Which role and meaning for the concepts of 'universality' and territoriality', 'unity' and 'plurality' (of proceedings) in future international insolvency law – especially in the relations between EU and third countries?

Elina Moustaira

Abstract:

This paper examines the evolving roles of universality, territoriality, unity, and plurality in international insolvency law, with a special focus on the relationship between the EU and third countries.

Keywords: international insolvency; universality; territoriality; modified universalism; cross-border proceedings; EU law; forum shopping.

A. Introductory comments

It is really very interesting that states, all over the world, follow different paths, when it comes to handling international insolvency issues. They did follow different paths in the past, they still follow different paths, even if some of the states have changed paths.

The target is always the applicable law – even when the 'fight' is about international jurisdiction of the (national) courts. The fact that in the case of insolvencies with foreign elements, that is, assets and creditors in more than one country, the generally applicable law (even when there are exceptions) is the law of the country, the court of which opens the insolvency proceeding, explains this 'phenomenon'.

Generally speaking, the different approaches to the choice of the applicable law are determined by the different legal traditions.[1] When the law defined as applicable by the forum's private international law rules, in all cases, is rarely a foreign law, then it is very difficult, if not impossible, to accept that a foreign law will govern everything concerning an insolvency

1 Moustaira, International Insolvency Law, p. 15.

proceeding opened by that foreign country's court – even the assets being found in other countries.

On the other hand, the world is changing extremely quickly and both large and small businesses 'operate globally using nothing but a mobile phone'; especially '[c]ompanies today are no longer confined to work within a single country or geographic region'.[2]

B. Modified universalism – universal proceduralism – cooperative territorialism

Modified universalism seems to be the dominant approach almost everywhere, nowadays. Not all consider it as the best solution, obviously.

There have been other proposals. One of them is the 'universal proceduralism'[3]. This universal proceduralism is based on a choice-of-law principle that its proponent calls 'virtual territoriality'[4].

According to this proposal, 'the goal is to facilitate a bankruptcy case administered at the debtor's center of main interest that is procedurally global, but substantively territorial'.[5] Universal proceduralism is less concerned with equality of distribution across borders and more concerned with the respect of local priorities.

The supporters of modified universalism disagree with those of universal proceduralism about the importance of respecting local priorities.[6] The first believe in a regime of 'one case under one law', while the latter believe in a regime of 'one case under many laws'.[7]

It is rather obvious, that modified universalism works best when the insolvency regimes of the interested countries are harmonized, something very difficult to happen. Furthermore, it is almost convincingly argued that by allowing ancillary courts to retain their right to apply their own law and protect their own local creditors, modified universalism is territorialist in its nature and that that is its downfall. Predictability is guaranteed only when pure universalism reigns. This predictability is sacrificed when

2 Sachdev 93 Am.Bankr.L.J.2019, 343 (346).
3 His proponent is Janger, 32 Brook. J.Int.L. 2007, 819.
4 Janger 48 Col.J.Trans.L. 2010, 401 (408).
5 Janger 46 Tex.Intern.L.J. 2011, 441 (442).
6 Westbrook 48 Col.J.Transn.L 2010, 503 (517).
7 Janger 46 Tex.Intern.L.J. 2011, 441 (442).

modified universalism governs because the 'regime or regimes that will ultimately distribute the debtor's assets may depend on the country in which the assets are located at the time of bankruptcy'.[8]

And what about forum shopping? It is considered as one of the main problems (or evils) of pure universalism. Forum shopping is not necessarily an evil strategy, since it is allowed to choose a forum among more 'offered'. But when the forum shopping is abusive, it may reduce the legal certainty of the proceedings, since the applicable law may be changed.[9]

The lack of legal certainty has given the opportunity to the debtors themselves or to the directors of distressed companies to resort to abusive forum shopping, because of the differences between the various insolvency laws. By selecting jurisdiction and consequently the [most favorable to their own interests][10] applicable law, it is very possible that certain creditors may be harmed by this choice, since the applicable law might not be favorable to them – it might cause them unexpected monetary expenses and liabilities or it might discriminate between domestic and foreign creditors, or it might not guarantee the equal protection of creditors, or the payoff might be altered, etc.[11]

Because of the above abusive forum shopping danger, another approach has been proposed, that of 'cooperative territorialism'. Under this approach, each country may open and administer its own bankruptcy case, applying each its own law. None of these cases may be considered a main case or an ancillary case.

Nevertheless, while cooperative territorialism might have some advantages – for example, it solves the 'home' country problem and it provides greater predictability to lenders – it seems too optimistic an approach, given the fact that the regime that it promotes *does not require* cooperation.

