lawyer
TILJ	Texas International Law Journal
U.K.	United Kingdom
UNCITRAL	United Nations Commission on International Trade Law
WM	Wertpapiermitteilungen - Zeitschrift für Wirtschafts- und Bankrecht
ZEuP	Zeitschrift für Europäisches Privatrecht
ZIP	Zeitschrift für Wirtschaftsrecht und Insolvenzpraxis
ZZP	Zeitschrift für Zivilprozess

INTRODUCTION

With globalisation spreading further and faster in recent years, businesses have become more internationally integrated by maintaining worldwide subsidiaries. This development leads to growing number of multinational cross-border insolvencies with problems arising from interference between different national insolvency laws. Moreover, financial failures of multinational companies caused by misfortune, fraud or mismanagement can have a great impact on the economic growth of a country and, moreover, on the trust of creditors in financial markets and accounting systems. Effective insolvency systems provide a valuable incentive for the maintenance of high standards of corporate governance, including financial discipline in the course of managing a company's affairs, with the objective to maintain public confidence in the integrity of the credit system. Therefore, the consistent application of orderly and effectual insolvency procedures plays a critical role in fostering growth and competitiveness and may also assist in the prevention and resolution of financial crises.

Since insolvency cases of multinational corporations have a greater significance in terms of size and impact upon people's lives and economic importance, this paper is primarily concerned with identifying and discussing the key issues that arise in the design for and application of effective cross-border insolvency procedures to these companies. Following Enron and WorldCom in the United States, Parmalat is one of the biggest business failures in European history. The company collapsed in 2003 due to massive fraud in the form of looting the company, financial non-disclosure and overstatement and invention of non-existent assets respectively. As a result of these indiscretions, Parmalat filed multiple insolvency cases in various jurisdictions, including Italy, Ireland and the United States. A comparative study of the Parmalat case discloses multiple questions concerning international insolvency proceedings, the responses in national jurisdictions and the principal policy choices that need to be made when resolving cross-border insolvency cases. The Parmalat case exemplifies both the positive and negative aspects of the newer cross-border insolvency schemes. In the first instance, the interaction between the American and Italian proceedings demonstrates how parties can effectively manage a complicated cross-border insolvency to the satisfaction of creditors in all jurisdictions. However, the Irish case of Eurofood demonstrates that unclear resolutions with respect to cross-border insolvencies can serve to create the very problem they are enacted to resolve.

Part I introduces and examines previous international efforts in developing international insolvency systems, and discusses the basic judicial conflicts underlying cross-border insolvency proceedings and the principles of international insolvency in terms of territorialism, universalism and modified universalism.

Part II describes the key issues of the national bankruptcy laws of the United States, Ireland and Italy as well as the European Union approach. This serves as the legal background to understand the Parmalat case conducted in the European Union and United States.

Part III discusses the background of the Parmalat case. Parmalat SpA, the operating unit, and Parmalat Finanziaria SpA, the holding company, filed for insolvency in December 2003. In response, many subsidiaries around the globe were also declared insolvent and put into bankruptcy in 2004.

Part IV considers the American and European Perspective of Parmalat in dealing with the reorganisation and liquidation respectively of its subsidiaries. One of the European subsidiaries of Parmalat is the Eurofood IFSC Ltd., located in Ireland. The Italian and Irish court still struggle whether Eurofood should be included in the Italian group reorganisation as demanded by the Extraordinary Commissioner administering the Italian proceeding, or wound up in a liquidation procedure as asked by the Irish creditors. The subject arose in interpreting key issues (centre of main interests, public policy) of the European Council Regulation on Insolvency Proceedings (EIR) and regarding the control over the process. Finally, the Irish Supreme Court asked the European Court of Justice for a preliminary ruling.

In the meantime, the American subsidiaries Farmland Dairies LLC, Parmalat USA and Milk Product of Alabama LLC filed for Bankruptcy Protection under the United States Bankruptcy Code. While the Irish subsidiary was to be included in the Italian group reorganisation, the Extraordinary Commissioner did not insist on the American companies to be included in that proceeding. One reason may have been that the American subsidiaries were not part of Parmalat's core business, which the Italian reorganisation procedure was rescuing; another being the debtor-friendly approach of the American Bankruptcy Code.

Finally, Part V concludes, despite valuable guidelines and treaties of handling cross-border insolvency proceedings have been achieved and cooperation has been increased between different national courts, which improved cross-border proceedings, a failure of including the procedures of dealing with group insolvency in the EIR and UNCITRAL Model Law. Therefore, the approaches adopted in the EIR and UNCITRAL Model Law are a successful step for developing a harmonised universal standard in this complex judicial field.

1 DEVELOPMENT OF INTERNATIONAL INSOLVENCY PROCEEDINGS

1.1 The Foundation of International Insolvency

Insolvency¹ procedures have a long history, rooted in legal and business practice from Lombardy.² Historically, companies crossed borders and founded colonial empires³ in order to trade and control the sources of raw material, and to protect and enhance their own economic development. Due to their roots in societal values and public policies,⁴ the importance of national economic interests varies from country to country, resulting in different insolvency approaches.⁵ This economic aspect was always closely related to political interests of the state towards intervening in the performance of the market.⁶

Nevertheless, in a market economy where competition dictates that the strongest survives, some businesses fail.⁷ Insolvency laws “provide a safety net”⁸ by promoting fairer and more efficient recapture of assets from a failed business. This is done through balancing conflicting policies of providing a fresh start or rehabilitation for insolvent debtors against the enforcement of creditors’ rights to receive payment. Insolvency laws provide a “collective standard for creditors as opposed to a first-come-first-served practice”.⁹ However, in recent years there has also been a tendency to use bankruptcy law to deal with emerging social and economic problems; e.g. products liability cases, and environmental liabilities.¹⁰

The rise of international trade and the ease of incorporating subsidiaries in multiple jurisdictions gave rise to both the growth of multinational corporations and the necessity of cross-border insolvencies.¹¹ Multinational insolvencies may appear in many different

¹ See White & Case, *Bankruptcy Guide* 2000, 3. See also Omar, Ashgate 2004, 3. Bankruptcy and Insolvency are used interchangeably. The term “bankruptcy” itself is defined as being financially unable to pay one’s debts as they become due, or to have more debts than assets. The word derives from the Italian phrase “banca rotta” meaning “broken bench”, which was the punishment of the trader who failed to pay his creditors denying him the ability to continue exercising his craft. The term is illustrative of the fact that early bankruptcy law was developed in the Italian city-states and generally dealt with traders.

² See Omar, Ahgate 2004, 5: Although earlier references are known, the first major legislation is the English Statute of Bankrupt from 1542 providing proceedings against absconding debtors.

³ For example foundation of the East India Company (1599), the Hudson’s Bay Company (1670), Royal Africa Company (1672).

⁴ See Lechner, *AJCL* 2002, 977. See also Flaschen/Smits/Plank, *CJIL* 2001, 3.

⁵ See Omar, *ILP* 2001, 138. See also Rajak, Sweet & Maxwell 1993, 10.

⁶ See Wood, Sweet & Maxwell 1996, 31. See also Rajak, Sweet & Maxwell 1993, 236. See also Pootow, *University of Michigan* 2005, 19.

⁷ The key elements of a market economy are self-interest and profit maximisation (Smith, *The Wealth of Nations*, 1776). However, Keynes (Keynes, John Maynard, *General Theory of Employment, Interest and Money*, 1936) argued that the state should intervene when necessary to lead the economy through the business cycles and establish trust in the market by creating necessary proceedings in regulating insolvencies.

⁸ ERBD, <http://www.ebrd.com/country/sector/law/insolve/>, 07.02.2006.

⁹ ERBD, <http://www.ebrd.com/country/sector/law/insolve/>, 07.02.2006.

¹⁰ See Dewey Ballantine LLP, *Overview of Chapter 11*, 2. See also Laut, Duncker und Humblot 1997, 160. Examples for filing for a Chapter 11 reorganisation to emerge from e.g. product liability include Johns-Manville Corp. (*In re Johns-Manville Corp.*, 36 B.R. 727 (S.D.N.Y. 1984)), or from financial distress Texaco Inc. (*In re Texaco Inc.* 73 B.R. 960 (S.D.N.Y. 1987)).

¹¹ See Leonard, *TILJ* 1998, 543. See also Smart/Booth, *ILP* 2004, 147.

shapes, e.g. a single debtor having operations or relations with its creditors,¹² or assets located in various countries.¹³ However, the insolvency scenario arising from a failure within a multinational corporate group¹⁴ is complex. The insolvency proceeding then no longer concerns only one debtor but rather a bundle of affiliated companies.¹⁵ Despite having their own legal identity with separate assets and liabilities,¹⁶ these debtors may be seen as a group because of inter-group financial transactions, inter-company letters of credit,¹⁷ or an integrated management directly controlling all the interrelated companies.¹⁸ Furthermore, creditors may continue to deal with solvent members of the group,¹⁹ which varies the position of the creditors in terms of classification with one entity and within the group, while some creditors may have dealt with the group as a whole, whereas others just dealt with a local subsidiary.²⁰ The complex financial issues of cross-border insolvencies resulting from the diversification in interests of the participating parties²¹ lead to the search for a solution in dealing with cross-border insolvencies.²²

The world's jurisdictions often do not agree on basic policies. This is not just based on the differences between common²³ and civil law²⁴ systems that determine a different approach in insolvency proceedings.²⁵ It is rather deeply rooted within a nation's legal traditions and culture. Insolvency policy typically divides the world's legal system in the context of commercial and financial law because it is the test of a jurisdiction's ability to realise its own views of fairness, equity and legal civilisation.²⁶ The lack of an international insolvency framework forces multinational business to look at domestic laws for guidance.²⁷ However, domestic laws differ significantly from each other by either being pro-debtor or pro-creditor oriented.²⁸

¹² An insolvent company with an international network of branches, a company holding assets around the world or simply a company employing foreign employees or dealing with foreign creditors.

¹³ See Blumberg/Fowler, Aspen 2001, xvii.

¹⁴ See Van Galen, INSOL 2003, 5.

¹⁵ See Leonard, TILJ 1998, 543.

¹⁶ See Van Galen, INSOL 2003, 5. See also Blumberg/Fowler, Aspen 2001, xi. See also LoPucki, MLR 2000, 2219.

¹⁷ See Flaschen/Smits/Plank, CJIL 2001, 3. See also Bufford et al., International Insolvency 2001, 2.

¹⁸ See Mevorach, Road to a Suitable and Comprehensive Global Approach, 17-19.

¹⁹ See Leonard, TILJ 1998, 543.

²⁰ See von Wilmsky, WM 1997, 1462.

²¹ See Lüke, ZZP 1998, 276.

²² See Ehrlicke, EWS 2002, 101. See also Westbrook, MLR 2003, 2286.

²³ Common law is based on judicial precedent (*ratio decidendi* and *stare decisis*). England, Scotland and Ireland are common law jurisdictions.

²⁴ Civil law jurisdictions like Germany or France apply a codified body of law and there is no doctrine of precedent, although previous court decisions may be influential.

²⁵ See Cherubini, Graham & Trotman 1994, 175. In common law jurisdictions the bankruptcy trustee becomes the owner of the debtor's estate. In contrast, in civil law jurisdictions the consequence of adjudication of bankruptcy is the debtor losing capacity but not ownership of its property.

²⁶ See Cooper/Jarvis, John Wiley & Sons. 1996, XIII.

²⁷ See Lechner, AJICL 2002, 977.

²⁸ See Lechner, AJICL 2002, 977. See also Wood, Sweet & Maxwell 1996, 3. Other jurisdictions are mainly former communist states, fundamentalist Muslim States and states without a commercial tradition and, therefore, no insolvency law.

The pro-creditor jurisdiction allows a creditor to protect himself by security or set-off to avoid losses resulting from a debtor's default. If it would be impossible for the creditor to use these measures prior to insolvency, insolvency may create unpredictable risks for the creditor with no chance of recovering.²⁹ Since the creditor does not have perfect information about the status of the debtor, he rather divests instead of investing, leading to a harmstringing of economic activity,³⁰ or good debt would be disadvantaged by having to cross-subsidise the prize of the market for bad risk, causing additional instability in the market. In consequence, the pro-creditor system tends to either take-out management in its entirety, or at the least subordinate management's position, in favor of a receiver, or similar entity. In pro-creditor systems, the focus is more on asset realization and maximizing value on behalf of the creditors than on reorganizing the debtor pursuant to the debtor's interests.

On the other hand, a pro-debtor jurisdiction supports the rescue of a debtor in the event of default since it leaves the debtor in control of its day-to-day operations, which gives a debtor some negotiating power with respect to treatment of creditors through the bankruptcy process. This jurisdiction has mechanisms available for a creditor to secure its position prior to insolvency. Therefore, generally speaking, a secured creditor will not lose its security simply because of a bankruptcy filing but the creditor may have to accept losses in its position because the debtor's assets are usually available for equal distribution among all creditors.³¹

1.2 The Organisation of Insolvency across Borders

Several approaches for handling multinational insolvency cases have been developed during the years, and there has been a gradual change in measures from the pure liquidation of the debtor for the benefit of the creditors to preserving and rescuing the debtor with the cooperation of the creditors, assuming there is some benefit in rescuing the company.³² Although national governments have introduced rules and procedures incorporating aspects of cross-border insolvency, international cooperation, and comprehensive assistance,³³ these approaches are limited to their boundaries³⁴ and depend on other jurisdiction laws and policies.³⁵ Apart from the conflict of bankruptcy law crossing international boundaries, the differences in domestic scope of the insolvency process, e.g. the position of creditors and the presence of securities, are also an important aspect of the national jurisdiction.³⁶ An effective and meaningful insolvency process should aim to treat creditors fairly, impartially and equally, and to generally promote integrity in the system.³⁷

²⁹ See Fletcher, Oxford 1999, 4.

³⁰ See Wood, Sweet & Maxwell 1996, 3.

³¹ See Wood, Sweet & Maxwell 1996, 3.

³² See Gromek Broc/Parry, Kluwer 2004, 3: Effective corporate rescue procedures promote economic and social stability by preserving the value of assets represented by an insolvent company and by preserving the jobs of employees. See also Leonard, TILJ 1998, 543. See also Carruth, TIL 2004, 360.

³³ See Hacking, NJILB 1979, 9.

³⁴ See Lechner, AJICL 2002, 978. See also Hacking, NJILB 1979, 1.

³⁵ See Lechner, AJICL 2002, 981.

³⁶ See Smid, Manz 2002, 8. See also Pootow, University of Michigan 2005, 30. See also Franken, EJL 2005, 233.

³⁷ See Lüke, ZZP 1998,

1.2.1 *Universalism and Territorialism*

Historically there are two different approaches in describing the basis for a countries' international insolvency law: universality and territoriality.

The universal approach demands a single international insolvency procedure that would be applicable worldwide.³⁸ The universal approach assumes that the unitary bankruptcy case would administer all the assets of the debtor, including those located in countries other than that where the insolvency case is being heard, and presumes mutual recognition and equal treatment of all creditors (*par conditio creditorum*).³⁹ This approach distinguishes between main insolvency proceedings and secondary or ancillary insolvency proceedings, which assist the main proceeding in e.g. transferring local assets to the main proceeding.⁴⁰ A single legal forum applies to all aspects of a debtor's affairs on a worldwide basis.⁴¹ This approach assumes coordination of laws and courts of different jurisdictions in transnational cases.⁴²

Under the territorial approach, however, each country conducts its own insolvency proceedings with respect to the assets located within its jurisdiction⁴³ and disregards any parallel proceedings in a foreign nation. The country is interested in satisfying its own creditors before contributing assets to pay creditors in other countries.⁴⁴ Under procedural consolidation and coordination, the territorial approach may manage international insolvency proceedings better, assuming that the corporate group is neatly arranged into separate national entities with their own assets and liabilities.⁴⁵ In fact, many companies operate directly, rather than through subsidiaries, in countries outside of their country of incorporation. Subsidiaries usually serve regional purposes, and assets and liabilities are not concentrated within one region but are regionally or even globally spread, since efficient international group accounting transfers assets within the group for business and tax reasons as part of global cash management programs.⁴⁶ In short, the reality for most multinational companies is a complicated mass of assets and liabilities sprawled across borders, not a neat territorial division, resulting in inconsistent and inequitable results for creditors.⁴⁷ The corporate-group problem greatly complicates international bankruptcy issues. It does not make the insolvency proceeding territorial.

³⁸ See von Wilmsowsky, WM 1997, 1462.

³⁹ See Breitenstein, Internationales Insolvenzrecht 1990, 24. See also Hirte/Otte, ZIP 1994, 1493. See also Lechner, AJICL 2002, 983

⁴⁰ See Tobler, BCICLR 1999, 400.

⁴¹ See Lechner, AJICL 2002, 981.

⁴² See Lüke, ZZP 1998, 303.

⁴³ See LoPucki, MLR 2002, 2218: "territoriality means that the bankruptcy courts of a country have jurisdiction over those portions of the company which are within its borders and not those portions that are outside of them".

⁴⁴ See Lechner, AJICL 2002, 982. See also Wimmer, ZIP 1998, 983. See also Cooper/Jarvis, John Wiley & Sons Ltd. 1996, 81: The Netherlands adheres to the territoriality approach, so local assets will not be transferred even if a foreign forum formally requests a Dutch Court or administrator to transfer the assets to a foreign jurisdiction.

⁴⁵ See Leonard, TILJ 1998, 548.

⁴⁶ See Beltzer 2005. See also Blumberg/Fowler, Aspen 2001, xxi.

⁴⁷ See Lechner, AJICL 2002, 982.

In practice, no country adheres either to the universal or the territorial approach without modification;⁴⁸ in consequence, a principle of “modified universalism” has arisen.⁴⁹ The forum hosting the primary proceeding seeks to achieve the broadest extraterritorial effect possible of its orders while leaving open the possibility of cooperation with secondary proceedings commenced in other jurisdictions, thereby making cooperation between primary and secondary proceedings discretionary.⁵⁰

1.2.2 Cross-Border Treaties and Protocols

There are two ways to resolve a debtor’s international financial difficulties: in-court and out-of-court restructuring. While formal insolvency proceedings are governed by national insolvency law, informal insolvency processes are not regulated by insolvency law and generally involve voluntary negotiations between the debtor and some or all of its creditors. These negotiations are often initiated by banks and law firms to provide some form of restructuring of the insolvent debtor. While not regulated by insolvency law, these voluntary negotiations nevertheless depend for their effectiveness upon the existence of an insolvency law.⁵¹ Therefore, even where the parties seek to resolve their disputes out of court, the mechanisms for coordinating multinational cases may still apply.

Favoured options for handling multinational insolvencies have been bilateral treaties between nations and or insolvency protocols.⁵²

Bilateral Treaties

Bilateral treaties between countries are easy to negotiate; however, there are still very few examples in existence.⁵³ These treaties try to regulate commercial interest in the event of a default. The problem arises when the treaties are perceived to touch national sovereign rights.⁵⁴ Furthermore, governments need time to negotiate and approve these treaties and therefore treaties are not a practical solution where a company is nearing the zone of insolvency and needs immediate cross-border bankruptcy relief.

Protocols

Protocols are usually drafted in and pertain only concluded to a specific case.⁵⁵ The main purpose of protocols is to coordinate either two main or secondary cross-border insolvency

⁴⁸ See Virgòs/Garcimartín, Kluwer 2004, 15.

⁴⁹ See Lechner, AJICL 2002, 984. See also Smid, Manz 2002, 38-39.

⁵⁰ See Wessels, Kluwer 2004, 36.

⁵¹ See Beltzer 2005.

⁵² See Dolan/Orzy, Lexpert 2000, 1. See also Rajak, Harry, Sweet & Maxwell 1993, 226. See also Fletcher, Mohr 1990, 271-284.

⁵³ See Omar, Ashgate 2004, 17, 34. See also Wood, Sweet & Maxwell 1996, 291. There are different international treaties applying to discrete groups of states: bilateral initiatives, e.g. Franco-Swiss Convention (1869), regional or wider multilateral initiatives, e.g. Nordic Convention (1933) applying to Scandinavian countries, Bustamante Code of Private International Law (1928), applying to South American States.

