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Cross Border Insolvency – COMI Shifts: An Entitlement under EU Fundamental Freedoms?

Dearbháile Banahan

UNIVERSIDADE CATÓLICA PORTUGUESA

CATÓLICA GLOBAL SCHOOL OF LAW

LL.M. MASTER OF LAWS - LAW IN A EUROPEAN & GLOBAL CONTEXT

CROSS BORDER INSOLVENCY -

COMI SHIFTS: AN ENTITLEMENT UNDER EU FUNDAMENTAL FREEDOMS?

SUPERVISOR: ANTÓNIO FRADA DE SOUSA

DEARBHÁILE BANAHAN

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List of Abbreviations:

AG	Advocate General
ECIR	EC Regulation on Insolvency Proceedings
ECJ	European Court of Justice
EU	European Union
COMI	Centre of Main Interests
MS	Member States
TFEU	Treaty on the Functioning of the European Union
UK	United Kingdom
USA	United States of America

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"I would argue therefore that a creditor is never able to predict which insolvency law his claim will be subject to – as long as the Internal Market consists of different substantive insolvency regimes."

– Wolf George Ringe

"As the freedom of EU citizens to relocate from one MS to another is enshrined within the European legal order, the question begged is whether any relocation involving a forum shop, be it temporary or permanent, should be regarded as an undesirable abuse of EU law freedoms or whether this is only so where the relocation is an outright fiction."

– Adrian Walters & Anton Smith

I. INTRODUCTION

Most areas of substantive law in the European Union are not uniform, hence we can find as many substantive Laws as the amount of Member States, some of which have many differences in substance, judicial style and reasoning[1]. At the same time, the huge variety of legal systems means that instruments and conceptions may differ from Member State to Member State[2]. If we combine these aspects with the Internal Market and EU fundamental freedoms, one can easily conclude that EU citizens and legal companies have an indirect choice of law. As long as there is freedom of movement and freedom of establishment, there will be forum and law shopping, as natural and legal persons can move to the Member State with the most favorable law. This is a situation that has been raised and discussed in situations concerning company law and tax law. Nowadays, however, there is a "new" phenomenon, whereby natural and legal persons are shopping for the most favourable Insolvency forum and, consequently, the most favourable Insolvency Law[3], raising a number of new issues.

Regarding Insolvency law in the European Union, there is a clear divergence between the different legal systems, contrary to what happens in the USA where there is a Bankruptcy Code and,

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[1] There are four groups of private law regimes that can be identified within the EU: (1) the common law systems of Ireland and the UK with their emphasis on judge-made law, (2) the traditional civil law countries with their national civil code, (3) the Scandinavian MS and (4) the large group of countries that entered the EU in 2004. –see *Oscar Chase & Janet Walker, "Common Law, Civil Law and the future of categories", LexisNexis, 2010 , NYU School of Law, Public Law, Research paper no. 10-40*

[2] Ex: Whilst a gift is a contract (donation) in Portugal, in common law it isn't. Marriage is a contract according to many legal systems but it isn't in Italy. Under Article 1321 of the Italian Civil Code, "*A contract is an agreement between two or more parties for the purpose of creating, providing for or extinguishing amongst themselves a legal patrimonial relation*".

3 See William W. McBryde, Axel Flessner, Sebastianus Constantinus Johannes Josephus Kortmann, "Principles of European Insolvency Law", Kluwer Legal Publishers, January 1, 2003 whereby Insolvency is defined as a "*state of affairs where a debtor is being overwhelmed by liabilities and where, as a consequence, the creditors at large can no longer expect to receive fully and in time what is owed to them from a normal management of the debtor's affairs or business*". The law of insolvency "*makes available to all the creditors the remaining property and economic potential of the debtor and by readjusting the debtors legal position towards the outside world and economic reality*".

therefore, a uniform set of substantive and procedural law. However, in the European Union we only have the EC Regulation on Insolvency[4] (from now onwards Insolvency Regulation) which establishes common rules for insolvency proceedings in the European Union, regarding the court competent to open insolvency proceedings, the applicable law and the recognition of the court's decisions for cases where a debtor becomes insolvent. In other words, the Insolvency Regulation is merely a private international law Regulation, with uniform rules on jurisdiction, applicable law and regime of recognition and enforcement of decisions, not attempting in any way to "introduce a uniform substantive insolvency within the EU."[5] In other words, each Member State continues to preserve their own insolvency Laws.

The purpose of the Insolvency Regulation, by harmonizing certain procedural aspects regarding insolvency proceedings, is, on the one hand, for cross border insolvency proceedings to operate efficient and effectively[6], and, on the other hand, to avoid assets or judicial proceedings from being transferred from one Member State to another in order to obtain a more favourable legal position, which the Insolvency Regulation defines as "forum shopping[7]", a definition that we will take into consideration further on. However, while interpreting and applying the Insolvency Regulation, these goals must also be balanced with EU fundamental freedoms.

Under Article 3 of the Insolvency Regulation, the Courts with jurisdiction to open the main proceedings are those of the Member State where the debtor has its *centre of main interests* (COMI), considered to be where the debtor usually administers its interests and that is verifiable by third parties. In the case of a company or legal person, this is the place of its registered office, in the absence of proof to the contrary. In the case of a natural person it is, in principle, the place where the debtors' work is domiciled or the place of its usual residence. Moreover, under Article 4 of the Insolvency Regulation, the applicable substantive law is the law of the State where the procedure commences. Hence, by simply reading these two articles, it is easy to understand that debtors may be led to analyse and compare legal systems in order to find the most favourable substantive law[8]. In fact, the consequences are

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4 Council Regulation (EC) No 1346/2000 of 2000 on Insolvency proceedings

[5] W. McBryde (2003)

[6] Recital 2, Preamble, ECIR

[7] Recital 4, Preamble, ECIR

[8] This means that debtors from a legal system where it takes 6 years to be discharged, for example Germany, may move to a different MS with a

quite obvious when one understands the meaning of, on the one hand, freedom of movement (in the case of a personal debtor) and freedom of establishment (in the case of a corporate debtor) and, on the other hand, the manipulability of the connecting factor that the Insolvency Regulation chose, this is, the COMI.

As we will see in Chapter IV and V, the ECJ has had an essential role in interpreting and determining the meaning of COMI, especially in what concerns the meaning of a corporate debtor's COMI - our main concern in this paper. *Interedil*[9], its most recent case concerning this topic, has, if not brought astonishing novelties, at least clarified what had been said in *Eurofood*[10], making it easy (or at least easier) to rebut the presumption whereby a corporate debtors COMI is the place of its registered office. By giving less importance to the place of the registered office, a number of issues and concerns are raised.

Whilst Member States' Insolvency substantive laws vary, and taking into account the debtors entitlement to benefit from freedom of movement and freedom of establishment, the Insolvency Regulation in fact opens doors to *forum-shopping*, entitling debtors to "shop around" for the most favourable insolvency law (by settling in the Member State where the jurisdiction has a more favourable substantive law). Hence, whilst companies, when setting up business[11], can plan where they would rather have their COMI, they may also plan a shift of their COMI to another Member State before filing for insolvency. This phenomenon – forum and law shopping - is not necessarily bad, as we will discuss further on. In other words, forum shopping is not necessarily negative. In fact, it is one of the great achievements and natural consequences of the Internal Market and fundamental freedoms. However, what must not be allowed is abusive forum shopping, as analysed in Chapter III and VII.

At the same time, the European Parliament has made recommendations to the Commission, one of which concerns alterations regarding the definition of the COMI. It will be, to say

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more favourable substantive law, such as the UK, when predicting they are going insolvent.

[9] Case C – 396/09, *Interedil Srl (in liquidation) v Fallimento Interedil Srl, Banca Intesa Gestione Crediti Spa, Tribunale Ordinario di Bari*, [2011]

[10] Case C-341/04, *Eurofood* [2006] ECR I-3813

[11] See Wolf-George Ringe, "*Sparking Regulatory competition in European Company Law: the impact of the Centros Line of Case Law and its concept of "abuse of law*" in Prohibition of Abuse of Law, a new general principal of EU, edited by Rita de la Feria and Stefan Vogenauer, 2011 - Whilst before, companies were *shopping* for more favourable company law, they are now *shopping* for more favourable insolvency law.

the least, exciting to see what alterations relating to the COMI will be proposed and eventually approved. As we will analyse in Chapter VI, it is doubtful that such alterations will go against the ECJ's case law and, therefore, the introduction of a desired irrebuttable definition of a corporate debtor's COMI as being the place of its registered office, is not to be expected. What may happen, we speculate, is the introduction of a time limit, which, nevertheless, also raises a number of issues and may not be the (perfect) problem solver. Our position is that, no matter what alteration comes into force, *forum shopping* will never be totally eliminated. To suggest the contrary, would mean putting fundamental freedoms and the Internal market at stake.

Meanwhile, and until alterations are actually introduced, a solution is needed. Creditor's interests need and deserve protection; hence abusive shifts of COMI may not be permitted. This is why we believe that it will be down to the principle of abuse of law - and future ECJ case law - to solve this issue (Chapter VII and VIII). Looking at past case law in other areas of law may be helpful.

In resume, a first problem is interpreting the term COMI. The second problem is to understand to what extent it is and should be manipulable.

II. The Insolvency Regulation – A First Approach

The Insolvency Regulation[12], adopted on May 29, 2000, by all Member States with the exception of Denmark[13], came into force on May 31, 2002. The enactment of the Insolvency Regulation was long awaited for, after the failure of the EC Convention on Insolvency Proceedings, which did not come into effect in 1996, due to the refusal of the UK to sign it. Being very similar to the former Convention of Insolvency Regulation, many continue to take into account the *Virgos-Schmit Report*[14], which, in fact, was never actually officially published, but continues to provide guidance on the effects and goals of the Regulation.

The Insolvency Regulation is extremely important, determining uniform insolvency procedures for all EU Member States. The proper functioning of the internal market was

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[12] Council Regulation EC no. 1346/2000 of 29 may 2000 on Insolvency Proceedings

[13] Recital 33 of the Insolvency Regulation

[14] Virgos, Miguel and Schmit, Etienne. (1996) *Report on the Convention on Insolvency Proceedings.*

incompatible with a system whereby each Member State had its own procedural and substantive insolvency law. Before the Insolvency Regulation, there were proceedings in every Member State where the debtor had assets and, in principle, only the creditors in each Member State could participate in the proceedings.[15] In other words, before the Insolvency Regulation, from a "Private International Law perspective, the situation in the Community in the field of insolvency [had been] was far from encouraging. There was a conflict of laws at both the internal level, with divergent national substantive rules, and the international level, with different Private International Law solutions."[16]

The Insolvency Regulation established, for the first time, a common framework with common rules for insolvency proceedings in the European Union regarding the competent court for the opening of insolvency proceedings, the applicable law and the recognition of the court's decisions for cases where a debtor becomes insolvent. It applies to "collective insolvency proceedings that entail the partial or total divestment of a debtor and the appointment of a liquidator"[17], applying equally to all proceedings, whether the debtor is a natural or a legal person, a trader, or an individual[18]. Purely internal insolvency proceedings are excluded from its scope, applying only to Insolvency proceedings that have cross border effects[19] and where the debtors' COMI is situated in the European Union[20]. This means that a number of international insolvency proceedings are left out of its scope, namely those that involve debtors with substantial connections to one or more Member State, but that have their COMI situated outside the European Union. In such a scenario, the national laws of that Member State will apply separately, regarding the competent court, insolvency proceedings and recognition and enforcement in foreign countries[21].

