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**COMMISSION STAFF WORKING DOCUMENT**

**IMPACT ASSESSMENT**

*Accompanying the document*

**Revision of Regulation (EC) No 1346/2000 on insolvency proceedings**

{COM(2012) 744 final}

{SWD(2012) 417 final}

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## **1. BACKGROUND AND POLICY CONTEXT**

At a time where the European Union is facing the biggest economic crisis in its history, the European Council has repeatedly emphasised the Union's role in promoting sustainable growth while pushing for financial consolidation. Growth has therefore been put at the heart of the Commission's agenda in the area of justice (“Justice for Growth”).

One of the measures supporting economic activities in the area of justice as set out in the Commission's Action Plan implementing the Stockholm Programme<sup>1</sup> is the revision of Council Regulation (EC) No 1346/2000 on insolvency proceedings (the “Regulation” or “EIR”). The Regulation establishes a legal framework for cross-border insolvencies in the European Union. From 2009-2011, an average of 200,000 firms went bankrupt per year in the EU, resulting in direct job losses each year of 1.7 million. About one-quarter of these bankruptcies have a cross-border element, and so fall under the EIR. As firms that trade cross-border tend to be larger than average, the share of the number of jobs affected is likely to be greater than the share of bankruptcies, even before taking into account the effects on creditors of these firms.

The Commission has put the revision of the EIR in its Work Programme for 2012. The revision links in with the EU's current political priorities to promote economic recovery and sustainable growth, a higher investment rate and the preservation of employment, as set out in the Europe 2020 strategy. The reform will also contribute to ensuring a smooth development and the survival of businesses, as stated in the Small Business Act<sup>2</sup>. The Annual Growth Survey 2012 announces the revision of the EIR, emphasising the importance of improving the effectiveness of cross border insolvency rules.<sup>3</sup> The revision is also one of the key actions listed in the Single Market Act II<sup>4</sup>.

The review of the Regulation also links in with the broader issue of improving the efficiency of justice in the European Union. In its experience with the Member States under an economic recovery programme, the Commission has identified the key role of judicial reforms, including reforms of national insolvency laws, as a means to promote economic recovery. This was reflected in the European Semester in 2012 by recommendations made to certain Member States relating to efficient insolvency proceedings. In October 2011, the European Parliament raised the same issue when adopting a resolution calling for the revision of the Regulation and further recommending the harmonisation of specific aspects of insolvency law and company law.

The revision of the Regulation will be adopted together with a report on its application, in line with the review clause of the Regulation<sup>5</sup>.

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<sup>1</sup> COM(2010)171, 20.4.2010.

<sup>2</sup> COM(2008)394,25.6.2008.

<sup>3</sup> COM(2011)815

<sup>4</sup> COM(2012)573,3.10.2012

<sup>5</sup> Article 46 reads: “No later than 1 June 2012, and every five years thereafter, the Commission shall present to the European Parliament, the Council and the Economic and Social Committee a report on the application of this Regulation. The report shall be accompanied if need be by a proposal for adaptation of this Regulation.”

## **2. PROCEDURAL ISSUES AND CONSULTATION OF INTERESTED PARTIES**

### **2.1. Impact assessment study and expertise**

DG Justice contracted two external studies to support the impact assessment: an evaluation study performed by the Consortium Heidelberg/Vienna University and an impact assessment study by the Consortium GHK/Milieu. The reports and results of these studies have been used for this Impact Assessment.<sup>6</sup>

In May 2012, DG Justice set up an expert group of 20 individual experts in the field of cross-border insolvencies. The group met five times from May to October 2012 and provided input on the problems, the options and helped on the drafting of the revised Regulation.

An IA Steering group was established in April 2012. Two meetings were organised on 3 May and 6 September 2012 and were attended by SG, SJ, ENTR, DGT, EMPL, COMP, MARKT, SANCO, CNECT, and ECFIN. The feedback received from the DGs has been taken into account throughout the report.

### **2.2. Consultation of the IAB**

This impact assessment report was presented to the Commission's Impact Assessment Board on 3 October 2012. The Board recommended streamlining the problem definition by grouping the presented problems and sub-problems. The Board also suggested providing more information on the Member States' insolvency regimes, in particular as regards the hybrid and pre-insolvency proceedings. The presentation of objectives and options was asked to be rechecked to follow the streamlined problem definitions. As regards objectives, more operation objectives were to be identified. Furthermore, the IA Board recommended to present more expressly the analysis of advantages/disadvantages of the planned measures as well as to strengthen the existing quantification e.g. of the administrative burdens. Finally, the Board proposed improving the presentation of stakeholders' views in the relevant parts of the report. The recommendations and suggestions are reflected in particular in chapters 3 to 6 that were further elaborated compared to the earlier version commented on by the IA Board and by the inclusion of a new Annex 5 on hybrid and pre-insolvency proceedings.

### **2.3. Stakeholders' consultation**

Stakeholders have been consulted as follows:

- Public consultation on the future of European Insolvency Law (29 March – 21 June 2012);<sup>7</sup>
- European Judicial Network in civil and commercial matters, meeting of Contact Points on 27 April 2012 and national insolvency experts;
- Meetings with business organisations such as UEAPME, Business Europe.
- Meetings with insolvency practitioners' organisations, such as INSOL Europe.

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<sup>6</sup> The reports of the studies are available in the Europa-website of DG Justice: [http://ec.europa.eu/justice/civil/document/index\\_en.htm](http://ec.europa.eu/justice/civil/document/index_en.htm)

<sup>7</sup>

<http://ec.europa.eu/yourvoice/ipm/forms/dispatch?userstate=DisplayPublishedResults&form=Insolvency>



The public consultation contained 31 questions related to the scope and the functioning of the Regulation. 134 answers were received from stakeholders in 25 Member States. While there are certain differences in opinion depending on the group of stakeholders (public authorities, businesses, legal practitioners), the answers to the consultation confirm the problems and options that the Commission had identified in the questionnaire. In particular, a majority of respondents consider that while the EIR works relatively well in general, it should accommodate national pre-insolvency procedures, it does not work for the insolvency of a group of companies, and finally, the absence of mandatory publication of decisions relating to insolvency procedures is a problem. A summary of the public consultation is in Annex 2.

The opinions of the stakeholders have been taken into account throughout the IA process in the determination of the problems, in particular on the extent of the problem and the most affected groups, and further, in the identification of possible solutions.

## **2.4. Analysis of Fundamental Rights**

With the Lisbon Treaty, the Charter of Fundamental Rights of the European Union (“the Charter”)<sup>8</sup> has become legally binding<sup>9</sup>. This means that the EU's institutions, as well as the Member States when implementing Union law, have to respect the rights, observe the principles and promote the application of the Charter in accordance with their respective powers<sup>10</sup>. For this reason, all legislative proposals proposed by the Commission are subject to systematic and rigorous monitoring to ensure their compliance with the Charter<sup>11</sup>. When assessing the impact of the envisaged initiative to improve cross-border insolvency proceedings, this report pays particular attention to fundamental rights in order to ensure that the proposed schemes fully respect the rights and principles set out in the Charter, in particular those in Article 17 (*right to property*), Article 16 (*freedom to conduct a business*), Article 47(2) (*right to a fair trial*) and Article 8 (*protection of personal data*). The basic rights and freedoms protected by the Treaties as well as the Charter, in particular the *free movement of persons, services and establishment*, Article 15 of the Charter, are also very relevant for this measure.

## **3. PROBLEM DEFINITION**

### **3.1. The key problems identified in the evaluation of the application of the Regulation**

The EIR establishes uniform EU level rules for jurisdiction, the recognition and enforcement of insolvency-related decisions, and applicable law. It also provides for some coordination of different proceedings relating to the same debtor. In short,

- The Regulation applies to legal and natural persons, whenever the debtor has assets or creditors in more than one Member State.

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<sup>8</sup> OJ 2010 C 83/02, 389ss.

<sup>9</sup> Cf. Article 6 TEU.

<sup>10</sup> Cf. Article 51 (1) of the Charter.

<sup>11</sup> Communication from the Commission “Compliance with the Charter of Fundamental Rights in Commission legislative proposals. Methodology for systematic and rigorous monitoring” COM (2005) 172; Report on the practical operation of the methodology for a systematic and rigorous monitoring of compliance with the Charter of fundamental rights”. COM(2009) 205.

- Jurisdiction for opening main insolvency proceedings lies with the court where the debtor has its centre of main interest (COMI). The opening decision and all other decisions issued by that court in the insolvency proceedings are recognised and enforced in all other Member States;
- Secondary proceedings can be opened in any Member State where the debtor has an establishment, i.e. any place where the debtor carries out economic activity. The effect of secondary proceedings is limited to the assets located in that Member State. The liquidator of the secondary proceedings has to cooperate with his counterpart in the main proceedings (and vice-versa) in order to coordinate the proceedings; and
- The law applicable to the insolvency proceedings is, in principle, the law of the opening of proceedings. This law determines, in particular, the ranking of claims and the procedural rights of the creditor.

Adopted in May 2000, the EIR applies since 31 May 2002.<sup>12</sup> It is binding for all Member States except Denmark.<sup>13</sup> The Regulation unified the private international law rules related to insolvency proceedings for all Member States as regards cross-border insolvencies inside the EU. However, it should be stressed that the Regulation did not harmonise the substantive insolvency legislations of the Member States, but insolvency laws vary from country to country. The different national solutions relating to certain aspects of insolvency laws are presented in Annexe 5.

Ten years after its entry into force, the Commission has evaluated the practical application of the Regulation. While the EIR is generally considered to operate successfully in facilitating cross-border insolvency proceedings within the European Union, the evaluation shows that a range of problems exists in the implementation of the Regulation and that the Regulation does not sufficiently reflect current EU priorities and national practices in insolvency law, in particular in promoting the rescue of firms in difficulties.

The evaluation of the EIR has highlighted the following key problems:

- (1) Obstacles to the rescue of companies and to the free movement of entrepreneurs and debt-discharged persons;
- (2) Difficulties in determining the appropriate jurisdiction to open proceedings;
- (3) Inefficiencies of cross-border procedures;
- (4) No legal framework to cover insolvency of groups of companies.

This section analyses the four problems, linking them together as they are interrelated. This means grouping the above problems around two themes, first problems regarding the scope of the Regulation and second, problems revealed in the implementation of the Regulation.

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<sup>12</sup> For Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia, the Regulation applies as from their accession in 1 May 2004 and for Bulgaria and Romania as from 1 January 2007.

<sup>13</sup> Denmark has opted out from the whole area of judicial cooperation in civil matters pursuant to Protocol (No 22) on the position of Denmark. UK and Ireland have possibility to opt-it to the instruments in the area of judicial cooperation in civil matters on the basis of Protocol (No 21) on the position of the UK and Ireland in respect of area of freedom security and justice, and they are participating to the EIR.

### 3.2. Problem group 1: Problems relating to the scope of the current Regulation

The first set of problems covers issues relating to gaps in the current scope of the Regulation, such as lack of provisions on pre-insolvency schemes, of provisions on debt discharge procedures for natural persons as well as of specific rules on groups of companies.

Indeed, the current Regulation covers “collective insolvency proceedings which entail the partial or total divestment of the debtor and the appointment of a liquidator”<sup>14</sup>. The debtor can be a natural or a legal person, a trader or a private individual<sup>15</sup>. The Regulation contains a list of national procedures which fulfil these criteria in its Annex A. It is for each Member State to decide whether it wants to notify a particular national procedure to be included in Annex A of the EIR.

Since the Regulation was enacted, many Member States have modernised their insolvency laws by introducing new procedures which aim at rescuing businesses, providing a second chance to honest entrepreneurs and allowing a debt discharge for private persons. Many of these new procedures are not covered by the Regulation and their effects are not recognised in other Member States. Moreover, although a large number of cross-border insolvencies involve groups of companies, the Regulation does not contain specific rules dealing with the insolvency of a multi-national enterprise group.

#### 3.2.1. *The Regulation does not cover national insolvency proceedings which aim at rescuing companies*

The EIR's definition of insolvency proceedings does not cover national procedures which provide for the restructuring of a company at a pre-insolvency stage (“pre-insolvency proceedings”) or leave the existing management in place (“hybrid proceedings”). However, such proceedings have recently been introduced in most Member States and are considered to increase the chances of successful restructuring of businesses. They enable financially distressed enterprises to become again competitive and productive participants in the economy, thereby benefitting not only their creditors but society at large.

**The benefits of business rescue can be summarized as follows:**

- **Maximisation of asset value:** The rescue of a company allows preserving the value of its technical know-how and business goodwill whereas liquidation is limited to the value of the company's physical assets<sup>16</sup>.
- **Better recovery rates for creditors,** i.e. the percentage of their debt that creditors get back: In France, the median recovery rates for liquidated firms are less than one-third of those for “rehabilitated” firms (31% vs. 96%); the same is true also for

<sup>14</sup> Article 1 of the EIR.

<sup>15</sup> See Recital 9 of the EIR.

<sup>16</sup> A Second Chance for Entrepreneurs, Prevention of Bankruptcy, Simplification of Bankruptcy Procedures and Support for a Fresh Start’, Final Report of the Expert Group (January 2011), DG Enterprise and Industry, available at [http://ec.europa.eu/enterprise/policies/sme/business-environment/files/second\\_chance\\_final\\_report\\_en.pdf](http://ec.europa.eu/enterprise/policies/sme/business-environment/files/second_chance_final_report_en.pdf), p. 7.; see also IMF, Orderly and Effective Insolvency Procedures (1999) available at <http://www.imf.org/external/pubs/ft/orderly/#genobj>

the UK, even though the difference between the median recovery rates seems smaller.<sup>17</sup>

- **Saving jobs.** Saving companies saves jobs. This is an important benefit given that the total number of insolvency related job reductions in 2009 is estimated at 1.7 million.<sup>18</sup>
- **Lower costs:** the costs of pre-insolvency and hybrid insolvency proceedings are on average lower than that of traditional insolvency proceedings.
- **Avoidance of reputational risks and directors' liability,**<sup>19</sup> allowing entrepreneurs to continue their activities.
- **Encouraging entrepreneurship:** fear of bankruptcy and its consequences acts as a deterrent to entrepreneurship,<sup>20</sup> efficient pre-insolvency and hybrid insolvency proceedings ease entrepreneurs' fears and encourage entrepreneurial activity.

The aim of these rescue proceedings is to help the recovery of fundamentally sound firms that face temporary difficulties; they are not intended to prevent the exit of inefficient firms from the market, as this would impede the growth of more efficient competitors and hamper structural changes in the economy.

The Heidelberg study revealed that almost two thirds of Member States have pre-insolvency or hybrid proceedings which are not covered by the Regulation with the consequence that there is no EU-wide recognition of their effects, notably the stay of individual enforcement actions. As a result, **the following problems occur:**

- **Foreign creditors can continue with individual enforcement actions** against the company and its assets; individual enforcement action can jeopardize the success of the rescue or restructuring. This possibility can in particular be used by dissenting foreign creditors (the so-called 'holding-out' problem).<sup>21</sup>
- **Foreign creditors will be less willing to fully engage** in restructuring negotiations or consent to rescue plans involving a certain reduction of their claims; as a consequence, the opportunity of rescuing the company may be lost.<sup>22</sup>
- **Opportunities for the continuation of businesses through pre-insolvency and hybrid proceedings are reduced and jobs are lost.**

These problems are reflected by the views of respondents to the public consultation in which 51% of those who expressed an opinion felt that the **lack of coverage of pre-insolvency or**

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<sup>17</sup> Forum Shopping and the Global Benefits of Soliciting Insolvency, p. 9 citing IMF, "2 – General Objectives and Features of Insolvency Procedures", p.8.

<sup>18</sup> The Expert Group, "A Second Chance for Entrepreneurs, Prevention of Bankruptcy, Simplification of Bankruptcy Procedures and Support for a Fresh Start.", Final Report for Directorate General Enterprise and Industry (2011) (available at [http://ec.europa.eu/enterprise/policies/sme/business-environment/files/second\\_chance\\_final\\_report\\_en.pdf](http://ec.europa.eu/enterprise/policies/sme/business-environment/files/second_chance_final_report_en.pdf))

<sup>19</sup> Nunez-Lagos, A., 'The scenario and trends', available at <http://www.eir-reform.eu/uploads/papers/PAPER%206-2.pdf>, p. 143.

<sup>20</sup> A Second Chance for Entrepreneurs, Prevention of Bankruptcy, Simplification of Bankruptcy Procedures and Support for a Fresh Start

<sup>21</sup> *ibid.*

<sup>22</sup> *ibid.*

**hybrid insolvency proceedings is problematic.** 59% also agreed the EIR should accommodate national pre-insolvency procedures, with academics, public authorities and **insolvency practitioners particularly in favour of this.** Views were mixed on exactly **which** proceedings should be covered and in particular where court oversight should be required.

Examples of problems raised included cases differing views of Member States on which proceedings could be covered by the EIR; uncertainty relating to schemes of arrangement available to UK firms in financial difficulty and how they are recognised at EU level and risks to workers interests.

**Case example: Rechtbank 's Gravenhage, judgment of 10 June 2010<sup>23</sup>**

A Dutch national had lived for several years in Germany and had taken out loans from several German banks to invest in the German property market. After his return to the Netherlands, his business went into financial difficulties and he was unable to repay the instalments on the loans. He eventually filed a petition with the court in The Hague requesting the opening of debt reorganisation proceedings under the Dutch Bankruptcy Act. In these proceedings, a debtor can request the court to oblige dissenting creditors that have not consented to an offer made by the debtor to do so if the judge considers that they are unreasonably withholding their consent from the proposed arrangement (“cram down”). However, the court refused to grant the requested order, arguing that since the debt reorganisation proceedings were not covered by the EIR, the cram-down of dissenting creditors would not be recognised in Germany, where the debtor's creditors were located, and therefore be ineffective. The Dutch entrepreneur had to apply for insolvency and have his business liquidated.

The case illustrates that the fact that a national pre-insolvency, hybrid or personal insolvency procedure is not covered by the EIR can prevent the successful rescue of business or reorganisation of personal debt in cross-border situations.

