

Group insolvencies under the EIR recast

Jessica Schmidt explains the new rules and definitions in the revised EIR Chapter V

With the new Chapter V on group insolvencies, the EIR recast has finally filled an often moaned about gap in the EIR.

But the new rules have been deliberately confined to the procedural level – they do not provide for any substantive consolidation. This is a sensible approach, because substantive consolidation would not only frustrate the legitimate expectations of creditors, but would be tantamount to completely abandoning the fundamental cornerstone principles of separate legal entity and limited liability at the very moment when they are most important: insolvency.¹

Scope: the definition of “group of companies”

Of fundamental importance is, firstly, the definition of the term “group of companies”. Art. 2(13) EIR recast defines it as meaning “a parent undertaking and all its subsidiary undertakings”. The term “parent undertaking” is then defined in art. 2(14) EIR recast as an undertaking which controls, either directly or indirectly, one or more subsidiary undertakings; an undertaking which prepares consolidated financial statements in accordance with the EU Accounting Directive² shall be deemed to be a parent undertaking. Hence, in contrast to the Commission proposal³, where the definition in art. 2(1)(j) had been limited to subordination groups, the adopted definition also encompasses the so-called *Gleichordnungskonzerne* (i.e. where undertakings are managed

on a unified basis within the meaning of art. 22(7) EU Accounting Directive).⁴

Despite its complexity⁵, the approach of building on the well-established group concept of accounting law undoubtedly has the great advantage of systematic consistency and coherency in EU law.⁶

The two pillars of procedural coordination

The concept of procedural coordination in the EIR recast rests on two pillars: (1) group-specific duties of cooperation and communication (art. 56 – 60 EIR recast), and (2) the option of special group coordination proceedings (art. 61 – 77 EIR recast).

Group-specific duties of cooperation and communication

The first pillar consists of specific duties of cooperation and communication between (i) the insolvency practitioners appointed in proceedings concerning group members (art. 56 EIR recast), (ii) the courts before which insolvency proceedings concerning group members have been opened or are pending (art. 57 EIR recast), and (iii) all the insolvency practitioners appointed and all the courts involved (art. 58 EIR recast). These rules have been deliberately shaped in similar form to art. 41-44 EIR recast on cooperation and communication between those involved in main and secondary proceedings relating to the same debtor.⁷ In addition, art. 60(1) EIR recast grants the insolvency practitioners of the group members mutual

rights of participations in the proceedings opened with respect to other members of the group; these include: (a) the right to be heard, (b) the right to request a stay in order to ensure the proper implementation of a restructuring plan, and (c) the right to apply for the opening of group coordination proceedings.

Group coordination proceedings

The second pillar is the option of special group coordination proceedings, which are regulated in section 2 of Chapter V EIR recast (art. 61-77).

The concept

The concept of group coordination proceedings was only introduced into the EIR recast in the course of the legislative procedure in the European Parliament and the Council. The original Commission proposal⁸ had favoured a different approach: it had wanted to achieve coordination only via extensive mutual participation rights of the insolvency practitioners of the individual group companies. But this approach immediately met with severe criticism: on the one hand, it was widely perceived as too cautious and not far-reaching enough⁹; on the other hand, there were concerns that it would have led to severe difficulties and frictions and ultimately even a mutual logjam of the proceedings¹⁰. Given these disadvantages and risks associated with the Commission’s approach, Germany lobbied successfully both in the European Parliament and in the Council for an alternative concept, which the



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THE NEW RULES HAVE BEEN DELIBERATELY CONFINED TO THE PROCEDURAL LEVEL - THEY DO NOT PROVIDE FOR ANY SUBSTANTIVE CONSOLIDATION





THE EUROPEAN LEGISLATOR HAS IMPLEMENTED AN “OPT-OUT” MODEL WHICH IS INTENDED TO ENSURE THE VOLUNTARY NATURE OF THE GROUP COORDINATION PROCEEDINGS



German government had also favoured for the insolvency reform on the German national level¹¹: the concept of group coordination proceedings.¹²