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[15] Vide António Frada de Sousa "*Exoneração do passivo restante e fórum shopping na insolvência de pessoas singulares na União Europeia*", in "Estudos em Memória do Prof. Doutor J. L. Saldanha Sanches - Vol II", Coimbra Editora (2011), p 63- 64

[16] VIRGÓS & SCHMIT, p. 10

[17] Article 1, Paragraph 1, ECIR

[18] Recital 9 ECIR

[19] Recital 4 ECIR

[20] Recital 14 ECIR

[21] Luís Manuel Teles de Menezes Leitão, "*Direito da Insolvência*", Almedina, 2009, footnote p. 341.

Whilst, under Article 3 of the Insolvency Regulation, the courts[22] with jurisdiction to open main proceedings are the courts of the EU Member State where the debtor has its COMI[23]/[24], the law applicable to the insolvency proceedings is, under Article 4 of the Insolvency Regulation, the law of the Member State where they were opened (*lex fori concursus*). Applying the *lex fori concursus* makes sense as it is the Member State where the insolvency proceedings are opened that will be the most interested in regulating the insolvency and ascertaining that public interest pursued with the liquidation of the insolvent estate is protected and safeguarded. Also, it is normally in that Member State where the majority of assets and creditors can be found, guaranteeing equality of creditors under its law. Meanwhile, it is the law that the Court - Judge - is most familiar with, which certainly leads to a better administration of justice, avoiding difficulties which would emerge if a foreign law had to be applied[25]. Therefore, and in other words, it is the *lex fori concursus* that determines the entire insolvency proceedings, namely, the opening of the proceedings, their conduct and their closure[26].

The Insolvency Regulation's main goal is to provide rules on jurisdiction and conflict of law matters in the context of cross-border insolvencies and does not in any way harmonize or intend to harmonize substantial insolvency laws of the Member States[27].

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[22] Article 2 paragraph d) defines Court as meaning "*the judicial body or any other competent body of a member State empowered to open insolvency proceedings or to take decisions in the course of such proceedings.*"

[23] Secondary proceedings may also be opened in another EU MS if the debtor has an establishment in that MS, although such proceedings are limited to the debtors' assets in that MS. Establishment" meaning any place of operations where the debtor carries out a non-transitory economic activity with human resources and goods.

[24] See, portuguese case where this was discussed, Acórdão do Tribunal da Relação de Lisboa, 5.09.2008, Processo n.º 1351/2007-6, Relator Fernanda Isabel Pereira , available at www.dgsi.pt

[25] Menezes Leitão (2009), p.342

[26] Article 4, paragraph 2 ECIR. Note that, under Recital 22 ECIR, there is automatic recognition of judgments concerning the opening, conduct and closure of insolvency proceedings in other EU countries without further scrutiny.

[27] Recital 11 ECIR

III. FORUM SHOPPING – DEFINITION

As above mentioned, one of the goals of the Insolvency Regulation is to avoid forum shopping. Recital 4 of the Insolvency Regulation refers to forum shopping as the "transfer [of] assets or judicial proceedings from one Member State to another, seeking to obtain a more favourable legal position". This definition alone raises a number of doubts. Forum shopping does not usually mean the "transfer of assets or judicial proceedings". At "its simplest, forum shopping means little more than identifying the optimal jurisdiction for a certain transaction, in the context of insolvency certainly for the purpose of the restructuring or insolvency of a given company, and taking measures so that the law of that jurisdiction is applied".[28]

In order to forum shop, the debtor will need to move its COMI from one Member State to another Member State in order for the forum (Article 3) and applicable insolvency law (Article 4) be those of the new Member State. By doing this, the debtor is, naturally, seeking to obtain a more favourable legal position. The main problem, and the first necessary clarification, is related to whether this behavior should be allowed or, on the contrary, condemned. It is our view that moving a COMI to another Member State in order to obtain a more favourable forum and law is perfectly acceptable, being, in fact, a necessary consequence that has emerged with the Internal Market and its Fundamental Freedoms, namely freedom of movement and freedom of establishment. Therefore, forum shopping is and should be allowed under EU Law. What should not be allowed, is abusive forum shopping.

Hence, the Insolvency Regulation, when referring to forum shopping in Recital 4, must be read as meaning "abusive forum shopping". At least, this is the way we read and interpret it. In other words, our concern and research is developed on the premise that what must be avoided and condemned is abusive forum shopping, considerations that will be developed further on, in chapter VII and VIII.

IV. CENTRE OF MAIN INTERESTS (COMI)

Cross-border insolvency situations occur in a wide variety of

[28] Wolf-George Ringe, "*Forum Shopping under the EU Insolvency Regulation*" available at Social Science Research Network http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1209822 (August 1, 2008)

circumstances, giving rise to complex questions related to the interplay of competing legal systems[29]. As hinted above, it is not possible to discuss cross-border insolvency (or forum shopping) without mentioning the term COMI and its implications.

Cross-border insolvencies require first and foremost locating the COMI of the debtor (whether it is an individual debtor or a corporate debtor), as this is the first necessary step to determine the Member State with jurisdiction and, consequently, the applicable substantive insolvency law.

So, what exactly is the *centre of main interests* (COMI)? What does it mean? Why do some refer to it as the *magic word*[30] in Modern International Private Insolvency Law? Regarding natural persons, under Article 3, the COMI will be, in principle, the place of its work or habitual residence. It is regarding the COMI of legal persons[31] (companies) where more doubts arise. Before looking at the wording of the Insolvency Regulation a previous word must be said to contextualize. Before the Insolvency Regulation, each Member State had different criterions and gave importance to different factors. Whilst the UK regarded the place of registration as the connecting factor (which meant that whenever there were insolvency proceedings that involved more than one Member State, the main proceedings would take place in that State), the "continental approach" focused on the "real seat" of the company[32]. It is, therefore, curious that the Insolvency Regulation apparently tries to refer to both "theories". On the one hand Article 3 (1) of the Insolvency Regulation states that in the case of a company or a legal person, it is the place of its registered office. On the other hand, the place of the registered office may be rebutted, according to recital 13, if the debtor "conducts the administration of its interests on a regular basis [elsewhere] that is ascertainable by third parties", this meaning the "real seat" of the company.

In either case, the COMI, as the connecting factor, is clearly manipulable and can be used to the advantage of debtors, whether personal or corporate debtors.

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[29] Stefan Ramel, "Cross Border Insolvency Update", Guildhall Chambers, January 2011, available at <http://www.guildhallchambers.co.uk/seminars/index.cfm?id=522&a=292>

[30] Vide António Frada de Sousa (2011), p. 66.

[31] Ian F. Fletcher, "Insolvency in Private International Law", Second Edition, Oxford, Oxford Private International Law Series, p. 368 -375

[32] See Gabriel Moss, Ian Fletcher and Stuart Isaacs, "The EC Regulation on Insolvency Proceedings: A Commentary and Annoted Guide", Oxford, Oxford University Press, 2002

1. Personal Migration

Regarding natural persons, such phenomenon has led to a number of deliberate migrations with the exclusive purpose of benefiting from more favourable insolvency regimes[33]. Some authors, such as Adrian Walters and Anton Smith[34], call this phenomenon *Bankruptcy Tourism*, which basically consists in *forum shopping* for favourable bankruptcy[35] law, whereby the most attractive "tourist" destination is England and Wales. Whilst these people contract and raise their debts in a certain Member State, they then move their COMI to another Member State "with a view to opening main proceedings and discharging their debts under that State's bankruptcy law"[36]. The effects of such insolvency proceedings will then be automatically recognized throughout the European Union, including the home country where the debts were contracted, under Articles 4, 16 (1) and 25 of the Insolvency Regulation[37], meaning that such effects apply also to the creditors, who can no longer claim to be repaid, even though they would be entitled to do so under the jurisdiction where the credit was granted.

A Daily Telegraph Article[38] written in 2009 explains this reality ever so well. It explains that the Royal Tunbridge Wells in Kent is becoming the "debt capital of Europe", having many Germans and Austrians moved there in order to take advantage of Britain's bankruptcy laws which are obviously much more

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[33] For more on Forum shopping concerning natural persons, vide António Frada de Sousa "*Exoneração do passivo restante e fórum shopping na insolvência de pessoas singulares na União Europeia*", in "Estudos em Memória do Prof. Doutor J. L. Saldanha Sanches - Vol II", Coimbra Editora (2011), p. 57-98

[34] Adrian Walters and Anton Smith, "Bankruptcy Tourism under the EC Regulation on Insolvency Proceedings: A view from England and Wales", International Insolvency Review, Vol. 19, No.3, pp. 181-208, 2009 (also available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1630890) pp. 2-49

[35] Bankruptcy is used in its English sense to refer exclusively to the insolvency of, and insolvency proceedings relating to, individuals (natural persons) and not corporations (legal persons)

[36] Adrian Walters and Anton Smith (2009), pp. 3

[37] The principle of mutual trust is one of the most fundamental principles in Private International Law

[38] "Tunbridge Wells the "debt capital of Europe"", Daily Telegraph, 22 September 2009, available at <http://www.telegraph.co.uk/finance/personalfinance/6219396/Tunbridge-Wells-the-debt-capital-of-Europe.html>

favourable. People with huge debts[39] "move to Britain and at once they are there for six months can be declared bankrupt in a British Court, writing off their debts just one year later. This compares to a wait of seven or nine years[40] in Germany". The even more surprising part is that there are agencies such as "Insolvenz Agentur" that are benefitting from this loophole, and for a fee of £7000 are "advising Germans and Austrians to take advantage of British Bankruptcy laws as well as helping with relocation and finding a job", advertising and promising "bankruptcy tourists to get rid of the rest of their debts in England after just 12 months"[41].

Obviously this is quite disturbing and unfair to accept that somebody can raise million euro debts under a certain legal system and then go to another legal system to discharge them. These are not just academic examples. Numerous situations like this occur daily. A recent case that brought this concept of Bankruptcy tourism to the forefront of legal debate was *Anglo Irish Bank (now Irish Bank Resolution Corporation IBRC) v Sean Quinn*.

Sean Quinn filed a debtor's petition before the High Court of Justice in Northern Ireland on 10 November 2011 seeking to be declared bankrupt, under the UK Insolvency Order 1989, having successfully been adjudged bankrupt on the basis that "he was born, bred and worked all his life" in Northern Ireland[42]. It was considered that despite Mr. Quinn's habitual residence being in the Republic of Ireland, his COMI, was the place where he carried out economic activity on a regular basis, which was in Northern Ireland.

