European law and trust

Commercial law is at the forefront of European integration. **Marc Udink** and **Professor Dr Christoph Paulus** assess why insolvency law is central to this development.

The law becoming ever more European is a familiar topic in legal discourse. In particular, commercial law has, for a long time, proven to be a forerunner of this development. This is no coincidence since the main players concerned with business law, companies and businesses, are those who have most keenly felt the great variety of law within Europe and still continue to feel it.

Insolvency law is an integral part of commercial law

Since the Eastern Asia crisis in the second half of the last decade the 'global players' – the United Nations, the International Monetary Fund and the World Bank – have discovered that insolvency law is an integral part of commercial law, and a very important one at that. This area of law, which until then was considered a little disreputable and consequently was looked down upon, has since been recognised has having central importance to the functioning of the economy. An efficient, modern insolvency law is after all nothing less than the background to all economic life, and thereby defines its ground rules.

New regulation introduced in May 2002

On the EU level these correlations have been recognised for some time and the EU has consequently taken action. On 31 May 2002, a regulation came into force uniformly and directly in all Member States (with the exception of Denmark). In essence, it regulates which law is applicable if in one of the Member States insolvency measures are applied to the assets of a debtor who also has assets in other Member States.

With the enactment of this regulation the tug-of-war for the right solution, which had lasted for decades, was ended. For a long time the opinion prevailed that insolvency and bankruptcy laws, in general, were so closely tied to national laws that unification could not be achieved. But, in truth, this technical argument was used to obscure the desire to protect one's own people and companies against the application of foreign insolvency law.

This became very clear in the position taken on foreign tax claims: one should not be made to collect foreign taxes – especially if at the expense of local debtors. Another stronghold was formed by the so-called 'exequatur proceedings': a number of Member States reserved the right to determine, in proceedings of their own, whether the insolvency proceedings started in another country and claiming to extend their effects into that state should really be recognised. A few years ago such proceedings for the recognition of a German insolvency in Spain lasted more then three years; the final decision was only given when the insolvency had already been brought to a conclusion and the bankruptcy had been closed.

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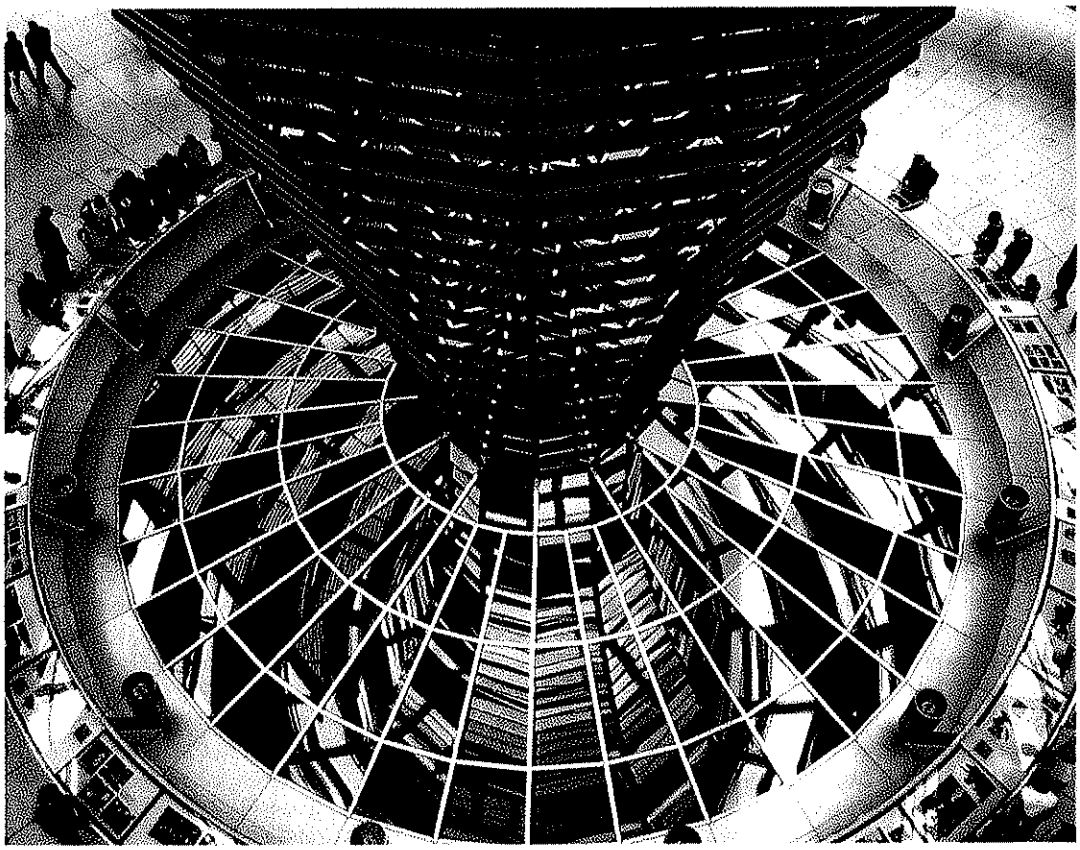
Based on trust