In addition, concerns have been raised that a few Member States have included proceedings in Annex A, which actually do not fulfil the criteria of the EIR. Following the ruling of the CJEU in the *Eurofood case*, a court cannot challenge the validity or appropriateness of any proceedings included in the Annex of the Regulation. This situation creates a **risk to mutual trust** since some courts do not consider it appropriate to recognise certain proceedings, yet they are required to.

*3.2.2. The Regulation does not effectively cover the full range of personal insolvency schemes of Member States*

The growth of personal over-indebtedness in Europe since the late 1980s has led to many Member States introducing personal insolvency schemes, including debt discharge proceedings<sup>24</sup>. Such personal insolvency scheme can be applicable either to individuals as

<sup>23</sup> Full decision available at [www.insolvencycases.eu](http://www.insolvencycases.eu) .

<sup>24</sup> Denmark (1984); France (1989); Finland (1993), Sweden (1994), Austria (1993), Germany (enacted 1994 but not in force until 1999), Belgium (1998), Netherlands (1997), Luxembourg (2000), England and Wales (2002), Portugal (2004), Latvia (2008) (based partly on English model of individual voluntary arrangement), Czech Republic (2008), Slovakia (2006), Slovenia (2008), Poland (2009), Greece (2010) (based partly on German model), Italy (2012), Ireland (on-going). Ramsay, I., ‘Between Neo-Liberalism and the Social Market: Approaches to Debt Adjustment and Consumer Insolvency in the EU’, EUI Working Papers 2011/09, available at [http://cadmus.eui.eu/bitstream/handle/1814/18255/2011\\_09.pdf?sequence=1](http://cadmus.eui.eu/bitstream/handle/1814/18255/2011_09.pdf?sequence=1) (accessed on 17 August 2012), p. 5.

entrepreneurs or consumers or both of them, depending of the Member State's political choices. This development reflects the increasing awareness that insolvency and the ensuing personal debt is a significant obstacle to entrepreneurship because entrepreneurs often finance their business using personal loans, possibly secured against their houses. The introduction of the possibility to obtain a debt discharge also aims to counter the negative social impacts which private over-indebtedness has on the individuals concerned and their families.

The Regulation covers the insolvencies of natural persons, and some MSs have indeed already notified procedures that apply to "consumer insolvencies". There seem to be no problems in the application of the Regulation to these proceedings in practice. However there is an obstacle to the coverage of further national personal insolvency procedures by the Regulation. While several personal insolvency procedures are covered by the Regulation, a considerable number of others are not<sup>25</sup>. This situation is partly because the proceedings do not match the EIR's definition - e.g. the Scandinavian procedures and some common law systems, because they do not foresee the appointment of a liquidator -, were only recently introduced or are not considered to fall within the scope of the Regulation by the respective Member States.

**As a consequence, some personal insolvency schemes are not recognised in other Member States** and there is a heterogeneous situation in the EU. The diversity of national laws adds complexity to the issue: Some Member states have no personal insolvency schemes at all. Other have personal insolvency schemes that apply both to self-employed or sole-traders and consumers. A third group has schemes only for consumers and include self-employed and sole-traders in company insolvencies, whereas a fourth group has separate schemes for consumers, self-employed and sole traders.

The current situation is a problem because it can result in debtors remaining liable to foreign creditors. However there is no good reason why the Regulation should discriminate between the personal insolvency proceedings available at national level and why it should cover some but not the others. Where a debt discharge procedure is not covered by the Regulation, the debt discharge has no effect against foreign creditors of the individual. Consequently, an honest entrepreneur, who has been discharged from its debts in one Member State may be prevented from starting a new business in or trading with another Member State, thereby affecting his freedom of establishment or to provide services and to conduct business. The problem can also discourage debtors who have benefitted from a debt discharge at home to live or seek employment in another Member State, thereby affecting the free movement of persons and workers. The fact that the EIR does not cover some personal insolvency schemes therefore constitutes an obstacle to offering a second chance to honest entrepreneurs and debt-discharged persons, and allowing them to make full use of the opportunities of the single market. This is in contradiction with EU policies on entrepreneurship.

Half of respondents to the public consultation (49%) agreed that the EIR should apply to private individuals/self-employed, while one third (34%) disagreed, with those in favour including judges, insolvency practitioners and academics. Some respondents did not think an expansion should include consumers.

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<sup>25</sup> Personal insolvency proceedings of AT, BE, CZ, DE, LV, NL, PL and UK are covered in the EIR but some of these Member States have not included all proceedings allowing a debt discharge of natural persons in the annex, e.g. the Dutch *schuldsaneringsregeling* and the UK debt relief orders and debt management plans are not covered. The personal insolvency proceedings of EE, EL, FI, FR, IT, LT, LUX, PT, SK, SL and SV are currently not covered in the Regulation; the EIR does not apply to DK. Moreover, some Member States which have included personal insolvency schemes in the annex have not included all their schemes.

### 3.2.3. *The Regulation does not effectively deal with the insolvency of groups of companies*

The basic premise of the Regulation is that insolvency proceedings relate to a single legal entity and that, in principle, separate proceedings must be opened for each individual member of the group. There is no compulsory coordination of the independent insolvency proceedings opened for a parent company and its subsidiaries. The Regulation has no provision allowing corporate groups to reorganise together or – where this is not possible – at least to coordinate their liquidation. Neither liquidators nor courts are under a duty to coordinate the independent proceedings opened for each group member. While it is possible for the liquidators in the respective main proceedings to coordinate their work in order to maximise the value of the group's assets or the prospects for successful restructuring, judges in many Member States are currently prevented from cooperating with each other because there is no legal basis authorising them to do so.

The lack of specific provisions for group insolvency is problematic because it often diminishes the prospects of successful restructuring and reduces the value of the group's assets. An individual group member may not be economically viable outside the group structure because the group is structured in a way that indispensable assets, e.g. intellectual property rights, or activities, e.g. cash management, are pooled in a different member of the group. In such cases, it will be difficult if not impossible to reorganise different group members separately.

Similarly, a significant part of the value of a group may lie in the cooperation of its members, e.g. distribution networks tailored to particular production patterns, operational and financial management, or simply business goodwill such as brand recognition. This value is lost when assets and affairs of related group members are liquidated separately rather than as a package. The following case is an example of how such piecemeal liquidation can lead to value destruction:

#### ***Case example: The insolvency of KPNQwest***<sup>26</sup>

The KPNQwest group owned cables running through a number of States and across the Atlantic Ocean. However, cables in Member States were owned by subsidiaries registered in those States. When the Dutch parent company, KPNQwest N.V., went into bankruptcy many of the subsidiaries had to enter insolvency proceedings as well. As a result it proved very difficult to coordinate the sale of the cables. The subsequent disintegration of the group likely resulted in much lower proceeds than if assets of the enterprise had been sold as a whole.

Case-law has tried different ways to overcome the lack of specific provisions on group insolvency:

In the first years after the entry into force of the Regulation, some national courts interpreted the Regulation's rules on jurisdiction broadly so as to bring insolvency proceedings for all members of the group, including those located in another Member State, before the court at the parent company's registered office. The courts concerned generally justified such a consolidation of insolvency proceedings on the grounds that the subsidiaries' commercial decisions were controlled by the parent company<sup>27</sup>. This approach has obvious advantages in

<sup>26</sup> Van Galen, R., 'The European Insolvency Regulation and Groups of Companies', INSOL Europe Annual Congress, October 2003, p. 2.

<sup>27</sup> This approach began in England and was adopted by courts in Member States such as France, Germany, Hungary and Italy, cf Christoph Paulus, Group Insolvencies – Some thoughts about new approaches, Texas International Law Journal, vol 42, p. 819, 822.

terms of efficiency but was also criticised for not respecting the legitimate expectations of creditors who did not contemplate the application of the parent company's law to the insolvency proceedings and, in particular, the ranking of their claims when entering into commercial relationships with the subsidiary<sup>28</sup>.

The 2006 CJEU's *Eurofood* decision considerably reduced the scope of application of the possibility for such procedural consolidation and reinforced the rule that each legal entity should be treated separately<sup>29</sup>. According to the Court, control of corporate direction alone does not suffice to locate the centre of economic interest of a subsidiary with its parent company, rather than at its own registered address. After *Eurofood*, it is still possible to open insolvency proceedings over a subsidiary in the Member State where the parent company has its registered office, but only if the factors showing that the subsidiary's COMI is located at the seat of the parent company are objective and ascertainable by third parties. This means in practice that courts have to examine a complex bundle of factors, including whether the financing of a subsidiary is taken care of by the parent company, whether the parent company controlled the operational business (e.g. by approving purchases above a certain threshold) and the hiring of staff, whether certain functions (e.g. the management of the IT equipment or the visual/business identity) were centralised<sup>30</sup>. Essentially, these conditions will only be fulfilled in the case of heavily integrated companies.

Another approach taken in practice is the appointment of the same insolvency practitioner in the proceedings of all members of the group involved, or of insolvency practitioners who have previously worked together successfully on group insolvencies<sup>31</sup>. Such best practices may reduce the problems outlined above. However, without specific rules on group insolvency, the success of such measures will depend on the willingness of the respective insolvency practitioners and judges to cooperate.

The reason for the lack of specific rules on enterprise groups in the Regulation is threefold: when the Convention that later became the Regulation was negotiated in the 1980s and 1990s, the phenomenon of groups of companies was not as widespread it is today. The drafters of the Insolvency Convention conceived multinational operations to be structured predominantly as “establishments” in other Member States rather than independent legal entities. Moreover, at that time, the reorganisation or rescue of companies was not a prevailing option in the domestic insolvency laws of Member States and liquidation was the norm. Finally, the creation of rules for groups of companies raised complex problems and it may have been considered politically and practically prudent to postpone it to a later date<sup>32</sup>. The UNCITRAL Model Law on cross-border insolvency which was adopted two years after the European Insolvency Convention in 1997 also does not contain any rules on group insolvency<sup>33</sup>.

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<sup>28</sup> The Regulation provides that the law applicable to the insolvency proceedings and, in particular, the ranking of creditors is the law of the State where proceedings are opened, i.e. usually the place of the company's registered office. If proceedings are opened in a different country, e.g. that of the parent company, creditors are faced with different rules than those on which they based their risk assessment when entering into commercial relations with the subsidiary.

<sup>29</sup> Case C-341/04 *Eurofood IFSC Ltd*, 2006, at para 30.

<sup>30</sup> See e.g. the decision of the High Court in *Daisytek*, 16.5.2003.

<sup>31</sup> E.g. Nortel

<sup>32</sup> See Bob Wessels, *Multinational Groups of companies under the EC Insolvency Regulation: Where do we stand*, 2009 at [www.bobwessels.nl](http://www.bobwessels.nl); Alain Stomel, *Answering the call of the European Court of Justice in Eurofood*, IES Working Paper 10/2011; Nicolaes W.A. Tollenaar, *Proposal for Reform: Improving the ability to rescue multinational enterprises under the European Insolvency Regulation*, IILR 2011, p. 252.

<sup>33</sup> A legislative guide on the treatment of enterprise groups in insolvency was only adopted in 2010.



Half of respondents to the public consultation (49%) felt the **EIR does not work efficiently for multinational group** insolvencies with one third (30%) feeling it does.

### **3.3. Who is affected by problem group 1 and what is the extent of these problems?**

The problems set out above affect all parties involved in insolvency procedures. Debtors are affected in their capacity to rescue and continue their business (which impacts on their freedom to conduct business in the EU); creditors are affected as the problems reduce the value of the assets and their recovery rate. SMEs, which tend to be heavily dependent on one or a small number of large customers, can be particularly affected by the liquidation of one of them. Employees are affected because they lose their jobs if a restructuring fails due to the problems outlined. Tax and social security authorities (as creditors) see the chances of contribution payments by companies reduced.

On the other hand, the gaps in coverage of personal insolvencies primarily affect the individual debtors whether they are professionals, sole traders or consumers. However, doubts over the recovery of assets and difficulties that can occur with restructuring plans also reduces the readiness of foreign businesses and banks to grant credit to natural persons. Ultimately, given the impacts of indebtedness on entrepreneurship and on individuals including their family life, health and work, this will have impacts on society and on the economy.

Between 2009 and 2011, more than 200,000 companies, or about 1% of all EU companies, went bankrupt per year in the EU<sup>34</sup>, which means more than 550 companies go bankrupt every day. It is estimated that about 1% of these insolvencies concern companies which are member of a multi-national group of companies. This means that more than 2 100 companies (2050 SMEs and large enterprises) are affected by inefficiencies in handling group insolvency (for details see Annex 6).

The job losses are estimated to be about 1.7 million per year. It is estimated that 25% of European companies (about 5 Million) have customers, creditors or business partnerships (subsidiaries, joint ventures or branches) in other Member States and are therefore potentially affected by the Regulation as debtors or creditors in case of an insolvency. About 50,000 companies (1% of 5 Million) per year will be debtors and at least twice as many will be creditors in a cross-border insolvency to which the EIR applies. As to the relevance of secondary proceedings, there are close to 700 enterprises with foreign establishments entering into insolvency procedures every year. Insolvency proceedings for these companies can potentially trigger secondary proceedings in the Member States where their establishments are located. (See Annex 3 for further details).

Cross-border insolvencies particularly affect large companies because these are more likely to do business across borders than SMEs. The insolvency of a large company has significant effects on the European economy because large companies, although only representing 0.2% of European companies, provide 30% of jobs in the EU and produce 41% of gross added value. Essentially, the larger a company, the more likely it is to be a member of a group. According to the April 2011 report of the Reflection Group on the Future of EU Company Law, the international group of companies has become *the* prevailing form of European large-sized enterprises, in which business activity is typically organised and conducted through a multinational network of subsidiaries. About 20% of large enterprises (ca. 8,500) have foreign subsidiaries or joint ventures<sup>35</sup>. By contrast, only 5% of EU SMEs have reported that they

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<sup>34</sup> Estimates by Creditreform; see Annex 6 for details.

<sup>35</sup> 2007 Eurobarometer survey, for details see Annex XXX.

have subsidiaries or joint ventures abroad. Nevertheless, with over twenty million SMEs in the EU as a whole, this means that there are more than one million SMEs in Europe which have subsidiaries or joint ventures abroad<sup>36</sup>.

Moreover, large companies will often source their supplies from smaller companies, possibly located in a number of Member States, so that the insolvency of a large company can have sizeable knock-on effects, as the following example shows:

#### **The bankruptcy of MG Rover**

MG Rover was a British manufacturer. The company was formed in 2000 out of the car-making and engine manufacturing assets of the original Rover Group. When the company went into liquidation in 2005 more than 6,000 workers at MG Rover lost their jobs and as many as 25,000 jobs were reported to have been lost in related supply industries, meaning that the total number of job losses brought on by MG Rover's collapse was somewhere in the region of 30,000.

Where pre-insolvency and hybrid proceedings exist, companies increasingly resort to them rather than to traditional insolvency proceedings because they are considered to be particularly effective in rescuing troubled businesses. Since the French *sauvegarde* procedure was introduced in 2006, the number of enterprises resorting to it has reached more than 1000 per year. While this number may seem small compared with the 58,195 companies that had recourse to the traditional insolvency proceedings (*redressement judiciaire* and *liquidation judiciaire*) in 2011, many *sauvegarde* proceedings apply to big and medium-sized companies and enterprises, meaning that their impact on employment and the economy at large is out of all proportion to the number of companies making use of these proceedings<sup>37</sup>. The positive economic effect of pre-insolvency and hybrid proceedings is also corroborated by data from the OECD which shows that the rate of loss of manufacturing companies is lower in countries where those proceedings are available (1.8 versus 2.6%)<sup>38</sup>.

As regards personal insolvencies, it is estimated that for the 17<sup>39</sup> Member States with personal insolvency schemes, there were around 470,000 insolvencies in 2011 (for details see Annex 5). On the basis of this figure, the number of personal insolvencies which are currently not covered by the EIR can be estimated at about 200,000 per year<sup>40</sup>. Not all of these individuals will want to make use of their freedom to move to another Member State but for those who do, the absence of the recognition of their debt discharge in another Member State would constitute a significant deterrent.

### **3.4. Problem group 2: Problems in the implementation of the Regulation**

Various difficulties have been experienced in the practical implementation of the EIR, concerning e.g. difficulties with the definitions and difficulties when the main and secondary proceedings run in parallel. There are also problems in practice caused by lack of transparency or by lack of facilitation of lodging claims.

<sup>36</sup> Internationalisation of European SMEs, EIM, report for DG Enterprise and Industry.

<sup>37</sup> GHK/Milieu report

<sup>38</sup> GHK/Milieu report

<sup>39</sup> Denmark is not counted because the EIR does not apply to Denmark.

<sup>40</sup> Exact figures exist for FI, FR, ES, SV and the UK. Given that only some UK schemes are covered by the EIR, only half of the UK personal insolvencies were counted. For the remaining five countries, the median rate of 12603 personal insolvencies was taken.

### 3.4.1. No definition for COMI and consequent difficulties relating to determining jurisdiction for opening insolvency proceedings (the concept of COMI) and forum shopping

#### 3.4.1.1. Determination of jurisdiction

The Regulation grants jurisdiction to open main insolvency proceedings to the courts of the Member State where the debtor has its centre of its main interests (“COMI”). The concept of COMI is crucial for the functioning of the EIR because, subject to the opening of secondary proceedings, the entire international insolvency case will be handled in the Member State of the COMI and be subject to that State's insolvency law.

The EIR does not offer a definition of COMI. It only contains a presumption that the COMI of a company is located at the place of its registered office. A recital clarifies that COMI should correspond to the place where the company “conducts the administration of its interest on a regular basis and in a manner ascertainable by third parties”<sup>41</sup>.

The concept of COMI has considerable merits because the emphasis on the real seat rather than on mere formalities ensures that the case will be handled in a jurisdiction with which the debtor has a genuine connection rather than in the one chosen by the incorporators. COMI has also been chosen as a jurisdictional standard by UNCITRAL in its Model Law on cross-border insolvency.

