ARTICLE

Conflicts under the EC Insolvency Regulation: First Come, First Served?

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It is said that the Parmalat collapse represents the largest fraud in Europe to date. The black hole which was created amounts to at least EUR 4.5 billion with over 100,000 private investors and the like directly affected, not to mention over 30,000 job losses. There are, it seems, over 400 different corporations or entities involved across the world, including substantial offshore elements including, but not limited to, the Cayman Islands, where at least one piece of intriguing litigation is in the process of working itself out, primarily with regard to which officeholder or officeholders run which corporations or entities.

Before turning in more detail to the litigation which is the subject of this article, it is perhaps important to bear a number of basic legal requirements in mind. The EC Insolvency Regulation Council Regulation (EC) No. 1346/2000, 29 May 2000, has been in force for long enough to be the provider of a significant body of case law even in the English High Court. The Regulation came into force on 31 May 2002. Since the beginning of May 2004 the 10 new States who have joined up to the European Union are also now bound by the Regulation. The Regulation permits Member States in which a debtor's 'centre of main interests' is situated to open so-called main proceedings (Article 3(c)). In the case of a corporate debtor there is a rebuttable presumption that such a centre is the location of the corporation's registered office. The Recitals to the Regulation are critical in assisting in its interpretation and implementation. Consequently, an examination should invariably be conducted into where the debtor, personal or corporate, is seen to conduct the administration of his or its interests on a regular basis as ascertainable by third parties (Recital 13). The above approach has in effect been applied by the first fully contested English decision on the Regulation, namely *Geveran Trading Company Limited v Skjevesland* [2003] BCC 209; see also *Re Daiseytek ISA Limited* [2003] BCC 562.

Main proceedings when opened in any one Member State can only be succeeded by secondary proceedings in another Member State. Article 3(3) provides that the latter must be of a winding-up nature. The law of the State of the opening of the proceedings in general determines the conditions for the opening of those proceedings as well as their conduct and closure: Article 4(2). An extensive number of illustrations of that general principle is afforded by Article 4(2), e.g. the rules governing the powers of a liquidator and the question of claims generally.

Article 2(e) defines the term 'judgment' in relation to the opening of insolvency proceedings or the appointment of a liquidator as including 'the decision of any court empowered to open such proceedings or to appoint a liquidator'. The term 'judgment' is important because Article 16(1) prescribes that any 'judgment' opening insolvency proceedings handed down by a court of a Member State which has jurisdiction pursuant to Article 3 should be recognized in all other Member States from the 'time it becomes effective in the State of the opening of proceedings'. Equally important, therefore, is the definition of the expression 'the time of opening of proceedings' in Article 2(f) which is interpreted as meaning 'the time at which the judgment opening proceedings becomes effective whether it is a final judgment or not '. The particular expression 'the time of the opening of proceedings' is not found extensively throughout the Regulation but can be found in such Articles as Article 5 which excludes third parties' rights in rem as being subject to the law of the State of the opening of proceedings with regard to assets within the territory of another Member State 'at the time of the opening of proceedings'. On the other hand it must be arguable that when Article 3 talks about the jurisdiction being afforded to the court of the Member State where the centre of main interests is situated 'to open insolvency proceedings' it can only be on the basis that it had such jurisdiction at the relevant time. Indeed Article 2(f) is extremely important because much turns on whether or not insolvency proceedings have actually been opened. There is for the moment an academic debate in England on whether an English creditors' voluntary liquidation would be regarded as opened in the absence of court confirmation. Moreover the relevant conditions which must be in place for the opening of proceedings must also be satisfied at this 'time' although as indicated above this is more a matter of necessary construction

of the relevant language rather than express importation of the phrase defined in Article 2(f).

