

Student Paper

Multinational enterprise groups in insolvency: how should the European Union act?

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1. Introduction

Although multinational enterprise groups¹ are a common phenomenon, legal regimes generally do not provide for means to deal in an encompassing way with multinational enterprise groups.² Most jurisdictions only recognize the legal concept of a 'corporation', an entity which has a legal personality separate from the individuals comprising it. But the business of corporations is increasingly conducted through (multinational) 'enterprise groups'. The economic advantages, as well as the legal incentives, are various.³ For instance, the formation of a multinational enterprise group may be driven by fiscal considerations or the lowering of risks of legal liability by confining them to particular group members. Despite the reality of the multinational enterprise group, much of the legislation relating to corporations solely deals with the single corporate entity.⁴ This inconsistency is also apparent in the area of cross-border insolvency. Legal entities within the multinational group are subject to separate insolvency proceedings, which is at odds with economic reality. This may come at a cost, as is illustrated by the KPNQwest case.

KPNQwest operated a glass fiber network, providing business customers telecommunication services throughout Europe. For these services, KPNQwest had built a modern broadband network of glass fiber cables which was divided into six interconnected 'EuroRings', the pan-European Ring. In their turn, these rings were connected to Qwest's network in the United States. KPNQwest had at least two separate group companies in nearly every jurisdiction, one of which owned the assets and provided the actual access to the network in the country concerned and to

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1 Multinational enterprise groups consist of entities that are mutually connected either by shareholding or via contracts. This article will often refer to multinational groups of companies as such basic structures underlie many multinational enterprise groups.

2 I. Mevorach, *Insolvency within Multinational Enterprise Groups*, 2009, p. 1.

3 U.N. Comm'n on Int'l Trade Law (UNCITRAL), UNCITRAL Note by the Secretariat, Working Group V (Insolvency Law), 10 February 2010, A/CN.9/WG.V/WP.92, Paras. 17-25, available at: <<http://www.uncitral.org>> (last visited: 22 November 2010) [hereinafter: WP.92].

4 See WP.92, supra note 3, Paras. 1-5.

the pan-European Ring.⁵ When the parent company of the group, KPNQwest N.V., went into insolvency, many of its subsidiaries in Europe entered into insolvency proceedings as well. As the trustees of the parent did not have any powers with respect to bankrupt subsidiaries in other Member States, it proved to be very difficult to coordinate the sale of the rings. As a result, the KPNQwest group disintegrated and it is likely that the proceeds of the sale of the assets were much lower than they would have been if the enterprise had been sold as a whole.⁶

This article aims to provide some guidance on how the European Union should deal with the issue of multinational enterprise groups in insolvency. Section 2 will establish that the European Insolvency Regulation ('EIR') needs reform. In line with the foregoing, the EIR deals with the single corporate entity (Section 2.1). Nonetheless, some judges and insolvency representatives have developed solutions to achieve results that more accurately reflect the economic reality of multinational enterprise groups (Section 2.2). It is often argued that the EIR should contain specific rules concerning the insolvency of multinational groups of companies. In this respect, the article by Wessels, which provides an overview of proposals for reform that have been made in relation to the EIR, will be elaborated upon (Section 2.3).⁷ In his opinion, there is a large variety of possibilities in the way these multinational groups of companies are structured, which should be appreciated when considering new principles or rules to apply in the cross-border context.⁸ However, most of the suggestions provided give only one solution to the treatment of multinational enterprise groups in insolvency, irrespective of whether the group consisted of companies that acted autonomously or whether the group acted as one 'economic unit'. But new initiatives are developing. Most remarkable in this respect is the theoretical framework developed by Mevorach, who has published extensively in the area of multinational enterprise groups in insolvency and has actively participated in the UNCITRAL work in the area of insolvency. Mevorach suggests a comprehensive model for dealing with the insolvency of multinational enterprise groups, which can be used within the current cross-border insolvency frameworks, such as the EIR. According to the model, the approach to multinational enterprise groups adapts to the specific case at hand. This implies that under the appropriate circumstances, the group can be treated in the same way as a single legal entity in the course of cross-border insolvency. As a result, the insolvency proceedings against multinational enterprise groups can be administered centrally by a single court applying a single insolvency law (Section 2.4). This could be beneficial in terms of efficiency and costs, as illustrated by the KPNQwest case.

This article will analyze whether the adaptive model would be workable under the EIR (Section 3). The first question that needs to be addressed is how to identify the 'specific case at hand', since this would be determinative as to how to treat the insolvency of a group in a particular case (Section 3.1). The second issue that needs consideration is whether the concept of the centralization of insolvency proceedings against multinational enterprise groups would match the system of the EIR (Section 3.2). It is argued that a major drawback of the adaptive approach is that it might lead to legal uncertainty. In addition, the centralization of insolvency proceedings against multinational enterprise groups does not match the current system of the EIR. It is suggested here that the coordination of insolvency proceedings taking place against group companies from a 'leading forum' would constitute a suitable alternative to handling the

5 KPNQwest, first public report dated 13 June 2002, available at: <<http://www.houthoff.nl>> (last visited: 22 November, 2010).

6 R. Van Galen, 'The European Insolvency Regulation and Groups of Companies', 2004 *Tijdschrift voor Insolventierecht (Tvl)* 10, pp. 57 et seq.

