The Inevitability of 'Insolvency Tourism'

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Abstract
This article seeks to describe and analyse the phenomenon of 'insolvency tourism', a popular term used to describe the manoeuvring of debtors to secure the application of (more favourable) insolvency proceedings in a jurisdiction other than the one where they are incorporated or domiciled. This article argues that insolvent debtors are assisted in this by two factors: (i) the jurisdiction rules in the European Insolvency Regulation that permit a latitude of interpretation and are susceptible to manipulation; and (ii) the current and continuing disparity in domestic insolvency laws and available procedures within the European Union. This article looks at whether the phenomenon of 'insolvency tourism' will be diminished as a result of changes to the European Insolvency Regulation and the gradual convergence of national approaches to insolvency and European initiatives in this field.

Keywords
Insolvency, European Insolvency Regulation, debtor, creditor, COMI, jurisdiction, harmonisation, regulatory arbitrage.

1 Introduction

The fact of international commerce, a continuation of age-old imperative, some may say, prompts many businesses to gear their economic expansion to a global scale. Interaction between economic entities located in different countries, as a by-product of globalisation and the increasing dependence on new and powerful technologies that effectively 'shrink' the world, facilitates the delocalisation of business and renders the search for new markets and new places from which to operate throughout the world an easy task. The number of internationally-known businesses and brands that appear on High Streets throughout the world increases from day to day with a consequent rise in the number of 'multinationals', many of which are household names the world over. The prevalence of these 'universal' brands may be viewed both as a signal of globalisation as well as its by-product for good or ill. But, before the business and its brand go global, there is a simple choice that begins the process: that of where to domicile or, in the case of legal entities, incorporate its activities to begin with.

This question, which may seem to attract a matter of fact response: 'wherever the entrepreneur wants to do so', has actually quite a complex answer. This is because, normally, the choice of domicile or incorporation determines the applicable law and is thus susceptible to prior selection by promoters of the business, including its would-be managers and investors. One clear advantage of this is where domiciliation or incorporation in one jurisdiction is followed by carrying on business

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in that state or, using that location as a bridge-head, for activities elsewhere.[1] This may occur in geographically contiguous groups of states, but, more especially, in those that have formed an economic union, such as the European Union, and where attempts have been made to equalise access to the market for entrepreneurs by the progressive diminution of tariffs and other impediments to conducting business across borders. The issue, though, is what law applies to the business vehicle when it carries out such activity across a frontier.

The private international law position to which many states subscribe is that the entrepreneur and/or business vehicle takes their/its personal, place of domicile or incorporation, law with it when settling in another jurisdiction and may benefit from having this 'home' regime applied to it for legal questions associated with its status. However, adding an extra layer of complexity, transactional rules will usually be governed by the law of the 'host' jurisdiction where the business vehicle carries out business. As such, *inter alia*, the usual rules on contract formation and delictual liabilities in that jurisdiction would normally apply, as would any rule deemed to be of *ordre public* status (i.e. mandatory rules of public order). Nonetheless, taking personal law with you does usually have a benefit: the relative advantages or disadvantages of such status questions may then be contrasted with the normal regime applied to those domiciled or incorporated in that jurisdiction, where these have an impact on status.[2] In addition, the contrast between 'home' and 'host' rules in a number of transaction-related areas may determine the relative advantage/disadvantage (and associated costs) of domicile or incorporation in those jurisdictions being compared.

In this light therefore and in relation to overall incorporation/domicile decisions, a number of legal factors, both status and transaction connected, may play a part in the choice: the existence of a favourable environment for lending and security as well as perceived 'lighter' rules in certain sensitive areas, such as employment relations, although the extent to which favourable legal rules are a dominating factor in this choice is debatable, as good legal planning and sound professional and tax advice is available in most jurisdictions. However, in many instances, it is clear that the selection of incorporation venues is partly dependent on a prior appreciation of whether the legal system as a whole is perceived as business-friendly.[3] This does not wholly supersede other factors playing a part in that choice, including such intangible ones as unfamiliarity with culture, language and geography as well as the lack of desire to be adventurous or take risks. Nonetheless, for those entrepreneurs keen to take the leap into the (relatively) unknown, domicile or incorporation choice and attendant issues are a firm part of their ultimate investment decisions.

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[1] There is some evidence in the case law of North American companies using the United Kingdom in particular as a stepping-stone to carrying out business in Europe: BRAC, Daisytek, Collins & Aikman, Enron, Nortel all being examples of this practice.

[2] This was certainly the thinking evident in cases like Case C-212/97 *Centros Ltd v. Erhvervs- og Selskabsstyrelsen* [1999] ECR I-1459, which tested the use of the then Art. 48, EC Treaty to facilitate such incorporation choices, driven for the most part by the disparity in incorporation costs between some Continental jurisdictions (Austria, Denmark and Germany) and the United Kingdom. Case C-208/00 *Überseering BV v. NCC Nordic Construction Company Baumanagement GmbH* [2002] ECR I-09919, another case in the Art. 48 line of jurisprudence illustrated the use of 'requalification' rules to effectively subject foreign incorporations to domestic status rules, with the unfortunate consequence in that case that the entity concerned lost its juridical status under German law. See Roth (2003).

