CASE REVIEW

EC Regulation on Insolvency Proceedings – Recent Decisions on Shifting and Changing the COMI

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1. Introduction

Since EC Regulation No. 1346/2000 of 29 May 2000 on Insolvency Proceedings (the 'Regulation') has established a uniform standard for international jurisdiction within the European Community, its article 3, in particular, has repeatedly been the key subject of court decisions. In fact, determination of international jurisdiction for insolvency proceedings is currently one of the most controversially discussed legal topics. For instance, a ruling of the English Court of Appeal[1] was required to clarify the question as to what was the relevant date for determining the centre of main interests ('COMI') within the meaning of the Regulation. The underlying fact in the case was that prior to filing the insolvency application, the debtor had moved his domicile from England to Spain and now held that the English courts no longer had jurisdiction. The majority of the judges of the Court of Appeal considered the opening of the insolvency proceedings to be the relevant date. However, one judge took a differing view.

2. Current developments in legal practice

There are now two recent rulings that develop the criteria for interpreting article 3, paragraph 1 of the Regulation further. In the first, proceedings before the European Court of Justice were again concerned with the specific date for determining the COMI. In the second, a German insolvency court ruled on what effect is produced by a cessation of business operations before the filing of the insolvency application. In both proceedings, the jurisdiction of German insolvency courts was in question.

2.1 European Court of Justice – Staubitz-Schreiber

On 17 January 2006,[2] the European Court of Justice ruled on a case, in which the debtor had moved her domicile (and thus the COMI) from Germany to Spain after the filing of the application. The Wuppertal Local Court [*Amtsgericht*], the insolvency court properly having jurisdiction pursuant to German law, refused to open proceedings due to lack of assets. The appellate court rejected the appeal on the grounds that, pursuant to article 3, paragraph 1 of the Regulation, German courts no longer had international jurisdiction due to the change of domicile. During the appeal on points of law, the German Federal Court of Justice referred the matter to the European Court of Justice for a ruling on whether the courts of a member state still retain jurisdiction over the decision to open insolvency proceedings even if the debtor has transferred its domicile to the territory of another member state after the filing of the application.[3]

According to the ruling of the European Court of Justice, a change of COMI after the filing of the application but before the decision on opening the proceedings is irrelevant. Instead, the court where the case was originally filed retains jurisdiction. If a subsequent change to another member state were to be considered relevant to international jurisdiction pursuant to article 3, this would throw the doors wide open to 'forum shopping', which is precisely what the Regulation is intended to prevent.[4] The debtor could attempt to improve its legal position by cleverly shifting assets and in the process selecting the insolvency regulations of one of the member states that are to its advantage, thereby itself determining the place of jurisdiction as established by

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1 [2005] EWCA Civ 974 (*Shierson v Vlieland-Boddy*); cf. S. Fuller, 'EC Regulation: COMI moves to Spain' (2005) 5 *International Corporate Rescue* 285, and H. Thornley, 'EC Regulation on Insolvency Proceedings – Shifting the COMI after Debts are Incurred' (2005) 6 *International Corporate Rescue* 348.

2 Case C-1/04 *Staubitz-Schreiber*.

3 See referred question in European Court of Justice, Case C-1/04 *Staubitz-Schreiber*, margin number 20.

4 See recital 4, European Insolvency Regulation and European Court of Justice, note 3 above, margin numbers 24 et seq.

article 3, paragraph 1 of the Regulation.[5]

The European Court of Justice was further guided by the protection of creditors. If the court where the application was first filed retains jurisdiction, creditors enjoy greater legal certainty. The latter have assessed the risks inherent in their relationship of mutual trust with the debtor according to the system of laws that were applicable on the basis of the previous COMI.[6] This reliance of the creditors on the applicable law would be disregarded.

Moreover, the debtor would be able to evade proceedings through a frequent change of domicile, which would result in an undesirable prolongation of the proceedings if the debtor could always 'flee' to the next member state after filing an application. Thus the efficiency that the Regulation endeavours to promote would no longer be achieved precisely in the case of cross-border proceedings.[7]

2.2 *Hamburg Local Court* [Amtsgericht]

In a recent case,[8] the Hamburg Local Court had to rule on jurisdiction over the opening of main insolvency proceedings pursuant to article 3, paragraph 1, sentence 1 of the Regulation.

The debtor was a company that had been founded on 2 August 2004 in the legal form of a 'private company limited by shares' ('Limited') according to the law of England and Wales. It was registered at Companies House Cardiff. The registration of a branch office in Hamburg failed. The location of the 'registered office' was in Great Britain. However, the debtor was not actually managed from there but – since its founding – exclusively from Hamburg. In Hamburg, the debtor operated a cafeteria and a bistro, each in leased facilities. Even before the filing of the insolvency application in October 2005, Limited had completely ceased its commercial activities aimed at generating profits. There were no winding-up proceedings.