7 B. Wessels, 'The Ongoing Struggle of Multinational Groups of Companies under the EC Insolvency Regulation', 2009 *European Company Law* 6, no. 4, pp. 169-176.

8 See Wessels, *supra* note 7, p. 172.

insolvency of integrated multinational enterprise groups. Section 4 will highlight the need for the standardization of domestic laws within the EU, as an integral approach to the insolvency of multinational enterprise groups is difficult to achieve without measures for consolidating their insolvencies. This area turns out to be problematic, because it touches upon the concept of ‘asset partitioning’. Finally, in Section 5 some conclusions will be drawn on how the European Union should act. A logical first step would be to amend the EIR, followed by the standardization of the law.

2. Renovation of the EIR

2.1. *The system of the EIR*

The aim of the EIR is to introduce an efficient and effective system concerning the mutual recognition of insolvency proceedings opened in individual Member States.⁹ The EIR is based on *modified universalism*. It permits the opening of the main insolvency proceedings in the Member State where the debtor’s ‘Centre Of Main Interests’ (COMI) is located and gives this process a universal scope.¹⁰ At the same time it allows local proceedings to take place in the Member State where the debtor has an establishment.¹¹ The uniform law applicable to the proceedings is that of the Member State within the territory of which such proceedings are commenced (the *lex concursus*),¹² but the EIR also provides for a set of exceptions to this rule.¹³ Notably, the EIR does not contain specific provisions to deal with the issue of groups of companies. For ascertaining jurisdiction, domestic courts should therefore identify the COMI of companies that operate under a group structure (‘group companies’) on a separate basis.

2.2. *Determining the COMI of group companies*

The EIR does not offer a clear definition of COMI, but Recital 13 retains the principle that was originally laid down in the Virgos/Schmit Report¹⁴ according to which the COMI corresponds to the place where the debtor conducts the administration of his interests and is therefore ascertainable by third parties. In case of a company or legal person, the place of the registered office shall be presumed to be its COMI (Article 3(1) EIR).

In the *Eurofood* case,¹⁵ the European Court of Justice (ECJ) provided guidance on the determination of the COMI of group companies. The ECJ ruled that the presumption of Article 3(1) EIR can only be rebutted ‘if factors that are both objective and ascertainable by third parties enable it to be established that an actual situation exists which is different from that which locating at that registered office is deemed to reflect.’¹⁶ Where a company carries on its business in the territory of the Member State where its registered office is situated, ‘the mere fact that its economic choices are or can be controlled by a parent company in another Member State is not enough to rebut the presumption laid down by that Regulation.’¹⁷

9 Recital 2 EIR.

10 Art. 3(1) EIR.

11 Art. 3(2) EIR.

12 Art. 4 EIR.

13 Arts. 5, 6, 7, 8, 9, 10, 11, 12, 14 and 15 EIR.

14 M. Virgós & E. Schmit, ‘Report on the Convention on Insolvency Proceedings’ was the principal report on the Convention on Insolvency Proceedings, which was converted into the EU Regulation. Although the Report does not have an official status, Commission officials today still refer to the Virgos-Schmidt Report for assistance with its interpretation. The Virgós/Schmit Report is published as Annex 2 in G. Moss et al., *The EC Regulation on Insolvency Proceedings: A Commentary and Annotated Guide*, 2009.

15 Case C-341/04, *Eurofood IFSC Ltd*, [2006] ECR I-3813 210.

16 *Re Eurofood*, Para. 33.

17 *Re Eurofood*, Para. 35.

Until the *Eurofood* judgment, the ‘head office functions approach’ was frequently followed by domestic courts, in particular by the English, German and French courts.¹⁸ The COMI of group companies was interpreted in such a way that it was located at the place where the head office functions were carried out. As a result, the insolvent multinational group could be subject to single main insolvency proceedings. Although this approach had the potential of efficient administration of the insolvency proceedings against multinational groups of companies, it was often criticized: domestic courts would attempt to administer multinational group failures by including in the same insolvency proceedings both the parent company and its subsidiaries, which qualifies as ‘jurisdictional competition’;¹⁹ the head office functions approach would be too subjective and inscrutable to third parties in that considerable emphasis is placed on where the management decisions of a group company are taken, which is not in conformity with the rationale laid down in Recital 13 EIR;²⁰ the head office functions approach would serve as an invitation to forum shopping and the head office functions approach would lead to conflicts of jurisdictions.²¹

The ECJ in *Eurofood* did not disqualify ‘parental control’ as a relevant factor in determining the COMI of group companies, but clarified that the presumption that the COMI is the registered office of the debtor can only be rebutted by factors which are both objective and ascertainable by third parties. The ECJ has thus put obstacles in the way of achieving unified solutions. But even after *Eurofood*, domestic courts have been able to identify mutual COMIs in a group context.²² However, in *Re Stanford International Bank Limited*²³ Mr. Justice Lewison explicitly stated: ‘I considered and applied the head office functions test in *Lennox Holdings* (...) I now consider that I was wrong to do so. Pre-*Eurofood* decisions by English courts should no longer be followed in this respect. I accept Mr Zacaroli’s submission that COMI must be identified by reference to factors that are both objective and ascertainable by third parties.’²⁴

