Future EU Regulation: Legal uncertainties and challenges to insolvency

Jean-Luc Vallens comments on a proposal of the EC for a new EU Regulation for assignments of claims

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The European Commission legislative proposal on conflicts of laws for assignments of claims chose the law of the assignor's habitual residence as the law that should apply to the third-party effects of the assignment of claims, allowing at the same time the possibility for the parties to derogate from it.

This proposition could generate conflicts with the principles established by the European Insolvency Regulations, which give jurisdiction to the Law of the assignor's habitual residence when it comes to locating the right *in rem* resulting from a debt assignment.

The European Insolvency Regulation of 20th May 2015 (Reg. (EU) 2015/848)_

The EIR is supposed to provide for rules defining the law applicable to assets and rights of insolvent debtors during insolvency proceedings, and to detrimental acts prior to such proceedings.

Among a debtor's assets, insolvency practitioners have to deal with financial claims toward third debtors to the extent as they still belong to the insolvency estate: such claims may have been sold to any third party, granting rights to third debtors in spite of the insolvency proceedings opened in the meantime.

Regarding these claims, the EIR provides for some specific rules:

i) a financial claim is deemed to be located either in the country where the third debtor is located or in the country in which a bank account is held for claims and cash registered in such an account (EIR art. 2(9));
ii) a transferred financial claim grants to the assignee a right *in rem* that remains enforceable to the debtors' estate (EIR art. 8); and
iii) avoidance actions are currently regulated by the law of the opening State (EIR, art. 7(2) m): if an insolvency practitioner commences an avoidance action against such a transfer he has to take into account the applicable foreign law, because this law may not allow any means of challenging that act (EIR art. 16).

The Proposal for a Regulation on the law applicable to the third-party effects of assignments of claims of 12 March 2018 (COM (2018) 96 final)

A proposal for a new Regulation has been adopted by the European Commission in order to amend and complete the "Rome I" Regulation of 17 June 2008 on conflicts of laws. It focuses on assignments of claims and securitisation (as Rome I Regulation did not address these issues).

The purpose of the draft regulation seems relevant and useful, as it clarifies rules on validity and opposability of such assignments in situations where there is only a likelihood of insolvency or where insolvency proceedings are opened.

It actually could improve predictability for creditors, especially in cross-border assignments: such contracts will be valid and enforceable towards the third debtor, the creditors of the assignor and the appointed insolvency practitioner in case of insolvency of the latter.

The main purpose of the proposal is to solve the conflict of laws in favour of the law of the habitual residence of the debtor. Such a rule seems clear and convenient for third parties, and generally corresponds to the *lex fori concursus,* on which rights and duties of debtors and creditors depend. It grants legal certainty to third parties. According to the authors of the Proposal, it is fully consistent with EIR.

Risk of conflict by the combined application of those two texts

Parties will be authorised by the proposed Regulation to choose another law for regulating the validity and opposability of such assignments. Indeed, if the law of the assignor's habitual residence applies as a general rule, certain assignments could be subject, as an exception, to the law of the assigned claim and with a free choice of law possibility for securitisation.

If the assignor becomes insolvent, such rules will deprive the estate of valuable assets, such as claims on third parties, for the benefit of one creditor, possibly located out of a Member State, under foreign laws. The assignment of a claim will therefore be enforceable against

the insolvency practitioner and other creditors.

It is true that the EC Proposal however establishes a general principle providing that its rules "*shall not prejudice the application of provisions of Union law which, in relation to particular matters, lay down conflict of laws rules relating to the third-party effects of assignments of claims*" (art. 10): it should be therefore compliant in principle with the EIR.

However, the rule contained in Article 16 of the EIR could create an obstacle to any actions against the assignment of claims during the period of time where the rules relating to the voidness, voidability or unenforceability of legal acts detrimental to the general body of creditors apply, at the disadvantage of the debtor's estate and of all the creditors.

Moreover, the proposal is not clear with respect to the applicable law: to which extent could the applicable law, that should be the law of the third debtor in case of insolvency, be replaced by the law chosen by the parties in favour of the assignee?

Valuable assets could be put out of the debtor's estate by the way of opposable assignments of claims before the assignor becomes insolvent, depriving European companies and their creditors of a relevant part of assets.

It could finally appear to be in opposition with the objectives set by the Capital Markets Union New Action Plan of 24 September 2020. The EU Commission focuses on specific actions for the next years "to review the current regulatory framework for securitisation to enhance banks' credit provision to EU companies, in particular SME" (Action 6) and "*to make the outcomes of insolvency proceedings more predictable and to allow for a regular assessment of the effectiveness of national loan enforcement regimes (Action 11)...*"

Let's take the concrete example that a financial claim belonging to a debtor is assigned to a third party. The insolvency practitioner appointed by the court begins an avoidance action to get the value of the claim back for the collective interests of the debtor: the courts of the opening State have jurisdiction, but the applicable law may hinder such an action. In such a situation, the proposal of the Commission to regulate assignments would facilitate, thanks to a free choice, any foreign law granting a right that can be opposed to the action of the practitioner.

A similar disadvantage could occur, if an insolvent debtor, who remains in possession, transfers a claim belonging to the estate after the court has opened insolvency proceedings. The EU proposal does not raise any exception as to the applicable law for such an assignment: the value of the assigned claims will thus be out of the reach of insolvency practitioners.

Insolvency practitioners and law makers of Member States should be aware of risks created by rules relating to conflicts of laws provided by the EU legislative proposal, the consequences of which maybe have been underestimated. ■

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