A week later, on 17 November 2011, the IBRC filed an application to the High Court of justice in Northern Ireland in order for it to annul the order pursuant to Article 256 (1a) of the 1989 Insolvency Order, basing its arguments on the facts that the court in Northern Ireland did not have jurisdiction to open the proceedings under Article 3(1) of the Insolvency Regulation because Mr Quinn's COMI was in the Republic of Ireland. On 24 November 2011, the case was heard by Judge Mr. Justice Deeny[43], who stated that in order to determine the competent jurisdiction, he would apply the criteria set out in the Insolvency Regulation.

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[39] It reports one case that has debts of £16 million!

[40] Now it is actually 6 but it is still a major difference

[41] "Tunbridge Wells the "debt capital of Europe""(2009)

[42] At the same time, Mr. Quinn was being subject of Commercial Court applications for judgments by the Irish Bank Resolution Corporation Limited (IBRC) in the Republic of Ireland.

[43] Irish Bank Resolution Corporation [Limited] v John Ignatius Quinn (DEE 8396 2011 No.133303)

Sean Quinn claimed in his petition that the place where he conducted his business was in Northern Ireland and it was there where the Quinn Group had its registered office. He defended that he had business interests in Northern Ireland and that he could prove that his COMI was there. Nevertheless, and as pointed out by Mr. Justice Deeny, regarding the position he occupied in the Quinn Group as senior office and shareholder, he had in fact resigned from the Group in April 2010. Following this, Mr. Quinn stated that he had another office in Northern Ireland since 2 May 2011, where he claimed to be carrying out the administration of his various business interests. However, such an address had not been disclosed in his petition for bankruptcy, neither the telephone number nor address of that office appeared in any trade directory or on the Internet, neither IBRC nor the Revenue Commissioners had been informed of it and Mr. Quinn was unable to exhibit any correspondence sent to him at that office. While the Court accepted that Mr. Quinn was keen to protect his privacy, it found that this could not be reconciled with the requirement that a person's COMI should be ascertainable by third parties.

The Court determined that although Mr. Quinn was a UK taxpayer, 20% of his tax was, by agreement, paid in the Republic, determining that his habitual residence was in the Republic Ireland for 32 years, having an Irish passport and not a UK one. Also, the Court decided that all elements were insufficient to establish general economic activity. Taking everything into consideration, the Court decided that Mr. Quinn's COMI was not in Northern Ireland, but in the Republic of Ireland[44], hence annulled its previous bankruptcy order, and declared the Irish Courts to have jurisdiction, having been declared bankrupt by the High Court in Dublin, on 16 January 2012.

This was an important decision for creditors (namely financial institutions) across Ireland, "who have been left to deal with the bad loans of some of Ireland's most well-known and formerly very high net worth individuals, many of whom have begun to make their way outside of this jurisdiction to present bankruptcy petitions elsewhere"[45]. As above mentioned, the UK has a more attractive insolvency law, in comparison to Irish Insolvency Law, which was enacted in 1988 and has remained

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[44] William Fry, "Insolvency update", Spring 2012, available at
< http://www.williamfry.ie/Libraries/test/Insolvency-Update---Spring-2012.sflb.ashx >

[45] Una Leavy, *Intra Jurisdictional Bankruptcy and IBRC v Quinn*, Summer 2012, available at <http://www.mhc.ie/publications/item/568/intra-jurisdictional-bankruptcy-and-ibrc-v-quinn >

practically unchanged. For instance, under Section 85 (1) of the Irish Bankruptcy Act 1988, a debtor, i.e. bankrupt, cannot apply for automatic discharge until a period of 12 years has elapsed since the date of adjudication[46]. On the contrary, in the UK after just 12 months, an automatic discharge from bankruptcy is possible. The bankruptcy administration is also more attractive as it makes the process faster.

This case did not reach the ECJ but it would have been very interesting to see whether the ECJ would have decided in the same way as the Northern Irish Courts, who clearly interpreted COMI restrictively[47]. It balanced freedom of movement with the goal of insolvency regulation to avoid forum shopping. And, also, it was very sensible and reasonable while interpreting "ascertainability to third parties". This meaning, it is arguable that if Mr. Quinn had moved to Northern Ireland for a reasonable time and made his move public to creditors, then it would have been very hard for the northern Irish Courts to refuse his application.

One thing is for sure: Ireland is waiting patiently for a new Bankruptcy Code, which is expected to reduce the discharge period from twelve years to a likely three years. This is certainly an attempt to keep debtors from forum shopping for more favourable bankruptcy laws[48].

2. Corporate Migration

Regarding companies, our main concern in this paper, there has also been insolvency forum (and law) shopping.

Member Sates' insolvency laws differ and in some cases are more attractive than the law applicable in the current Member State where the company is located. This has led different companies to shop around for more favourable insolvency laws, some of which are very attractive, incentivating the COMI shift.

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[46] Una Leavy, 2012

[47] It is the liberal interpretation of COMI that allows for migration and leaves creditors unprotected. Whilst creditors give credit counting on the protection of their legal system, debtors now have the possibility to "run" from their legal duties and go to another legal system that is more beneficial to them. There is nothing that creditors can do as the sentence granted by the Court of the other legal system must be recognized by all Member States including the Member State where the debts were contracted.

[48] Frances Flynn, "Frances Flynn discusses international bankruptcy regimes with a spotlight on recent trends in the UK where forum shopping has gained momentum", available at <http://www.mcdowellpurcell.ie/content/uk-bankruptcy-courts-and-forum-shopping>

For example, regarding the management's duty to file for insolvency, the UK has a more attractive regime. There is no duty, and therefore no liability, if the management files late for insolvency. If the management knows (or ought to know) that the insolvency is unavoidable and yet takes all necessary attempts to minimize creditors losses, then he can avoid his liability. In other words, the management does not have a duty to avoid insolvency but at once it becomes obvious, then he must take creditors interests into account, as it "is bound to the interests of the creditors instead of the shareholders because once all equity is lost, the creditors are the beneficial owners of the company."[49] However, in Germany this is not the case. The management has a strict duty to file for insolvency with very serious consequences, should it fail to do so. When a company becomes insolvent or balance-sheet over-indebted the management has to file an insolvency petition within three weeks and if it doesn't, the management will be personally liable towards the creditors for their loss, and there may even be criminal liability. In Portugal, there is also a duty to file for insolvency 30 days after the knowledge of its insolvency, whereby knowledge of the situation will be presumed (a presumption that is not rebuttable!) 3 months after the general incompliance with its duties and obligations[50]. The failure to do so may imply liability of the management. It is therefore quite understandable that "the management of a company has great incentives to file in a management-friendly jurisdiction in order to limit or even exclude claims against the directors"[51].

There are also other differences that may be attractive to certain companies while predicting insolvency. In France, bankruptcy can only be declared when a company is not able to pay debts after they are due[52]. UK and Germany also require "over-indebtness" when the total of debts exceeds the total assets. Either way, the UK does have a more inviting insolvency regime, when compared to the strict liability that the management faces under German insolvency law. On the other hand, in France, the

[49] See Alexander Schall, "*The UK Limited Company Abroad – How foreign Creditors are protected after Inspire Art (Including a Comparison of UK and German Creditor Protection Rules)"* (2005), 16 European Business Law Review 1534, 1639

[50] Article 18.º of the Portuguese Insolvency Code (Law no º16/2012, 20 April)

[51] See George Schlaefer, "*Forum Shopping under the Regime of the European Insolvency Regime",* 2010, available at http://www.iiiglobal.org/component/jdownloads/finish/39/5922.html

[52] Article L.621-1 Code de Commerce

interests of the employees are a (if not "the") main concern. Also, insolvency proceedings in France, meaning under French law, are "costly and time-consuming which is underlined by the fact that most bankruptcies result in the liquidation of the insolvent firm"[53]. Once again the UK is a better place in comparison to France for the purpose of restructuring and, therefore, it does not come as a surprise that London is regarded as the European "restructuring capital"[54].

Another important distinguishing factor is related to the fact that creditor's interests are attended to differently according to the different Member State. Whilst in the UK minority and unsecured creditors are not very well protected and do not have any control rights, obtaining payout only after the secured creditors' claims have been totally satisfied, the secured creditors gain control rights which allow them to even sell the firm if necessary or to liquidate it. The Managers, i.e. directors, are excluded from all relevant decisions, as all managing powers are taken away from them. [55] On the contrary, in France, an administrator is appointed by the court, whereby the administrator is given control over the company, who must in this order "maintain the firm as a going concern, preserve employment, and satisfy creditors' claims"[56]. If employment is better protected with the sale of the firm, then it may do so. Interestingly, the secured creditors have, in comparison to the UK, a weak position in France, and their approval is neither required for the sale of the firm nor for the reorganization plan! In Germany, there is also an administrator who monitors the bankrupt firm and comes up with a restructuring plan. Nevertheless, in order to approve such a plan, it must be approved by a majority of the secured creditors and, if majority cannot be reached it will be sold[57]. Also, nowadays, there is a big incentive for debtors to shift their COMI to Member States where obtainment of credit and financing is facilitated and easier,

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[53] See Sergei A Davydenko and Julian R Franks, "*Do Bankruptcy Codes Matter? A Study of Defaultas in France, Germany and the UK",* (2008) LXIII The Journal of Finance 565, 603-604

[54] Gerard McCormack, "*Jurisdictional Competition and Forum Shopping in Insolvency Proceedings"*, (2009) 68, The Cambridge Law Journal 169, 180.

[55] Sergei A Davydenko (2008)

[56] Sergei A Davydenko (2008)

[57] see the role of creditors in Wolf-George Ringe, *Forum Shopping under the EU Insolvency Regulation* August 1, 2008, available at Social Science Research Network

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1209822 which will ultimately make the recovery of the company more probable.

In other words, and as resumed by John Armour [58] "secured creditors have traditionally found considerable favour in insolvency proceedings under English law. In contrast, the position of employees has traditionally been privileged in French insolvency law. Different codes also adopt widely different decision-making processes. For example, English law accords considerable weight to the business judgment of an insolvency office-holder, in particular over decisions about the future of the enterprise, and supplements this with creditors' votes. In France, on the other hand, the court makes important decisions such as how the assets should best be realized. German law involves a combination of creditor and court input that might crudely be characterized as lying somewhere between these two cases."

Hence, there are a number of reasons and incentives behind why a company may want to emigrate, by moving its COMI, to another Member State and then file for insolvency proceedings there.

In order to do so, and taking into account that, as we have mentioned, the connecting factor according to the Insolvency Regulation is the debtors COMI, the first necessary step is to understand what exactly is meant by such a term. Under Article 3 (1) of the Insolvency Regulation, the registered office shall be presumed to be the COMI in the absence of proof to the contrary. On the contrary, Recital 13 states that "the COMI should correspond to the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties." These two "definitions" in practice won't (and don't) always correspond, which raises a problem. In other words, the registered office may not (and in many cases does not) correspond to the place where the debtor conducts the administration of its interests. In other words, the place where the head office functions of the company are performed is not necessarily the place where the head office is actually situated.

