Case study – secondary insolvency proceedings against a solvent debtor

Specific problems arising in a few Polish-French cases.

Deficiencies of the old EIR vs. changes introduced by the recast EIR

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A real-life case: Christianapol

- CJEU judgment of 22 November 2012, Case C-116/11, Bank Handlowy and Adamiak
- The debtor, Christianapol sp. z o.o., was a company established in Poland, producing furniture. Its factory, all assets and employees were located in Poland.
- Christianapol sp. z o.o. was fully controlled by a French group of companies Cauval Industries.
- Tribunal de commerce de Meaux (Meaux Commercial Court) (France) opened French *sauvegarde* proceedings against the debtor. *Sauvegarde* proceedings were opened in parallel against several companies in the group, incorporated in several Member States → effort to coordinate restructuring within the group

A real-life case: Christianapol

- *Sauvegarde* proceedings are applicable to debtors who are **not yet insolvent but they are threatened by insolvency**. Its purpose is to prevent insolvency and to restructure the debtor
- the entire estate of the debtor was located in Poland, the activities were concentrated in Poland. Economic choices controlled by the parent company in France. Decisions of the management were taken partly in Poland, partly in France → highly doubtful decision of the French court that COMI was in France
- the Polish subsidiary was functioning and solvent at the time of the opening of main proceedings in France.
- A creditor filed for the opening of secondary insolvency proceedings against Christianapol.

Concept of 'insolvency proceedings' under the EIR

- initial meaning of Article 1(1) of the old EIR
- Constitutive elements under the old EIR: collective proceedings, insolvency, divestment of the debtor, appointment of a liquidator
- „a very broad framework"; „conditions which enable proceedings to be added to the lists [in the Annexes]" (Virgos-Schmit report, paragraph 48)

Concept of ‘insolvency proceedings’

- question: how far can the term ‘insolvency proceedings’ under the old EIR include restructuring proceedings aiming at avoiding insolvency

- practice: Member States themselves proposed proceedings to be included into Annexes A and B to the old EIR → expansion beyond the original concept of insolvency proceedings

Jurisdiction to open main insolvency proceedings

- the concept of COMI
- the first court to open main proceedings maintains jurisdiction – no examination of its jurisdiction by courts in other Member States [Eurofood]

Result → „race to the court”

Possibility for an effective opening of main proceedings under questionable grounds for jurisdiction

main problem area– groups of companies, insolvency proceedings against subsidiaries in other Member States.

Consequence for secondary proceedings under the old EIR

- *Secondary proceedings as 'second prize' for the 'losing court' in a conflict over jurisdiction*

- *no examination of insolvency (grounds to open proceedings) after the request to open secondary proceedings → 'automatism of opening' (Art. 27 old EIR) – duty to open or right to open proceedings?*

- *secondary proceedings opened always as winding-up proceedings (Art. 27 old EIR, Annex B)*

Back door to automatic opening of winding-up insolvency proceedings against solvent and functioning debtors [under the old EIR]

Economic consequence

- even if COMI is located in France (which was doubtful but the French court was first to open main proceedings → Eurofood), any restructuring efforts would necessarily need to be concentrated in Poland

Result of application of the old EIR (as interpreted in Eurofood)

- *Unnecessary opening of secondary proceedings as winding-up proceedings which includes the entire estate of a solvent, functioning debtor.*

- *Hampering of restructuring efforts in main proceedings.*

- *A disastrous blow to the debtor's reputation, resulting in a likely loss of business partners.*
- *Even if the debtor is not wound up in the result (see below) – a long period of legal uncertainty.*

Reference of the Polish court to the CJEU

- Reference by the Bankruptcy Court of Poznań lodged on 7.3.2011, Case C-116/11, Judgment of 22.11.2012

- Practical aspects of the questions raised:

- When do main proceedings end? (=how long is there a duty to open secondary proceedings?)

[the court in Poznań has lodged the reference to the CJEU already after a restructuring plan has been adopted in the French main proceedings, during the phase of the realisation of the plan]

- Can the opening of secondary proceedings be refused if the debtor is solvent?

- Should secondary proceedings be opened if it would hamper restructuring efforts in main proceedings?

CJEU judgment in Case C-116/11

- Judgment of 22 November 2011, Case C-116/11, Bank Handlowy and Adamiak v. Christianapol

- Answer to 1st question – **the moment of closure of main proceedings** needs to be established under the law applicable to main proceedings (Article 4(2)(j) old EIR), not under criteria set by the EIR → French law applies

- Answer to 2nd question – under the old EIR the court hearing the request to open secondary proceedings **could not re-examine** the insolvency of the debtor against which main proceedings had been opened in another Member State, even if those main proceedings were applicable to solvent debtors

CJEU judgment in Case C-116/11

- Answer to 3rd question – the opening of main proceedings of „protective nature" (=applicable to solvent debtors, aimed at restructuring) **permitted the opening of secondary proceedings** in another Member State, even if the secondary proceedings needed to be opened as winding-up proceedings

- The court deciding on the opening of secondary proceedings needs to „have regard to the objectives of the main proceedings and take account of the scheme of the [old] EIR, in keeping with the principle of the sincere cooperation" → <u>unanswered question:</u>

Can the opening of secondary proceedings be refused in such case?

Possibilities for rescue under the old EIR?

- *Refusal of recognition of main proceedings on public policy grounds (Article 26 old EIR)? – not justified*
- *Restructuring measures in secondary proceedings (Article 34 old EIR)*
- *Stay of liquidation in secondary proceedings (Article 33 old EIR)*
- *Sale of the debtor's enterprise as a going concern*

Changes in the recast EIR resulting from (i.a.) the Christianapol case

- **broader definition of „insolvency proceedings”** – inclusion of proceedings aiming at rescue, adjustment of debts or reorganization , also applicable in cases of only a likelihood of insolvency (Art. 1(1) EIR)

- more precise **definition of COMI** (Art. 3(1) EIR)

- **requirement to explain grounds for jurisdiction** (in particular to explain the decision on COMI) (Art. 4 EIR) and possibility to **challenge the decision to open main insolvency proceedings** (art. 5 EIR) → but no change to the principle that courts in other member states **cannot scrutinise the decision of the first court** to open main proceedings (recital 65, cf. Eurofood case)

Changes in the recast EIR resulting from (i.a.) the Christianapol case

- **reorganization possible in secondary proceedings** → removal of the limitation to winding-up proceedings in Art. 34 EIR → removal of Annex B to the old EIR listing winding-up proceedings (not needed anymore)

- no re-examination of insolvency of the debtor for the purpose of the opening of secondary proceedings only if the main insolvency proceedings required that the debtor be insolvent (Art. 34 EIR) → if main proceedings were opened against a solvent debtor, the court in the secondary jurisdiction may refuse to open secondary proceedings if law of the secondary jurisdiction requires actual insolvency of the debtor as a condition for the opening of insolvency proceedings

Changes in the recast EIR resulting from (i.a.) the Christianapol case

- introduction of „**synthetic secondary proceedings**" to avoid opening secondary proceedings – unilateral undertaking (= binding promise) of the insolvency pratictioner (liquidator) in main proceedings to satisfy creditors in the secondary jurisdiction as if secondary proceedings were opened (Art. 36 EIR)

Additional reading

- CJEU judgment of 22 November 2012, Case C-116/11- Bank Handlowy and Adamiak

- M. Porzycki, Secondary Insolvency Proceedings against a Solvent Debtor: A Polish Case Highlights Weak Points of the European Insolvency Regulation, International Corporate Rescue 2010, Volume 7, Issue 2, p. 118