THE EU INSOLVENCY REGULATION: SOME *CAPITA SELECTA*

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1. INTRODUCTION: A QUICK SUMMARY OF THE EU INSOLVENCY REGULATION

The EU Insolvency Regulation entered into force on 31 May 2002.[1] The Insolvency Regulation does not harmonise the substantive rules on insolvency existing in the EU Member States, but provides rules on jurisdiction, recognition and the applicable law regarding cross-border insolvency proceedings within the European Union.[2]

The Regulation is based on the principle of mitigated universality. In principle, an insolvency proceeding which is opened in the Member State where the debtor has its centre of main interests is recognised in all other Member States (Art. 16). This proceeding is called the 'main proceeding'. However, if the debtor has an establishment in a Member State other than the Member State where the centre of its main interests is located, a secondary proceeding can be opened in this Member State (Art. 3(2)). The effects of such a secondary proceeding are restricted to the assets of the debtor situated in the territory of that Member State. The effects of a main proceeding do not extend to Member States where a secondary proceeding has been opened.

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1. Council Regulation (EC) No. 1346/2000 of 29 May 2000 on insolvency proceedings, *OJ* 2000, L 160.

2. See, among others, H.C. Duursma-Kepplinger, D. Duursma and E. Chalupsky, eds., *Europäische Insolvenzordnung* (Vienna, Springer 2002); P. Torremans, *Cross Border Insolvencies in EU, English and Belgian Law* (Alphen aan den Rijn, Kluwer Law International 2002); J. Israël, *European Cross-Border Insolvency Regulation. A Study of Regulation 1346/2000 on Insolvency Proceedings in the Light of a Paradigm of Cooperation and Comitas Europaea* (Antwerp, Intersentia 2004); P.J. Omar, *European Insolvency Law* (Aldershot, Ashgate 2004); P.M. Veder, *Cross-Border Insolvency Proceedings and Security Rights: A Comparison of Dutch and German Law, the EC Insolvency Regulation and the UNCITRAL Model Law on Cross-Border Insolvency* (Deventer, Kluwer 2004); M. Virgós and F. Garcimartín, *The EC Regulation on Insolvency Proceedings: A Practical Commentary* (Alphen aan den Rijn, Kluwer Law International 2004); B. Wessels, *Current Topics of International Insolvency Law* (Deventer, Kluwer 2004); A.J. Berends, *Insolventie in het international privaatrecht* [Insolvency in private international law] (Kluwer, Deventer 2005) (thesis); I.F. Fletcher, *Insolvency in Private International Law* (Oxford, Oxford University Press 2005); C.G. Paulus, *Euopäische Insolvenzordnung* (Frankfurt-on-Main, Verlag Recht und Wirtschaft 2006); B. Wessels, *International Insolvency Law* (Deventer, Kluwer 2006); K. Pannen, ed., *European Insolvency Regulation* (Berlin, De Gruyter Recht 2007) (Pannen 2007a); K. Pannen, ed., *Europäische Insolvenzordnung* (Berlin, De Gruyter Recht 2007) (Pannen 2007b); B. Wessels, *Cross-Border Insolvency Law; International Instruments and Commentary* (Alphen aan den Rijn, Kluwer Law International 2007); F. Mélin, *Le règlement communautaire du 29 mai 2000 relatif aux procédures d'insolvabilité* (Brussels, Bruylant 2008); L. Westpfahl, U. Goetker and J. Wilkens, *Grenzüberschreitende Insolvenzen* (Cologne, RWS Verlag 2008); G. Moss, I.F. Fletcher and S. Isaacs, eds., *The EC Regulation on Insolvency Proceedings: A Commentary and Annotated Guide*, 2nd edn. (Oxford, Oxford University Press 2009); W-G. Ringe, L. Gullifer and P. Théry, *Current Issues in European Financial and Insolvency Law, Perspectives from France and the UK* (Oxford, Hart Publishing 2009); S. Bariatti, *Cases and Materials on EU Private International Law* (Oxford, Hart Publishing 2010).

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In principle, the law which is applicable to the insolvency proceeding and its effects is the law of the Member State within the territory of which that proceeding is opened: the *lex concursus* (Art. 4(1)).

There are two categories of exceptions to the principle of the *lex concursus*. The first category of exceptions can be found in Articles 5 to 7. These exceptions are 'material exceptions': Articles 5 to 7 do not refer to any law other than the *lex concursus*, but state that if the *lex concursus* contains a specific rule (e.g., the rule that 'the opening of the insolvency proceeding affects third parties' rights *in rem*'), then that rule does not apply. The rule that does not apply is not substituted by a rule from the domestic law of another Member State.

The second category of exceptions can be found in Articles 8 to 15. These are exceptions of a private international law nature and they do refer to a law other than the *lex concursus*. For example: the effects of the insolvency proceeding on employment contracts are not governed by the *lex concursus*, but by the law which is applicable to the contract of employment, the *lex causae* (Art. 10).

An *ad hoc* working group worked on a explanatory report with respect to a predecessor of the Insolvency Regulation, a convention with an almost identical text, but which never entered into force.[3] One can use this report as an explanatory report with regard to the Insolvency Regulation as well, as long as one bears in mind that it was never adopted as an official explanation.

In this article, I shall elaborate on several *capita selecta*. They are not really interrelated, except for the fact that they pertain to some ambiguities which I found in the text of the Regulation. I shall give some of these ambiguities some consideration and I shall propose respective solutions for each of them.

2. PROTECTION OF THIRD-PARTY PURCHASERS

An insolvency proceeding entails the partial or total divestment of the debtor (Art. 1(1)). As a result, a debtor who is subjected to an insolvency proceeding can no longer *de iure* dispose of his assets. However, he may *de facto* conclude an act by which he disposes, or pretends to dispose, of an asset which forms part of the estate. An act of disposal must be understood to include not only transfers of ownership but also the constitution of a right *in rem* relating to assets belonging to the estate.[4] For instance, he may transfer an asset to a third party, although he has lost his capacity to do so. Is the third party protected? In other words, does the third party become the owner of the asset, for instance because he could have

3. This – unfinished – report is referred to as the Virgós/Schmit Report, after the Spanish and Luxembourg delegates of the *ad hoc* working group. The English version is published as Appendix 2 in G. Moss, I.F. Fletcher and S. Isaacs, eds. and the authors, *The EC Regulation on Insolvency Proceedings: A Commentary and Annotated Guide* (Oxford, Oxford University Press 2002) pp. 261-327.