While there is general support for the concept of COMI as such – 77% of the respondents to the public consultation approved the use of COMI to determine jurisdiction for main proceedings – its application in practice has given rise to difficulties<sup>42</sup>. 51% considered that the interpretation of the term COMI by case-law caused practical problems, with the most critical being private individuals/self-employed (67%), banks (75%), judges (58%), and insolvency practitioners (61%). While some felt clarifications given by the ECJ have been very helpful to achieve a more uniform application of the term, the COMI standard has been criticised for being too vague and unclear, making it difficult for the parties concerned to predict the decision on jurisdiction and for the courts involved to decide in a coherent manner.<sup>43</sup> It has also been reported (for example, in the Heidelberg study) that national courts are not sufficiently aware of the jurisprudence of the CJEU.

Furthermore, the procedural framework for determining jurisdiction in many Member States has been criticised as being deficient. There is no routine examination of jurisdiction in several Member States<sup>44</sup>. Even where there is, judges often do not specify whether the proceedings are main or secondary proceedings under the EIR. In addition, many national procedures do not give creditors the possibility to make their views heard, because there is no

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<sup>41</sup> Cf Recital 13.

<sup>42</sup> Asked whether the interpretation of the term COMI by case-law causes problems in practice, a small majority of national reporters of the Heidelberg/Vienna study answered in the affirmative. Most of those answering in the negative did so because they were unable to report cases on COMI from their jurisdiction, LT, LUX, MT, HU, SL, RO, NL (cf answers to Question 7).

<sup>43</sup> It has notably been argued that the assessment of multiple factors required by the Court of Justice to determine COMI (e.g. in CJEU C-396/09, judgment of 20.10.2011 *Interedil Srl*, para 53; C-341/04, judgment of 2.5.2006 *Eurofood*, para 33-36) requires a complex analysis which is prone to diverge between courts.

<sup>44</sup> The EIR does not contain an express obligation for the court opening insolvency proceedings to investigate the international jurisdiction, although the CJEU held repeatedly that this obligation follows from the system of the EIR.

hearing on the opening of proceedings or no effective means to challenge the opening decision.

The problems of the procedural framework make it difficult for a judge seized with a request to open proceedings to determine whether proceedings have already been opened in another Member State and, if so, which type of proceeding is still “available” to be opened by him. This risks the opening of parallel main proceedings with ensuing conflicts of competence. These issues also facilitate forum-shopping by debtors applying for the opening of proceedings in a Member State with a more favourable insolvency regime (see immediately below).

#### 3.4.1.2. COMI shift

The EIR's jurisdiction rules have also been criticised for allowing forum shopping by companies and natural persons through abusive COMI-relocation. It does indeed happen that a debtor relocates its COMI to another Member State but not all such relocations can be considered abusive.

There are various reasons for moving COMI to another country. Most of these are not directly related to insolvency: the move may be driven by the desire to benefit from the better market conditions, working opportunities, tax regime or company law of another country.

In relation to **companies**, such moves have been accepted by the Court of Justice as a legitimate exercise of the freedom of establishment. Thus, the Court of Justice clarified in its *Centros* decision that doing business in a Member State through a company incorporated in another Member State is covered by the freedom of establishment, even if the company's registered seat was chosen to avoid the minimum capital requirement rules of the Member State of the company's real seat and it was never intended to conduct business in the State of incorporation<sup>45</sup>. There are also cases of companies relocating their COMI specifically with the aim of benefitting from a more favourable foreign insolvency regime. Such COMI shifts often occur with the consent or at the instigation of the (senior) creditors in order to facilitate the company's restructuring. There are several cases where COMI relocation to the UK allowed the successful restructuring of a company because of the flexibility which English insolvency law grants companies in this respect<sup>46</sup>.

COMI-relocation has also been reported with respect to **over-indebted natural persons**. This phenomenon has been termed “bankruptcy tourism” and has recently become popular with Irish debtors moving – really or allegedly - to the UK to get a quicker discharge of their debts (the discharge period currently being 1 year in the UK vs. 12 years in Ireland, although reforms of bankruptcy laws currently being considered would cut this to 3 years). The UK is also a popular destination for over-indebted persons from Germany and Eastern Europe. Cases of bankruptcy tourism are also reported from northeast France where German nationals seek to obtain a quicker discharge of their debt, and from Latvia where over-indebted Lithuanians seek relief in the absence of a personal insolvency regime in their home

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<sup>45</sup> CFEU, Case C-217/97, judgement of 9.3.1999, *Centros Ltd.*

<sup>46</sup> E.g. the companies Deutsche Nickel and Schefenacker where COMI was shifted from Germany to the UK by way of a transfer of assets and liabilities, thereby allowing the companies to apply for an English company voluntary arrangement (CVA). The moves were vital for the survival of the companies because the English CVA allowed a debt for equity swap and the release of guarantees without which the group was likely to have collapsed, see Webb and Butler, p. 39; in the *Damovo* and *Wind Hellas* cases, COMI was shifted from Luxemburg to the UK in order to benefit from the English possibility of a pre-packaged administration sale.

jurisdiction<sup>47</sup>. Bankruptcy tourism is problematic because a debtor takes advantage of a more favourable insolvency regime in another jurisdiction without genuinely relocating to the other Member State, to the detriment of his creditors who are prevented from enforcing their claims. A genuine relocation to another Member State is an exercise of the right to freedom of movement and establishment and justifies the application of the insolvency regime of that other country; a sham move does not.

The problem of abusive COMI relocation can be illustrated by the following case:

#### **Case example Sparkasse Velbert v. Benk<sup>48</sup>**

Mr. Benk was a German notary who had run into financial difficulties, notably owing €3 Mio to his bank, the Sparkasse Velbert. Enforcement proceedings by the Sparkasse against Mr Benk's real estate and pension fund in Germany were pending. In June 2009, Mr. Benk was suspended from his practice as a German notary because of his unsound financial situation and filed for bankruptcy in the UK later that month. Mr Benk alleged COMI in the UK claiming that he had lived in Birmingham since late 2008 and exercised a professional activity as a sports photographer. The discharge order was granted on 17 June 2010 following which Mr. Benk moved back to Germany.

On appeal by the Sparkasse, the High Court carried out an in-depth examination of the circumstances of the case. It discovered that Mr. Benk had relocated with the help of a German relocation agency which had assisted him with renting a furnished room in Birmingham as well as purchasing and registering a car in the UK. Moreover, Mr. Benk's business as a sports photographer was loss-making from day one as his only client was an old friend from Germany and he had not even owned a camera in the first months in his new "job". The court concluded from the evidence that Mr Benk's COMI was in Germany at the time of the presentation of the bankruptcy petition because he had neither his habitual residence nor his professional domicile in England, as his presence in England was only temporary and the photography business was merely window-dressing, with no potential for any significant degree of permanence. Consequently, the discharge order was annulled and the Sparkasse could continue enforcing its claim against Mr. Benk. However, the appeal cost the Sparkasse about €50000 in lawyers' fees because on appeal, it is the creditor who has to prove that a COMI shift was not genuine. The high costs of appealing a court decision in the UK deter many creditors from challenging a debt discharge for their debtor because they are not sure to be able to recover the legal costs from the insolvent debtor.

The problem of forum shopping is essentially driven by differences in national insolvency and company laws. In the absence of harmonisation at EU or international level, Member States' insolvency laws and procedures vary considerably and offer a range of advantages and disadvantages to companies and individuals. For example, the flexible regime for restructuring companies offered by English law, and, in particular, the pre-packaged administration sales which enables a company to restructure by wiping out some of its creditors and converting into a new company shorn of its liabilities<sup>49</sup>, attracts companies from

<sup>47</sup> This situation is likely to change with the introduction of a new law on personal insolvency in Lithuania.

<sup>48</sup> Decision of 29.8.2012 by Judge Purle QC, High Court, Chancery Division, Birmingham District Registry, [2012] EWHC 2432 (Ch).

<sup>49</sup> The English pre-packaged administration sale (or prepack) is a procedure by which a company is put into administration and where the administrators, immediately following their appointment, sell the business and its assets under a sale that was arranged with their knowledge prior to their formal appointment. The central appeal of a pre-pack lies in its speed and its ability to preserve the value of the

other European jurisdiction. Even more strikingly, periods for the discharge of personal debts vary widely across the EU: in some Member states there is no discharge at all (e.g. Bulgaria), meaning that debtors remain liable for life, while in others it is possible to obtain discharge within a few or even one year (e.g. UK).

Half of the respondents (49%) indicated **evidence of abusive relocation of COMI** with less than one third (29%) feeling there was no abusive relocation. The most common situation cited was moves to UK in particular from Ireland and Germany with relief of the debtor and the promotion of rescue culture towards businesses in the UK being suggested as drivers.

### 3.4.2. *Relationship between the main and the secondary proceedings under the Regulation*

The EIR allows secondary proceedings to be opened where the debtor has an establishment but provides that secondary proceedings must be winding-up or liquidation proceedings, that is, cannot be restructuring or rehabilitation proceedings. This requirement has triggered criticism that the EIR is oriented towards liquidation rather than rehabilitation, and is therefore incompatible with today's "corporate rescue" culture. A vast majority of stakeholders consider this to be a problem.

The narrow scope of secondary proceedings can constitute an obstacle to the successful restructuring of a company having branches in several Member States, thereby diminishing the total value of the debtor's assets and destroying jobs. This sub-problem therefore reinforces the first sub-problem that the current Regulation constitutes **an obstacle for the continuation of business and the saving of jobs**.

The problem can be illustrated by a case which is currently pending before the Court of Justice of the European Union:

#### **Case example: Bank Handlowy and Ryszard Adamiak v. Christianopol sp.zoo (C116/11)**

Christianopol is a Polish company specialised in the production of furniture. It is part of the Cauval Industries Group with its head office in France to which it supplies all its production. The group suffered from the recession and went into financial difficulties. In an attempt to rescue the group, several members, including *Christianopol*, filed for *sauvegarde* proceedings in France. These proceedings aim at permitting solvent companies to restructure themselves under court protection at a pre-insolvency stage. They are covered by the Regulation although concerns have been raised as to whether they comply with the definition

One of the Polish creditors of Christianopol, Bank Handlowy, applied for secondary proceedings in Poland where the company's furniture factory was located. The winding-up of the factory would have prevented the successful implementation of the restructuring plan elaborated in the French *sauvegarde* proceedings. This problem prompted the Polish court to seek a preliminary ruling from the CJEU.

In her conclusions of 24 May 2012, advocate-general Kokott strongly encouraged the European Legislator to modify the Regulation:

55. « L'exposé de la juridiction de renvoi montre clairement qu'une procédure secondaire de liquidation peut gêner, voire mettre en échec les objectifs d'une telle procédure de redressement [*procédure de Sauvegarde*]. Ce résultat n'est effectivement pas souhaitable. Si

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business because the sale of solvent parts of the business can take place before the financial and reputational damage that results from prolonged insolvency can occur.

l'on songe en particulier que la législation en matière d'insolvabilité de nombreux États membres s'est éloignée des procédures de liquidation «pures» au profit de procédures de redressement et de réorganisation, et compte tenu des ajouts qui ont été de ce fait apportés à l'annexe A du règlement ces dernières années, intégrant également de plus en plus de procédures de redressement, il apparaît que ces procédures sont de plus en plus importantes et devraient, par conséquent, également relever du champ d'application du règlement.

56. Indépendamment de ces ajouts apportés à l'annexe, le texte même du règlement n'a cependant pour le reste subi aucune modification, ce qui peut concrètement générer des contradictions ou des problèmes pratiques, comme en atteste cette affaire. »

Moreover, the opening of secondary proceedings can jeopardize the efficient administration of the estate: Under the current Regulation, main insolvency proceedings have EU-wide effect and encompass all of the debtor's assets. Secondary insolvency proceedings can be opened in any other Member State where the debtor has an establishment. The system of secondary proceedings was introduced to protect the interests of local creditors and/or to facilitate the administration of complex cases. In practice, however, secondary proceedings can obstruct both the effective administration of the estate and the successful reorganisation of a company, because the opening of secondary proceedings removes part of the assets from the control of the insolvency administrator of the main proceedings. Secondary proceedings also increase the costs of proceedings because an additional insolvency practitioner has to be paid.

The problems arising from a lack of coordination between main and secondary proceedings are illustrated by the following case:

#### ***Case example: The liquidation of Alitalia***

By August 2008, the well-known airline Alitalia was heavily insolvent. In September of the same year, extraordinary administration proceedings aiming at reorganising the company were opened in Italy and an administrator was appointed. Since Alitalia's COMI was in Italy, these proceedings were main proceedings for the purposes of the EIR. The administrator found a buyer for the company's assets which, however, took over only those employees indispensable for the operational activity. All other employment contracts were terminated but the administrator reached an agreement with the employees which provided for a payment of an equivalent of 3 months' salary in compensation for the failure to comply with the information and consultation requirements under the Directive on Transfer of Undertakings. The administrator kept one of the company's UK bank accounts with funds sufficient to make the compensation payment to the 46 UK employees.

In November 2008, secondary proceedings over the UK branch of Alitalia were opened in the UK. The UK liquidator blocked the distribution of the monies to the UK employees, arguing that under UK law employees had no priority rights and divided the sum among all of Alitalia's UK creditors. This argument was approved by the High Court<sup>50</sup>. As a consequence, the Italian administrator was obliged to pay the UK employees from the funds of the Italian estate to the detriment of other unsecured creditors.

This shows that the opening of secondary proceedings can jeopardize the efficient administration of cross-border insolvency because the main administrator is no longer in control of assets located in the country where secondary proceedings have been opened.

<sup>50</sup> Judgment by Justice Newey, High Court of Justice, Chancery Division, Companies Court, 18.1. 2011, [2011] EWHC 15 (Ch).

When secondary proceedings are opened, all actors involved report that there is a lack of coordination between the main and secondary procedure. In order to ensure the coordination of proceedings opened in several Member States, the Regulation obliges insolvency practitioners to communicate information and cooperate with each other. Several guidelines for practitioners on cooperation and communication in cross-border insolvencies have been developed by associations of practitioners<sup>51</sup>. In practice, this cooperation works well when the practitioners have common interests and/ or have developed a working relationship but is more difficult where this is not the case.

However, cooperation between liquidators alone does not suffice to ensure efficient coordination of cross-border proceedings. There are no similar duties of cooperation between the courts and between insolvency administrators and the courts. As a result, the judge in the main proceedings is not informed of relevant developments in the secondary proceedings before deciding on further actions and vice-versa. Further the judge who exercises control of the activities of the liquidator in the main or secondary proceedings has no means to control the coordination.

The failure to co-ordinate can result in numerous problems and impacts which reduce the efficiency of proceedings, and increase their length and costs. Ultimately, chances to maximise the value of the assets may be lost. Problems are disagreements over the distribution of assets, difficulties in achieving restructuring plans, and a lack of notice or information about proceedings which prevents creditors from effectively participating in them.

Difficulties in cooperation may arise when the liquidators of the main and secondary proceedings are effectively in competition with each other to maximise assets for their creditors, despite the fact that a coordinated approach may result in greater overall returns. The additional cost of cooperation, language barriers and national procedural rules preventing the disclosure of information may also be a source of difficulties in cooperation.

Finally, the absence of rules in the EIR for cooperation between judges makes this cooperation between practitioners difficult to control.

### *3.4.3. Difficulties in practical implementation relating to lack of publicity of the decisions relating to an insolvency procedure and to lodging of claims*

The good functioning of cross-border insolvency proceedings relies to a significant extent on the publicity of all relevant decisions relating to an insolvency procedure. In particular, a court opening insolvency proceedings needs to know whether the company or person is already subject to insolvency proceedings in another Member State.

The Regulation leaves it up to the insolvency practitioners to decide whether to request publication and registration of the opening judgment in another Member State, or up to Member States to impose mandatory publication and registration. Today there is no systematic publication or registration of the decisions in the Member States where a proceeding is opened, nor in Member States where there is an establishment. There is also no European Insolvency Register which would permit searches in several national registers.

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<sup>51</sup> The most recent example are the Global Principles for Cooperation in international insolvency cases from the American Law Institute and the International Insolvency Institute, elaborated by Ian Fletcher and Bob Wessels (2012).



Therefore there is always the risk that a judge does not know that a procedure has already been opened in another Member State. This situation results in judicial battles and wrong decisions that cannot be reversed once the assets have been liquidated.

The lack of information on existing proceedings has resulted in unnecessary concurrent proceedings being launched. Even if the problem is resolved on appeal, parallel proceedings may have been going on for several weeks, thereby entailing not only legal uncertainty about who has the power to direct the debtor's estate but also legal costs for determining the procedure which takes priority.

The problem is illustrated by the German – UK case set out below:<sup>52</sup>

**Case example: Opening of parallel insolvency proceedings<sup>53</sup>**

A temporary insolvency administrator, charged with the divestment of a debtor, was designated by a German court. Four days after the designation, main insolvency proceedings were opened in England. Upon appeal by the German liquidator, the Croydon County Court held that the designation of a temporary main insolvency administrator had to be recognised as if the main proceedings had been opened in Germany and, since the opening of the German proceedings occurred prior to the opening of the English proceedings, reversed the decision opening proceedings in England.

Further, when the decisions are not publicly available in the EU, there is always the risk that unknown creditors are unaware of the on-going procedure, and further that potential customers, employers or banks do not know that a company or a person is subject to an insolvency proceeding or debt-discharge scheme.

For the good coordination of proceedings, the information contained in the decision, such as the type of procedure, the name of the administrators, their tasks and mandate, are also essential elements. This information is also necessary for the efficient lodging of claims for creditors in another Member State. Today it is sufficient to publish only notice of the opening decision.

It is also essential that the decision closing a procedure, e.g. a liquidation or debt discharge, be accessible, as being registered as insolvent may have serious consequences on the capacity of persons/companies and on their rights. The Regulation currently takes no account of this issue. A ruling of the ECtHR against Italy has held that the entry of a debtor's name in the bankruptcy register without any subsequent possibilities of updating or deleting it had prevented the applicants from developing their social and business relationships with the outside world which resulted in violation of the right to respect for their private life.<sup>54</sup>

There is widespread support for the conclusion that the failure to publish the opening of proceedings in a public registry reduces considerably the ability of stakeholders to know about proceedings. The public consultation results showed that the vast majority of respondents (86%) who expressed an opinion agreed that the absence of mandatory publication of the decision opening proceedings is a problem.

