

# Coordinating the Preventive Restructuring Directive and the Recast European Insolvency Regulation

Lorenzo Stanghellini and Andrea Zorzi highlight potential issues with the new Directive



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## A problematic freedom for Member States

Issues arising from coordination among possible cross-border procedures seem underestimated in the Directive on Preventive Restructuring Frameworks (the “Directive”). The Directive purports to be almost indifferent to the Recast European Insolvency Regulation (“Recast EIR”). It cites the Recast EIR in various recitals and articles, but expressly takes into account the

possibility that the restructuring framework which a Member State designs or selects from the existing ones in order to implement the Directive, will not be a procedure listed in Annex A of the Recast EIR, thereby leaving the Member States a freedom that, if fully used, may raise thorny issues.

Leaving aside the issue of debtor discharge, with reference to restructuring frameworks, Recital 12 refers to the Directive as a step towards the

establishment of “substantive minimum standards for preventive restructuring procedures”, vis-à-vis the procedural coordination sought by the Recast EIR.

That said, Recital 13 and its implications are the main focus below. In a somewhat ambiguous, if not contradictory, manner, this Recital states that:

- (a) the Directive is “complementary” and “fully compatible” with the Recast EIR;



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- (b) the Directive can be implemented by means of procedures which do not satisfy “all conditions for notification” under Annex A of the Recast EIR (and are therefore outside the scope of the Recast EIR); but
- (c) the Directive also seeks to “facilitate cross-border recognition” of procedures and judgments.

Finally, Recital 14 refers to the safeguards against abusive COMI relocation contained in the Recast EIR and mentions the need for “[c]ertain restrictions”, also with regard to procedures not covered by the Recast EIR. This Recital serves as an introduction to the provision against forum shopping for a stay contained in the Directive (Article 6, para. 8, second part), which is the only substantive part of the Directive expressly mentioning the possibility of the implementation of the Directive by means of procedures that are not included in Annex A of the Recast EIR. Note also that Article 6 para. 8, second part of the Directive, takes into account the case of a

debtor that relocates before (and, implicitly, with a view to) filing for the opening of a restructuring procedure, shortening, in this case, the allowed maximum duration of the stay to four months.

In light of the relative “indifference” between the Recast EIR and the Directive, Member States could keep in place their Recast EIR-compliant procedures without them being compliant with the Directive, as long as they do offer debtors *at least one* restructuring framework which is, in fact, compliant with the Directive. This could give rise to various issues, at least with regard to the recognition of a stay or of judgments. At a minimum, this is not exactly what Recital 13 envisages, when it states that the Directive facilitates cross-border recognition: it does so only inasmuch as the Member States decide to implement it with Annex A procedures, a decision which is left to their discretion.

#### Transposition through a non-Annex A Instrument: Issues

Let us assume that a Member State chooses to transpose the Directive through a non-Annex A instrument (and an instrument for which it does not demand an amendment of Annex A). If a procedure which is not listed in Annex A of the Recast EIR is opened in a Member State, there are various possibilities with regard to the recognition and enforcement of the opening decision, and especially of the possible stay obtained by the debtor with regard to assets located abroad. Whether the decision has any effect abroad mainly depends on the Member State where the decision is to be recognised and the stay enforced.

#### **Case A: Coincidence of the Directive Forum and the Debtor’s COMI**

If the court petitioned by the debtor to open a procedure not listed in Annex A is located where the debtor has its COMI, the effects of the opening of the

procedure on assets located abroad depend on whether or not the debtor has an establishment in the foreign Member State where the court order is to be recognised.

If there is an “establishment” in the “recognising” Member State, the debtor could petition the latter Member State’s court to open a local proceeding (which would be a “territorial” proceeding in the words of the Recast EIR; it could never become a “secondary” proceeding because what would otherwise be the “main” procedure is not listed in Annex A). The effects of this procedure are of course limited to the assets in that Member State (Article 3(2), Recast EIR). Except when a creditor has petitioned the “local” court, if at all allowed, and thus has forced the choice of a particular procedure, it will be up to the debtor to choose whether to petition the local court for a procedure, and to choose which one (listed in Annex A or not).

However, if there is no “establishment” of the debtor in the other Member State, such a Member State is precluded from opening its own Annex-A proceedings and the debtor’s choice would be restricted to non-Annex-A procedures. It should be noted, however, that, in some Member States, there are no restructuring frameworks which are *not* listed in Annex A (for example, both in Spain and in Italy, the procedures most similar to schemes of arrangement are listed in Annex A and could therefore be used as “local” procedures, but only if there is an “establishment” within the meaning of the Recast EIR).

