European Insolvency Regulation

APPLICABLE LAW

Cross Border Insolvency in the EU – September 2020

Sónia Pereira
A financially distressed company with COMI in European State “A” and an establishment in European State “B” files for insolvency proceedings in State “A”. No secondary proceedings are opened in State “B”.
To avoid further losses, the appointed insolvency practitioner intends to close the establishment situated in State “B” and terminate immediately the contracts of employment of its employees, which are subject to the law of this State.
State “A” law permits him to do so, whereas the law of State “B” imposes a period of notice to the employees of 30 days.
Is the law of State “A” applicable, allowing the insolvency practitioner to terminate those employment contracts with immediate effects?
• Yes
• No
1. The system on the applicable law in the Regulation (EU) 2015/848

1.1. Format of rule (Article 7) - exceptions (Articles 8-18)

1.2. Main features - Recital (66)
- Simple;
- Uniform;
- Comprehensive;
- Applies to all different categories of insolvency proceedings prescribed in Article 3 (main and secondary proceedings – Article 35).
2. General rule: the *lex fori concursus*

2.1. Article 7(1) – the law of the State of the opening of proceedings governs the insolvency proceedings and their effects;

- importance of the COMI: international jurisdiction as determined by the COMI governs the applicable law;
- underlying policy: legal certainty and predictability of applicable law;
- predominance of the *lex fori concursus*: determines all effects of insolvency proceedings.
2. General rule: the *lex fori concursus* (cont)

2.2. The examples of article 7(2) – applicably of the *lex fori concursus* to the conditions for the opening, conduct and closure of insolvency proceedings and thirteen specific matters;

- the role of the list: facilitates the interpretation of the primary provision;
- non exhaustive (Judgment of 21 January 2010, MG Probud Gdynia, C-444/07, par. 25);
- application insofar as Articles 8-18 do not apply.
2. General rule: the *lex fori concursus* (cont)

2.3. Specific matters governed by the *lex fori concursus* according Article 7(2):

2.3.1. Conditions for the opening of the insolvency proceedings:

- The debtors that may be subject to insolvency proceedings, on account of their capacity, form (corporate or unincorporated) or ownership (private or State-owned) – Article 7(2)(a);
- Requirements and standards for commencement of proceedings;
- Capacity to file the petition – parties that may apply;
- Type of proceedings that may be opened (e.g. liquidation or reorganization).
2. General rule: the lex fori concursus (cont)

2.3.2. Conduct of insolvency proceedings

- The divestment of the debtor, the appointment of an insolvency practitioner and the powers of the debtor and the practitioner – Article 7(2)(c);
- The assets which form the insolvency estate – Article 7(2)(b);
- The claims which are to be lodged against the debtor’s estate (insolvency claims) and claims arising after the opening of the insolvency proceedings (estate liabilities) – Article 7(2)(g);
- Lodging, admission and verification of claims – Article 7(2)(h);
- Ranking of claims and distribution of proceeds – Article 7(2)(i).
2. General rule: the lex fori concursus (cont)

2.3.3. Closure of insolvency proceedings
- The conditions and effects of closure of proceedings – Article 7(2)(j);
- Creditor’s rights after the closure of insolvency proceedings – Article 7(2)(k).

2.3.4. Effects of the insolvency proceedings
- The conditions under which set-off may be invoked – Article 7(2)(d);
- The effects on current contracts in which the debtor is a party (e.g. termination of contracts) – Article 7(2)(e);
- The effects of insolvency proceedings on proceedings brought by individual creditors, with exception of pending lawsuits - Article 7(2)(f);
- Rules relating to voidness, voidability or unforceability of legal acts detrimental to the general body of creditors, including clawback actions – Article 7(2)(m).
2. General rule: the *lex fori concursus* (cont)

2.4. Problems of qualification:

- *lex concursus* only applies within the limits of ‘insolvency proceedings and its effects’;
- qualification of a legal question as concerning ‘insolvency proceedings and their effects’ when it does not fall within the list of Article 7(2) – may include questions governed, not only by provisions qualified as insolvency law, but by any legal system if its provisions interfere with the right or obligation for insolvency law reasons.

- Criteria developed by the CJEU:
  1.º - source in derogating rules specific to insolvency proceedings (Judgements of 4.09.2014, Nickel, C-157/13, par. 27, and of 10.12.2015, Kornhaas, C-594/14, par. 17); or, if it’s not the case,
  2.º - direct and inseparable consequence of the insolvency proceedings (Judgement of 21.11.2019, Ce De Group, C-198/18, par. 34-37).
3. Exceptions to the general rule

3.1. General policy – Recital (67) – protection of legitimate expectations and certainty of transactions;

3.2. Two main groups of cases:
   3.2.1. Allocation of the effects of insolvency proceedings to the law of a Member State other than the opening of proceedings:
   - Contracts relating to immoveable property – Article 11;
   - Payment systems and financial markets – Article 12;
   - Contracts of employment – Article 13;
   - Rights subject to registration – Article 14;
   - Protection of third party purchasers - Article 17;
   - Effects on pending lawsuits and arbitral proceedings – Article 18.
3. Exceptions to the general rule (cont)

3.2.2. Exclusion of some rights or entitlements from the effects of insolvency proceedings:

- Third parties rights in rem – Article 8;
- Set-off – Article 9;
- Reservation of title – Article 10.
4. Third parties *rights in rem* on assets located in another Member State

4.1. Article 8 and the exclusion of third parties rights *in rem* on assets of the debtor located in another Member State from the effects of insolvency proceedings – rule of relative immunization.