2.3. Options for solutions

The *Eurofood* decision points at an important lacuna of the EIR, namely that it does not explicitly deal with the insolvency of multinational groups of companies. The EIR requires that every single legal person in any Member State must be considered as a separate entity, even when there are strong economic, financial or personal ties between the companies involved.²⁵ It seems that the EIR is largely based on *entity law* considerations, but the absence of provisions dealing with multinational groups of companies may also go back to the complexity of this issue. As Wessels states, cross-border insolvency within Europe was discussed over forty years before the enactment of the EIR. At the time the decision to postpone ‘group insolvencies’ to a later date may have been considered both politically and practically prudent.²⁶ In relation to the EIR, several suggestions have been made to solve problems related to the reorganization or insolvency of

18 See for example: *Re Daisytek-ISA Ltd* [2004] BPIR 30; *Re Collins & Aikman* [2005] EWHC 1754 (Ch); *Re MPOTEC GmbH* [2006] BCC 681 and *Re Hettlage* ZIP 2004, 962.

19 W.G. Ringe, ‘Forum Shopping under the EU Insolvency Regulation’, 2008 *European Business Organization Law Review (EBOLR)* 9, no. 4, pp. 579-620.

20 See Wessels, *supra* note 7, p. 171.

21 See Wessels, *supra* note 7, p. 176; M. Menjuca, ‘EC-Regulation No 1346/2000 on Insolvency Proceedings and Groups of Companies’, 2008 *European Company and Financial Law Review (ECFR)* 9, no. 2, p. 138.

22 See for example: *Re Eurotunnel Finance Ltd*, Tribunal de Commerce de Paris 2 August 2006 (unreported); *Re PIN Group AG*, ZIP 2008, 423 and District Court of Roermond 17 November 2008, JOR 2009, 55.

23 *Re Stanford International Bank Limited* [2009] EWHC 1441 (Ch).

24 *Re Stanford International Bank Limited*, Para. 61.

25 See Wessels, *supra* note 7, p. 169.

26 See Wessels, *supra* note 7, p.175.

multinational groups of companies. Wessels has made a comprehensive overview of these suggestions.²⁷ These include:

- To leave matters as they are. The treatment of multinational groups of companies is preferably left to national case law under the control of the ECJ in order to avoid excesses.²⁸
- To codify the head office functions approach under the EIR.²⁹ Paulus claims that such a solution should only apply to groups that operate as an ‘economic unit’. This will be elaborated upon in the next section.
- To relinquish the COMI standard in case of companies or legal persons and to allow the registered office to become the decisive criterion for determining jurisdiction.³⁰ Although this solution does not provide ways to deal with the special problems of the cross-border insolvency of multinational groups of companies, it would certainly provide coherence between the applicable insolvency law (the *lex concursus*) and the applicable company law, which is in most instances determined by the location of the registered office.³¹ As a consequence, the possibility of friction between those laws, which is possible under the current model of the EIR in case the location of the registered office of a company does not match the location of its COMI, is annulled.
- To regard a subsidiary as an establishment within the meaning of Article 2(h) EIR. This would imply that ‘secondary proceedings’ may be opened in the Member State where the subsidiary is located.³²
- To amend Article 4 EIR in such way that the recognition of the *lex concursus* also takes place if a court opens insolvency proceedings against different group companies.³³ Other elements of this proposal include the mandatory appointment of a national law expert and the possibility to use creditors’ language.
- To equip the parent’s liquidators with powers of coordination with respect to the subsidiary’s proceedings as well as the power to effect the coordinated sale of the assets of the companies in question.³⁴
- Cooperation between individual courts and countries administrating assets on a territorial basis, i.e. ‘cooperative territorialism’.³⁵

For the purpose of regulating the cross-border insolvency issues of multinational groups of companies, the choice is generally between either taking a worldwide perspective so that global solutions may be applied (*a universalist approach*), or to have proceedings against group members handled within each relevant territory (*a territorialist approach*). Solutions such as ‘cooperative territorialism’, ‘coordination’, or ‘secondary proceedings’ are rather weakened versions of one or the other. In effect the EIR currently endorses a territorialist approach to

27 See Wessels, *supra* note 7, pp. 172-174.

28 M. Menjucq & R. Damman, ‘Regulation no. 1346/2000 on Insolvency Proceedings: Facing the Companies Group Phenomenon’, 2008 *Business Law International* 6, no. 2, pp. 145-158.

29 G. Moss & C. Paulus, ‘The European Insolvency Regulation – The Case for Urgent Reform’, 2006 *Insolvency Intelligence* 19, no. 1, pp. 1-5.

30 H. Eidenmüller, ‘Free choice in international company insolvency law in Europe’, 2005 *EBOLR* 6, no. 3, p. 447.

31 L. Strikwerda, *Inleiding tot het Nederlandse Internationaal Privaatrecht*, 2008, p. 202.

32 M.E. Koppenol & X.E. Kramer, ‘Kroniek van het internationaal privaatrecht 1998-2002 (deel II)’, 2003 *Nederlands Tijdschrift Burgerlijk Recht*, no. 5, p. 267.