In favor of forum shopping, it is argued that it has several benefits. One of them is centralized management, but the primary benefit, it is pointed out, is 'the traditional choice of law motivation: namely, the application of congenial substantive law'. Although it is not certain whether that would be the 'traditional' choice of law motivation in all countries' private international law, one is inclined to accept that in insolvency matters this is really it. As it is mentioned, an easy example of this would be the situation

8 LoPucki 84 Cornell L.Rev. 1999, 696 (728).
9 McCormack 63 IJLQ 2014, 815.
10 Szydlo 11 EBOR, 2010, 253.
11 Coburn, Insolv.Intellig, 2012, 8.

of a debtor who would like to reorganize its business, but is in a legal system which is liquidation oriented. That debtor would try to relocate to a jurisdiction which would allow a reorganization and thus he would avoid the liquidation.[12]

C. Has universalism suffered a major setback?[13]

It seems that no absolute answer may be given. Furthermore, legal scholars often 'translate' differently the paths that national laws take towards recognizing foreign insolvency proceedings and accepting the universal application of that foreign *lex [fori] concursus*.

For example, modified universalism is translated as a threshold to absolute universalism, an optimism not convincingly expressed. It is argued by US scholars, that:

"[Universalists] deploy modified universalism both as a theory to undergird a transitional system sensitive to the interests of sovereign states and local stakeholders, pending the establishment of a fully universalist system, and as a normatively laden method or principle that, applied correctly, will help bring about a fully universalist system[14]".

That was also what had been said about 20 years ago, by one of the best US insolvency scholars: that modified universalism was the best interim solution in the way to the optimal solution, the 'true universalism'.[15]

One could easily doubt about that… That interim solution tends to become a permanent one. The following chapter rather confirms that.

D. Is modified universalism becoming customary international law?

It has been supported that modified universalism, from a transitory approach could become customary international law.[16] Could it? Should it? It seems doubtful.

12 Pottow 56 Tex.Intern.L.J. 2021, 155 (161).
13 As it is argued by Sokol in 44 Hastings Intern. & Comp.L.Rev. 2021, 39 (41).
14 Walters 93 Am.Bankr.L.J. 2019, 47 (49).
15 Westbrook 98 Mich.L.Rev. 2000, 2276.
16 Mevorach, pp. 80 ff.

It is argued that 'we are witnessing a gradual reunification of private and public international law in both theory and practice'.[17] But, really, are we? It is also pointed out that this is not a question of merger of private international law and public international law but that it is about an 'internationally oriented mission of private international law' which 'should continue to evolve'[18] and learn from public international law,[19] seek guidance from foreign law through the notion of the law of nations (*ius gentium*).[20]

Still, one wonders whether this would be something new. In continental European countries, at least, private international law was never really nationally oriented, since the traditional choice of law rules were and are neutral and the application of a foreign law was and is almost always guaranteed, when the private international law rules point to that. The exception of public policy is only in specific circumstances activated. On the contrary, in common law countries (with many variations between them, of course), private international law or, as it is mostly called there, conflict of laws/choice of law very often points to lex fori, as the applicable law.[21]

But even in European continental countries, before the regulations' entry in force, there were differences, regarding the application of a foreign law in the case of an insolvency the consequences of which were not limited in one country.

For example, several countries wanted their insolvency judgments to have universal effect but refused such effect to foreign insolvency judgments and, consequently, refused to recognize them and apply a foreign law, e.g., by rendering assets located in their territory to the foreign administrator, according to the rules of the foreign *lex fori concursus*. They were universalists and territorialists, regarding the domestic and the foreign insolvencies, respectively.

On the contrary, [very] few countries (Greece was among them) were willing to recognize a foreign insolvency and consequently apply the foreign *lex fori concursus*. Obviously, modified universalism is rather a drawback for these countries: their private international law did have an internationally oriented mission that gradually – and obligatorily, because of the

17 Mevorach, p. 105.
18 Mevorach, p. 105.
19 Michaels 4 J.Priv.Int.L.2008, 121 (137–138).
20 Waldron 119 Harv.L.Rev. 2006, 129 (135–138).
21 About that, see Moustaira, International Insolvency Law.

governing European Regulations and the adoption of a law incorporating the MLCBI – was restricted.

As it is perfectly and sincerely stated, 'modified universalism is not a unified phenomenon with a single set of characteristics or predicates'. MLCBI system 'is dominated by the US, the leading producer of Model Law jurisprudence'. Judges in other countries that also have adopted Model Law should not be expected 'to subscribe to a strong, American version of modified universalism', would not be willing to accept such an exercise of American soft power.[22]

So, no repeated application of the same rules is observed. One could hardly speak about modified universalism as customary international law.

