Cross-border business: any threat of cross-border insolvency? (1) (2/29/19)

EU registered companies are increasingly doing business across the EU by setting up branches, subsidiaries, or permanent establishments. Cross-border business is an outcome of the free market economy that favourably affects society, including corporate competitiveness, employment, innovation, and overall economic growth. However, if a company's financial indicators suggest any financial difficulties, then it should consider insolvency proceedings. An insolvent cross-border company has a number of questions including which court has jurisdiction to hear an insolvency petition and which national law will govern it. This article explores key aspects of starting cross-border insolvency proceedings.

The main insolvency proceedings

Cross-border insolvency proceedings are governed by Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (applicable to insolvency proceedings opened after 26 June 2017), which applies to insolvency proceedings that include a cross-border element within the EU. Under the Regulation, the court receiving an insolvency petition should check on its own initiative to see if it has jurisdiction to accept that petition under article 3 of the Regulation.

Article 3(1) of the Regulation provides that the jurisdiction to open the main insolvency proceedings (MIP) goes to the court of the member state in which the debtor's centre of main interests (COMI) lies, i.e. the place where he regularly manages his interests and which is identifiable by third parties. In the case of a company or another entity, its registered office is taken as the COMI unless there is evidence to the contrary. This presumption applies only if the entity did not move its registered office to another member state within three months before filing the insolvency petition. This statutory limitation mitigates the risk that a company being aware of pending insolvency proceedings will move its registered office to a member state that offers more favourable rules.

The COMI should be determined according to objective criteria that are verifiable by third parties and necessary to provide legal certainty and legitimate expectations in determining the court that has jurisdiction to open the MIP.[1] Special significance is attached to legal certainty and legitimate expectations because article 7(1) of the Regulation provides that insolvency proceedings are governed by the law applicable in the member state in which the proceedings were opened.

National insolvency procedure rules vary considerably from country to country. In Italy, Spain and France, for example, the tax authority may exercise its right to seize the debtor's assets before secured creditors. On the other hand, German law does not give the tax authority any tax recovery preference.[2] For employee protection, wage claims in France take priority over all other claims, while a Germany national fund pays wages for the last three months before the company's insolvency was announced.[3] It is therefore crucial that the member state whose courts have jurisdiction to open a company's insolvency proceedings should be determined early, because this will drive measures to be taken after the opening of insolvency proceedings.

As noted above, the lawmaker has made a presumption that a company's COMI lies at its registered office, but this presumption is rebuttable. Its rebuttal is possible if from a third party perspective the company's principal seat of management is not at its registered office. We should also consider any locations where the company carries on a business and where it has assets, to the extent those locations are seen by third parties. It is important to note, however, that these aspects are considered sufficient for rebutting the presumption only if a comprehensive assessment of the circumstances allows us to find that the actual centre of the company's management and control as well as management of its interests lies in another member state.[4]

A classic example of rebutting the registered office presumption is a PO box entity or shell company set up to evade a heavy tax burden and circumvent any stringent employment rules. A shell company in fact performs no economic activity in the member state of registration but often posts low-income employees to a member state of expensive labour. So there are no grounds for opening insolvency proceedings in the country of the registered office.

However, if a company carries on a business in the country of its registered office, the fact that its parent company established in another country controls its economic freedom is not a sufficient basis for rebutting the presumption.[5]

Also, if a national court has opened the MIP, the courts of other member states must recognise this and they have no power to review the jurisdiction of the court of the member state in which the proceedings were opened.[6]

(to be completed)

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[1] CJEU Ruling of 2 May 2006 on Eurofood IFSC Ltd C-341/04, paragraph 33
[2] Harmonizing Insolvency Laws in the Euro Area Rationale, stocktaking and challenges Diego Valiante No. 153 / December 2016, p. 14–15.
[3] Restructuring and insolvency in Germany: overview, 2019
[4] CJEU Ruling of 20 October 2011 on Interedil Srl C 396/09, paragraphs 51–53
[5] CJEU Ruling of 2 May 2006 on Eurofood IFSC Ltd C-341/04, paragraph37
[6] CJEU Ruling of 2 May 2006 on Eurofood IFSC Ltd C-341/04, paragraph 44