33 H. Hirte, ‘Towards a Framework for the Regulation of Corporate Groups Insolvencies’, 2008 *ECFR* 5, no. 2, pp. 213-236.

34 See Van Galen, *supra* note 6.

35 G. McGormack, ‘Jurisdictional Competition and Forum Shopping in Insolvency Proceedings’, 2009 *The Cambridge Law Journal* 68, no. 1, p. 169; L.M. Lopucki, ‘Global and Out of Control?’, 2005 *American Bankruptcy Law Journal* 79, no. 1, pp. 96-97.

multinational groups of companies, as the COMI needs to be determined on a separate entity basis.

2.4. Implications of the adaptive framework

Mevorach argues that the framework for dealing with multinational enterprise groups should rather adapt to the specific case at hand. According to her view, a universalist approach to multinational groups of companies should be possible when the group was integrated. In this case a universalist approach is generally more conducive to certain goals of insolvency, such as wealth maximization and the facilitation of rescues.³⁶ For example, in the KPNQwest case a coordinated sale of the assets of the group would have been highly beneficial in terms of wealth maximization, as they together comprised a data communication network.

Universalism suggests conducting insolvency proceedings against multinational groups in a unified matter from a single court applying a single insolvency law.³⁷ Indeed, the adaptive framework highlights the need to subject the debtor to one insolvency regime.³⁸ The possibility of an 'Enterprise Group COMI' is rejected by UNCITRAL Working Group V ('Working Group').³⁹ It was emphasized that one key issue with respect to a definition of an Enterprise Group COMI would be the extent to which that definition was accepted, widely adopted and voluntarily enforced by the courts of states affected by it. Furthermore, it was recalled that it would be difficult to avoid parallel proceedings being commenced in several states with each seeking to be the main proceedings and that determining the Enterprise Group COMI would not reduce the number of different laws that might be applicable.⁴⁰ At the European Union level these arguments are flawed to some extent, as the EIR is binding in its entirety and directly applicable in all Member States (except for Denmark). The EIR provides a system of automatic recognition of insolvency proceedings commenced in other Member States (Article 16 EIR) and provides as a main rule that the law which is applicable to the insolvency proceedings and their effects shall be the law of the Member State in which the insolvency proceedings are commenced (see Section 2.1).

According to Mevorach, the identification of the 'home country' of the group is only relevant for *integrated* multinational enterprise groups. In this case universalism matches the way the group actually operates and 'cross-entity insolvency solutions' are likely to be attainable.⁴¹

3. The adaptive framework revisited

3.1. The adaptive approach

The framework for dealing with multinational enterprise groups in insolvency that is contemplated by Mevorach adapts to the specific case at hand. In this way, the existence of a large variety of multinational groups of companies is certainly appreciated. However, crucial to an adaptive framework is the determination of the economic reality of the insolvent group. The relevant factors in this respect will be elaborated upon separately below. Thereafter, Section 3.2

36 I. Mevorach, 'The "Home country" of a Multinational Enterprise Group Facing Insolvency', 2008 *International Comparative Law Review* 57, no. 2, p. 431.

37 I.F. Fletcher, *Insolvency in Private International Law*, 2005, p. 15.

38 See Mevorach, *supra* note 2, p. 80.

39 This is a working group of UNCITRAL dealing with insolvency matters.

40 U.N. Comm'n on Int'l Trade Law (UNCITRAL), UNCITRAL Report of Working Group V (Insolvency Law) on the work of its thirty-fifth session, 2 December 2008, A/CN.9/666, Paras. 24-27, available at: <<http://www.uncitral.org>> (last visited: 22 November 2010) [hereinafter: A/CN.9/666].

41 See Mevorach, *supra* note 36, p. 432.

will question whether the centralization of the insolvency proceedings, as a possible outcome of the adaptive framework, is actually workable under the EIR.

3.1.1. *The level of integration*

The first question that arises is in what way the level of integration of a multinational group should be identified. This generally requires the use of economic theories of corporate integration. It follows that the determination of the level of integration will in each case depend on a certain interpretation of the facts.⁴² This might result in legal uncertainty. The ‘presumption approach’ is often used to mitigate this. German law provides that a majority holding leads to the *presumption* that dominant influence is exerted and that, in turn, leads to the presumption of uniform management.⁴³ This can also be seen in the *Akzo-Nobel* case,⁴⁴ where the ECJ held that a 100% shareholding of a parent company in a subsidiary created a rebuttable presumption that the parent company exercises a decisive influence over the commercial policy of its subsidiary.

Multinational groups operating via parents and subsidiaries are a major form of multinational organization. However, modern business organizations more often choose decentralized or horizontal patterns replacing the traditional hierarchical model as the primary leading form for multinational enterprise groups.⁴⁵ A trend towards more open ‘heterarchical’ business organizations, consisting of networks of cooperative and lateral relationships, has been observed.⁴⁶ It follows that in certain cases ‘majority holdings’ may not constitute a proper criterion for determining the level of integration in a multinational enterprise group. This is not really problematic, as long as other (contractual) linkages between group companies are recognized as well. The Working Group holds that different tests may apply in order to determine what constitutes the group, e.g. the ability to dominate the composition of the board of directors or the ability to control the majority of the votes at a meeting of the board. What is important is not so much the legal form of the relationship between the entities, but rather the substance of that relationship.⁴⁷ A flexible approach is to be preferred over setting a prescribed level of ownership, as in this way the diverse economic realities of enterprise groups are certainly appreciated.

