Principles of European Insolvency Law

Edited by

Prof. W.W. McBryde

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Law of Business and Finance

Volume 4

Kluwer Legal Publishers

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PRINCIPLES OF EUROPEAN INSOLVENCY LAW

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Editors

Sebastian Kortmann
Dennis Faber

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PREFACE BY THE SERIES' EDITORS

The Business and Law Research Centre, established in 1994, is a leading research institute in the field of commercial and private law, recognised by the Royal Dutch Academy of Sciences. It is a co-operation of the Faculty of Law of the University of Nijmegen and a number of renowned law firms and companies.

In 1999, the Business and Law Research Centre founded the International Working Group on European Insolvency Law, in which insolvency law experts from ten Member States of the European Union have participated. This Volume 4 in the Series Law of Business and Finance is the result of the research conducted by the working group.

We are most grateful to the distinguished members of the working group for their dedication to the project. Our special gratitude extends to Professor Axel Flessner and Professor William McBryde, who - as visiting professors at the Business and Law Research Centre (Van der Grinten-chair) - have written an extensive *General Commentary* to the *Principles of European Insolvency Law*. Furthermore, we would like to thank Shannon McBriar, Niels Vermunt, Harmen Wielens, Marianne Koopman and Gonnie Jakobs for their outstanding work in preparing the manuscript for publication. Finally, we would like to thank the Netherlands Organisation for Scientific Research (*Nederlandse Organisatie voor Wetenschappelijk Onderzoek*) for its generous financial support, without which the working group would not have been able to conduct its work. The cut-off date for the texts of this book is 1 March 2003.

June 2003

Professor Sebastian Kortmann
Chairman of the Board of the
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GENERAL INTRODUCTION

1. Background and objective of the project

In the past decades, many Member States of the European Union have introduced important new legislation in the field of insolvency law. In several countries, such as *Belgium*, *France* and *Germany*, this has led to a fundamental revision of existing insolvency law. In *England* and *Scotland*, notable changes in the insolvency law were introduced recently. In other countries, such as *The Netherlands* and *Spain*, as well as a number of Eastern European countries, a substantial revision of the insolvency law is being prepared. It is remarkable that the more recent European insolvency laws continue to show substantial differences in underlying policy considerations, structure and content. The question arises how these differences can be reconciled with the ongoing economic integration of Europe. Increasingly, the activities of companies transgress national borders and are regulated by European legislation. How do these developments relate to the formation and application of national insolvency law? The development of a European market requires an understanding of the differences between legal systems, a move towards uniformity in legal terminology and concepts and the avoidance of diversity resulting from a lack of knowledge about other European jurisdictions. The question also arises whether there should be one common insolvency proceeding that applies to the entire European Union. A similar question has been raised during the preparation of the European Convention on insolvency proceedings of 1995. The Report of Virgós and Schmit on this Convention states:

> "The idea of a single exclusive universal form of insolvency proceedings for the whole of the Community is difficult to implement without modifying, by the application of the law of the State of the opening of proceedings, pre-existing rights created before insolvency under the different national laws of other Contracting States. The reason for this lies in the absence of a uniform system of security rights in Europe, and in the great diversity of national insolvency laws as regards criteria for the priority to be given to the different classes of creditors."[1]

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1 M. Virgós and E. Schmit, Report on the Convention on insolvency proceedings, nr. 12.

The Convention and its successor, Council Regulation (EC) No 1346/2000 on insolvency proceedings, do not attempt to introduce uniform substantive insolvency law within the European Union, but are largely limited to issues of jurisdiction, recognition and applicable law.

Even though the idea of establishing in the short term one single universal insolvency proceeding for the entire European Union may perhaps seem illusive, this does not mean that national insolvency laws do not share common characteristics. On the contrary, when looking beyond the differences in structure and formulation, the insolvency laws of the various countries appear to have many common elements. The *Principles of European Insolvency Law* try to capture these common elements. They can be seen as the *essence* of insolvency proceedings in Europe as they reflect, on a more abstract level, the common characteristics of the insolvency laws of the European Member States.

