

23 April 1999

A4-0234/99

# **REPORT**

on the Convention on Insolvency Proceedings of 23 November 1995

Committee on Legal Affairs and Citizens' Rights

Rapporteur: Kurt Malangré

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At the request of the Conference of Presidents the President of the European Parliament announced at the sitting of 19 September 1997 that the Committee on Legal Affairs and Citizens' Rights had been authorised to draw up a report on the Convention on Insolvency Proceedings of 23 November 1995.

At its meeting of 8 July 1997, the Committee on Legal Affairs and Citizens' Rights had appointed Mr Malangré rapporteur.

It considered the draft report at its meetings of 29 March 1999 and 22 April 1999.

At the latter meeting it adopted the motion for a resolution by 10 votes to 0 with 1 abstention.

The following took part in the vote: De Clercq, chairman; Malangré, vice-chairman and rapporteur; Añoveros Trias de Bes (for Casini C.), Barzanti, Berger, Cassidy, Gebhardt, Medina Ortega, Ullmann, Verde I Aldea and Wijnsbeek (for Thors).

The report was tabled on 23 April 1999.

The deadline for tabling amendments will be indicated in the draft agenda for the relevant part-session.

**A**  
**MOTION FOR A RESOLUTION**

**Resolution on the Convention on Insolvency Proceedings**

The European Parliament,

- having regard to the Convention on Insolvency Proceedings of 23 November 1995<sup>(1)</sup>,
  - having regard to the findings of the hearing held by the Committee on Legal Affairs and Citizens' Rights on 15 April 1998,
  - having regard to Rule 148 of its Rules of Procedure,
  - having regard to the repeated requests by the European Parliament that the Commission submit a proposal for a directive on bankruptcies involving companies which operate in several Member States<sup>(2)</sup>,
  - having regard to the report of the Committee on Legal Affairs and Citizens' Rights (A4-0234/99),
- A. whereas the deadline for the signing of the Convention on Insolvency Proceedings has passed with one Member State not having signed; whereas the Convention cannot therefore enter into force unless it is amended by unanimous accord,
- B. whereas this stalemate has been caused by the fact that one Member State has refused to sign the Convention, despite having accepted it,
- C. whereas all the Member States agree that the absence of rules on insolvency proceedings in the Community is a deficiency with respect to the completion of the internal market,
- D. whereas bankruptcies, compositions and similar proceedings were excluded from the scope of the Convention on jurisdiction and the enforcement of judgments in civil and commercial matters signed in Brussels on 27 September 1968<sup>(3)</sup>,
- E. whereas a committee of experts in the Commission of the European Communities drew up a first draft Convention from 1963 to 1980 and - after the enlargement of the Community beginning in 1973 - a second draft Convention, which provided for a single procedure to be recognised in the other Contracting States and precluded the simultaneous opening of domestic proceedings in these other States (principles of 'unity' and 'universality'),

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<sup>(1)</sup> Council Document CONV/INSOL/X1, reproduced in OJ L

<sup>(2)</sup> Resolution of 16 December 1998 on the Commission's work programme for the year 1999.

<sup>(3)</sup> In the version modified after the accession of new Member States in 1978, 1982 and 1989, OJ C 189, 28.7.1990 ('Brussels Convention')