4. Virgós/Schmit Report, para. 140.

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reasonably presumed that the debtor still had the right to dispose of the asset and therefore acted in good faith? Or does he not obtain ownership, for instance because the debtor's lack of a right of disposal is of overriding importance in order to protect the creditors? As mentioned above, the Insolvency Regulation does not answer this question directly, since it does not harmonise the substantive rules; it only states which law governs this issue.

As we have seen, the general rule is that the *lex concursus* governs the consequences of an insolvency proceeding. Article 14 contains one of the exceptions to this general rule.[5] This article states that where, by an act concluded after the opening of insolvency proceedings, the debtor disposes, for consideration, of an immovable asset, a ship or aircraft subject to registration in a public register or securities whose existence presupposes registration in a register laid down by law, the validity of that act shall be governed by the law of the state within the territory of which the immovable asset is situated (hence: *lex rei sitae*) or under the authority of which the register is kept (hence: *lex registrationis*).

What is striking is that two situations are not covered by Article 14: (a) the debtor disposes of an asset which is not an immovable asset, an aircraft or a ship, or dematerialised securities, and (b) the debtor disposes of an asset not for consideration, e.g., gratuitously. Which law answers the question of whether the third party acquires ownership of the asset or not?

Some authors claim that the 'normal choice of law rule' designates the law which applies to the question of whether or not the third party acquires ownership of the asset.[6] Although they do not say which law is determined by the 'normal choice of law rule', I presume that they suggest that this law is the *lex rei sitae* or the *lex registrationis*. Their main argument seems to be that the question is a matter of property law,[7] not of insolvency law, and that therefore it should be governed by the *lex rei sitae*. This is not convincing. If the *lex rei sitae* nevertheless applies, then why should this be stated once more in Article 14? In their view, Article 14 must be unnecessary.

Secondly, if the question would really be a matter of property law (which is in their view opposed to insolvency law), then why does the Insolvency Regulation address the issue? Besides, the distinction between 'insolvency law' and 'property law' is not a clear one. Opposing 'insolvency law' to 'property law' is like opposing 'black' to 'round'. Insolvency law governs property aspects, contractual aspects and procedural aspects.

Thirdly, which choice of law rule refers to the *lex rei sitae*? Such a choice of law rule can only be found in the Member States' domestic legislations; there is

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5. With regard to Art. 14, see: Duursma-Kepplinger, Duursma and Chalupsky, eds., *supra* n. 2, pp. 328-338; Fletcher 2005, *supra* n. 2, pp. 418-419; Wessels 2006, *supra* n. 2, pp. 406-408; R. Dammann, in Pannen 2007a, *supra* n. 2, pp. 294-298; R. Dammann, in Pannen 2007b, *supra* n. 2, pp. 302-305; Paulus, *supra* n. 2, pp. 186-189.

6. S.C.J.J. Kortmann and P.M. Veder, 'De Europese Insolventieverordening' ['The European Insolvency Regulation'], *WPNR* 6421 (2000) pp. 764-774, esp. p. 771.

7. They use the term '*goederenrecht*', which comprises not only property *stricto sensu*, but rights *in rem* as well.

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no EU legislative instrument which refers to the *lex rei sitae* as the applicable law. For instance, Article 2 of the Dutch Act on choice of law rules concerning property rights designates, in principle, the *lex rei sitae*.[8] However, the domestic legislation of a Member State may be set aside by EU legislation. Therefore, the question we must ask ourselves is whether there is a EU legislative instrument that sets aside domestic provisions referring to the *lex rei sitae*. The search for such a provision does not take long: Article 4 is such a provision, which designates the *lex concursus*. If someone would remark that Article 4 does not concern the consequences of an insolvency proceeding with respect to property rights, such a remark is erroneous. The first paragraph of Article 4 is not confined to consequences other than property rights. Articles 5 (rights *in rem*) and 7 (reservation of title) concern property aspects. Here again, why would the Insolvency Regulation provide exceptions to Article 4 with respect to property rights if Article 4 does not relate to property rights?

If someone would argue that property law is not dealt with by EU legislative instruments: that is not true. See, for example, recital 38 of the Preamble to 'Rome I' which states that, in the context of voluntary assignment, the term 'relationship' should make it clear that Article 14(1) also applies to the property aspects of an assignment as between assignor and assignee.[9] See, for another example, the Preamble to the settlement finality directive.[10] Recital 17 of this Preamble states that the directive aims at determining which insolvency law is applicable to the rights and obligations of a participant in connection with its participation in a system. However, recital 18 states that collateral security should be insulated from the effects of the insolvency law which is applicable to the insolvent participant. Apparently, the European Parliament and the Council are of the opinion that collateral security belongs to the area of insolvency law.

Those who claim that the *lex rei sitae* applies seem to have come to their view because they think that it is undesirable that the question of whether or not the third party who claims to have purchased a movable asset is protected, is governed by the *lex concursus*. If that really is the underlying reason: the fact that something is undesirable in itself does not necessarily mean that it is not true. But is it really undesirable that the *lex concursus* governs the question of whether a third party who claims to have purchased a movable asset is protected or not? The basic principle of the Insolvency Regulation is the following: as much unity in the insolvency proceeding as possible. The drafters of the Insol-

8. *Wet conflictenrecht goederenrecht*, Act of 25th february 2008, *Staatsblad* [Bulletin of Acts and Decrees of the Kingdom of the Netherlands] (2008) no. 70.

9. Regulation (EC) No. 593/2008 of the European Parliament and the Council of 17 June 2008 on the law applicable to contractual obligations, *OJ* 2008, L 177/6.

10. Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems, *OJ* 1998, L 166, as amended by Directive 2009/44/EC of the European Parliament and of the Council of 6 May 2009 amending Directive 98/26/EC on settlement finality in payment and securities settlement systems and Directive 2002/47 EC on financial collateral arrangements as regards linked systems and credit claims, *OJ* 2009, L 146.

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vency Regulation weighed this principle against the interest of the protection of trade and reliance on publication systems. They came to the conclusion that where there is a system of publication the interest of relying on such a system is of overriding importance.[11] In cases where there is no such publication system, the protection of such reliance is not an issue and we must fall back on the basic principle, as laid down in Article 4.