The *Principles of European Insolvency Law* may provide a foundation for greater harmonisation. They are the first attempt to tackle an area of law which is of great commercial importance, but in which some think it too difficult to detect a European approach. The *Principles* are not a work of comparative law, although there is much comparative material of value in the *National Reports*. The *Principles* themselves look to a future of more European integration in areas of commercial law and practice. The *Principles* together with the *General Commentary* to the *Principles* may serve as working material for further study, which could result in proposals for legislation on a supranational level. In the shorter term, they may be of use in efforts to modernise national insolvency laws by serving as a European framework.

Considering this background, one cannot be too surprised that the *Principles of European Insolvency Law* differ from the Principles of European Contract Law as well as from the UNCITRAL Legislative Guide on Insolvency Law in so far that it is not the objective of the *Principles* to provide model provisions for national legislation. The *Principles* do not try to reflect the ideal rules for a European Insolvency Code; they do, however, state the areas of conformity and divergence and may thus be helpful when such a Code should come on the agenda.

The *Principles* and the *General Commentary* are also intended to enable lawyers with different national backgrounds to better understand the existing systems of insolvency law in Europe. The entry into force of Council Regulation (EC) No 1346/2000 on insolvency proceedings has increased the necessity of accessibility and understanding of the insolvency laws of the Member States of the European Union, as it entails that courts and practitioners will regularly be confronted with insolvency laws of other Member States.

The selection of the jurisdictions in the project reflects the intention to represent the *insolvency systems* occurring within the European Union. Given this intention, it was not considered essential to present the insolvency laws of all Member States.

2. Scope; unitary approach

The structure of insolvency laws in Europe differs widely from country to country. Some countries provide for a variety of insolvency proceedings laid down often in several different statutes and regulations (e.g. *England, Scotland, Italy, Denmark*). Other countries have only one (comprehensive) proceeding (e.g. *Germany, France*). There are countries where insolvency law applies only to debtors with commercial or professional activities (e.g. *France, Belgium*) and other countries where insolvency law applies to debtors of any type whatsoever (e.g. *England, Scotland, Germany, The Netherlands*). In a few countries a sharp distinction is made between individual debtors (natural persons) and incorporated debtors (juridical persons) (*England, Scotland*). In other countries a distinction is made between commercial debtors according to the size of their enterprise (*France*).

In the *Principles* no distinction is made between kinds of debtors, whether incorporated or not, whether business people, professionals or consumers. It is obvious, however, that the need for an integrated view of insolvency law in Europe arises foremost in the field of commercial and professional activity and less so with respect to purely private households. Therefore, the *Principles* are framed with a view to the insolvency of debtors carrying on a business (commercial and professional debtors). With the focus on

business insolvency, the scope of the *Principles* is congruent with the definition and the list of proceedings in Council Regulation (EC) No 1346/2000 on insolvency proceedings. The insolvency of private individuals is covered by the *Principles* to the extent that consumers may also be subject to general insolvency law in the various legal systems. The *Principles* do not, however, reflect provisions (mainly of recent origin) which are aimed at the problem of consumers' over-indebtedness.

In many countries a clear distinction is made from the outset between proceedings aimed at liquidation of the debtor's assets and proceedings aimed at reorganisation of the debtor's liabilities (*Belgium, Denmark, England, Italy, Luxembourg, Scotland, Spain*). There are other countries where liquidation and reorganisation are viewed only as alternative or even combinable possible outcomes of a (unitary) proceeding (*France, Germany, The Netherlands*). The *Principles* are meant to show the common characteristics of European insolvency laws. For this reason they refer to "the insolvency proceeding" without any further subdivision. It is hoped that this unitary approach allows to reflect and integrate all the proceedings in Europe that carry the essential attributes of legal insolvency treatment.

The essential legal attributes of insolvency proceedings are twofold. On the one hand, the proceedings relate to the debtor's assets. The debtor will be or may be deprived of the power to manage its property and to dispose of it, or the debtor is at least restricted and supervised in the exercise of those powers, and eventually the assets may be realised for the benefit of the creditors. On the other hand the proceedings relate to the creditors. They are barred from enforcing their claims individually and they may lose at least part of their claims as a result of a liquidation with insufficient proceeds or as a result of a reorganisation by which their claims are modified.