[3] This also explains the interest by the World Bank in determining access to markets by entrepreneurs collated in its annual Doing Business Report, which ranks jurisdictions according to criteria associated with the ease of establishing businesses.

2 The Essential Premise: Insolvency(-Avoidance) Planning Is Natural

Given that the factors described above form part of the investment decision, it should not be surprising that part of the legal environment that will be subject to a prior examination is whether there are favourable insolvency rules in case the business fails, i.e. when the entrepreneur and the business they run becomes or risks becoming an insolvent debtor.[4] This is a natural concern, since the same process that sees globalisation at times of economic upturns will bring the need to consider the availability of sound insolvency processes when the inevitable (and all too periodic) downturns in the world economy occur, a particularly acute concern in the wake of the Global Financial Crisis and continuing concerns as to whether global economies will ever return from the downturn. The existence of turnaround mechanisms and/or preventive measures that assist recovery, whether creditors and debtors are assisted by formal or informal frameworks in insolvency, whether there are upstream components to these procedures allowing for early intervention, whether there are good prospects for negotiating positive outcomes with creditors and/or other stakeholders, whether there is a strong office-holder profession that is sufficiently innovative in restructuring techniques, whether there is a good supportive environment through the courts and regulatory bodies are all reasons for choosing a legal system and, by extension, a country to operate in. Even where the choice of domicile or incorporation location may be predetermined by some necessity, such as the imperative to carry out business there, the above questions play a part in determining the recourse to insolvency-avoidance techniques and measures seeking to insulate the investment from the risk of adverse rules.

The nature of international insolvency, nonetheless, is such as to raise a considerable number of issues, the attempted resolution of which may bring legal systems into conflict, particularly at the level of the potential conflict of private international law rules. For example, quite apart from status questions, the diversity of laws applicable to the transactions of the debtor is nowhere more important than when their consequences are felt at the time of insolvency. The rules applicable to assets and their disposal may be subject to different laws. The type of security that may be taken, the extent of execution and recovery exercisable as well as guarantees and support for security by means of registration or notice requirements will, without saying, differ from jurisdiction to jurisdiction. Liabilities attendant on the use of these assets will also change with their location. The laws applicable to claims by creditors pressing their suit in a number of different jurisdictions will raise issues of conflict of laws and the precise nature of the law applicable to the resolution of any dispute. These claims may be made more complex by the presence of qualifications such as security and quasi-security. The identity of creditors may affect their treatment, with some national laws giving or refusing priority to certain categories of creditors. The priorities of these debts are also important with the identification of who may benefit from statutory ranking or privileges and, ultimately, from any distributions that may

[4] The availability of turnaround, restructuring and/or market exit procedures is also one of the indicia in the Doing Business Report. Although there is little evidence that concerns about insolvency preoccupy the average entrepreneur at the time of setting up, the focus on insolvency in the report does explain the interest of the international institutions (such as the World Bank, the International Monetary Fund and others) in insolvency law reform across the world.

be made. Furthermore, how different classes of creditors are to be treated fairly across all the jurisdictions where the insolvent debtor possesses assets are also important issues in the context of insolvency proceedings.

In fact, issues of efficiency and effectiveness of proceedings involving the debtor are fundamental in the insolvency context. Tied up with this question is the matter of which court will exercise jurisdiction in respect of procedural and/or substantive issues. This is especially important if it results in a restriction on insolvency representatives entering and claiming assets in another jurisdiction, especially where there are local rules that are significantly different from those experienced elsewhere. The number of proceedings in existence involving the same debtor will have an impact on the assets left for distribution to creditors, not only because of the absorption of fees by the management of the process in the courts, but because of the lack of consensus between jurisdictions in dealing with fundamental issues of principle including the subjection of the debtor to proceedings, the qualification of the moment of insolvency, the availability of preservation measures over assets as well as a near-infinity of procedural and substantive questions.

Furthermore, of particular relevance in an age which places a premium on 'rescue', the availability of rescue procedures may, because collections of assets necessary for the viability of the debtor or of a part of its business are located in several jurisdictions, depend on coordination between different courts. The lack of consensus between jurisdictions will be particularly important where the diversity of procedures available in different jurisdictions means that rescue procedures are not universally available, resulting in the impossibility of saving many debtors. The differential pace of development in insolvency and disparity in the availability of the 'right' procedure(s) can therefore be a matter of grave concern for business. Even where coordination may be forthcoming, it would be highly unlikely that exactly the same procedural or substantive rules would be available, leading to issues in respect of how coordination will be achieved at the procedural level or how the rescue would be applied to all the assets necessary for the restructuring, especially in the absence of a uniform framework for rescue plans at European level. In these instances, the success of coordination will depend on vast amounts of goodwill on the part of the practitioners and the courts as well as the absence of national rules that may serve as impediments to the process.