It is time to wrap up this issue. It is all about the question of which law governs the issue of whether a third party who claims to have purchased a movable unregistered asset, or an asset gratuitously, is protected or not. In my view that law is the *lex concursus*. In the theory that that law is the *lex rei sitae*, two aspects are not clear. Firstly: it is not clear what the added value of Article 14 is if the *lex rei sitae* nevertheless applies. Secondly, in that theory it is not clear why Article 14 is confined to immovable assets, registered assets and gratuitous disposals, and why it does not refer to movable unregistered assets or disposals for valuable consideration. In my theory it is clear what the added value of Article 14 is: without Article 14, Article 4 would apply because Article 14 is an exception to Article 4. Article 14 is restricted to immovable assets, registered assets and gratuitous disposals because in these situations reliance on registers should be protected. With respect to movable unregistered assets and gratuitous disposals, reliance on registers does not play a role, so the scope of the exception to Article 4 would be too wide and the infringement of the unity of the insolvency proceeding would be too serious.

3. ARTICLE 5 AND THE DUTCH COOLING-OFF PERIOD

3.1 **Introduction**

In this section, I would like to consider the question of whether the so-called Dutch 'cooling-off period' falls within the scope of Article 5.

Article 5(1) reads:[12]

> 'The opening of insolvency proceedings shall not affect the rights in rem of creditors or third parties in respect of tangible or intangible, moveable or immoveable assets

11. See also the Virgós/Schmit Report, para. 141.

12. With regard to Art. 5, see E. Dirix and V. Sagaert, 'Verhaalsrechten en zekerheidsposities van schuldeisers onder de Europese insolventieverordening/Les droits des créanciers et le règlement européen relatif aux procédures d'insolvabilité', 107 *Revue de droit commercial belge* (2001) pp. 580 et seq.; N. Watté, 'L'opposabilité des sûretés dans le nouveau règlement européen des procédures d'insolvabilité', 24 *Revue de droit de l'ULB* (2001) pp. 7 et seq.; Duursma-Kepplinger, Duursma and Chalupsky, eds., *supra* n. 2, pp. 204-239; C. Naumann, *Die Behandlung dinglicher Kreditsicherheiten und Eigentumsvorbehalte nach den Artikeln 5 und 7 EuInsVo sowie nach autonomen Deutschen Insolvenzkollisionsrecht* (Frankfurt-on-Main, Lang 2004); Fletcher 2005, *supra* n. 2, pp. 401-408; Paulus, *supra* n. 2, pp. 153-162 Wessels 2006, *supra* n. 2, pp. 367-378; T. Ingelmann, in Pannen 2007a, *supra* n. 2, pp. 245-253; T. Ingelmann, in Pannen 2007b, *supra* n. 2, pp. 253-262; Mélin, *supra* n. 2, pp. 233-242.

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– both specific assets and collections of indefinite assets as a whole which change from time to time – belonging to the debtor which are situated within the territory of another Member State at the time of the opening of proceedings.'

The cooling-off period must not be confused with a general moratorium, during which any commencement or continuation of individual actions or individual proceedings concerning the debtor's assets, rights, obligations or liabilities is stayed. Such a moratorium exists in Dutch law as well. An exception is made with respect to secured claims. In principle, the moratorium does not apply to secured creditors. They can exercise their rights if there were no insolvency proceedings at all. However, there is an exception to this exception: the cooling-off period. The cooling-off period is a period during which the exercise of rights *in rem* is suspended, or more precisely, rights *in rem* can only be exercised if the court gives permission to do so. In other words: when the court orders a cooling-off period, there is a certain period during which secured creditors cannot exercise their rights unless they have permission from the court, despite the rule that they can, in principle, exercise their rights if there were no insolvency proceedings. The objective of a cooling-off period is to give time to the liquidator to investigate the debtor's situation, and to prevent creditors who claim they have a right *in rem* from removing assets before the liquidator can verify their claims. Moreover, if the secured creditors would exercise their rights by removing assets, this could hamper a reorganisation or a transfer of a company going concern, which may be in the interest of the secured creditors as well. The cooling-off period can be ordered by a separate court decision. In theory, the cooling-off period is optional, by which I mean that it is up to the court which opens the insolvency proceeding to decide whether or not to order a cooling-off period. In practice, courts always order a cooling-off period. Article 63(a)(2) of the Dutch Bankruptcy Act states that the court which orders a cooling-off period can lay down certain conditions with respect to the cooling-off period itself or with respect to the exercise of certain rights, by which is meant the rights of the secured creditors. The law does not specify these conditions. One could think of the condition that the liquidator provides some guarantee that the secured creditors do not end up in a worse position because of the temporary impossibility to exercise their rights. As far as I know, courts do not lay down such conditions very often. The cooling-off period can be ordered for two months at most, and can be extended by two months only once.

The question I would like to answer is the following: does a cooling-off period, ordered by a Dutch court, have effect in other Member States, or does Article 5 prevent this? As we shall see, Article 5(1) contains a 'hard and fast rule'.[13] First, I shall elaborate on the hard and fast nature of the rule. Secondly, I shall answer the question of whether the hard and fast nature of the rule is relevant with respect to answering the question of whether the cooling-off period is cov-

13. The term 'hard and fast rule' was introduced with respect to this issue by Dirix and Sagaert, *supra* n. 12.

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ered by Article 5. My answer to that question will be no, and so I ask myself which factors do decide whether a cooling-off period is covered by Article 5 or not. My answer will be that material aspects are decisive and that, under certain circumstances, the cooling-off period can have effect in other Member States.

3.2 The hard and fast rule

If we want to understand the meaning of Article 5, we first have to take a look at Article 4. As we have seen, Article 4 refers to the *lex concursus* as the applicable law. Article 4 has many consequences. Some of those consequences are not desirable. One of those undesirable consequences that was envisaged by the drafters of the Insolvency Regulation was the following. Let us suppose that a creditor has a right *in rem*, vested in a good which is situated in a Member State other than the Member State where the debtor has its centre of main interests. Let us also suppose that the *lex concursus* contains the rule that the opening of an insolvency proceeding would affect rights *in rem*, vested in goods that belong to the debtor. In that case, the insolvency proceeding opened in the Member State of the debtor's centre of main interests would affect the right *in rem* vested in the good in the other Member State. In the hypothesis that only Article 4 applies, this would mean that the right *in rem*, vested in that other Member State, would be affected by that specific rule in the *lex concursus*. The drafters of the Insolvency Regulation were of the opinion that this consequence would be going too far.