In Ireland, unlike the United Kingdom, a provisional liquidator is treated as a liquidator for the purposes of Article 2(b) which defines the term 'liquidator' and has recourse to the persons and bodies listed in Annex C. Moreover, under Irish domestic law, if and when a liquidator is appointed, the appointment takes effect for most purposes from the date of the petition and not from the date of the subsequent winding-up order: section 220(2) Companies Act 1963. The English Insolvency Act in section 127 contains the same stipulation.

Article 16 of the Regulation provides that judgment in the sense described above is to be immediately and automatically recognized across all Member States: Recital 22 confirms this principle of immediate recognition and also emphasizes that this is in turn based 'on the principle of mutual trust'. A Member State may refuse to recognize insolvency proceedings opened in another Member State where the effects of such recognition would be manifestly contrary to the former State's public policy including its fundamental principles or the constitutional rights and liberties of the individual: Article 26. Article 26 will be dealt with further below.

Eurofood IFCS Limited was a wholly-owned subsidiary of Parmalat, an Italian corporation. As with so many other Parmalat subsidiaries across the world, Eurofood's business was the provision of financial services and related activities to companies within the Parmalat Group. By January 2004 Eurofood was insolvent. Any assets it owned were worthless and were largely, if not exclusively, debts due from other Parmalat entities. Despite having a Dublin registered office, Eurofood had two Italian directors who acted alongside two Irish directors. Parmalat went into what is called extraordinary administration in Italy on 9 February 2004. As is well known, in insolvency circles at least, Signor Bondi was appointed administrator by the Italian Ministry of Productive Activities.

Following the formal collapse of Parmalat, Eurofood's two Italian directors resigned. Until that point all board meetings of Eurofood except one had taken place in Dublin. Eurofood conducted its day-to-day administration under the terms of an administration agreement which was subject to Irish law and which contained an Irish jurisdiction clause. On 27 January 2004 a bank presented a petition for the winding up of Eurofood to the Irish court, alleging a debt of USD 3.5 million. There were numerous supporting creditors, mainly noteholders who were owed in excess of USD 122 million. On the same day the court appointed a provisional liquidator and the hearing of the winding-up petition was adjourned to a later date. On 30 January 2004 the Irish provisional liquidator notified Signor Bondi of his appointment as provisional liquidator. On 9 February 2004 Signor Bondi was appointed extraordinary administrator and on 13 February 2004 the Irish provisional liquidator was served with notice of a hearing due to take place on 17 February at which a court in Parma was to determine an application with a view to declaring the formal insolvency of Eurofood. By then Signor Bondi had purported to appoint 3 Italian directors to Eurofood, remove an Irish director and seek the declaration referred to in the Italian court. The latter court issued a direction that interested parties be given notice of the hearing: however, neither the bank which had issued the petition in Ireland nor the supporting noteholders were, it seems, given any notice.

On 16 February 2004 the Irish provisional liquidator, who admittedly had been given notice shortly before the Italian hearing but was not given a copy of the Italian administrator's petition, applied to the Irish court for leave to appear at and participate at the hearing before the court in Parma. On 20 February 2004 the Italian court, having heard submissions from the provisional liquidator as well as from Signor Bondi and in the event from other interested parties including the bank which had issued the Irish winding-up petition, formally declared that Eurofood was insolvent and that its centre of main interests was Italy. It also held that the appointment of the provisional liquidator in Ireland did not constitute the opening of main proceedings and in consequence determined that the Italian proceedings were the main proceedings under the Regulation.

On 23 March 2004 the Irish court gave judgment in the Irish winding-up petition. The judgment delivered by Mr Justice Kelly found, not surprisingly, that the centre of main interests of Eurofood was in Ireland and that the appointment of a provisional liquidator on 27 January 2004 had constituted the opening of main proceedings under Article 3 of the Regulation. It was also confirmed, again perhaps not unexpectedly, that Eurofood was grossly insolvent and that its creditors were entitled to have it wound up in accordance with the relevant Irish legislation. Of particular note was the finding by Mr Justice Kelly that the principal reason why the creditors were not bound to participate in the Italian proceeding was that the latter constituted a form of reorganization and was not therefore a winding up. The Irish court, therefore, made a winding-up order with regard to Eurofood relating back to the date of the presentation of the petition on 27 January 2004.