Nonetheless, although admitting that insolvency planning may feature as a natural part of the entrepreneurial decision, overall, we face a particular problem. While it may be acceptable for insolvency to feature, as one of a number of factors naturally, in a choice of where to incorporate as part of normal business planning at the outset, it is not seen as desirable that such choices should be possible once the 'predictability' of commercial relations exists through the incorporation location being determined, the idea being that the choice of location determines, as for many status questions, the outcome of the procedure and the consequent impact on the debtor, e.g. the dissolution of a legal entity or the discharge of a natural person.[5] Paradoxically, one of the issues in *Centros* and *Uberseering* was whether a 'real seat' rule (*Sitztheorie*) could apply to negate the incorporation choice for legal entities with

[5] There is no explicit articulation of this perspective in the literature, but it is highly possible that the structure of texts (such as the Brussels Convention 1968 and the European Insolvency Regulation) which single out particular constituencies to which more flexible rules apply (involuntary (or tort) creditors, employees etc.), is a reflection of a concern that more vulnerable participants in the process lack the means to elect for a jurisdiction of their choice in the same way that tortfeasors or business entities might.

respect to certain jurisdictionally sensitive rules, such as a minimum capital requirement or employee participation in management, to which the European Court of Justice's clear answer was not if in fact it served as an impediment to the freedom of movement for companies (a freedom also enjoyed by individuals) by imposing obligations that denatured the absolute nature of that right.[6] The same could be argued for resort to adequate restructuring processes which, in light of recent developments at European level, may be becoming an accepted norm among member states of the European Union.[7]

What is, however, important in the insolvency context is that such a test is in fact used as the means by which choice of court is determined for the purposes of jurisdiction to open proceedings in the European Insolvency Regulation ('EIR'),[8] a prospect that opens up the possibility of proceedings occurring otherwise than in the jurisdiction of domicile or incorporation. As will be seen, the use of this test is not subject to a 'one-off' assessment at the time of incorporation or election of domicile, but may in fact change throughout the life of the debtor, as its 'centre of main interests' ('COMI') can of course fluctuate with the commercial reality of its business. Concomitantly, what can fluctuate naturally owing to entrepreneurial choices might also be the subject of choices targeting particular outcomes, leading to the choice of a particular jurisdiction to host the restructuring regime for the entity/person and/or its business. This is what is termed 'COMI-requalification' (a more neutral term) or 'COMI-manipulation' (for those who view it pejoratively).[9] The factors that drive this process are similar to those that exist at the time of election of domicile or incorporation (adequate laws, procedures and methods, availability of office-holders and supportive institutions etc.).[10] There is little evidence that such choices are driven by reasons of fraud or illegitimate avoidance of liabilities, although this cannot be entirely ruled out of the equation. Nonetheless, there is a fear that debtors may use such techniques simply to flee their creditors or to, at the very least, make life difficult for them. However, there is some doubt that the numbers of such creditors who 'forum shop'[11] for (il)legitimate reasons are statistically significant.[12] In the end, it might simply be a question of perception, rather than reality, but one that

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[6] See above n. 2.

[7] Recommendation on a New European Approach to Business Failure and Insolvency (Document COM(2014) 1500 Final) (12 March 2014) ('EU Recommendation').

[8] Council Regulation (EC) No. 1346/2000 of 29 May 2000 (in force 31 May 2002). This has recently been amended and replaced by Regulation (EU) No. 2015/848 of 20 May 2015 (mostly to come into force 26 June 2017) ('Recast EIR').

[9] One of the more amusing (depending on one's perspective) terms used is that of the 'bankruptcy brothel', meaning a jurisdiction that takes all comers who can pay, often applied to the United Kingdom, whose rules are seen as particularly accommodating. See E. Moya, 'London Risks Becoming "Brothel" for Bankruptcy Tourists', *The Observer*, 31 January 2010.

[10] For consumers/individuals, the critical issue has been the availability of discharge from bankruptcy and the period before it can be obtained, which differs wildly across Europe. This is also an issue picked up in the EU Recommendation, above n. 7.

[11] This is a term of some vintage that denotes the ability to elect for a (usually) favourable forum. It also carries connotations that one can choose one's law as if it were simply a commodity, like handbags or shoes. See A. Walters and A. Roman, '"Bankruptcy Tourism" under the EC Regulation on Insolvency Proceedings: A View from England and Wales', Insolvency and Corporate Law Working Group Working Paper Series, Nottingham Law School, 2010, p. 17 (particularly the literature cited in footnote 40), copy available at: <http://www.ntu.ac.uk/PSS/Nottingham%20Law%20School/Publications/99914.pdf>.

[12] Walters and Roman, above n. 11, pp 4-5 and 22 et seq., discussing the relevance of the statistics and impact on institutional responses in England and Wales.

frightens some and indeed constitutes a concern reflected by the European institutions in formulating legislative texts in the area of insolvency.

Another factor added into the mix is the fact that the assessment of the adequacy of laws is continually changing as a result of the drive towards reform, in Europe noticeably, leading to a form of 'regulatory competition' or 'arbitrage' between jurisdictions and legal systems, in which, for the moment, certain countries are perceived to have an ascendancy. Nonetheless, the continued disparity between legal systems is a source of some concern and has led to European Union intervention in this field for the first time. Returning, however, to the EIR, it is not just the COMI issue that leads to jurisdiction choice being subject to determination, but other structural defects it contains that lead to COMI-manipulation becoming the preferred route for practitioners dealing with debtors in need of restructuring.