The *Principles* follow this *legal* view of insolvency proceedings. Views on the economic, social and political purposes of insolvency proceedings may vary considerably in different jurisdictions and different periods of time. The policy behind legislation may favour creditors or debtors or the preservation of enterprises and employment, or a combination of these goals.

Policies also determine attitudes as to distribution of powers. There are, at the one end, systems with an emphasis on governmental or judicial authority (e.g. *France*). At the other end, there are systems with considerable trust in the ability of private actors to make responsible use of insolvency law instruments (e.g. *England*). In between, there are systems where a court will inevitably be involved but where its role is mostly organisational, leaving much room to the desires of the parties affected by the insolvency (e.g. *Germany, The Netherlands*). In any case, whatever the policy and the attitude as to the distribution of powers, the law will use the aforementioned essential legal attributes. The focus on these legal attributes facilitates the establishment of common characteristics of insolvency proceedings in Europe.

3. Exclusions

The *Principles* do not deal with insolvency proceedings concerning insurance undertakings, credit institutions, investment undertakings which provide services involving the holding of funds or securities for third parties, or to collective investment undertakings (see also art. 1 (2) Regulation (EC) 1346/2000 on insolvency proceedings).

The *Principles* do not address voluntary debtor-creditor-arrangements ("work outs") outside insolvency law - although such arrangements may have a very important part to play in a country's insolvency practice. Voluntary arrangements are based on general contract and property law and they require the consent of every participant to be affected. The very essence of insolvency law is, however, to impose solutions even without the consent of debtor and creditors, and only this aspect gives rise to the need for these *Principles*.

Likewise, the *Principles* do not include obligatory information systems which have been set up (or are at least provided for) in some countries, notably *France* - although they may be regarded there, together with the insolvency proceeding proper, as an integral part of an overall enterprise rescue system. The reason for this is that they have no legal impact on the debtor-creditor-relationship. They may provide a framework for bringing

debtor and creditors together for negotiations on a voluntary arrangement and they may trigger the insolvency proceeding.

Furthermore, the *Principles* do not address the issue of liability of directors and shareholders. In many jurisdictions, liability may be imposed on management and shareholders for loss unlawfully caused to creditors, shareholders and parties contracting with the company when insolvency may be forthcoming. The grounds of liability are manifold and they vary from country to country. They can be found in the law of contracts, the law of torts, company law and insolvency law. Such potential liability may be an important factor for the debtor and its management to consider an insolvency application, but in itself is not within the scope of the *Principles*.

4. Structure of the book

This *General Introduction* is followed by the *Principles* together with the *General Commentary*. This part of the book is followed by the *National Reports* of the countries represented in the *International Working Group on European Insolvency Law* (*Belgium, Denmark, England, France, Germany, Italy, Luxembourg, The Netherlands, Scotland, Spain*). Finally, the text of the *Principles* is presented in English, French, German and Spanish.

The *General Commentary* does not provide exhaustive comparative reflections. References to national laws are in the first place meant as examples. The *General Commentary* to each *Principle* starts with a brief introduction to the problem, followed by an explanation of the *Principle* itself. The *General Commentary* indicates as much as possible where national systems substantially deviate from a particular *Principle*.

The *National Reports* contain an outline of the insolvency laws in the countries represented in the working group. The *National Reports* are all structured in more or less the same manner and contain information on, *inter alia*, the most important types of insolvency and insolvency related proceedings, the institutions and participants involved in the proceeding(s), the protective effect of insolvency proceedings, the position of creditors and employees, specific issues such as the reversal of juridical

acts (*Actio Pauliana*), set-off, the effect of insolvency on existing contracts and pending law suits and the issue of directors' liability, and the adoption, contents and effects of reorganisation plans and compositions.

PRINCIPLES AND

GENERAL COMMENTARY