4.2. Substantive rule, and not a conflict-of-laws rule.

4.3. Rationale – Recital (68) importance of third parties rights *in rem* for the granting of credit.
4. Third parties *rights in rem* on assets located in another Member State (cont)

4.4. Requirements of application:

4.4.1. Rights *in rem*

- concept given by the *lex rei sitae*;
- covers any rights in rem, regardless of their nature – Judgement of 26.10.2016, SCI Senior Home, C-195/16;

4.4.2. Relevant time – rights *in rem* constituted before insolvency proceedings were opened;

4.4.3. The situs of the debtor’s assets – location in another Member State; criteria to determine where assets are situated – Article 2(9);

4.4.4. Protection covers all kinds of property.
4. Third parties rights in rem on assets located in another Member State (cont)

4.5. Consequences of the exception – non-alteration of the right in rem (Recital 68):

   4.5.1. Ability to enforce despite the prohibition of new executions or automatic stay;

   4.5.2. The right to segregation or separate settlement of the collateral security in case of realization of assets.

5. Detrimental acts

5.1. Conflict-of-law regime regarding effects of insolvency proceedings on detrimental acts

- the general rule of Article 7(2)(m) – in principle, the *lex concursus* determines the rules relating to voidness, voidability or unenforceability of acts detrimental to all creditors (e.g. fraudulent or preferential transactions);

- the exception established in Article 16 – prevents the application of *lex fori concursus* if an action for voidness, voidability or unenforceability of a detrimental act is governed by the law of another Member State that precludes such an action.

5.2. Policy of the exception – Recital (67) protection of the legitimate expectations of third parties.
5. Detrimental acts (cont)

5.3. Requirements of the exception:

5.3.1. The act must have been undertaken before the opening of the insolvency proceedings (Judgement of 16.04.2015, Hermann Lutz, C-557/13);

5.3.2. The person who benefited from the act must prove that it is subject to the law of a Member State other than the that of the opening of proceedings;

5.3.3. And that that law does not allow any means of challenging that act in the relevant case, i.e. taking into account the circumstances of the case.
5. **Detrimental acts** (cont)

5.4. Application to all requirements necessary under the law of the Member State, regardless of their procedural or substantial nature, including:

- statutes of limitation relating actions to set aside transactions (Judgement of 16.04.2015, Hermann Lutz, C-557/13);

- procedural questions such as form and time-limits for the opposition of the exception and the question of knowing if the article can be applied by the court of its own motion after those time-limits (Judgement of 08.06.2017, Vinlys Italia, C-54/16).
6. Pending lawsuits or arbitral proceedings

5.1. Conflict-of-law regime regarding effects of insolvency proceedings on pending lawsuits:

- general rule - Article 7(2)(f) – the *lex fori concursus* determines the effects of insolvency proceedings on proceedings brought by individual creditors (e.g. automatic stay);

- exception - Article 18 - allocates the effects of insolvency proceedings on pending lawsuits or arbitral proceedings concerning an asset or a right which forms part of the debtor’s estate to the *lex fori processus*. 
6. **Pending lawsuits or arbitral proceedings** (cont)

5.2. Actions covered by the general rule and actions covered by the exception – distinction between pending lawsuits (*lex fori processus*) and pending enforcement actions (*lex fori concursus*); different consequences of each proceedings on the debtor’s estate (Judgement of 9.11.2016, Enefi, C-212/15).

5.3. Rationale of the exception – legal certainty and close link with the procedure.

5.4. Wide interpretation of the notion ‘Lawsuit concerning an asset or right which forms parte of the debtor’s estate, including monetary claims’ (Judgement of 6.06.2018, Tarragó da Silveira, C-250/17).
A highly indebted company with COMI in European State “A” pays a considerable sum, in respect of a loan agreement, to a company of the same economic group established in State “B” and, a few days later, files for insolvency in State “A”. Six months after the opening of the proceedings, the insolvency practitioner brings an action to challenge these payments. The company that benefited from the payment contests that according to the law of State “B”, which was the law chosen by the parties, the lawsuit should have been filed within three months after the opening of proceedings. The limit for clawback actions of the law of State “A” is one year.

Is the law of State “A” applicable an the lawsuit go ahead?

- Yes
- No