3 The First Issue: The Inadequacy of the EIR

3.1 The Inception and Paradigm of the EIR

The EIR began life with a handicap: it was the product of a different age with a different conception of how things should work. At its inception, the project was simply an off-shoot of the work which led to the Brussels Convention 1968[13] and was conceived as a private international law text allocating jurisdiction between courts, a choice which, subject to certain 'carve-outs', determined the relevant substantive and procedural laws which would apply. Using a form of 'modified universalism', it trod a cautious path between the aims of unity and universality and the reality of jurisdictional competition motivated by the desire to hold on to economically sensitive decision making. As such, a 'constellation' paradigm resulted, in which a 'main' proceeding, at the COMI of the debtor, was circled by 'secondary' proceedings (subject to a minimum 'establishment' threshold test) with which it would be coordinated using rules especially formulated for that purpose and designed to ensure the primacy of main proceedings. By the time the text came to be enacted, which took a number of decades and many painful negotiations and attempts, this formula was no longer adapted to the needs of the modern age and contained, one could say, a number of major, and arguably fatal, defects.

The first was a limiting feature that did not quite make sense: 'main' proceedings could be of both rescue and liquidation types; 'secondary' proceedings could only be liquidation in nature. One might reasonably suppose that the original idea was to avoid competing rescues. Surprisingly, however, it might also be a holdover from the original intention of the EIR, which, according to the Virgos-Schmit Report,[14] was simply to coordinate liquidations occurring in parallel. The inclusion of rescue-type procedures within the text as an option was an afterthought, given that at the time of the EIR's enactment, such procedures were by no means universally available in the European Union. It is no surprise, therefore, that present in

[13] Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters 1968, later readopted as Council Regulation (EC) No. 44/2001 of 22 December 2000 (as revised and amended by Regulation (EU) No. 1215/2012 of 12 December 2012).

[14] M. Virgos and E. Smit, Report on the Convention of Insolvency Proceedings, Brussels 3 May 1996, EU Council Doc. 6500/96, para. 51 (Virgos-Schmit Report). The report was written to accompany the European Bankruptcy Convention 1995 as a guide to its interpretation and has since been used to cast light on the contents of the EIR, which it resembles.

the literature on the EIR (and its predecessor Convention) from an early date has been the concern that the jurisdictional paradigm would artificially limit the scope for rescue and result in rescue being dependent on the fortuitous location of proceedings.[15] This would lead inevitably to forum shopping taking place and a race to the court seen as providing the most beneficial outcome for interested parties. No real surprises there!

This might also explain why the co-ordination elements of the EIR, designed to assist the maintenance of the 'constellation' paradigm, have mostly been passed over in favour of certain avoidance techniques, despite the avowed intention of the text to discourage forum shopping.[16] The techniques used have included the requalification of COMI as well as the growing practice in the United Kingdom of using Letters of Request to minimise the risk of proliferation of proceedings in other jurisdictions through instituting a form of 'early warning' system.[17] This can work reasonably well in the case of single individual or entity proceedings, where the existence of establishments can allow for the intervention of jurisdictional choice, leading to the logical (if absurd) recent outcome in the case of a company that the location of its incorporation, in the case of a requalification of COMI elsewhere, could nonetheless retain sufficient threshold activity to warrant retaining establishment status for the purposes of opening proceedings.[18] It works less well in the case of groups of companies, which is the second major defect of the text, because of the interference of the separate legal entity principle in company law.[19]

It is this second defect, the absence of a special rule for groups of companies in the EIR and one that is related in terms of its outcome, which undoubtedly has become the critical catalyst for COMI-requalification. Although groups of companies (or enterprise groups) are not a recent phenomenon, their importance has increased in recent years, as reflected in greater awareness within the literature,[20] though recognition of this reality may have come too late for the drafters of the text. The absence of any definitive rule dealing with groups of companies has led directly to the competition for jurisdiction seen in cases as early as that involving the Parmalat group, where the courts in Italy and Ireland each claimed jurisdiction over one of the group's subsidiaries, Eurofood IFSC Ltd.[21] On a reference from the courts in Ireland, where the subsidiary was incorporated, the judgment of the European Court of Justice in *Eurofood*[22] was notable for emphasising two things: the strength of the presumption in the text in favour of the registered office of the corporate debtor and the need for mutual trust between courts hearing matters potentially involving the same corporate debtor. What this was felt to mean was that there could not be jurisdiction on a group-wide basis unless and until the presumption was rebutted in the case of subsidiaries, a factor that would undermine attempts at obtaining a rescue synergy across boundaries.