As at the time of writing there are appeals pending both in Ireland and in Italy. It is likely that the Irish appeal will come on prior to the Italian appeal. It is equally highly likely that future developments in this matter will be tracked in the pages of this publication.

For the moment, however, there are a few principal areas of interest raised by these decisions.

First, there is the question of when insolvency proceedings are considered 'opened'. As the Irish

judge pointed out, Article 2 defines insolvency proceedings as the collective proceedings referred to in Article 1(1) and they are listed in Annex A to the Regulation. In the case of Ireland, compulsory winding up by the court falls within the definition. In the case of Italy, extraordinary administration or its Italian translation also falls within the definition. The term 'winding-up proceedings' is also defined. In the case of Ireland it includes compulsory winding up. In Italy, however, it does not extend to extraordinary administration. Mr Justice Kelly rejected the argument put forward by Signor Bondi that the definition of the 'time of opening of proceedings' in Article 2 is when the final winding-up order is actually made, since that was completely inconsistent with the definition in Article 2(f) already referred to that the relevant 'time' is 'the time at which the judgment opening proceedings becomes effective, whether it is a final judgment or not'. There are two reasons for this finding: firstly, section 220(2) of the Irish Companies Act with its inbuilt notion of relation back, and, secondly, the actual appointment on the date of the petition's presentation of the Irish provisional liquidator.

Both those reasons seem correct on the facts of the case. However, there remains an oddity. At the heart of the regulation is the granting of jurisdiction to the courts of the Member State within the territory of which the centre of the debtor's main interests is situated 'to open insolvency proceedings'. The latter proceedings are defined by Article 2(a) as meaning the collective proceedings referred to in Article 1(1) which are as indicated above listed in Annex A. In the case of Ireland these include a court-driven compulsory winding up but not, and perhaps naturally enough, provisional liquidation. However, the language of Articles 2(e) and (f) already referred to enable the Irish court to find that an act or event which of itself would not have constituted insolvency proceedings was sufficient to clothe the Irish court with jurisdiction so as to be able to adjudicate upon the main proceedings. This was done in the two ways indicated above. In particular the Irish court found that even if the provisional liquidator had not been appointed, then, on the basis of the relation back provision referred to above, the insolvency proceedings could properly be deemed to have commenced at the date of the petition. This might be regarded as debateable for reasons which will be set out at the end of this article but it is hoped that the same result would be reached in the United Kingdom where the appointment of a provisional liquidator is not listed in Annex C. To justify a similar holding in the United Kingdom a generous reading must be given to the definition set out in Article 2(f) of the Regulation. The judgment opening the proceedings is the winding-up order and becomes effective within the meaning of that sub-Article in accordance with its terms, namely in accordance with the relation back provisions.

The Virgos–Schmidt Report on the Convention on Insolvency Proceedings, now commonly referred to as an aid to the textual interpretation of the Regulation, merely states in paragraph 67 that with regard to Article 2(e) the word 'judgment' must be taken in a 'broad sense' to mean 'decision, consistent with what is said in paragraph 66', namely applying an equally broad complexion to the notion of 'court'. In paragraph 68 of the Virgos–Schmidt Report it is stressed that with regard to Article 2(f) 'the time of the opening of proceedings' is a very important expression. The Report merely goes on to state that 'the time of the opening of proceedings is deemed to be the time when the decision begins to be effective under the law of the State of the opening of the proceedings.'

That comment is perhaps not particularly illuminating but it certainly does not hurt an extended reading of Article 2(f), which extended reading would be wide enough to include the relation back doctrine embedded in Irish and English law.