<sup>52</sup> Other examples include Local Court (AG) Köln 6/11/2008, 487/07, NZI 2009, 133; AG Nürnberg 15.8.2006 and 1.10.2006

<sup>53</sup> County Court Croydon 21/10/2008 1258/08, NZI 2009, 136

<sup>54</sup> *Albanese; Campagnano and Vitiello v Italy* App no 77924/01, 77955/01 and 77962/01 (ECtHR 23

The evaluation study and respondents to the public consultation (in particular the European Association for SMEs) have reported that creditors experience difficulties in lodging claims under the Regulation.

In the first place, it is sometimes difficult for creditors to obtain information on the opening of proceedings and the person designated as insolvency practitioner. Furthermore, liquidators do not always inform creditors in due time about their right to lodge a claim. This may entail the total loss of the claim if it is lodged after deadlines under national law have expired. In some Member States, deadlines for lodging claims are very short and do not take into account the additional time a cross-border filing may require. Creditors also complain about being insufficiently informed about the formalities regarding the lodging of their claim and about how to contest decisions by the liquidator to reject a claim. In addition, it is not clear under the current Regulation whether claims must be lodged in the language of the country in which the proceedings are conducted.

As a result, foreign creditors lodging their claims often have to bear not only translation costs but also legal costs in order to obtain advice on the foreign insolvency law. Moreover, in certain Member States, representation by a lawyer in the lodging of claims is mandatory. The costs and difficulties act as a deterrent for small creditors.

***Case example***<sup>55</sup>

A foreign creditor had not been informed in time by the French administrator of the insolvency proceedings and therefore was unable to lodge a claim within the proscribed deadline. The French Court of appeal dismissed the creditor's claim, arguing that the Regulation did not provide for extensions to deadlines under national law and that French national law did not provide for remedies against a violation of the duty to inform creditors under Article 40 EIR.

**3.5. Who is affected by problem group 2 and what is the extent of these problems?**

The problems relating to determining jurisdiction for opening insolvency proceedings and forum-shopping affect in the first place creditors and their expectations as to the law applicable to the insolvency. It is again mostly creditors, both of the main and secondary proceedings, who are affected by the coordination problems as there is no maximisation of assets and the recovery rate is smaller. Viable companies and their employees are also affected as any plans for restructuring the business are thwarted by the opening of secondary proceedings.

The transparency and claiming problems affect all stakeholders:

- Judges, as they are not informed of other proceedings being opened already, with the risk of the wrong decisions being made. They can lack of information before taking decisions and also lack of means to control the coordination.
- Insolvency practitioners, as the burden of publication relies heavily on them. They are faced with a variety of practices and obligations in each Member State. This increases their costs at the expense of all creditors. There are also problems when they are unable to cooperate and maximise the efficiency and the value of assets.

<sup>55</sup> CA Bordeaux (Mankowski) 3/1/2011 No. 09/04655, IILR 2012, 72.

- Existing creditors, as the information about insolvency proceedings in which they might be involved is not readily available and might prevent them from lodging their claims.
- Potential new creditors including consumers who are not informed of their situation
- Debtors (companies and natural persons), as the decision closing the proceedings is not always publically known or available.
- All foreign creditors and in particular SMEs are affected with claiming problems, since the costs of translation and legal advice are often too high for them.

As regards the extent of the problems, issues relating to determining COMI are a frequent source of litigation although practitioners confirm that COMI litigation is becoming less frequent. Research on the basis of 500 cases reviewed concluded that COMI issues arise in 40-50% of the cases albeit sometimes not as a contested issue but simply as a statement of the court satisfying itself of its jurisdiction<sup>56</sup>. A study carried out by a UK academic revealed that the COMI concept is actually applied with some consistency throughout the EU<sup>57</sup>.

There are no comprehensive figures as to the examination of jurisdiction in insolvency cases. According to the Heidelberg/Vienna study, judges in several Member States do not routinely examine their jurisdiction.<sup>58</sup> Research carried out by a Polish judge of the decisions opening insolvency proceedings in the district court of Poznan revealed that although about 60% of the cases contained an international element making the EIR applicable, judges only examined their international jurisdiction in about 1% of the cases<sup>59</sup>.

The extent of abusive COMI-relocation is difficult to quantify, partly because of diverging views as to whether a COMI relocation is actually abusive and partly because due to the deficiencies in the procedural framework not all abusive COMI-shifts are detected. In the area of personal insolvency, the problem is limited to a few regions in the EU – UK, north-eastern France and – to a lesser extent - Latvia. **In France, the court of appeal of Colmar delivered 24 judgments between 2009 and 2011, all but one<sup>60</sup> rejecting applications from German nationals seeking to open insolvency proceedings in France.** As to the UK, a survey suggests that out of about 200 bankruptcy orders relating to foreign nationals in the two years ending 31 March 2010, 14 orders have been annulled on the grounds that there was no real relocation to the UK ; in about half of the cases there were circumstances to suggest that the relocation may not be real<sup>61</sup>. **This means that there are less than 100 cases per year in the UK in which the COMI-shift could be considered to be abusive.** The recent Irish financial crisis may have increased these statistics but evidence on the numbers of Irish flocking to the UK

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<sup>56</sup> GHK/Milieu report.

<sup>57</sup> Irit Mevorach, Jurisdiction in Insolvency: A study of European Courts' Decisions, Journal of Private International Law 2009, p. 327, 352. The study analysed 104 decisions from several EU countries from 2002 until 2009.

<sup>58</sup> For example Poland and the Czech Republic.

<sup>59</sup> Anna Hrycaj

<sup>60</sup> In this case, the court found that a German national who had moved to France 5 years before his financial difficulties, had built a house there and whose daughter had been entirely educated in France, had genuinely relocated to France (CA Colmar, 19 May 2009, see Heidelberg study, French country report (Cuniberti), Question 9.

<sup>61</sup> GHK/Milieu report, p. 17; given that the majority of foreign petitioners were German, the development has been commented as a “quiet invasion” of German nationals petitioning for their own bankruptcy in England and Wales; Walters and Smith, Bankruptcy tourism under the EC Regulation on Insolvency Proceedings: A view from England and Wales.

remains anecdotal. A newspaper identified **55 Irish residents** relocating to the UK with the help of an Irish solicitor to escape more than €1bn of debt<sup>62</sup>.

The use of secondary procedures has declined since the EIR was enacted because companies tend to organise their cross-border activities through subsidiaries rather than branches. However, the use of branches remains the norm in the aviation sector, with big assets and many employees. It is estimated that about 700 companies with branches in another Member State go bankrupt every year; some of these companies will have more than one branch abroad. In practice, secondary proceedings are also sometimes opened in cases of group insolvencies to liquidate assets of the subsidiary in situations where main proceedings for the subsidiary have been opened at the seat of the parent company. Secondary proceedings are not opened in every case: the assets of the branch may not justify the opening of secondary proceedings, there may be no local creditors requesting such opening, or the main liquidator may have reached an agreement with the local creditors. There are no exact figures of the number of secondary proceedings opened in the EU. On the basis of the number of companies with branches, it can be estimated that there are several hundred cases per year.

The costs of secondary proceedings vary considerably between legal systems. Costs essentially consist of liquidator's fees and court costs. In some countries, the fees charged by liquidators are based on a percentage of the monies recovered (typically 3% or 5%), in others, they are based on an hourly rate (e.g. around €250 per hour in the Netherlands).<sup>63</sup> Costs of proceedings are also significantly higher in systems where creditors' committees are involved than in systems where this is not the case.

Problems of coordination have been reported by judges and insolvency practitioners. Results of the public consultation and of the evaluation study provide strong indications that the current provisions on coordination are insufficient. 70% of those expressing an opinion in the public consultation were dissatisfied with the coordination between main and secondary proceedings, with 61% stating that the duty to cooperate does not work efficiently and effectively. In addition 75% of those expressing an opinion stated that the lack of a duty of cooperation between practitioners and the foreign court, or between the courts, has created problems. Similar results were reported in the initial findings of the Heidelberg report with 61% of those expressing an opinion stating that co-operation was inefficient.

Turning to the extent of transparency problems, in all but two Member States, information about insolvency proceedings is collected at a central point, but the procedures for registration and the accessibility of the information to the public vary considerably. While insolvency proceedings of legal entities are registered in every Member State, insolvencies of individuals are only registered in some. In some Member States, the information is published in a register (either in a separate insolvency register, in others, in a commercial register) or in an official bulletin. Some Member States publish the court decisions opening and closing insolvency proceedings in the relevant register, others publish only information on the status of the company or individual (e.g. “in liquidation”) and, partly, the name of the liquidator and the competent court, without registering the court decision itself.

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<sup>62</sup> Henry McDonald, ‘Irish Dodge Debts through UK ‘bankruptcy tourism’ The Guardian (Sunday 27 May 2010) (available at: <http://www.guardian.co.uk/world/2012/may/27/irish-dodge-debts-uk-bankruptcy-tourism>)

<sup>63</sup> GHK/Milieu report,

**Currently, only 14 Member States publish decisions relating to insolvency in an insolvency register accessible online by the public free of charge<sup>64</sup>.** In 9 other Member States, some information on insolvency is available in an electronic register or database, e.g. a company register or an electronic version of the official bulletin. Detailed information on national insolvency registers is in Annex 6.

Finally, the average cost of lodging a claim for a foreign creditor has been estimated at between €2,000 and €5,000 in a cross-border situation. This sum covers the costs for reviewing the file, defining priority rights, compiling documents, liaising with the court and trustee<sup>65</sup>.

46% of those who expressed an opinion in the public consultation considered there were **problems with lodging claims**. Crucially, a significant proportion of key stakeholders who will often be the entities making claims felt there was a problem – 83% of private individuals/self-employed and 75% of banks.

### **3.6. EU right to act**

#### *3.6.1. Legal basis*

The original EIR was adopted under Article 61(c) TEC stipulating that the Council shall adopt measures in the field of judicial cooperation in civil matters and Article 67(1) TEC defining the legislative procedure to be followed. Following the entry into force of the Lisbon Treaty, any revision to the EIR will be based on Articles 81(2) (a), (c) and (f) TFEU. Article 81(1) TFEU provides that ‘The Union shall develop judicial cooperation in civil matters having cross-border implications, based on the principle of mutual recognition of judgments and of decisions in extrajudicial cases. Such cooperation may include the adoption of measures for the approximation of the laws and regulations of the Member States’, and related Article 81(2) TFEU under points (a), (c) and (f) empowers the EU to adopt measures aimed at

- ensuring the mutual recognition and enforcement of judgments between Member States;
- the compatibility of the rules applicable in Member States concerning conflict of laws and of jurisdiction; and
- the elimination of obstacles for proper functioning of civil proceedings.

The adoption of the measures will take place in ordinary legislative procedure.

#### *3.6.2. Principle of subsidiarity*

The development by the EU of more efficient cross-border insolvency rules is in complete compliance with principle of subsidiarity. First, the issue being addressed has transnational aspects, which cannot satisfactorily be dealt by the Member States’ individual action. The need to establish rules for the insolvency of companies operating on a cross-border basis, including groups of companies, is well recognized by all Member States and the international community. This is especially true in view of the increasing number of companies and

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<sup>64</sup> These Member States are: AT, CZ, FI, DE, HU, LV, NL, PL, PT, RO, SI and SE. SK has established a register as a pilot project; the UK has a division of registers between Scotland, North Ireland and England and Wales. Information available in the E-justice portal: [https://e-justice.europa.eu/content\\_insolvency\\_registers-110-en.do](https://e-justice.europa.eu/content_insolvency_registers-110-en.do).

<sup>65</sup> GHK/Milieu report,

traders/self-employed persons that operate in more than one Member State, the rise in the number of groups of companies, and the constantly growing number of companies that have to make recourse to insolvency proceedings because of the economic crisis. The objective of facilitating the expansion of cross-border operations for businesses in the internal market cannot be fully achieved if the way cross-border insolvency proceedings operate is not amended to better reflect developments since 2000. Furthermore, action at the EU level would produce clear benefits (compared to Member States' action) in terms of effectiveness as the amended Regulation will rectify the deficits identified in the previous Regulation, thus rendering its application more effective.

#### 4. POLICY OBJECTIVES FOR THE REVISION OF THE EIR

The general and specific objectives for the revision of the Regulation in relation to the problems described above are summarised in the following table:

<b>General Objective</b>
To improve the efficiency of the European framework for resolving cross-border insolvency cases in view of improving the functioning of the internal market and its resilience in economic crises.
<b>Specific Objectives</b>
To ensure EU-wide recognition of national insolvency-related proceedings contributing to rescuing businesses, protecting investments, preserving jobs and encouraging entrepreneurship; and providing a second chance to honest entrepreneurs and over-indebted consumers;
To increase legal certainty for creditors, thereby encouraging cross-border trade and investment;
To improve the efficient administration of cross-border insolvencies that protects the interest of all creditors and other interested persons, including the debtor;
To improve the efficiency of handling the insolvency of members of a multi-national group of companies, thereby maximising the value of their assets and facilitating rescue.
<b>Operational Objectives</b>
To address the problem of scope of the Regulation that does not take into account the increased use of non-liquidation oriented proceedings (e.g. pre-insolvency and hybrid proceedings);
To set up a process that enables the Regulation better to adapt to the evolution of national insolvency law and to allow secondary proceedings to be restructuring, pre-insolvency and hybrid proceedings;
To clarify the rules relating to jurisdiction for opening insolvency proceedings without prejudice to the rights of companies' and natural persons' legitimate exercise of the freedom of establishment and movement in the Union;
To reduce the number of cases where the determination of jurisdiction has been an issue;
To improve the procedural framework for taking the decision on jurisdiction and ensuring the possibility for judicial review for interested parties;
To reduce the number of secondary proceedings opened outside of the main jurisdiction;

To improve coordination between courts and practitioners, both prior to the opening of and during the proceedings;

To increase transparency by requesting mandatory publication of all relevant decisions in each Member State;

To increase number of insolvency related decisions that have been made public;

To improve access to justice, in particular for SMEs, by devising measures to facilitate the lodging of claims;

To create a specific legal framework for group insolvency

## 5. POLICY OPTIONS

There are three composite policy options that have been identified as to tackle with the above problems in order to achieve the above-mentioned objectives: These are

- 1) Status Quo, or baseline scenario;
- 2) Option A, modernising the existing Regulation while preserving the current balance between creditors and debtors and between universality versus territoriality; and
- 3) Option B, modifying the fundamentals of the Regulation and requiring some approximation or convergence of national insolvency laws and proceedings.

The elements (or suboptions) of which these composite options consist are explained below against the problems that have been streamlined into four categories (after the table). Certain elements are common to both options A and B: both options would provide for an extension of the scope, for the introduction of national insolvency registers and for the simplified procedures for lodging a claim

<b>Problem</b>	<b>Status Quo (Baseline scenario)</b>	<b>Option A “Modernizing the framework for cross-border insolvency proceedings”</b>	<b>Option B “Towards approximation of national insolvency laws and proceedings”</b>
Limited scope of the Insolvency Regulation	The scope and definition of the EIR do not cover pre-insolvency, hybrid and most personal insolvency proceedings	First element:  Extend the scope of the EIR to include hybrid proceedings, pre-insolvency proceedings and personal insolvency proceedings and do away with the requirement that secondary proceedings have to be winding-up proceedings	
	No rules for groups of companies	Second element: Coordination of main proceedings through general cooperation mechanisms, with the possibility, when appropriate, to nominate a lead insolvency practitioner	Second element:  Single court competent for all main proceedings; single insolvency administrator appointed for all members of the group (“procedural consolidation”)

Difficulties in implementing the Insolvency Regulation	No obligation to publish and not all MS have an electronic insolvency register	Third element : Require that Member States publish all relevant decisions of insolvency proceedings in a national electronic register and define common categories for interconnection of national registers through the e-justice portal	
	No standard forms for lodging of claims. The procedures are entirely left to national law	Fourth element: Introduce procedures and standardised form and at EU level for the lodging of claims and encourage Member States to set-up electronic means for the lodging of claims	
	Jurisdiction remains at the COMI, which is defined by case law	Fifth element: Improve the procedural framework and train judges on the EIR.	Fifth element: Harmonise elements of national insolvency laws
	The coordination is limited to coordination between practitioners	Sixth element: Maintain secondary proceedings but improve coordination with the main proceedings prior to the opening and during secondary proceedings	Sixth element: Abolish secondary proceedings

## 5.1. Option A

**First element: Extend the scope of the EIR to include hybrid proceedings, pre-insolvency proceedings and personal insolvency proceedings and do away with the requirement that secondary proceedings have to be winding-up proceedings**

Under the first element of Option A, the definition of insolvency proceedings would be broadened to include hybrid, pre-insolvency and personal insolvency proceedings. National insolvency procedures notified by Member States and which fall under the definition included in the Regulation would be listed in the Annex. The definition would require, in particular, that the insolvency proceeding entail some degree of court supervision, as a necessary condition for recognition based on mutual trust. The Commission would be tasked with ensuring that only proceedings which comply with the definition are listed in the Annex of the Regulation.

In addition, the current requirement that secondary proceedings have to be “winding-up proceedings” would be abolished in order to include proceedings promoting restructuring in the scope of secondary proceedings.

**Second element: Coordination of main proceedings through general cooperation mechanisms, with the possibility, when appropriate, to nominate a lead insolvency practitioner**



Option A would retain the entity-by-entity approach of the Insolvency Regulation but provide for a coordination of the insolvency proceedings concerning members of the same group.

The coordination would apply in three respects:

- (1) There would be an obligation of the liquidators of the different main proceedings to communicate and cooperate, notably by trying to develop a reorganisation plan for the insolvent members of the group. This obligation would build on the existing mechanism for coordination between liquidators in main and secondary proceedings.
- (2) Secondly, the Regulation would oblige the courts competent for the different main proceedings to communicate information and cooperate, e.g. by appointing the same liquidator or several liquidators which have indicated they can cooperate with each other.
- (3) Thirdly, the liquidator in the main proceedings for one group member would be under a duty to communicate and cooperate with the courts competent for the proceedings relating to another group member.

For certain companies, e.g. wholly-owned subsidiaries, the coordination mechanisms above would be complemented by the possibility to grant a “leading role” to the liquidator of the parent company. The “lead” liquidator would have the power to direct the reorganisation of the insolvent group members, in particular, by requesting the competent court to order a stay of the process of liquidation of a subsidiary, to obtain information from the other liquidators or courts involved or to propose a restructuring plan.