E. Trajectory of national laws – two examples of actuality

Examples of new national laws – in regard to the concepts [and the practice, obviously] of universality and territoriality – show a rather confused attitude. The reason, very probably, is the tremendous increase of insolvencies that have consequences in more countries. Instead of accepting/enforcing the universality principle, national laws (either written or judge-made) often show a reluctance to that. Rather obviously, this is the result of the pressure by the interested persons – debtors, creditors, insolvency practitioners, etc.

I. Brazil

It is extraordinarily interesting, that Brazil had enacted (and repealed) various bankruptcy laws during the last decades of the 19th century, in which laws there were rules about recognition and enforcement of foreign insolvency judgments and that this fact changed during the 20th century.[23]

The former Federal Bankruptcy and Reorganization law, of 2005, contained no provision on international insolvencies. International insolvency issues were decided in Brazil on a case-by-case basis, mostly following the principle of territoriality.[24] In December 2020, Brazil adopted a modified

22 Walters 93 Am.Bankr.L.J. 2019, 47 (104).
23 Campana Filho, Int.Insolv.Rev. 2022, 1 (2).
24 Moustaira, International Insolvency Law, p. 34.

version of the MLCBI on cross-border insolvency. The law entered into force in January 2021. Two big cases were already tried according to its rules. It is argued that 'the time is ripe for Brazil to embrace modified universalism and to leave behind its long history of refusals of recognition of foreign proceedings and of the absence of cooperation with courts of other countries'.[25] It remains to be seen, whether this new legislation/situation will bring best results in the future.

II. China

Article 5 of the Enterprise Bankruptcy Law 2006 is the first – and only – Chinese provision to address cross-border insolvencies – there are no rules governing international jurisdiction or choice of law.[26] It consists of two paragraphs, respectively concerning the universal ambitions of Chinese insolvency proceedings and the modified universalist (or, rather, territorialist) approach to foreign insolvency proceedings in China.[27]

The first paragraph says that insolvency procedures commenced in accordance with this Law are binding on the debtor's property located outside the territory of the People's Republic of China (PRC).

The second paragraph sets out the criteria for recognition of foreign insolvency proceedings. Therefore, for an insolvency proceeding opened outside mainland China to be recognized and enforced, the conditions are that:

1. relevant international treaties between the country concerned and mainland China have been concluded; or
2. reciprocal relations between the country concerned and Mainland China have been established;
3. the insolvency proceeding shall not violate the basic principles of the laws of the PRC;
4. the insolvency proceeding shall not jeopardize the sovereignty and security of the State or public interests;
5. the insolvency proceeding shall not undermine the legitimate rights and interests of creditors within mainland China.[28]

25 Campana Filho, Int.Insolv.Rev. 2022, 1 (15).
26 Moustaira, International Insolvency Law, pp. 39–40.
27 Parry/Gao Int.Insolv.Rev.. 2018, 5 (10–17).
28 Gong, p. 40.

It is argued that this article 5 ‘reflects the key principles of modified universalism’, but it is not a convincing argument.[29] As it is admitted, up until now there have been scarce cases in which Chinese courts have recognized foreign insolvency proceedings and granted assistance to them.

F. And what about the schemes of arrangement?

They are not included as an insolvency proceeding, in the recast EIR's Annex. That means that their recognition and enforcement (or not) will be based (conditioned) on other regulation(s).[30] In regard of all the other states of the world, the question of whether a scheme of arrangement will be recognized and enforced will depend on their private international law rules of national origin, except if there are relevant bilateral or multilateral treaties (rather not). Thus, in case of a scheme of arrangement, universality appears as an even more frail principle.

It has been argued that the existence of the scheme proceedings ‘suggests that the universalist benefits of centralized administration may be more easily achieved within Europe than outside the continent’;[31] this argument is based on the opinion of other scholars, according to which a scheme, while not recognized as insolvency procedure under EIR, it will be recognized and enforced under Brussels I-bis.[32] It is true that somehow a scheme will be recognized and enforced within Europe (and this fact leads to a somewhat universalist tendency in regard to ‘insolvency’ proceedings), but it is not certain under which regulation this recognition and enforcement will take place. The following case proves that:

On the 08.06.2021, the English High Court sanctioned the DTEK Energy B.V. and the DTEK Finance PLC schemes of arrangement.[33]

The judge did not accept that:

> “Prior to 1 January 2021, the general approach was that the EU Courts would recognize a scheme sanctioned in this jurisdiction under EU Regulation 1215/2012 on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters (‘the Judgments

29 Zhang EBOR 2022, 735 (737).
30 Rodriguez, European Insolvency and Restructuring Journal 2023, 1 (11).
31 Pottow 56 Tex.Intern.L.J. 2021, 155 (161).
32 Kokorin/Madaus/Mevorach 56 Tex.Intern.L.J. 2021, 109 (126).
33 [2021] EWHC 1551 (Ch).