The key issue for the ruling was whether the cessation of commercial activities aimed at generating revenue had an effect on the COMI of the debtor, and whether such a case would automatically be subject to the presumption of article 3, paragraph 1, sentence 2 of the Regulation (according to which the proceedings would have to be opened in Great Britain as the country of statutory domicile).

In its ruling, the Hamburg Local Court arrived at the conclusion that the cessation of commercial activities aimed at generating revenue was not relevant to the COMI. In particular, it was deemed not to shift the COMI to the statutory domicile. It was found that ascertaining the COMI had to be guided by previous business operations, which, in the present case, had been carried out exclusively in Hamburg. In its ruling, the Court relied on the following points:

The relevant date for a ruling on the question of the location of the COMI was indeed found to be the filing date of the insolvency application.[9] The location of a debtor's COMI must be ascertained by an interpretation in line with the intent and purpose of the Regulation.

In this context, the focus must be on the creditors' perspective, since recital 13 of the Regulation, in particular, indicates that the normative purpose of article 3 was to create legal certainty through predictability of international jurisdiction and the applicable insolvency statute. This normative purpose had to be taken into consideration even if commercial activities aimed at generating revenue are discontinued without substitute. Absent the initiation of winding-up proceedings, such commercial activities were deemed effectively to continue until the filing of the insolvency application, for instance through the presence of (future insolvency) liabilities, (future insolvency) assets, etc. To that extent, it was held that creditors make an assumption that insolvency proceedings will be conducted in the country of the previous business operation.

In conclusion, the court advances the argument that the debtor, though no longer actively engaged in commercial relations due to the cessation of commercial activities aimed at generating revenues, nevertheless continues to exist in the country of its previous business activity as a relevant holder of assets under insolvency law. Therefore, insolvency proceedings – giving consideration to the creditors' point of view – should take place in the country in which commercial activities aimed at generating revenues had given rise to liabilities.

In addition to this weighing of normative purposes, the court also relies on the argument in recital 4 of the Regulation that 'forum shopping' should be prevented. It would violate the spirit of the Regulation if a debtor could delay the filing of the insolvency application until the complete cessation of commercial activities aimed at generating revenue and thereby exerting influence on the applicable insolvency statute and on the jurisdiction of the insolvency court.

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5 This was also taken into consideration by the Court of Appeals in *Shierson v Vlieland-Boddy*; cf. Thornley, note 1 above at 349.

6 European Court of Justice, note **2 above, margin number 27.**

7 See recital 8, European Insolvency Regulation and European Court of Justice, note **2 above, margin number 26.**

8 Ruling of December 1, 2005, Case No. **67a IN 450/05.**

9 See reference of the Hamburg Local Court to, among other citations, Haß/Herweg in Haß/Huber/Gruber/Heiderhoff (eds.), *Kommentar zu EuInsVO* [Commentary on the European Insolvency Regulation], article 3, margin number 17.

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3. Summary and Outlook

The above-referenced ruling of the European Court of Justice declares a change of COMI after the filing of the insolvency application to be irrelevant. According to the Hamburg Local Court, the cessation of commercial activities aimed at generating revenue does not cause the presumption pursuant to article 3, paragraph 1, sentence 2 of the Regulation (opening of the insolvency proceedings in the statutory domicile of the company) to become automatically applicable. Instead, the general criteria for ascertaining the COMI remain in effect. In both cases, the courts base their reasoning predominantly on the prevention of 'forum shopping' and legal certainty for the creditors.

However, there are still some open questions, which were also addressed by the Court of Appeal in *Shierson v Vlieland-Boddy*. Most prominently, the question of whether the relation back-principle, which is codified in English, Welsh and Irish law, must also be applied within the context of the Regulation. This principle holds that the date of the application filing is retroactively deemed to represent the start of the insolvency proceedings.[10] The European Court of Justice will have to decide whether this is compatible with the Regulation and its goals.

These and other questions are the subject of the *Eurofood* proceedings before the European Court of Justice,[11] which are related to the collapse of the Parmalat Group.[12] They are also concerned with the treatment of cases of true conflict, especially the question of whether a court must recognise the erroneous affirmation of jurisdiction by a court of another member state.[13]

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10 See section 220 nos. **1, 2 Irish Companies Act.**

11 Case C-341/04 *Eurofood*.

12 An extensive discussion of the facts, and of the final statement already presented by the Advocate General, can be found in T. O'Grady/N. Counihan, 'Advocate General's Decision in *Eurofood*' (2005) 6 *International Corporate Rescue* 294.

13 See article 16, paragraph 1 of the Regulation.

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