What could be the underlying reason for this? One reason one could think of is that a creditor stipulates a right *in rem* in case something goes wrong, i.e., the debtor cannot pay his debt. If something *does* go wrong, he must be certain that he can exercise this right *in rem*. The creditor would not have bargained for an infringement of his right *in rem* as the result of the application of the *lex concursus*. He must not be taken by surprise when he finds out that his right *in rem* is affected by the opening of an insolvency proceeding in another Member State. This in itself is not convincing. Every person is supposed to know the law, including the Insolvency Regulation. If one enters into an agreement with someone in another Member State, one should take into account that the law of that Member State applies to the insolvency proceeding to which that partner to the contract is subjected. Yet in the Virgós/Schmit Report it is stated that rights *in rem* can only properly fulfil their function in so far as they are not more affected by the opening of insolvency proceedings in other Member States than they would be by the opening of national insolvency proceedings.[14]

Maybe the reason for Article 5 was the possibility that a right *in rem* vested in a good in Member State A would be affected by the opening of an insolvency proceeding in Member State B and this would hamper trade between Member States.

14. Virgós/Schmit Report, para. 97.

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Anyway, the one initial objective of the drafters of the Regulation was to prevent the possibility that the opening of an insolvency proceeding in a Member State could affect a right *in rem* vested in a good that was situated in another Member State. They wanted to draft an article having the following as its essence: if the *lex concursus* contains a rule which states that the opening of the insolvency proceeding affects rights *in rem*, that rule does not apply to rights *in rem* vested in goods which are located in a Member State other than the Member State where the insolvency proceeding has been opened. It is useful to bear in mind that that rule does not refer to any other law than the *lex concursus* as the applicable law. It does not, for example, determine the *lex rei sitae* as the law which applies to the effects of opening of an insolvency proceeding to rights *in rem*. It simply excludes a rule of the *lex concursus*, without replacing that rule with a rule from another national law.

When the drafters had decided to include an article with such a content, they asked themselves the following: but what if the *lex rei sitae* also contains a rule which says that the opening of an insolvency proceeding affects rights *in rem*? The question that arose was: should we not say that in such circumstances the secured creditor must accept that his right *in rem* is nevertheless affected by the opening of the insolvency proceeding? After all, the secured creditor is prepared to accept the possibility of an infringement of his right *in rem* if the debtor would be subjected to an insolvency proceeding in the state of the *lex rei sitae*. Even if the debtor was subjected to an insolvency proceeding in another state, the secured creditor even may have thought – mistakenly – that his right *in rem* would be affected according to the *lex rei sitae* and not by the *lex concursus*.

Those who say that the *lex rei sitae* should play a role adhere to what I call the 'soft and slow rule'. According to this rule, rights *in rem* can be affected by the opening of the insolvency proceeding if the *lex rei sitae* contains such a rule. One could think of two variants of the soft and slow rule. The first one is that if both the *lex concursus* and the *lex rei sitae* contain a rule according to which rights *in rem* are affected by the opening of an insolvency proceeding, the rule in the *lex concursus* does not apply to rights *in rem* vested in goods which are situated in another Member State, and is replaced by a similar rule in the *lex rei sitae*. The second variant is that the *lex concursus* nevertheless applies. If the *lex concursus* contains a rule according to which rights *in rem* are affected by the opening of an insolvency proceeding, that rule does not apply to rights *in rem* vested in goods which are situated in another Member State, but if the *lex rei sitae* also contains a rule according to which the opening of an insolvency proceeding affects rights *in rem*, the *lex concursus* applies nevertheless. In the second variant, an exception to an exception is made.

The drafters did not choose the soft and slow rule, but the hard and fast rule. According to the hard and fast rule, rights *in rem* can never be affected by the opening of an insolvency proceeding, even if both the *lex concursus* and the *lex rei sitae* would contain such a rule, provided that the rights *in rem* are vested in

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goods which are situated in a Member State other than the Member State where the insolvency proceeding has been opened.

What could be the rationale of the hard and fast rule? The rationale cannot be to protect the secured creditor against an unexpected infringement of his right *in rem*, because, in the hypothesis that Article 5 had not yet been drafted, he had accepted the possibility or should have accepted the possibility that his right *in rem* would be affected by the opening of an insolvency proceeding. On the contrary: in the view of the adherents to the hard and fast rule, it is undesirable that the secured creditor can be surprised by the application of the *lex concursus*. That supposes that in their view the secured creditor had accepted the possibility or should have accepted the possibility of an infringement of his right *in rem* as a result of the *lex rei sitae*. However, as a result of the hard and fast nature of the rule, the fact that his right *in rem* is not affected at all simply falls into his lap only because his debtor is subjected to a main insolvency proceeding in another Member State. The rationale of the hard and fast nature of the rule cannot be to protect the secured creditor. This rationale must be something else. The rationale was, so to speak, to protect the liquidator: in the situation where Article 5 had contained a soft and slow rule, the liquidator would have the obligation to acquaint himself with the content of the *lex rei sitae*. See in this respect two 'founding fathers' of the Regulation. Balz wrote:

> 'Such an approach [the soft and slow rule, AJB] was rejected, essentially because considerable complexity would have been created by combining the effects of two insolvency laws and also because liquidators might be at loss when asked to apply foreign insolvency laws.'[15]

Virgós wrote, not in the Virgós/Schmit Report, but somewhere else:

> 'The reason for this [the hard and fast rule, AJB] is clear: to avoid complex forms of regulation which may work well within individual cases, but which require a high level of expertise and are difficult to administer in a collective setting.'[16]

This is only partly convincing. It is true that it is difficult for a liquidator to find out what the law of another Member State says about the effects of an insolvency proceeding with respect to rights *in rem*. On the other hand, if he *does* know the law of another Member State, his fingers may be itching to save money for the estate by applying the rules which affect the rights *in rem*, but he cannot do anything about this.

Let us now take a look at Article 6 of the Insolvency Regulation, with respect to set-off by way of an intermezzo. The gist of Articles 4 and 6 is that, in prin-

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15. M. Balz, 'The European Convention on Insolvency Proceedings', 70 *American Bankruptcy Law Journal* (1996) pp. 485 et seq., esp. p. 509.