- F. whereas the Council suspended its deliberations of these drafts in 1985 in the absence of sufficient agreement,
- G. whereas the European Convention on certain international aspects of bankruptcy negotiated within the Council of Europe and deposited for signature on 5 June 1990 in Istanbul has not entered into force, since not enough States have ratified it,
- H. whereas a set of rules to be established in the Community on the model of the Insolvency Convention should as far as possible provide for simple and flexible solutions and be based on the principle of the universality of proceedings, which principle is, however, restricted by the possibility of secondary insolvency proceedings being opened in one or more instances, although their effects remain confined to the territory of the Member State concerned,
- I. whereas Article 65 (ex Article 73m) of the Treaty of Amsterdam provides for the elimination of 'obstacles to the good functioning of civil proceedings, if necessary by promoting the compatibility of the rules on civil procedure applicable in the Member States' in the field of judicial cooperation in civil matters having cross-border implications; whereas, pursuant to Article 67 (ex Article 73o) of this Treaty, the Council, acting unanimously, may enact legislation on a proposal from the Commission or on the initiative of a Member State and after consulting the European Parliament and these new provisions cover the subject matter governed by the Insolvency Convention,
- J. whereas this opportunity should be seized, if possible, before the end of the current Council Presidency,
1. Calls on the Commission to draft, with the assistance of the Member States, a 'regulation or directive on cross-border insolvency proceedings' pursuant to Articles 65 (ex Article 73m) and 67 (ex Article 73o) of the Treaty of Amsterdam without delay on the basis of the Convention on Insolvency Proceedings of 23 November 1995 and to forward it to the Council for its consideration and to Parliament for its opinion as soon as the Treaty of Amsterdam enters into force;
  2. Instructs its President to forward this resolution to the Commission, the Council and the governments of the Member States.

**B**  
**EXPLANATORY STATEMENT**

**1. The failure of the Insolvency Convention**

The Convention, which is based on ex Article 220 of the EC Treaty, was signed by all the Member States, with the exception of the United Kingdom, within the period for signature prescribed in its Article 49 (this expired on 23 May 1996). The United Kingdom has given no official reason for its stance.

Neither the Austrian nor the German Council Presidency has included the Convention in its work programme. The Commission has no current plans to take action in any way.

It therefore has to be said that, where this matter is concerned, the Community is once again exactly where it was 20 years ago.

It is difficult to determine the precise reasons for the British stance. While it was based initially on the dispute with its partners over the consequences of the BSE scandal, the unofficial reason given now is the Gibraltar question. The relevant provision is Article 229 (ex Article 227(4) of the EC Treaty), according to which the EC Treaty, and hence all law based thereon or derived therefrom, applies to the European territories for whose external relations a Member State is responsible. This provision actually leads to the conclusion that the Convention in question would also apply to Gibraltar, for whose interests the United Kingdom has been responsible since the Treaty of Utrecht in 1713.

It should be pointed out that in the only case concerning Gibraltar brought before the ECJ to date the argument that EC law does not apply to Gibraltar was evidently not put forward by any party, including Spain<sup>(4)</sup>.

Final clarification of the legal situation by the Court of Justice is likely to be forthcoming in the near future. On 18 January 1999 the Commission forwarded four substantiated opinions to the United Kingdom, accusing it of not having applied the directives on consolidated accounts in Gibraltar<sup>(5)</sup>. If the United Kingdom does not provide a satisfactory answer within two months, the Commission may institute proceedings for contravention of the Treaty.

At the time of British accession to the Community in 1972 all the parties to the Treaty were in agreement that Community law should apply to Gibraltar; otherwise, the following special provision would not have been included in the Act of Accession:

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<sup>(4)</sup> Judgment in Case C-298/89, *Government of Gibraltar v Council of the European Communities*, [1993] ECR I-3605. The action was brought against an article in a Directive on air services, in which Gibraltar was excluded from the Directive. It was rejected as inadmissible because the criteria of Article 173(2) of the EC Treaty regarding a 'decision' were not met.

<sup>(5)</sup> These are Directives 78/660/EEC and 83/349/EEC, amended by Directives 90/604/EEC and 90/605/EEC.

'Acts of the institutions of the Community relating to the products in Annex II to the EEC Treaty and the products subject, on importation into the Community, to specific rules as a result of the implementation of the common agricultural policy, as well as the acts on the harmonization of legislation of Member States concerning turnover taxes, shall not apply to Gibraltar unless the Council, acting unanimously on a proposal from the Commission, provides otherwise.'<sup>(6)</sup>

This provision forms part of the *acquis communautaire*, which Spain accepted on accession.

