# Should Articles 8 and 16 of the EIR be amended?

Reinhard Bork reviews if and how the EIR and EIR Recast have made cross-border insolvencies any easier in practice

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**25 years of EIR, 10 years of the EIR Recast – is that a reason to celebrate? In my opinion, it certainly is. From a practical point of view, the EIR has made cross-border insolvencies considerably easier. It has contributed significantly to legal certainty, simplified procedural processes, and enabled predictable outcomes.**

In particular, the fact that – unlike the UNCITRAL Model Law – there are rules on international jurisdiction and applicable law, even if these rules are not perfect, helps practitioners, as does the provision that foreign insolvency proceedings are recognised automatically and not in a complex recognition or relief procedure. It is also extremely helpful that we have the CJEU, a court that can ensure a uniform interpretation and application of European insolvency law.

On the other hand, there are also norms that cause more difficulties than support in practice. A particularly striking example is the rules on group coordination proceedings, which have proved to be dead law from the outset – not only in Europe, but also in Germany, where there are comparable regulations. Further, the provisions on virtual secondary proceedings live in the shadow. Finally, I am not sure whether we need six articles on data protection.

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## Targets for reform

When, however, discussing the upcoming evaluation and possible reform of the EIR, as prescribed by Article 90 EIR, we should also take a look at two other provisions that cause considerable problems for insolvency practitioners and make cross-border proceedings in Europe expensive and legally uncertain.

One provision is Article 8, which – according to the prevailing opinion and case law of the CJEU – excludes rights *in rem* not only from the application of the *lex fori concursus*, but also from any insolvency law at all. This is an exception to the principle of universalism which does not fit into the EIR system and serves no purpose other than to protect local interests. The fact that this exception is limited to security assets located in an EU Member State is particularly bizarre, as it is completely incompatible with the idea of a single market. Finally, it treats security holders from the EU better than domestic and foreign creditors and therefore violates the principles of equal treatment of (secured) creditors and procedural justice. After all, there is a risk that the secured creditor will withdraw the collateral from the company's organisational structure, thereby jeopardising the restructuring, which is not compatible with the principle of optimal realisation of the debtor's assets.

The same applies to Article 16, which allows an opponent of an avoidance action the defence that the legal act that is challengeable under the *lex fori concursus* is subject to a law other than that of the opening state (the *lex causae*) and that it is in no way challengeable under that law. This rule also makes life difficult in practice, since the Insolvency Practitioner, even though not encumbered with the burden of proof, before starting litigation against the recipient, has to assess in advance the law of which jurisdiction the *lex causae* is and what it says about the contestability of the transaction in question.

This leads to sincere legal uncertainty for the Insolvency Practitioner,[1] gives leeway for manipulation by choice of law clauses,[2] and causes a significant amount of cost which is incompatible with the principle of efficiency. This rule is contrary to the system, violates the fundamental principles of universalism, mutual trust between Member States, equal treatment of creditors, and optimal realisation of the debtor's assets. Above all, it has yet to be convincingly justified.

Typically, the principle of protection of trust is invoked in defence of both norms: the secured party and the opponent to an avoidance action respectively must be protected in their expectation that, even in the event of insolvency, the *lex situs* or the *lex causae* respectively will continue to apply. But these expectations are not legitimate. Anyone who grants credit to a debtor abroad or otherwise does business with them must expect that, in the event of the debtor's insolvency, the debtor's insolvency law will apply.

As regards Article 8, lenders which grant credit to a foreign debtor in exchange for security, must be aware that the debtor's insolvency will be administered in a foreign state and in foreign insolvency proceedings under foreign insolvency law. Hence, they can only trust in the application of the *lex fori concursus*. Further, Article 8 addresses the wrong point in time because creditors invest their trust when concluding the contract whereas Article 8 refers to the collateral's location when insolvency proceedings are opened.

As regards Article 16, it has repeatedly and rightly been argued by Michael Veder that protection of trust as granted by this norm is not justifiable, since the challenging of the act in question is a 'foreseeable risk'.[3] And indeed, creditors who enter into transactions with a debtor (who is, in most cases, subject to insolvency proceedings shortly after the transaction) have to take into account the possibility that they cannot keep what they have received due to the debtor's transactions avoidance law. The trust to be protected under the *lex causae* as an exception to the *lex fori concursus* therefore constitutes wishful thinking rather than legitimate expectations.

Consequently, both norms prove to be overprotective. In my opinion, the only topic that has to be taken account of is COMI change. If it is true that the creditor can only trust in the application of the insolvency law of the debtor's jurisdiction, these expectations might be jeopardised if the debtor has transferred their COMI after the contract with the creditor but before the application for insolvency proceedings. In this case, the expected insolvency law is not the applied insolvency law. However, as I have explained in more detail in my book on the principles of cross-border insolvency law,[4] this can be honoured by respective rules which could be shaped as follows:

> ***Article 8***
> *(1) The law of the state of the opening of proceedings shall determine the effects of insolvency proceedings on rights in rem.*
> *(2) Where the secured creditor provides proof that, when creating the right in rem, the debtor had their centre of main interests in a state other than the state of the opening of proceedings, the law of this state shall determine the effects of the proceedings on the right in rem.*

And similarly:

> ***Article 16***
> *(1) The law of the state of the opening of proceedings shall determine the rules relating to the voidness, voidability, or unenforceability of legal acts detrimental to the general body of creditors.*
> *(2) Where the person who benefited from such an act provides proof that the debtor had their centre of main interests in a state other than the state of the opening of proceedings when accomplishing the act, the law of this state shall determine the rules governing these detrimental acts.*

## Summary

In summary, I would like to advocate that these two Articles also be reviewed when the European Commission starts its evaluation process under Article 90 EIR and to finally return to the principle of universalism by amending these unnecessary and unjustified exceptions to the *lex fori concursus*. Admittedly, one cannot be very optimistic that this will lead to the desired success. But one should not give up hope too soon...

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**Footnotes:**

1 In *Nike*, in asserting that Article 16 EIR enhances legal certainty (Case C-310/14, ECLI:EU:C:2015:690, paragraph 18) – the CJEU misses the fact that nothing is more legally certain than the *lex fori concursus*.

2 Cf. CJEU, *Vinyls Italia*, Case C-54/16, ECLI:EU:C:2017:433, paragraph 40 et seq.

3 For a first mention of this, see Michael Veder, *Cross-Border Insolvency Proceedings and Security Rights* (Kluwer, 2004), 315 et seq.

4 See Reinhard Bork, *Principles of Cross-Border Insolvency Law* (Intersentia, 2017), paragraphs 6.40 et seq., 6.99.