Member State Courts have had difficulty interpreting this term and have needed to refer to the ECJ various questions in an attempt to desperately obtain clarifications regarding what the meaning of a company's COMI should entail.

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[58] John Armour, "Abuse of European Insolvency Law? A Discussion", p.157-168, chapter taken from Stefan Vogenauer & Rita de La Feria, "Prohibition of Abuse of Law: A New General Principle of EU Law", Studies of the Oxford Institute of Europan & Comparativa Law, Hart Publishing, 2011

It is important to highlight that, while reading and analyzing the ECJ's case law regarding this matter, a certain struggle by the ECJ can be noticed, whilst it desperately tries to balance three things: (1) not put at stake previous ECJ case law which has conferred and developed a number of fundamental rights and freedoms (2) comply with one of the Insolvency Regulations goals which is certainty, predictability and efficiency under Recital 2 (3) whilst also complying with the goal of avoiding forum shopping[59].

Reference will be made to some of these cases that we consider essential for a complete understanding of the conclusions we intend to reach:

2.1. Staubitz-Schreiber

Staubitz-Schreiber[60] is a case that, although concerning personal insolvency, has important consequences surrounding the definition of COMI, for both types of debtors (natural and legal persons). Regarding the relevant facts, a debtor applied to open insolvency proceedings in Germany but, before the application was determined, moved to Spain, to live and work. The German Court stated that it no longer had jurisdiction as the debtor had changed its COMI to Spain, ending up referring to the ECJ for a preliminary ruling. According to the ECJ, the German Court still retained jurisdiction as the debtor changed its COMI in the period between the filing of the request and the opening of proceedings. Therefore, according to Staubitz-Schreiber, "forum shopping" is only ruled out in cases where the debtor has already filed for the opening of the main proceedings. *A contrario sense*, debtors can freely move, before filing for bankruptcy.

This case law is in accordance with recital 4 of the Insolvency Regulation, which clearly states that it is necessary, for the proper functioning of the internal market, to avoid incentives for the parties to transfer judicial proceedings from one Member State to another, in order to obtain a more favourable legal position. "Judicial proceedings" implies that proceedings have already commenced in Court[61] and, therefore, the Regulation was already quite clear that this is not allowed.

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[59] H. Eidenmuller essentially analyses the balance between efficiency and forum shopping.

[60] Case C-1/04 *Staubitz-Schreiber*[2006] ECR I-701

[61] For more on the definition of forum shopping and the meaning of judicial proccedings, see António Frada de Sousa, (2011), p. 11

2.2. Eurofood

Eurofood[62], represents a first major decision of the ECJ related to a corporate debtor's COMI which, according to the ECJ, should be given an "*autonomous and uniform meaning*".

Eurofood was an Irish subsidiary, wholly owned by parent company Parmalat SpA (Italian dairy), which provided financial services to companies in the Parmalat group. Eurofood's registered office was in Dublin. It had two Italian executive directors and two Irish non-executive directors, and all but one of its board meetings took place in Dublin. Following the collapse of Parmalat, insolvency proceedings on behalf of Eurofood were instituted in both Ireland and Italy, leading to dual insolvency proceedings. Whilst the Irish courts considered that Ireland was the company's COMI and that therefore, primary proceedings were appropriate in that jurisdiction, Italian courts, on the other hand, considered Italy to be the place of its COMI. The Irish Court ended up referring the case to the ECJ.

This case clearly "represents a clash between the "Anglo-Saxon" approach of giving a wide, purposive interpretation to COMI, and the "Germanic" strict, literal approach"[63]. The Italian court looked at where the effective management and control of the company was located, using a substance over form test, contrary to the Irish Court, who was focusing on a more strict approach to interpreting the COMI, namely where third-party creditors thought the COMI was located[64].

Advocate-General Jacobs[65] defended a test of "pure head office functions"[66], focusing on where the head office functions of the company were carried out. The ECJ, although partially agreeing, emphasized that the COMI also had to be "objective and ascertainable by third parties". In other words, it stated that the

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[62] Case C-341/04, *Eurofood* [2006] ECR I-3813

[63] Lynn Hiestand & Christian Pilkington, *"Eurofood's COMI Ruling Has Global Implications"*, Jul 1, 2006, (TMA International Headquarters), available at

<http://turnaround.webitects.com/Publications/Articles.aspx?objectID=6300>

[64] Lynn Hiestand (2006)

[65] AG opinion delivered on 27 September 2005, Case C-341/04

[66] Luci Mitchell-Fry & Sarah Lawson, "*Defining COMI: Where are we now?"*, SNR DENTON, available at <http://www.snrdenton.com/news__insights/publications/restructuring_and_insolvency/defining-comi-where-are-we.aspx> whereby it is noted that this is a test which had been applied many times before by the UK courts.

presumption regarding the location of the place of the registered office could be rebutted but only upon demonstration that the debtor regularly administered its interests elsewhere in a manner that was objective and ascertainable by third parties, which, in this case, did not happen. Therefore, the ECJ ended up deciding the case in favor of the Irish liquidator of Eurofood, ruling that main proceedings were properly opened in Ireland rather than in Italy. Note, however, that if it were objective and ascertainable by third parties, it would have ruled otherwise.

Hence, there are extremely important consequences that may be taken from Eurofood. First and foremost, Eurofood goes against the interpretation that the COMI of a subsidiary will always be in the Member State in which its parent company is registered. When a debtor is a subsidiary company whose registered office is situated in a different jurisdiction than of its parent company, it is presumed that the COMI of that subsidiary is situated in the jurisdiction where its registered office is situated. However, such a presumption is rebuttable if there are a number of relevant factors that are both objective and ascertainable by third parties (namely creditors), that indicate that the subsidiary/company does not in fact carry out any type of business in the territory where it has its registered office. The place where the "head office functions" are located, must be attended to and if it does not correspond to the place where it has its registered office, then the former is the essential factor, at once, of course, it is objective and ascertainable by third parties. Ultimately, and this is extremely innovative, the mere fact that the parent company - who has a registered office in another jurisdiction and carries on its business in another jurisdiction - controls or can control the economic choices of its subsidiary is not enough to rebut this presumption.

V. INTEREDIL

1. Case background

Interedil[67] is the most recent case to be decided by the ECJ, providing further guidance on the meaning of a company's COMI.

Interedil srl was a company incorporated in Italy. Its initial registered office was situated in Monopoli, in Italy. However, on 18 July 2001, Interedil transferred its registered office to London,

[67] Case C – 396/09, *Interedil Srl (in liquidation) v Fallimento Interedil Srl and another* [2011] ECR I-0000

registering as a foreign corporation under the British Companies Act 1985 and de-registering from the register of companies of Italy. It then sold its undertaking to a British company known as Canopus by way of a business transfer, this meaning that Interedil transferred properties which it owned in Italy at Taranto to a British company known as Windowmist Limited. After that, is seems as though Interedil was removed from the register of companies of England and Wales. Note that by then Interedil had already de-registered in Italy, so, in fact, it seems as though Interedil no longer had a registered office with the companies register of any Member State. Also, it retained immovable property in Italy (two hotel complexes, lease agreements with another company, agreement with a financial institution).

On 28 October 2003, Intessa Gestione Crediti SpA filed a petition with the Tribunale Ordinario di Bari seeking the opening of Italian insolvency proceedings (fallimento). Interedil challenged the Italian's court's jurisdiction to hear the petition and sought a reference from the Italian Corte di Cassazione. The first instance tribunal did not, however, wait for the Corte di Cassazione to issue a ruling and went ahead and made an order on 24 May 2004 placing Interedil in fallimento. Interedil appealed that decision to the Corte di Cassazione on 18 June 2004.

On 20 May 2005, the Corte di Cassazione ruled on the jurisdiction issue which had been referred by Interedil (i.e. not on the appeal). It purported to apply article 3 (1) of the Regulation and held, according to the ECJ's judgment, that the registered office presumption was rebutted as a result of the assets apparently retained by Interedil in Italy after it de-registered there and after it sold its undertaking to Canopus. Therefore, the Italian Courts ended up referring a number of questions to the ECJ: 1) whether the term "centre of a debtor's main interests" in Article 3 (1) of the Regulation is to be interpreted in accordance with EU Law and if so, what the decisive factors are for the purpose of identifying the COMI; 2) whether the presumption laid down in Article 3 (1) of the Insolvency Regulation, whereby the place of the registered office is presumed to be the COMI, may be rebutted "if it is established that the company carries on genuine business activity in a State other than that in which it has its registered office, or is it necessary, in order for the presumption to be deemed rebutted, to establish that the company has not carried on any business activity in the State in which it has its registered office"; *3)* whether a company that has immovable property in another Member State other than where it has its registered office, if these are sufficient factors or considerations to rebut the presumption laid down in Article 3 (1) of the Insolvency Regulation.

The ECJ had already responded to the first part of the first question in *Eurofood*, by stating that the COMI was to have "an autonomous and uniform meaning" and therefore it was already clear that the expression "COMI" is to be interpreted in accordance with EU law (parag. 43). Regarding the second question, the ECJ did not definitively define COMI nor set out a full list of relevant objective factors and considerations to rebut the registered office presumption, which is understandable as COMI cases depend heavily on the facts[68]. Regarding how the presumption may be rebutted, the ECJ considered that the place where the company has its "central administration" is extremely relevant when determining the competent jurisdiction (parag. 48). In other words, the ECJ stated that if the "bodies responsible for the management and supervision of a company are in the same place as its registered office and the management decisions of the company are taken in a manner that is ascertainable by the third parties, the presumption cannot be rebutted". However, in cases where it can be demonstrated that the "place in which an entity's central administration" is located somewhere other than the registered office, then the presumption can be rebutted (parag. 51).

Regarding the factors to rebut the presumption, the ECJ stated that the company's business operations, besides being objective must also be ascertainable. In other words, similar to what it had done in *Eurofood*, the ECJ took into account the wording of Article 3 (1) and the wording of recital 13 of the Insolvency Regulation, whereby the registered office presumption can only be rebutted by factors which are both objective and ascertainable by third parties. Nonetheless, this time it stated that by *"objective and ascertainable by third parties"* it meant factors that had "been made public or, at the very least, made sufficiently accessible to enable third parties, that is to say in particular the company's creditors, to be aware of them"[69]. In cases where "the bodies responsible for the management and supervision of a company" are located in the same place as the registered office, the presumption may not be rebutted.[70] But, when this is not the case, "objective factors" may entail, for example, "the places in which the debtor company pursues economic activities and all those in which it holds assets". However, these objective factors must be

[68] Luci Mitchell-Fry and Sarah Lawson, *Defining COMI: Where are we now?,* February, 2012, SNR DENTON<http://www.snrdenton.com/news__insights/publications/restructuring_and_insolvency/defining-comi-where-are-we.aspx >

[69] Interedill, Paragraph 49

[70] Interedil, Paragraph 50

ascertainable by third parties.

