

PROJECTS OF HARMONIZATION OF THE LAWS ON INSOLVENCY

LAVINIA IANCU

TIBISCUS UNIVERSITY, Timișoara, Daliei Street, 1/A
relicons@yahoo.com

Abstract:

Ample legislative projects are in progress, both at a European level and at an international level, in order to harmonize the insolvency regulations. Undoubtedly, at the present time the implementation of a unitary insolvency law applicable at a global level cannot be brought into discussion because of the significant differences existing among the national legal systems. The project initiated at the level of the European Union sets out to identify the aspects that may be harmonized in the matter of insolvency at a European level while the Project of the Global Principles in Insolvency is trying to lay down the principles that may apply in case of a cross-border insolvency procedure.

Key words: project, harmonization, insolvency

JEL classification: K33

The Project of harmonization of the laws on insolvency at the level of the European Union was submitted, in April 2010, upon request of the Legal Affairs Committee of the European Parliament¹. This action was performed by Insol Europe, the Professional Association for European restructuring and insolvency specialists.

The legislation on insolvency acts as a counterbalance for several objectives. It has the purpose to protect the rights of creditors and, at the same time, on the one side, the interests of the shareholders and of the customers and, on the other side, to avoid the liquidation of potentially viable businesses. Within this context, in many of the member states, the legislation of insolvency cultivates the discipline and correctness of the financial management and facilitates the rehabilitation or helps inefficient companies go off the market in an orderly way. The manner in which the legislation on insolvency protects the different parties involved may be very different from one member state to another. Thus, significant differences may be identified within the national insolvency regimes with respect to fundamental considerations of policy, structure and content.

The document identifies and underlines the differences among the national insolvency legislations that may create obstacles, competitive advantages and/or disadvantages as well as the difficulties of the companies that perform cross-border activities or operate within the EU. In particular, it displays a list of problems that may occur in the absence of common rules on insolvency as issues pertaining to the insolvency of company groups, the liability of the shareholders who are citizens of different member states, references to the national legislations related to the insolvency of "community" companies and strategic cross-border movements for insolvency-related purposes. Moreover, the document identifies a series of areas associated with the insolvency legislation within which the harmonization at the level of the European Union is possible and worthwhile. Finally, the document evaluates the extent to which the harmonization of the insolvency legislation might facilitate the harmonization of the legislation on commercial companies within the European Union.

¹ <http://www.europarl.europa.eu/studies>

The objective of the report is to evaluate whether the harmonization of the insolvency legislation at the level of the EU is necessary or worth being achieved. The report evaluates the manner in which the adoption of common insolvency rules may facilitate the harmonization of the legislation on commercial companies in the EU.

It is important, in order to create a framework of management of the crisis for the internal market and for the structural measures to be efficient at the EU level, to establish the extent to which the harmonization of insolvency legislations in the different member states of the EU is necessary. There is a limited number of areas in which harmonization is expected and can be achieved. These areas are mainly the following: a possible common test of the insolvency as a requirement for a formal insolvency procedure; the formal aspects pertaining to the submission and the resolution of the requests within the framework of a formal insolvency procedure; certain aspects concerning the manner in which the reorganization plans are adopted and their content; the rules for prejudicial actions; and, finally, the responsibilities of the administrators.

The conclusions of this report are based on the answers to a questionnaire that Insol Europe delivered to a representative sample of members from France, Germany, Italy, Poland, Spain, Sweden and Great Britain, Belgium and the Netherlands.

Within this context, the report identifies the most important fifteen aspects that must be harmonized so as not to become obstacles to the successful execution of the cross-border insolvency procedures. The primary fields of the insolvency law targeted by this report, that require immediate harmonization, are: the eligibility and the criteria for the opening of an insolvency procedure; the general suspension of the powers of creditors to exploit and exercise the rights that they acquire after the initiation of the reorganization and insolvency procedures; the rules pertaining to the management of insolvency procedures; the classification of creditors, the rules concerning the process of submission and verification of the requests submitted by creditors; the responsibility for the proposal, the verification, the adoption, the modification and the content of the reorganization plans; the object of the estate subject to the insolvency procedure, the rules concerning the avoidance of the transactions concluded before the opening of the insolvency procedure, the cessation of contracts and rules on the mandatory continuation of the execution of contracts, the responsibility of the legally appointed administrators, of the actual administrators, of the investors and of other parties associated to the debtor; provisions on the post-opening financing; the qualifications and eligibility of the practitioners in order for them to be appointed representatives within the insolvency procedure and different rules of authorization, regulation, supervision and professional ethics and conduct; the coordination of insolvency procedures in connection with companies that belong to a group of companies; the need for a European database of judicial decrees and orders and the scope of application of the EC Regulation No. 1346/2000.