The United Kingdom might, however, take exception to an 'explanatory report', which was commissioned by the Council from Mr Virgos (Madrid) and Mr Schmit (Luxembourg) and was submitted by them on 8 July 1996. The observations by Virgos on the Convention's territorial applicability (paragraphs 300 - 302) are to the effect, inter alia, that it cannot apply to territories whose external relations are assumed by one of the Contracting States 'but which are not an integral part of their territory, being a separate entity.'

Spain might regard Gibraltar as being such a 'separate entity', since in 1964 Gibraltar received a new constitution which gives its people the right to manage their home affairs themselves to a large extent.

The view put forward by Virgos that Article 229 (ex Article 227(4) of the EC Treaty) applies only to territories which belong to the sovereign territory of the Member State responsible for their external relations is not convincing<sup>(7)</sup>. Even if the German version, which uses the words '*Europäische Hoheitsgebiete*', could be interpreted in this way, the French version refers only to '*territoire européen*' and the English version to 'European territories'. If the territories in question had to belong to the 'sovereign territory' of the relevant Member State, the provision in Article 229 (ex Article 227(4) of the EC Treaty) would, moreover, be superfluous, because according to Article 29 of the 1969 Vienna Convention on the Law of Treaties, which is quoted by Virgos, international treaties apply in any case to a State's sovereign territory in its entirety, save as otherwise agreed.

At most, there might be doubts as to whether agreements within the meaning of ex Article 220 of the EC Treaty fall within the scope of the term 'Treaty' within the meaning of Article 229 (ex Article 227(4) of the EC Treaty) and thus apply to Gibraltar, save as otherwise agreed.

In this connection, the following should be noted:

Ex Article 220 of the EC Treaty has a dual function. First, in order to achieve the internal market objectives specified therein, ex Article 220 maintains the power of the Member States, parallel to the Community's negotiating powers, to conclude among themselves multilateral treaties. It thus follows from the existence of this provision that within its field of application the powers of the Community institutions compete with a parallel power held by the Member States regarding international treaties. The second function of ex Article 220 is to mobilise this power to conclude

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<sup>(6)</sup> Article 28 of the Act concerning the Conditions of Accession and the Adjustments to the Treaties of 22 January 1972, OJ L 73, 27.3.1972, p. 14

<sup>(7)</sup> See also von der Groeben, Thiesing and Ehlermann: Commentary on the Treaty on European Union/EC Treaty, 5th edition, point 28 on Article 227 of the EC Treaty.

treaties by establishing an obligation under Community law to conduct negotiations<sup>(8)</sup>. The majority opinion is that agreements concluded pursuant to ex Article 220 of the EC Treaty are neither primary nor secondary Community law, but agreed international law which implements primary Community law, namely ex Article 220. Since the agreements implement precepts of the EC Treaty (ex Article 220) and turn the objectives set by the EC Treaty into reality, they do not supplement the EC Treaty but, as international treaty law common to all the Member States, supplement the secondary Community law enacted on the basis of the EC Treaty<sup>(9)</sup>. The case law of the European Court of Justice is that agreements concluded pursuant to ex Article 220, on account of their purpose and function in implementing the Treaty, 'are linked to the EEC Treaty'<sup>(10)</sup>. They may therefore be regarded, at least functionally, as belonging to the 'Treaty' within the meaning of Article 229 (ex Article 227(4)).

As the Insolvency Convention will not be revived or ratified, these considerations are, however, more of a theoretical nature.

The main problem is the blocking of the Convention, to which 14 Member States have, after all, declared their agreement by signing it.

The problem could be solved by reducing the number of parties to the scheme, for instance by abandoning the Community context and switching to a normal international treaty. This would have the advantage of enabling other countries, e.g. Switzerland, to join, but there would then no longer be binding interpretation of the Convention by the European Court of Justice (Articles 43-46 of the Convention).