As above mentioned, Interedil had retained assets in Italy which, in principle, could be taken into account in determining its COMI, at once they qualified as *objective factors*. However, the ECJ concluded that, although they were likely to be in the public domain, unless a "comprehensive assessment of all the relevant factors makes it possible to establish, in a manner that is ascertainable by third parties, that the company's actual centre of management and supervision and of the management of its interests is located in that other Member State"[71], then it can not be considered that Interedil's COMI was in Italy. In other words, by reference solely to the remaining assets in Italy, it is not possible to conclude that Interedil's COMI was in Italy. It was, however, necessary to determine Interedil's COMI on the date at which the opening of the proceedings had been requested. Therefore, taking into account that Interedil's last known registered office was in England and Wales, the ECJ decided that the Italian Courts did not have jurisdiction to open insolvency proceedings.

2. Interedil – In a Nutshell

A corporate debtor's COMI is determined by looking at the place of the company's central administration, which must be established by objective factors that are ascertainable by third parties. Obviously, when the bodies responsible for the management and supervision of a company are located in the same place as its registered office and the management decisions of the company are taken there, in a manner that is ascertainable by third parties, the presumption will not be rebutted. However, in cases where a company's central administration is not in the same place as its registered office, the mere presence of assets and contracts for financial exploitation of those assets in a Member State other than that in which the registered office is situated are not sufficient objective factors to rebut the presumption unless, analyzing all relevant factors make it possible to establish, in a manner that is ascertainable by third parties, that the company's actual centre of management and supervision and of the management of its interests is located in that other Member State.

The ECJ drew a line between a debtor's administrative activities and its business activities, by referring to "*the bodies responsible for the management and supervision of a company*"[72]. It

[71] Interedil, Paragraph 53

[72] Interedil, Parag 50.

concludes in the sense that a company's COMI is to be found at the place where it conducts its administrative activities and not its business activities. Questions have been raised regarding the ECJ's interpretation. For example, Luci Mitchell-Fry and Sarah Lawson [73], question whether "the bodies responsible for the management and supervision of a company" refers to the *de facto* board and, in the case of a positive answer, whether the board has to be in the same place 24/7 or just the majority of the time. They also suggest that it is not always very easy for third party creditors to ascertain this as most creditors usually know more about a company's day to day business operations than its management and supervision. Their main criticism is that "uncertainty remains for COMI determinations". Although we are sensitive to these criticisms, we must not forget that the ECJ, by ascertainable, means "in the public domain", "been made public or, at the very least, made sufficiently accessible to enable third parties, that is to say in particular the company's creditors, to be aware of them". This could be perfectly accomplished by publishing such information on an equivalent to the Member States' Official Journal[74]. Also, and very importantly, ascertainable does not mean that third parties have to effectively know about it. The ECJ in no way states that third parties have to actually know about the shift, but that enough publicity was given to the shift in order for third parties to know[75]. It means that they know or they ought to know. Enough publicity was given in order to consider that the central administration was in the public domain and, therefore, accessible to creditors knowledge. At once this is the case, the shift of the corporate debtor's COMI - to elsewhere other than its registered office - will be perfectly in accordance with EU law. Nevertheless, one thing is for sure: the COMI definition remains unclear and, therefore, this will certainly not be the last ECJ case regarding this topic.

3. Interedil – Registered Office Vs. Central Administration

The ECJ, while interpreting the corporate's COMI, gives less importance to the registered office. It makes it easy (or at least easier) to rebut the presumption, which may indeed be dangerous. The ECJ had a great opportunity to interpret a corporate debtor's COMI in a manner and sense that could, in fact, avoid forum shopping. In order to do so, it could have simply held on to and

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[73] Luci Mitchell-Fry (2012)

[74] For example, in Portugal, Diário da República

[75] in Portuguese terminology, "*conhecer ou dever conhecer*".

given more importance to the place of the registered office, by making the presumption hard to rebut.

Why would the place of the registered office be better? For two reasons: First, because if the COMI is the place of the registered office, there may be additional burdens associated to its shift. With the exception of a limited number of Member States that allow a direct cross-border transfer of a national company's registered office to another Member State, such as Portugal[76], in most Member States a cross border shift of a registered office is done indirectly, via the European Company (SE) or via a cross-border merger, whereby there are a number of safeguards associated to the shift, in order to guarantee that shareholders, creditors and employees interests are protected. So, if the place of the registered office were to be considered the place of the corporate debtor's COMI, before a company migrated for the purposes of benefitting from a different jurisdiction and law, in the majority of situations a number of conditions would have to be fulfilled beforehand. Also, they would have to register in the new Member State, making it easier for third parties' interests to be protected. Second, and more importantly, if a corporate debtor's COMI is the place of its registered office, it would at least allow creditors to have some certainty about the place considered to be the place of its COMI and, consequently, have more certainty regarding the competent jurisdiction and applicable law if future insolvency proceedings were to apply. In other words, at the time the loan or credit is granted, the creditor, being as cautious as possible, could look at the place of the registered office of the other party, future debtor. By doing so, the creditor becomes aware of the jurisdiction and, consequently, the applicable law to future possible litigation proceedings connected to the credit granted. In fact, this is why many authors defend that abolishing a "rebuttable presumption" could be a solution to Insolvency forum shopping, because it would allow for a "predictable jurisdiction venue" and a "predictable applicable insolvency law," which, obviously reduces information costs and enhances the efficiency of a reorganization procedure[77]. We are now left with a regime whereby the place of the central administration[78] is relevant (of course, at once it is objective and ascertainable by third parties), leaving room for more

[76] Article 3 of the Portuguese Company's Law Act (Código das Sociedades Comerciais)

[77] Wolf George Ringe, (2008), p. 18

[78] Jean-Luc Vallens, "Transfert du siège et transfert du centre des intérêts principaux", Procédure d'insolvabilité, Recueil Le Dalloz, 2011, p.2915 – 2919

uncertainty and, in fact, very little protection for creditors. This is why it is, at least to us, surprising that the ECJ would, in fact, make the place of the registered office more easily rebuttable because, by doing so, it seems to put at stake three of the insolvency Regulation's goals: efficiency of the insolvency proceedings, protection of creditors and also avoidance of forum shopping. Creditors will most likely look at the place of the registered office as a determinant factor whether to give credit or not. But if it is the place of the effective central administration that is indeed relevant, creditors – even the most aware ones – can do nothing against a shift of a debtors COMI to another Member State. Even so, whilst creditors hypothetically could certify that a debtor's COMI remains the same, it is difficult and involves extra costs, to control if the debtor has moved their central administration to another Member State. And if the debtor does successfully change its COMI, creditors will then have to claim credits in a jurisdiction that they do not know, under a law they are not familiar with, which also involves further costs and which is, ultimately, less efficient. Therefore, Wolf George Ringe's [79] criticisms after *Eurofood*, are still, in general, applicable. The definition of COMI remains "fuzzy"[80], in the sense that it remains an unpredictable criterion for one that is of "such importance for the reorganization procedure which a company might face" and "represents a high burden on the effectiveness of any business activity", also raising "the information costs". Creditors are left in an unprotected situation, having, apparently, no way to stop a shift of a debtors' COMI to another Member State. By moving away from the place of the registered office, shifts of debtors' COMI are facilitated. Ultimately, the interpretation given by the ECJ may actually open doors to forum shopping. A company, predicting its insolvency can shift its COMI to another Member State, by simply moving the control of its central administration there, needing merely to certify that such a shift is objective and ascertainable to third parties. Little certainty or safety is left for creditors' interests, hence must be addressed as a huge concern.

So, after Interedil, what are we left with? Cross border insolvency and (abusive) forum shopping being welcomed with wide "open" doors? Until a similar situation is addressed by the ECJ, is there any possible way to halt shifts of COMI for pure insolvency reasons?

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[79] Wolf-George Ringe, (2008) , p. 26

[80] Horst Eidenmüller, 'Free Choice in International Company Insolvency Law in Europe' (2005) 6, Eur Business Organization L Rev 423, 434 ff.

VI. EU Fundamental Freedoms – Impossibility to Ever Forbid Shifts of Debtors' COMI?

1. Freedom of Establishment – (In)Direct Choice of Insolvency Law

As above suggested (chapter III), forum shopping is a natural consequence of EU Law and its fundamental freedoms. As noted by Wolf-George Ringe[81], "quite independently from the discussion for and against the benefits of forum shopping, it can be argued that already the current impetus of EC law, namely its fundamental freedoms, mandates for the admissibility of forum shopping". The ECJ has already stated that using to ones benefit the "disparities of different jurisdictions within the Internal Market" is perfectly acceptable.[82] Therefore, we must not interpret insolvency forum shopping in a stricter way than the Insolvency Regulation or former ECJ case law. At the same time, it can not mean that all types of insolvency forum shopping ought to be allowed under freedom of establishment.

A first question that must be asked is whether insolvency law falls within the scope of fundamental freedoms, namely freedom of establishment (our main concern in this paper). This question is raised because there are authors that defend that the scope of freedom of establishment is limited to provisions of company law[83]. Obviously, we do not agree with such a position. There is nothing in EU law that even suggests that freedom of establishment is confined to company law. If this were the case, Member States could, for example, hide company rules that restrict freedom of establishment under their insolvency law[84]. Also this does not make sense as company law and insolvency law are connected to each other in many ways. Article 49 refers to restrictions on the freedom of establishment and, naturally, there are many Member States' rules that can cause these restrictions

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[81] Wolf-George Ringe, (2008), p. 22

[82] Case C-212/97 *Centros Ltd v Erhvervs og Selskabsstyrelsen* [1999] ECR I-1459

[83] P Ulmer, 'Gläubigerschutz bei Scheinauslandsgesellschaften- Zum Verhältnis zwischen gläubigerschützendem nationalem Gesellschafts-, Delikts- und Insolvenzrecht und der EG- Niederlassungsfreiheit' (2004) Neue Juristische Wochenschrift 1201, 1205. Also, P Kindler, 'Internationales Insolvenzrecht' in K Rebmann and others *Münchener Kommentar zum Bürgerlichen Gesetzbuch* (4th ed CH Beck, Munich 2006) vol 11 para 43.

[84] John Armour, 'Who should make corporate law? EC legislation versus Regulatory Competition' (2005) 58 Current Legal Problems 369, 402.

and not just company law (for example tax, social security, procedural law, etc.).[85]

When aware of the meaning of freedom of establishment, the power surrounding the term and connecting factor chosen by the Insolvency Regulation (COMI) becomes evident. It means that a debtor may raise debts in a certain Member State and then, predicting its insolvency, and aware of the applicable law, plan a shift of its COMI to another Member State with a more favorable forum and, consequently, more favourable insolvency law. In other words, it means that there is a choice of insolvency law. It means that one of the goals of the Insolvency Regulation - avoid incentives for forum shopping - may not be achieved.