There is rarely likely to be any practical problem and the Irish decision may be regarded as a template for a typical situation. In most cases, leaving aside considerations of relation back, a debtor will retain its centre of main interests both at the date of the presentation of the petition as well as at the date of the winding-up order and if there is a shift the court will be quick to examine any such change in emphasis, no doubt at the instance of an aggrieved creditor. If, though, a debtor does acquire a different centre of main interests at the time a winding-up order is made subject to the scrutiny described above, it may not be appropriate in such a case to cede primary jurisdiction to another Member State or even to a non-Member State. The practical answer is in effect found by the Irish court's reflection of the practice obtaining in UK insolvency practice that in drawing up a winding-up petition presented in England there should be a statement verified by affidavit stating that the Regulation applies or does not apply as the case may be, reflecting, therefore, the need to show at the inception of the proceedings which in due course will mature into a winding-up order, all things being equal, that the debtor has a centre of main interests which attracts the jurisdiction of the English court or not as the case may be.

The practical effect of the recognition provisions set out particularly in Article 16(1) should however be noted. That Article as above referred to shows that any judgment opening insolvency proceedings handed down by a court of a Member State which has jurisdiction under Article 3 shall be recognized in all other Member States 'from the time that it becomes effective' in the State of the opening of proceedings. It may be that the language of Article 16(1) suggests something of a forward-looking interpretation but this is not to say that the relation back principle is not workable under the terms of the Regulation. Indeed

Article 4(2) already mentioned affords the law of the State of the opening of proceedings full rights to determine which assets form part of the estate: see Article 4(2)(b). In addition Article 4(2) also affords that law full rights with regard to treatment of assets 'acquired by or devolving on the debtor after the opening of the insolvency proceedings'. This is almost 'relation back'-type language.

In short it seems difficult to impeach the basis of the Irish court's pronouncement on this score. However, reference should be made to the general comments made at the end of this article.

The next issue concerns Eurofood's centre of main interests. As indicated above, the court indicated that the company's registered office was in Ireland and also noted that it was supervised by the Irish Ministry of Finance, the Irish Revenue and the Irish Central Bank.

Applying the criteria considered in the *Geveran* and *Daisytek* decisions, the Irish court focused upon how Eurofood's creditors would have perceived where the company was located. There was simply no evidence that those creditors ever considered that the company was based in Italy, at least according to the evidence before the Irish court. Key factors included the fact that the majority of board meetings took place in Dublin, that the Revenue stipulated that records and accounts be kept in Dublin for inspection purposes, that Irish Corporation Tax was levied and paid, that the administration agreement referred to was subject to Irish law and that as at the date of the petition's presentation all Eurofood's directors were Irish and located in Ireland. At that stage the Italian directors had resigned.

Particular reliance was placed on the fact that Eurofood's creditors at large were not heard by the Parma court. As indicated above, the Italian administrator argued that there had been no formal pronouncement at the time of the provisional liquidator's appointment that Eurofood's centre of main interests was in Ireland. The judicially provided answer seems, with respect, correct. The Regulation does not require there to be such a declaration: Article 3(1) merely contains a rule of jurisdiction. In any event Mr Justice Kelly found such a declaration necessarily implied that Eurofood had a centre of main interests in Ireland at the relevant time.

The learned judge commented that it would be helpful if the Irish form of winding-up petition then in use could be changed to reflect the English practice which has already been alluded to.

This is perhaps an appropriate place to comment briefly on the decision of the Parma court. There can be no doubt that, although it claimed to have regard to the substance of the matter by relying on correspondence and exchanges between Eurofood's Irish office and the office or offices of Parmalat in Italy, it did not apparently pay any or any real attention to the test as to centre of main interests prescribed by the Regulation, particularly in the criteria referred to in Recital 13 mentioned above.

It seems that only a short period prior to its giving judgment against Eurofood the same court in Parma had rendered similar decisions with regard to certain Dutch and Luxembourg subsidiaries of Parmalat, albeit that in those cases there were no anterior local proceedings. The Parma court held that the Irish provisional liquidation did not constitute a proper formal opening of main proceedings.