Another possibility would be to get round the requirement of unanimity by opting for a directive or a regulation under Article 47 (ex Article 57(2)), 55 (ex Article 66), 95 (ex Article 100a) or 308 (ex Article 235) of the EC Treaty, rather than a treaty pursuant to ex Article 220 of the EC Treaty. In that case the question of whether those legal forms can cover the subject-matter governed by the Convention would have to be carefully checked. A possible counter-argument to this is that the Insolvency Convention is intended to supplement the 1968 European Convention on jurisdiction and the enforcement of judgments in civil and commercial matters, which was likewise based on ex Article 220 of the EC Treaty, and that supplementary legal acts must be enacted on the same basis. A further point is that, following the entry into force of the Treaty of Amsterdam, a provision will exist, in the form of the new Article 65, which might be seen as 'lex specialis'.

Another possibility would be to press for ratification of the Istanbul Bankruptcy Convention of 5 June 1990 concluded between the Member States of the Council of Europe, which has so far been ratified only by Cyprus and has therefore not entered into force.

The final possibility would be not to seek any solution binding in international or Community law, but simply to attempt to harmonise insolvency legislation on the basis of the UNCITRAL model law.

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<sup>(8)</sup> Von der Groeben, Thiesing, Ehlermann, op. cit., points 43 and 44 on Article 220 of the EC Treaty

<sup>(9)</sup> Von der Groeben, Thiesing, Ehlermann, op. cit., point 12

<sup>(10)</sup> Judgment in Case C-398/92, *Mund & Fester v Hatrex Internationaal Transport*, [1994] ECR I-467, paragraph 12.



The unavoidable impression, however, is that at present neither the Commission nor the Council is interested in making progress in this matter.

Your rapporteur, however, echoing what emerged from the hearing held by the committee, considers there to be an urgent need for rules on insolvency in view of the single market and its single currency.

## **2. The situation after the entry into force of the Treaty of Amsterdam**

In order to establish progressively an area of freedom, security and justice' Article 61 (ex Article 73i) of the EC Treaty provides, among other things, for the Council to adopt 'measures in the field of judicial cooperation in civil matters' insofar as necessary for the proper functioning of the internal market. According to Article 65, such measures include 'improving and simplifying ... the recognition and enforcement of decisions in civil and commercial cases, including decisions in extrajudicial cases' and 'eliminating obstacles to the good functioning of civil proceedings, if necessary by promoting the compatibility of the rules on civil procedure applicable in the Member States'. In adopting such measures the Council is required, during a transitional period of five years following the entry into force of the Treaty of Amsterdam, to act unanimously on a proposal from the Commission or on the initiative of a Member State and after consulting the European Parliament. After this period of five years the Council acts solely on proposals from the Commission (Article 67( ex Article 73o)).

As the Treaty does not define the legal nature of the measures to be adopted by the Council in any greater detail, it must be assumed that any of the binding acts available under Article 249 (ex Article 189 of the EC Treaty), viz. regulations, directives and decisions, may be adopted.

National provisions on insolvency proceedings are also likely to be in the nature of the 'rules on civil procedure' whose compatibility is to be promoted pursuant to Article 65 of the EC Treaty (ex Article 73m) with a view to 'eliminating obstacles to the good functioning of civil proceedings', which also include insolvency proceedings. Furthermore, all judicial decisions to be taken in the context of insolvency proceedings are of the type whose recognition and enforcement are similarly to be improved and simplified pursuant to Article 65 of the EC Treaty (ex Article 73m).

This gives rise to some competition with ex Article 220 of the EC Treaty, which requires the Member States to 'enter into negotiations with each other with a view to securing for the benefit of their nationals ... the simplification of formalities governing the reciprocal recognition and enforcement of judgments of courts or tribunals and of arbitration awards'. Ex Article 220 of the EC Treaty is not repealed by the Treaty of Amsterdam. The relationship between the two provisions must therefore be assumed to be one of open competition. The Council's legal service assumes that the Member States may continue ratification procedures in the case of conventions which are based on ex Article 220 of the EC Treaty and which are in the process of being ratified. However, they would be required to interrupt these procedures as soon as the Commission or a Member State submitted a proposal for the adoption of a Community act. This requirement is said to arise from the principle of Community-friendly conduct as set out in Article 10 (ex Article 5) of the EC Treaty.