⁵⁴ See Leonard, TILJ 1998, 546.

⁵⁵ See *In re Maxwell Communication Corp. plc*, 170 B.R. 800 (S.D.N.Y. 1994): Cross-border protocol between the U.S. and U.K. This protocol has been used in several recent cases involving dual plenary proceedings, e.g. *In re Livent (US) Inc, et al.* Case No B-48312 (AJG) (S.D.N.Y. 1998). Maxwell was an English holding company, with the majority of financial affairs administered in the U.K. while the operating subsidiaries which constituted its principal assets were located in the U.S.. The company

proceedings, by setting forth recognition of individual countries' insolvency legislation, communications amongst the various courts⁵⁶ and the use of available technology in those countries where two proceedings are conducted concurrently affecting the same parties.⁵⁷ Protocols provide instruments for more efficient insolvency proceedings because possible disputes have been negotiated up front and eliminate overlapping proceedings. Although protocols may be used between courts from civil law and common law jurisdictions,⁵⁸ they are usually used between involved countries that share the same legal system. Although cross-border protocols have become more commonplace in multi-jurisdictional restructurings, there are cases demonstrating the possibility to achieve a complex multinational restructuring even without formal arrangements.⁵⁹

Following the successful use of cross-border insolvency protocols, the International Bar Association developed the Cross-Border Insolvency Concordat to serve as a model for future cross-border insolvency protocols. The Concordat provides non-statutory guidelines⁶⁰ that the parties or the courts could adopt as practical solutions to cross-border issues arising from insolvency proceedings in different states.⁶¹ Thereby, the Concordat is not a substitution for existing treaties or statutes but is rather a guideline in the case of absence of appropriate measures "to guide practitioners in harmonizing cross-border insolvencies".⁶²

In preference of solving a cross-border insolvency issues, the Concordat prefers a single responsible administrative forum (Principle 1) and the proceedings should be coordinated by the main forum (Principle 2). However, in case of more than one main forum (Principle 3) or plenary forums (Principle 4) respectively, the Concordat provides a course of action for the parties involved.

commenced dual plenary proceedings in the U.S. under B.C. (Chapter 11) and in the English High Court of Justice (Insolvency Act 1986). The unprecedented cooperation of the courts set forth a protocol with respective rights and duties of the U.S. examiner and British administrators.

⁵⁶ See Power/Mears/Barrett, Graham & Trotman 1994, 234-235.

⁵⁷ See Lechner, AJICL 2002, 992. See also Beltzer 2005. Protocols include specific aspects of the proceeding such as the appointment of examiners or foreign representatives. Recent important breakthrough in terms of international cooperation involves the use of direct judicial communications and negotiations by various means such as telephone conversations, videoconferences and exchanging emails. Also Dolan/Orzy, Lexpert 2000, 2. The protocols regulate the proceeding and deal with issues such as how and where a creditor will be entitled to prove its claim and to vote on the restructuring proceedings and which court have jurisdiction over various aspects of the restructuring. Therefore, focus on communication between foreign administrators or foreign courts to guarantee fair and equal treatment for foreign creditors.

⁵⁸ See *In re AIOC Corporation and AOIC Resources AG*: cross-border liquidation protocol between the United States and Switzerland. Protocols involving two countries with a common legal tradition are more likely to include clear substantive rules, while protocols between civil and common law countries tend to focus more on procedural rules.

⁵⁹ See Beltzer/Ginsberg, *Euromoney* 2004, 19.

⁶⁰ Ten principles guide the harmonization of international insolvency proceedings.

⁶¹ See III, <http://www.iiiglobal.org/international/projects/concordat.pdf>, 23.02.2006

⁶² See III, <http://www.iiiglobal.org/international/projects/concordat.pdf>, 23.02.2006, 3.

2 LEGAL BACKGROUND ON INSOLVENCY PROCEEDINGS

2.1 Important International Insolvency Approaches

On the international level, it is agreed upon that the system should minimise disadvantages for creditors participating in a foreign insolvency proceeding. However, difficulties also arise in answering the problem of time, distance, costs, foreign languages and resources.⁶³ The extensive work in recent years reflects the growing impact of failures and financial difficulties in the corporate world and the push for institutional solutions of problems inherent in international insolvencies. The most important international cross-border approaches are from recognised international institutions like the World Bank, the International Monetary Fund (IMF), INSOL Lenders Group (LSG) as well as the United Nations Commission on International Trade Law (UNCITRAL); regional progress include the Community Law of the European Union⁶⁴ and The American Law Institute (ALI) describing the cooperation among the members of the North American Free Trade Agreement (NAFTA). A universal approach in dealing with multinational cross-border default has not been found yet, and progress in the international insolvency area is highly dependent on the insolvency community to find structures and solutions to cross-border and multinational financial problems. However, the initiatives that have emerged on the international level are a valuable step towards efficient and effective cross-border insolvency proceedings.⁶⁵

2.1.1 World Bank Principles and Guidelines for Effective Insolvency and Creditor Rights Systems

In April 2001, the World Bank⁶⁶ identified 35 core principles⁶⁷ that underpin sound insolvency and creditor rights worldwide. The principles emphasise contextual, integrated solutions and the policy choices involved. They rely on the fundamental premise that sustainable market development requires access to affordable credit.⁶⁸ Capital investment can only happen in an environment where parties can manage the insolvency risk associated with credit relationships.⁶⁹ These principles incorporate international best practice in the design of insolvency and creditor rights mechanisms and are used to benchmark strengths and weaknesses of existing systems.

⁶³ See Wimmer, ZZP 1998, 983.

⁶⁴ The implementation of the EIR corresponded with reform efforts in most European Member States in their national insolvency laws (among them France, Germany, and Italy).

⁶⁵ See Hamilton 2005.

⁶⁶ The World Bank Group include the International Bank for Reconstruction and Development, the International Development Association, the International Finance Corporation, and the Multilateral Investment Guarantee Agency.

⁶⁷ See <http://www.worldbank.org>, 23.02.2006.

⁶⁸ See Uttamchandani, JIBFL 2004, 452.

⁶⁹ Affordable credit with reduced interest rates and secured lending transaction costs require efficient laws and legal systems. Lenders need certainty of their legal position. The ability in defining market risks and making them predictable permits lenders to price loans and make financing available. Uncertainty not only raises the cost of capital but also limits the availability of capital (problem of adverse selection).

2.1.2 International Monetary Fund Orderly and Effective Insolvency Procedures

Over the years, the IMF has become increasingly involved in the promotion of orderly and effective insolvency systems among its members. The IMF report⁷⁰ refers to the UNCITRAL Model Law and the European Regulation on Insolvency Proceedings.⁷¹ Experience has demonstrated that reform in insolvency procedures can play an important role in strengthening a country's economic and financial system, especially for economies in transition from centralisation to market economy, independent from their stage of development.⁷² The report discusses the major policy choices to be addressed by countries when designing an insolvency system and expresses certain preferences with respect to e.g. the choice-of-law and debtor-creditor rights.

2.1.3 INSOL International “Cross-Border Insolvency – A Guide to Recognition and Enforcement”

In order to assist foreign representatives who are endeavouring to deal with insolvency proceedings spanning national borders, INSOL International⁷³ published the first edition of its guide in 1996. This guide, however, is not intended to replace legal advice but rather intends to provide practitioners with a general understanding of cross-border insolvency law. This is more important since insolvency procedures are no longer mainly liquidations, but bankruptcy courts increasingly emphasise reorganisations that need timely and predictable assistance.

2.1.4 UNCITRAL Model Law on Insolvency Proceedings

In 1997, the United Nations Commission on International Trade Law (UNCITRAL) adopted the Model Law on Cross-Border Insolvency,⁷⁴ which provides the broadest global framework for cooperation and coordination of cross-border insolvencies. Focusing on providing a procedural framework to facilitate easy recognition, access and relief, it also encourages coordination and cooperation co-operation between courts and office holders in differing states (Article 25,26,27 UNCITRAL Model Law). The Model Law was negotiated among more than 40 countries, representing a broad spectrum of differing legal systems. It attempts to achieve limited but effective cooperation, compatible with all legal systems⁷⁵ and therefore acceptable to all countries. However, it does not attempt to harmonise the substantive insolvency laws of participating jurisdictions and does not involve rules of direct jurisdiction and choice-of-law.⁷⁶ Countries are free to adopt and adapt the Model Law by modifying and excluding its provisions to accommodate local laws. Thus, its success depends on the discretion of each state wishing to embrace it.⁷⁷ As of today, only a

⁷⁰ See <http://www.imf.org/external/pubs/ft/orderly/>, 17.01.2006. The report builds upon--and is consistent with--the Key Principles and Features of Effective Insolvency Regimes set forth in the report of the G-22 Working Group on International Financial Crises.

⁷¹ See Paulus, IPRax 1999, 149.

⁷² See Vassallo et al., TIL 2001, 461.

⁷³ See INSOL, <http://www.insol.org>, 16.01.2006. INSOL International is a world-wide federation of national associations for accountants and lawyers who specialise in turnaround and insolvency.

⁷⁴ See <http://www.insol.org/uncitral.htm>, 17.01.2006.

⁷⁵ See Lechner, AJICL 2002, 1010: The Model Law respects the sovereignty of the states because the local court still has the opportunity to review the automatic stay following the recognition of a foreign proceeding if it is inconsistent with national law and may modify the relief granted.

⁷⁶ See Benning/Wehling, EuZW 1997, 618-619. See also Fletcher, Kluwer 2004, 153.

⁷⁷ See Benning/Wehling, EuZW 1997, 622-623.

few states⁷⁸ have adopted the Model Law. However, it is being strongly considered in a number of major states, among them the United States⁷⁹ and the United Kingdom.⁸⁰

A distinction should be made between the recognition of foreign main proceedings (Article 2(b) UNCITRAL Model Law) and foreign secondary proceeding (Article 28).⁸¹ A foreign main proceeding takes place where the debtor has its centre of main interests, determined by the debtor's registered office "in the absence of proof to the contrary" (Article 16(3), 17(2)(b) UNCITRAL Model Law).

2.1.5 The American Law Institute

The North American Free Trade Agreement has stimulated a large increase in economic activity crossing Canadian, Mexican, and United States borders. Inevitably, this has resulted in an increase of insolvencies of multinational companies within the NAFTA territory. The ALI Principles⁸² supply an understanding of the insolvency laws of NAFTA countries.⁸³ The principles draw upon formulations set forth in the 1997 UNCITRAL Model Law but are firmly grounded in the realities of U.S., Canadian, and Mexican law and practice.

Furthermore, the American Law Institute initiated the project 'Guidelines for Court-to-Court Communications in Cross-Border Cases', which is intended to enhance coordination and harmonization of insolvency proceedings that involve more than one country. These guidelines were also adopted by the International Insolvency Institute in 2001.

However, neither of the abovementioned initiatives deals with the case of a multinational default with a multiple debtor.⁸⁴

2.2 American Bankruptcy Law

The first American bankruptcy law to provide an acceptable legal system to establish and determine the rights and obligations of debtors and creditors in an insolvency proceeding was adopted in 1898.⁸⁵

⁷⁸ In May 2000, Mexico became the first major economy to officially adopt the UNCITRAL Model Law as part of its domestic insolvency legislation, followed by South Africa in November 2000.

⁷⁹ The U.S. implemented the provisions of the UNCITRAL Model Law closely in Chapter 15 U.S.B.C.

⁸⁰ A new part to the Insolvency Act, implemented in 2005.

⁸¹ See Benning/Wehling, *EuZW* 1997, 620.

⁸² See <http://www.ali.org>, 25.01.2006. The American Law Institute's Transnational Insolvency: Cooperation Among the NAFTA Countries, which apply only to legal persons, while the EIR and UNCITRAL Model Law apply to natural persons as well.

⁸³ The Project's goal was to develop principles and procedures for managing the general default of an enterprise having its centre of interest in a NAFTA country and having assets, creditors, and operations in more than one NAFTA country. A protocol for cooperation should include provisions for coordinated court approval of decisions and actions when required and for communications with creditors as required under applicable law.

⁸⁴ See Mevorach, *Global Approach to Insolvencies* 2005, 6.

⁸⁵ See Duberstein, *RDAI* 1989, 257. See also Miller/Waisman, *ABLIJ* 2004, 160. The bankruptcy debates in 1800, 1841, 1867, and 1898 did not address corporate reorganisation but the Bankruptcy Act 1898 was the first to introduce provisions contemplating corporate bankruptcy.

Drawing from the failures the prior law,⁸⁶ Congress passed a new Bankruptcy Code in 1978,⁸⁷ 11 U.S.C. §§ 101 et seq., permitting modern businesses a better opportunity to reorganise rather than liquidate.⁸⁸ In order to file for bankruptcy in the U.S., the debtor only needs to have “a place of business, or property in the United States” (11 U.S.C. §109).⁸⁹

With the American consumer misunderstanding the benefits that credit financing provides for their economy,⁹⁰ and with the U.S. spinning towards being the most hedonistic global society living on debt,⁹¹ a growing number of consumers and corporations file for bankruptcy relief.⁹² To stop this development, the government signed the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 into law on April 21, 2005, which took effect in October 17, 2005.⁹³ The bill also added Chapter 15 to ease the handling of multinational bankruptcies.

The Bankruptcy Code⁹⁴ constitutes the whole of Title 11 of the United States Code.⁹⁵ Title 11 is divided into Chapters, of which the first three Chapters – 1, 3, 5 – are general provisions that apply to all types of Bankruptcy proceedings.⁹⁶

⁸⁶ In 1974, the German Bankhaus IB Herstatt KGaA collapsed. On June 26, 1974, Herstatt’s banking license was revoked and its liquidation was ordered. There was no advance preparation for a coordinated proceeding. As the news arrived New York, still active due to the time difference, creditors rushed to attach Herstatt’s assets at Chase Manhattan Bank New York. Within a few days of Herstatt’s closure, various New York state and federal courts had issued orders of attachment. The legal battle resulted from the issue that the German liquidator wanted to include the attached assets in the German proceeding.

⁸⁷ See Lebow/Tait, RDAI 1989, 258. “Largely as the result of Herstatt disaster [...] the new Code included an attempt to address the unique problems inherent in international commercial bankruptcy disputes where a U.S. creditor is a party to the transaction.”

⁸⁸ See White & Case LLP, Bankruptcy Guide 2000, 1. See also Dewey Ballantine LLP, Overview Chapter 11, 1. See also Lebow/Tait, RDAI 1989, 258.

⁸⁹ See Zennek, VVF 1996, 246. The principal place of business may deviate from the place of incorporation but both have to be in the U.S. See also Fletcher, Oxford 1999, 122-123. The possibility of dual citizenship is accepted.

⁹⁰ See Miller/Waisman, ABLJ 2004, 156.

⁹¹ See Samuelson, Spiegel 38/2005, 86-91.

⁹² The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 Act will only apply to cases filed on and after the October 17, 2005. *Herewithafter* the 2005 Act.

⁹³ The 2005 Act is the most extensive revision of the Bankruptcy Code since its enactment in 1978 and surpasses, in both its breadth and substance, the scope of reform sought by Congress the last time it amended the Bankruptcy Code in 1994.

⁹⁴ Entities not eligible for relief under one or more chapters of the Bankruptcy Code are e.g. banking and insurance companies, entities having no residence, domicile, place of business or property in the United States.

⁹⁵ 11 U.S.C. *Herewithafter* “the Code”. When a Code section is cited, only the section symbol and number are used.

⁹⁶ See Blum, Aspen 2004, 94. See also Treister, et al., ALI 1993, 391. Chapter 1 “General Provisions”, Chapter 3 “Case Administration”, Chapter 5 “Creditors, the Debtor and the Estate”. Note: Chapter 13 is a reorganisation chapter for natural persons who wish to repay all or a portion of their debt over time. While Chapter 9 is reserved for the bankruptcy of municipalities or other local government institutions, Chapter 12 governs the debts of family farmers with a regular annual income. When a bankruptcy petition is filed, one of these chapters is selected and applicable. See Blum, Aspen 2004, 94: Conversion from one chapter to another is possible. However, even when conversion occurs, only one of the specific chapters is applicable at that time.

The two basic types of Bankruptcy proceedings relevant to multinational corporations are Chapter 7 (liquidation) and Chapter 11 (reorganisation). Reorganisation is the dominant proceeding, at least in the sense that most substantial businesses will attempt a Chapter 11 filing before confessing final failure in Chapter 7.⁹⁷

The vast majority of cases are filed voluntarily by the debtor.⁹⁸ Voluntary petitions must be filed in “good faith” but require no proof of insolvency.⁹⁹ Critically, this means on the one hand that rescue procedures are available to struggling companies at an earlier stage than is the case in other jurisdictions,¹⁰⁰ but, on the other hand, provide greater prospects for a successful restructuring. However, creditors¹⁰¹ are permitted to file involuntary petitions against a debtor¹⁰² in case of equitable insolvency.

2.2.1 Chapter 7 Liquidation

In order to qualify for relief under Chapter 7, the debtor must be an individual, a partnership, or a corporation. (§§109(b), 101(41)) The debtor can file a petition for a straight liquidation. Its aim is the surrender and dissolution of the debtor’s executable estate for the purpose of generating a fund to be applied to the payment of the creditors.¹⁰³ The automatic stay ensures the orderly liquidation.¹⁰⁴ A corporate debtor does not receive discharge, once it has been liquidated, it becomes defunct (§727 (a)(1)).¹⁰⁵

2.2.2 Chapter 11 Reorganisation

Chapter 11 is a reorganisation proceeding with the general purpose of preserving the debtor’s business as going concern. The debtor¹⁰⁶ is able to continue its business (§§1104, 1107) under the shelter of automatic stay (§362).¹⁰⁷ The company is thereby able to

⁹⁷ Allen & Overy LLP, U.S. Report 2004, 28/7. §706 (a)“...a liquidation case can be commenced by the conversion of a Chapter 11, 12 or 13 case in circumstances where the debtor is unable to reorganise its affairs, or if there has been an unreasonable delay in its reorganisation efforts”. See also Blum, Aspen 2004, 101.

⁹⁸ See Blum, Aspen 2004, 195. See also Blumberg, CJIL 1989, 8.

⁹⁹ See Blum, Aspen 2004, 63. See also Laut, Duncker und Humblot 1997, 157.

¹⁰⁰ Frey/McConnico/Frey, West Publishing 1990, 15. “American bankruptcy law has no provisions which suggest that it is morally wrong for a debtor to file for bankruptcy and there is no requirement that the debtor be insolvent in order to file a voluntary petition under any chapter of the Code”.

¹⁰¹ See Blum, Aspen 2004, 201. The petition requires three or more creditors who are owed a total of at least \$10,000.00; if there are less than 12 creditors in total; then the involuntary petition may be filed by one creditor who is owed at least \$10,000.00 (§303(b)(1)).

¹⁰² See Blum, Aspen 2004, 199. Only under Chapter 7 and Chapter 11, a debtor cannot be placed involuntarily into bankruptcy under Chapter 12 and 13. (§303(a)).

¹⁰³ See Blum, Aspen 2004, 173-174. On the filing, the court appoints a trustee, whose primary duty is to collect the debtor’s nonexempt unencumbered assets, liquidating them and distributing the cash to creditors who have proved claims in the estate.

¹⁰⁴ See ALI, Juris 2003, 15.

¹⁰⁵ See Blum, Aspen 2004, 174. The existence of undischarged debts prevents trafficking in shell corporations. However, the individual debtor is discharged from all existing debt and thereby receives a “fresh start” (See Blum, Aspen 2004, 99).

¹⁰⁶ See Blum, Aspen 2004, 176. Debtor under the Code may be an individual, including partnerships and corporations, but not a governmental unit (§101(41)), or a municipality (§101(13)).