16. M. Virgós, 'The 1995 European Convention on Insolvency Proceedings: An Insider's View', *Forum internationale* (1998) no. 25, pp. 19-20.

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ciple, set-off is governed by the *lex concursus*. If the *lex concursus* would say that set-off is not possible, we have to look at the *lex causae*. If that law permits set-off, set-off is possible nonetheless, despite the fact that the *lex concursus* prohibits it. This is a soft and slow rule. Why did the drafters of the Insolvency Regulation choose the hard and fast rule with respect to rights *in rem* and why did they choose a soft and slow rule with respect to set-off? I can think of two reasons.

The first reason is that with respect to rights *in rem* and the wording of Article 5, a hard and fast rule leads to an improvement to the rights of the counterparty of the debtor: the secured creditor. Let us suppose that the drafters of the Regulation had adopted a soft and slow rule with respect to rights *in rem*. In that hypothesis we would have to take the *lex rei sitae* into account. If the *lex rei sitae* would not state that the opening of insolvency proceedings affects rights *in rem*, the exception to the *lex concursus* would be left intact: the opening of the insolvency proceeding does not affect rights *in rem*. But if the *lex rei sitae* would state that the opening of an insolvency proceeding affects rights *in rem*, the exception to the *lex concursus* would be undone: the opening of the insolvency proceeding would indeed affect rights *in rem*. This is not the case with respect to set-off and the wording of Article 6: there it is a soft and slow rule which leads to an improvement of the position of the counterparty of the debtor: the person who wants to exercise a right to demand set-off. If the *lex concursus* would affect the right to demand set-off, the debtor's counterparty could nevertheless exercise this right if the *lex causae* would permit this.

The second reason I can think of is that there is a huge variety of infringements of a right *in rem*, whereas with respect to the question of whether one can exercise his right to demand set-off in a specific case, the possible answers are mostly just yes or no. A right *in rem* can be affected in various ways: the secured creditor may be obliged to contribute to the costs of the insolvency proceeding, or he may exercise his right *in rem* under specific circumstances only. It is difficult for the liquidator to compare these different infringements.

I conclude with respect to the nature of the hard and fast rule. Whether we like it or not, Article 5 contains a hard and fast rule. This means that even if both the *lex concursus* and the *lex rei sitae* determine that the opening of an insolvency proceeding affects rights *in rem*, these rights *in rem* cannot be affected.

Now I come to the question of whether the cooling-off period falls within the scope of Article 5. In other words: if a Dutch court orders a cooling-off period, does this have consequences for a right *in rem* vested in a good situated in another Member State? At first sight, it may be tempting to say that since Article 5 contains a hard and fast rule, a Dutch cooling-off period cannot have consequences in another Member State. This reasoning is erroneous, however. This would be a traditional mistake: confusing the private international law aspects with material law aspects. The question of whether or not we have to take the *lex rei sitae* into account has nothing to do with the question of what, exactly, is an infringement of a right *in rem*, and neither does it concern the question of as

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a result of what is a right *in rem* affected. To illustrate this, I would like to ask two rhetorical questions. Do floating charges fall within the scope of Article 5? And does a reservation of title fall within the scope of Article 5? The answer to the first question is yes,[17] and the answer to the second question is no, because Article 7 deals with that subject. These questions deal with the material scope of Article 5. The answer to such questions does not depend on the answer to the question of whether Article 5 is a hard and fast rule or a soft and slow rule.

Therefore, in order to discover whether or not the cooling-off period falls within the scope of Article 5, we must analyse the material scope of Article 5. Two aspects of Article 5 attract attention: (1) rights *in rem* must not be affected, and (2) they must not be affected by the *opening of an insolvency proceeding.*

(1) Rights *in rem* must not be affected. As we have seen, the cooling-off period suspends the exercise of a right *in rem*. It does not affect the right *in rem* itself. After the cooling-off period has expired, the right *in rem* can be exercised to its full extent. The exercise of the right *in rem* is affected, not the right *in rem* itself. Does this suffice to say that a cooling-off period does not affect rights *in rem*? I think that, in itself, that is not sufficient. The bottom line of Article 5 is that the position of a creditor who has a right *in rem* should not be adversely affected by an insolvency proceeding in another Member State. The loss suffered by a suspension of the *exercise* of a right *in rem* is as relevant as the loss suffered by the infringement of a right *in rem itself*. However, as we have seen, Article 63(2) of the Dutch Bankruptcy Code offers a possibility for the court to compensate the loss caused by the suspension of the exercise of the right *in rem*. The court can attach a condition to the cooling-off period. One of the conditions the court can impose is that the liquidator provides security with respect to the loss that the liquidator may suffer by the suspension of the exercise of his right *in rem*. As far as I know, the Dutch courts have so far never used this possibility. That is a pity. I would like to encourage the Dutch courts to do so. If they do, the Dutch cooling-off period can have consequences in another Member State. This is the case if the court orders the liquidator to provide security with respect to the loss that the liquidator may suffer by the suspension of the exercise of his right *in rem*. If the court would so order, the bottom line of Article 5 (the position of a creditor who has a right *in rem* should not be adversely affected by the opening of an insolvency proceeding in another Member State) would be complied with.

(2) Rights *in rem* must not be affected by the *opening of an insolvency proceeding.* A cooling-off period is not *ex lege* the result of the opening of an insolvency proceeding. The liquidator needs a separate court decision ordering a cooling-off period. The conclusion is that the wording of Article 5 is not sufficient to say that the cooling-off period falls within the scope of Article 5. One could argue against this: whether a loss is caused by the opening of the insolvency proceeding itself or by a separate decision, what does it matter? In both cases the position of the secured creditor is adversely affected, which is not al-

17. See the Virgós/Schmit Report, para. 104.

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lowed under Article 5. I do not agree. In the first place, the court can take into account all circumstances in a separate decision. It can, as we have seen, order the liquidator to provide security with respect to the loss that the owner of the right may suffer by the suspension of the exercise of his right *in rem*. When the suspension of the exercise of the right *in rem* follows from the opening of the insolvency proceeding itself, the court cannot distinguish between creditors who have a right *in rem* vested in a good situated in the Member State where the insolvency proceeding is opened and creditors who have a right *in rem* vested in a good in another Member State. Therefore, when the suspension of the exercise of the right *in rem* follows from the opening of the insolvency proceeding itself, the court cannot order the liquidator to provide security with respect to only those creditors who have a right *in rem* vested in a good situated in another Member State.