As in the present case no Member State has yet initiated the ratification of the Insolvency Convention, this question does not arise.

It should therefore be borne in mind that a proposal which largely corresponds to the Insolvency Convention in content might be based on Articles 65 (ex Article 73m) and 67 (ex Article 73o) of the EC Treaty. The legal form to be recommended is a regulation, since it applies as it stands and does not need to be transposed. This does not, of course, rule out the need for supplementary national legislation governing procedural details in particular.

### **3. The contents of a regulation on cross-border insolvency proceedings**

The debate on cross-border insolvency proceedings has always been dominated by two incompatible principles, the principle of the universality of insolvency on the one hand and the principle of the territoriality of insolvency on the other, although in practice neither of these principles is applied in its pure form<sup>(1)</sup>.

Under the 'universality principle' insolvency proceedings relating to the assets of a debtor are to be opened in only one country, normally the country in which he has his domicile, his registered office or his headquarters. The proceedings opened in this country are then to cover all the debtor's assets, whether they are situated in the country of insolvency or elsewhere.

All creditors, regardless of their domicile, their nationality or the geographical origin of their claims, are to participate in a single round of comprehensive proceedings and to lodge their claims at these proceedings. Other countries are required to refuse to permit parallel insolvency proceedings to be opened.

The 'principle of the territoriality' of insolvency is precisely the opposite of the universality principle that has just been described. It essentially says that the effects of the opening of insolvency proceedings are limited to the assets situated in the country in which the proceedings are opened. Consequently, the aim must be to open separate insolvency proceedings in all countries in which other of the debtor's assets are situated. If assets are situated in a country in which insolvency proceedings are not opened, the debtor remains free to dispose of them as he will.

If it is assumed that the main purpose of insolvency proceedings is to attain and maintain equality among a debtor's various creditors, the territoriality principle is clearly unsatisfactory. Equality of the treatment of creditors can hardly be achieved if the effects of opening proceedings are restricted to property in a single country, and one and the same debtor is exposed to parallel and separate insolvency proceedings in a number of countries opened and completed in accordance with different legal systems. Such parallel proceedings force creditors to lodge their claims in each individual country, which may pose practical difficulties and be extremely costly.

In these circumstances the natural course of action might appear to be unrestricted endorsement of the principle of the universality of insolvency. In fact, it is less straightforward than it appears, since the application of the universality principle in its pure form would pose a number of other problems that are no less serious than the disadvantages of the territoriality principle referred to above. The application of the universality principle would mean, inter alia, only one round of proceedings being

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<sup>(1)</sup> The following comments are based on the statements made especially by Mr Bogdan, Mr Westphal and Mr Moss at the hearing held by the Committee on Legal Affairs and Citizens' Rights on 15 April 1998.

opened. However, it is unlikely that the liquidator appointed in the debtor's country would be familiar with either the languages or the legal systems of all the other countries in which the debtor might have assets. The liquidator would therefore have to rely on support from lawyers, translators and interpreters in all these countries, which might prove even more costly than separate insolvency proceedings. An even more serious disadvantage of the universality principle in its pure form is that all creditors from all countries are forced to lodge their claims in a single round of insolvency proceedings, which may take place in a distant country.

Probably the most serious obstacle to the unrestricted application of the universality principle consists in the substantial claims under tax and social insurance law that play a part in almost all major insolvency proceedings today. Almost all countries refuse to help each other in the settlement of such claims unless such help has been contractually agreed. The unconditional surrender of assets to a foreign insolvency liquidator would have two undesirable outcomes when seen from this angle. Firstly, the assets thus transferred might very well end up in the hands of the tax authorities of the country in which insolvency has occurred, primarily because in many countries tax claims are given preference and settled before claims lodged by private creditors. Secondly, and more importantly, the tax claims of the country in which the assets are situated would probably not be settled at all, because they would be regarded as unenforceable under the law of the country in which insolvency had occurred. The courts of the country in which the assets were situated would probably think twice before surrendering property to a foreign liquidator if this meant a significant financial loss to their own country.