The themes considered being the most important within the project, the insolvency of the group of companies and the responsibility of the executive bodies of the debtor in the insolvency procedure were taken over by UNCITRAL and steps are being taken to modernize the European legislation in these fields².

A well-balanced and well thought approach is necessary with respect to harmonization, an approach that may modify or condition the attempts to harmonize on the whole all the aspects pertaining to the insolvency legislation. By its very nature, the insolvency legislation interacts with many other fields as civil law, tax law, labor law. Until the latter ones are unified, the harmonization of all the aspects pertaining to the insolvency legislation will not be possible.

2 *I.Mevorah*, The Prospect of Harmonization of Insolvency Laws in Europe. Learning from UNCITRAL Work on Groups and Directors Duties in Insol Europe, Academic Forum Conference, Venice 2011, p. 124.

Nonetheless the harmonization of the provisions on insolvency at a European level is possible and is inevitably going to lead to the transparency of the execution of the procedure, to greater trust of the parties involved and also, for the parties involved, better understanding of the available means and methods with a view to satisfy the needs of commercial entities that are in a difficult situation and of the remedies available to the creditors of those entities and other parties involved in such entities.

In February 2006 the American Law Institute (ALI) together with the International Insolvency Institute (III or Triple-I) initiated a project in order to investigate on the possibility to adapt and extend the principles of cooperation in insolvency existing among the NAFTA states³, so as to make them applicable at a global level.

The principles applicable to the NAFTA states originate the Transnational Insolvency Project of the American Law Institute that was carried out between 1995 and 2000, having the objective of laying down guidelines for international cooperation in transnational insolvency⁴ cases, targeting the United States of America, Canada and Mexico⁵.

The documentation that lies at the basis of the initial principles is made up of four sections, as follows:

- the first part exhibits the reasons for which the implementation of these principles is necessary. The main reason for the determination of these principles is in direct connection with the need for commercial security of those who engage in international transactions;
- the terminology used is defined in the second part. The Insolvency terminology, that is intended to be used at a global level, was established after having consulted several states, public institutions, international non governmental organizations, insolvency practitioners associations as well as experts who participated in time to the elaboration of Insolvency best practice manuals. This section aims at standardizing at a global level of the notions used in the insolvency procedures, which is going to lead to a better communication between the syndic judges and the insolvency practitioners involved in cross-border insolvency cases;
- the third section exhibits the global coordination Principles in the international insolvency cases;
- the last part contains a list of abbreviation that are frequently used in the documentation and a summary of the material.

The ALI NAFTA Principles were approved in May 2000 at the Annual Meeting of the American Law Institute. From this date on, a sustained work of collaboration between the American Law Institute and the International Insolvency Institute has been performed in order to translate these principles in 13 languages while some other 3 translations are still in progress.

Having had this experience of implementation of some general principles in insolvency, the American Law Institute together with the International Insolvency Institute examined for the first time in 2005 the possibility to adjust the ALI NAFTA principles to a standard of applicability at a global level in the international insolvency cases.

Within the framework of the project initiated in 2006, entitled the III/ALI Global

3 The NAFTA states are the ones that adopted, in the month of May 2000, the North American Free Trade Agreement, USA, Canada and Mexico.

4 According to the NAFTA Principles, the terms: insolvency and bankruptcy are used as synonyms. We are pointing out to this because in the European legislation the notion of insolvency defines the state of the debtor of incapacity to pay, while in the legislations of the NAFTA states this definition corresponds to the notion of bankruptcy.

5 American Law Institute, Transnational Insolvency: Cooperation Among the NAFTA Countries, ALI NAFTA Principles Report, 2003.

Principles, the insolvency law was analyzed in over 50 jurisdictions.

The insolvencies studies and projects developed in time by the World Bank, the Asian Development Bank, the European bank for reconstruction and development, UNCITRAL, UNIDROIT and so on were contemplated while elaborating these principles. The result of these projects was a series of texts called principles, directives, best practice standards or recommendations:

- The Model Law on cross-border insolvency elaborated by UNCITRAL⁶ IN 1997;
- The report drawn up by the Legal Department of the International Monetary Fund in 1999⁷;
- The report on the cooperation principles among the NAFTA states drawn up by the American Law Institute and the International Insolvency Institute in 2000;
- Directives applicable to the communication among the law courts involved in the cross-border insolvency cases, drawn up in 2000 by the American Law Institute;
- Best practice standards for the Insolvency Law drawn up by the Asian Development Bank, starting with 2000;
- Material drawn up by the World Bank in 2001 and revised in 2005 on the insolvency principles and directives and the creditor rights system;
- The Council Regulation (EC) No. 1346/2000 of May 29, 2000, on the insolvency procedures;
- The study on the basic principles in the application of the Insolvency Law drawn up by the European Bank for reconstruction and development in 2004;
- Report on the International civil procedure principles drawn up by the American Law Institute in collaboration with UNIDROIT⁸ in 2004;
- The legislative guide and recommendations on the Insolvency Law created by UNCITRAL in 2004;
- The report of the European Bank for reconstruction and development from on the principles of insolvency practitioners;
- The material drawn up by the International Insolvency Institute in June 2009 on the principles of restructuring of multinational groups⁹;
- The practice guide on cross-border insolvency cooperation drawn up by UNCITRAL in July 2009¹⁰;