Basic elements of the concept of group coordination proceedings

The concept of group coordination proceedings consists of three key elements: (a) a coordination court, (b) a coordinator, and (c) a group coordination plan.¹³

Group coordination proceedings may be requested before any court having jurisdiction over the insolvency proceedings of a member of the group by an insolvency practitioner appointed in insolvency proceedings opened in relation to a member of the group (art. 61(1) EIR recast). If multiple requests are filed at different courts, art. 62 recast establishes the priority rule. This has the clear advantage of providing a simple and precise criterion.¹⁴ However, given that the priority principle also has some well-known drawbacks¹⁶, the EIR tries to counterbalance them by

allowing the choice of another (more appropriate) court by agreement of a two-thirds majority of the insolvency practitioners involved (art. 66 EIR recast).¹⁶

A court seized of a request to open group coordination proceedings first executes a kind of preliminary examination whether the three conditions for the opening of group coordination proceedings laid down in art. 63(1)(a)-(c) EIR recast are fulfilled.¹⁷ These conditions are that: (a) the opening of such proceedings is appropriate to facilitate the effective administration of the insolvency proceedings relating to the different group members; (b) no creditor of any group member expected to participate in the proceedings is likely to be financially disadvantaged by the inclusion of that member in such proceedings; and (c) the proposed coordinator fulfils the requirements laid down in art. 71 EIR recast. If the court is satisfied that these conditions are fulfilled, it shall give notice as soon as possible to the insolvency

practitioners appointed in relation to the members of the group and offer them the opportunity to be heard (art. 63(1), (4) EIR recast).

Given that there had apparently been concerns with respect to a “coercive nature” of the group coordination proceedings, the European legislator has implemented an “opt-out”-model which is intended to ensure the voluntary nature of the group coordination proceedings.¹⁸ Pursuant to art. 64(1)(a), (2) EIR recast, an insolvency practitioner appointed in respect of any group member may object to its inclusion in the group coordination proceedings within 30 days of receipt of the notice. The consequence of such a “veto” is that the respective insolvency proceedings shall not be included in the group coordination proceedings (art. 65(1) EIR recast). However, this “opt-out” does not necessarily have to be the “final word”: art. 69 EIR recast establishes the possibility of a subsequent “opt-in” under certain conditions.¹⁹

After the 30-day-period for objections has elapsed, the court

may open group coordination proceedings when it is satisfied that the conditions of art. 63(1) EIR recast (see above) are met; in the opening decision, the court appoints a coordinator, and decides on the outline of the coordination, the estimation of costs and the share to be paid by the group members (art. 68(1) EIR recast).

The **Coordinator** shall be a person eligible under the law of a Member State to act as an insolvency practitioner; the coordinator shall not be one of the insolvency practitioners appointed to act in respect of any of the group members, and shall have no conflict of interest in respect of the group members, their creditors and the insolvency practitioners appointed in respect of any of the group members (art. 71 EIR recast). Under the conditions laid down in art. 75 EIR recast, the appointment of the coordinator can be revoked.

The two essential tasks of the coordinator are: (a) identifying and outlining recommendations for the coordinated conduct of the insolvency proceedings, and (b) proposing a group coordination plan (art. 72(1) EIR recast). Art. 72(2) contains an indicative list of five additional tasks and powers of the coordinator.

The **group coordination plan** shall identify, describe and recommend a comprehensive set of measures appropriate to an integrated approach to the resolution of the group members' insolvencies (art. 72(1)(b) 1 EIR recast). Art. 72(1)(b) 2 EIR recast sets out an indicative list of potential contents.

The function of the group coordination plan is that of a mere "reference plan": its implementation is not effected centrally, but within the framework of the individual insolvency proceedings.²⁰ As art. 70(2) subpara. 1 EIR recast explicitly stipulates, the group coordination plan is not binding upon the insolvency proceedings, which are not obligated to follow it either in whole or in part. In fact, the EIR relies on a "comply-or-explain"-mechanism: If an

insolvency practitioner does not follow the group coordination plan, he/she shall give reasons for not doing so to the persons or bodies that he/she is to report to under its national law, and to the coordinator (art. 70(2) subpara. 2 EIR recast).²¹ Moreover, if an insolvency practitioner does not follow a sensible group coordination plan because of a valid reason, this may constitute a violation of his/her duties and lead to (civil or even criminal) liability for damages or even the revocation of his/her appointment.²²