**Third element: Require Member States to publish decisions opening and closing insolvency proceedings as well as other decisions issued in the proceedings in a national electronic register and define common categories for the interconnection of national registers through the e-justice portal**

Option A would require all Member States to set up and maintain an electronic register for insolvency decisions, both for companies and private persons. It would further define common categories for the interconnection of national registers through the e-justice portal<sup>66</sup>. The interlinking of national registers would lead to the creation of a generally accessible and comprehensive EU database of insolvency proceedings allowing creditors, shareholders, employees and courts to determine whether insolvency proceedings have been opened in another Member State.

**Fourth element: Introduce procedures and a standardised form at EU level for the lodging of claims and encourage Member States to set-up electronic means for the lodging of claims**

Option A would define a standard form in all EU languages that could be used for the lodging of claims by all creditors in a cross-border proceeding. It would also define some EU procedures for the lodging of claims in order to ensure that national laws take into account the cross-border dimension of certain proceedings, e.g. reasonable time for lodging a claim, sanction when practitioner did not respect the procedure, information to creditors on the fate of their claim.

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<sup>66</sup> The e-justice portal is intended to be a “one-stop shop” in the area of justice, providing information and improving access to justice throughout the EU.

This element of Option A would also encourage Member States to set-up electronic interfaces for the lodging of claims that would be available to foreign creditors. These could be set up through private means and not necessarily by public authorities.

#### **Fifth element: Improve the procedural framework and train judges on the EIR**

Under Option A, the EIR would clarify the definition of COMI by codifying certain elements of the CJEU case-law. The Regulation would also provide that the court opening insolvency proceedings is obliged to examine *ex officio* its basis of jurisdiction and to specify in the opening decision whether the proceedings are main or secondary proceedings. Where the COMI-shift has occurred recently and debts remain in the original Member State, the courts would be obliged to examine already at first instance, i.e. prior to pronouncing the debt discharge, whether the relocation is genuine. This could be done by, e.g. requesting further documents from the debtor or hearing foreign creditors. In addition, creditors would have an effective remedy against the decision opening insolvency proceedings; in particular, they would be informed of the decision in due time to be able to challenge it.

In addition, judges would be trained about the Regulation and about the case-law of CJEU on COMI.

#### **Sixth element: Maintain secondary proceedings but improve coordination with the main proceeding prior to the opening and during secondary proceedings**

Option A would

- Require that the court hears the practitioner of the main proceeding, prior to the opening of secondary proceedings.
- Enable the court to postpone or refuse the opening of secondary proceedings if this would obstruct the effective administration of the estate and further benefit local creditors. The liquidator and the courts may further undertake to treat local creditors as if secondary proceedings had been opened (“synthetic secondary proceedings”).
- Oblige courts and insolvency practitioners to cooperate with one another, as well as courts to communicate and cooperate between themselves.

#### **5.2. Option B**

Those elements that are common to both options A and B are already explained above; they are

- **First element: Extend the scope of the EIR.**
- **Third element: Require Member States to publish decisions in a national electronic register.**
- **Fourth element: Introduce procedures and a standardised form for the lodging of claims.**

As regards the elements specific to Option B, **second element: single court competent for all main proceedings and single insolvency administrator appointed for all members of the group (“procedural consolidation”)** would contain a single insolvency administrator appointed for all members of the group (“procedural consolidation”), whereby the insolvency

proceedings for all members of the group would be consolidated in a single court at the place of the COMI of the parent company. The same insolvency practitioner would be appointed in all main proceedings of the subsidiaries.

**Fifth element: Harmonise elements of national insolvency laws** would involve a harmonisation of certain aspects of national insolvency procedures, in particular, debt discharge periods, conditions and rules for opening proceedings, rules on hearing of creditors and effective remedy.

Finally, there is **sixth element: Abolish secondary proceedings** to Option B. This would abandon secondary proceedings and have one, single main insolvency proceeding with EU wide effect dealing with the parent company and all branches and establishments.

### 5.3. Discarded options/elements

There were certain other elements identified or proposed by stakeholders as possible options to solve the problems. In particular, there was an option of introducing a suspension period in relationship to the removing of COMI (relating to lack of definition): This option would provide that following a shift in COMI to another Member State, jurisdiction remains for a certain period (e.g. 1 year) with the courts of the Member State of origin.

A preliminary screening of the options have led to discarding an element under option A addressing the difficulty to determine jurisdiction as follows: **Introducing a suspension period** is not sufficiently effective to achieve the desired objectives: this element primarily aims at preventing forum-shopping by providing that jurisdiction for opening insolvency proceedings stays with the original Member State for a certain period of time (e.g. 1 year) after the COMI has shifted. However, it is doubtful whether this element would effectively achieve this objective because it may be expected that the legal advisors of big companies will find a way to circumvent the suspect period or to hold out until it has elapsed. Moreover, the element does not improve legal certainty for creditors because it would replace the current uncertainty relating to the determination of COMI by a new uncertainty relating to the time the COMI shifted. New creditors would have difficulties to determine whether the suspension period was still running – with the consequence that the law applicable to their claims would be the one of the Member State where COMI was previously located – or whether it had already ended; also, the judge's assessment of the moment of the COMI shift could very well vary from that of the creditors. Consequently, such element would not improve legal certainty with respect to the Status Quo.

## 6. EVALUATION OF THE IMPACTS OF POLICY OPTIONS

### 6.1. Baseline scenario (Status Quo)

The situation under the Status Quo, i.e. without any measures taken, would evolve as follows:

#### *Problem Group 1: Problems relating to the scope of the Regulation*

The insolvency laws of Member States have evolved in the past ten years to respond to new economic thinking and realities and it is likely that this process will continue. In a few years one can expect virtually all Member States to have pre-insolvency and hybrid procedures, as well as personal insolvency procedures. Consequently, problem 1 is likely to increase, with more national proceedings falling outside the scope of the Regulation because they do not

match the EIR's definition and the Regulation being increasingly out of tune with the reality in the Member States.

Further, the EIR having been adopted before the entry into force of the Lisbon Treaty, the mechanism for updating its Annex which lists the national procedures within the scope of the EIR is inconsistent with the Treaty. The updated Annex is adopted via a Council Regulation upon notification of Member States, while there is no explicit mechanism for controlling the content.

The Status Quo in relation to insolvencies of groups of companies only allows for efficient handling of the insolvency of heavily integrated groups where the COMI of the subsidiary is located at the registered office of the parent company. For all other groups, maintaining the Status Quo would have no effect on the problem identified and would not contribute to achieving the objectives set out above.

### ***Problem Group 2: Problem in the implementation of the Regulation***

The problem of forum-shopping is likely to decrease to some extent even in the absence of EU action because regulatory competition and a focus on enabling 'second chances' will inevitably drive some convergence in national legislation, which will reduce incentives for forum shopping. Thus, the Council Conclusions of May 2011 endorsing the recommendation of the Second Chance group to provide a three year discharge period have already been followed by some Member States. However, the current differences in Member States' approaches to insolvency and, in particular, the issue of personal insolvency, make complete convergence in the short and medium term unlikely so incentives for forum-shopping will remain.

Although the use of branches as a means to structure cross-border activities has declined since the time when the EIR was enacted, secondary procedures will remain relevant proceedings under the EIR because they can also be used in the context of group insolvency if the subsidiary's COMI is located at the registered office of the parent company. In practice, insolvency practitioners have sometimes managed to avoid the opening of secondary proceedings by undertaking to treat the local creditors as if such proceedings had been opened (so-called "synthetic secondary proceedings"). This solution is accepted by the courts in the UK but is not permitted under the procedural laws of most other Member States.

The problems of coordination are expected to increase as more cross-border restructurings are being attempted to try to rescue viable business and save jobs. Without an obligation on courts to coordinate between themselves and with the insolvency practitioners, current experience shows that this coordination will not function effectively.

The problems related to the publicity and the absence of registers will partially improve by the interconnection of national company registers at EU level by the recently adopted Directive 2012/17/EU on the interconnection of central, commercial and companies' registers which is planned for 2017 at the latest. The Directive

1. creates the interconnection of national business registers through a European portal;
2. requires that the register shall, through the system of interconnection of registers, make available, without delay, the information on the opening and termination of any winding-up or insolvency proceedings of the company;

3. ensures that companies have a unique identifier allowing them to be unequivocally identified in communication between registers through the system of interconnection of central, commercial and companies' registers.

However, the Directive solves the problem of publicity only partially because

1. in most Member States the register does not cover all companies (only limited liability companies);
2. the Directive does not include natural persons, sole traders or self-employed; and
3. the information provided is not sufficient: it is not enough to know that a company/person is subject to an insolvency proceeding; courts and creditors need additional information, in particular the name and address of the liquidator, the type of insolvency procedure and the exact powers of the liquidator and the extent to which the debtor has been divested.

The problem with the EIR will not be solved sufficiently by the interconnection of business registers.

Regarding the lodging of claims, standardised national forms are being developed. However, no standard European form could be imposed without intervention by the legislator, and the difficulties faced by foreign creditors described above will remain. A few Member States are putting in place electronic interfaces for the lodging of claims<sup>67</sup> which could – if the (linguistic) needs of foreign creditors are taken into account – significantly facilitate the lodging of claims. However, it is unlikely that all Member States will embark on such projects in the short or medium term.

## **6.2. Option A: Modernizing the framework for cross-border insolvency proceedings**

### *Effectiveness in achieving the objectives*

**Strengths: Option A will be effective in achieving the objectives.**

**Weaknesses: Theoretically there is a risk that extending the scope to cover a higher number of insolvency schemes would have an effect on forum shopping.**

The new scope of the EIR and EU-wide recognition of hybrid, pre-insolvency and personal insolvency schemes will be effective as the new rules for determining which schemes fall within the scope of the EIR will ensure that the scope of the EIR remains in synch with national developments and that these are taken into account in a more consistent manner.

Improving the procedural framework for determining the jurisdiction, together with training of judges, would considerably improve legal certainty in this area. Routine examination of jurisdiction before opening insolvency proceedings will allow judges to request further proof from the applicant debtor in case of doubts as to whether COMI is really located in that Member State or to give creditors the opportunity to be heard on the issue before opening proceedings. It would discourage sham claims as to jurisdiction or false statements of affairs by the debtor, thereby reducing the possibilities for forum shopping. It would also facilitate the tasks of courts seized with a request relating to the same debtor to determine which type of

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<sup>67</sup> Such a scheme is being developed for example by the French association of liquidators and insolvency practitioners.

proceedings is still “available”. The coordination of proceedings, whether secondary proceedings or parallel proceedings, publicly available information on all proceedings, and standardised forms for lodging claims will all contribute positively to the efficiency and fairness of cross-border proceedings, protecting the interests of all parties and improving access to justice.

The risk of forum shopping by debtors seeking to relocate abusively their COMI in countries where pre-insolvency schemes and discharge of debt exist is limited in practice by the criteria laid down by domestic insolvency law for opening proceedings, as well as the powers of national courts to examine the circumstances of the case.

### *Impacts on Fundamental Rights*

**Strengths: Option A will improve the rights of persons involved in cross-border insolvencies (right to property, freedom to conduct business and right to engage in work, freedom of movement and residence, and right to an effective remedy).**

**Weaknesses: It will also affect their rights of protection of personal data and right to property, in a way which is proportionate to the objectives. Measures need to be put in place to ensure compliance with Directive 95/46/EC on data protection.**

**Right to property:** Hybrid, pre-insolvency and personal insolvency schemes affect the rights to property of creditors compared to liquidation procedures, because these schemes are all based on some form of arrangement between the debtor and a majority of creditors. In these schemes, dissenting creditors can be overruled by the majority. This impact on the right to property is considered to be proportionate to the objective of rescuing businesses and saving jobs, not the least since it has been shown that the median recovery rate for creditors may be significantly higher in case of restructuring as compared to liquidation.

The reduction in abusive forum-shopping combined with a right for all creditors of judicial review of the jurisdiction, would improve the protection of the creditor's right to property because there would be fewer cases where his claim was lost or diminished in value due to the shift of his debtor's COMI to another country.

**Freedom to conduct business and right to engage in work:** The EU-wide recognition of personal insolvency schemes and ensuing debt discharge will impact positively on the freedom to conduct business and right to engage in work in the EU as it facilitates the possibility of a second chance for debt-discharged entrepreneurs and natural persons. Further the EU-wide recognition of national hybrid and pre-insolvency proceedings will positively affect the freedom to conduct businesses for companies, as these proceedings will be recognised by all their creditors EU-wide.

**Freedom of movement and of residence:** The EU-wide recognition of personal insolvency schemes and ensuing debt discharge will impact positively on the freedom of movement and of residence of natural persons within the EU as the arrangements of the schemes, including payment plans and possible debt discharge would be recognised by all creditors and other authorities.

**Protection of personal data:** The inclusion of data on companies, but also especially natural persons and other debtors who are subject to insolvency proceedings within public electronic registers constitutes a data processing activity. Thereby it affects the right to the protection of personal data. The obligation of Member States to comply with Directive 95/46/EC is self-

evident, but needs to be referred to expressly in the amending Regulation as Regulation 1346/2000 does not refer to it in any way. Information on the opening and closing of proceedings is necessary on the one hand to allow the debtors to exercise their right of free movement or the right to conduct business in another Member State, and on the other to protect potential creditors, customers or employers. It is also necessary for the good and efficient administration of the proceedings themselves. For this impact to be considered necessary and proportionate with respect to the objectives of the policy, specific provisions will need to be introduced in the amending Regulation to justify the necessity and purpose of each category of data to be published by Member States. Further, the right to access to data subjects encompassing the right to rectification and erasure will need to be highlighted.

Finally, access to the data in the register of another Member State, especially data on natural persons subject to insolvency proceedings, must be for legitimate reasons. The usage and processing of this data shall be regulated.

**Right to an effective remedy:** This option would improve the situation with respect to creditors' right to an effective remedy and fair trial. It would ensure that creditors in another Member State have the possibility of judicial review of the decision opening insolvency proceedings, either by being heard before the decision is taken or by being effectively able to challenge it.

### *Economic Impacts*

**Strengths: Option A will have a positive impact on economic growth, investment and the Single Market.** By providing greater legal certainty, preventing unnecessary bankruptcies, reducing obstacles to second chance for entrepreneurs, improving the availability of information, and cutting litigation costs, it will contribute to improving the conditions for investment in Member States. All these improvements are likely to have a positive effect on cross-border transactions, whether contracts, partnerships, acquisitions, or developments of new branches/subsidiaries.

**Weaknesses: There is a risk that giving a second chance to debtors would impact other entrepreneurs' access to affordable credit.**

Hybrid and pre-insolvency schemes rescue more company value, help viable businesses to survive temporary financial difficulties, improve recovery rates for creditors, and contribute to saving jobs. There are 50,000 cross-border insolvencies per year, meaning that at least twice as many companies are involved in cross-border insolvency proceedings and could benefit from broadening the scope of the EIR. SMEs will especially benefit from the EU-wide recognition of hybrid and pre-insolvency schemes. The rescue of large businesses requires the business to go on during the procedure and therefore requires that creditors such as suppliers are still being paid. This would benefit many SMEs that tend to be heavily dependent on one or a small number of large customers. Moreover, ensuring that the effects of personal insolvency schemes are recognised throughout the EU will reduce obstacles to second chance for entrepreneurs.

Rescue procedures, second chance and discharge of debt are deemed to encourage moral hazard, debt forgiveness and subsequent increase of credit cost where such proceedings would not be sufficiently tightened and closely monitored. However the organisation of the judicial systems is a competence of Member States; the option only aims at the recognition of such national proceedings in the EU.

Allowing secondary proceedings to participate in restructuring and pre-insolvencies will further facilitate the survival of viable businesses, as will the efficient coordination of parallel proceedings for a group of companies. This will benefit the business as a whole but also the branches/establishments of parent companies that would have a possibility to be rescued on their own. This is particularly relevant for SMEs that are establishments/subsidiaries of parent companies, as it would allow them to be re-organised or acquired when the parent company goes insolvent and they have a viable business. Maximisation of assets and value of companies will also be supported by these provisions.

Effective and less expensive lodging of claims will benefit all companies as creditors. It is estimated that the costs for lodging a claim by a foreign creditor would be at least halved to a mean value of less than €1,000 compared with the current average of between €2,000 and €5,000. This reduction in costs should particularly benefit SMEs as foreign creditors, for which the additional costs of lodging claims abroad entail important costs with regard to their turnover and cash-flow and may even deter them from lodging the claim.

The publication of all relevant decisions in national insolvency registers will benefit companies as creditors. They will have the means to be informed of the on-going insolvency proceedings, thereby being able to take all necessary measures including the lodging of claims. It also benefits companies as potential customers or suppliers as they can anticipate and possibly avoid potential difficulties in fulfilling contracts.

Cooperation between insolvency practitioners would entail certain additional costs, but these costs would be offset against the savings which the cooperation would achieve.

### *Social Impacts – Impact on employees*

**Option A will facilitate the preservation of jobs**, as viable businesses are able to continue. The impact will be more significant for employees of large companies (more than 250 employees) as these are more likely to be involved in EU insolvency procedures. Also, the survival of branches/establishments is particularly important for saving jobs whenever manufacturing or job-intensive activities tend to be situated in another Member State than the parent company, and this would be supported by extending the scope of secondary proceedings.

There is no evidence of any additional impact on the situation of employees as to the law applicable to their contracts of employment, the guarantees and protection already provided by Directive 2008/94/EC<sup>68</sup> in the Status Quo. There is a need to avoid the automatic opening of local secondary proceedings for the purpose of the payment of wage claims, as this happened to be counter-productive in the Alitalia case. Instead, the reassurance given by the main liquidator in the proposed "synthetic" secondary proceedings should include the protection of workers' rights.

### *Impacts on Member States*

**Option A will have a low impact on national insolvency laws, mostly procedural, while it will contribute to the development of rescue schemes in all Member States.** It has costs for the insolvency register and the training of judges. However, these will be justified by the expected benefits for society of increased efficiency and quality of cross-border insolvency

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<sup>68</sup> Directive 2008/94/EC of the European Parliament and of the Council of 22.10.2008 on the protection of employees in the event of insolvency of their employer, OJ L283, 28.10.2008, p.36.



procedures, even if these lead to the rescue and restructuring of only a small percentage of the tens of thousands of cross-border bankruptcies and associated job losses and lost output.