¹⁰⁷ See Blum, Aspen 2004, 221-222. Its effect is to impose a wide-ranging prohibition on all activity. It comes automatically in effect upon the filing of the petition, remains in effect during the case and is binding on all entities.

preserve its profitable activities and assets while negotiating with creditors, and attempts to develop a strategy for the satisfaction of debts and the revitalisation of the failing enterprise.¹⁰⁸ If negotiations are successful, a reorganisation plan is formulated, which sets out the way to financial recovery and contains proposals for the treatment of debt. A plan often calls for the debtor to repay creditors from future earnings, from borrowings, or from the sale of assets.¹⁰⁹

The debtor files a petition,¹¹⁰ and is granted all the powers of a trustee,¹¹¹ called a "debtor in possession" (DIP) (§1101(1)).¹¹² The key to the recovery prospects of a company in financial difficulty is the availability of debtor in possession (DIP) finance.¹¹³ In the U.S. there is a ready marketplace for companies to obtain rescue funding to operate as going concerns while putting in place a rescue plan.¹¹⁴

2.2.3 Chapter 15 Ancillary and Other Cross-Border Cases

The new Chapter 15 provides proceedings for ancillary and cross-border cases, and incorporates the UNCITRAL Model Law on Cross-Border Insolvency into federal bankruptcy law.¹¹⁵ When Chapter 15 is applicable, the determination of such problems in U.S. courts will turn on the meaning and application of crucial new concepts, similar to those of numerous other industrialized countries:¹¹⁶ centre of main interests (§1516(c)), foreign main proceeding (§1502(4)),¹¹⁷ foreign non-main proceeding (§1502(5)),¹¹⁸ and establishment (§1502(2)) that do not presently exist in U.S. bankruptcy law at all. The new Chapter deletes the former §304, but the application does not differ significantly from that of the former §304 in procedure and application.

¹⁰⁸ See Miller/Waisman, ABLJ 2004, 154. See also White & Case LLP, United States Report, 2.

¹⁰⁹ See Blum, Aspen 2004, 468-474. In Chapter 11, priority claims, including recent tax claims, are required to be paid in full, plus interest. Secured claims are required to be paid in full, also with interest. Unsecured non-priority claims are required to be paid a dividend at least equal to that which they would receive if it were a Chapter 7 case.

¹¹⁰ The petition includes a list of assets and liabilities, and a detailed statement of financial affairs. The debtor has the exclusive right to file a reorganisation plan during the first four months after filing the petition. Thereafter, creditors are permitted to file plans.

¹¹¹ See Allen & Overy LLP, U.S. Report 2004, 28/8.

¹¹² Sweeney, Interview 2005. DIP means the debtor under Chapter 11 responsible for the operation of the debtor's business affairs. The DIP is given the same rights and duties as a trustee. The trustee is empowered to recover money and property for the benefit of the creditors. However, the court can appoint a trustee for cause of mismanagement and fraud.

¹¹³ See ALI, Juris 2003, 49. Bhandari/Weiss, Cambridge 1996, 315. DIP financing „is valuable because the firm can borrow on cheaper terms and thus conserve scarce cash“.

¹¹⁴ See Beltzer, 2005. See also White & Case LLP, United States Report, 22. See also Frey/McConnico/Frey, West Publishing 1990, 35. See also Harold, Interview 2005.

¹¹⁵ See Westbrook, ABLJ 2002, 18.

¹¹⁶ Compare also with principles of the EIR and the UNCITRAL Model Law.

¹¹⁷ Before §101(23) Foreign proceeding means "a proceeding, whether judicial or administrative and whether or not under bankruptcy law, in a foreign country in which the debtor's domicile, residence, principal place of business, or principal assets were located at the commencement of such proceeding, for the purpose of liquidating an estate, adjusting debts by composition, extension, or discharge, or effecting a reorganisation".

¹¹⁸ Note: Chapter 15 and the Model Law both use the term non-main proceeding, a less felicitous locution than the term secondary proceeding that is used in the EIR. The meanings are identical. Compare §1502(5) and Model Law, Art. 2(c) (definition of non-main proceeding) with EIR Art. 3.(2)(3) (designation of proceeding as secondary proceeding).

Under §304 of the U.S. Bankruptcy Code, a non-U.S. debtor would be required to move to the U.S. bankruptcy court for recognition prior to receiving any relief. Recognition was a complicated process whereby the court balanced specific factors,¹¹⁹ including the treatment of U.S. creditors under the foreign system and general notions of international comity. After recognition, the non-U.S. debtor was still not entitled to any relief from the U.S. bankruptcy court; the court had discretion to order relief, including enjoining proceedings pending in the U.S. or turnover of U.S. assets to the non-U.S. receiver, however, it was not required to do so. A non-U.S. debtor could, however, apply directly to a U.S. non-bankruptcy court for relief, such as a stay or dismissal of a proceeding, or could file a plenary U.S. bankruptcy case, thereby limiting the uncertainty with respect to §304.

2.2.4 Recognition of Foreign Insolvency Proceedings

The U.S. Bankruptcy Code plays a significant role in multinational restructurings.¹²⁰ In foreign insolvency proceedings, U.S. Courts have historically cooperated with foreign courts and administrators.¹²¹ The purpose of introducing Chapter 15 is to aid foreign courts and accommodate the increasing number of foreign insolvency proceedings that have extraterritorial effects within the U.S.¹²²

A foreign entity may commence two types of cases under U.S. bankruptcy law – an ancillary case pursuant to Chapter 15 or on a plenary case pursuant to §301 or 303.¹²³

Plenary Proceedings

A foreign entity may become a debtor in a full plenary case in the U.S. under §301 or §303.¹²⁴ Since the Bankruptcy Code and U.S. law automatically apply in a plenary case, there is considerable potential for forum shopping.¹²⁵ The absence of more restrictive jurisdictional and eligibility requirements for plenary cases involving foreign debtors requires courts to embrace the choice-of-law rule.¹²⁶ In a plenary case commenced by or

¹¹⁹ In deciding whether to grant relief pursuant to § 304(b), courts are guided by the following factors: “ (1) the just treatment of all holders of claims against or interests in [the] estate; (2) the protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in [the] foreign proceeding; (3) the prevention of preferential or fraudulent dispositions of property of [the] estate; (4) the distribution of proceeds of [the] estate substantially in accordance with the order prescribed by this title; (5) comity; and (6) if appropriate, the provision of an opportunity for a fresh start for the individual that [the] foreign proceeding concerns.”

¹²⁰ See Beltzer/Ginsberg, *Euromoney* 2005/2006, 44.

¹²¹ See Allen & Overy LLP, *U.S. Report* 2004, 28/17. See also Cooper/Jarvis, *John Wiley & Sons* 1996, 129-130.

¹²² See Schrag/Walker/Blumberg, *BLI* 2004, 170. See also Beltzer 2005.

¹²³ However, where a “foreign proceeding” has been commenced prior to a U.S. plenary bankruptcy case, the non-U.S. entity must commence a Chapter 15 proceeding and the U.S. bankruptcy court must recognise the foreign proceeding prior to commencing a U.S. plenary proceeding.

¹²⁴ A foreign debtor may file a voluntary petition under § 301, involuntary cases are commenced by a foreign representatives under § 303(b)(4).

¹²⁵ See Schrag/Walker/Blumberg, *BLI* 2004, 152.

¹²⁶ *In re Maxwell Communication Corp. plc*, 170 B.R. 800 (S.D.N.Y. 1994) which involved plenary bankruptcy cases in both England and the United States. The British administrators of the joint case brought a preferential transfer action in the U.S. court to set aside certain payments that had been made to two British banks and one French bank shortly before the filing of the bankruptcy cases. The U.S. court applied traditional choice-of-law principles to find that the controversy must be decided under English law. Given this decision, the court dismissed the suits on the grounds of comity.

against a foreign entity, however, all of the eligibility requirements of Bankruptcy Code §109 must be met.¹²⁷ A U.S. court can embrace greater power in a multinational case when the plenary proceeding is filed in the U.S.¹²⁸

Ancillary Proceeding

The recent enactment of Chapter 15 was meant, in part, to alleviate the problems inherent in the U.S. ancillary system. Chapter 15 simplifies the process of recognition, making it an almost automatic process. Moreover, at least in the case of a foreign main proceeding, Chapter 15 provides for certain automatic relief, including the automatic stay. In the case of a foreign nonmain proceeding, the U.S. bankruptcy court has discretion to order relief, including a stay of proceedings. Chapter 15 also mandates cooperation and coordination of U.S. and non-U.S. insolvency proceedings; whereas under prior law the court had discretion to initiate a protocol with the non-US courts, Chapter 15 requires a U.S. court to work with a non-U.S. court to achieve a global reorganisation of the debtor.

Chapter 15, however, creates new issues with respect to cross-border bankruptcy proceedings. Under present law, a foreign representative must commence a Chapter 15 case and have the non-U.S. proceeding recognised prior to applying for relief directly to a U.S. non-bankruptcy court - whereas under prior law, a foreign representative could apply directly to a court in the U.S. for relief, without first commencing an ancillary case. Moreover, the requirement also applies where a foreign representative seeks to commence a plenary case in the U.S. There are also new limitations on a U.S. bankruptcy court's jurisdiction over assets not located within the territorial boundaries of the U.S.

Many of the uncertainties that will be discussed in respect of the present European Insolvency laws are also found in Chapter 15. Most notably, at least for the purposes of this paper, is that the Chapter 15 has adopted the centre-of-main-interests-test, which is presumably the same as that found in the EIR. Therefore, the problems with the definition of centre of main interests that are presently being litigated in the Eurofood case could also arise under U.S. bankruptcy law.

2.3 European Insolvency Proceedings

2.3.1 European Insolvency Initiatives

Preparations for legislation on cross-border insolvencies began in the 1960s when the European Union grew larger and "an obvious need to regulate the insolvencies of entities whose affairs transcend international boundaries"¹²⁹ arose. Requirements for the accurate functioning of the internal market within the territory of the European Community include

¹²⁷ That is, pursuant to § 109(a), the entity must have a place of business or assets in the U.S., may not be a railway or a foreign insurance company, bank, savings bank, cooperative bank, savings and loan association, building and loan association, homestead association, or credit union engaged in such business in the U.S.

¹²⁸ See Westbrook, ABLJ 2002, 22. §305(a)(2) permits a U.S. court to suspend or dismiss a full domestic bankruptcy whenever a foreign proceeding satisfies the requirements of §304. See also Bufford et al., International Insolvency 2001, 7.

¹²⁹ Goldring, Insolvency Law & Practice 2002, 52.

cross-border insolvency proceedings that operate efficiently and effectively.¹³⁰ Since these objectives were hard to achieve on the national level,¹³¹ it was necessary to refer provisions on jurisdiction, recognition and applicable law to the Community law level.¹³² Initiated in 1963 and first presented in 1970,¹³³ the European Union Bankruptcy Convention was the initial attempt for a single bankruptcy law for all Member States.¹³⁴ However, a single bankruptcy law applicable for the Community was not well received;¹³⁵ as a result, the second draft introduced a set of principles of conflict-of-laws.¹³⁶ From this attempt, the European Convention on Insolvency Proceedings 1995 was drafted and then signed by all Member States¹³⁷ except the UK within the set time period¹³⁸ and, hence, it never came into force.¹³⁹

2.3.2 European Council Regulation on Insolvency Proceedings

The adoption of the European Union Regulation on Insolvency Proceedings (EIR)¹⁴⁰ has been a major step forward in the effective and efficient administration of cross-border insolvency proceedings within the European Union (Recital 2). The Regulation came into force on 31 May 2002 and contains the framework for cross border insolvency within the

¹³⁰ See Treaty of Amsterdam, Article 65. See also Carriat, Working Paper 2004, 1. See also Council Regulation (EC) No 1346/2000, Recital 1.

¹³¹ See Ehrlicke, EWS 2002, 101.

¹³² See Moss/Fletcher/Isaak, Oxford 2002, 44.

¹³³ In 1968, the Brussels Convention was signed, yet, with insolvency proceedings deliberately excluded because they were regarded as a special area requiring separate treatment.

Brussels Convention on Jurisdiction and Recognition of Judgements in Civil and Commercial Matters, J.O. L. 299/32 (1972), amended by O.J. L. 304/77 (1978), amended by O.J. L. 304/77 (1978). The Brussels Convention regulates jurisdiction among the Member States and enforcement of civil and commercial judgement within the Community's Member States.

¹³⁴ See Wood, Sweet & Maxwell 1996, 296. See also Kemper, ZIP 2001, 1610.

¹³⁵ See Dawson, Kluwer 2004, 197. The convention "was based on the principles of unity and universality of insolvency proceedings. [However, unity and universality are not interchangeable because] unity of proceedings implies there is only one set of proceedings while universality of insolvency proceedings refers to the recognition of a set of insolvency proceedings in any other jurisdiction." The EIR is an example for both universality and plurality of proceedings. See also Morscher, Manz 2002, 12.

¹³⁶ Wessels, ABIJ 2001, 24: By including conflict-of-law rules, the Regulation goes beyond the scope of the Brussels Convention. See Wood, Sweet & Maxwell 1996, 296. See also Lechner, AJICL 2002, 1012.

¹³⁷ In order for the Insolvency Convention to come into force, all Member States of the EU had to ratify it.

¹³⁸ See Omar, ILP 2001, 135: At the time, this refusal was put down to the beef crisis (mad-cow disease), although the Anglo-Spanish relationships over the status of Gibraltar may well have been another explanation.

¹³⁹ Andrés/Subrá, Butterworths 1995, 619. No state ever formally ratified the Convention.

¹⁴⁰ Council Regulation (EC) No 1346/2000 on insolvency proceedings, Official Journal L 160, 30.6.2000 p. 0001-0013. *Hereinafter* the Regulation; Articles and Recitals without any notation refer to this Regulation. The Regulation consists of two parts. In the first part, the 33 Recitals set out various comments about the need for regulating insolvency proceedings within the internal market and how this should be achieved, often overlapping with or expanding upon the Articles contained in the second part of the Regulation. The Articles are divided into five chapters (dealing with scope, recognition, secondary insolvency proceedings, provision of information to creditors and transitional matters) comprising 47 Articles and three Annexes. The Recital is an important part of the Regulation since the courts of Member States are likely to be guided by its principles and explanations when interpreting the provisions of the various Articles.

The Regulation excludes from its scope insolvency proceedings concerning insurance companies, credit institutions, investment undertakings holding funds and securities for third parties, and collective investment undertakings (Article 1(2)).

European Union¹⁴¹ and is directly effective (Recital 8) within the Member States of the European Union (except Denmark)¹⁴² As the European Union continued to expand in May 2004, the Regulation now also applies to the new Member States.¹⁴³

The European Commission has begun a review of the Regulation, which itself has to be conducted by 2012 to consider proposals for amendment if necessary.¹⁴⁴ Despite its name implying a European approach to resolving cross-border issues, the Regulation does not replace the national insolvency regimes applicable in each state (Recital 15).¹⁴⁵

The objective of the EIR is to introduce uniform conflicts-of-law rules, not substantive rules, for insolvency proceedings and judgements (Recital 12). The Regulation addresses difficulties that arise when an insolvency case involves a number of different European jurisdictions (Recital 11). It designates the state whose courts may open insolvency proceedings in respect to the debtor's centre of main interests, and is an instrument to mediate between potentially competing courts of each Member State in order to determine which country has jurisdiction over the insolvency of a particular debtor (Recital 12).

Proceedings

The insolvency procedure consists of the main proceeding with universal scope but leaves room for open secondary proceedings.¹⁴⁶

The main insolvency proceeding is opened by the court in the Member States where the debtor has the centre of main interests (Recital 13, Article 3(1)), hence *lex concursus* is applicable.¹⁴⁷ Once a main proceeding has been opened in one Member State, further proceedings in other Member States can only be secondary proceedings (Article 3(2)(3)). Secondary proceedings may be opened in one or more other states to protect the diversity of interests arising in the context of cross-border insolvencies (Recital 12). The Regulation principally assists in those cases where a company or business has an establishment (Article 2(h)), or significant assets (Article 2(g)) in more than one Member State. Secondary proceedings may comprise only liquidation or winding up proceedings (Article 3(3)) and

¹⁴¹ See Wessels, Norton Annual Survey of Bankruptcy Law, 2003, 481.

¹⁴² Recital 33: Denmark [...] is not participating in the adoption of this Regulation, and is therefore not bound by it or subject to its application. *Note:* This is in accordance with its position under the Treaty of Amsterdam. Instead, Denmark is expected to introduce rules for determining conflicts of law for cross-border insolvency proceedings.

¹⁴³ The lists of proceedings and liquidators set out in Annexes to the Regulation have been modified by the Treaty of Accession, signed in Athens on April 16, 2003.

¹⁴⁴ See Freshfield, Restructuring and Insolvency Bulletin 2004, 5.

¹⁴⁵ See Van Galen, INSOL 2003, 1. One of the weaknesses of the EIR is that it contains almost no rules harmonising the national insolvency laws of the Member States, although in a number of areas that would have been preferable.

¹⁴⁶ Not only insolvency procedures (Article 1(1)) are available but supplemented by other proceedings (Article 2(a)) in Annex A.

¹⁴⁷ See Lechner, AJICL 2002, 980: Besides *lex concursus* which grants jurisdiction to the country where the insolvency proceeding occurs, there are four other sources of jurisdiction: the law of the creditor's country of residence (*lex domicilii*), the law of the debtor's country of residence (*lex domicilii*), the law of the county where the transaction occurred (*lex loci contractus*), and the law of the country with subject-matter jurisdiction over the assets (*lex situs*).

are limited in scope to the realisation of the debtor's assets within that jurisdiction (Article 27). The law applicable to secondary proceedings is the law of that Member State opening those proceedings (Article 28). To ensure the dominance of the main proceedings, the liquidator (Article 2(b))¹⁴⁸ in such proceedings is given the express opportunity to intervene in the secondary proceedings (Article 37), and even to request a stay of the secondary proceedings if these measures benefit the creditors in the main proceedings (Article 33(2)).

A territorial insolvency proceeding (Article 3(4)) is a proceeding opened prior to the opening of a main proceeding when the main proceeding cannot be opened because of the law of the Member State where the debtor's centre of main interests is situated (Article 3(4(a))), or on request of creditors sited within the jurisdiction of the Member State where the debtor is located or claims arise respectively (Article 3(4(b))).¹⁴⁹ In a territorial or secondary proceeding, the scope of assets is limited to the territory where the debtor is located and the insolvency proceedings are still subject to the law of the Member State in which they are opened (Article 28). In addition, for secondary proceedings only winding up proceedings are available.¹⁵⁰

One of the principal facets of the EIR is that it provides that any judgment opening main or secondary proceedings is to be recognised automatically (Article 17) in other Member States without the need for further formalities, unless the Regulation provides otherwise, or a secondary proceeding has been opened in the jurisdiction in question (Article 16). There is also a residual public policy exception that gives a Member State the discretion to refuse to recognise proceedings brought in another Member State if to do so would be "manifestly contrary to the State's public policy" (Article 26). This provision has already been given its first airing in the Eurofood litigation as described below.

As discussed before, the universal and the territorial model models distinguish international insolvency laws. Despite its universal scope, the EIR is not a single exclusive universal form of insolvency proceeding¹⁵¹ but rather a "compromise between the principle of universality and the principle of territoriality".¹⁵² Although the law of the Member State which is competent to open and conduct insolvency proceedings is applicable in one universal insolvency procedure, the Regulation is rather "a system of recognition and priority throughout the EU for insolvency proceedings".¹⁵³ These distinctions serve the great diversity of national insolvency laws and the specific rights provided under the relevant legislation in dealing with local issues.¹⁵⁴

The centre of main interests is rather new concept and provides some compromise between the 'state of incorporation theory' and 'real seat theory', existing under the national law of

¹⁴⁸ Liquidator is both the administrator of affairs or liquidator of assets divested from the debtor, listed in Annex C.

¹⁴⁹ See also Recital 17: The right to request the opening insolvency proceeding should be limited to local creditors.

¹⁵⁰ Virgòs/Schmit 1996, No. 11.

¹⁵¹ See Becker, ZeuP 2002, 301.

¹⁵² Halén, Master Thesis 2002, 16. See also Carriat, Working Paper 2004, 3. See also Wimmer, ZIP 1998, 951.