The conclusion is that Article 5 does not preclude that the cooling-off period has consequences in another Member State if the position of the secured creditor is not adversely affected by the cooling-off period.

4. THE *GERMAN GRAPHICS* CASE[18]

A German company, German Graphics, sold machinery to a Dutch company, Holland Binding, and stipulated a reservation of title in its favour. Subsequently, Holland Binding was subjected to an insolvency proceeding in the Netherlands, which was the main proceeding. A German court granted the application by German Graphics for the adoption of protective measures with respect to some of the machinery, which was situated in the Netherlands, based on the reservation of title clause. A Dutch court, responsible for granting interim measures, declared the judgment of the German court to be enforceable, but that decision was revoked by a higher court. Then the case was brought before the Dutch Supreme Court. The question was whether the decision of the German court to order protective measures (1) could be recognised in the Netherlands, and if so (1a) whether this was on the basis of the Insolvency Regulation, or (1b) on the basis of the so-called Brussels I Regulation,[19] or was it a decision which (2) could not be recognised at all, neither on the basis of the Insolvency Regulation nor on the basis of the Brussels I Regulation?

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18. ECJ 10 September 2009, Case C-292/08, *German Graphics* v. *Van der Schee*, [2009] *ECR* I-8421. See also S. Bariatti, 'Recent Case-law Concerning Jurisdiction and the Recognition of Judgments under the European Insolvency Regulation', 73 *Rabels Zeitschrift für Ausländisches und internationales Privatrecht* (2009) pp. 629-659; L. Carballo Piñeiro, '*Vis attractiva concursus* in the European Union: Its Development by the European Court of Justice', *InDret Revista para el análisis del derecho* (2010) (also available at <http://www.indret.com>).

19. Council Regulation (EC) No. 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement in civil and commercial matters, *OJ* 2001, L 12.

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Why is it relevant to know the answer to this question? If the decision concerned is a decision in the field of insolvency law, it can be recognised and enforced on the basis of the Insolvency Regulation. If the decision is not a decision in the field of insolvency law, but a decision in civil and commercial matters, it can be recognised and enforced on the basis of the Brussels I Regulation. If it is not a decision in civil or commercial matters, or if it is a decision which is excluded from the scope of the Brussels I Regulation, it is left to domestic law whether it can be recognised or enforced, unless it is a decision which is dealt with by another Regulation, for instance on matrimonial matters, which is obviously not the case in the *German Graphics* decision.

Article 16 of the Insolvency Regulation deals with judgments opening insolvency proceedings handed down by a court that has jurisdiction to open the main proceeding, and it states that such decisions are recognised in all the other Member States from the time that it becomes effective in the state where it is opened. The Dutch Supreme Court ruled that the decision of the German court in the *German Graphics* case was not a decision as meant in Article 16. It seems rather obvious that the German decision to order protective measures is not a decision as meant in Article 16.

Subsequently the Dutch Supreme Court ruled that it was not a decision as meant in Article 25(1) of the Insolvency Regulation either.[20] Article 25(1) deals with (a) decisions concerning the course and closure of the proceeding, handed down by the court that opened the proceeding, (b) judgments deriving directly from the insolvency proceeding and which are closely linked therewith, 'even if they were handed down by another court', and (c) judgments relating to preservation measures after taken the request for the opening of the insolvency proceeding.[21] It goes without saying that the German decision was not a decision as meant in Article 25(1)(a).

With respect to decisions as meant in Article 25(b), the Dutch Supreme Court ruled that the German decision was not a decision deriving directly from the insolvency proceeding and which is closely linked with the Dutch insolvency proceeding, because it was not handed down by 'the same court that opened the insolvency proceeding, nor by another court'. It is clear that the German decision was not handed down by the court that had opened the insolvency proceeding, but by 'another court'. The Dutch Supreme Court ruled that by 'another court' the following is meant: a court in the same Member State as the court that had opened the insolvency proceeding. The text of Article 25(1)(b) is not restricted to the courts of the Member State where the insolvency proceeding was opened. However, paragraph 194 of the Virgós/Schmit Report reads:

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20. See, with regard to Art. 25: Duursma-Kepplinger, Duursma and Chalupsky, eds., *supra* n. 2, pp. 419-443; Mélin, *supra* n. 2, pp. 358-372.

21. The lettering (a), (b) and (c) does not occur in the text of Art. 25(1); this was added by the author.

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> 'Recognition and enforcement of such judgements are always governed by the [Insolvency Regulation] whether they are adopted by the bankruptcy court or by an ordinary court, *as could be the case under national law*.'[22]

The words in italics are a strong indication that by 'another court' the following is meant: a court of the Member State where the insolvency proceeding was opened, since it is extremely unlikely that the national law of the Member State where the insolvency proceeding is opened would hand over competence to a court of another Member State. I agree with the Dutch Supreme Court that the German decision was not a decision as meant in Article 25(1)(b), but the grounds that were given by the Dutch Supreme Court could have been more extensive.

With respect to Article 25(1)(c) one could have some doubt at first sight. The wording of the text does not exclude preservation measures ordered by another court than the court that opened the insolvency proceeding, not even a court from another Member State. On the other hand, with respect to decisions as meant in Article 25(1)(c), the phrase 'even if they were handed down by another court' is lacking. Paragraph 198 of the Virgós/Schmit Report reads:

> 'The same system of recognition and enforcement shall apply to preservation measures ordered by a court having jurisdiction under Article 3(1) after the request for the opening of the insolvency proceedings.'

This means that only preservation measures ordered by the court that opened the insolvency proceeding must be recognised and enforced on the basis of Article 25(1)(c). With respect to both sub. (b) and sub. (c), it is clear that what is meant are decisions given in favour of the liquidator, who might have requested them. It would be illogical for Article 25(1) to provide a rule with regard to the recognition and enforcement of decisions against the estate. It is therefore correct that the Supreme Court ruled in one and the same breath that the German decision was not a decision as meant in Article 25(1)(a), (b) and (c).