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[15] See Johnson (1996).
[16] Preamble Clause 4, EIR.
[17] *Re Nortel Networks SA & Ors* [2009] EWHC 206 (Ch).
[18] *Burgo Group v. Illochroma SA*, C-327/13, ECLI:EU:C 2014:2158.
[19] Although the issues are similar, though not identical, in the case of individuals and legal entities, for the sake of simplicity, the discussion below will refer to the company/companies in view of their use as the business vehicle of choice.
[20] See, particularly, Mevorach (2009).
[21] It is also noteworthy that, reading the judgments of the Irish (*Re Eurofood IFSC Ltd* [2004] IEHC 607; [2006] IESC 41) and Italian (*Tribunale di Parma*, *Sentenza* of 19 February 2004) courts, the stress placed by courts on different facts could lead legitimately to an assumption of jurisdiction on those connecting factors each court deemed relevant.
[22] Case C-341/04 *Eurofood IFSC Limited* [2006] ECR I-3813, para. 37.

Indirectly, the judgment cast doubt on the practice, largely pioneered by United Kingdom practitioners leading to a collocation of COMIs in the same location in cases such as *Re Brac*[23] and *Re Daisytek-ISA*,[24] the latter involving a parent company located in the United States which had filed for Chapter 11 protection, where the English court granted administration orders in respect of its English subsidiary (and its immediate subsidiaries domiciled in England and Wales). This part of the judgment was not contentious, given that the COMI of these companies was clearly in England and Wales. However, the fact the judge purported to open proceedings involving other European subsidiaries, located in France and Germany, on grounds that the English company was not only the holding company for the European operations of the group but also provided management support and co-ordination of the group's activities, was contentious and provoked alarm, expressed by both courts and commentators in France and Germany, and in the latter case, in quite virulent terms.[25] The technique was, however, further developed in cases such as *Re MG Rover España SA*, which illustrated that synergy could be obtained, so as to enable the co-ordination of rescue across a group of companies, through the avoidance of secondary proceedings being opened.[26]

Pushing boundaries further in what has become the archetypal case, the decision in *Re Collins & Aikman*[27] showed how this synergy could lead to positive results for interested parties where a conscious attempt is made at avoiding secondary proceedings through persuading creditors that their interests will be adequately safeguarded through limiting proceedings to a single (main) set of proceedings.[28] In fact, the decision in *Re Collins & Aikman* has been described as a 'valuable judgment which instils confidence' that the EIR is 'capable of operating in an efficient and pragmatic way and achieving advantageous outcomes in international insolvencies'.[29] In the case, European members of the group lodged petitions for administration in England and Wales, which were granted on the High Court being satisfied on the evidence presented to it that main proceedings as defined in Article 3 of the EIR were possible and appropriate.[30] When the administrators that were appointed considered the affairs of the companies, the conclusion reached was that the companies formed an inter-connected group with operational functions being administered on a Europe-wide basis. For this pre-eminent reason, consideration was given to how the continuation of the business could be co-ordinated and the disposal of the business and assets could be organised to maximise the benefit to and possible return for creditors.[31]

It became apparent to the administrators that a Europe-wide strategy was at risk from creditors using the provisions of the EIR to initiate secondary proceedings

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[23] *Re Brac Rent-A-Car International Inc.* [2003] EWHC 128 (Ch).

[24] *Re Daisytek-ISA Limited and others* [2003] BCC 562.

[25] See the judgment of the CA Versailles (24ème chambre), 4 September 2003 (Case RG No. 03/05038), which recites the reasons given by the Pontoise Commercial Court to deny recognition of the English judgment (a decision later overturned by the Supreme Court on 27 June 2006); see Paulus (2003).

[26] *Re MG Rover España SA and others* (Norris J, 11 May 2005, Chancery Division, High Court: Birmingham District Registry), reported in Springford (2005).

[27] *Re Collins & Aikman Europe SA and others* [2006] EWHC 1343 (Ch).

[28] 'Secondary' proceedings would still exist as hypotheticals in the mind of the office-holders who would need to determine the allocation of value to each procedure for distribution purposes. This technique is also known as the 'virtual secondary'.

[29] *Insolvency Lawyers Association Technical Bulletin*, July 2006, p. 1.

[30] *Re Collins & Aikman Europe SA and others* [2006] EWHC 1343 (Ch), paras. 5-6.

[31] Ibid., para. 8.

in various countries where group companies were located, provided, of course, that the threshold test for an establishment was met. Given that a number of the companies potentially met this criterion, the result could have been to put into jeopardy the continued trading of the businesses and the conduct of sales on a group-wide basis. To forestall the possibility of proceedings proliferating, the administrators provided assurances to individual creditors and creditors' committees at meetings held across Europe that local priority rules would be respected as far as possible within the proceedings ongoing in England and Wales, provided that no secondary proceedings were opened. The measure of the success of the strategy taken can be seen in the fact that in only three minor instances were secondary proceedings initiated.[32]

Following further consultation of the creditors and the absence of dissent, the court was persuaded to accept arguments that grounded jurisdiction on a number of bases[33] and permitted the administrators to maintain the assurances given to creditors, which meant that secondary proceedings were largely avoided, a factor which avoided the significant disadvantage which would have arisen because of further expense and delay while these proceedings took place.[34] The interest of this judgment was in illustrating a very pragmatic method by which rescue can be coordinated, but which relies for its success on the avoidance of secondary proceedings taking place. The outcome of this case incidentally also brought focus to a recommendation to lift the bar on rescue procedures in secondary proceedings, noted earlier and also suggested by Moss and Paulus.[35] This would, even if changed, inevitably raise the question of whether secondary proceedings would continue to be avoided on the grounds of costs and delay occasioned by the proliferation of proceedings or whether the co-ordination paradigm in the EIR might finally prove of some use in regulating the relationship between main and secondary proceedings in cases where rescue could be effected by the availability of rescue-type procedures in both main and (all of the) secondary jurisdictions. One outstanding point, however, is that the disparity between national laws may still constitute an impediment to the coordination of multiple rescue proceedings.