¹⁵³ See Kochberg/Crowley, The Lawyer 2004, 23.

¹⁵⁴ See PricewaterhouseCoopers, Introduction, 2002, 1.

the Member States.¹⁵⁵ A company's centre of main interests is described as "the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties" (Recital 13) and "in the case of a company or legal person, the place of the registered office shall be presumed to be the centre of its main interests in the absence of proof to the contrary" (Article 3(1)). However, the Regulation does not provide further criteria for establishing a company's centre of main interests, and consequently the definition "is open to legal challenge".¹⁵⁶ There are also other issues not sufficiently dealt with by the Regulation, e.g. it does not include any provisions on how group insolvencies should be pursued.

Ultimately, the Regulation provides a framework for Member States in cross-border insolvency proceedings where "courts eventually [are] showing deference to each other and cooperation [is] becoming more commonplace",¹⁵⁷ greater control is afforded to the main insolvency proceeding and the appointed liquidator, facilitating one main proceeding over a company's assets instead of a series of competing local liquidation with no one overall in charge.

In addition, the EIR includes some effective remedies for the jurisdiction of cross-border insolvencies, and the UNCITRAL Model Law is built on some key features of the EIR. The Regulation may also serve as a model for future multinational insolvency treaties reaching beyond the territory of the European Union¹⁵⁸ and "is a giant step forward in promoting international cooperation on cross-border insolvency cases".¹⁵⁹ For a proceeding involving a non-EU entity, the EIR applies rules of international jurisdiction and choice-of-law to promote greater efficiency and in order to avoid forum shopping

2.3.3 Italian Insolvency Proceedings

The Italian Bankruptcy Law¹⁶⁰ is based on the Bankruptcy Act 1942.¹⁶¹ At the time of enactment, the most important resource of the Italian economy was still the property of land, public companies were rare.¹⁶² Due to fundamental changes in the Italian economy and financial market,¹⁶³ its bankruptcy proceedings had become inadequate, outdated¹⁶⁴ and were "too bureaucratic, complex and expensive for the creditors";¹⁶⁵ moreover, the length

¹⁵⁵ See Halén, Master Thesis 2002, 1. See also Vogler, Center of Legal Competence 2004, 107. See also Wimmer, ZIP 1998, 982. See also Omar, Ashgate 2004, 130.

¹⁵⁶ Williams, IFLR 2003, 23.

¹⁵⁷ Kochberg/Crowley, The Lawyer 2004, 23.

¹⁵⁸ See Lechner, AJICL 2002, 1024. See also Westbrook, ABJL 2002, 40.

¹⁵⁹ Bufford, Working Draft 2005, 99.

¹⁶⁰ See Houghton/Cooper, Tolley 1984, 175. "All Italian company and bankruptcy law is statutory, case law having no more than a persuasive influence".

¹⁶¹ See Alberti, Kluwer 2003, 381. *Disciplina del Fallimento, del Concordato Preventivo, dell'Amministrazione Controllata e della Liquidazione Coatta Amministrativa* (The Italian Royal Decree No. 267 of March 16, 1942).

¹⁶² See Bruni, Overview Italian Bankruptcy Law 2003, 1. See also Alberti, Kluwer 2003, 383.

¹⁶³ Note: The Italian banking system is still a central banking system with the Bank of Italy having multiples roles as the accounting and audit authority, financial regulatory body, and antitrust power in the financial services industry. Since the Bank of Italy and its Governor Antonio Fazio played an unfavourable role in the takeover of two Italian Bank by foreign competitors, demonstrating that the centralisation of power may be abusive, steps are already being taken to decentralise its power.

¹⁶⁴ See Murphy, IFLR 2004, 17. See also Jorio, Kluwer 2004, 102.

¹⁶⁵ Ghia, The Italian legislation.

of proceedings restrained the Italian economy.¹⁶⁶ For these reasons, the “useless [...] current framework”¹⁶⁷ was under scrutiny by the European Commission. Even with the few partial alterations of the previous years,¹⁶⁸ the proceedings needed further adjustments in order to complete insolvency cases in a timely and stringent matter.

Proceedings

In the first phase the Italian court verifies the extent of the distress. An alternative solution to liquidation can be submitted to the court by all participants (debtor, creditor, and liquidator). The company is allowed to reorganise when it is advantageous to the creditors.¹⁶⁹

The main corporate insolvency proceedings in Italy include:¹⁷⁰

Bankruptcy or judicial liquidation (fallimento)

The aim of this procedure, which applies to all commercial entities,¹⁷¹ is to liquidate the company in order to pay off the creditors. From the day the debtor declares bankruptcy, the debtor loses control, but not ownership over its assets and freedom of movement. All business activities are stopped and payments are suspended immediately to protect the interests of the creditor.¹⁷²

Deed of Arrangement (concordato preventivo)

The Deed of Arrangement is the most common reorganisation procedure where the debtor reaches an agreement with creditors to discharge debts by (part) payment.¹⁷³ The primary goal is to liquidate the debtor while avoiding bankruptcy. If the creditors reject or otherwise fail the agreement, or the debtor fails to meet the conditions, an order of bankruptcy can still be issued by the court.¹⁷⁴

Moratorium (amministrazione controllata)

This procedure is available for a debtor¹⁷⁵ who has temporary liquidity problems but no deficiency of assets. It can be resolved by freezing the payments for all debts for a period of up to two years.¹⁷⁶ The company has six months for drawing up a restructuring plan, which must be approved by the court and agreed upon by at least two thirds of the creditors.¹⁷⁷ This proceeding must not exceed two years and is overseen by a designated judge and court

¹⁶⁶ See Ghia, The Italian Survey. The average length of a bankruptcy proceeding in Italy consists of seven years.

¹⁶⁷ Ghia, The Italian Survey.

¹⁶⁸ See Legislative Decree No. 270 of July 8, 1999 (L.D. 270/1999) “Extraordinary Administration of large corporations in distress”.

¹⁶⁹ See Alberti, Kluwer 2003, 382-383.

¹⁷⁰ See Bruni, Overview Italian Bankruptcy Law 2003, 4. See also Nanni/Greco, Italy 2004, 15/5.

¹⁷¹ With exception: certain public entities (i.e. banks, insurance companies), which are subject to different insolvency procedures, and big companies, which are subject to L.D. 270/1999

¹⁷² See Castellani/Ivone, Italy 2002. See also Monateri, Italian Insolvency Law.

¹⁷³ See Wood, Sweet & Maxwell 1996, 180.

¹⁷⁴ See Castellani/Ivone Italy, 2002. See also Monateri, Italian Insolvency Law.

¹⁷⁵ See Castellani/Ivone, Italy, 2002: The debtor is the only one able to file for the proposal.

¹⁷⁶ See Wood, Sweet & Maxwell 1996, 180.

¹⁷⁷ Only an insolvent debtor may file a petition, creditors do not have the right to initiate this proceeding.

commissioner. Should the restructuring plan not achieve its purpose and the debtor does not recover from its financial distress, the company will be automatically declared bankrupt by the designated judge.¹⁷⁸

Compulsory Winding up (liquidazione coatta amministrativa)

The compulsory liquidation is a specific insolvency procedure for certain financial institutions¹⁷⁹ and where “the debtor’s business is deemed to be of public interest”.¹⁸⁰ It is an alternative to bankruptcy procedures, and the relevant administrative authority,¹⁸¹ depending on the industry the debtor is active in, orders the winding up with the primary purpose of the withdrawal of the debtor from the market and, secondly, the sale and distribution of the debtor’s asset to satisfy the creditors.¹⁸²

Extraordinary Administration (amministrazione straordinaria)

The Extraordinary Administration of large corporations in distress exists in two versions,¹⁸³ and is designed to preserve the value and business of a large corporation as a going concern by reorganising rather than liquidating. However, the insolvent debtor must demonstrate that it is possible for the business to return to profitability through the sale of assets or by providing the sale of one or more businesses.

The procedure consists of the judiciary and the administrative phase. While the former is overseen by the Ministry of Industrial Affairs and deals with assessing the debtor’s status and appointing designated judge and court commissioner, the latter administers the financial recovery until the debtor has successfully complied with the restructuring plan. However, the procedure may end in bankruptcy when the reorganisation fails. The procedure may last up to two years and in case of groups of companies up to five years.¹⁸⁴

The original version, regulated by Legislative Decree No. 270/1999,¹⁸⁵ whereby the eligibility requirements are that the indebted company

- i) must have had a work force of not less than 200 employees for at least a year and
- ii) it must be indebted for a global amount of not less than two thirds of its total assets or of proceeds of sales and services over the last fiscal year.

Special Extraordinary Administration (speciale amministrazione straordinaria)

With the Marzano Decree,¹⁸⁶ the Italian Government supplemented the L.D. 270/1999 which specifically targets large groups.¹⁸⁷

¹⁷⁸ See Castellani/Ivone, Italy 2002. See also Albert, Kluwer 2003, 381.

¹⁷⁹ See Wood, Sweet & Maxwell 1996, 219. Compulsory administration is only available for public companies, financial institutions, insurance companies and credit institutions, and is not compatible with another proceeding, but it is irrelevant if the companies belong to the private or public sector.

¹⁸⁰ Monateri, Italian Insolvency Law.

¹⁸¹ See Castellani/Ivone, Italy 2002. See also Wood, Sweet & Maxwell, 219: The compulsory administrative liquidation is an administrative, not a judicial procedure.

¹⁸² However, it is also possible for the debtor to file for a declaration of insolvency.

¹⁸³ See Bruni, Overview Italian Bankruptcy Law 2003, 1.

¹⁸⁴ See Wood, Sweet & Maxwell 1996, 221.

¹⁸⁵ Italian Legislative Decree No. 270 of July 8, 1999 (L.D. 270/1999).

The threshold of eligibility has been raised, in fact

- i) the company work force must be of at least 1,000 employees, inclusive of those admitted to redundancy measures
- ii) the overall indebtedness, which now encompasses debts deriving from bonds and guarantees issued to third parties (a problem which has seriously affected the stability of Parmalat) has been raised to no less than 1 billion Euro.

These rules tried to avoid any interruption of the business of large insolvent companies by admitting that these companies are able to promptly present an economic and financial restructuring plan, following an administrative order. Therefore, the order of the two phases is reversed. After the Ministry has admitted and approved the reorganisation plan, and appointed extraordinary commissioner,¹⁸⁸ the judiciary phase begins when the competent court is notified by the company's application and the Ministry's order together with the petition to declare insolvency.

Only bankruptcy and compulsory administrative winding up are available as secondary proceedings under the EIR.

Section 9 of the Bankruptcy Act 1942 offers ground for international competence of a foreign insolvency proceeding (*competenza giurisdizionale*).¹⁸⁹ This section also includes the recognition of international treaties.¹⁹⁰

2.3.3.1 Marzano Decree (*Decreto Legge Nr 347 from December 23, 2003*)

The Marzano Decree was approved by the Italian Government on December 23, 2003. It was tested for compliance with EU rules on state aid rules and prohibiting public subsidies by the European Commission.¹⁹¹ The urgency of the Decree originated from the default of Parmalat SpA, which had applied for extraordinary administration, as discussed above. These procedures are "often politically and administratively driven to avoid job losses or economic instability".¹⁹²

The Marzano Decree gave consolidated powers to the Extraordinary Commissioner, Enrico Bondi,¹⁹³ and established a Surveillance Committee (*Comitato di Sorveglianza*), composed of a small number of creditors, which, together with Mr. Bondi, crafted a Reorganisation

¹⁸⁶ Italian Legislative Decree No. 347 of December 23, 2003 (L.D. 347/2003), updated on February 19, 2004, No. 39 (Law 39/2004), modified on May 3, 2004, No. 42 (Law. 119/2004). *Herewithafter* Marzano Decree.

¹⁸⁷ Italian Legislative Decree No. 270 of July 8, 1999 (L.D. 270/1999).

¹⁸⁸ With the administrative phase where the company files directly with the Ministry of Industrial Affairs prior to the judiciary phase, the insolvency procedure is bypassing the bankruptcy courts. The minister can appoint the extraordinary commissioner immediately.

¹⁸⁹ See Laut, Duncker und Humblot 1997, 228.

¹⁹⁰ See Cooper/Jarvis, John Wiley & Sons 1996, 68. International treaties include the Rome Treaty between France and Italy (1930) or U.K. and Italy (1964.).

¹⁹¹ See Eubusiness Ltd., Brussels studies post-Parmalat Italian bankruptcy law 2004. See also Murphy, IFLR 2004, 17.

¹⁹² See Laughton, Recovery 2004, 17.

¹⁹³ Note that under the previous decree, the extraordinary commissioner would have been appointed after the court had appointed one or three interim judicial commissioners who would file a report regarding the reasons for insolvency and prospects for restructuring and would have to share his power amongst the three interim judicial commissioners.

Plan (*Piano di Risanamento*). The restructuring proceeding is subject to continuing supervision by the Ministry of Industrial Affairs.¹⁹⁴ By appointing the Extraordinary Commissioner immediately, the Marzano Decree establishes a quicker and more efficient system of bankruptcy protection.¹⁹⁵ In fact, the Ministry had already admitted Parmalat SpA to the extraordinary administration procedure, thus clearly by-passing the Court of Parma which was confined to acknowledging the insolvency.

On January 12, 2004 the European Commission received formal notification of the Marzano Decree. Later that month Italy obtained preliminary approval from the European Commission since the European Commission spokesman said his agency's preliminary opinion is that Italy's new bankruptcy decree does not violate EU jurisdiction.¹⁹⁶

2.3.3.2 Position of the Italian Government

In Italy, an estimated 99 % of companies are family controlled. Truly independent directors are rather rare, "even at listed Italian companies, external scrutiny tends to be casual, and conflicts of interest are rife".¹⁹⁷ These conflicts of interest are also displayed in national politics. While the Italian Government had not been able to agree on guidelines for the reform on insolvency procedures before, in response to the Parmalat collapse,¹⁹⁸ however, the government quickly passed the Marzano Decree.

There is another obstacle in Italy concerning the financial markets.¹⁹⁹ So far, the Italian financial market has failed to adapt to international standards of transparency, credibility and good corporate governance. Since only a few of Italian companies have a credit rating,²⁰⁰ investors are forced to base their decision on the company's brand, instead of the company's credit, which heightens credit risk.²⁰¹ The Parmalat failure also put the Italian accounting system under scrutiny,²⁰² which led to the demand for a new regulatory board that oversees the financial market and its participants.

¹⁹⁴ See <http://www.bankrupt.com/parmalat.txt>, 16.12.2005.

¹⁹⁵ See Murphy, IFLR 2004, 17: However, all companies not covered by the prerequisites of the law will still be adjudicated under the old framework.

¹⁹⁶ See Eubusiness Ltd. ,Brussels clears post-Parmalat Italian bankruptcy law 2004.

¹⁹⁷ Gumble, Fortune 2004, 20.

¹⁹⁸ See Carruth, TIL 2004, 361. See also Gromek Broc/Parry, Kluwer 2004, 1. In spite of the economic importance [...] insolvency laws of some Member States have tended to stagnate over time, with legislature failing to ensure that their laws adapt to modern society [...]. In many cases reforms will not be made until the emergence of some major stimulus exposing weaknesses in the laws“.

¹⁹⁹ See Murphy, IFLR 2004, 17: Italy has long been one of Western Europe's riskiest and most opaque markets.

²⁰⁰ During a credit rating process, the rating agency may have unlimited access to all information of the company. A rating displays the probability of default of a company's debt, and is reviewed regularly to track the progress of the quality of debt (e.g. bonds). When the company itself does not have or want a rating, their bonds may be rated separately in order to place them on the market. A bond rating is cheaper for the company but signifies a greater risk for the investor who is compensated with a higher return on his investment.

²⁰¹ See Murphy, IFLR 2004, 17. See also Hamilton 2005.

²⁰² Until the end of 2003, a company's total amount of paid in share capital was the limiting amount for issuing bonds, the amendments previously made limit the amount to the share capital plus reserves. However, companies can circumvent the old and the new limitation by issuing bonds through subsidiaries incorporated in tax-advantaged foreign jurisdictions, but guaranteed by the parent company (e.g. BONLAT Financing Corporation). In Italy, there is no holding period on bonds for institutional investors

2.3.3.3 Reform Efforts

In 2002, a government commission made some key recommendations on how the Italian bankruptcy law should be reformed,²⁰³ bringing it closer to market needs by giving more consideration to creditors' interests and decreasing the number, time and costs of judicial proceedings.²⁰⁴ The commission submitted the proposal to the Council of Ministers which introduced important amendments to the Italian Bankruptcy Law in May 2005.²⁰⁵ Some of the main obstacles are the internal judicial aspects,²⁰⁶ the specific right and duty of information to the creditors and, more importantly, communication and coordination in cross-border cases between the court, judges and commissioners. The key amendments are a simplification of insolvency proceedings²⁰⁷ and an encouragement of out-of-court settlements by allowing creditors and companies to find a more flexible basis to settle their difficulties,²⁰⁸ even before the "crisis becomes a full-blown insolvency".²⁰⁹

2.3.4 Irish Insolvency Proceedings

For historical reasons, the Irish Insolvency²¹⁰ Law is based on statutes of the United Kingdom,²¹¹ and Ireland is therefore a common law jurisdiction. The 1908 Act included provisions for liquidating insolvent companies, whereby the debtor is wound up by a liquidator and its property is distributed to the creditors. The first major modification came with the enactment of the Companies Act in 1963, which altered the 1908 Act. The law then allowed for a fresh start after a business failure as well as a scheme of arrangement. However, as with previous legislation, the 1963 Act focused on winding up instead of a possible rescue of an insolvent company. The 1990 Companies Act introduced the examinership, which was reformed by the Companies Act 1999.

Three main corporate insolvency proceedings can be applied to insolvent companies, however, only the first two of them can be main insolvency proceedings under the EIR:

(compared to Rule 144 U.S. Law where it is illegal to sell unregistered bonds in the public market for one year after purchase). Most of Italy's unrated companies sell their bonds to institutional investors overseas or the EUROMARKET.

²⁰³ See Castellani/Ivone, Italy 2002, 10. See also Ghia, The Italian Survey.

²⁰⁴ See Jorio, Kluwer 2004, 110-113.

²⁰⁵ See Tersilla, Reform of Italian Bankruptcy Law. Italian Law Decree No. 35/2005 of May 14, 2005 (Law 80/2005).

²⁰⁶ Since the same judge is responsible for the various stages of the proceeding, thus leading to faster decisions and outcomes, there is a deep uncertainty in what role the judge actually plays in the proceedings. However, the court requires retaining its jurisdiction in rather minor aspects of a proceeding, therefore slowing down and prolonging the procedures.

²⁰⁷ See Bruni, Overview Italian Bankruptcy Law 2003, 4. See also Nanni/Greco, Italy 2004, 15/39. The government should reduce the existing proceedings from five to two: a crisis composition proceeding (procedura di composizione concordata della crisi), which is aimed at reorganising the corporation based on a restructuring plan with continuing management under court control, and an insolvency proceeding (procedura di liquidazione concorsuale), which liquidates the company's assets and activities.

²⁰⁸ See De Tomas, Bankruptcy Reform 2003, 36.

²⁰⁹ See Tersilla, Reform of Italian Bankruptcy Law.

²¹⁰ In Irish law, the term bankruptcy is reserved to private individuals.

²¹¹ Ireland declared his independence in 1921.

Liquidations

After the affairs of a company have been wound up by a liquidator,²¹² the company will be dissolved and its separate legal personality will terminate. The liquidation procedure can be divided into voluntary liquidation²¹³ and compulsory liquidation.²¹⁴ The main distinction between voluntary and compulsory liquidation lies with the entity that has control of the process. In a voluntary liquidation it is the members of the board of directors that have control while in the case of a compulsory liquidation it is the court.