> Regulation'). Certainly, he said, English schemes were generally not approved as effective on that basis"

He proceeded, saying (among other comments) that in two recent judgments addressing the effectiveness of English schemes in the Netherlands, the two Dutch expert evidence brought before him demonstrated: in the first case (Re Hema UK 1 Ltd.)[34] that the scheme would be effective either under the Judgments Regulation or as a matter of private international law and in the second case (Re Selecta Finance UK Ltd.),[35] that the scheme would be recognized in the Netherlands under the Judgments Regulation, or under EU Regulation 593/2008 applicable to contractual obligations ('Rome I') or under the Lugano Convention. He also mentioned another case (*Re Lecta Paper*),[36] in order to show that the same approach has been or will be adopted by Luxembourg, France, Spain and Italy, in which case the various experts based their opinions upon the judgment's regulation, principles of private international law and Rome I.[37]

G. EU – third countries: universality

Do the words and their meanings change role? Or is it that people who use them, who refer to the concepts expressed by those words, try to adapt versions of them to what they themselves would like best? Personally, I believe that the latter happens.

Personally, too, I believe that only the absolute universality (together with unity: one insolvency proceeding and one applicable law) would contribute to a fair insolvency procedure, with equal opportunities for all persons concerned – and especially for the creditors. Only one applicable law can achieve that. When more laws 'ask' to be applied and they achieve that, often the result is far from what the institution of insolvency had ever put forth as its aim. Modified universality/universalism is not only becoming a permanent solution, instead of an interim one, but it is slowly but steadily corroded by neo-territorialist national attitudes, both in the European Union space and in other parts of the world. For example, voices in favor of an amendment of the conflict of laws rules in the EIR, aiming

34 [2020] EWHC 2558 (Ch).
35 [2020] EWHC 3220 (Ch).
36 [2020] EWHC 382 (Ch).
37 Moustaira, in Arvanitakis (edn), 2021, pp. 195 (202–203).

at enlarging the list of exceptions to the application of the *lex fori concursus*, would contribute to the final reign of territoriality in the insolvency proceedings.

Having in mind all the hurdles in a cross-border insolvency case, the fact that the Recast EIR does not follow the *erga omnes* approach followed by several other EU Private International Law instruments seems a bad choice.[38] The result of such a choice is that in each Member State there are two different regimes about cross-border insolvencies: the European one and the national private international law of insolvency. This fact may be cause of many problems, one of the reasons being that 'the line of division between these two laws is artificial'.[39]

In *Schmid*[40], the CJEU held that the (former) EIR applies even when only the debtor's COMI is in a Member State, while all the other elements of an insolvency are located in third countries. One can imagine the difficulties that are created in such cases.

It is necessary to extend – unilaterally – the scope of application of the EIR, since – as it is eloquently pointed out – 'the real world does not end at the geographical borders of the EU'.[41] One of the advantages of such an extension would be that the equal treatment of creditors would have a more solid guarantee. Another one would be the more efficient administration of insolvency proceedings.

Thus, I argue that the rules of the EIR should be extended as to be also applied towards third countries. As a consequence, non-EU insolvencies too should be recognized and the foreign *lex fori concursus* (the third country's insolvency law) should be applied, if the insolvency proceeding was opened at the place of its (non-EU) COMI. The public policy exception could always be used, if deemed absolutely necessary.

On the contrary, non-EU insolvencies should not be recognized in the EU, if COMI is in an EU member state. The opposite would demolish decades of work inside the (European Communities, first, and next) European Union.

38 Nisi, J.Priv.Int.L. 2017, 324 (325).
39 Jault/Robine, Rev.Crit. DIP 2016, 21 (23) (« *dès lors que la ligne de partage entre ces deux droits est artificielle* »).
40 ECJ, 16.1.2014 -C-328/12, ECLI:EU:C:2014:6- Ralph Schmid (liquidator of the assets of Aletta Zimmermann) v Lilly Hertel.
41 Nisi, J.Priv.Int.L. 2017, 324 (330).

A (legal) practice followed in some countries, in order to overcome the different ranking of claims that different national insolvency laws have, is that of the virtual territoriality: courts treat foreign (from other member states of the EU) creditors 'as if' a secondary insolvency proceeding had been opened in their respective jurisdictions.[42] Thus, proceedings are simplified through consolidation of local priorities and assets are distributed according to a hypothetical territorial distribution. Could that be a solution in cases where COMI is in the EU, and establishments outside the EU? I am not at all certain. Furthermore, there is no doubt that this is an opposite discrimination of creditors.[43]

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