It will have an indirect consequence on the Member States who do not have national hybrid and pre-insolvency proceedings (11) (BG, HU, LT, NL, SK, SI, SV, IRL, PT, CY, FI) as it will increase the pressure to adopt such proceedings. Further, it would put pressure on Member States which do not have personal insolvency proceedings (9 MS), second, it will encourage in the medium term some convergence in the personal insolvency proceedings (for whom, purpose, discharge periods...) as today the EU landscape is very diverse.

The scrutiny procedure to include national proceedings in the Annex and the information to be provided on these national procedures will have a positive impact on the judicial systems of Member States and on the European area of justice as a whole by increasing confidence and mutual trust of judges in the procedures from other Member States.

Member States will not have to bear any additional costs due to standard forms as they will only entail costs for the EU Institutions.

There exist no specific data on the administrative burden relating to the new information obligation to publish all court decisions. However, such a requirement may be attenuated and confined to those decisions which most Member States publish anyway in order to reduce additional costs.

#### Specific Costs

Training of insolvency judges will be incurred by national public administrations, i.e. Member States' budgets. Part of these costs could be taken on by the EU as part of the programme on training. Member States will also incur costs related to the development, upgrading, and interconnecting of national insolvency registers, as set out in the table below:

<i>Action</i>	<i>Estimated cost</i>
Training of judges	<p>€50 - 1300/judge</p> <p>€7 - 10 million (10% of all judges) for all Member States</p>
National electronic insolvency register	<p>Development of new insolvency register: €0.5 - 1 million (per MS concerned)</p> <p>Upgrading existing insolvency register: €100k - 300k (per MS concerned)</p> <p>Maintenance: €100k- 150k per MS per year</p>
Interconnection of national registers	<p>Development central interconnection) : €0.5 - 1 million (EU budget)</p> <p>Maintenance central interconnection: €100k - 300k per year (EU budget)</p> <p>Development and maintenance (per MS): €50k /year</p>

The costs for the national register distinguish costs between those Member States that need to develop a new system or profoundly change the architecture of their current system, and Member States that need only to upgrade an existing system. The former (as FR, FI) are not favourable to a compulsory register; the latter have concerns that additional obligation is put on the courts (UK) and that the obligation extends to natural persons (SE, FI). Nevertheless the majority of countries that have currently a register do not oppose the plans, e.g. AT sees some benefits in a cross-border situation. The interconnection of national registers in the framework of the e-Justice Portal would affect both Member States and the EU budget, and comes in addition to the costs of the national registers. However the Commission will ensure that the risk of parallel overlapping network of registers is minimised because the revised Regulation would allow Member States to build on the network established by Directive 2012/17/EU in order to avoid the costly creation of new registers.

The requirement that courts cooperate and communicate with each other would entail some additional costs in terms of working time and possible costs of translation. As a specific impact, the requirement to hear the main liquidator before opening secondary proceedings would entail certain costs for the court but these costs are likely to be outbalanced by the guidance the liquidator can give the court in determining whether to open secondary proceedings. About 10% of the 50,000 cross-border insolvencies per year involve establishments and subsidiaries. That means that judges will have additional coordination work for up to 5,000 cases per year (compared with the total of about 200,000 insolvencies per year in the EU). Thus, the number of cases involved is relatively small compared to the total number of insolvency cases, and the costs of additional working time would, moreover, be at least partly offset by savings of working time achieved by a more efficient flow of information which the cooperation between courts would bring about. Costs for translation of documents or other may be borne by the proceedings. Based on average costs of translation of €30 per page, the translation costs can be estimated at between €90 and €300, depending on the length of the court decision to be translated. Additional costs incurred by courts are also likely to be compensated by a decrease of legal dispute resulting from the proposed procedural improvements and the consequent diminution of judicial claims.

### **6.3. Option B: Towards approximation of national insolvency laws and proceedings**

#### *Effectiveness in achieving the objectives*

**Option B will be very effective in achieving the objectives.** It will address the underlying problems of the EIR.

Having a single proceeding for companies with establishments and for groups of companies, would ensure efficient handling of the insolvency proceedings because they would be consolidated before a single judge, administered by a single insolvency practitioner and governed by a single law, that of the state of the opening of proceedings. There would be no efficiency losses due to multiple proceedings being opened in different jurisdictions or divergences of opinion between different liquidators involved. They also have positive economic impacts on companies as debtors.

#### *Impacts on Fundamental Rights*

**Similarly to option A, option B will improve the rights of persons involved in cross-border insolvencies** (right to property, freedom to conduct business and right to engage in work, freedom of movement and residence and right to an effective remedy). **It will also affect their rights of protection of personal data**, in a way which is proportionate to the

objectives. Measures need to be put in place to ensure compliance with Directive 95/46/EC. Finally, to avoid disproportionate impacts on the right to property, measures allowing the fair treatment of all creditors, such as harmonised European provisions on the treatment of foreign creditors will need to be put in place.

**Right to property:** Option B would change the approach towards the rights of the creditor, as, in contrast to the Status Quo, the ranking of creditors will no longer be determined by the law of the seat of the company with whom he established a legal relationship.

**Weaknesses:** Having a single proceeding for companies with establishments and for groups of companies has significant negative repercussions on the right to property of the creditors of establishments or subsidiaries with respect to the Status Quo. The creditors of establishments or subsidiaries, that could be in particular local SMEs, but include also employees, social security and tax authorities, would lose all possibility to open a local insolvency proceeding governed by the law of the state of the establishment/subsidiary. This negative impact on creditors would in turn also mitigate the economic and social benefits of these options. The impacts on the right to property seem disproportionate with respect to the objectives. In order to reduce this important negative impact on some creditors, option B would have to be accompanied by measures allowing the fair treatment of all creditors, such as harmonised European provisions on the treatment of foreign creditors (of an establishment or subsidiary in another Member State).

**Freedom to conduct business and right to engage in work:** Option B may affect the freedom of companies to conduct business and to organise themselves, because there would be only one procedure for a group of companies.

**Freedom of movement and of residence:** The positive impacts of Option B are similar to Option A.

**Protection of personal data:** The impacts on the right to protection of personal data are similar to Option A

**Right to an effective remedy:** The harmonisation of the procedural framework for cross-border insolvencies and national insolvencies would improve the rights to an effective remedy.

### *Economic Impacts*

**Similarly to Option A, Option B will have a positive impact on economic growth, investment and the Single Market.**

On top of the economic benefits of Option A, harmonised rules e.g. on certain procedures, on treatment of foreign creditors and on discharge periods, will considerably increase legal certainty for creditors, take away a large part of the incentives for abusive forum-shopping, which will contribute to improving conditions for investment in Member States and benefit the Single Market. Option B may further improve the resilience of the Single Market in economic crises, as the effectiveness of national insolvency laws is essential in alleviating the effects of the crisis.

*Harmonised rules may also facilitate investments from third countries.*

As with Option A, Option B will facilitate the survival of viable businesses by ensuring EU-wide recognition of hybrid and pre-insolvency proceedings.

Having a unique proceeding for companies with establishments or groups of companies will simplify proceedings for companies as debtors and creditors, and would also generate savings by reducing the number of insolvency administrators and courts involved. It will also benefit SMEs that are establishments/subsidiaries of parent companies and have a viable business, as they can be integrated in the rescue of the whole company and they do not have to bear additional costs of a local procedure.

Businesses, as debtors and creditors, will benefit from more harmonized rules. These will have a positive effect on cross-border transactions in the Single Market, whether contracts, partnerships, acquisitions, developments of new branches/subsidiaries. Indeed, business stakeholders (Eurochambers, UEAPME, Business Europe) often complain about inefficiencies of national insolvency laws. SMEs would particularly benefit from the harmonisation of discharge periods throughout the EU. The great divergence of discharge periods, and in particular the excessive length of discharge periods in certain Member states, has been identified as a major obstacle to providing a second chance to SMEs.

Similarly to option A, more effective and less expensive lodging of claims will benefit all companies, and in particular SMEs, as creditors. The publication of all relevant decisions in national insolvency registers will also benefit companies as creditors.

### *Social Impacts – Impact on employees*

As Option A, also **Option B is likely to facilitate the preservation of jobs**, as viable businesses are able to continue. The impact will be more significant for employees of large companies (more than 250 employees) as these are more likely to be involved in EU insolvency procedures. Also, the survival of branches/establishments is particularly important for saving jobs whenever manufacturing or job-intensive activities are situated in another Member State than the parent company, and this would be supported by having unique procedures that can efficiently define and implement a rescue plan for the whole company or group of companies.

### *Impacts on Member States*

**Weaknesses: Option B would entail a substantial element of harmonisation. It would therefore have an important impact on Member States' insolvency laws and on national judicial systems.**

The harmonisation or convergence of discharge periods would affect those Member States that have not yet implemented the Council Conclusions of May 2011 on the Small Business Act.

Option B would modify the rules on the applicable law and on the rights of creditors that are now defined in the EIR. The harmonisation of certain procedural aspects, regarding the opening of procedures, the availability of an effective remedy for creditors, and on the ranking of creditors, will have important consequences on national laws as the differences between national systems are important. The approximation of national insolvency laws and procedures would therefore require an in-depth comparative-law analysis of national insolvency laws and procedures which would enable the Commission to identify the precise areas in which procedural harmonisation would be necessary and feasible, and not too intrusive to the national legislations and insolvency systems.

Costs relating to training and to establishing, upgrading and interconnecting insolvency registers would be incurred as in option A.

## **7. COMPARISON OF THE OPTIONS AND SUMMARY OF THE PREFERRED OPTION**

The Status Quo would not solve the problems identified and would allow the negative effects of the two groups of problems to continue. Although a degree of regulatory convergence between Member States might be expected in some areas, in others the problems are likely to become more acute.

Option A has overall positive impacts with respect to the baseline. It would effectively achieve the policy objectives and address the problems identified, without intrusion in national legislation or policies. It would increase the efficiency of the Regulation, extend its scope to proceedings that aim at rescuing viable business and saving jobs and promoting second chance, and make provisions for groups of companies.

Option A will have a positive impact on economic growth, investment and the Single Market. By providing greater legal certainty, preventing unnecessary bankruptcies, reducing obstacles to second chance for entrepreneurs, improving the availability of information, and cutting litigation costs, it will contribute to improving the conditions for investment in Member States. All of these improvements will also have a positive effect on cross-border transactions, whether contracts, partnerships, acquisitions, or developments of new branches/subsidiaries.

Option A will benefit all business, in particular groups of companies and SMEs as debtors and creditors. It will increase efficiency, fairness and transparency of cross-border insolvency proceedings and improve access to justice.

Option A imposes some costs on Member States' authorities related to insolvency registers and training of judges, which is largely justified by the benefits and savings for society of the increased efficiency and quality of cross-border insolvency procedures.

Option A will have a positive impact on mutual trust between Member States' judicial authorities. It preserves the current balance between debtor and creditor and between universality and territoriality. However, one important cause of the problems identified - inefficiencies and differences in the national insolvency laws themselves - would not be addressed.

Option B is potentially more effective than Option A in reaching the objectives and providing economic and social benefits for the Single Market. It would increase the effectiveness and efficiency of insolvency proceedings in the EU as a whole; it would create elements of a fully universal system, going towards features of the regulation of insolvency in the 50 States of the US under the US Insolvency Act.

Option B would be more completely address the European Parliament's Resolution of November 2011, in which it gave recommendations to the Commission regarding the harmonisation of specific aspects of insolvency proceedings on the basis that the internal market would benefit from a level playing field, and that disparities between national insolvency laws create competitive advantages or disadvantages and difficulties for companies with cross-border activities, which could become obstacles to a successful restructuring of insolvent companies and favour forum-shopping.

However, option B's impact on national systems is more significant. The proposed changes go beyond the modernising of the EIR, and would require an in-depth comparative analysis of national insolvency laws, preventing the immediate implementation of option B. In the meantime, the current problems would persist, and could even worsen.

Therefore, while there is a lack of supporting evidence in favour of option B, option A seems a more proportionate option at this stage. Accordingly **the preferred option for the revision of the Insolvency Regulation is option A:**

<p><b>Extending the scope</b> by revising the definition of insolvency proceedings:</p> <ul style="list-style-type: none"><li>- to include hybrid and pre-insolvency,</li><li>- and include debt discharge and those insolvency proceedings for natural persons which currently do not fit the definition,</li><li>- and opening the scope of secondary proceedings to large categories of proceedings promoting restructuring.</li></ul> <p>Task the Commission with <b>ensuring that only procedures which comply with the definition</b> are listed in the annex.</p>
<p><b>Improving the procedural framework:</b> the EIR would clarify that the court opening insolvency proceedings is obliged to examine its basis of jurisdiction and to specify in the opening decision whether the proceedings are main or secondary proceedings; in addition, creditors would have a right to judicial review of the opening decision.</p>
<p><b>Enable the court to postpone or refuse the opening</b> of secondary proceedings if this would obstruct the efficient administration of the estate.</p> <p><b>Require the court to hear the liquidator in the main proceedings</b> prior to opening secondary proceedings.</p>
<p><b>Extend the cooperation requirements to courts</b> by obliging courts of the main and secondary proceedings to cooperate between themselves and by obliging liquidators and courts to cooperate with each other.</p>
<p>Require Member States to publish all court decisions relating to cross-border insolvency cases in a <b>publicly accessible electronic register</b>;</p> <p>Oblige liquidators of the main proceedings to <b>publish these court decisions in the insolvency register of other Member States</b> where the debtor has an establishment or creditors;</p> <p>Enable definition of common entries for the interconnection of national registers.</p>
<p><b>Introduce standardized forms</b> in all EU languages for the lodging of claims;</p> <p>Encourage Member States to set up <b>electronic systems for the lodging of claims.</b></p>
<p><b>Coordinating main proceedings through general cooperation mechanisms:</b> This option would retain the entity-by-entity approach of the Insolvency Regulation but provide for a coordination of the insolvency proceedings concerning members of the same</p>

group in three respects:

(i) by obliging the liquidators of the different main proceedings to communicate and cooperate, notably by trying to develop a reorganisation plan for the insolvent members of the group;

(ii) by obliging the courts competent for the different main proceedings to communicate information and cooperate, e.g. by appointing several liquidators which have indicated they can cooperate with each other;

(iii) by obliging the liquidator in the main proceedings for one group member to communicate and cooperate with the courts competent for the proceedings relating to another group member.

The coordination mechanisms above can be complemented by the nomination of a “lead” insolvency practitioner and court with the power to direct the reorganisation of the insolvent group members, when the structure and level of integration of the group allows for it.

The “lead” insolvency practitioner would, in particular, have the power to request a stay of the process of liquidation of a subsidiary, to propose a restructuring plan and to obtain information from the other insolvency practitioners or courts involved. The “lead” insolvency practitioner could either be the liquidator of the parent company or an additional liquidator nominated by the “leading” court.

## 8. MONITORING AND EVALUATION

In order to monitor the effective application of the amended Regulation, regular evaluation and reporting by the Commission will take place. To fulfil these tasks, the Commission will prepare regular evaluation reports on the application of the Regulation, based on consultations with Member States, stakeholders and external experts. Regular expert meetings will also take place to discuss application problems and exchange best practices between Member States in the framework of the European Judicial Network in civil and commercial matters.

In most Member States, there is no systematic collection of statistical data on the application of the EIR, which makes it very difficult to measure how the Regulation operates for cross-border insolvencies. The Commission will therefore include in the revision of the EIR a requirement on Member States to *provide* information on the application of the EIR in practice, notably on the number of secondary proceedings and proceedings concerning groups of companies.