The following step in the reasoning of the Supreme Court was that it asked itself whether the German decision was a decision as meant in Article 25(2). Article 25(2) reads:

> 'The recognition and enforcement of judgments other than those referred to in paragraph 1 shall be governed by the [Brussels I Regulation], *provided that that [Regulation] is applicable*.'[23]

The question of the Dutch Supreme Court centred on the following. Suppose there is a national court which is responsible for enforcing a foreign judgment. That court asks itself whether it is able to declare that that foreign judgment should be recognised for the purposes of Article 25(2) of the Insolvency Regu-

22. Emphasis added.
23. Emphasis added.

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lation on the basis of the Brussels I Regulation. The question that the Dutch Supreme Court submitted to the Court of Justice of the European Communities was the following: must that national court determine whether the foreign judgment falls outside the material scope of the Brussels I Regulation?

In my opinion, the question is not well phrased. When a court has to answer the question of whether a foreign judgment must be recognised on the basis of the Brussels I Regulation, it seems rather obvious that that court must determine whether that foreign judgment falls within or outside the scope of that Regulation. That goes without saying. The fact that the court must ask that question for the purposes of the Insolvency Regulation does not alter the situation. The words 'provided that that Regulation is applicable' do not alter the situation either. It is therefore not surprising that the Court of Justice gave the most natural answer:

> 'Article 25(2) of the [Insolvency Regulation] must be interpreted as meaning that the words "provided that the [Brussels I Regulation] is applicable" imply that, before it can be concluded that the recognition and enforcement provisions of the [Brussels I Regulation] are applicable to judgments other than those referred to in Article 25(1) of the [Insolvency Regulation], *it is necessary to determine whether such judgments fall outside the material scope of the [Brussels I Regulation]*.'[24]

I do not think that the Court of Justice lost much sleep in answering this question. Needless to say, I do agree with this decision.

The second question by the Dutch Supreme Court relates to Article 2(b) of the Brussels I Regulation. This article reads:

> 'The Regulation shall not apply to bankruptcy, proceedings relating to the winding-up of insolvent companies or other legal persons, judicial arrangement, compositions and analogous proceedings.'

This second question boils down to the following: what is the nature of a decision concerning a reservation of title *against a debtor that is subjected to an insolvency proceeding*: a decision in the field of insolvency law, or a decision in the field of civil and commercial law?

The question seems to be somewhat contrived. The Dutch Supreme Court had already ruled that the German decision was not a decision concerning the course and closure of the proceeding, nor a judgment deriving directly from the insolvency proceeding and which was closely linked therewith, and neither that it was a judgment relating to preservation measures after taken the request for the opening of the insolvency proceeding. Did the Dutch Supreme Court really believe that it was nonetheless conceivable that such a decision is a decision related to insolvency in the sense of the Brussels I Regulation?

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24. Emphasis added.

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The third question by the Dutch Supreme Court was whether Article 4(2)(b) was relevant. This provision states that the *lex concursus* determines, *inter alia*, the assets which form part of the estate.

The Court of Justice rephrased the second and the third question by the Dutch Supreme Court as follows:

> 'The referring court asks, in essence, whether as a result of the opening of an insolvency proceeding against a purchaser, where the asset covered by the reservation of title is situated in the Member State of the opening of those proceedings, an action brought by the seller against that purchaser based on the reservation of title clause, is excluded from the scope of application of [the Brussels I Regulation].'

After having referred to the respective Preambles to the Brussels I Regulation and the Insolvency Regulation, the Court of Justice ruled that the scope of the Brussels I Regulation should be broadly interpreted and that the scope of the Insolvency Regulation should not be broadly interpreted. Furthermore, the Court of Justice referred to its previous decisions in the cases of *Gourdain-Nadler*[25] and *Seagon-Deko Marty*.[26] In its decision in the case *Gourdain-Nadler*, the Court of Justice ruled that an action is related to bankruptcy if it derives directly from the bankruptcy and is closely linked to proceedings for realising the assets or judicial supervision. These considerations led the Court of Justice in the case of *German Graphics* to the conclusion that the action concerning a reservation of title clause constitutes an independent claim, as it is not based on the law of the insolvency proceeding and requires neither the opening of such a proceeding nor the involvement of a liquidator.

I agree with this decision. In this respect, the decision in *Gourdain-Nadler* should be recalled. In this case, the central question was whether a specific action was an action in the field of insolvency law or an action in the field of civil and commercial law. It concerned an action against a manager of a company, which was the subject of an insolvency proceeding, to bear part of the company's debts. When we analyse the decision of the Court of Justice in the *Gourdain-Nadler* case, we can find eight elements which determined that the action was an action in the field of insolvency law:

1. The law on bankruptcy laid down the rules with respect to this action;
2. The action can only be obtained from the bankruptcy court;
3. It is only the liquidator, apart from the court which can make the order of its own motion, who can make the application;
4. The liquidator can make this application on behalf of and in the interest of the general body of creditors with a view to the partial reimbursement of the creditors by respecting the principle that they rank equally and by taking any lawfully acquired preferential rights into account;

25. ECJ 22 February 1979, Case C-133/78, *Gourdain* v. *Nadler*, [1979] *ECR* 733.
26. ECJ 12 February 2009, Case C-339/07, *Seagon* v. *Deko Marty Belgium*, [2009] *ECR* I-767.

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5. The application derogates from the general rules of the law of liability;
6. The period of limitation runs from the date when the final list of claims is drawn up and is suspended for the duration of any scheme of arrangement which may have been entered into;
7. If the application succeeds, it is the general body of creditors which benefits, some assets being added to the funds to which they are entitled, as happens when the liquidator establishes a claim which benefits the general body of creditors;
8. The court may open the insolvency proceeding against those managers who have been responsible for part or all liabilities of a legal person and who do not discharge the said liabilities, without having to verify this.

When we look at these elements, we should not be surprised that in the *German Graphics* case the Court of Justice ruled that the action of the seller against the purchaser, based on the reservation of title, was not an action in the field of insolvency law. It was not the German Bankruptcy Act that provided the rules for this action, the action was not requested from the German bankruptcy court, it was not the liquidator who made the application, the application was not made on behalf of and in the interest of the general body of creditors, the application did not derogate from the general rules, and the limitation period did not depend on an event in an insolvency proceeding, just to refer to the first six elements in the *Gourdain-Nadler* decision.