3.2 Has the Recast EIR Resolved the First Issue?

The legacy of *Re Collins & Aikman* has been that avoidance techniques have become the norm, and necessarily so in the case of corporate groups, to the extent that their use has become absorbed into mainstream practice through incorporation in the Recast EIR. The Executive Summary accompanying the proposal for amending the EIR gives a flavour of the reasons why incorporation of this technique was viewed as a necessity. It recites as its *leitmotiv* the background economic statistics, which reveal an annual average loss of some 1.7 million jobs occurring as a result of the 200,000 or so annual insolvencies of companies in the European Union between 2009 and 2011. It estimates that there are at least 5 million European companies with cross-border relationships, whether with customers, creditors or other business partners (including co-contractants such as suppliers, distributors etc.), of which some 1% will be debtors and 2% creditors in cross-border insolvencies. These insolvencies are stated as particularly affecting large companies, which are more likely to engage in cross-

[32] Ibid., para. 11.

[33] Ibid., paras. 15-17, citing *Re Condon, ex parte James* (1874) LR 9 Ch App 609 and the statutory purpose of rescue in Paragraph 3, Schedule B1, Insolvency Act 1986.

[34] Ibid., paras. 42-48.

[35] See Moss and Paulus (2006), p 5.

border transactions and whose importance is especially acute because they provide 30% of all jobs within the European Union and some 41% of the 'gross added value' in transactions. Knock-on insolvencies affecting the trading partners of these companies, including many small and medium enterprises ('SMEs'), is a particular hazard highlighted in the Executive Summary.[36]

In light of this, the Recast EIR seeks to emphasise the need for efficiency and effectiveness in proceedings. As such, although reiterating the legislators' distaste for forum shopping,[37] the text now authorises an office-holder to give *Re James*-type promises to avoid the opening of secondary proceedings and consequent impediments to rescue (especially the proliferation of proceedings and costs as well as difficulties in achieving coordination). The effect of the promise is that the office-holder states his intention to comply with the national rules regarding priority and distribution as well as what factual assumptions regarding the value of the estate and proposed means of realising that value the undertaking is based on. Subject to approval by local creditors, the effect of the undertaking, if made in the requisite form, will bind the estate and permit local creditors to enforce its terms in main proceedings.[38] The availability of the remedy here simply underscores the importance of ensuring adequate protection of the interests of creditors, but does not remove the benefits of the avoidance of secondary proceedings in enabling rescue synergy to be achieved.

While the distinction between main and secondary proceedings has been removed in terms of what types of procedures they may consist of, what this framework does not entirely avoid is the continuing need to requalify COMI, although usefully it institutes a 'virtual constellation' of procedures, paying lip service to the value of the main-secondary paradigm. In fact, where an attempt at requalifying COMI is made, a court will still be required to carry out a comprehensive assessment of whether jurisdiction is founded.[39] Furthermore, although the presumption as to COMI may still be rebutted, COMI will only be regarded as hard and fast if the debtor has not moved its registered office, place of business or habitual residence within a look-back period of 3-6 months,[40] thus attempting to forestall some of the questionable COMI-shifts that have been seen in recent years.[41] However, these look-back periods may simply serve to focus the attention of the debtor (or of their advisors more probably) on the need to organise responses to COMI questions further in advance. As responses to the issue of COMI-requalification, the new provisions do nothing to resolve the underlying issue of its desirability and, in the end, merely seek to confine it within acceptable bounds. This may simply be an acknowledgment of the reality of insolvency practice and the benefits coordination can achieve in the case of the rescue of multiple entities.

4 The Second Issue: The Disparity between Legal Systems

[36] Executive Summary, p. 4.

[37] Preamble Clause 5, Recast EIR. Preamble Clause 29 goes on to say that the text 'should contain a number of safeguards aimed at preventing fraudulent or abusive forum shopping', perhaps hinting that not all forum shopping is bad.

[38] Ibid., Art. 36. See also Preamble Clauses 41-44.

[39] Ibid., Preamble Clause 30 and Art. 4.

[40] Ibid., Preamble Clause 31 and Art. 3(1). The 3-month period applies to businesses, while the 6-month period applies to individual debtors. Preamble Clause 32 goes on to say that further evidence may need to be supplied by a debtor in support of its assertions on the question of jurisdiction.

[41] *O'Donnell & Anor v. The Bank of Ireland* [2012] EWHC 3749 (Ch) (21 December 2012); *JSC Bank of Moscow v Kekhman & Ors* [2015] EWHC 396 (Ch) (20 February 2015).