Examinership

The aim of the procedure is to facilitate the survival of a company as going concern. The protection of the court period begins once the petition is presented and it lasts until the court orders it to end when a scheme of arrangements comes into operation.²¹⁵ Within 21 days of appointment, the examiner is obliged to present his first report in whether he is convinced about the company's capability to survive. If the examiner is of the opinion that the company can be rescued, a second report is compiled, which will contain the scheme of arrangement. Once the scheme of arrangement is approved and confirmed by the court and the requisite number of creditors and members has voted in favour of it, it will become binding on the creditors and members and will take effect within 21 days.²¹⁶

Receivership

Where a company owes money under a debenture which is secured by a charge over all or part of the company's assets, the debenture holder can appoint an out-of-court a receiver over the company's assets if the issuer of the debenture commits an event of default. The receiver becomes the agent of the company. The function of the receiver appointed by a debenture holder is to take possession of the assets, subject them to the debenture holder's charge, and then realise those assets in order to discharge the sum due under the debenture. If the court appoints the receiver, he functions as the trustee of the assets under his control. The appointment of the receiver does not affect the legal status of the company and, therefore, does not prevent directors from continuing to exercise their powers and duties in respect of the assets and liabilities other than those assets now controlled by the receiver.

²¹² The liquidator assumes the functions and authorities which the directors of the company previously had. The general functions are to wind up the company, to inquire into its affairs, to realize and distribute its assets and pay its debts.

²¹³ §251(1) Company Act 1963 sets out three circumstances in which a company may be voluntarily liquidated. The first two categories refer to a members' voluntary winding up and the third category relates to a creditors winding up. The basic difference is that in a members' voluntary winding up, the company is solvent and the creditors' debts are paid in full, whilst in a creditors' voluntary liquidation the company is insolvent and not in a position to pay its debts as they fall due. It should be noted, however, that the powers and the duties of the liquidator are similar in both categories of voluntary liquidations. The processes differ in the manner in which they are set in motion and in terms of to whom the liquidator is accountable.

²¹⁴ A compulsory liquidation is commenced by order of the High Court in response to a petition. Court supervision is an integral part of this category of liquidation as the liquidation is carried out by the court acting through the "official liquidator". The two most grounds upon which a petition may be presented are that a company is unable to pay its debts, and the court has the opinion it is just and equitable that the company should be wound up.

²¹⁵ See Cox, Ireland 2004, 14/6.

²¹⁶ See Cox, Ireland 2004, 14/7.

The only types of proceedings which are available as secondary proceedings are the compulsory liquidation and creditors' voluntary winding up.²¹⁷ For cross-border cases outside the EU, §250 of the Companies Act provides the basis for recognising foreign court orders and cooperation with other jurisdictions.²¹⁸

2.3.5 Differences in Irish and Italian Insolvency Proceedings

In line with English law, the Irish Insolvency law used to be extremely pro-debtor. With the Company Act 1990, however, the law moved towards being more pro-creditor, adopting a mild rehabilitation statute.²¹⁹

The Italian law adopted German bankruptcy ideas in 1942, moving from being pro-debtor "as a result of the Napoleonic conquest"²²⁰ to being pro-creditor. This approach was later overlaid with an extreme pro-debtor rescue statute in 1979 when Italy introduced the extraordinary administration for large enterprises which dispensed with the courts and put the politicians in charge.²²¹ The Italian system, while not really being pro-debtor, is harmful to the interests of the creditors, and is viewed as the least-creditor friendly insolvency jurisdiction in Europe.²²² One of the major inefficiencies of the Italian system include the timeframe: a typical Italian bankruptcy proceeding lasts for years and, at least prior to the passage of special laws with respect to the Parmalat case, did not include tools like the automatic stay. Under the Italian bankruptcy law there is also no way to bind dissenting creditors to a plan of liquidation or reorganisation.

There are some overlapping features as both states allow insolvency set-offs prior to insolvency. The distinction between the pro-debtor and pro-creditor approach and Italy's reputation concerning creditor rights, however, may be one of the reasons why the Extraordinary Commissioner of the Parmalat proceeding wants the subsidiary Eurofood to be included in the Italian reorganisation. However, Bank of America, Eurofoods' largest creditor, did not want to get caught up in the Italian proceeding, fearing that the length of time and lack of certainty with respect to the relief available would lessen their recovery, and therefore petitioned in Ireland for Eurofoods' liquidation.

²¹⁷ See EIR, Annex B.

²¹⁸ See Cox, Ireland 2004, 14/29.

²¹⁹ See Wood, Sweet & Maxwell 1996, 4.

²²⁰ Wood, Sweet & Maxwell 1996, 8.

²²¹ See Wood, Sweet & Maxwell 1996, 5. See also Jorio, Kluwer 2004, 108-109.

²²² See Murphy, IFLR 2004, 17. See also Hamilton, 2005.

3 FACTS ON THE PARMALAT GROUP

3.1 Company Background on the Parmalat Group

3.1.1 Origin of Parmalat Finanziaria SpA

The origins of the Parmalat Group²²³ date back to 1961 when Calisto Tanzi created Dietalat Srl to enter the market for pasteurised milk, which, at that time, was dominated by public dairies. Seven years later, Dietalat Srl changed its name to Parmalat Srl.²²⁴ In 1973, Parmalat Srl became a joint stock company incorporated under Italian Law (Società per Azioni), Parmalat SpA, and a year later, the company went international, first with operations in Brazil, later in Venezuela and Ecuador.²²⁵

Parmalat Finanziaria SpA is a joint stock company incorporated under Italian law on June 24, 1972. The company is listed on Telematico (Italian Exchange). In 1990, Finanziaria Centro Nord (holding company of the Tanzi family) acquired 75% of Parmalat SpA's capital, which then subsequently renamed itself to Parmalat Finanziaria SpA. Three years later, Parmalat Finanziaria SpA acquired a further 20.54% Parmalat SpA shares from the Tanzi family, raising its participation to 95.54% of the company's voting capital. The ownership reached 100% by the end of 1994. Therefore, Parmalat Finanziaria SpA acts as the holding company of the Parmalat Group with its principal subsidiary being Parmalat SpA, which is the main operating company in the Italian market and, moreover, the holding company and co-ordinator for the Group's commercial subsidiaries. Parmalat SpA guarantees many of the holding company's debt obligations.²²⁶

Parmalat Finanziaria SpA is controlled by La Coloniale SpA, which holds 50.68% of its shares. La Coloniale SpA is the holding company of the Tanzi family, founders of the Parmalat Group. The remaining 49.32% of capital of Parmalat Finanziaria SpA are listed on Telematico (Italian Exchange).

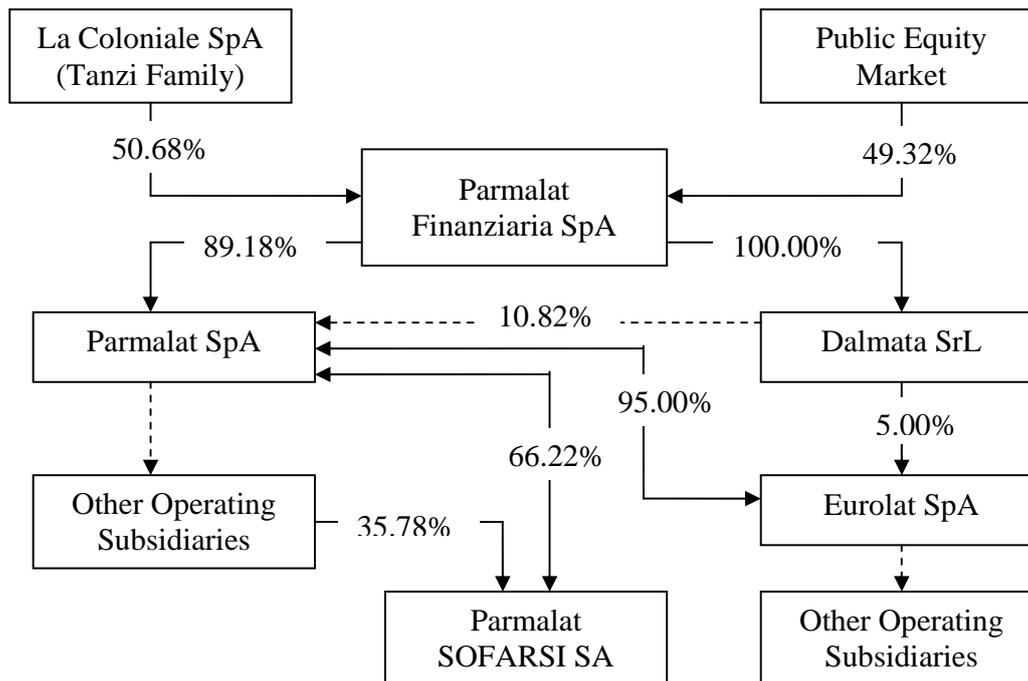
The illustration below shows the complex structure of the Parmalat Group.

²²³ The Parmalat Group includes all entities; the most important one being the holding company Parmalat Finanziaria SpA and the operating subsidiary Parmalat SpA. The Corporate Structure is shown in Illustration 1, p 29.

²²⁴ See <http://www.bankrupt.com/parmalat.txt>, 16.12.2005.

²²⁵ See Ramonet, *Le Monde Diplomatique* 2004, <http://www.mondediplo.com/2004/02/01ramonet>, 13.01.2006.

²²⁶ See <http://www.bankrupt.com/parmalat.txt>, 16.12.2005.



Own illustration with reference to <http://www.bankrupt.com/parmalat.txt>, 16.12.2005.

3.1.2 Overview of the Corporate Structure

The corporate structure of the Parmalat Finanziaria SpA is complex and involves hundreds of affiliated entities; however this paper will only focus on the Italian parent company and the interdependencies between its subsidiaries in Ireland and the United States. From 1974 on, Parmalat extended its network of entities internationally into countries with either a simple tax system (i.e. Luxembourg) or by using tax havens (i.e. Cayman Islands).²²⁷ The structure emphasised a series of back-to-back loans through Cayman Island banks, as well as cash rising by issuing securities for companies that only existed on paper, and also took advantage of a network of conspirators in Italian politics and in international financial markets.²²⁸ These developments were supported by major foreign banks (Bank of America, Chase, AMRO, UBD and Deutsche Bank),²²⁹ that assisted Parmalat Finanziaria SpA in issuing securities (i.e. bonds, collateralised debt obligations) without questioning the purpose or examining more closely the financial situation of the company.²³⁰

3.1.3 Business Description and Principal Markets

Until the beginning of 1997, Parmalat SpA was Parmalat Finanziaria SpA's only operating subsidiary. However, as of December 2002, the Parmalat Group operated 139 plants in 31 countries on six continents and had a workforce of over 36,000 employees in total. Generating 7.6 billion euros in annual revenues and with a world market share of 0.59% in the same year, the Group was the 14th largest packed food company in the world and Italy's

²²⁷ See Ramonet, *Le Monde Diplomatique* 2004, <http://www.mondediplo.com/2004/02/01ramonet>, 13.01.2006.

²²⁸ See Bruni, *Collapse of Parmalat*, 2004.

²²⁹ See Stickel, *CLT* 2004, 58.

²³⁰ See Bruni, *Collapse of Parmalat* 2004.

8th-largest business.²³¹ Parmalat SpA's core business operations were divided into four main divisions:²³² Vegetable Products (9%), Fresh Products (9%), Bakery Products (23%) and Milk Products (59%). Before filing for bankruptcy and selling its foreign subsidiaries, the company operated worldwide to ensure expeditious supply to satisfy demand.²³³ The Group's operations were grouped into four geographical areas, accordingly to the size of the market: Europe (41%), South America (26%), North and Central America (26%) and Rest of the World (7%).²³⁴

3.2 Situational Overview December 2003

In early 2003, the difficulties of Parmalat Finanziaria SpA became obvious for the first time. Parmalat had attempted to sell as much as €500 million of bonds. As a result of unfavourable market conditions, Parmalat was forced to abandon the sale. However, the circumstances surrounding the sale raised questions about the ability of the company to pay back its existing debts.²³⁵

After Italian fund managers asked to meet with company executives to discuss accounts on March 6, Chief Financial Officer Fausto Tonna resigned on March 28, and was replaced by Alberto Ferraris.²³⁶ The company's shares subsequently fell after questions were raised regarding other transactions and discovery of funds of €500 million with the Epicurum fund based in the Cayman Islands.²³⁷ Three days later, CFO Alberto Ferraris resigned and was replaced by Luciano Del Soldato. By this time, however, the financial difficulties of the company had become obvious.

Parmalat SpA was not able to raise cash from the Epicurum fund to pay back interest on an outstanding Parmalat Finance Corporation bond,²³⁸ despite seemingly having sufficient liquidity on its balance sheet (€4.2 billion).²³⁹ In response, Standard & Poor's decreased Parmalat debt to "junk bond" level.²⁴⁰ The company missed the payment due date but later redeemed the bond, with funds from Italian tax authorities.²⁴¹

On December 15, 2003, Mr. Tanzi resigned as chairman and chief executive officer of Parmalat Finanziaria SpA and was replaced by Mr. Bondi who had just been called in two days earlier as a consultant to help the company out of its crisis when CFO Luciano Del Soldato quit. Four days later, Bank of America denied the authenticity of a document for

²³¹ See Houlihan, Lokey, Howard & Zukin, Parmalat, 2004.

²³² Figures as per 31.12.2002, Homepage Parmalat <http://www.parmalat.com>, 14.12.2005.

²³³ See <http://www.bankrupt.com/parmalat.txt>, 16.12.2005.

²³⁴ See <http://www.bankrupt.com/parmalat.txt>, 16.12.2005.

²³⁵ See BBC News, Parmalat Timeline 2003, 26.01.2004, <http://news.bbc.co.uk/1/hi/business/3369079.stm>, 16.12.2005.

²³⁶ See Houlihan, Lokey, Howard & Zukin, Parmalat 2004.

²³⁷ See See Ramonet, Le Monde Diplomatique 2004, <http://www.mondediplo.com/2004/02/01ramonet>, 13.01.2006

²³⁸ Parmalat Finance Corp. B.V. identified with No. 8/6/200-8712/2003, 6% coupon.

²³⁹ See CNN Parmalat to decide on bankruptcy, 22.12.2003, <http://www.cnn.com/2003/BUSINESS/12/22/italy.parmalat/index.html>, 17.12.2005.

²⁴⁰ S&P cut off Parmalat bonds from a B+/B level to a CC (concerning long-term issues).

²⁴¹ See Houlihan, Lokey, Howard & Zukin, Parmalat 2004.

the Cayman Islands-based Bonlat's €3.95 billion bank account.²⁴² Standard & Poor decreased subsequently Parmalat bonds to rating category D.²⁴³

On December 21, the company's shares dropped to €0.11 and, on December 22, were suspended from trading by the Italian Exchange.²⁴⁴ A put option requiring Parmalat Finanziaria SpA to acquire 18.18% of its Brazilian subsidiary matured and negotiations to delay payment (US\$400 million) failed.²⁴⁵ Thus, Parmalat was in dire financial straits.

The boards of directors of Parmalat Finanziaria SpA and Parmalat SpA met in Collecchio on December 23. At the same time, an Extraordinary Shareholder Meeting of Parmalat SpA was called. Both meetings agreed to follow either the Legislative Decree 270/99,²⁴⁶ or the anticipated procedure foreseen under the Marzano Decree,²⁴⁷ approved the same day by the Italian Cabinet, which was tailor-made by legislation to cope with the financial disaster of the Parmalat Group and companies of similar size by amending the Italian bankruptcy law.²⁴⁸

Parmalat SpA filed a request for protection from creditors under the extraordinary administration procedure on December 24.²⁴⁹ Enrico Bondi was appointed Extraordinary Commissioner. At the end of December, Mr. Tanzi admitted that the hole in Parmalat's accounts was about €8 billion but denied any responsibility for wrongdoing although he admitted siphoning off about €500 million from other Parmalat-owned companies. Meanwhile, Parmalat shares and bonds were suspended from trading indefinitely by the Italian Exchange until a restructuring plan had been formed, and the US Securities and Exchange Commission (SEC) charged Parmalat with securities fraud for filing misleading financial statements (cover: €1.5 billion).²⁵⁰

In the first week of 2004, Parmalat's new management met with creditor banks to ask for money to keep the Parmalat group operating. By that time, the Cayman Islands-based Parmalat Capital Finance was declared to be in default. The Cayman Islands Government authorities reported a few days later that Parmalat had eight off-shore companies based on the Cayman Islands. Meanwhile, various investigations into accounting firms as well as Italian and foreign banks were launched.²⁵¹

²⁴² See Ramonet, *Le Monde Diplomatique* 2004, <http://www.mondediplo.com/2004/02/01ramonet>, 13.01.2006. When Mr. Bondi searched for liquidity, he scrutinised all existing documents stating liquidity in accounts both in Italy and abroad. According to these documents, Bonlat was having €3.95 billion in bank accounts with Bank of America on the Cayman Islands.

²⁴³ Rating D represent a real state of insolvency.

²⁴⁴ See Fritz, *Orac* 2004, 27.

²⁴⁵ See CNN News, *Parmalat to decide on bankruptcy*, 22.12.2003, <http://www.cnn.com/2003/BUSINESS/12/22/italy.parmalat/index.html>, 17.12.2005.

²⁴⁶ Italian Legislative Decree No. 270 of July 8, 1999 (L.D. 270/1999).

²⁴⁷ Italian Legislative Decree No. 347 of December 23, 2003 (L.D. 347/2003), updated on February 19, 2004, No. 39 (Law 39/2004), modified on May 3, 2004, No. 42 (Law. 119/2004).

²⁴⁸ See *Parmalat Finanziaria SpA*, Press Release, 23.12.2003. See also Marzano Decree 347/2003, Article 3(3).

²⁴⁹ See *Parmalat Finanziaria SpA*, Press Release, 24.12.2003.

²⁵⁰ See Houlihan, Lokey, Howard & Zukin, *Parmalat 2004*. See *Securities and Exchange Commission v. Parmalat Finanziaria SpA*, 03 CV 10266 (PKC) (S.D.N.Y.).

²⁵¹ See Houlihan, Lokey, Howard & Zukin, *Parmalat 2004*.

Mr. Bondi reported that he would seek €150 million Debtor-in-Possession Financing (DIP) from banks in order to ensure a source of working capital during reorganisation and enable the company to fulfil purchase orders, and to expand and accelerate production.²⁵²

On January 8, Parmalat Finanziaria SpA, Eurolat SpA and Lactis SpA were declared insolvent by the Parma Court's Bankruptcy Section (Tribunale di Parma, Sezione Fallimentare).²⁵³ On January 24, the controlling company, Coloniale SpA was declared insolvent. Two days later, the auditors determined that, as of September 2003, Parmalat had debts of €4.3 billion, almost eight times of what the management admitted at the time. Nine days later, the Court in Parma declared another seven foreign Parmalat companies insolvent.²⁵⁴

On February 24, the American subsidiaries Farmland Dairies LLC, Parmalat USA and Milk Products of Alabama LLC filed for Chapter 11 status under the American Bankruptcy Code in order to avoid any major deterioration in the operating and financial position of the businesses concerned.²⁵⁵

3.3 Review of Important Events from the Parmalat SpA Insolvency Filing until Today

In Italy, the task of the Extraordinary Commissioner is to achieve the Reorganisation Plan in a timely and stringent manner as well as to recover as much cash for the creditors as possible.²⁵⁶ The objective of the Reorganisation Plan was to concentrate on Parmalat's core business in Europe as well as securing the survival of the company by selling its subsidiaries abroad.²⁵⁷

In March, Italian banks finalised the financing of €105.8 million for duration of twelve months, securing the current operating business.²⁵⁸ The Extraordinary Commissioner started suing various banks in June 2004, among them Deutsche Bank (\$20 million), Citigroup (\$10 billion), UBS (\$350 million), Bank of America, Credit Suisse First Boston International (\$300 million), and accountants Grant Thornton and Deloitte Touche Tohmatsu for their role in overlooking the endemic fraud and thereby contributing to the bankruptcy. The extraordinary amount demanded from Citigroup was due to the allegations that Citigroup had manipulated Parmalat's true financial picture and therefore helped looting the company.²⁵⁹ Citigroup allegedly helped to set up joint ventures that disguised

²⁵² See Houlihan, Lokey, Howard & Zukin, Parmalat 2004.