## ANNEX 1: GLOSSARY OF LEGAL TERMS AND ABBREVIATIONS

Term	Meaning
COMI	Centre of main interest of the insolvent debtor. For a company it is deemed to be the place of its registered office; for a private individual it is in general its habitual residence
EIR	Council Regulation (EC) No 1346/2000 on insolvency proceedings (or "European Insolvency Regulation")
Jurisdiction/international jurisdiction	Jurisdiction is the power conferred upon a court or tribunal to hear a specific case; international jurisdiction is the competence of the courts of a particular country to hear a case. The EIR only defines the international jurisdiction for opening insolvency proceedings
Main insolvency proceedings	Insolvency proceedings which have been opened in the Member State where the debtor has its centre of main interests
Secondary insolvency proceedings	Insolvency proceedings opened in the Member State where the debtor has an establishment but not its COMI.
Liquidator	Person or body whose function is to administer or liquidate assets of which the debtor has been divested or to supervise the administration of his affairs
Winding-up	Insolvency proceedings involving realising the assets of the debtor (liquidation), including where the proceedings have been closed by a composition or other measures terminating the insolvency, or closed by reason of the insufficiency of the assets
Insolvency practitioner	Liquidator
Insolvency proceedings	Collective proceedings –subject to court supervision, either for reorganisation or liquidation, which entail the partial or total divestment of a debtor and the appointment of a liquidator
Insolvency	Inability to pay one's debts as they fall due
Bankruptcy	Determination of insolvency made by a court of law with resulting legal orders intended to resolve the insolvency; another meaning is a synonym of winding-up/liquidation
Hybrid proceedings	At the border between out-of-court arrangements (contracts, conciliation) and formal judicial insolvency proceedings, they are a mix combining the advantages of both types of proceedings (flexibility, enforceability). In such proceedings the debtor can continue to manage its assets ("debtor in possession")
Pre-Insolvency Proceedings	Semi-collective proceedings (conducted between a debtor in financial distress and its main secured creditors) starting at an early



	stage prior to insolvency, in view of maximising the chance of successful reorganisation. They may be out-of-court arrangements or under the supervision of the court
Establishment	Any place of operations where the same debtor carries out a non - transitory economic activity with human means and goods or services
Branch	Establishment
Group of Companies	Consists of separate units, each with its own legal personality, its own assets, contracts and creditors. The companies of the group may have an integrated business, a market stronger position, an integration of assets or a financial integration (holding). In case of horizontal integration several units in different countries have similar activities; in the vertical integration each of the units is responsible for a separate activity in the process
Parent Company	Company which owns a majority of shares of its subsidiaries. It may determine the common policy of the group at its headquarters
Subsidiary	Companies owned and controlled by a parent company

## ANNEX 2: EXECUTIVE SUMMARY OF THE OUTCOME OF THE PUBLIC CONSULTATION

Regulation (EC) No 1346/2000 on Insolvency proceedings came into force in May 2002. It includes an obligation on the Commission to review the application of the Regulation and to make a proposal for adaptation of the Regulation if needed in 2012. Such a review is included in the European Commission's 2012 work programme and has gained greater impetus in view of the current financial crisis and the positive impact that effective insolvency regimes can have on entrepreneurship and economic growth.<sup>69</sup>

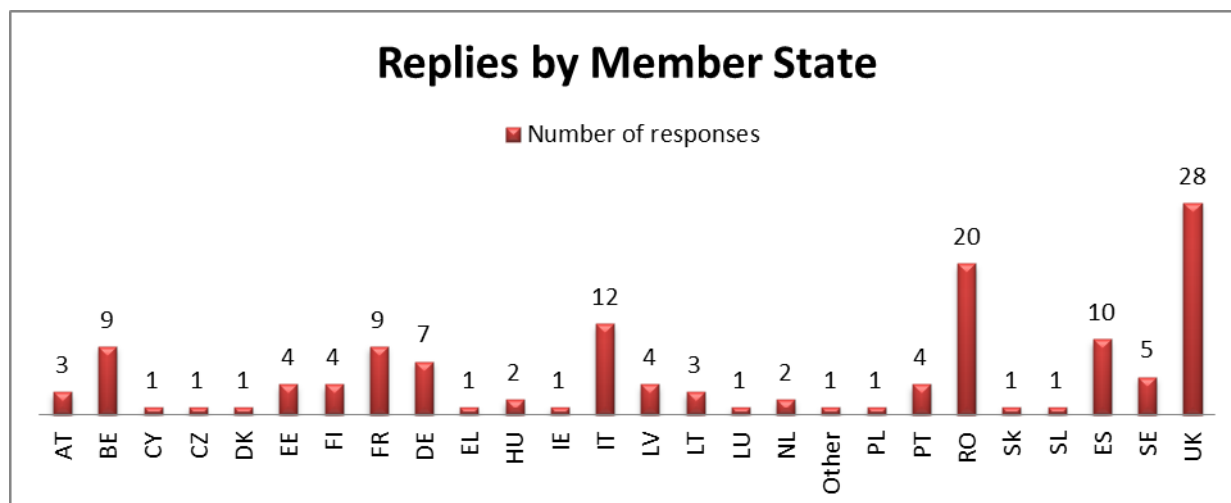
As part of the Commission's review, it is not only examining issues in relation to the implementation of the Regulation but also considering whether the Regulation continues to reflect current trends in insolvency practice. To this end, it launched a public consultation on 30 March 2012 asking a total of 31 questions related to the Insolvency Regulation as well as seeking broader opinions on problems faced and possible solutions including how the Regulation might be amended.

This report aims at providing a general overview of the main results of the public consultation.

### *Overview of respondents*

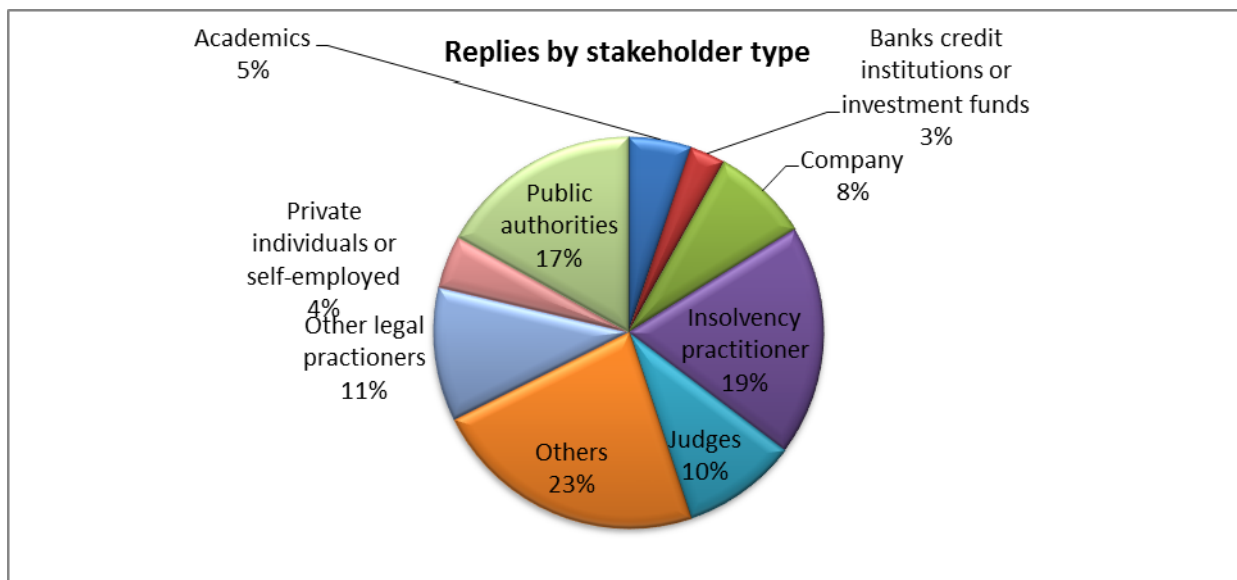
The public consultation was closed on 21 June 2012 having received 103 replies via the IPM tool. Additional replies were received by email, including full responses to the consultation, comments on specific points and documents. A total of 136 responses were recorded. For statistical purposes, 126 responses were analysed since a number of responses did not cover all questions and were not suitable for statistical purposes.

Replies have been received from all Member States except Bulgaria and Malta with the UK (21%), Romania (20%) and Italy (12%) representing more than 50% of all respondents.



Replies were received from a wide range of stakeholders with academics, legal practitioners and public authorities providing the greatest number of replies.

<sup>69</sup> Communication from the Commission: Commission work programme 2012, delivering European renewal.



## OVERVIEW OF MAIN FINDINGS

A narrow majority (52%) of respondents agreed that the European Insolvency Regulation (EIR) operates efficiently (Question 1), with legal practitioners, public authorities and academics expressing the most positive views. Less favourable views were expressed by private individuals/self-employed and bank/credit institution/investment funds.

### MOST COMMON SUGGESTION FOR IMPROVEMENTS

- the drafting of a clearer definition of the Centre of Main Interest (COMI)
- The inclusion of and guidelines on 'groups of companies' and corporate groups
- the creation of an EU register for insolvency proceedings;
- development of measures to instil a duty of cooperation between courts;
- an introduction of the UNICITRAL Model Law on cross border insolvency;
- A few stakeholders favoured greater harmonisation.

**SCOPE OF THE INSOLVENCY REGULATION:** Pre Insolvency, Hybrid Proceedings, private individual and extra EU Proceedings - (Question 3, 4, 5, 6)

Views were evenly balanced between those who felt the lack of coverage of pre-insolvency or hybrid proceedings was problematic (43%) and those who did not (42%). Nevertheless, a significant majority (59%) felt the EIR should cover such proceedings with academics, public authorities and insolvency practitioners particularly in favour of this. Views were mixed on exactly which proceedings should be covered and in particularly where court oversight should be required.

Examples of problems raised included cases differing views of Member States on which proceedings could be covered by the EIR; uncertainty relating to schemes of arrangement and how they are recognised at EU level and risks to workers interests.

A majority of respondents (49%) agreed that the **EIR should apply to private individuals/self-employed**, with 34% disagreeing with those in favour including judges,

insolvency practitioners and academics. Some respondents did not think an expansion should include consumers.

Opinion was evenly spread on whether the **lack of provisions for the recognition or coordination of extra-EU insolvency proceedings had created problems** with 44% agreeing and 37% disagreeing. Most banks, judges, insolvency practitioners considered this as problematic.

Suggestions for improving the scope of the EIR include removing the requirement of the appointment of an office holder; clarifying the definition of COM; creating a special agency to address problems of over indebtedness; harmonising rules on consumer insolvencies; incorporating the UNICITRAL model law or at least some concepts of it into the EIR and include pre-insolvency and hybrid proceedings in scope of EIR.

### **COMPETENT COURT TO OPEN INSOLVENCY PROCEEDINGS (Question 7, 8, 9, 10)**

A significant majority of respondents (77%) **approved of the use of the COMI** to locate the main proceedings whilst only 25% of banks approved. However 51% considered that the **interpretation of the term COMI by case-law caused practical problems**, with the most critical being private individuals/self-employed (67%), banks (75%), judges (58%), and insolvency practitioners (61%).

Nevertheless, some felt clarifications given by the ECJ have been very helpful to achieve a more uniform application of the term whilst others felt the COMI concept should not be revised.

Almost half of the respondents (49%) indicated **evidence of abusive relocation of COMI** with 29% feeling there was no abusive relocation. The most common situation cited was moves to UK in particular from Ireland and Germany with relief of the debtor and the promotion of rescue culture towards businesses in the UK being suggested as drivers.

44% of respondents reported **no problems with the interaction between the EIR and Brussels I** which have not been satisfactorily solved by case-law.

### **Groups of Companies - (Question 11)**

Almost half of respondents (49%) felt the EIR does not work efficiently for multinational group insolvencies with 30% feeling it does.

### **CO-ORDINATION BETWEEN MAIN AND SECONDARY PROCEEDINGS - (Questions 12, 13, 14, 15)**

36% of respondents felt the **division** between main and secondary proceedings was helpful with 37% disagreeing. However, 48% were **dissatisfied with the coordination** between main and secondary proceedings with 21% being satisfied. 40% also felt that the **duty to cooperate** between insolvency practitioners did not work effectively compared with 26% who thought they did. These concerns were reflected in the fact that 53% felt that the lack of a duty of cooperation between practitioners and the foreign courts or between courts had created problems with 18% stating that it had not.

### **APPLICABLE LAW – (QUESTIONS 16-19)**

A majority of respondents (55%) agreed the EIR's provisions on **applicable law are satisfactory** while 32% disagreed. A majority (56%) also agreed that **the exceptions in the EIR to the general rule** on applicable law are justified to protect legitimate expectations and legal certainty whilst 19% disagreed. Almost half of the respondents (49%) stated that the provision on **rights in rem operates** satisfactorily in practice, while 25% said it did not. Views on the provision on **detrimental acts** were rather divided, with 33% stating they operated satisfactorily in practice, 37% stating they did not.

#### **RECOGNITION AND ENFORCEMENT – (QUESTIONS 20-22)**

40% of respondents thought that there were **problems of recognition and enforcement** of the decision opening the proceedings or with the recognition and enforcement of further decisions during the proceedings whilst 34% disagreed

Only 23% of respondents stated that they were aware of cases where a **Member State has refused to recognise** insolvency proceedings or to enforce a decision on the grounds of public policy (**Question 21**). 56% stated that they were not aware of such cases.

Half of the respondents (51%) agreed that the definition of the **decision ‘opening insolvency proceedings’** should be amended to take into account national legal regimes where there is not an actual court opening the proceedings.

#### **PUBLICATION OF PROCEEDINGS AND LODGING OF CLAIMS- (QUESTIONS 23-25)**

Three quarters of respondents (75%) agreed that the **absence of mandatory publication** of the decision opening insolvency is a problem. Those stakeholders who mostly thought it was a problem belonged to the group of insolvency practitioners, companies and public authorities.

46% of those who expressed an opinion considered there were problems with lodging claims (question 24). Crucially, a significant proportion of key stakeholders who will often be the entities making claims felt there was a problem – 83% of private individuals/ self-employed and 75% of banks.

45% of respondents stated that there were **no difficulties with the EIR's rules on languages** for informing creditors and lodging claims and 23% felt that there were problems.

#### **DIFFERENCES IN NATIONAL INSOLVENCY LAWS – (QUESTIONS 26-28)**

Over half of the respondents felt that the **differences in national insolvency laws** create obstacles for the administration of proceedings or difficulties for companies with cross-border assets whilst 21% disagreed. On the other hand 38% felt there were important **inefficiencies in their national insolvency law** with 43% feeling there were not inefficiencies. A majority (55%), however, considered that their **national insolvency laws strike an adequate balance** between the need for efficient proceedings and the parties' right to an effective remedy. Only 23% of respondents disagreed.

#### **COSTS OF PROCEEDINGS – (QUESTIONS 29-31)**

32% of respondents indicated that the costs were disproportionate with regard to debt with 36% disagreeing. The issue of disproportionate costs for natural persons and small firms was

raised. Similarly, close to a third (36 %) considered that the costs of cross-border restructuring or reorganisation were not disproportionate and 21% felt that they were.

Opinions were divided on the question of whether there should be a simplified insolvency regime at reduced costs for certain debtors in particular for self-employed persons and SMEs (**Question 31**), with 37% in favour of the idea, 36% against, and 27% expressing no opinion. Stakeholders called for simplified proceedings and enhanced use of information technology to **expedite** proceedings.

### ANNEX 3: DATA ON ENTERPRISES AND INSOLVENCIES IN THE EU

#### Number of enterprises, employment and gross value added

According to the 2010/2011 Annual Report on EU Small and Medium sized Enterprises<sup>70</sup> SMEs comprise 99.8% of all enterprises (20,796,192 SMEs) while large enterprises account only for 0.2% (43,034 large enterprises). In employment terms, in the non-financial business economy<sup>71</sup> SMEs provide about two-thirds of workers with large enterprises accounting for the remainder.<sup>72</sup> This means that large enterprises, despite their smaller number are extremely important for the European economy as 33.1% of the working population is employed by them. Table 1 provides an overview of the number of enterprises, employment and gross value added in EU-27, by size class, in 2010.

**Table 1 Number of enterprises, employment and gross value added in EU-27, by size class, 2010 (estimates)<sup>73</sup>**

	Micro (1 – 9 persons employed)	Small (10 – 49 persons employed)	Medium (50 – 249 persons employed)	SMEs (1 – 249 persons employed)	Large (250 + persons employed)	Total
<b>Enterprises</b>						
Number	19,198,539	1,378,401	219,252	20,796,192	43,034	20,839,226
%	92.1	6.6	1.1	99.8	0.2	100
<b>Employment</b>						
Number	38,905,519	26,605,166	21,950,107	87,460,792	43,257,098	130,717,890
%	29.8	20.4	16.8	66.9	33.1	100
<b>Gross Value Added</b>						
EUR Millions	1,293,391	1,132,202	1,067,387	3,492,979	2,485,457	5,978,436
%	21.6	18.9	17.9	58.4	41.6	100

Source: Eurostat/National Statistics Offices of Member States/Cambridge Econometrics/Ecorys

Note that the six largest EU economies, i.e., France, Germany, Italy, Poland, Spain and the UK represent over 70% of all EU-27 SMEs.<sup>74</sup>

<sup>70</sup> Wymenga P. et al, 'Are EU SMEs recovering from the crisis? Annual Report on EU Small and Medium sized Enterprises 2010/2011', Report for the European Commission, DG Enterprise and Industry, available at [http://ec.europa.eu/enterprise/policies/sme/facts-figures-analysis/performance-review/files/supporting-documents/2010-2011/annual-report\\_en.pdf](http://ec.europa.eu/enterprise/policies/sme/facts-figures-analysis/performance-review/files/supporting-documents/2010-2011/annual-report_en.pdf) (last accessed on 9 July 2012).

<sup>71</sup> Note that the statistics in the report mentioned in Wymenga P. et al, 'Are EU SMEs recovering from the crisis? Annual Report on EU Small and Medium sized Enterprises 2010/2011' include NACE Rev. 1.1., sections C to K thus excluding agriculture, forestry, fishing, education, health, etc. *ibid*, p. 5, footnote 1.

<sup>72</sup> *ibid*, p. 7 – 8.

<sup>73</sup> *ibid*, p. 8.

<sup>74</sup> Internationalisation of European SMEs', EIM, Report for DG Enterprise and Industry available at [http://ec.europa.eu/enterprise/policies/sme/market-access/files/internationalisation\\_of\\_european\\_smes\\_final\\_en.pdf](http://ec.europa.eu/enterprise/policies/sme/market-access/files/internationalisation_of_european_smes_final_en.pdf), p. 23.

### **Scale of cross-border business**

It has been estimated that 25% of small and medium-sized enterprises (SMEs) in Europe export and 29% import within the single market<sup>75</sup>. This means that 5000 000 European SMEs have transactions with consumers, creditors or business partners from other Member States. Eurostat's database of multinational enterprise groups (Eurogroups Register — EGR) also adds to this picture: so far, it has registered 299 570 legal units located in the EU Member States (314 031 in EU and EFTA Member States) that belong to the 6 350 largest multinational enterprise groups.

### **Insolvencies within the EU**

According to the Creditreform 'Insolvencies in Europe 2011/12' report, in 2011 164,895 corporate insolvencies took place in EU-15 countries<sup>76</sup> and 39,423 in EU-12 countries excluding Cyprus (i.e., (Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia)<sup>77</sup> which amounts to 203,318 corporate insolvencies within the EU-27 (excluding Cyprus).

Considering that there are 20,839,226 enterprises within the EU it can be estimated that almost 1% of all companies went bankrupt in 2011

**Given that 25% of companies operate cross-border, one can infer that 25% of insolvencies that is 50000 companies are subject to proceedings falling within the scope of the EIR.**

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<sup>75</sup> Around 7% of SMEs in the EU are involved in technological cooperation with a foreign partner, another 7% are subcontractors to a foreign partner and 7% more have foreign subcontractors. Some 2% of SMEs are active in foreign direct investment. Most exports and imports by SMEs remain within Europe. See also 'Internationalisation of European SMEs', 2010:

<sup>76</sup> Creditreform 'Insolvencies in Europe, 2011/12', available at [https://www.uc.se/download/18.782617c713603ab70837ffd368/Europa\\_statistik\\_konkurser\\_2011.pdf](https://www.uc.se/download/18.782617c713603ab70837ffd368/Europa_statistik_konkurser_2011.pdf), p. 3.