4.1 The Quest for Optimal Insolvency Laws

The second issue arises because of the unceasing quest for the optimal insolvency law system, which has stimulated reform activity in the European Union since the 1990s, well before the enactment of the EIR, but also during the currency of the project. Indeed, as will be seen below, it could be argued that the existence of the EIR has spurred the process by which reforms have taken place. This issue is very much related to the afore-going, simply because there is no point in requalifying COMI to end up in a jurisdiction whose laws exhibit lacunae and defects. In certain countries, notably in Central and Eastern Europe, reforms were prompted by the disintegration of the Soviet Bloc, with countries like Czechoslovakia,[42] Estonia,[43] Hungary,[44] Latvia[45] and Lithuania[46] needing to enact insolvency laws *ex nihilo*,[47] as insolvency was a feature that was wholly absent in their prior Socialist legal systems. Reforms in Germany were also prompted by the need to reconcile legislation in West Germany with that in the former East Germany when both parts of the country were reunited in 1990. The 1990s were also propitious for changes in Finland,[48] Ireland,[49] Malta,[50] Portugal[51] and Sweden.[52] France also faced strong calls for readjustment of the balance between debtors and creditors, prompting the passing of a major amendment law.[53]

At the point the EIR was enacted, at the turn of the millennium, projects were ongoing and subsequently completed in the United Kingdom,[54] Spain[55] and again in France.[56] The accelerated pace of reforms, especially during this period, has led some authors to speak of a 'second wave' of collective reforms, which it has been thought might lead to a convergence in European insolvency laws, perhaps on the model of the American 'Chapter 11' procedure.[57] Other countries reassessing their legislation included, *inter alia*, Finland,[58] the Netherlands[59] and Slovakia.[60] Greece also enacted a new law in 2007 based on the French system,[61] while in France, two sets of

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[42] Act no. 328/1991. After the separation of this country into two territories in 1993, Slovakia readopted the same piece of legislation as Act no. 328/1993.
[43] Law on Bankruptcy 1992; Commercial Code 1995.
[44] Law no. 49 of 1991.
[45] Law of 3 December 1991.
[46] Law on Bankruptcy 1992.
[47] Or, more problematically, re-enact, as interim measures, pre-Soviet laws.
[48] Corporate Reorganisation Law 1993:47.
[49] Companies Act 1990.
[50] Companies Act 1995.
[51] Decree Law no. 132/93 of 23 April 1993; Decree Law no. 127/96 of 8 August 1996.
[52] Reorganisation of Business Act 1996:764.
[53] Law no. 94-475 of 10 June 1994.
[54] Insolvency Act 2000; Enterprise Act 2002.
[55] Law no. 22/2003 of 9 July 2003.
[56] Law no. 2005-845 of 26 July 2005.
[57] See Parry (2004), pp. 2-5. The 'first wave' is regarded as being constituted by the introduction of rescue laws in Europe in the 1980s.
[58] Bankruptcy Law no. 120/2004.
[59] Bankruptcy Act 2004. A later proposal, initiated in 2007, to rewrite the entire bankruptcy law, was abandoned by the Dutch Government in 2010, although pre-packs have been the subject of a proposal in 2014 likely to become law.
[60] Act no. 7/2005.
[61] Insolvency Code of 2007. Major changes were made to this text in 2011 and it is likely to be the subject of review in the near future.

amendments were made to its law in 2008 and 2010.[62] In 2011, Spain comprehensively reviewed its earlier law.[63] More recently, France again enacted comprehensive reforms to all of its insolvency procedures in 2014.[64] Further reform proposals in other European Union countries are known, particularly in states that have had to respond to the enduring Global Financial Crisis and the more recent spectre of sovereign bankruptcy.

While part of the reform process in these countries will have involved the use of international benchmarking texts[65] as well as advice from the relevant organisations operating in the insolvency sector, consideration of the scope of reforms in other jurisdictions has undoubtedly also taken place. As such, there has been a notable similarity in the responses to insolvency law reform as well as some striking dissimilarities.[66] This insight into, acknowledgment of and, in some cases, direct inspiration from the laws elsewhere has been, it could be suggested, accelerated by the existence of the EIR itself. Since its entry into force, the EIR has generated hundreds of cases, many on the issue of jurisdiction. It has also seen avoidance techniques used to overcome the cumbersome nature of its jurisdictional paradigm, as in *Re Collins & Aikman* (noted above). Indirectly, these cases have pitted insolvency legal systems against one another as they have revealed the desire by office-holders and creditors alike to be able to choose the system that appears to offer them the best outcomes. This has led to examination of other states seen as 'competitors' in a process of 'regulatory competition' or 'arbitrage' and emulation of the best features of these models through direct borrowings of institutions, procedures and techniques. Where, however, legislators have not been quick to act, the office-holders have used practice techniques to place the debtors they manage in jurisdictions perceived as offering more optimal outcomes in terms of restructuring. While disparities between national systems exist, these techniques will seemingly continue to proliferate.[67]