Nonetheless, if there is no “establishment” in the Member State where the non-Annex A procedure is to be recognised, other venues may be tried. Recognition of the opening of the procedure, including the possible stay, may depend on whether the Member State where recognition is sought has adopted rules similar to those of the UNCITRAL Model Law on Cross-Border Insolvency (see, in



**IN LIGHT OF THE RELATIVE “INDIFFERENCE” BETWEEN THE RECAST EIR AND THE DIRECTIVE, MEMBER STATES COULD KEEP IN PLACE THEIR RECAST EIR-COMPLIANT PROCEDURES**





## MEMBER STATES SHOULD THINK TWICE BEFORE TRANSPOSING THE DIRECTIVE THROUGH A NON-ANNEX A INSTRUMENT



particular, Article 19).

If this is not the case, then a negative conflict of jurisdiction may occur: the non-Annex A procedure opened in the Member State where the COMI is located cannot be recognised in a Member State which does not follow UNCITRAL-style principles, but no autonomous proceedings could be opened in that Member State, if this Member State takes a COMI approach (perhaps, as mentioned, a local proceeding or a “territorial” one could be opened, depending on domestic law, if there is an establishment).

### **Case B: No coincidence of the Directive Forum and the Debtor’s COMI**

On the contrary, if the non-Annex A proceedings are opened in a State which is not the COMI State, the opening of the non-Annex A proceedings could not then prevent the opening of (main) proceedings in the COMI State, possibly on request of creditors. This could give rise to positive conflicts of jurisdiction, because the main proceedings could also seek recognition in the Member State where the non-Annex A proceedings were opened.

### **Possible avenues for recognition outside the EIR**

Imagining that it is not possible to recognise the opening decisions and the connected possible stays on the basis of the Recast EIR, and that it is not possible (or is unsatisfactory) to open some sort of local procedure in a foreign Member State in order to protect assets located there, other ways to recognise the opening decision and the stay could be based upon the provisions traditionally used to such ends. Among the possibilities, the Brussels Regulation (Regulation (EU) No 1215/2012) and the Rome I Regulation (Regulation (EC) No 593/2008) are the most relevant.

The argument with the Rome I Regulation runs under its Article 12 (Scope of the Law Applicable), which states that the

law applicable to a contract governs “the various ways of extinguishing obligations, and prescription and limitation of actions.” This argument has been made for the recognition of the effects of schemes of arrangement, by Jennifer Payne for example, in her 2014 book published by The Cambridge University Press (Payne, 2014: 312-313). Without entering into the discussion about schemes, it seems very difficult to include a stay on individual actions in Article 12, given that a stay, by no means, causes the extinction of obligations.

The Brussels Regulation, on the other hand, does not seem *prima facie* a proper avenue either, since it excludes from its scope “*bankruptcy, proceedings relating to the winding-up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings.*” (Article 1(2)(d)).

First of all, it should be noted that Recital 7 of the Recast EIR expressly states that, although general proceedings excluded by the Brussels Regulation should be covered by the Recast EIR, “*the mere fact that a national procedure is not listed in Annex A to this Regulation should not imply that it is covered by Regulation (EU) No 1215/2012.*”

It is therefore perfectly possible that a procedure is not included in Annex A *and* does not fall within the scope of the Brussels Regulation. The opening of a procedure which aims at implementing the Directive, but which is not listed in Annex A of the Recast EIR, may well be one of the cases in point, in which neither regulation applies.

One could argue that the “light touch” extra-judicial focus (see Recital 29) of the Directive may warrant a narrow reading of Article 1(2)(d) of the Brussels Regulation, with the consequence of allowing for recognition to take place under the Brussels Regulation, at least in some of the possible implementing frameworks (e.g. depending on the degree of pervasiveness of

court control, etc.), but the result is far from guaranteed.

Finally, one possibility would be to resort to each Member State’s private international law rules, outside the scope of the Rome I Regulation. In Italy, for example, one could think of applying Article 66 of Act 31 May 1995, No. 218, on private international law, according to which foreign judgements on non-contentious jurisdiction are recognised with no formality, subject to certain conditions. In any event, a huge area of uncertainty would open, as each Member State has its own tradition and approach to private international law (and to the related issue of “public order”).

### **Conclusion**

All this considered, we believe that Member States should think twice before transposing the Directive through a non-Annex A instrument, at least for the provisions of the Directive that aim to allow the debtor to bind third parties. This is certainly the nature of the provisions regarding the stay on individual enforcement actions (Article 6), the consequences of the stay on executory contracts (Article 7), and the binding effect of restructuring plans on creditors (Articles 10 and 11). Apart from the provisions on pure mediation, early warning and fully consensual restructuring plans, transposing the Directive through exclusively domestic instruments may bring debtors into uncharted international waters. ■