3.1.2. *The home country*

The second issue is from which jurisdiction the insolvency proceedings should be conducted. This requires the identification of the ‘home country’ of the integrated multinational group. The Working Group noted that referring to one factor would result in a too narrow definition of an Enterprise Group COMI.⁴⁸ However, referring to a basket of factors which will be equally relevant for ascertaining the leading forum will not be beneficial in terms of legal certainty.⁴⁹

Mevorach suggests that the ‘operational headquarters test’ would be an appropriate tool in determining the home country of the group (the ‘group COMI’). The idea is that the group COMI lies where the operational headquarters of the group are located.⁵⁰ The main difference with the

42 P.T. Muchlinski, *Multinational Enterprises and the Law*, 2007, p. 320.

43 Sections 17 and 18 German Stock Corporation Act.

44 Case C-97/08P, *Akzo Nobel and Others v Commission*, [2009] ECR I-0000.

45 M. Eroglu, ‘Modern Organisation of Multinational Enterprises and Liability Discussions: Critical Analysis of Control Theory’, December 2008, available at: <<http://www.ssrn.com>> (last visited: 22 November 2010).

46 See Muchlinski, *supra* note 42, pp. 47-49.

47 See WP.92, *supra* note 3, Para. 29.

48 A/CN.9/666, *supra* note 40, Para. 29.

49 I. Mevorach, ‘Towards a Consensus on the Treatment of Multinational Enterprise Groups in Insolvency’, 2010 *Cardozo Journal of International and Comparative Law* 18, no. 1, pp. 359-423.

50 See Mevorach, *supra* note 36, p. 440.

head office functions test lies with the fact that the head office functions approach seeks to rebut the presumption of Article 3(1) EIR for the specific group companies, thereby qualifying as a ‘bottom-up approach’, whereas the operational headquarters test contemplates the identification of a single group COMI for the group *as a whole*, which requires the introduction of a group COMI under the EIR.⁵¹ The purpose of the headquarters test is to identify one common place for the multinational group, which represents a real connection to the whole group. For example, in the KPNQwest case, the home country of the group would have been the Netherlands, as this was the main place for administering the debtor’s affairs. It is true that this would ensure the possibility of efficiently handling the insolvency proceedings against an insolvent group, such as joint sales of assets. In addition, due to the fact that the operational headquarters test is based on the functional realities of the group, problems of forum shopping and inscrutability for third parties can arguably be reduced to some extent.⁵²

Mevorach asserts that the operational headquarters test is not an appropriate tool in cases where a single head office is an elusive notion.⁵³ She suggests that ‘ad hoc contractualism’ could assist in such situations, ‘encouraging the parties to agree on a venue between the options representing equal connections between the MEG [Multinational Enterprise Groups] and the jurisdiction.’⁵⁴ However, it is argued that the recognition of contract choices cannot be based on the ‘principle of mutual trust’. On the basis of this principle domestic courts within the EU should automatically recognize *judgments* concerning the commencement and conduct of insolvency proceedings delivered by the courts of other Member States (Recital 22 EIR). The principle of mutual trust is grounded on the concept of loyalty (Article 10 EC Treaty) inciting Member States and judges (but not the parties to a contract) to be guided by the aims and purposes of a given Community measure.⁵⁵ Furthermore, insolvency law generally overrides contract law, property law and other legal rights that would normally exist. Legal regimes will naturally prefer their own policy choices in this respect. To a certain extent this can be illustrated by the *Amiraike* case,⁵⁶ where a limited company under UK law was removed from the register at Companies House for failure to comply with publicity obligations, resulting in the forfeiture of its assets, including real estate situated in Germany, to the Crown. A German court raised the question before the ECJ whether it should recognize an expropriatory measure ordered by the legal system of another Member State on the basis of Articles 10, 43 and 48 EC. Germany claimed that the decision to be taken by the court did not contain the elements of a judgment. For this reason the ECJ eventually found that it had no jurisdiction to rule on the matter. It is to be expected that Member States will often refuse to recognize contractual choices regarding the applicable insolvency regime on the basis that this is contrary to their ‘domestic public policies’ (Article 26 EIR).⁵⁷

3.1.3. The level of centralization

The third question that arises is what role the leading forum should have in the insolvency proceedings. It was noted that the ultimate aim of universalism is the centralization of proceedings, i.e. the administration of multinational insolvencies by a single court which preferably

51 J.E. Antunes, *Liability of Corporate Groups: autonomy and control in parent-subsidiary relationships in the US, German and EEC law: an international and comparative perspective*, 1994, p. 211.

52 See Mevorach, *supra* note 36, p. 442.

53 See Mevorach, *supra* note 2, pp. 203-204.

54 See Mevorach, *supra* note 2, p. 204.

55 B. Wessels, *International Insolvency Law*, 2006, p. 301.

56 Case C-497/08, *Amiraike Berlin GMBH*, OJ C 63, 13.1.2010, p. 19.

57 F. Tung, ‘Is International Bankruptcy Possible?’, 2001-2002 *Michigan Journal of International Law* 23, no.1, p. 45.

applies its own insolvency law. However, centralization may result in serious interferences with domestic policies, as legally there is much divergence amongst the insolvency laws of the Member States.