Particular stress was placed by Signor Bondi in his submissions before the Irish court on Recital 22 to the Regulation to the effect that, where the courts of two Member States both claim competence to open main proceedings, the first in time prevails. In the present case it was said that there had been no formal declaration as to opening of main proceedings by the Irish court when the provisional liquidator is appointed. That argument, as indicated above, was rejected on the basis also already indicated that the first operative date was the date of the presentation of the petition. It is, however, important to note that Signor Bondi in making his presentation to the Parma court was found to have relied upon expert Irish law evidence which, according to Mr Justice Kelly, at least, 'was not a correct statement of the position …'.

The final major factor of importance in the Irish Eurofood decision is with regard to public policy. Mr Justice Kelly noticed that no proper opportunity had been afforded to the creditors of Eurofood to be heard by the Parma court, although clearly some opportunity was given to some of the affected parties. Reference was made to Article 26 already referred to which ends with the reference to a possible infringing of 'fundamental principles or the constitutional rights and liberties of the individual …'. Failure to give notice to the creditors and notice of only one working day to the Irish provisional liquidator was found by Mr Justice Kelly to be in breach of those parties' rights to a fair hearing.

Article 26, especially in view of the final words referred to, has a restrictive ambit and should be used, it is suggested, in exceptional cases only. It may be that recourse to its provisions was justified on the present facts, namely effective absence of any real ability to deploy all possible arguments in the matters before the Parma court, at least on the part of the Irish provisional liquidator, but that clearly is a matter on which the book is not yet closed.

In conclusion, the decision in Ireland seems largely supportable but there are a number of residual contentious issues. It has been pointed out above that Annex C does not make an English provisional liquidator a liquidator for the purposes of Article 2(e). A possible argument runs as follows: namely Article 2(e) defines judgment either as one relating to the opening of proceedings or in relation to the appointment of a liquidator, but the definition of liquidator in

Annex C is relevant only to the second type of judgment. That view is certainly possible but that still does not mean that the time of the opening of proceedings cannot be when the first kind of judgment, i.e. an English or Irish style winding-up order with its inbuilt relation-back effect, is made. Admittedly an English court could not hold that the appointment of a provisional liquidator as such would itself constitute the opening of main proceedings but there seems a strong argument for supporting the alternative limb of Mr Justice Kelly's finding based on relation back.

The competing issues as to the appropriate centre of main interests seem largely factual. Perhaps in this case, or in a future case where factual elements are strongly in dispute, a determining reference to the European Court of Justice will be needed. It is certainly arguable that creditors may perceive there to be more than one place where a company is in practical terms located; indeed the underlying fairly simplistic analysis in the Virgos–Schmidt report regarding the seeking out of a debtor may be said to ignore the reality of cases where there are distinct groups of creditors each with differing interests and characteristics, each group dealing with, say, different branch offices but in similar ways. There is certainly more than a flavour, which is apparent in the Eurofood case, that Eurofood was in a large part at least merely a vehicle for financing head office or main company activity, and therefore the necessary independent quality of its existence was perhaps more lacking than would have been the case with, say, a genuine self- supporting independent though notionally connected corporate vehicle.

The public policy element is also open to further scrutiny perhaps even in the present case. The Irish decision considered failure to give notice, admittedly against the backdrop of human rights law, largely it could be said in Irish law terms. The question could be asked whether the Italian courts' own domestic processes were necessarily infringed as regards the hearing in Parma and whether on a broader level the opening of main proceedings generally in a Member State must take into account considerations of fairness, procedural or otherwise, which reflect yet other Member States' requirements in a similar context. Against this, however, it could be said that the thrust of the Regulation quite clearly is to give an unambiguously predominant status to a properly constituted insolvency process which has been carried out in the particular lead Member State, which is in the result found to be the one in which the centre of main interests is located.

One thing is certain, however: conflicting judicial approaches under the Regulation will continue for some considerable time to come.