Nevertheless, to say that it was the Insolvency Regulation that gave rise to the possibility to forum shop would not be a fair accusation. As noted previously, the EU, over the past decades, through its legislation and contribution from the ECJ, has constructed an Internal Market that is not just an economic market – one of its initial goals – but a market that confers to all EU citizens and legal persons, a number of fundamental freedoms and rights, namely the right of free movement and establishment within any Member State[86]. In principle, no Member State can deny citizens or companies from other Member States to move their habitual residence or registered office (or central administration!) there, as this would mean a serious breach of EU law. By not denying them freedom of movement and establishment, they can then not deny them the right to benefit from their substantive laws. Therefore, it seems as though, as long as there is a European Union, an Internal Market and fundamental freedoms, there will always be forum shopping.

Knowing that moving to another Member State in order to benefit from a more favourable law is included in freedom of establishment, the next necessary step is to determine when that freedom of establishment may be restricted.

2. Restrictions on the freedom of establishment

Under Article 49 and 54 of the TFEU, restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State are, in principle, prohibited. Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the European Union must be treated in

[85] Wolf-George Ringe (2008), p. 23

[86] Title IV, Chapter I of TFEU

the same way as natural persons who are nationals of Member States. In other words, any obstacle that creates barriers or difficulties to establish in another Member State may be in breach of freedom of establishment, unless it can be justified. Therefore, and as referred by Wolf-George Ringe[87] "every attempt to hinder company migration or to make it less attractive – even and in particular in the vicinity of insolvency – is liable to violate the freedom of establishment."

But what is considered restrictive? According to Advocate General Kokott, in her opinion to Interedil, although it is clear that creditors interests may be unprotected by allowing COMI shifts, if these shifts were to be strictly regulated, freedom of establishment would be at stake. Even a requirement such as a time limit between the transfer of COMI and the filing for insolvency, would put at stake the freedom of establishment[88], according to Advocate General Kokott. Unfortunately, she does not analyse the question of abuse in detail as that question regarding the lawfulness of the transfer and/or the eventual fraud or abuse that such a transfer may entail to the creditors rights was not referred to the ECJ. To this extent, we can agree with AG Kokott's opinion. Where we have difficulty in agreeing is with something that is said further on. In paragraph 71, she refers that all acts related to the liquidation of a company are, in principle, relevant for determining the COMI because, "after all" a shift of a companies' COMI to another Member State in order to proceed with its liquidation is also covered by EU fundamental freedoms (!). In other words, the AG states that, if a corporate debtor chooses to move its COMI to a different Member State purely for the purpose of its dissolution or liquidation pursuant to that Member State's insolvency regime, then that was also a legitimate purpose and an expression of Freedom of Establishment. She continues by saying that if the management of the liquidation is done from its new COMI, in a way that is ascertainable by third parties, during the period previous to its extinction, then that will be the place of its COMI[89]. This, to us, is not acceptable. Not all shifts of COMI may be allowed, under freedom of establishment. It is true that Member States, in principle, may not restrict freedom of establishment. However, this does not mean that no restrictions are allowed. If they are justifiable under EU law, there will be no problem with it, whatsoever.

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[87] Wolf-George Ringe, (2008) p. 29

[88] Paragraph 45-48 of AG Kokott's opinion to Interedil

[89] In this case Interedil had registered in England, so, in fact there weren't much doubts or need to rebut the presumption

Therefore, we partially agree with what is said by AG Kokott in her opinion to Interedil: (i) Although we agree that some kind of transfer of COMI will always be allowed, because of freedom of establishment, (ii) we do not go as far as defending that all and every form of shift of COMI should be allowed under European Union law. It is true that Member States have assumed the obligation to create an Internal Market and to guarantee that it functions adequately. Member States are obliged to remove all obstacles, which in any way may be a threat or may hinder cross border circulation of goods, persons, services and capital throughout the European Union. This means that, in principle, domestic rules and measures that are protective of a Member State are not allowed. Nonetheless, this does not mean that fundamental freedoms (namely freedom of establishment) are absolute. Member States may restrict freedom of establishment, once such restriction is justifiable under EU law.

In other words, although it is true that COMI shifts will never be completely forbidden, this does not mean that certain shifts may not be restricted. They may be, once such restrictions are justifiable under EU law.

3. Not every type of shift of a Debtor's COMI should be allowed: How to solve the Problem?

3.1. Changing the Insolvency Regulation – Defining COMI & Introducing An Irrebuttable Presumption

The Insolvency Regulation has now been in force since 31 May 2002 and, as we have seen, applies whenever a debtor has assets or creditors in more than one Member State, setting out provisions in relation to jurisdiction, recognition, applicable law and the coordination of insolvency proceedings opened in several member states. On 17 October, 2011, the European Parliament published a report whereby it recommends a number of alterations. One of the four main proposals set forward by the European Parliament[90] concerns revising the Insolvency Regulation, namely, the introduction of a formal definition of COMI, formulated in such a way as to prevent fraudulent forum-shopping. According to the suggestions set forward, this formal definition should be inserted, based on the wording of recital 13, which is concerned with the objective possibility for third parties to ascertain it and the

[90] EU parliament Resolution 15th November 2011, available at <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2011-0484+0+DOC+XML+V0//EN >

definition should take account "such features as the externally ascertainable principal transaction of business operations, the location of assets, the centre of the operational or production activities, the workplaces of employees, etc.".

The Commission, on 30 March 2012, decided to consider revising the Insolvency Regulation and opened consultation on the future of European Insolvency law, to seek the views of the public on the issues involved[91]. Amongst other questions the consultation raised, the following are linked to what concerns us in this paper: "Is it correct that the Insolvency Regulation provides that only the courts of the member state in which the debtor has the centre of its main interests have jurisdiction to open main insolvency proceedings, or has this concept been open to abuse by debtors or the interpretation of this concept by the courts been problematic?" and "Are there difficulties created by the lack of harmonisation of the various national laws on insolvency, and are there any particular inefficiencies in the various national laws?".

The report published by the European Parliament dated 17 October, just three days before Interedil was decided (20 October, 2011). Perhaps the questions posed in the report would have been different if Interedil had been decided beforehand. We will never know. Nevertheless, one thing is for sure: the ECJ in Interedil did set forward guidelines to the questions that it asks, regarding what should be considered "ascertainable and objective to third parties". Also, it seems to us as though, a formal definition, being set forward, would not leave us far from what we have and where we are now, because the Commission will, most probably, take into account the ECJ's case law while trying to set forward a formal definition of COMI.

Also, many suggest that a corporate debtors' COMI should be the place of its registered office, defending that it should be an irrebuttable presumption. As noted above, there would be a number of advantages associated to this. It would allow for more certainty for creditors, and it would lead to less cost information and, consequently, more efficiency, which are all goals of the Insolvency Regulation. Nevertheless, it would not stop forum shopping. It may make it slightly more complicated for a corporate debtor to shift its COMI, as there may be a number of extra safeguards related to the changing of a company's registered office, but it will not stop shifts of COMI to take place, nor will it be capable of distinguishing when a shift is abusive or not.

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[91] The deadline for responses to the consultation was 21 June 2012, whereby a number of responses were submitted, although the report on the feedback by the Commission is still awaited

3.2. Harmonized Substantive Insolvency Law Vs. Convergence – an option?

There are two reasons why a formal definition of COMI and an irrebutable presumption would never be capable to solve this phenomenon of insolvency tourism and COMI shifts. On the one hand, because, as above mentioned, as long as there is freedom of movement, in the case of individuals, and freedom of establishment, in the case of companies, debtors will always be able to plan a shift of their COMI. On the other hand, Member States will continue to not have identical conditions and identical insolvency substantive law, meaning there will always be an incentive to forum and law shop, because the Insolvency Regulation is "only" a Regulation on private international law rules. Many, therefore, defend harmonizing substantive law as a generic solution for forum shopping. Others point to convergence. Neither, in our view, solve the problem.

Regarding harmonization[92], it is first and foremost unlikely that Member States would come to an agreement on a unified substantive insolvency law. But even if they did, it would not solve the problem. Regarding harmonization in general, some authors, such as Pierre Legrand, are very skeptical towards such possibility, arguing that each Member State would continue to have cultural differences which will lead them to interpret and apply the law differently[93]. Each Member State will continue to interpret and apply their law according to their system, "*the English man will continue to look at European measures as a common lawyer and the Frenchman as a civil lawyer*". Others defend that it represents "a reckless denial of legitimate difference between the legal systems of Europe".[94] Also, even if this were a possibility, it would take a long time before this was legislated and approved and what we need at the moment is a rapid and temporary solution to face insolvency migration.

Ultimately, harmonization of substantive insolvency law does not eliminate all differences between Member States. There

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[92] For more on Convergence, see Jan M Smits, *Convergence of Private Law in Europe: Towards a New Ius Commune?,* in comparative law, A handbook edited by Esin Orucu and David Nelken, Hart publishing, Oxford, 2007.

[93] Vide Jan M Smits, (2007)

[94] Roger Cotterrell, "Is it so bad to be different? Comparative Law and the Appreciation of Diversity", in "Comparative Law- A handbook edited by Esin Orucu and David Nelken, Hart publishing, Oxford, 2007

will always be differentiating factors. For example, certain Member States may be faster at deciding insolvency proceedings; Certain Member States' Courts may interpret and apply the same law in a different way. In fact, in the USA, there is harmonized insolvency law throughout the States and, even so, there is still forum shopping.

Regarding Convergence [95], it also does not solve our problem. It is true that the conditions for the "market of legal rules" to function are in place. First, debtors are able to choose (directly or indirectly) a jurisdiction and its law because of the fundamental freedoms guaranteed under the EU Treaties. Second, there is a possibility in engaging in regulatory arbitrage. And, third, there is a "threat of migration to the more favourable jurisdiction". National legal systems are, indeed, competing. It is also evident that there is a phenomenon across the EU whereby most Member States have either changed their Insolvency laws or are changing them. Innumerous Member States are altering their national insolvency substantive law, making it more similar to the ones of other member States that are more attractive[96]. It is also a known fact that Member States are happier to converge than to harmonize, as convergence allows to unify its substantive law but it will be from legal practice itself and not by "imposition from above". Notwithstanding, and as pointed out regarding harmonization, there will still be differences and incentives to migrate to other Member States. Also, before convergence happens – and note that it will not happen in all domains and/ or in all Member States, in a short period of time - we need a temporary solution. Creditors' interests must and need to be protected.

3.3. Introducing a time limit

Advocate General Kokott, in paragraph 48 of her opinion to the *Interedil* case, states that freedom of establishment would be damaged, at least indirectly, with a restrictive regulation. According to the AG, imposing a time limit for the new COMI to be in the new Member State before filing for insolvency proceedings would be restrictive. Unfortunately, she does not develop this

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[95] For more on convergence see Anthony Ogus, "Competition Between National Legal Systems: A Contribution of Economic Analysis To Comparative Law" (1999), International and Comparative Law Quarterly, 48, pp 405-418

[96] Ireland, for example, is changing its legislation, negotiating alterations regarding the discharge period of 12 years to 3 years.

argument because in the present case the transfer had occurred a year before the filing for insolvency.