All these documents prove the globalization of the commercial activity and the imperative need to regulate international problems emerged within the context of the insolvency state¹¹. The special interest that these organizations - the activity of which targets the international financial system - show to the insolvency law leads to the recognition of the fact that insolvency plays an especially important role within the

6 The United Nations Commission on International Trade Law was constituted on December 17, 1966 in order to eliminate the differences among the national legislations as far as the international trade is concerned.

7 The report is entitled „Orderly&Effective Insolvency Procedures. Key Issues and it was based on the report drawn up by the G-22 work group on the International financial crisis.

8 The International Institute for the Unification of the Private Law is an inter-governmental organization constituted in order to study methods to modernize and harmonize private law in general and trade law in particular. www.undroit.org

9 See *T.C.Hallidaz, B.G. Carruthers*, Bankrupt. Global Lawmaking and Systemic Financial Crisis, Stanford University Press, California, 2009.

10 See *B.Wessels, B.A.Markell, J.J.Kilborn*, International Cooperation in Bankruptcy and Insolvency Matters, Oxford University Press, New York, 2009.

11 *R.Tomasic*, Insolvency Law Reform and Emerging Insolvency Norms, 15 Insolvency Law Jurnal, 2007, p.241.

economic and financial system of any jurisdiction¹².

In April 2010 a preliminary model on the ALI/III Global Principles was presented for the first time. This preliminary report has not yet been published, nevertheless it is known among insolvency specialists, because the text is provisional and subject to revision. It is intended to enter into force by the end of 2011.

The preliminary report contains 41 global principles of international insolvency cooperation and two addenda in which we can find 18 global directives on the communication among the law courts involved in cross-border insolvency cases and 23 global rules on the conflicts of laws in international insolvency cases. The studies performed for this project target the compatibility of the national legal systems with the effects of globalization. The most relevant effect is the reduction of the autonomy of national legislative systems in favor of the international character. Nevertheless there is a precedent of such an extent, the European Insolvency Regulation being adopted by 26 of the 27 member states of the European Union.

The mechanism based on which these principles were approved was the individual vote of every member that is a party of the consultative group for the implementation of the ALI/III Principles. If a certain text was considered by at least two members unacceptable for application at a universal level, it was modified in order to allow the intervention of national legislation.

Also, if two of the members of the consultative group substantially opposed the adoption of a principle, a directive or a rule, the debated text was eliminated. Taking into consideration this system of adoption of texts, the global Principles for cooperation in international insolvency cases were constituted in international consensus.

Although the opinions expressed do not always reflect a unanimous agreement with respect to the texts, these principles reflect the observance of the fundamental values and of the general standards of many jurisdictions, by preventively eliminating all the aspects which created controversies¹³.

The global principles of cooperation in cross-border insolvency cases constitute a set of general non mandatory rules¹⁴, created in such a way so that they could be taken over by all the jurisdictions in the world.

The ALI/III Principles may be used as an alternative solution when it turns out to be impossible to determine an applicable law rule, but also as a legislative guide for the management of the insolvency procedures.

Within the framework of these principles that target the international insolvency cases, notions as cooperation, coordination and communication are particularly important. Cooperation reflects the closeness of the legal systems involved in an international insolvency case in order to find solutions to multinational problems, without standardizing the law systems, coordination implies a limited harmonization in order for the legal systems involved to organize efficiently the execution of the insolvency procedure, without them actually being harmonized, while communication implies the exchange of information among the jurisdictions at all levels - law courts, syndic judges, clerks of the court, insolvency practitioners or other entities involved¹⁵.

12 *L.Elliot, N.Griffiths*, UNCITRAL Practice Guide on cross-border insolvency cooperation, Corporate Rescue and Insolvency, February 2010, p.12.

13 *P.L.Friedman*, Chairman of ALI Program Committee: „achieving coherence, reflecting current best practices, and better adapting the law to social needs”, The President Letter, 32 The ALI Reporter, nr.2, Summer 2010, p.3.

14 Their adoption by the states will be performed in the same manner as in the case of the European Insolvency Regulation 1346/2000, the states having the possibility to take over or not to take over in their national legislation these international principles.

15 *M. Nunner*, Kooperation internationaler Gerichte, *Jus Internationale et Europaeum* 36, Mohr Siebeck, 2010, p.112.

In addition to the 41 global principles, the document contains two addenda, of which the first individuates directives for the communication between the law courts in international insolvency cases while the second one contains applicable rules in case of conflicts of laws.

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