Mevorach claims that if centralization is only applied where the integrated group was centrally controlled, territorialism is not necessarily interfered with. The centralization of the insolvency proceedings would fit with the degree of control exerted by host countries over local companies and will therefore not undermine state sovereignty or domestic policies. For the more decentralized integrated group she suggests a weaker universalist solution, that is local proceedings for the affiliates, coordinated by the principle group process. As a result, the role of the leading forum (centralization or coordination) would be matched with the economic reality of the group and would thus also be predictable for third parties.⁵⁸

Mevorach's approach may constitute an excellent solution in order to maintain a balance between universalism and territorialism if the level of centralization of the relevant multinational group in default is determined in a proper way. Mevorach points to a variety of factors that can be taken into account; the size of the group, the type of product it manufactures, the targeted market and how subsidiaries are owned.⁵⁹ Nevertheless, it is argued that legal certainty might be at stake. The level of centralization of the multinational group is to be determined by domestic courts that may not be sufficiently equipped to adjudicate on this matter and debtors may be tempted to manipulate the factual circumstances of the case.

3.1.4. Interim conclusion

Mevorach's work must be regarded as a great source of inspiration to the development of a comprehensive framework for dealing with the insolvency of multinational enterprise groups. However, inherent in an adaptive framework is that it in each case is dependent on the determination of the economic reality of the multinational enterprise group in insolvency by domestic courts. It follows that the 'principle of mutual trust' is heavily relied upon. In addition, legal certainty might be at stake in certain cases, e.g. when the degree of integration or centralization is difficult to determine or in cases in which it is not clear where the operational headquarters lies. However, it must be noted that all this might be mitigated to some extent when clear rules on determining various linking tools are developed.⁶⁰

3.2. The concept of centralization under the EIR

A possible outcome of the adaptive framework might be that the proceedings against multinational enterprise groups should be conducted centrally from one court. In certain cases this can facilitate a harmonious process against multinational groups of companies. There will be a global perspective on the group as a whole, which will entail considering the position of connected affiliates and their stakeholders rather than solely focusing on the interests of local creditors.⁶¹

However, this approach is rejected by the Working Group. Instead, it focuses on facilitating coordination and cooperation between courts and representatives handling insolvency proceedings against different group entities.⁶² The Working Group provides enhanced measures for

58 See Mevorach, *supra* note 2, pp. 175-194.

59 See Mevorach, *supra* note 2, p. 133.

60 See Mevorach, *supra* note 2, p. 285.

61 See Mevorach, *supra* note 49.

62 U.N. Comm'n on Int'l Trade Law (UNCITRAL), UNCITRAL Note by the Secretariat, Working Group V (Insolvency Law), 10 February 2010, A/CN.9/WG.V/WP.92/Add.1, Paras. 7-54, available at: <<http://www.uncitral.org>> (last visited: 22 November 2010) [hereinafter: WP.92/Add.1].

cooperation, such as joint hearings, the appointment of a single court representative and a single insolvency representative and direct communications between courts and insolvency representatives. In this case the court representative will rather act as a ‘go-between’ for the courts and the insolvency representatives involved rather than having any additional powers by virtue of being the coordination centre.⁶³ The solution of the Working Group can be regarded as a very weakened version of universalism or rather a strong version of cooperative territorialism (see Section 2.3, last solution).

I agree with Mevorach that greater universalist solutions allow a more harmonious insolvency process, thereby saving *ex post* costs and maximizing the asset value. Greater universalist solutions are particularly beneficial with regard to global rescue attempts, as this involves complex decision-making and the need to take urgent measures. Doing that within a system of ‘equal parties’ with no directing centre can be problematic, especially if the multinational group is big and widespread.⁶⁴

Nevertheless, it is argued that the concept of the centralization of insolvency proceedings against multinational groups of companies is not workable under the EIR. First, according to Article 4 EIR, the law applicable to the insolvency proceedings and their effects is the law of the Member State in which the proceedings are opened (*the lex fori concursus*). As a result, the centralization of the proceedings will result in a ‘mismatch’ between the applicable insolvency law and local law in various related areas, such as corporate law, security law, tax law and employment law.⁶⁵ Second, the opening of secondary proceedings against establishments of the group companies, as this will generally undermine the centralization of insolvency proceedings against multinational groups of companies.⁶⁶ The applicability of one of the exceptions to the main rule that the *lex concursus* shall be the uniform law applicable to the insolvency proceedings will have the same result.⁶⁷ For example, the opening of insolvency proceedings against a multinational group company in one Member State will not affect security rights on assets of group companies located in other Member States.⁶⁸ Finally, as the EIR provides that the realization of foreign assets must take place according to the procedures under local law, a centralized approach may be hard to achieve.⁶⁹

It follows that the centralization of insolvency proceedings against multinational enterprise groups is not workable under the system of the EIR. It is argued that the coordination of the multiple insolvency proceedings taking place against various group companies conducted from the place of the home country of the group would be a good alternative to handling the insolvency of integrated multinational groups of companies under the EIR.⁷⁰ This will generally require the determination of the level of integration in a specific case (Section 3.1.1). As argued above, it is necessary to adopt a flexible approach in this respect. In addition, in certain cases it will be necessary to identify the home country of the integrated multinational group. For this purpose I generally support the headquarters test as proposed by Mevorach (Section 3.1.2). It was established that this test is not an appropriate tool where a single head office is an elusive notion. In my view this is only relevant where the centralization of the insolvency proceedings is sought.