It is needless to say that restrictive measures to freedom of establishment are allowed if they are justifiable. Fundamental freedoms, namely freedom of establishment, is not an absolute freedom, hence must be balanced with other freedoms and with other rights. Creditors' interests must also be taken into consideration, also deserving protection. Therefore, introducing a time limit, whereby a company before filing for insolvency in a certain Member State would have to show evidence of being there for a one or two year period, for example, is a restriction that is easily justifiable, in our view. It would be a way to guarantee that companies are not moving to a new member State to benefit from a new law, leaving creditors in a worse off position. It would be a way to avoid abusive shifts of COMI.

Nevertheless, unfortunately this measure presents its fragilities and, therefore, we do not see it as a viable solution to our concerns. Considering the following example: a Portuguese company, registered under Portuguese Law, shifts its central administration (its COMI) to the UK. Eleven months later, that company starts to show difficulties and after trying to overcome its struggles, concludes that it must file for insolvency. By imposing a time limit of one year, this company does not qualify for the opening of insolvency proceedings in UK Courts and, consequently, it is not the UK insolvency law that will apply. This company that, note, after 11 months may have no other connection with Portugal, other than the fact that it had its previous COMI there (registered office), will be forced to go back to Portugal, in order to open insolvency proceedings there. Note that it may have nothing in Portugal, having all its activity and assets in the UK. Does it make sense to have to file for insolvency proceedings in Portugal when its central administration has been in the UK for the past eleven months? Not only does it not make sense, but it also is not efficient, another goal of the insolvency Regulation, leading to extra costs. At the same time, a one year period is not that long a time to have to be in another Member State before opening proceedings there. In other words, a one year time limit may not be a sufficient safeguard for (abusive) forum shopping. Therefore, if a time limit were to be imposed, we believe that it would be at least an 18 to 24 month time limit. Applying the abovementioned example to this new time limit, the consequences are even more dramatic.

3.4. Requirement That Consists In the Debtor Seeking Assent of its Creditors with respect to a Planned COMI Shift

Many authors such as H. Eidenmuller[97] and John Armour[98] make this suggestion, whereby creditors could include loan covenants specifying that reincorporation without their consent would constitute an event of default. Also, such a possibility of regulatory arbitrage would be taken into account in the loan contracts. Basically, this possibility concerns a clause, inserted in a loan or financing contract, whereby the creditor and debtor agree that a shift of the debtors COMI depends on the creditors consent. It is not the Member State that imposes the creditor to give its consent in such cases (in which case, it is possible that freedom of establishment would be put at stake). On the contrary, the debtor agrees to the limitation and restriction of future COMI shifts by signing such a contract. Such clauses are more and more frequent, nowadays, as they allow creditors some guarantee and reinsurance that their interests will not be left unprotected. It allows them a degree of protection and certainty about the predictable forum and applicable law, should future judicial proceedings apply. Ultimately, by inserting such a clause, the creditor will incur less costs.

Nevertheless, although agreeing that such a measure would allow for protection of the creditor's interests, it raises a number of doubts to us, and does not seem to be a perfect solution, we think. It is true that the debtor only gives its consent if it wishes to. But it is also true that those who need the credit (the debtor) will always be in a less favourable position and, therefore, may be forced into giving their consent to such a clause, as if they don't, credit will not be granted. With this clause, creditors are enabled with a huge amount of power. The replacement of a debtors COMI (hence freedom of establishment of a company) is put in the hands of a creditor, giving it the power to authorize or not the shift of its COMI, when such a shift may be essential to save the company and its business.

Also, it is dubious to us, whether this measure contradicts, in a certain way, the interpretation that the ECJ gives, in Interedil, to the role and importance of the place of the registered office, whereby, it may be easily rebutted. By handing so much power to creditors, it seems to give the place of the registered office, the power and role that the ECJ said that it did not have.

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[97] This is suggested in Horst Eidenmuller, Abuse of law in the context of European Insolvency Law, in Proibition of Abuse of Law: A new general principle of EU Law?, edited by Rita de La Feria and Stefan Vogenauer, 2011, p. 146

[98] John Armour, 'Who should make corporate law? EC legislation versus Regulatory Competition' (2005), 58 Current Legal Problems 369, 402, p. 30-31

VII. Abuse Of Law - Principle of prohibition of abusive practices

The above measures (formal definition, irrebutable presumption, time limit and creditor's assent) were presented as possible solutions to the situation that we have at the moment, although they all present certain fragilities and are not perfect solutions. In the absence of coming up with a perfect justifiable restrictive measure to freedom of establishment that is, at the same time, capable of distinguishing and stopping abusive shifts of corporate debtors' COMI, comfort may be found in the principle of prohibition of abusive practices, considered by many, such as Rita de la Féria, to be a general principle of EU Law.

As analysed, under the current European Union design of freedom of establishment, it is impossible to simply forbid this type of Insolvency forum shopping. As pointed out by Adrian Walters and Anton Smith[99], "as the freedom of EU citizens to relocate from one MS to another is enshrined within the European legal order, the question begged is whether any relocation involving a forum shop, be it temporary or permanent, should be regarded as an undesirable abuse of EU law freedoms or whether this is only so where the relocation is an outright fiction". Also, António Frada de Sousa distinguishes between forum shopping and abusive forum shopping[100]. Therefore, a main and primary distinction that must be made is between shifts of COMI which are totally abusive and shifts of COMI that, although benefiting from a more favourable law, are not abusive.

The ECJ has stated in numerous cases that fundamental freedoms can be restricted when there are abusive structures at stake. But where is the borderline to be drawn? What is abusive? A corporate debtor that shifts it's COMI in order to treat and try to save its business, is that abusive? What about a company, that has no hope for survival, and that, benefiting from its freedom of establishment, shifts its COMI to another Member State only to benefit from its insolvency rules and harm creditors, is that abusive? Should there be a difference in treatment regarding both of these two examples? Where should the line be drawn? How

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[99] Adrian Walters (2009)

[100] António Frada de Sousa "*Exoneração do passivo restante e fórum shopping na insolvência de pessoas singulares na União Europeia*", in "Estudos em Memória do Prof. Doutor J. L. Saldanha Sanches - Vol II", Coimbra Editora (2011), p. 92-98

would or should the ECJ decide when there is no rational reason except for the fact that the debtor wants to benefit from a more favourable law, this meaning that there is only an artificial arrangement? It should only be in the absence of alleged abuse or fraud that a transfer of the central administration ought to be licit under freedom of establishment[101]. When this is not the case, then freedom of establishment may be licitly restricted. Nontheless, in order to attempt answering this question, it is indispensable to look at former ECJ case-law, regarding abuse of law.

The concept of "abuse of law" has not only attained a certain prominence at European level in tax law, the discipline in which it was originally conceived, but also in the case of company law[102] and now in Insolvency law. As above mentioned, the ECJ, in Interedil did not, unfortunately, comment on any possible situation of abuse of law. In fact, AG Kokott, in paragraph 72 of her opinion, stated that the question regarding the potential abusive character of a shift of COMI raises interesting questions about the balance between fundamental freedoms of the debtor, on the one hand, and the protection of the creditor and concern in combatting forum shopping referred to in recital 4 of the Insolvency Regulation, on the other hand. She also stated that the *Centros* case law would be relevant in analyzing such balance, as the ECJ had held there that, the fact that a company makes use of its freedom of establishment, to benefit from legal rules that are more favourable to them, does not constitute abuse of freedom of establishment. Nevertheless, because the Italian Court had not posed a question regarding this issue, and because the facts did not entail abuse, it was not an adequate place or time to discuss such a question in a conclusive manner. But what if that question related to abuse had been asked? What if the court had been asked how such a balance should be reached?

1. Centros

The first reference to abuse and abusive practices was in *Van Binsbergen* case[103], where the ECJ's initial approach was that national legislation preventing circumvention was not contrary to EU law.

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[101] Jean-Luc Vallens, (2011), p.2915 – 2919

[102] Wolf-George Ringe, "Sparking Regulatory competition in European Company Law: the impact of the Centros Line of Case Law and its concept of "abuse of law", in Prohibition of Abuse of Law, a new general princiale of EU, edited by Rita de la Feria and Stefan Vogenauer.

[103] Case 33/74 *Van Binsbergen v Bestuur van de Bedrijfsvereniging* [1974] ECR 1299

It was then developed with freedom of establishment in the *Centros* case. In fact, it was *Centros*[104] that created a certain awareness of the possibilities that the Internal Market offered and the debate concerning the abuse and misuse of fundamental freedoms in company law, as the Court declared conduct that was previously considered abusive, to be covered by the freedom of establishment[105].

Regarding the facts of the case, in *Centros*, a Danish couple set up a company in the UK in order to then form a branch in Denmark in order to circumvent the strict Danish capital requirements for companies. The Danish authorities refused to recognize the foreign company, as it regarded this as constituting an abuse of freedom of establishment[106] and the Courts referred the question to the ECJ. The ECJ did affirm that abusive or fraudulent exercise of community law would not be permissible. Nevertheless "although in such circumstances, the national courts may, case by case, take account – on the basis of objective evidence – of abuse or fraudulent conduct … they must nevertheless assess such conduct in the light of the objectives pursued by those provisions."[107] It therefore concluded that the fact that someone who chooses to set up a company in a Member State that has less restrictive company law and then sets up branches in other Member States "cannot in itself, constitute an abuse of the right of establishment … but its inherent in the exercise, in a single market, of the freedom of establishment guaranteed by the treaty"[108].

Nonetheless, the ECJ did refer to the Member State's capacity to restrict fundamental freedoms, whereby in such circumstances national courts ought to (a) take account of abuse or fraudulent conduct on a case by case basis; (b) act on the basis of objective evidence; and (c) assess such conduct in the light of the objectives pursued by Community law provisions. In other words, freedom of establishment may not be restricted by general anti-avoidance rules that prevent national courts from examining each case individually.

The ECJ stated that the mere fact that a EU citizen exercised its secondary right of establishment in another State in order to benefit from more favourable legislation does not in itself

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[104] Case C-212/97 *Centros Ltd v Erhvervs-og Selskabsstyrelsen* [1999] ECR I-1459

[105] Wolf-George Ringe (2009)

[106] Centros, Paragraph 23

[107] Centros, paragraph 25

[108] Centros, paragraph 27

constitute abuse, adding that the fact that the UK company did not conduct any business in the UK and pursued its activities solely through its branch in Denmark was not enough to prove the existence of abuse or fraud[109]. In other words, the ECJ said in *Centros* that a company may choose where it wants to be established even if the only motive for establishing in another Member State is the fact that it is more beneficial. In other words, not all circumvention situations constitute abuse.

2. Uberseering & Inspire Art

In the *Uberseering*[110] case and *Inspire Art Ltd* case[111], the ECJ, once again, made clear that Articles 49 and 54 of the TFEU prevent Member States through its national legislation from imposing certain conditions on companies formed in accordance with the law of another Member State for the exercise of secondary establishment. What was stated in *Centros* was upheld in *Uberseering* and *Inspire Art*. However, the ECJ did state that certain measures implemented by national legislation may be allowed in order to protect certain interests.