<sup>77</sup> Ibid, p. 31



**Table 2: Breakdown of Enterprises by category (SMEs/Large) and foreign connections and respective rate of insolvency**

	SMEs (1 – 249 persons employed)	Large (250 + persons employed)	Total	Number of insolvencies (calculations are based on an insolvency rate of 1%)
<b>Enterprises</b>	20,796,192	43,034	20,839,226	<b>208,392</b>
<b>Enterprises transactions with consumers, creditors or business partners from other Member States</b>	25%		5,000,000	<b>50,000</b>
<b>Enterprises with foreign connections (subsidiaries, joint ventures) in the EU and third countries</b>	266,191	8,564	274,737	<b>3000</b>
<b>Enterprises with foreign establishments (branches) within the EU</b>	64,052	1,792	65,844	<b>700 (note that every insolvency can create several secondary proceedings)</b>

## Number of companies with foreign branches and number of groups

### (1) SME

According to the report on the ‘Internationalisation of European SMEs’, 2% of SMEs in the EU-27 plus Croatia, Iceland, Liechtenstein, FYROM, Norway and Turkey are active in foreign direct investment.<sup>78</sup> The incidence for the non-EU countries under examination is somewhat higher, i.e., 3% of non-EU SMEs have invested abroad as opposed to 2% of EU-27 SMEs. Based on this figure it can be estimated that approximately **415,923 SMEs in the EU-27 have any type of foreign connections (subsidiaries, joint ventures, branches and other unidentified connections).**<sup>79</sup>

The same report indicates that most foreign establishments are subsidiaries (42%) but considerable numbers are joint ventures (22%) and branch offices (i.e., not separate legal

<sup>78</sup> ibid , p. 15. Enterprises are considered to be active in foreign direct investment if they have foreign establishments (subsidiaries, branch offices, joint ventures).

<sup>79</sup> This estimation is based on data from the 2010/2011 Annual Report on EU Small and Medium sized Enterprises (20,796,192 SMEs in the EU-27 \* 2%).

entities) (20%). Note that these figures have been estimated on the basis of data from all the countries under review (i.e., EU-27 plus Croatia, Iceland, Liechtenstein, FYROM, Norway and Turkey). However, in view of the facts that the difference on the percentages of SMEs engaged in foreign direct investment between the EU-27 and the non-EU countries under review is not so significant it can be assumed that the percentages concerning the SMEs having each type of establishment would be the same for the EU-27. Consequently, it can be estimated that **83,185 SMEs in the EU-27 have foreign branches** [415,923 EU SMEs with foreign establishments multiplied by 20% of enterprises with foreign branches] and **266,191 SMEs in the EU have foreign subsidiaries and joint ventures** [(415,923 EU-27 SMEs with foreign connections multiplied by 42% of enterprises with foreign subsidiaries) + [(415,923 EU-27 SMEs with foreign connections multiplied by 22% of enterprises with foreign joint ventures)]].

Most of the SMEs with foreign connections limit themselves to one country (71%).<sup>80</sup> The size of the enterprise is directly related to the number of SMEs that invest abroad. In the period 2006 – 2008, only 2% of micro enterprises invested abroad as compared to 6% of small and 16% of medium-sized enterprises. On average, SMEs active in foreign direct investments have 2.2 foreign partner countries (2 countries per micro/small enterprise and 2.4 per medium-sized enterprise).<sup>81</sup> Again, even though these figures refer to the EU-27 plus Croatia, Iceland, Liechtenstein, FYROM, Norway and Turkey it can be expected that they would not significantly differ for the EU-27.

The ‘Internationalisation of European SMEs’ report however does not specify the destination of these foreign establishments and therefore alternative sources of information needed to be identified. The ‘2007 Eurobarometer - Observatory of European SMEs’ (‘2007 Eurobarometer’) concluded that 77% of European SMEs have foreign subsidiaries and joint ventures within the EU.<sup>82</sup> A combination of the data of the two reports leads us to the conclusion that **204,967 EU-27 SMEs have foreign subsidiaries and joint ventures within the EU** [(266,191 EU-27 SMEs with foreign subsidiaries and joint ventures multiplied by 77% of European SMEs with foreign subsidiaries and joint ventures within the EU).

The 2007 Eurobarometer does not include information on the destination of foreign establishments (branches) of EU-27 SMEs. Arguably, it could be submitted that the percentage of EU SMEs which chooses the EU as its destination for its foreign subsidiaries and joint ventures is the same as that of EU SMEs which chooses the EU as its destination for its foreign branches, i.e., 77%. Therefore, it is estimated that **64,052 EU-27 SMEs have foreign establishments (branches) within the EU** [83,185 SMEs in the EU-27 with foreign branches multiplied by 77% of European SMEs who choose as their business destination the EU].

## **(2) European Large Enterprises engaged in foreign direct investment**

The report ‘Internationalization of European SMEs’ does not contain any data on the number of large enterprises engaged in foreign direct investment. Therefore, this data will be estimated on the basis of the data contained in the 2007 Eurobarometer. Note that these two reports were prepared by different companies and therefore their methodology, and consequently their conclusions, may differ.

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<sup>80</sup> Ibid, p. 21-22.

<sup>81</sup> Ibid, p. 38

<sup>82</sup> Eurobarometer – Observatory of European SMEs 2007, see footnote 5, p.58.

According to the 2007 Eurobarometer 19.9% of EU-27 large enterprises have some kind of turnover from foreign partnerships, i.e., **8,564 large enterprises have any kind of turnover from foreign business partnerships** [43,034 of large enterprises in the EU multiplied by 19.9%].

Note that the definition of ‘foreign business partnerships’ under this report does not seem to include branches. Therefore, in view of the lack of information from other sources, for the time being it could be assumed that the percentage of large enterprises having foreign branches would be at least equal to the percentage of SMEs having foreign branches as specified in the ‘Internationalisation of European SMEs’ report. This would mean that at least **2,676 large enterprises have foreign establishments (branches)** [under the ‘Internationalisation of European SMEs’ report 64% of EU-27 enterprises engaged in foreign direct investments have foreign subsidiaries and joint ventures. This means that the 8,564 large enterprises with foreign subsidiaries and joint ventures represent the 64% of large enterprises engaged in any kind of foreign direct investment, i.e., 13,381 large enterprises are engaged in foreign direct investment. The percentage of enterprises having foreign branches under the ‘Internationalisation of European SMEs’ report is 20%; if the percentage is similar for large enterprises, it would mean that at least 2,676 large enterprises have foreign branches] Furthermore, the 2007 Eurobarometer provides that 67% of EU-27 large enterprises with foreign subsidiaries and joint ventures choose as their destination the EU, i.e., **5,738 large enterprises have foreign subsidiaries and joint ventures within the EU**.

If the percentage of EU-27 large enterprises with foreign branches which chooses as their destination the EU is similar to that of EU-27 large enterprises with foreign subsidiaries and joint ventures which chooses as their destination the EU it would mean that **1,792 EU-27 large enterprises have at least one establishment (branch) within the EU** [2,676 large enterprises have foreign branches multiplied by 67%].

#### ANNEX 4: INFORMATION ON PERSONAL INSOLVENCY PROCEEDINGS IN MEMBER STATES

PERSONAL INSOLVENCIES IN CERTAIN MEMBER STATES		
Personal Insolvencies in certain Member States in 2011 <sup>83</sup>		
Member State	Number of Insolvencies in 2011	
Austria	10,861	
Czech Republic	17,600	
Finland	3,531	
France	56,079	
Germany	129,800	
Latvia	810	
Netherlands	14,344	
Spain	999	
Sweden	8,051	
United Kingdom	143,871	
<b>Total Insolvencies</b>		<b>385,946</b>
<b>Median Insolvencies</b>	Calculated as insolvencies half between the figure for Austria and Netherlands	<b>12603</b>
<b>Estimated total personal insolvencies in EU</b>	Based on 17 Member States having personal insolvencies schemes. The median rate of 12603 is applied to 7 states	$385,846 + 88,221 =$ <b>474,067</b>

- In the UK, the number of consumer bankruptcy cases between 2003 and 2008 tripled from 35,604 to 106,544.
- In Germany, the new insolvency regulation, which entered into force in 1999, led to an increase in the number of consumer bankruptcy cases that were accepted at court from 1,634 in 1999 to 103,085 in 2007 and 95,730 in 2008.

<sup>83</sup> Credit Reform – Insolvencies in Europe 2011/12; [https://www.uc.se/download/18.782617c713603ab70837ffd368/Europa\\_statistik\\_konkurser\\_2011.pdf](https://www.uc.se/download/18.782617c713603ab70837ffd368/Europa_statistik_konkurser_2011.pdf)

- In France, 159,967 applications were admitted to the household debt commission situated at the French Central Bank and 87,673 amicable settlement plans were negotiated in 2008. The number of amicable settlement plans used to be higher in 1998 – 2003 ranging between 63% and 69%. This decrease is due to the fact that the number of personal reestablishment procedures, providing for the discharge of debt before a judge, has doubled from 16,321 in 2004, when the procedure was introduced, to 33,378 in 2008.
- In Spain, consumer bankruptcy procedures were introduced in 2004. In 2005, only 50 individuals applied for bankruptcy with the numbers rising to 96 in 2007 and 374 in 2008, representing an increase of 648% in the number of applications despite the fact that discharge of debt is not available under the Spanish legal system.
- In the Czech Republic, the number of private insolvencies rose dramatically – from around 10,600 in 2010 to 17,600 in 2011 (an increase of 66 %).
- In Latvia, the number of private insolvencies rose from 246 in 2010 to 810 in 2011 (an increase of 254%).
- Note that there are also countries where consumer bankruptcy cases are seldom due to the legislative framework; in Ireland, in 2007 only 5 persons were declared bankrupt, 10 were discharged of their debt and these numbers have not significantly changed throughout the years.

**ANNEX 5: HYBRID PROCEEDINGS IN MEMBER STATES AND THEIR INCLUSION IN ANNEX A OF THE INSOLVENCY REGULATION**

EU Member State	Pre-insolvency	Annex A	Hybrid	Annex A	Comments	Is it a problem that pre-insolvency and hybrid proceedings do not fall within the Regulation' scope?
<b>Austria</b>	Proceedings under the Business Reorganisation Act (Unternehmensreorganisationsgesetz BGBl I 1997/114 or URG)	No				No (URG proceedings are rare)
<b>Belgium</b>	<p>Enquete Commercial (Commercial Investigation) (Article 12 LCE)</p> <p>Designation d'un mediateur d'entreprise (Article 13 LCE)</p> <p>Accord amiable (Article 15 LCE)</p>	<p>No</p> <p>No</p>	<p>Designation d'un mandataire de justice (Article 14 LCE)</p> <p>Designation d'un administrateur provisoire (Article 28 LCE)</p>	No		Yes

	Reorganisations judiciaire par accord amiable (Article 43 LCE)	No  No		No		
<b>Bulgaria</b>	None		None			No answer
<b>Croatia</b>						
<b>Cyprus</b>						
<b>Czech Republic</b>			Reorganisation proceedings where the debtor remains in possession of his estate under the supervision of a trustee	No		No
<b>Denmark</b>						
<b>Estonia</b>			Reorganisation Proceedings (Estonian Reorganisation Act) and debt adjustment proceedings for natural persons (Debt Restructuring and Debt			Yes; this problem has appeared in case No. 3-2-1—114-11 of the Estonian Supreme Court (not possible for secondary proceedings to be reorgasniation proceedings)

			Protection act).			
<b>Finland</b>						
<b>France</b>	<p>1) Conciliation (Article L.611-4 to 611-15 of the French Commercial Code)</p> <p>2) Mandate ad hoc (Article L. 611-3 of the French Commercial Code)</p>	<p>1) No</p> <p>2) No</p>				Yes
<b>Germany</b>	Schutzschirmverfahren (Protective shield proceedings, Section 270B of the Insolvency Act)	No	Eigenverwaltung (Sections 270 and 270a of the Insolvency Act)	Yes	<p><b>Eigenverwaltung:</b> even though it is a debtor-in-possession proceeding it is included in Annex A</p> <p><b>Schutzschirmverfahren:</b> it is not included in Annex A as it applies at the pre-insolvency stage and is aimed at the preparation of insolvency</p>	No answer



					proceedings (elaboration of a restructuring plan)	
Greece			<b>Reorganisation</b> (Article 99 – 106ia of the Greek Bankruptcy Code)	No	<b>Reorganisation</b> is not included in Annex A despite the collective nature of the procedure	Yes
Hungary	No		No			No
Ireland						
Italy	<b>Piano di risanamento attestato</b> (Article 67(3)(b) of Italian Insolvency Act): workout project certified by advisor but not binding for other creditors	No	<b>Concordato preventivo</b> (Article 161 – 182 Italian Insolvency Act): binding workout agreement approved by creditors' majority voting under strict court supervision and sanctioned by a court  <b>Accordo di</b>	Yes	<b>Concordato preventivo</b> is included in Annex A even though it does not require a debtor's insolvency – it can be implemented in case of a debtor's liquidity or financial distress.  <b>Accordo di ristrutturazione dei debiti</b> : this procedure does not require a debtor's insolvency, it can be implemented in	Yes

			<b>ristrutturazione dei debiti</b> (Article 182bis of the Italian Insolvency Act): agreement with as many creditors representing 60% of the overall creditors and sanctioned by a Court	No	case of a debtor's financial distress  <b>Piano di risanamento attestato</b> is not included in Annex A as it is not of a collective nature.	
<b>Latvia</b>	<b>Out-of-court legal protection proceedings:</b> [NB: to be asked if these are pre-insolvency proceedings]	Yes			<b>Out-of-court legal protection proceedings</b> : these proceedings are a type of legal protection proceedings which are included in Annex A of the Regulation	No, as out-of-court legal protection proceedings are considered to fall within the Regulation's scope
<b>Lithuania</b>	No		No			No
<b>Luxembourg</b>	Gestion Controllee  Concordat preventif  (NB: to obtain more details on these	Yes				No

	proceedings to determine whether they are pre-insolvency or hybrid insolvency proceedings)					
Malta			<p><b>Statutory scheme of compromise/arrangement:</b> a scheme may be implemented within a liquidation proceeding and is binding upon its members and creditors if appropriately sanctioned.</p> <p><b>Company Recovery Procedure:</b> this procedure is modelled after the administration procedure in the UK. When a company is unable or is likely to become unable to pay its debts, it may request the Court to place the company under the recovery procedure and to appoint a special controller to take over, manage and</p>	No		Yes
				No		

			administer its business			
<b>the Netherlands</b>	Out-of-court workouts in the Netherlands require the consent of all creditors and there is no reference to such proceedings in the Dutch Bankruptcy Code	No	No (for companies)			Yes: in Rechtbank's – Gravenhage10 June 2010, LJN: BN9606, the Court did not issue an order according to Article 287a of the Dutch Bankruptcy Act (thereby blocking a successful workout) on the basis that the workout would not be recognized in other Member States
<b>Poland</b>	Rehabilitation proceedings (postepowanie naprawcze, Article 492 – 521 of the Bankruptcy and Rehabilitation Law): this proceeding applies to companies still solvent but in danger of insolvency	No	Forms of enforcement proceedings by administration or sale of the entire enterprise of the debtor (Article 10641 – 106413 and Article 106414 – Artucke 106423 of the Code of Civil Procedure): these proceedings are not linked to insolvency but they are of a collective nature	No		No: Rehabilitation proceedings are barely used in practice but if they were used and were successful they could raise problems.
<b>Portugal</b>						
<b>Romania</b>	Mandat ad hoc is a confidential procedure for the renegotiation of the	No (to be confirmed)	Preventive agreement which is a reorganization proceeding, supervised by the Court. The reorganization plan must	No		No  However, concerning preventive

	debtors' debt		be accepted by at least 2/3 of the creditors.			agreements problems may arise if creditors in other Member States can initiate liquidation proceedings
<b>Slovakia</b>						
<b>Slovenia</b>	NB: not clear from the national report which are the pre-insolvency and hybrid proceedings in Slovenia					No
<b>Spain</b>			Pre-insolvency schemes of arrangement	No		Yes
<b>Sweden</b>			Skuldsanering (debt relief, available only for private individuals)	No	Skuldsanering is not included in Annex 1 as it does not entail the partial or total divestment of the debtor.	No However, with regard to skuldsanering proceedings, it could be positive if they were included within the scope of the Regulation
<b>UK</b>			Schemes of arrangement (part 26 of the Companies Act 2006)	No		No

**ANNEX 6: INFORMATION ON INSOLVENCY REGISTERS IN THE MEMBER STATES**

Member State	Separate insolvency register	Electronic and publicly available	Free of charge	Other electronic database containing information on insolvency
Belgium	No	-	-	the Belgian Official Gazette
Bulgaria	Yes	No	-	register on liquidators and register of sales and auctions
Czech Republic	Yes	Yes	Yes	
Germany	Yes	Yes	Yes	
Estonia	No	-	-	the Estonian Commercial Register
Ireland	Yes, but limited to personal bankruptcies	No	-	records of the Company Registration Office
Greece	Yes	No	-	
Spain	Yes	Yes	Yes	
France	No	-	-	Database of registrars of the commercial courts (infogreffe)
Italy	Yes	No	-	
Cyprus	No	-	-	-

Latvia	Yes	Yes	Yes	
Lithuania	No	-	-	Register of legal entities
Luxemburg	No	-	-	The Business Register
Hungary	No	-	-	The Business register and the Company Gazette
Malta	No	-	-	
The Netherlands	Yes	Yes	Yes	
Austria	Yes	Yes	Yes	
Poland	Yes	Yes	Yes	
Portugal	Yes	Yes	Yes	
Romania	Yes	Yes	Yes	
Slovenia	Yes	Yes	Yes	
Slovakia	Yes	Yes	Yes	
Finland	Yes	Electronic but not publicly available; information has to be requested via the Legal Register Centre	No, an extract costs €10	

Sweden	Yes (various registers accessible through a single website)	Yes	Yes	
United Kingdom				
England and Wales	Yes	Yes	Yes	
Northern Ireland	No	-	-	Department of Enterprise, Trade and Industry (Online DETI)
Scotland	Yes	Yes	Subject to a fee	

It follows from the table that there are

- 14 Member States which have electronic insolvency registers
- 9 Member States which have information on insolvency of companies or individuals available in another electronic database which is publicly available
- 4 Member States which have neither.