²⁵³ See Parmalat Finanziaria SpA, Press Release, 08.01.2004.

²⁵⁴ Five companies from the Netherlands and two from Luxembourg. The extraordinary commissioner wanted to avoid the risk of filing foreign procedures without any coordination with the Italian main proceeding.

²⁵⁵ See Parmalat Finanziaria SpA, Press Release, 24.02.2004.

²⁵⁶ Dumiak, U.S. Banker 2004, 14.

²⁵⁷ Parmalat Finanziaria SpA, Press Release, 24.02.2004. *Note* that Parmalat Finanziaria SpA sold its participation in Thailand in April 2004. Parmalat de México S.A. de C.V. signed agreements with Grupo Industrial Lala S.A. de C.V. for the sale of its industrial operations on July 19, 2004. Parmalat discharged the USA Bakery Division (Mother's Cake & Cookies, Archway Cookies and three production units in Canada) in January 2005, and Parmalat Uruguay was sold in February 2005.

²⁵⁸ See Parmalat Finanziaria SpA, Press Release, 04.03.2004.

²⁵⁹ See Stickel, CLT 2004, 58.

Parmalat's debt, making it look like it had purchased assets which, in fact, never existed; such joint ventures were called "Buconero" – the Italian word for black hole.²⁶⁰

The Reorganisation Plan as presented by the Mr. Bondi was approved by the Minister of Industrial Affairs on July 23, 2004. Three days later the plan was filed at the Court of Parma.²⁶¹ With all submissions of the creditors, the judge had until September 18, 2004 to either approve or modify the reorganisation plan.

In November 2004, Parmalat Finanziaria SpA announced that the claims by creditors (mainly Italian banks) will become part of a debt for equity swap. The Plan, already approved by the Ministry of Industry, was reviewed by a judge in Parma who also approved it.²⁶²

At the beginning of 2005, Parmalat announced its emphasis on returning to the Italian Exchange as soon as possible. In February, the creditors voted for the Reorganisation Plan and a debt swap for shares of the new Parmalat Company, which is a criterion for going public again.²⁶³ Advantageous for Mr. Bondi was the fact that the majority of the banks were seeking to return to normality. Therefore, they were willing to settle the charges pressed against them by Bondi in connection with the irregularities out of court.²⁶⁴ On March 1, 2005, corporate capital was increased to serve the debt/equity swap for unsecured creditors.²⁶⁵ Mr. Bondi accepted the settlement proposal with Morgan Stanley on June, 18 2005 for an amount of €155 million.²⁶⁶

Following a settlement with the three U.S. companies (Farmland Dairies LLC, Parmalat USA and Milk Products of Alabama LLC) in Chapter 11 in June 2005,²⁶⁷ these companies have been permanently removed from the Parmalat Group in August 2005.²⁶⁸

²⁶⁰ See Stickel, CLT 2004, 59.

²⁶¹ See Parmalat Finanziaria SpA, Press Release, 27.06.2004.

²⁶² See PPL, Parmalat Swap 2004.

²⁶³ See Fromm, FTD, 29.12.2004, 18.

²⁶⁴ See Fromm, FTD, 11.01.2005, 19.

²⁶⁵ See Tersilla, Recent Developments in the Parmalat Insolvency 2005, 4.

²⁶⁶ See Parmalat Finanziaria SpA, Press Release, 23.06.2005.

²⁶⁷ See Parmalat Finanziaria SpA, Press Release, 01.06.2005.

²⁶⁸ See Parmalat Finanziaria SpA, Press Release, 31.08.2005. The former U.S. entities are no longer included in the scope of consolidation.

4 THE PARMALAT CASE UNDER CONSIDERATION OF AMERICAN AND EUROPEAN INSOLVENCY PROCEEDINGS

4.1 Applicability of the American Bankruptcy Code to Parmalat Subsidiaries

As to the U.S. proceedings in the Parmalat bankruptcy, the U.S. court was able to create an efficient mechanism for dealing with certain cross-border issues. The U.S. bankruptcy court granted ancillary bankruptcy proceedings with respect to the Italian bankruptcy cases, dismissed ancillary proceedings that would have wasted the debtor entities' assets and was able to successfully administer the insolvency proceedings of the U.S. subsidiaries without interference from the foreign court.²⁶⁹ This serves as a stark contrast to the Eurofood case, which is discussed later.

4.1.1 United States Ancillary Proceedings

Parmalat Finanziaria SpA had several affiliates on the Cayman Islands for financial funding and tax purposes.²⁷⁰ On January 20, 2004, Gordon I. MacRae and James Cleaver, the Joint Provisional Liquidators of the Parmalat's Cayman Island affiliates, Parmalat Capital Finance Limited, Food Holdings Limited and Dairy Holdings Limited, filed petitions seeking to commence ancillary bankruptcy proceedings.²⁷¹ The reason for the proceedings was to seek injunctive relief in the U.S. and the turnover of property located in the U.S., if any existed.²⁷² One day later, the Bankruptcy Court S.D.N.Y. issued a temporary restraining order. The order enjoined parties from taking actions against the Parmalat affiliates or their property in the U.S. before a further hearing for a preliminary injunction took place on request of the Cayman Liquidators. On January 28, 2004, Mr. Bondi, as the Extraordinary Commissioner on behalf of Parmalat's creditors, questioned the need and costs of these ancillary proceedings. In his opinion, the ancillary proceedings would detract his global investigatory and restructuring efforts. The Bankruptcy Court agreed with Mr. Bondi and dismissed the ancillary proceedings for the Cayman Island affiliates.²⁷³

²⁶⁹ It should be noted that at the time of the US Parmalat proceedings, Chapter 15 had not been enacted. It remains to be seen whether, under Chapter 15, a US bankruptcy court would have the freedom to craft relief that is in the best interests of a multinational debtor.

²⁷⁰ Cayman Islands-based Bonlat's €3.95 billion non-existent bank account at Bank of America arouses suspicion of fraud and the stage of insolvency of Parmalat Finanziaria SpA in December 2003 in Italy. (See 3.2 Situational Overview December 2003).

Note A discussion concerning the reasons for incorporating subsidiaries in countries advantageous for tax purposes and special financial transactions, as well as the consequences in case of bankruptcy proceedings are discussed later in this paper.

²⁷¹ *In re* Petition of Gordon I Macrae and James Cleaver as Joint Provisional Liquidators of Parmalat Capital Finance Limited, et al., 04-10362 (RDD) (S.D.N.Y. 2004), Dairy Holdings Limited, 04-10363 (RDD) (S.D.N.Y. 2004), and Food Holdings Limited: Case No. 04-10364 (RDD) (S.D.N.Y. 2004). See also Mays, *INSOL World* 2004, 23. The rules of the Grand Court are substantially based on the English Rules of the Supreme Court and are regularly updated. The Cayman Islands insolvency regime is generally considered to be extremely "creditor friendly". The principal insolvency procedure under Cayman Islands law is liquidation; there are no formal concepts equivalent to UK administration or U.S. Chapter 11.

²⁷² See Mays, *INSOL World* 2004, 24. Most Cayman incorporated companies conduct their business and hold their assets outside the Cayman Islands.

²⁷³ See Parmalat Finanziaria SpA, 22.06.2004, NY2:\1369224\05\TC\$005!.DOC\66971.0003, Voluntary Petition filed with the S.D.N.Y.

4.1.2 United States Plenary Proceeding

Three companies, namely Farmland Dairies, LLC, (Farmland) its controlling company Parmalat USA Corporation and its subsidiary company Milk Products of Alabama, LLC (MPA)²⁷⁴ carried out Parmalat's US dairy activities.²⁷⁵ Having witnessed troubles since the parent company in Italy was under Extraordinary Administration, the U.S. dairy units²⁷⁶ filed voluntarily²⁷⁷ for Chapter 11 status under the U.S. Bankruptcy Code in the Southern District Court of New York.²⁷⁸ The voluntary application for Chapter 11 protection was necessary in order to avoid any mayor operational or financial disruption of the businesses or any impairment to their value as a result of changes to payment terms applied by suppliers, the securing of the necessary financing to cover the businesses' immediate ongoing needs, and to facilitate the examination of strategic alternatives for the business, including a potential sale.²⁷⁹ However, in the jointly administered Chapter 11 case, the reorganisation plan only applied to Farmland, Parmalat USA and MPA proposed liquidation plans.²⁸⁰

Success in the Chapter 11 proceeding was dependent on a \$35 million short-term DIP-financing from General Electric (GE) Capital to secure the cover of the companies' immediate operational needs.²⁸¹ The bankruptcy was not expected to last long because of the narrow time frame of the DIP-financing.²⁸²

Parmalat Finanziaria SpA and other international affiliates filed claims of US\$700 million against the three U.S. subsidiaries. Meanwhile the U.S. subsidiaries filed claims totalling more than US\$ 350 million against Parmalat Finanziaria SpA, Parmalat SpA and other Parmalat affiliates in the reorganisation proceeding in Italy.²⁸³

Plan of Reorganisation

The Plan of Reorganisation for Farmland Dairies LLC was confirmed by the U.S. Bankruptcy Court S.D.N.Y. on March 8, 2005.²⁸⁴ The cornerstone of the plan was an agreement with GE Commercial Finance, the lessor of a majority of Farmland's

²⁷⁴ 80% owned by Farmland Dairies, LLC and 20% by a minority shareholder.

²⁷⁵ See Parmalat Finanziaria SpA, Press Release, 24.02.2004.

²⁷⁶ See Berke, the Deal 24.02.2004. The application did not include the Canadian dairy business and the bakery operations in the USA and Canada. See NYT 2005, 4. Parmalat sold its U.S. and Canadian cookie businesses to a private equity firm.

²⁷⁷ See Day, NYT 25.02.2004, <http://www.nytimes.com>, 21.12.2005. Court filings listed assets of US\$414m and liabilities of US\$316.5 million.

²⁷⁸ *In re* Parmalat USA Corp, et al, 04-11139 (RDD) (S.D.N.Y. 2004).

²⁷⁹ See Hamilton, Forbes 24.02.2004.

²⁸⁰ *In re* Parmalat USA Corp, et al, 04-11139 (RDD) (S.D.N.Y. 2004).

²⁸¹ See Boston.com 24.02.2004, http://www.boston.com/business/articles/2004/02/24/parmalat_usa_files_for_chapter_11.htm, 21.12.2005.

²⁸² See Berke, the Deal 24.02.2004. The time frame from providing DIP-financing to "definitive documentation" for a sale was dependant on GE Capital. In the case of Parmalat the time frame was four weeks.

²⁸³ See Forbes Associated Press, Parmalat Agrees to Settle With Affiliates, 03.04.2005.

²⁸⁴ See NYT 17.09.2004, <http://www.nytimes.com>, 21.12.2005: For Milk Products of Alabama LLC there was no reason to file for a Plan of Reorganisation since it was included in the reorganisation plan of Farmland Dairies. During the Farmland Dairies' restructuring process, Farmland Dairies sold MPA to Dean Foods for \$21.7 million. The sale was approved by the U.S. Bankruptcy Court S.D.N.Y. on September 15, 2004

manufacturing equipment at its New Jersey and Michigan production facilities, and the Unsecured Creditors Committee. The plan called for the satisfaction of the company's pre-petition liabilities through the issuance of cash, notes, stock and rights to pursue certain causes of action. Specifically, Farmland's unsecured creditors would receive cash, a note, and preferential rights of recovery from causes of action pursued by a litigation trust. Farmland emerged from bankruptcy as a stand-alone entity. The plan provided for exit financing commitments totalling \$101 million consisting of a \$56 million loan from LaSalle Business Credit, and a \$45 million term loan from GE Commercial Finance.²⁸⁵

On April 3, Parmalat Finanziaria and the U.S. affiliates settled their claims against each other for \$22 million that the U.S. entities paid to “a litigation trust set up as part of Parmalat’s USA restructuring”.²⁸⁶ This was a major step towards a successful reorganisation of the U.S. subsidiaries and further business conduct on a stand-alone basis.²⁸⁷ With settling claims with the three U.S. companies, Parmalat finally left the U.S. dairy market in August 2005. As a consequence, the U.S. entities were permanently removed from the scope of consolidation of the Parmalat Group.²⁸⁸

However, despite the U.S. plenary proceeding, Mr Bondi still was required to commence a jointly administered ancillary proceeding in the U.S. Bankruptcy Court S.D.N.Y. for Parmalat Finanziaria SpA and Parmalat SpA²⁸⁹ to obtain a stay of all pending U.S. litigation against the non-U.S. debtors, including actions under the U.S. securities laws.²⁹⁰ The Extraordinary Commissioner also brought several actions against the companies’ accountants and others in U.S. Federal and State laws.²⁹¹

4.2 Legal Prosecution Proceedings at Eurofood IFSC Ltd. under consideration of the European Council Regulation on Insolvency Proceedings

While the U.S. Parmalat case demonstrates the height of cooperation between various insolvency courts, the Eurofood case highlights the low point. In Eurofood, the various parties contorted the EIR regulations designed to foster cooperation and certainty in cross-border insolvency cases so as to manufacture a jurisdictional dilemma. As discussed, the issues presented in the Eurofood case have wide ranging ramification to many cross-border insolvency cases.

²⁸⁵ See Day, NYT 25.02.2004, <http://www.nytimes.com>, 23.12.2005.

²⁸⁶ Forbes Associated Press, Parmalat Agrees to Settle With Affiliates, 03.04.2005.

²⁸⁷ Note: On April 14, 2005, Farmland Dairies LLC announced that it had filed its Disclosure Statement and Plan of Reorganisation with the Bankruptcy Court. This was possible through exit financing totalling \$101 million. The equity of the emerged Farmland is be majority-owned (80%) by the company's pre-petition leasing syndicate which is led by GE Capital Public Finance, a unit of General Electric.

²⁸⁸ See Parmalat Finanziaria SpA, Press Release, 01.06.2005.

²⁸⁹ *In re* Parmalat Finanziaria S.p.A., 320 B.R. 46 (S.D.N.Y.2005). See Annex C Parmalat Finanziaria SpA Case Ancillary to Foreign Proceeding. Also Parmalat SpA Case Ancillary to Foreign Proceeding.

²⁹⁰ See Security and Exchange Commission v. Parmalat Finanziaria SpA 03 10266 (PKC) (S.D.N.Y.2004). The SEC charged Parmalat with securities fraud over US\$1.5 billion bond sale. See Greiff, Bloomberg 27.02.2004. The SEC sought to settle its fraud suit over claims of US\$100 million bond offering against Parmalat as the company cooperates.

²⁹¹ See Bondi v. Grant Thornton International, 322 B.R. 44 (S.D.N.Y. 2005).

4.2.1 Legal Prosecution Proceedings in Ireland

The Parmalat Group founded the Eurofood International Financial Service Centre (IFSC)²⁹² Ltd.,²⁹³ incorporated and registered in Dublin on November 5, 1997. The company's capital was entirely held by Parmalat SpA, and the principal purpose was raising financing facilities for other subsidiaries in the Parmalat Group.²⁹⁴ Assisted by Bank of America, Eurofood has engaged in only three large financial transactions: bond issues of \$80 million for the Venezuelan subsidiary and \$100 million for the Brazilian entity by way of private placement with institutional investors in 1998. Both South American subsidiaries are controlled by Parmalat SpA, which guaranteed all the sums owed by Eurofood for capital, interest and documented costs which were incurred in relation to the financing operations; these accrued charges anticipated by Bank of America were secured in a swap deal in 2001.²⁹⁵

Eurofood had neither employees nor office premises in Ireland at any time. The (pro-forma) registered office was located in the law firm's office of McCan FitzGerald in Dublin.²⁹⁶ The entity was managed by a body of two Irish non-executive directors, by a partner of the law firm, and an employee of Bank of America as well as two Italian executive directors who were entrusted with the real management of the subsidiary. All board meetings were held in Dublin,²⁹⁷ which the Italian directors usually attended via telephone.

After both Parmalat SpA and Parmalat Finanziaria SpA had been admitted to Extraordinary Administration,²⁹⁸ the Irish Financial Services Regulatory Authority launched investigations into Eurofood on January 9, 2004. A week later, Milan prosecutors began investigating the role of Eurofood in the notes issues in 1998.²⁹⁹ On January 27, 2004, Bank of America presented a petition to the High Court in Dublin for the winding up of Eurofood since the company was insolvent, justifying the proceedings with claims exceeding US\$3.5 million, and applied for the appointment of a provisional liquidator.³⁰⁰ In its affidavit underpinning the petition, Bank of America expressed concern about an attempt to move Eurofood's centre of main interests from Ireland to Italy.³⁰¹ Other creditors (of the notes issued in

²⁹² The International Financial Services Centre provides a location for internationally traded financial services (i.e. banking, asset financing), which may be provided only to non-resident persons or bodies and are subject to the condition that the business is carried out in Dublin, governed by Irish regulatory authorities and Irish tax law.

²⁹³ *Herewithafter* Eurofood.

²⁹⁴ *See In re Eurofood IFSC Ltd.* [2004] No. 33 cos, EHC 130/04.

²⁹⁵ *See Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04. *See also Re The Insolvency of Eurofood IFSC Ltd.*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

²⁹⁶ *See In re Eurofood IFSC Ltd.* [2004] No. 33 cos, EHC 130/04.

²⁹⁷ *See Re The Insolvency of Eurofood IFSC Ltd.*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

²⁹⁸ *See Italian Legislative Decree No. 347 of December 23, 2003 (L.D. 347/2003)*, updated on February 19, 2004, No. 39 (Law 39/2004), modified on May 3, 2004, No. 42 (Law. 119/2004).

²⁹⁹ *See Houlihan, Lokey, Howard & Zukin, Parmalat*, 2004.

³⁰⁰ *See In re Eurofood IFSC Ltd.*, No. 33 cos, EHC 130/2004.

³⁰¹ *See Ci4Net.Com v. DBP Holdings Limited*, High Court of Justice Leeds, [2004] No. 556/557: The question of timing is of importance since a "removal of the seat of the company's operations [within the EU or] from the EU to a non-EU territory a few weeks or months before the business goes against the wall would not be regarded as working an alteration in the centre of main interests of the company" because it runs contrary to the policy in the EIR that the centre of main interests should connote some degree of permanence. Therefore, Bank of America had no ground for concern.

excess of US\$122 million) were willing to join the petition of Bank of America.³⁰² The same day, the High Court Dublin has made a winding up order, appointed a provisional liquidator with special powers (preserve assets and investigate its affairs) and set a respite not to exceed February 23, 2004. The provisional liquidator notified Mr. Bondi about the proceedings in Ireland on January 30, 2004.³⁰³

The petition of Bank of America for the winding up of Eurofood was heard in the High Court Dublin from March 2 to March 4, and the judgement of March 23 stated that the insolvency proceedings had been opened in Ireland on the day the petition from the creditors was presented to the court, and that the centre of main interests was in Ireland since the registered office was located there.³⁰⁴ Furthermore it ruled that the opening of insolvency procedures by the Court of Parma was contrary to the EIR (Recital 22, Article 16) and reasoned that the failure to give notice to neither the provisional liquidator nor the creditors of the hearing before the Parma Court justified the Irish Court's refusal to recognise the decision of the Parma Court (Article 16).³⁰⁵ Hence, the judge made a winding up order of Eurofood and appointed the provisional liquidator as liquidator.³⁰⁶

The High Court Dublin's interpreted the winding up order in accordance with the EIR and the definition of "insolvency proceedings" (Article 2(a), Annex B) which, with reference to Ireland, includes the compulsory winding up; the definition of a "liquidator" (Article 2(a), Annex C) includes, again with reference to Ireland, the provisional liquidator and the time of opening proceedings "shall mean the time at which the judgment opening proceedings becomes effective, whether it is a final judgment or not" (Article 2(e)). Therefore, all requirements were present to open main insolvency proceedings³⁰⁷ and "shall be recognised in all the other Member States from the time that it becomes effective in the State opening the proceedings" (Article 16(1)). The applicable law in case of opening an insolvency procedure "shall be that of the Member State" (Article 4(1)), referring to national law.³⁰⁸ Herewith, according to the Irish Companies Act 1963, the winding up is "deemed to commence at the time of the presentation of the petition for winding up", known as "relation back".³⁰⁹ However, if the ECJ affirms this "relation back" principle for proceedings opened by only presenting a winding up petition, it will have to consider what the effects would be if the court subsequently declined to issue a winding up order.