In *Inspire Art Ltd*, an EU citizen seeking to circumvent domestic rules regarding minimum share capital requisites by incorporating a company in another Member State (the UK) through the creation of a branch, hence exercising its secondary right of establishment, was denied such a right by the Dutch Authorities. The case reached the ECJ that said that the "reasons for which the company was formed in that other Member State, and the fact that it carries on its activities exclusively or almost exclusively in the Member State of [secondary] establishment, do not deprive it of the right to invoke the freedom of establishment guaranteed by the EC Treaty, save where the existence of an abuse is established on a case by case basis."[112] It was, therefore, essential to determine whether there was any type of abuse. According to the ECJ, the requirement for foreign companies to satisfy the minimum share capital rules imposed by Dutch law was deemed to hinder or make less attractive the exercise of the freedom of establishment, hence had to fulfill four conditions in order to be justifiable: (i) it had to be applied in a non discriminatory manner; (ii) it had to be justified by imperative requirements in the general interest; (iii) it had to be suitable for

[109] Paragraph 29

[110] Case C-208/00 *Überseering* [2002] ECR I-9919

[111] Case C-167/01 *Inspire Art* [2003] ECR I-10155

[112] Paragraph 143 Inspire Art

securing the attainment of the objective which it pursues; and (iv) must not go beyond what is necessary in order to attain such objective.[113] Hence, the Dutch rules were declared incompatible with EU law.

Reference is made to these cases to prove that there is nothing wrong with looking for more favourable legislation (forum shopping). What is condemned by the ECJ is abusive, fraudulent and improper conduct. And by mentioning this, the ECJ is very careful, stating that an abusive or fraudulent conduct must be identified on a case-by-case basis, on the basis of objective evidence and in the light of EU law, and not by reference to general rules.

3. Cadbury Schweppes – Wholly artificial Arrangement vs Genuine Economic Activity

In *Cadbury Schweppes*[114] the ECJ was confronted with a case whereby a UK parent company wanted to establish two subsidiaries in the territory of another Member State in order to benefit from a lower taxation rate[115]. According to the ECJ, "the fact that a Community national, whether a natural or a legal person, sought to profit from tax advantages in force in a Member State other than his State of residence cannot in itself deprive him of the right to rely on the provisions of the Treaty"[116].

This case is very important because the ECJ specified that a national measure that restricts the freedom of establishment may be justified in cases where it specifically targets wholly artificial arrangements aimed at circumventing the application of the legislation of the Member State concerned[117]. It is, therefore, the concept of '*wholly artificial arrangement*' that may be used to distinguish what is acceptable and what is not acceptable tax planning, what is and is not abusive. It is a determinant factor when analyzing whether a restriction is justifiable or not. In Marks & Spencer[118] case, the ECJ had already made it "clear that Member States are free to adopt or to maintain in force rules having the specific purpose of precluding from a tax benefit wholly artificial arrangements whose purpose is to circumvent or escape national tax law".[119]

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[113] Paragraph 133 Inspire Art

[114] Case C-196/04, *Cadbury Schweppes*, [2006] ECR I-7995

[115] *Cadbury Schweppes,* Paragraph 18,

[116] *Cadbury Schweppes,* Paragraph 36

[117] *Cadbury Schweppes,* Paragraph 51

[118] C-446/03 *Marks & Spencer* [2005] ECR I-10837

[119] *Marks & spencers* Paragraph 57

But what exactly is a "wholly artificial arrangement", hence abusive? It is, essentially, a creation that does not reflect economic reality, intending merely to escape a legal norm from its national territory[120]. The ECJ went further by laying down a test regarding what a "wholly artificial arrangement" entails, a test that consists of a subjective and an objective element. Whilst the former entails an "intention to obtain a tax advantage", the latter requires the existence of "objective circumstances showing that, despite the formal observance of the conditions laid down in Community law, the objective pursued by freedom of establishment…has not been achieved."[121] Both elements must be fulfilled. This means that intention is not sufficient on its own, nor are objective circumstances sufficient on their own. It is this test that will then allow us to conclude whether the establishment constitutes a fictitious arrangement or a genuine economic reality.

VIII. Abusive Shifts Of COMI – Genuine Economic Activity

The meaning of "wholly artificial arrangements" regarding tax law and company law seems to be clear (or at least clearer), nowadays. The new "*quaestio famosa*" [122] is what is abusive insolvency forum shopping? What are "wholly artificial arrangements" for insolvency purposes? Can it be used to determine a line between what is permitted under EU law and what should not be permitted, regarding cross-border insolvency?

Horst Eidenmuller[123] says that the Insolvency Regulation has two main goal and that "COMI shifts that do not contribute to maximizing the debtors' net assets are abusive". This will be the case if a COMI shift is evidently only undertaken to benefit the debtor at the expense of its creditors or some creditors at the expense of others."[124] According to this author, the main criterion for an abuse is the (in)capability of the conduct to further the maximization of the debtor's net assets that are available to satisfy the creditors' claims. Only in the cases where the COMI shift is capable of maximizing the net assets, should it be considered to be non-abusive. Hence, if the shift did not lead to a maximization of

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[120] *Cadbury Schweppes,* Paragraph 55

[121] *Cadbury Schweppes*, Paragraph 64

[122] Wolf-Georg Ringe (2009)

[123] Horst Eidenmuller, Abuse of law in the context of European Insolvency Law, in Proibition of Abuse of Law: A new general principle of EU Law?, edited by Rita de La Feria and Stefan Vogenauer, 2011

[124] Horst Eidenmuller, (2011), p. 144

the net assets it should be considered abusive. These are very valid considerations. Nonetheless, we would like to look at former ECJ case law and apply it to our present concerns.

So, as previously noted, whilst the ECJ in *Centros* stated that the mere fact that a company incorporated in a certain Member State in order to avoid laws that would apply to that company if it were to be incorporated in another Member State does not constitute abuse of the freedom of establishment, it also stated in *Cadbury Schweppes* that "*wholly artificial arrangements*" are not allowed, meaning that there must be an "actual pursuit of an economic activity through a fixed establishment in that State for an indefinite period". In other words, there must be an actual establishment of the company concerned in the host Member State and the pursuit of genuine economic activity there[125]. As stated by Horst Eidenmuller, "with this jurisprudence, the door has been opened for free choice of the applicable company law regime and regulatory competition in the area of company law regime and regulatory competition in the area of company law in Europe"[126]. We believe that such conclusions regarding freedom of establishment in a "company law perspective" apply also to insolvency law.

The terminology of "wholly artificial arrangements" and the need to pursue a genuine economic activity is essential while defining what is and what should be abusive insolvency forum law shopping. A debtor that shifts their COMI to another Member State will be abusive, hence not allowed under EU law, if it is a wholly artificial arrangement, this meaning, if it fails to entail the pursuit of a genuine economic activity in the new Member State[127]. This will be the case when a company migrates solely to *die*[128]. In other words, when it has no perspective whatsoever to benefit from this new law to the interests of the company and its creditors. A shift of a corporate debtor's COMI for pure liquidation reasons, benefiting the management of the company at the cost of creditors must be treated differently to shifts of COMI that intend to benefit from a new insolvency law that gives it more chances of

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[125] Wolf-Georg Ringe, (2009)

[126] Horst Eidenmuller, (2009)

[127] Cadbury-Schweppes, parag. 54

[128] See A. Frada de Sousa, who defends this distinction regarding companies that move to "die" and that move to "treat" their insolvency - Antonio Frada de Sousa, "A Europeização do Direito Internacional Privado – Os novos rumos na regulamentação das situações privadas transnacionais na UE", Dissertação de Doutoramento, Universidade Católica Portuguesa, Porto, [policopiado] Maio 2012, p. 718 – 733.

restructuring and saving the company. For example, the Member Sate of the new COMI may be a Member State where credit is granted easier, enlarging possibilities of saving the company.

Therefore, in order to determine whether a shift of a debtors COMI should be condemned or not, a distinction must be made between companies that manipulate the definition of COMI and migrate with the intention to *die*, for pure liquidation reasons, and fails to perform any genuine economic activity there, but merely to minimize or benefit from tax or criminal consequences, and companies that are, in fact, effectively struggling to keep their business above water level and migrate in an attempt to treat their insolvency and save their business[129]. The former should be condemned and can not nor should not be treated in the same way as the latter. In other words, a distinction must be made between a company that moves to another Member State for its funeral (here it is prejudicial) and a company that moves to another Member State for intensive care, to treat and try to save its business (here there should be a different type of treatment).

A debtor that shifts its COMI to another Member State for pure liquidation purposes, not performing any economic activity there, whatsoever, can not find protection under freedom of establishment. There is no genuine economic activity behind a COMI shift of this type, representing a pure artificial arrangement. This is not and must not be protected by freedom of establishment. Hence, any restrictions imposed by Member States to avoid or prohibit shifts of COMI in such circumstances will be perfectly justifiable, according to us, on the basis of the principle of prohibition of abusive practices.

IX. Conclusion

The place of the debtors COMI was chosen by the Insolvency Regulation as the relevant connecting factor in determining the competent Member State to open insolvency proceedings. Subsequently, it is the law of that Member State that will be applicable to those proceedings, regarding all aspects, namely conditions for their opening, conduct and closure. The place of the COMI is highly manipulable, leading to a high amount of insolvency forum (and law) shopping. The fact that it is easily manipulable seems to contradict two of the Insolvency Regulation's goals, namely the goal of avoiding forum shopping and the goal of efficiency.

[129] See A. Frada de Sousa, (2012), p. 726-728

Attending to EU fundamental freedoms, namely freedom of establishment, it will never be possible to purely prohibit COMI shifts. Nonetheless, this does not mean that, under freedom of establishment, every type of COMI shift is allowed. Corporate debtors do not have an absolute entitlement to shift their COMI to other Member States, under freedom of establishment. Member States may restrict freedom of establishment (or any other fundamental freedoms) once those restrictions are justifiable under EU law. After trying to come up with measures capable to resolve our concerns laid down in this paper, it is the principle of prohibition of abusive practices that is capable of answering them. By looking at former ECJ case law, we can apply the same conclusions to Insolvency Law. Hence, when a corporate debtor shifts its COMI to another Member State to save its company, pursue a genuine economic activity, then that shift will be protected under freedom of establishment. On the contrary, if a debtor shifts its COMI for pure liquidation reasons, not intending in any way to try to save its business, or to pursue a genuine economic activity, but merely to benefit from a better regime in detriment of creditors, then it must be considered a pure artificial arrangement, in no way fitting in with what is considered to be a general economic activity. Therefore, any restrictions imposed by Member States to avoid or prohibit shifts of COMI in such circumstances will be perfectly justifiable, on the basis of the principle of prohibition of abusive practices.

Alterations to the Insolvency Regulation are expected, in the near future. Nonetheless, as suggested along this paper, we predict that the answers we have come up with will still apply. More importantly will be to see how the ECJ will decide when it is asked to pronounce about abusive shifts of COMI. And, for that, we wait, patiently.

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