This is most certainly unsurprising because the Dutch Supreme Court had already ruled that the German decision was not a decision given by the 'insolvency judge'.[27]

In asking the second question, the Dutch Supreme Court not only referred to Article 2 (b) of the Brussels I Regulation, but also to Article 7(1) of the Insolvency Regulation. Article 7(1) of the Insolvency Regulation is related to reservation of title and provides an exception to Article 4, similar to Article 5 with respect to rights *in rem*. Article 7(1) governs the insolvency of the purchaser of an asset, by allowing the seller to preserve his rights based on the reservation of title, provided that the asset is located in a Member State other than the Member State where the insolvency proceeding has been opened.[28] Does Article 7(1) alter the conclusion that an action, based on a reservation of title against the purchaser who is insolvent, is an action in the field of civil and commercial law and is not excluded from the scope of the Brussels I Regulation? The Court of Justice determined that this is not the case, and rightly so. The Court of Justice ruled that Article 7(1) only constitutes a substantive rule intended to protect the seller.[29] Moreover, Article 7(1) applies only to assets which are situated in a Member State other than the Member State where the insolvency proceeding has been opened. In the *German Graphics* case, the Netherlands was both the

27. *Hoge Raad* 20 June 2008, no. R07/124HR, *NJ* 2008 No. 354, para. 4.5.
28. Virgós/Schmit Report, para. 113.
29. Para. 36 of the decision.

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Member State where the insolvency proceeding had been opened and the Member State where the assets were located.

The third question that was posed by the Dutch Supreme Court concerned Article 4(2)(b). It should be recalled that this article states that the *lex concursus* determines the assets which form part of the estate and the treatment of assets acquired by or devolving on to the debtor after the opening of the insolvency proceeding. The Court of Justice made short shrift of this question by saying that this provision has no effect on the scope of application of the Brussels I Regulation. I agree.

It is my impression that not everybody sufficiently understands the meaning of Article 4(2)(b). The question of whether the debtor is the owner of an asset is governed by the *lex rei sitae*. If so, a subsequent question is whether the asset belongs to the estate, in other words, whether the asset is added to the funds to which the general body of creditors is entitled. Especially with respect to natural persons, there are some assets to which the creditors are not entitled, because they are essential for everyday life. With respect to the assets acquired after the opening of the insolvency proceeding, the English, German and French versions of Article 4(2)(b) are less precise than the Dutch version. The English, German and French versions simply say that the *lex concursus* governs the *treatment* of these assets. The Dutch version says that the *lex concursus* determines whether assets, acquired after the opening of the insolvency proceeding, *form part of the estate*.

After all, the gist of this decision is that an action based on a reservation of title against the purchaser who is insolvent is an action in the field of civil and commercial law and is not excluded from the scope of the Brussels I Regulation. Article 7(1) of the Insolvency Regulation, which deals with reservation of title in the case of a purchaser who is subjected to an insolvency proceeding, does not alter that conclusion. In all honesty, it would have been surprising if the Court had ruled otherwise.

Is the same true with respect to the situation which is dealt with in Article 7(2) with regard to an insolvency proceeding against the seller? That provision states that the opening of an insolvency proceeding against the seller does not prevent the purchaser from acquiring the good. In other words: if the purchaser continues to make payments, he shall acquire the good.[30] If the purchaser does indeed pay, but the liquidator takes the position that the purchaser does not become the owner of the good, the owner can bring an action against the liquidator. I do not see any reason why such an action would be of any another nature than the action in the *German Graphics* case.

However, what if the liquidator brings an action? Let us suppose that the debtor sells a good to another party, stipulating a reservation of title, and he is subsequently subjected to an insolvency proceeding. The liquidator makes an application for the adoption of protective measures. Does such an action constitute an action in the field of insolvency law? It is true that the liquidator makes

30. Virgós/Schmit Report, para. 114.

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the application and that he does so on behalf of and in the interest of the general body of creditors. Nevertheless, I do not think that such a claim is a claim in the field of insolvency law. I am not aware of the situation in other Member States, but in the Netherlands such an action is not brought in a bankruptcy court. The law which lays down rules in respect of an action based on reservation of title will not be the law of bankruptcy. Maybe a Bankruptcy Act lays down certain rules with regard to the question of under which circumstances a liquidator can apply for the adoption of protective measures. For instance, under Dutch law the liquidator needs a specific authorisation from the court to file a lawsuit. However, once that specific authorisation has been granted, the application for the adoption of protective measures will be the same as any other application for the adoption of protective measures. In other words: the mere fact that one of the parties is a liquidator, even if he is the plaintiff, does not mean *eo ipso* that the claim is a claim in the field of insolvency law.

5. CONCLUDING REMARKS

The Insolvency Regulation entered into force about eight years ago. As far as I know, the Court of Justice of the European Communities has been asked to answer prejudicial questions on ten occasions.[31] Sometimes the prejudicial questions dealt with essential issues, sometimes they dealt with minor problems. Sometimes lawyers want to hear from courts how far they can stretch the rules, and sometimes the decisions concerned real ambiguities in the text of the Regulation. In this article, I have tried to draw the reader's attention to some of these ambiguities, but there are many more. My first conclusion is that the *lex concursus* governs the question of whether a third party who claims to have purchased a movable unregistered asset or an asset gratuitously from a person who was subjected to an insolvency proceeding is protected. The second conclusion is that the Dutch cooling-off period can have effects in other Member States, provided that some conditions are met. The third conclusion is that the Court of Justice of the European Communities has ruled that an action based on a reservation of title against the purchaser who is insolvent is an action in the field of civil and commercial law and is not excluded from the scope of the Brussels I Regulation, and that Article 7(1) of the Insolvency Regulation does not alter this conclusion.

31. ECJ 17 January 2006, Case C-1/04, *Staubitz-Schreiber*, [2006] *ECR* I-701; *Eurofood* case, *supra* n. 35; *Seagon* case, *supra* n. 26; ECJ 21 January 2010, Case C 444/-07, *Probud*; Case C-148/08, *Mejnertsen* (removed from the register); *German Graphics* case, *supra* n. 18; Case C-396/09, *Interedil* (pending); Case C-112/10, *Zaza Retail* (pending); Case 191/10, *Rastelli Davide* v. *Hidoux* (*Médiasucre*) (pending); Case C-213/10, *F-Tex Sia* v. *Jadecloud Vilma* (pending).

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