Considering this starting point, it is indeed already a small miracle that there is now a uniform insolvency law for cross-border insolvency proceedings within Europe. The exequatur and other obstacles have been removed: tax claims from other Member States can be lodged in any insolvency proceeding and once started, insolvency proceedings are recognised automatically in all Member States. The European legislature is aware of the consequences of this step. It already emphasises in the introduction, that this regulation is based on trust. The European countries have grown so close together that they need no longer look at the insolvency laws of their neighbours with suspicion, and they are now no longer allowed to do so. This trust thereby forms the cement that evens out the differences still existing between national insolvency laws.

This reign of trust brings along great responsibility. For, especially in the beginning, such trust must be justified and it must be firmly established. This is no small matter: a Greek company can now be wound up according to, say, Finnish law, and the personal insolvency of a German can be handled according to Spanish law. Such matters demand transparency and confidence, since the course of the proceedings is no longer the responsibility of one's own local court, but of a distant and often unknown foreign court. And on top of that, the receiver or liquidator concerned now is no longer necessarily someone who speaks the same language as the debtor. In the future the intervention of an interpreter may be necessary, so that people are able to understand each other!

Centre of main interests

This new situation has led German law to draw the conclusion that information brings trust. In his decision to open insolvency proceedings, a German judge must therefore provide robust reasoning on



German judges must provide sound justification for cross-border proceedings.

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what grounds he thinks that he can and may open proceedings of a cross-border nature. He has the choice to decide whether the proceedings will have effect in all of Europe or only in his own country. The decisive factor in that choice is the location of the debtor's 'centre of main interests' (COMI). If this is in Germany, German insolvency law extends to all Member States and the insolvency proceedings are main proceedings. If, however, the COMI is in another country, but the debtor has a branch in Germany, only proceedings with effect in Germany can be opened as secondary proceedings. In either case, it is significant that the judge gives the reasons for his decision.

Behind this duty to inform, lies the idea of the mature and competent legal subject. Even if the decision does not please him, he should feel he is taken seriously by being given an explanation why the decision is as it is, and not otherwise.

Old-fashioned thinking?

However much the establishment of a duty to explain or to give reasoning may illuminate matters, it is still understandable that the understanding of such correlations is obscured by received ideas and tradition. The limited experience with this new European law shows that English courts in particular are exposed to such danger. This may be due to the lingering effects of old, world-embracing Commonwealth thinking. This leads too quickly and thoughtlessly to the assumption that the debtor's COMI is, of course, in England even in the case of companies registered as a GmbH in Germany and with a completely German management team.

If, in such cases, the English court feels that the simple statement that main proceedings are opened is sufficient reasoning – and in a case where the petition for bankruptcy wasn't even put forward by the management of the company – the necessary trust can hardly be established. Instead, suspicion is engendered.

The achievements of European legislation are endangered because the understanding of the fragile equilibrium between Member States is blocked, possibly obscured by preconceptions formed by historic feelings of being the centre of an empire.

A unified Europe

Once again it is shown: the path to a unified Europe is a rocky one. Everyone must learn how to travel it. Caution in doing so is all the more required if such a valuable commodity as trust hangs in the balance. And such trust is hardly achieved if the judge later adds to his decision, originally given without any reasoning, extensive reasoning that is then backdated to the date of the first decision. e

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