Possibilities of coordination apart from group coordination proceedings

Since it was clear to the European legislator that the concept of group coordination proceedings has yet to pass the test of practice, it has been deliberately designed as a mere option.²³ Important other options are: (i) restructuring plans outside group coordination proceedings (cf. art. 56(2)(c), 60(1)(b) EIR recast), and (ii) the concentration of all proceedings in one single forum if the COMI of all group members is in the same Member State (but it should be noted that COMI shifts and "creative modifications" geared at achieving a certain COMI have been made much harder by the reform of art. 3(1) and recitals 27 ff. EIR recast).²⁴

Conclusion

The new group coordination proceedings certainly provide an interesting option. However, it remains to be seen whether the system will work in practice (especially the reliance on a "comply-or-explain"-mechanism and the "opt-out"-model raise some concerns).²⁵ In a way, the EIR recast can be perceived as a large-scale "field trial" in this respect; yet, given the almost endless variety of group structures, it may ultimately depend on the individual group which of the ("new" or "old") options is "the best".²⁶ ■

Footnotes:

- 1 Cf. *J. Schmidt* KTS 2015, 19, 35 with further references.
- 2 Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC, OJ 2013, L 182/19.
- 3 Cf. COM(2012) 744.
- 4 Cf. *J. Schmidt* KTS 2015, 19, 36 with further references.
- 5 Critically *Mock* GPR 2013, 156, 164; see also K. Schmidt KTS 2010, 1, 12 ff.
- 6 Cf. *J. Schmidt* KTS 2015, 19, 36.
- 7 Cf. recital 52 sentence 2 EIR recast; *J. Schmidt* KTS 2015, 19, 36.
- 8 COM(2012) 744, art. 42(d).
- 9 Cf. *JURI* report, A7-0481/2013, p. 48; *Eidenmüller* (2013) 20 MJ 133, 148; *Kindler* KTS 2014, 15, 43; *Mock* GPR 2013, 156, 165.
- 10 Cf. doc. 15657/13, p. 5; *Kindler* KTS 2014, 25, 43; *Reumas* ECFR 2013, 554, 586.
- 11 Cf. German reform draft, BR-Drs. 663/13. See in detail on this *J. Schmidt* KTS 2015, 19, 46 ff.
- 12 Cf. *J. Schmidt* KTS 2015, 19, 38.
- 13 Cf. *J. Schmidt* KTS 2015, 19, 38.
- 14 Cf. *J. Schmidt* KTS 2015, 19, 39 with further references.
- 15 See on these Cf. *Jessica Schmidt* 'Groups of companies in German autonomous insolvency law: The lex lata, its application and proposals for reform' in Bob Wessels and Paul Omar (eds), *Insolvency and groups of companies* (INSOL Europe 2012), 37, 46.
- 16 Cf. *J. Schmidt* KTS 2015, 19, 39.
- 17 Cf. *J. Schmidt* KTS 2015, 19, 39.
- 18 Cf. recital 53 subpara. 1 sentence 1; *J. Schmidt* KTS 2015, 19, 39 f. with further references.
- 19 Cf. *J. Schmidt* KTS 2015, 19, 40.
- 20 Cf. *J. Schmidt* KTS 2015, 19, 41.
- 21 Cf. *J. Schmidt* KTS 2015, 19, 41.
- 22 Cf. *J. Schmidt* KTS 2015, 19, 41.
- 23 Cf. *J. Schmidt* KTS 2015, 19, 42.
- 24 Cf. *J. Schmidt* KTS 2015, 19, 42.
- 25 See in more detail *J. Schmidt* KTS 2015, 19, 42.
- 26 Cf. *J. Schmidt* KTS 2015, 19, 43.



THE CONCEPT OF GROUP COORDINATION PROCEEDINGS HAS YET TO PASS THE TEST OF PRACTICE: IT HAS BEEN DELIBERATELY DESIGNED AS A MERE OPTION



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