4.2 Will the EU Recommendation Address the Second Issue?

A possible resolution to this issue has come in the shape of the launch in mid-2013 by the European Commission of a consultation on a new European approach to business failure and insolvency seeking to assess national approaches to allowing 'honest' entrepreneurs a second chance or fresh start. The consultation looked to other areas of potential harmonisation, including the conditions under which insolvency proceedings are allowed to begin and national legal frameworks on restructuring plans, to potentially eliminate divergences between these rules in the interests of users of the system. The consultation also sought to ascertain whether special rules should exist for SMEs and whether the rules on status, powers and supervision of liquidators should also converge. Of special interest, the consultation also interrogated responders on the issue of avoidance actions and aspects of national rules that could be brought more into line across Europe. Reflecting earlier work which contained an incidental

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[62] Ordinance no. 2008-1345 of 18 December 2008; Articles 57-58, Law no. 2010-1249 of 22 October 2010.
[63] Law no. 38/2011 of 10 October 2011.
[64] Ordinance no. 2014-326 of 12 March 2014.
[65] European Bank for Reconstruction and Development (EBRD) Core Principles for an Insolvency Law Regime 2004; World Bank Principles and Guidelines for Effective Insolvency and Creditor Rights Systems 2005 (as amended); United Nations Commission on International Trade Law (UNCITRAL) Legislative Guide on Insolvency Law 2004 (as amended).
[66] See Omar (2007) (especially in the latter half of the article).
[67] See Charny (1991).

focus on wrongful trading,[68] the consultation also asked whether directors' duties in the vicinity of insolvency and any penalties attached to their failure should be the subject of a Europe-wide text. In fact, the communication announcing the consultation advocated concentration on improving 'second chances' by introducing particular measures, including fast-track procedures for honest debtors, aligning and shortening discharge periods and, for SMEs in particular, improving prevention, access to out-of-court settlements and debt-recovery generally.[69]

The focus on SMEs readily explains how the European Commission has now moved towards promoting its own vision of what European insolvency should look like. In 2014, it published the EU Recommendation, which targets reforms to deal with four particular concerns: the availability of a framework to facilitate preventive restructuring, assisting restructuring negotiations through enabling the appointment of a mediator and for stays to be available, ensuring the success of restructuring plans through certain minimum content and clarifying creditor and court involvement in the adoption process as well as providing protection for new financing arrangements. To these priorities the European Commission has tacked on the issue of appropriate discharge periods for entrepreneurs, settling on 3 years as a new norm.[70] Although the Recommendation was primarily addressed to the member states with action expected by March 2015, the European Commission reserved the option (in light of a further study) to propose 'additional measures to consolidate and strengthen the approach […] in the recommendation', suggesting it might consider an enactment in some form to impose a common framework across the member states. It remains to be seen what the focus for this text will be and what role a European framework, which might take the form of a supranational procedure, will play in reducing the need to have recourse to COMI-requalification in order to obtain the advantages of optimal restructuring procedures in favourable jurisdictions. In the interim, arguably, the landscape will not significantly change in respect of COMI-requalification and prevailing practice will still see its use.

5 Summary

The issues behind insolvency tourism are complex and may differ according to whether the debtor is corporate or individual in nature. Nonetheless, the one thing all debtors have in common is the desire to optimise outcomes, both in terms of the law that will apply to any potential restructuring or debt-forgiveness as well as how the rules on jurisdiction operate so as to give those courts applying that law the opportunity to resolve matters in connection with that debtor. The paradox behind the EIR is that its jurisdictional paradigm directly encouraged forum shopping through the use of techniques avoiding its cumbersome coordination paradigm. The EIR's existence and the many cases involving jurisdiction have also pitted insolvency

[68] Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe (2002), pp. 9, 12 (Recommendation III.13).
[69] Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee — A New European Approach to Business Failure and Insolvency, Document COM(2012) 742 final (12 December 2012), pp. 5-6 and 8.
[70] EU Recommendation, above n. 7, pp. 6-10. See also INSOL Europe, Study on a new approach to business failure and insolvency – Comparative legal analysis of the Member States' relevant provisions and practices, Tender No. JUST/2012/JCIV/CT/0194/A4 (12 May 2014) assessing to what extent the member states were already compliant with the norms being promoted.

systems in direct competition with one another, like commodities subject to the demand and supply of the market. Astute debtors and their creditors alike have used these rules to obtain optimal or favourable outcomes. Less astute debtors have had no such benefit. This disparity neither excuses nor militates against recourse to such techniques, nor does it explain whether such techniques are in the end desirable. It is simply a fact whose existence one has to deal with in the here and now. As such, the argument is essentially: if one deprecates forum shopping, how is one to stop it? The answer is not evident. The experience thus far is that, however much one may wish to channel the natural desires of debtors, one cannot do so unless and until the shape of insolvency law is sufficiently proximate in all jurisdictions that there is no comparative advantage in seeking to use one system over another.[71] That way, there will be no further need for the practice techniques that enable the quest for optimal insolvency procedures. This may well be the position that is reached within the European Union as a result of the EU Recommendation, although there is a long way yet to go. In the interim, insolvency tourism is here to stay. As such, it needs to be embraced, even if not entirely accepted, or steps taken to minimise the consequences of the damage some may perceive it to cause.

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[71] This was indeed the fervent wish of Professor Josephus Jitta, doyen of Dutch private international law, as expressed in Jitta (1895).

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