63 WP.92/Add.1, *supra* note 62, Para. 37.

64 See Mevorach, *supra* note 49.

65 N.W.A. Tollenaar, ‘Dealing with the Insolvency of Multinational Groups under the European Insolvency Regulation’ 2010, *TvI* 14, pp. 94-103.

66 Art. 3(2) EIR.

67 Arts. 5, 6, 7, 8, 9, 10, 11, 12, 14 and 15 EIR, see Wessels, *supra* note 55, pp. 360 et seq.

68 Art. 5 EIR.

69 Art.18(3) EIR.

70 Such an approach is also supported by Van Galen. See Van Galen, *supra* note 6.

Coordination of the proceedings is still possible when there is more than one operational head office. In this case the leading centres should cooperate in coordinating the insolvency proceedings against the multinational group. This would generally match the economic reality of the multinational group and also correspond to the expectations of third parties.

4. Standardization of insolvency laws within the European Union

4.1. Procedural and substantive consolidation

Universalist solutions for handling the insolvency of multinational groups of companies will generally rely on mechanisms for consolidating the insolvency of related companies. In general, legal regimes tend to adhere to traditional concepts of limited liability and asset partitioning. Consequently, applying mechanisms for consolidating the insolvency of a group might be problematic. Although it has also been observed that insolvency law is an area of the law where 'entity law' is in the process of erosion.⁷¹

Two main types of mechanisms for consolidating insolvency proceedings may be recognized: procedural consolidation and substantive consolidation. Procedural consolidation is a matter of unifying insolvency proceedings against separate entities of the group. This involves varying degrees of coordination with respect to the administration of multiple insolvency proceedings commenced against group companies involving one or more courts, e.g. the combining of hearings and meetings; the preparation of a single list of creditors and other interested parties; the establishment of joint deadlines et cetera.⁷² Notably, the mechanism of procedural consolidation does not pose any problems to entity law, as long as the assets and debts remain attached to the specific entity.

Substantive consolidation, on the other hand, significantly interferes with the group's legal structure. It constitutes a measure for merging the assets and debts of the group.⁷³ It is only recognized in a few jurisdictions. Within the European Union, substantive consolidation is applied in France, Ireland and the Netherlands. Irish legislation specifically provides for such provisions in the Companies Act 1990 and whilst already recognized for a long time by the French courts, the possibility of substantive consolidation is now also codified by the French legislators in the *Code de Commerce*.⁷⁴ In the Netherlands, the admissibility of substantive consolidation is based on a ruling by the Dutch Supreme Court (*Hoge Raad*).⁷⁵ According to the Dutch draft insolvency bill (*Voorontwerp Insolventiewet*), the possibility of substantive consolidation will also be codified in the Dutch legislation.⁷⁶

A principal concern against the measure of substantive consolidation is that it overturns the principle of the 'separate legal identity' of each group member. Typically, the Working Group takes the view that the intermingling of assets and liabilities of enterprise groups in the course of insolvency should only be applied under very limited circumstances, which are to be regarded as exceptions to the main rule, which is that of corporate separateness.⁷⁷ Is the European Union ready to take an enterprise law approach in this respect? Within the European Union, the group

71 P.I. Blumberg et al. (eds.), *Blumberg on Corporate Groups*, Vol. I, 2005, s. 3.02.

72 See WP.92, supra note 3, Para. 23.

73 See Mevorach, supra note 2, pp. 159-165 and pp. 224-227.

74 See Art. 141 in conjunction with Art. 140 Companies Act 1990 (Ireland) and Article L621-2(2) *Code de Commerce* (France).

75 Hoge Raad 25 September 1987, NJ 1988, 136 (*Van Kempen/Zilfa en DWC*).

76 The Dutch draft insolvency bill is published in: S.C.J.J. Kortmann and N.E.D. Faber, *Geschiedenis van de Faillissementswet: Voorontwerp Insolventiewet*, 2007, pp. 3-128.

77 See WP.92, supra note 3, draft recommendations 219-220.

is already recognized for ‘specific purposes’, e.g. for disclosure purposes. For example, the Seventh Directive on Consolidated Accounts⁷⁸ requires an undertaking to draw up consolidated accounts and a consolidated report when there is a legal power to control another undertaking and according to Council Directive 90/435/EEC on the common system of taxation of parent companies and subsidiaries of different Member States, withholding tax is abolished on profit distributions by a company belonging to one Member State to its parent in another Member State.⁷⁹ But in these cases the notion of asset partitioning is not really interfered with. The segregation of assets and debts allows the creditors of each affiliate to confine their monitoring efforts to one group entity, because they are assured that they will not need to compete with the creditors of other group entities. It follows that the case for caution in the application of substantive consolidation is hence well grounded.⁸⁰