4.2.2 Legal Prosecution Proceedings in Italy

On February 9, 2004, the Italian Ministry for Productive Activities declared Eurofood insolvent under the collective insolvency proceedings of the Parmalat Group, and Mr. Bondi

³⁰² See *In re Eurofood IFSC Ltd.* [2004] No. 33 cos, EHC 130/04.

³⁰³ See *In re Eurofood IFSC Ltd.* [2004] No. 33 cos, EHC 130/04. See also Thompson, Credit Control 2004, 18.

³⁰⁴ See *In re Eurofood IFSC Ltd.* [2004] No. 33 cos, EHC 130/04. See *In re Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04.

³⁰⁵ See *In re Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04.

³⁰⁶ See *In re Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04.

³⁰⁷ See Freshfields, Restructuring and Insolvency Bulletin, 2004, 1.

³⁰⁸ See *In re Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04.

³⁰⁹ See Companies Act, 1963, Section 220 (2): The "relation-back" concept (i.e. a court order winding up a company made three to four weeks after the presentation of the petition takes effect from the date of presentation of the petition) is peculiar to Irish and UK insolvency law. See also Eidenmüller, NJW 2004, 3457: Art. 44 states that the backlash in Irish and English law is under the Regulation unremarkable.

was appointed Extraordinary Commissioner of Eurofood.³¹⁰ The admission to insolvency procedures followed on February 12, 2004. A court hearing was set before the Parma Court on February 17, 2004, but neither Bank of America nor other creditors nor the provisional liquidator were given appropriate notice of the petition presented by Mr. Bondi to the Parma Court or of other documents admitting Eurofood into insolvency procedures before the Parma Court. For that reason, there was no opportunity for the provisional liquidator or the creditors to place evidence before the Parma Court.³¹¹ On February 20, the Parma Court opened main insolvency proceedings, including Eurofood finding that its centre of main interests was in Italy.³¹²

According to the counsel to Mr. Bondi, insolvency procedures were first opened by the Court of Parma on February 20.³¹³ He pointed out that the function of the European Regulation “is to allocate jurisdiction between Member States. Jurisdiction to open main insolvency proceedings is not the Member State where the application is first made but rather where the company has its centre of main interests”.³¹⁴ The counsel submitted that the appointment of a provisional liquidator cannot be recognised as the opening of insolvency proceedings (Article 3(1)) but rather as a requirement to preserve the assets before the winding up order is finally made.³¹⁵ Furthermore, “the inclusion of “provisional liquidator” in Annex C of the Regulation is not relevant since there is no relevant proceeding in Annex A, and the winding up commences only when an order to that effect is made”.³¹⁶

4.2.3 Submissions on the opening of insolvency procedures

With consideration to Council Regulation 1346/2000 on insolvency proceedings (Article 3(1)), the question arises about which Member State court had the jurisdiction to open the main insolvency proceeding for Eurofood.³¹⁷

The EIR is responsible for determining which Member State is the debtor’s centre main interests, thus deciding the jurisdiction to open insolvency proceedings. This is important for insolvent companies that are operating in more than one jurisdiction. The Regulation provides that once a court of a Member State has found that a company’s centre of main interests is within its jurisdiction, “the law of the State [...] shall determine the conditions [...] of those proceedings” (Article 4(2)), which, in the event of a group insolvency, could coordinate the main insolvency proceeding within the Member States of the European Union. The Regulation requires the automatic recognition of the decision without Member States having the power to scrutinise the court’s decision (Recital 22). Therefore, the decision cannot be disregarded by other courts, even if they disagree.³¹⁸

³¹⁰ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

³¹¹ See *In re Eurofood IFSC Ltd*. [2004] No. 35 cos, IESC 145/04.

³¹² See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

³¹³ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

³¹⁴ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

³¹⁵ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

³¹⁶ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

³¹⁷ See *In re Eurofood IFSC Ltd*. [2004] No. 35 cos, IESC 145/04.

³¹⁸ See Kochberg/Crowley, *The Lawyer* 2004, 23. See also Thompson, *Credit Control* 2004, 17.

After the High Court Dublin had issued the winding up order for Eurofood, Mr. Bondi appealed against the decision with submissions on where first insolvency proceedings were first opened, where the centre of main interests of Eurofood was located and whether the procedures of the Italian Court, in consideration of the hearing, had been fair.³¹⁹

4.2.4 Submissions on Centre of Main interests

Eurofood IFSC Ltd. was a wholly owned subsidiary of the Parmalat Group, incorporated in Ireland with a registered office in Dublin.³²⁰ It operated under a certificate issued by the Irish Minister for Finance which required it to commence and continue to carry on its trading operations within a specified area in Ireland, and any material change of the company (including its shareholding) had to be cleared with the Department of Finance in Ireland.³²¹ Therefore, the High Court Dublin doubted the decision of the Court of Parma that Eurofood's centre of main interests was in Italy. The Judge referred to previous cases³²² as authority for how to locate a company's centre of main interests. Particular emphasis was placed on how "third parties (namely creditors)"³²³ perceived the company's centre of main interests.³²⁴ The fact that the creditors in this case clearly perceived that they were dealing with an Irish company was conclusive for the High Court and Supreme Court of Eurofood's centre of main interests being in Ireland.

The analysis of the Supreme Court is interesting in two respects. First, in determining where the company conducted the administration of its interests on a regular basis, the Supreme Court not only considered where Eurofood is incorporated³²⁵ but attached significant weight to the location of the company's board meetings. In previous cases³²⁶ the location of board meetings has only been persuasive of centre of main interests, as opposed to being almost determinative of the issue.³²⁷ Second, consistent with the developing jurisprudence, considerable emphasis was placed on the ascertainability of the company's centre of interest by its creditors.³²⁸

Mr. Bondi argued that the centre of main interests as the statutory seat may coincide with the legal seat "except where there is evidence of purely formal or fictitious nature of that legal seat, because the directive and organisational activity, or the most significant part thereof, occurs elsewhere".³²⁹ Since the management activities were carried out by the

³¹⁹ See *In re Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04.

³²⁰ See Müller, NZG 2003, 415.

³²¹ See *In re Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04.

³²² See *Re Daisytek-ISA Ltd.* [2003] BCC 562. See also *Re BRAC Rent-a-Car International Inc.* [2003] 1 WLR 1421. See also *Geveran Trading Co. Ltd. v. Skjeveland* [2003] BCC 209.

³²³ See *In re Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04. See also Paulus, ZIP 2003, 1727. See also Rapinet/Tucker, Parmalat, JIBFL 2005, 52.

³²⁴ See *Geveran Trading Co. Ltd. v. Skjeveland* [2003] BCC 209: "It is the need of third parties to ascertain the centre of a debtor's main interests that is paramount, because, if there are to be insolvency proceedings the creditors need to know where to go to contact the debtor..." See also Van Galen, INSOL 2003, 6: The creditors should not have to investigate where the debtor's centre of main interests is located.

³²⁵ See Moss/Fletcher/Isaacs, Oxford 2002, 12. See also Duursma-Kepplinger/Duursma/Chalupsky, Springer 2002, Art. 3, N. 24.

³²⁶ As mentioned before.

³²⁷ See *Re Daisytek-ISA Ltd.* [2003] BCC 562.

³²⁸ See Hamilton 2005.

³²⁹ See *Re The Insolvency of Eurofood IFSC Ltd.*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

Italian directors of Eurofood at the seat of Parmalat SpA in Collecchio,³³⁰ Mr. Bondi leaves no doubt that the real seat was Italy.³³¹

The case raises a further interesting point, which has also been referred to the ECJ by the Supreme Court of Ireland. The Irish High Court judge stated that, had he needed to, he would have refused to recognize the Italian order on public policy grounds (Article 26).³³² This happened on the basis that neither the provisional liquidator nor the major creditors had been given proper notice of the hearing in Italy when the court declared the company insolvent and that its centre of main interests was in Italy (Article 40).³³³ The decision was despite the Italian court having ruled that all interested parties should be served with notice of the hearing.³³⁴ According to the judge, this conflicted with the right to a fair hearing. Mr. Bondi appealed to the Supreme Court of Ireland on the basis that the High Court judge had misdirected himself in his interpretation of Article 26 and his finding that there had been a breach of public policy.³³⁵ The Supreme Court held that it would be manifestly contrary to public policy to give recognition to the decision of the Italian court on the ground that the provisional liquidator was not given the protection of the fundamental aspects of fair procedure, which is, ‘in Irish law, a principle of public policy of cardinal importance’.³³⁶

4.2.5 Clash of Jurisdictions

It seems that Mr. Bondi's rationale in applying to the Italian courts to declare that Eurofood's centre of main interests was in Italy was that he sought to consolidate Eurofood to the same jurisdiction and procedure as other Parmalat companies, and therefore to bring the administration of, at least the European, Parmalat group companies under his sole control.³³⁷ Although Mr. Bondi's reasoning may be understandable, it appears that he was indulging in forum shopping by “seeking to obtain a more favourable legal position” (Recital (4)) which is what the Regulation should prevent.³³⁸

³³⁰ *In Contrast* Ehrlicke, EWS 2002, 103: Internal orders, especially determining and administering the business of a company do not matter. The centre of main interests is located where these activities are carried out and perceived so by the creditors. *See also* Smid, DZWIR 2003, 402. “decisive for the centre of interest is the place of incorporation”. *See also* Pannen/Riedemann, NZI 2004, 651. ‘Mind of management’ is not conclusive with the centre of main interests.

³³¹ *See Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court. *See also Re Daisytek-ISA Ltd*, [2003] BCC 562: “...the identification of ‘the debtor’s main interests requires the court to consider both the scale of the interests administered at a particular place and their importance and then consider the scale and importance of its interests administered at any place which may be regarded as its centre of main interests, whether as a result of the presumption in Article 3(1) or otherwise”. *See also Ci4Net.Com v. DBP Holdings Limited*, High Court of Justice Leeds, [2004] No. 556/557: “There seems to be no reason to suppose that the presumption that a company has its CoMI at the place of its registered office is a particular strong one. It is, rather, just one factor to be taken into account with the whole of the evidence in reaching a conclusion as to the location of the CoMI”.

³³² *See In re Eurofood IFSC Ltd*, [2004] No. 35 cos, IESC 145/04. *See also Eidenmüller*, NJW 2004, 3457: “right to a hearing is a breach of law but too hear all creditors would be unpractical”.

³³³ *See In re Eurofood IFSC Ltd*, [2004] No. 35 cos, IESC 145/04.

³³⁴ *See Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

³³⁵ *See Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court. *See also In re Eurofood IFSC Ltd*, [2004] No. 35 cos, IESC 145/04.

³³⁶ *See In re Eurofood IFSC Ltd*, [2004] No. 35 cos, IESC 145/04.

³³⁷ *See Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court. *See also Thompson*, Credit Control 2004, 17.

³³⁸ *See Halén*, Master Thesis 2002, 26.

With two conflicting decisions made by two different courts in two different Member States, Eurofood also raises the anathema of a jurisdictional conflict, another matter the Regulation was designed to avoid. Ultimately, only the ECJ can resolve which of the two verdicts the "correct" decision is. Cases can only be referred to the ECJ by a Member State's highest court of appeal. Mr. Bondi has appealed the decision to the Irish Supreme Court (the hearing was due on 27 May 2004). Afterwards, the Irish Supreme Court referred some questions to the ECJ for preliminary ruling.³³⁹

4.2.6 Questions for preliminary ruling

The Irish Supreme Court did not propose "to refer any question relating to the contention that the Central Office of the High Court has power to open main insolvency proceedings, since the Court finds that it is quite clear that it does not".³⁴⁰ Instead the Court asked:³⁴¹

- (1) Where a petition is presented to a court of competent jurisdiction in Ireland for the winding up of an insolvent company and that court makes an order, pending the making of an order for winding up, appointing a provisional liquidator with powers to take possession of the assets of the company, manage its affairs, open a bank account and appoint a solicitor all with the effect in law of depriving the directors of the company of power to act, does that order combined with the presentation of the petition constitute a judgment opening of insolvency proceedings for the purposes of Article 16, interpreted in the light of Articles 1 and 2, of Council Regulation (EC) No 1346 of 2000?
- (2) If the answer to Question 1 is in the negative, does the presentation, in Ireland, of a petition to the High Court for the compulsory winding up of a company by the court constitute the opening of insolvency proceedings for the purposes of that Regulation by virtue of the Irish legal provision (section 220(2) of the Companies Act, 1963) deeming the winding up of the company to commence at the date of the presentation of the petition?
- (3) Does Article 3 of the said Regulation, in combination with Article 16, have the effect that a court in a Member State other than that in which the registered office of the company is situate and other than where the company conducts the administration of its interests on a regular basis in a manner ascertainable by third parties, but where insolvency proceedings are first opened has jurisdiction to open main insolvency proceedings?
- (4) Where
 - a) the registered offices of a parent company and its subsidiary are in two different Member States,
 - b) the subsidiary conducts the administration of its interests on a regular basis in a manner ascertainable by third parties and in complete and regular respect for its own corporate identity in the Member State where its registered office is situated and
 - c) the parent company is in a position, by virtue of its shareholding and power to appoint directors, to control and does in fact control the policy

³³⁹ See *In re Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04.

³⁴⁰ *In re Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04.

³⁴¹ *In re Eurofood IFSC Ltd.* [2004] No. 35 cos, IESC 145/04.

of the subsidiary, in determining the "centre of main interests", are the governing factors those referred to at b) above or on the other hand those referred to at c) above?

- (5) Where it is manifestly contrary to the public policy of a Member State to permit a judicial or administrative decision to have legal effect in relation persons or bodies whose right to fair procedures and a fair hearing has not been respected in reaching such a decision, is that Member State bound, by virtue of Article 17 of the said Regulation, to give recognition to a decision of the courts of another Member State purporting to open insolvency proceedings in respect of a company, in a situation where the court of the first Member State is satisfied that the decision in question has been made in disregard of those principles and, in particular, where the applicant in the second Member State has refused, in spite of requests and contrary to the order of the court of the second Member State, to provide the provisional liquidator of the company, duly appointed in accordance with the law of the first Member State, with any copy of the essential papers grounding the application?

4.2.7 Advocate General's Opinion for the European Court of Justice

Eurofood is the first case in which the definition of the centre of main interests and application of public policy ground has been raised and the ECJ's decision is awaited with interest.³⁴² The Regulation appears to have been drafted on the assumption that a company's centre of main interests is clear to all parties, which, as recognised above, is not the case. It remains to be seen how the ECJ will decide on where the main insolvency proceeding was opened in the context of where Eurofood had its main centre of interests. On September 27, 2005, the Advocate General Jacobs of the ECJ finally issued his opinion on the case before the Court.³⁴³ It is now a matter for the ECJ to confirm the opinion of the Advocate General and its judgement in this respect is expected in spring 2006.

In essence, the Advocate General concluded in his statement in response to the questions posed by the Irish Supreme Court to the ECJ that:³⁴⁴

- (1) Where a petition is presented for the winding up of an insolvent company and an order is made appointing a provisional liquidator with powers to take possession of assets and manage the affairs of the company this constitutes the opening of main insolvency proceedings.³⁴⁵
- (3) Where insolvency proceedings are first opened by a Court in the Member State in which the company's registered office is situated and in which the company conducts the administration of its interests on a regular basis in a manner ascertainable by third parties the courts of the other Member States do not have jurisdiction to open main insolvency proceedings.
- (4) The Centre of Main Interests (COMI) of a subsidiary is where its registered office is situated and where it conducts its administration ascertainable by third parties. COMI can not be rebutted because the parent is in a position to

³⁴² See Freshfields, Restructuring and Insolvency Bulletin 2004, 2. See also Carton-Kelly, INSOL World 2004, 12.

³⁴³ See Farrell/Grant/Sparks, ECJ Opinion 2005, <http://www.fgs.ie/aboutus.asp?id=20&cid=906>, 10.11.2005.

³⁴⁴ Farrell/Grant/Sparks, ECJ Opinion 2005, <http://www.fgs.ie/aboutus.asp?id=20&cid=906>, 10.11.2005.

³⁴⁵ Note Question 2 was in the event of a negative response to question 1, which is not the case.

exercise, by virtue of its shareholding and power to appoint directors, the policy of the subsidiary.

- (5) Where it is manifestly contrary to the public policy of a Member State to permit a judicial or administrative decision to have legal effect in relation to persons or bodies whose right to fair procedures and a fair hearing has not been respected in reaching such a decision, that Member State is not bound by Article 16 (of the Regulations) to give recognition to a decision of the courts of another Member State purporting to open insolvency proceedings in respect of a company, in a situation where the court of the first Member State is satisfied that the decision in question has been made in disregard of those principles.

In his conclusion, which is usually affirmed by the ECJ's preliminary ruling, the Advocate General affirms the view of the Irish Courts and Irish creditors. His opinion is sufficient in regard of solving the issue of the centre of main interests: the Advocate General focused on the inside operations and the registered office of the specific debtor entity in defining the centre of main interests rather than the operations and financial dependency within a group structure.

4.2.6 Aspects to consider by the European Court of Justice

While the Advocate General's opinion is generally accepted, the ECJ can also expand or contract the opinion. Therefore, there are other factors that the ECJ needs to consider in fully solving the issue of cross-border insolvencies within its territory.

As the High Court Dublin pointed out, it would have serious implications for the future of international corporate structures if it were to be accepted that the test for centre of main interests were to be ultimate financial control by a parent company rather than legal and corporate existence.³⁴⁶ Difficulties will arise when contract partners like banks, creditors, and lenders, as well as employees believe they are dealing with an Irish company, which is incorporated under Irish law but controlled by an Italian parent company; therefore insolvency proceedings will be carried out under the jurisdiction of the country where the parent company has its centre of main interests.³⁴⁷ This would mislead creditors in their impression with which company and therefore jurisdiction they are actually dealing with.³⁴⁸

Especially for offshore countries with more liberal capital market laws, the impact will be tremendous.³⁴⁹ Because of their advantageous law and tax systems,³⁵⁰ e.g. Ireland is used for various financial vehicle transactions. Investors "in asset-backed papers expect to have a market risk but not a risk of credit loss".³⁵¹ Since a rating for a structured deal is given upon the closing date and the analysis regarding insolvency has been done under the

³⁴⁶ See *In re Eurofood IFSC Ltd.*, No. 33 cos, EHC 130/2004. See also Thompson, *Credit Control* 2004, 18. See also Hamilton 2005.

³⁴⁷ See Hamilton 2005.

³⁴⁸ See Moss/Fletcher/Isaacs, *Oxford* 2002, 44. See also Carton-Kelly, *INSOL World* 2004, 12.

³⁴⁹ See Hamilton 2005.

³⁵⁰ See Hamilton 2005: It appears that Eurofood was set up in Ireland in order to take advantage of the beneficial tax regime for companies under that jurisdiction. It remains to be seen whether a company can claim that it is a tax resident in one jurisdiction but has its centre of main interests in another jurisdiction. See also Mays, *INSOL World* 2004, 23.

³⁵¹ Case, *National Conference of Bankruptcy Judges* 2002, 15. See also Eidenmüller, *NJW* 2004, 3456.

specific national law, the implications on the issuer moving its centre of main interests have a great influence on the rating: under another local insolvency law, the structure may not stand up, therefore, the prerequisites and implications of the transactions will have changed.³⁵² The determination of the centre of main interests as the place of incorporation may give rise to creative engineering of certain transactions by drafting and applying legal arrangements and contracts that limit the risks of being opposed to provisions with regard to detrimental acts (Article 13) or set off (Article 6).³⁵³ Although advance contractual waivers on the right of a special purpose vehicle to file for bankruptcy are thought to be invalid, it is not unusual for special purpose vehicles to be a corporation or limited liability company,³⁵⁴ which is eligible for bankruptcy filing.