In its approach the Convention on Insolvency Proceedings of 23 November 1995 is based on the principle of the universality of insolvency. Thus insolvency proceedings opened in a Contracting State have legal effects not only in that State but automatically in any other Contracting State (Article 17(1)). The liquidator in the main insolvency proceedings has in principle the same powers in all other contracting States as conferred on him by the insolvency law of the State in which proceedings are opened. In particular, he may remove and realise assets of the debtor in accordance with the rules of the State of the opening of proceedings (Article 18(1) and (2)). In contrast to the present legal situation, decisions on the conduct and termination of insolvency proceedings and on preservation measures will in the future be enforceable under the provisions of the Convention on jurisdiction and the enforcement of judgments in civil and commercial matters.

The courts of the Contracting State in whose territory the centre of a debtor's main interests is situated have jurisdiction to open insolvency proceedings. The centre of a company's or legal person's main interests is assumed to be the place of its registered office. Where there is jurisdiction under these provisions to open insolvency proceedings in one Contracting State, the courts of another Contracting State have jurisdiction to open other insolvency proceedings only if the debtor has an establishment in the other Contracting State. The effects of these proceedings are restricted to the assets of the debtor situated in the territory of the latter Contracting State. If proceedings are opened at the centre of the debtor's main interests, any proceedings opened subsequently at the place where an establishment is situated are deemed to be secondary proceedings (Article 3(1) to (3)). Pursuant to Article 4, insolvency proceedings and their effects are in principle governed by the insolvency law of the Contracting State in which such proceedings are opened. However, this principle is overruled by a considerable number of exceptions of a procedural nature (see Article 3(4)(a), Article 15, Article 18(3), Article 21(1) and (2), Article 22(2) and Article 38) and also of a substantive nature. Thus third parties' rights in rem, including registerable entitlements to rights in rem, are governed by the law of the State where the property is situated (further substantive derogations in Articles 6(1), 8, 9, 10, 11, 13 and 14).

This attempt by the Insolvency Convention to harmonise the principles of universality and territoriality for all practical purposes gives rise to a number of weaknesses which might be removed as the proposal for a regulation is drawn up.

The Convention provides for some flexibility in that it leaves it to the individual creditor to decide whether to participate in the main insolvency proceedings in the country where the centre of the debtor's main interests is situated or to opt for local insolvency proceedings in the country where the debtor has an establishment. Basically, however, the system is rather inflexible, since the choice is limited to two options: to seek secondary insolvency proceedings or to refrain from doing so. A more flexible system might consist in opening secondary insolvency proceedings, but permitting individual creditors to seek a judgment making the recognition of the main proceedings conditional on certain conditions adjusted to the circumstances in individual cases, e.g. permitting local creditors to lodge their claims in their own country or enabling certain general privileges to apply to local assets.

Another question that arises is whether it is appropriate to make the option of secondary insolvency proceedings conditional on the debtor having an establishment in the country concerned. It should instead be possible to open territorially limited proceedings in any Contracting State where the debtor has substantial assets. Otherwise, if there is no establishment, assets could, under the Convention, be taken abroad and distributed without regard for the legitimate interests of local creditors.

Finally, although granting the tax and social security authorities of other Contracting States the right to lodge their claims during insolvency proceedings is a step forward, the Convention does not specify where such claims would rank. According to Article 4, claims are ranked in accordance with the law of the State of the opening of proceedings. However, even if this law provides for certain tax demands to take precedence, it is extremely unlikely that this extends beyond domestic tax demands and demands for social insurance contributions. The practical consequence would be that tax authorities in countries granting a preference in this respect would always seek secondary insolvency proceeding.

Despite the reservations and difficulties referred to above, the rapporteur feels that the introduction of Union-wide rules on insolvency proceedings through the adoption of the regulation called for is overdue and urgently needed.