I agree with Mevorach that substantive consolidation should primarily take place in ‘asset’ integrated groups, i.e. where it appears that there was no partitioning de facto, as a matter of economic reality. Where the assets and debts cannot be reasonably ascertained, it should be possible to pool them together.⁸¹ In addition, substantive consolidation should also be permitted when fraudulent transactions involved the forming of separate entities into which, for example, assets were shifted so as to hide them from creditors. Yet, other remedies than substantive consolidation may be more adequate to nullify fraudulent transactions as they can be directed to particular group companies and the separate legal identity is respected.⁸² These grounds for substantive consolidation are generally in accordance with the existing models for substantive consolidation.⁸³ The Dutch draft insolvency bill provides that substantive consolidation should also be allowed where the distribution of the profits to the creditors of the separate affiliates would otherwise lead to ‘unjust and unreasonable outcomes’. Although it is indicated in the notes to the draft insolvency bill that this ground should be interpreted restrictively, it does allow a weighing of interests, a practice that is commonly accepted in the United States.⁸⁴ The principal concern here is the potential unfairness caused to one creditor group when forced to share the profits with creditors of a less solvent group member. Individual creditors may have relied on the separate assets or separate legal identity of the group.⁸⁵

4.2. Further improvements

Universalist solutions generally rely on standardized mechanisms for consolidation. For example, the establishment of a ‘leading forum’ for the purpose of centralizing the insolvency proceedings only makes sense if it is possible to file a joint application for the commencement of insolvency proceedings against several group members. It follows that the law should specify that the administration of insolvency proceedings may be centralized or coordinated for procedural purposes and should also facilitate the means for coordinating the insolvency proceedings. But the work does not stop here. It has already been mentioned that procedural consolidation will generally facilitate global group-wide solutions to groups of companies in insolvency, such as reorganizations or joint sales of assets, an option that was unfortunately not available in the

78 83/349/EEC, OJ L 193, 18.7.1983, pp. 1-17.

79 M. Andenas & F. Wooldridge, *European comparative company law*, 2009, p. 451.

80 See Mevorach, *supra* note 2, p. 225.

81 See Mevorach, *supra* note 2, p. 225.

82 See Mevorach, *supra* note 2, pp. 311-313.

83 M.L.H. Reumers, *Samengevoegde afwikkeling van faillissementen*, 2007, pp. 73-94.

84 *Re Orfa* 129 B.R. 404, 414 (Bankr. E.D. Pa. 1991).

85 See WP.92, *supra* note 3, Para. 109.

KPNQwest case. It follows that in relation to the insolvency of multinational groups of companies a further improvement would be standardized rules for group-wide solutions to (multinational) groups in insolvency. It goes beyond the scope of this article to discuss all options, but a general question is whether it should be possible to sacrifice particular group entities for the sake of benefiting the group as a whole. For example, is it possible to reject a lucrative offer for the sale of the assets of a group entity for the sake of a ‘package sale’ which will benefit the group as a whole? Or should it be possible to subject a group entity to a reorganization plan without its dissent? Whatever the answer may be, in such cases the rights of dissenting creditors must certainly be safeguarded.⁸⁶ Otherwise, the notion of asset partitioning will be unduly interfered with.

5. Conclusion

It is now time to answer the question of how the European Union should respond to the issue of multinational groups of companies in insolvency. It is argued that a logical first step would be to amend the EIR in such a way that it also deals with multinational groups of companies (Section 2). This article has elaborated on the adaptive framework proposed by Mevorach (Section 3). This framework certainly appreciates the large variety of multinational enterprise groups, but an inherent issue is the interdependence on the determination of the level of integration (Section 3.1.1), the location of the home country (Section 3.1.2) and the level of centralization (Section 3.1.3). Furthermore, it has been observed that the centralization of insolvency proceedings, as a possible outcome of the adaptive framework, is not workable under the system of the EIR (Section 3.2). Most importantly, centralization will result in a mismatch between the insolvency law which is applicable to group companies and the law which is applicable in many related areas of the law. In this article it is suggested that the coordination of the multiple insolvency proceedings against integrated multinational enterprise groups would be a good alternative to handling their insolvencies under the EIR.

The second step in the process of regulating multinational groups in insolvency would be the standardization of laws on the treatment of groups of companies in insolvency (Section 4). Universalist solutions will generally rely on unified mechanisms for procedural consolidation. It has been observed that procedural consolidation is an appropriate measure as asset partitioning is not interfered with (Section 4.1). This will generally facilitate group-wide solutions, such as reorganizations or coordinated sales of assets. Substantive consolidation should only be allowed in case the group entities are intertwined to such an extent that it is impossible to determine which assets belong to which entity of the group or where enterprise group members are engaged in a fraudulent scheme or activity and substantive consolidation is essential to rectify that scheme or activity. A further improvement would be standardized rules on group-wide solutions for (multinational) groups in insolvency (Section 4.2).

My final conclusion is that in the context of insolvency the European Union would in the first place benefit from special rules regarding the insolvency of multinational groups of companies under the EIR. The next step would be to make sure that an integral approach to multinational groups of companies is indeed possible through the standardization of insolvency laws.

⁸⁶ See Mevorach, *supra* note 2, p. 165.