Furthermore, for structured finance deals like DIP-financing,³⁵⁵ a problem could arise if a special purpose vehicle was deemed to have other operations³⁵⁶ within the EU. Contractors of providing DIP-financing³⁵⁷ usually impose controls on the company in order to monitor governance during an administered reorganisation.³⁵⁸ Therefore, they need to ensure their securities³⁵⁹ in respect that, where a financing structure includes foreign subsidiaries, the company has significant commercial operations in its jurisdiction of incorporation,³⁶⁰ leaving no doubt where the centre of main interests is located.³⁶¹ Furthermore, investors want to be sure that they are receiving the same broad legal protection under different law systems.³⁶² At the same time regulations must preserve the integrity of the internal financial market.³⁶³

The EIR focuses only on the centre of main interests of individual companies, with some guidance on interpretation in Recital 13 and the Explanatory Report,³⁶⁴ but does not include the administration or cooperation of multinational group insolvencies.³⁶⁵

³⁵² See Williams, IFLR 2004, 2. See also Marshall, IFLR 2002, 30. See also Curran/Danusso, JIBFL 2004, 116.

³⁵³ See Wessels, NASBL 2003, 486. See also Wessels, JIBLR 2003, 140.

³⁵⁴ See Case, National Conference of Bankruptcy Judges 2002, 16. See also Hamilton 2005. See also Beltzer 2005.

³⁵⁵ Most likely in UK and US. The British Enterprise Act 2002 came into force in September 2003 and modified the formal (administration, administration receivership) and informal rescue procedures ('London Approach'). The U.S.B.C. provides for DIP-financing during a Chapter 11 reorganisation. However, the EIR also provides for DIP procedure under Article 1(1) as Article 2(b) provides that 'liquidator' shall mean any person or body whose function is to administer or liquidate assets of which the debtor has been divested including the mere supervision of the administration of the debtor's affairs. Remark Mr. Bondi also received €150m DIP-financing for restructuring Parmalat in Italy.

³⁵⁶ As mentioned above, operations neither do nor need to be incorporated under the national law of a foreign country.

³⁵⁷ DIP-financing can be provided by banks, investment companies and debt traders.

³⁵⁸ See Calnan/Rose, JIBFL 2004, 252. See also Wessels, JIBLR 2003, 141. See also Miller/Waismann, ABLJ 2004, 181.

³⁵⁹ See Herrchen, Dissertation 1999, 18.

³⁶⁰ See Curran/Danusso, JIBFL 2004, 116. See also Williams, IFLR 2004, 1.

³⁶¹ See *Re BRAC Rent-a-Car International Inc.* [2003] 1 WLR 1421.

³⁶² See Wessels, Kluwer 2004, 252.

³⁶³ See Schaub, IFLR 2004, 21. See also Fletcher, Oxford 1999, 4.

³⁶⁴ See Virgòs/Schmit 1996, No 75: Comments on Article 3(1): "The concept of 'centre of main interests' must be interpreted as the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties". In addition, the report places the COMI "in the case

The question arises whether an insolvent foreign but parent-administered subsidiary may file for a main insolvency proceeding in its country of incorporation,³⁶⁶ or only for a secondary proceeding, in case of a group liquidation or reorganisation.³⁶⁷ Furthermore, it remains unclear whether the subsidiary may file for a main proceeding in the Member State of the parent company where the administration is conducted due the integrated organizational structure.³⁶⁸ Therefore, it depends on how interests may be viewed, as commercial or professional activities or rather general economic activities.³⁶⁹

Regarding a group of companies, the centre of main interests may be located where the ultimate European parent company and management control is situated,³⁷⁰ thus defining the centre of main interests as the place of professional/business domicile.³⁷¹ Another approach may be to look to the jurisdiction of the debtor's incorporation, statutory seat or place of residence as the appropriate forum for the centre of main interests³⁷² because that is where the debtor conducts its business on a non-transitory basis³⁷³ and is therefore recognisable for third parties.³⁷⁴ Determining the centre of main interests may prove to be difficult in the case of unincorporated associations.³⁷⁵ There will not be a statutory seat and the centre of main interests may not be easily determinable.

The authoritative resolution of the difference between the "respect for form"³⁷⁶ and the "substance for management"³⁷⁷ will be fundamental. The parent company or controlled subsidiary may choose to move its centre of main interests or assets to the legislation deemed most advantageous to the business prior to insolvency proceedings,³⁷⁸ thereby benefiting from forum shopping.³⁷⁹ That centre of main interests and jurisdiction may not be the most favourable to the creditors,³⁸⁰ which may cause creditors to forum shop as

of professionals [is] the place of of their professional domicile", which "is the place of his registered office. This place normally corresponds to the debtor's head office."

³⁶⁵ Virgòs/Schmit 1996, No. 76: '...offers no rule for groups of affiliated companies'. See also Carriat, Working Paper 2004, 3. See also Liersch, Syndikus 2003, 5.

³⁶⁶ See Duursma/Duursma-Kepplinger, DZWIR, 450.

³⁶⁷ See also Vogler, Center of Legal Competence 2004, 165.

³⁶⁸ See Huber, ZZP 2001, 142-143.

³⁶⁹ See Wessels, Kluwer 2004, 258.

³⁷⁰ See Van Galen, INSOL 2003, 5. See also Smid, DZWIR 2004, 411. See also Müller, NZG 2003, 415.

³⁷¹ See Wessels, International Jurisdiction 2003, 25. See also Vallender/Fuchs, ZIP 2004, 829.

³⁷² See Carruth, TIL 2004, 355. See also Taupitz, ZZP 1998, 315. See also Smart, Butterworths 1991, 348. See also LoPucki, Forthcoming ABLJ 2005, 9-10.

³⁷³ See Dawson, Kluwer 2004, 202.

³⁷⁴ See Pannen/Riedemann, NZI 2004, 651. See also Sejas, Sprecher/Grier/Halberstamm Solicitors 2004, 3.

³⁷⁵ See Blumberg/Fowler, Aspen 2001, xxi. There may be a dominant and subordinate relationship in form of stock ownership, franchise, license, or subcontract as well as strategic alliances.

³⁷⁶ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court. See also Rapinet/Tucker, JIBFL 2005, 52. See also Moss/Fletcher/Isaacs, Oxford 2004, 169.

³⁷⁷ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court. See also Rapinet/Tucker, JIBFL 2005, 52. See also Reiner 2005.

³⁷⁸ See Laukemann, RIW 2005, 107. See also Bufford, Working Draft 2005, 86.

³⁷⁹ See Freshfields, Restructuring and Insolvency Bulletin 2004, 1. *Contrary* Smid, Verlag W. Kohlhammer 2004, 41 No 14. To move the centre of main interests may not be easy to achieve, it will involve large financial funds, which may not be accessible in a case prior to insolvency.

³⁸⁰ See Leonard, TILJ 1998, 546. See also Reiner 2005. See also Hamilton 2005.

well.³⁸¹ However, locations of assets and operations are rather difficult to change. A multinational group may still accomplish to move its centre of main interests by engaging in acquisitions and divestitures.³⁸²

The Regulation was intended to combat the incidence of forum shopping within the EU.³⁸³ It appears to date that the operation of the Regulation may in fact have significantly assisted such forum shopping³⁸⁴ since the centre of main interests “is such an arguable issue”.³⁸⁵ Therefore, the ECJ’s judgment needs to reduce the opportunity for forum shopping³⁸⁶ and thereby reducing transaction costs and increasing predictability.³⁸⁷ Companies need to consider where their centre of main interests is located, regardless of where these companies are registered.³⁸⁸

This is even more important when the application of the EIR extends to companies incorporated outside the EU. The EIR can apply to non EU-companies as long as their centre of main interests is seen to be in a Member State of a European Union.³⁸⁹ As the test is a practical head-office location, rather than a place-of-incorporation test, the EIR should apply to non-EU incorporated entities which have their centre of main interests in the EU, but will not apply to EU incorporated entities whose centre of main interests is outside the EU.³⁹⁰ In any case, coordination and communication between the insolvency proceedings and the involved liquidators (Article 31) are a necessity.³⁹¹

The ECJ may also determine the kind of creditors contracting with Eurofood, following the Parma Court. The notes issued by Eurofood and guaranteed by Parmalat SpA as the parent company were acquired by professional and institutional investors via banks and other international financial institutions.³⁹² In light of their specific technical competences in

³⁸¹ See also Williams, IFLRF 2003, 23.

³⁸² See LoPucki, Forthcoming ABLJ 2005, 18. These acquisitions are mostly paper transactions but entitling the debtor to file for bankruptcy in the strategic useful state.

³⁸³ Recital 4: “is necessary for the proper functioning of the internal market to avoid incentives for the parties to transfer assets or judicial proceedings from one Member State to another, seeking to obtain a more favourable legal position (forum shopping)”.

³⁸⁴ See Williams, IFLR 2003, 24. See also Fritz/Bähr, DZWIR 2001, 235.

³⁸⁵ Carton-Kelly, INSOL World 2004, 12.

³⁸⁶ Bhandari/Weiss, Cambridge 1996, 197. The cost of forum shopping as a subcategory of delay and uncertainty costs, of which reorganisation is a principal cause Bankruptcy process imposes costs from strategic behavior. If a manager-equity investor has an advantage inside bankruptcy and the creditors have an advantage outside, the manager could waste the debtor’s resources in an attempt to use the bankruptcy process, even if a non-bankruptcy resolution would be less costly.

³⁸⁷ See Bufford, Working Draft 2005, 85.

³⁸⁸ See Williams, IFLR 2003, 23. See also Cree, Director 2002, 17.

³⁸⁹ See Wessels, International Jurisdiction for Group Companies, 8. See also Linklaters, A Guide to the European Regulation on Insolvency Proceedings, 3. See also *Re BRAC Rent-a-Car International Inc.* [2003] 1 WLR 1421. The English court made an administration order in respect of a Delaware incorporated company which traded from England.

³⁹⁰ See *Re Enron Directo Sociedad Limitad* – unreported but “Skeleton Argument” under www.iiiglobal.org. The English court placed a Spanish registered company into administration on the basis that it was managed

³⁹¹ See Vogler, Center of Legal Competence 2004, 165.

³⁹² See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court

international markets, knowledge of structured finance, and financial credit analysis,³⁹³ these investors likely understood that the income from the bonds could be asserted against the parent of the group; otherwise it is questionable whether these investors would have engaged with Eurofood at all.³⁹⁴ Therefore, the “real legal and economic entity with whom [the creditors] were negotiating and on whom they were placing reliance”³⁹⁵ was Parmalat SpA.

Furthermore, the ECJ has to consider the different intentions of the Irish and the Italian court.³⁹⁶ With the petition from Bank of America, the Irish court aimed for a liquidation of Eurofood rather than a reorganisation under the Parmalat Group insolvency procedures admitted by the Italian court.³⁹⁷ Although subsidiaries may be liquidated while the parent company is being reorganised, from an economic point of view³⁹⁸ it could make more sense to restructure or wind up a multinational company in one proceeding³⁹⁹ and determine the centre of main interests where the parent company has its incorporation.⁴⁰⁰ In circumstances where there was no possibility for Eurofood continuing as a going concern, an insolvency procedure under Italian administration with an effort to restructure the Parmalat group could create understandable creditor concern.⁴⁰¹ However, even if Eurofood was liquidated under the Italian insolvency law, the exceptions of Article 6 (security, set-offs) would still limit the impact of the Italian insolvency procedures on the secondary proceeding.⁴⁰² It seems that Bank of America wanted to secure its legal position with liquidation under Irish law.

³⁹³ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court. See also Reiner 2005.

³⁹⁴ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court. See also Smid, DZWIR 2004,410.

³⁹⁵ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court.

³⁹⁶ See Reiner 2005: The jurisdiction in which the problem arises dictates the magnitude of that problem. In France, e.g., a restructuring is almost impossible because it really is a liquidation-based process. The problem of determining the centre of main interests therefore includes the consideration which insolvency proceeding is possible to reach the desired outcome. See also Hamilton 2005.

³⁹⁷ See *Re The Insolvency of Eurofood IFSC Ltd*, 2004, I.L.Pr. 14, Parma Civil and Criminal Court. See also *In re Eurofood IFSC Ltd*. [2004] No. 33 cos, EHC 130/04. See also *In re Eurofood IFSC Ltd*. [2004] No. 35 cos, IESC 145/04.

³⁹⁸ Costs of insolvency procedures include costs for documentation, court orders, financial and judicial advice etc.

³⁹⁹ Wood, Sweet & Maxwell 1996, 228: “The advantage of a single insolvency proceeding is the avoidance of cost and inefficiency of two competing administrations”. Also Ehrlicke, EWS 2002, 102. It can be expected that one group insolvency proceeding will have positive effects generated by coordination, concentration and simplification of the proceeding leading to synergy effects, reduction of transaction costs and positive economic results in regard to process optimisation. See also Huber, ZZP 2001, 143. See also Laukemann, RIW 2005, 108.

⁴⁰⁰ See Reiner 2005. See also Rapinet/Tucker, JIBFL 2005, 52.

⁴⁰¹ Remark: With a liquidation procedure and the bonds secured by Parmalat SpA, the creditors of Eurofood may expect a high recovery rate since Parmalat SpA is going concern and recovers the ability to pay their debt of the guarantee. With a reorganisation procedure under Italian administration, the creditors may lose out on their recovery share since the assets would not be distributed equally among the creditors, or they are expected to reduce their right to repayment for the benefits of the restructuring of the group.

⁴⁰² All assets subject to any void, voidable or unenforceable transactions may be recovered under the Regulation. Where the special rules apply, the Regulation may in certain circumstances effectively impose a ‘double-actionability requirement’ in relation to the recovery of those assets. First, the suspect transaction must be capable of being avoided under the law of the main proceedings (Article 4(2)(m)). Secondly, an action cannot be brought by the office holder in the main proceedings in one Member State

In conclusion it is clear that the ECJ should promote a uniform interpretation of the Regulation.⁴⁰³ However, it remains to be seen if the problems of dealing with group insolvencies and the lack of explicit reference⁴⁰⁴ to the issue of the centre of main interests and public policy is solved with the preliminary ruling or further ground arises over these issues.

The problems inherent in consideration of Eurofood case could well have been reduced if the Irish and Italian court would have cooperated, as intended by the EIR. It seems that Member States' courts tend to determine the centre of main interests always in their own jurisdiction rather than cooperating with other Member States' courts.⁴⁰⁵ This is supported by the fact that there was a need to bring the Eurofood case to the ECJ and discuss where the centre of main interests is located, which itself is a comment on the drafting of the EIR: the whole notion of the centre of main interests was designed to prevent this exact situation from occurring, therefore it seems that the EIR ends up forcing the conflict that it was intended to prevent. However, it has only been three years since the EIR came into force. Therefore, problematic issues are not surprising but rather a necessity to learn for the future.

U.S. courts seem to support communication and transparency with foreign courts and foreign representatives to solve cross-border issues in a timely and stringent matter. Parmalat's U.S. entities did not entail any problems in filing a plenary case under §301 in the U.S. as they were U.S. incorporated entities with local assets. But also the ancillary filings under §304 from the Italian Parmalat Finanziaria SpA und Parmalat SpA did not experience any problems of recognition or lack of communication.

Cooperation is important to apply effective insolvency systems because it assures increased transparency between courts and insolvency representatives. Without cooperation, negative consequences can arise for creditors and the debtor: creditors may not be treated equally, and the lack of communication between courts may cause a debtor to file for liquidation although a reorganisation of the business would have been achievable.

It will be interesting to follow the interaction of the Italian and Irish proceedings with one another, as well as with the other insolvency proceedings involving Parmalat entities that are pending around the world, including those in the U.S. and South America.

to set aside a transaction subject to the law of another EU state, unless the transaction could be set aside not only under the Member State law, but also under the law of that other EU state (Article 13).

⁴⁰³ See Smart, Butterworths 1991, 265.

⁴⁰⁴ See Williams, IFRL 2004, 2.

⁴⁰⁵ See Carton-Kelly, INSOL World 2004, 12. In Enron Directo, the English court affirmed the COMI in England; in Daisytec, the German court affirmed the COMI in Germany; in Eurofood, the Irish court affirmed the COMI in Ireland while the Italian court affirmed its COMI in Ireland.

SUCCESS AND FAILURE IN CROSS-BORDER INSOLVENCY PROCEEDINGS

With the market moving towards a global dimension, multinational cross-border insolvencies and reorganisations have increased not only in frequency but also in complexity. This complexity is mainly attributed to the multiple debtor scenarios with a spread of assets and liabilities among entities in several countries, a large diversification in organizational structures and the degree of management integration and control. Furthermore, the proper jurisdiction to handle the multinational insolvency case is presumably difficult to ascertain since different entities may have been incorporated or operated and administered in various countries.

Bankruptcy is an integral part of the market economy and provides a suitable mechanism for ensuring both the survival of viable companies and the demise of unsuitable businesses. However, the health of a country's economy and the functioning of its financial system are dependent on effective insolvency procedures that promote economic and social stability. An effective insolvency law serves to make the risks and consequences of a business failure easier to quantify for all parties involved. By introducing a measure of certainty into insolvency results, effective insolvency regimes enable creditors to assess the risk more accurately. Moreover, without effective insolvency systems, the rights of debtors may not be adequately protected and different creditors may not be treated equally. By providing confidence to creditors regarding how and whether they will be able to recover assets from financially troubled debtors, appropriate creditor rights increase the willingness of lenders to extend loans and encourage caution in the incurrence of liabilities by debtors.

The uncertainty encompassing the insolvency of multinational companies is due to the fact that the international community has, as of yet, failed to provide uniform procedures so far. However, the developing experience with cross-border insolvencies and reorganisations initiate increasingly innovative approaches to multinational cases. Regional approaches include the EIR, which regulates insolvency proceeding among the Member States, and the ALI Principles for the NAFTA countries. Approaches from international organisations such as the UNCITRAL Model Law or the World Bank help to sensitise the issues of cross-border insolvencies in respecting the differences in cultural traditions, legal policies and national sovereignty. A number of states has already adopted or show consideration to the adoption of UNCITRAL Model Law. Especially the U.S. application of the UNCITRAL Model Law in Chapter 15 is a mayor step towards effective cross-border insolvency. The access by non-U.S. entities to U.S. courts will remain substantial since the U.S. is one of the world's biggest markets and attracts businesses from around the world. Therefore, the Bankruptcy Code continues to have a great influence on multinational cases.

Since the UNCITRAL Model Law and the U.S. Chapter 15 use the same terms like the EIR, the result may be the introduction of a comprehensive system for dealing with cross-border insolvencies affecting states around the world.

However, these approaches still fail to provide advice in certain relevant issues. The EIR does not provide legislation for group companies. Therefore, the Member State court's interpretation of the EIR encounters problems when a parent company and its subsidiaries file for a collective insolvency proceeding and it is unclear where the centre of main interests of the subsidiaries is located. This issue is currently discussed at the EJC and the

final decision is awaited with interest. The ECJ ruling on the centre of main interests could influence the conduct of European companies with subsidiaries abroad, which file for bankruptcy. In these circumstances the centre of main interests could well be judged to the overseas courts, despite the fact that the subsidiaries may be incorporated in the EU. The ECJ ruling is also important in another aspect. Since the U.S. Chapter 15 and the UNCITRAL Model Law both also inherit the centre of main interests, the ruling may serve as judicial precedent around the world and will influence further insolvency proceedings.

Although a convergence of international insolvency law is unlikely,⁴⁰⁶ the globalisation of business will lead eventually to the harmonisation of insolvency systems of the world,⁴⁰⁷ since “a globalizing market requires a globalizing insolvency law”.⁴⁰⁸ Recent experience shows that the courts and the international community can achieve considerable progress without legislative action and that model law, treaties and cross-border insolvency protocols will do the work equally acceptable and comforting for the multinational debtor and its creditors.

⁴⁰⁶ See Paulus, IPRax 1999, 150.

⁴⁰⁷ See LoPucki, MLR 2002, 2217. See also Westbrook, MLR 2002, 2292-2297. See also Schaub, IFLR 2004, 20.

⁴⁰⁸ Westbrook, ABLJ 2002, 8.

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